Report of the Auditor-General

Report 5 of 2018

Annual report
for the year ended 30 June 2018
Part B: Agency audit reports

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for the year ended 30 June 2018
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Contents

Agency audit reports 1
Adelaide Festival Centre Trust 3
Adelaide Oval SMA Limited 9
Adelaide Venue Management Corporation 15
Attorney-General's Department 19
Public Trustee 39
Auditor-General's Department 52
Department for Child Protection 53
Department for Correctional Services 63
Courts Administration Authority 73
Department for Education 80
Environment Protection Authority 92
Department for Environment and Water 98
Health sector overview 111
Department for Health and Wellbeing 121
Central Adelaide Local Health Network Incorporated 142
Country Health SA Local Health Network Incorporated 163
Northern Adelaide Local Health Network Incorporated 171
SA Ambulance Service Inc 182
Southern Adelaide Local Health Network Incorporated 190
Women's and Children's Health Network Incorporated 205
HomeStart Finance 212
Department of Human Services 224
Independent Commissioner Against Corruption 238
Lifetime Support Authority of South Australia 242
Motor Accident Commission 250
Department of Planning, Transport and Infrastructure 261
Department of the Premier and Cabinet 282
Department of Primary Industries and Regions 296
Return to Work Corporation of South Australia 308
South Australia Police 320
South Australian Fire and Emergency Services Commission 330
South Australian Government Financing Authority 345
South Australian Housing Trust 357
South Australian Tourism Commission 378

South Australian Water Corporation 383
Department of State Development 399
Superannuation sector overview 412
South Australian Superannuation Board 416
South Australian Superannuation Scheme 423
Southern State Superannuation Scheme 429
Super SA Retirement Investment Fund 433
Superannuation Funds Management Corporation of South Australia 437
TAFE SA 446
Department of Treasury and Finance 460
University sector overview 474
Flinders University 481
University of Adelaide 488
University of South Australia 496
Urban Renewal Authority 507

Agency audit reports

Introduction

Part B: Agency audit reports is a summary of the audit outcomes for each agency included in this Report. It features a snapshot of key agency information covering financial statistics, significant events and transactions, and whether the financial report and financial controls opinions are unmodified or modified (qualified). If modified, the key matters causing the modification are noted. The snapshot is followed by commentary on financial administration matters for each agency that, in my opinion, are important to the Parliament and the SA Government. This commentary also contains selected financial ratios and information for assessing the agency's financial performance and position, and significant financial transactions.

The financial reports of the agencies included in this Report are available on the Auditor-General's Department website (www.audit.sa.gov.au).

Agencies not included in this Report

The Auditor-General exercises the discretion to exclude agencies from this Report. The decision to exclude an agency is based on many factors including:

- the materiality of its financial operations
- its significance to the operations and services of the SA Government
- the materiality of any impact on the public finances
- the timeliness of information
- the materiality of issues arising from the audit
- the public interest
- the timely completion of this Report and meeting the statutory deadline to deliver the Report to the presiding members of Parliament.

A list of the public sector agencies not included in this Report is provided at the end of Part A: Executive summary. To strengthen accountability for the activities of these agencies I have elected to prepare a new report to Parliament annually that will identify agencies not included in my Annual Report with:

- a modified Independent Auditor's Report
- a modified controls opinion
- significant matters raised through the audit
- other matters that, in my opinion, need to be brought to the attention of the Parliament and the SA Government.

I will prepare the first of these reports in early 2019.

In addition, to strengthen accountability for the activities of these agencies, their financial reports will be published on the Auditor-General's Department website once the audit of each agency is finalised.

Modified Independent Auditor's Reports

Expressing an opinion on an entity's financial report by an independent professional auditor adds credibility to it and ensures that appropriate financial disclosures were made.

For the agencies that I am required to audit, I issue an Independent Auditor's Report on the financial report in line with professional requirements and standards. The opinion I give is usually unmodified, but if circumstances warrant it a modified opinion is expressed. In extreme cases it may not be possible to express an opinion.

When a modified opinion is given, the Independent Auditor's Report explains the reasons for the modification. This is also explained in the commentary on those agencies in this Report.

Of the agencies included in this Report, a modified opinion was expressed on the financial report of the University of South Australia.

In addition, without modifying my opinion on the financial reports of the Return to Work Corporation of South Australia and the Lifetime Support Authority, I drew attention to the inherent uncertainty in certain liabilities reported for those entities at 30 June 2018.

Assessment of controls

Section 36(1)(a)(iii) of the *Public Finance and Audit Act 1987* requires me to advise Parliament whether, in my opinion, the controls exercised by the Treasurer and by public authorities in relation to the receipt, expenditure and investment of money, the acquisition and disposal of property and the incurring of liabilities are sufficient to provide reasonable assurance that the financial transactions of the Treasurer and public authorities have been conducted properly and in accordance with law.

A controls opinion has been expressed for each public authority included in this Report. Where I issued a modified controls opinion, the opinion and my reason(s) for issuing it are provided.

Audit of the Auditor-General's Department

The *Public Finance and Audit Act 1987* requires the accounts of the Auditor-General's Department to be audited by an auditor appointed by the Governor. The audit for the financial year ended 30 June 2018 was conducted by Nexia Edwards Marshall, Chartered Accountants, who issued an unmodified Independent Auditor's Report on the Department's financial report and an unmodified controls opinion.

Adelaide Festival Centre Trust (AFCT)

Financial statistics		
	Net cost of providing services:	$29 million
	Revenues from SA Government:	$34 million
	Revenues from fees and charges:	$21 million
	Net assets:	$18 million
	Number of FTEs:	237 (including 90 casuals)
	Ticketed attendances:	405 357
	Total attendances:	823 270

Significant events and transactions

- During the year work commenced on the redevelopment and expansion of Her Majesty's Theatre. The AFCT purchased Her Majesty's Theatre from Arts South Australia in July 2017 for $8.2 million. The Theatre closed in March 2018 and the value of the building was impaired at 30 June 2018 as, except for the heritage façade, it will be demolished as part of the redevelopment.
- To date the AFCT has drawn down $5.5 million of the approved $62 million borrowing to fund the redevelopment of Her Majesty's Theatre.
- The $90 million redevelopment of the Adelaide Festival Centre and Plaza continued in 2017-18. The Festival Theatre was closed for five months in 2017-18 as a result of the redevelopment.

Financial report opinion — **Unmodified**

Financial controls opinion — **Unmodified**

Functional responsibility

The AFCT is a body corporate established under the *Adelaide Festival Centre Trust Act 1971*. It is under the general control and direction of the Minister for the Arts.

The AFCT is responsible for encouraging and facilitating artistic, cultural and performing arts activities throughout the State and managing and maintaining Her Majesty's Theatre (HMT) and the Adelaide Festival Centre and its facilities. Further information on the AFCT's objectives is provided in note 1 of its financial report.

The AFCT also operates the BASS ticketing system to sell tickets primarily for artistic performances held at the Adelaide Festival Centre and HMT.

Scope of the audit

The audit program covered major financial systems to obtain sufficient evidence to form an opinion on the financial report and internal controls.

Specific areas of audit attention in 2017-18 included:

- revenues from theatre services and box office
- BASS ticketing system
- salaries and wages
- procurement and expenditure on supplies and services
- fixed assets.

Audit findings and comments

Communication of audit matters

Matters identified by the audit were detailed in a management letter to the Chief Executive Officer. We recommended that the AFCT:

- develop a policy for negotiating fees and charges when they differ from the approved schedule
- implement a periodic review over user access to the time recording system
- ensure that all bona fide reports are returned to payroll in a timely manner.

The AFCT responded that these matters will be addressed.

Interpretation and analysis of the financial report

Highlights of the financial report

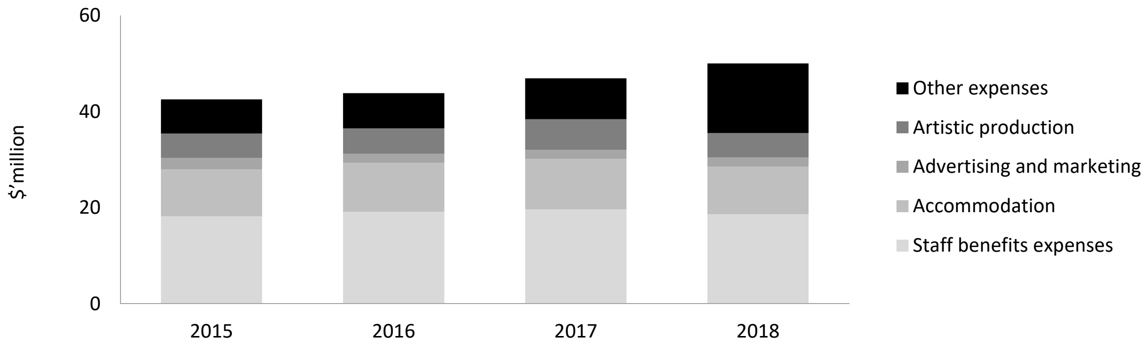
	2018 $'million	2017 $'million
Expenses		
Staff benefits expenses	19	20
Other expenses	31	27
Total expenses	50	47
Income		
User charges and interest	21	26
Net cost of providing services	29	21
Revenues from (Payments to) SA Government	34	22
Net result	5	1
Net cash provided by (used in) operating activities	18	(7)
Assets		
Current assets	20	10
Non-current assets	25	17
Total assets	45	27
Liabilities		
Current liabilities	18	11
Non-current liabilities	9	3
Total liabilities	27	14
Total equity	18	13

Statement of Comprehensive Income

The AFCT relies on SA Government funding to support its operations. That is, the net cost of services is met through funding provided by the SA Government. The AFCT's activities are largely dependent on the level of external demand for theatre services and the extent of AFCT programmed activities. Depending on the level and timing of these activities, the nature and amount of revenues and expenses will vary from year to year. In 2017-18, as a result of the redevelopment of the Adelaide Festival Centre and Plaza, the Festival Theatre was closed for five months.

Expenses

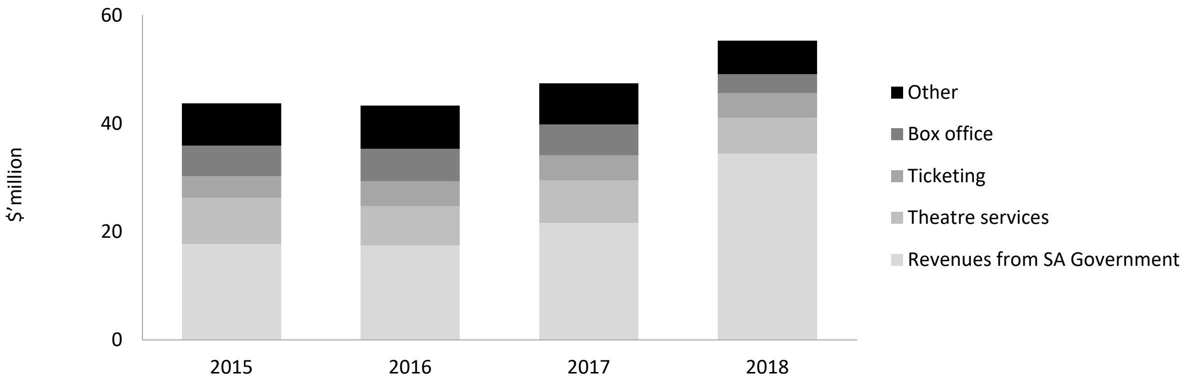
An analysis of the AFCT's expenses for the four years to 2018 is presented in the following chart.



In 2018 the AFCT's expenses increased by $3.5 million to $50 million due mainly to the $5.6 million impairment loss as a result of demolishing HMT for redevelopment. This was offset by a decrease in artistic production costs of $1.3 million as a result of the Festival Theatre being closed for five months.

Income

An analysis of AFCT's income for four years to 2018 is presented in the following chart. Revenues from the SA Government have been included in income for the purpose of this analysis.



In 2018 the AFCT's income increased by $7.9 million to $55.3 million due mainly to an increase in revenues from the SA Government of $12.8 million. This offset the decrease in revenue from fees and charges of $4.9 million to $20.7 million. The decrease in revenue from fees and charges is largely the result of the Festival Theatre being closed for five months and the closure of HMT from March 2018. The main components of revenues from the SA Government were:

- operating base funding of $16.5 million
- HMT redevelopment funding of $9.5 million – made up of the purchase of HMT, $8.2 million, supplementation funding for the theatre closure in March 2018 and $500 000 in donated HMT assets from Arts South Australia
- Adelaide Festival Centre redevelopment supplementation funding of $7.6 million – made up of the closure of the Festival Theatre for five months, $6.1 million, and the closure of the car park, $1.5 million.

Statement of Financial Position

Current assets

The AFCT's current assets of $19.9 million ($10.4 million) include cash of $17.5 million ($8.4 million), of which $7.8 million ($4.3 million) is proceeds from ticket sales through BASS held in trust until distributed to promoters. Cash also increased as a result of the increase in revenues received from the SA Government.

Non-current assets

The AFCT's non-current assets of $25.1 million ($16.5 million) comprise:

- works of art of $8.8 million ($8.8 million)
- property, plant, equipment and intangible assets of $9 million ($7.4 million)

- capital works in progress of $7.3 million ($200 000). The increase of $7.1 million is a result of the HMT redevelopment.

Liabilities

The AFCT's liabilities increased by $13.2 million to $26.7 million due mainly to:

- borrowings increasing by $5.5 million as a result of the redevelopment of HMT commencing
- amounts payable to promoters increasing by $3.5 million due mainly to the increase in ticket sales for shows as a result of the Festival Theatre reopening in December 2017
- accrued expenses increasing by $3.4 million as a result of amounts owing to Arts South Australia for rent of the Adelaide Festival Centre.

Further commentary on operations

Redevelopment of Her Majesty's Theatre

In June 2016, the SA Government announced a $35 million redevelopment and expansion of HMT.

The upgrade will expand the existing auditorium to increase seating capacity from 970 to around 1500 seats, as well as provide a more spacious foyer, improved front-of-house amenities, and upgraded orchestral pit and technical facilities. It will allow the hosting of large scale commercial touring productions within this historic theatre.

The SA Government was to provide funding of $32 million, with the remaining $3 million to be covered by the AFCT through a fundraising campaign by the Adelaide Festival Centre Trust Foundation (the Foundation).

As part of the redevelopment project, the Foundation purchased the property adjacent to HMT in 2016 for $2 million for the purpose of expanding HMT. This building will serve as new entrances and foyers on the western side of HMT. To facilitate the purchase, the AFCT took out a loan with the South Australian Government Financing Authority (SAFA). However, the loan was forgiven in 2016-17 at the drawn down amount of $1.33 million.

Additional unforeseen costs as well as new opportunities for the project were uncovered during the planning and design of the redevelopment. This included provision for an additional floor to allow a rooftop bar and gallery space.

Subsequently, on 22 June 2017, the SA Government announced in the 2017-18 State Budget additional funding of $31 million over three years to undertake further works within the upgrade and expansion of HMT. This brought the revised total capital cost of the project to $66 million. This initiative includes transferring the HMT and building from Arts South Australia to the AFCT from July 2017. Funding for the project will be provided by means of:

- a $62 million loan to the AFCT facilitated through SAFA. The loan will be a principal only loan for 10 years and will be drawn down as required. The interest will be subsidised by a grant from the SA Government

- $1.13 million already expended on the project in 2016-17, which will be capitalised and form part of the purchase of HMT in July 2017
- $3 million to be raised through a fundraising campaign by the Foundation.

HMT closed in March 2018. Major construction works commenced in April 2018 and are expected to be completed in early 2020.

Redevelopment of the Adelaide Festival Centre and Plaza

The $90 million redevelopment of the Adelaide Festival Centre and Plaza, as part of the major redevelopment of the Riverbank Precinct, continued in 2017-18. The construction works resulted in the closure of the car park, and restricted access to the Dunstan Playhouse, Space Theatre and the footbridge. The closure of the Festival Theatre from July to December 2017 impacted ticket sales for 2017-18 and the revenue earned from associated activities.

The Department of Treasury and Finance provided supplementary funding of $7.6 million in 2017-18 to help cover the financial impact of the redevelopment on the AFCT.

Adelaide Oval SMA Limited (AOSMA)

Financial statistics	Net assets:	$5.1 million
	Profit from trading activities:	$1.3 million
	Net contributions to the SANFL and SACA from trading activities:	$1.2 million
	Money collected as agent on behalf of the SANFL and SACA:	$25.5 million
	Money collected as agent on behalf of parties other than the SANFL and SACA:	$36 million

Significant events and transactions

In line with the requirements of the *Adelaide Oval Redevelopment and Management Act 2011*, AOSMA:

- paid $400 000 to the SA Government to lease the Adelaide Oval Core Area
- made a payment of $2.8 million into the sinking fund.

Financial report opinion

Unmodified

Financial controls opinion

Not applicable

A financial controls opinion is not required as AOSMA is not a public authority.

Functional responsibility

AOSMA is a company whose directors and members are appointed equally by the South Australian National Football League (SANFL) and the South Australian Cricket Association (SACA). AOSMA is not a public authority. It was created in December 2009 as a non-profit public company limited by guarantee.

AOSMA manages, operates and maintains the redeveloped Adelaide Oval stadium owned by the SA Government and also the area closely surrounding the stadium (the precinct). Under the *Adelaide Oval Redevelopment and Management Act 2011* the Adelaide Oval Core Area is leased to the Minister. The Minister has subleased it to AOSMA until 2091.

AOSMA also provides various services as agent on behalf of the SANFL, SACA and promoters in return for a fee.

Authority for audit

Section 9(3) of the *Adelaide Oval Redevelopment and Management Act 2011* provides for the Auditor-General to audit AOSMA's accounts each year.

Scope of the audit

The audit program covered financial accounting records and processes and was directed primarily to obtaining sufficient evidence to form an opinion on the financial report.

For the year ended 31 October 2017 specific areas of audit attention included:

- revenue from car parks, sponsorships, service fees, sales of food and beverages and contributions from the SA Government, SACA and the SANFL
- distribution of money collected as agent on behalf of the SANFL, SACA, Commercial Operations Trust (COT) and promoters, including receipts from the sale of tickets to events, supply rights, Adelaide Oval football memberships, Stadium Club corporate seats, corporate suites and the Adelaide Oval roof climb
- controls for managing contracts and agreements with the SANFL, SACA, SA Government, Australian Football League (AFL), Cricket Australia (CA), promoters, ticketing agent, car park operator, suppliers and various other parties
- procurement and expenditure on plant, equipment, supplies and services
- employee benefits expense.

Audit findings and comments

Communication of audit matters

Matters identified by the audit were detailed in a management letter to the Chief Executive Officer.

Audit matters raised with AOSMA

AOSMA agreed to improve its processes and policy documentation for a range of areas including: the negotiation of prices and documenting amendments to contracts for functions and events held at Adelaide Oval; maintaining a journals register; and independent review of masterfile data. These recommended improvements will ensure AOSMA's functions continue to be performed efficiently and effectively.

Interpretation and analysis of the financial report

Highlights of the financial report

	Year ended 31.10.17 $'000	Year ended 31.10.16 $'000
Trading activities		
Income	75 902	66 936
Expenses	74 585	64 824
Profit (Loss) from trading activities	1 317	2 112
Stakeholder contributions		
Contributions from the SANFL and SACA	7 867	8 919
Contributions to the SANFL and SACA	(9 114)	(8 379)
Net contributions	(1 247)	540
Trading result after net contributions to stakeholders	70	2 652
SA Government related items		
SA Government grants and other contributions	838	219
Lease to Minister	(400)	(200)
Acquisition of capital assets for the SA Government	(1 028)	(254)
Total comprehensive result	(520)	2 417
Net cash provided by (used in) operating activities	9 460	7 670
Assets		
Current assets	12 893	16 663
Non-current assets	19 156	15 156
Total assets	32 049	31 819
Liabilities		
Current liabilities	17 669	16 254
Non-current liabilities	9 292	9 957
Total liabilities	26 961	26 211
Total equity	5 088	5 608

AOSMA operates under a complex set of arrangements with the SANFL and SACA that dictate the accounting treatment of certain financial transactions and their presentation in the financial report.

Statement of Comprehensive Income

The Statement of Comprehensive Income includes only the income and expenses that AOSMA controls. It does not include money that AOSMA collects as agent on behalf of the SANFL, SACA, COT, AFL, CA, football clubs or promoters.

Trading activities

AOSMA reported a trading profit of $1.3 million in the 12 months to 31 October 2017 compared to a trading profit of $2.1 million in the previous year, a decrease of $800 000.

AOSMA reported trading income of $75.9 million ($66.9 million). The increase in trading income of $9 million was mainly due to:

- an increase of $2.4 million in recoveries and service fees charged to the SANFL, SACA and promoters under various agreements
- an increase of $6.5 million in revenue generated from catering activities and other sales attributable to AOSMA.

Trading expenses increased by $9.8 million to $74.6 million ($64.8 million). The increase was mainly due to increases in:

- employee benefits expense of $1.8 million
- raw materials and consumables of $2.2 million, largely as a result of increased catering activity during the year
- other expenses of $2 million. These costs include insurance and legal fees, laundry, linen and uniforms and other general expenses
- supplies and services expenses of $880 000. These costs include stadium cleaning costs, building maintenance costs, security expenses and utility costs
- depreciation and amortisation expense of $2 million to $4.9 million ($2.9 million).

Stakeholder contributions

Net contributions from AOSMA to the SANFL and SACA were $1.2 million. Under various agreements, AOSMA contributed $9.1 million of its trading income to the SANFL and SACA while the SANFL and SACA contributed $7.9 million to AOSMA to support its operations. The $9.1 million contributed to the SANFL and SACA was in addition to $25.5 million collected and distributed by AOSMA to the SANFL, SACA and the COT as their agent. For the SANFL and SACA, these distributions replace the funds formerly generated directly by SACA when it held the lease over the Adelaide Oval, and for the SANFL when AFL football was played at AAMI Stadium.

SA Government related items

SA Government grants and other contributions of $838 000 ($219 000) is grant income for safety, security and stadium operations provided by the SA Government under a Deed of Grant agreement. AOSMA also acquired capital assets of $1 million ($250 000) which were funded by the SA Government. In addition, AOSMA paid $400 000 to the SA Government to lease the Adelaide Oval Core Area in line with the *Adelaide Oval Redevelopment and Management Act 2011.*

Statement of Financial Position

The major movements in assets and liabilities over the year were:

- an $800 000 increase in the deferred income liability resulting from unearned income from customer deposits for catering events and promoters for stadium events
- a $5 million decrease in receivables attributable to $5.7 million received from the COT for the licence to operate the roof climb business.

AOSMA's main assets comprise property, plant and equipment of $19.1 million ($15 million), receivables of $3.4 million ($8.4 million) and cash of $7.7 million ($6.9 million).

Money collected on behalf of other parties

AOSMA collects money as agent on behalf of the SANFL, SACA, COT, AFL, CA, football clubs and various promoters. Collecting this money involves selling, on their behalf, tickets to events, supply rights, Adelaide Oval football memberships, Stadium Club corporate seats and corporate suites and the Adelaide Oval roof climb.

For the year ended 31 October 2017, AOSMA collected:

- $25.5 million on behalf of the SANFL, SACA and COT. This amount is disclosed as related party transactions in note 17 of AOSMA's financial report
- $36 million on behalf of the AFL, CA, football clubs and promoters. These collections are not disclosed in the financial report, apart from the balance awaiting distribution at 31 October 2017. Most of these collections related to tickets sold through AOSMA's ticketing agent on behalf of CA, the Port Adelaide Football Club, the Adelaide Football Club and promoters.

AOSMA's financial report does not include revenue generated at the Adelaide Oval that is not collected through AOSMA but directly by the SANFL, SACA, AFL, CA, football clubs or promoters.

Further commentary on operations

State legislative requirements

The operations of AOSMA are subject to the requirements of the *Adelaide Oval Redevelopment and Management Act 2011* which specifies the following matters:

- leasing and licensing requirements for the management of the Adelaide Oval. These requirements involve the Corporation of the City of Adelaide (Adelaide City Council), the responsible Minister, the SANFL, SACA and AOSMA
- financial and audit reporting requirements of AOSMA and the redevelopment in general
- that the Auditor-General audits AOSMA's accounts each year
- the establishment of a sinking fund to be managed by AOSMA to pay for non-recurrent expenditure of the Adelaide Oval in the years after its completion. After consulting AOSMA the Treasurer must determine annually the amount payable by AOSMA into the sinking fund. A report on money paid into and out of the fund must be provided to the Minister by 1 September each year.

AOSMA has established a bank account to hold sinking fund money. It obtained a report from a project consultant that provides an estimate of the forecast non-recurrent expenditure of the Adelaide Oval over a 50-year period and the required annual sinking fund contribution.

Sinking fund

AOSMA made a contribution of $2.8 million to the sinking fund in 2016-17. This amount was based on the updated 50-year forecast of expenditure provided by the project consultant. The amount was approved by the Treasurer. Payments totalling $780 000 were made out of the sinking fund in 2016-17 (refer note 3 of AOSMA's financial report). The balance of the sinking fund as at 31 October 2017 was $4.7 million.

Leasing and licensing arrangements

AOSMA leases from the SA Government the Adelaide Oval Core Area which includes the stadium. The rent payable by AOSMA to the SA Government over the 80-year term of the lease is expected to be $74.3 million before indexation. Rent was not payable for the lease period before 1 July 2015. AOSMA is required to pay the annual lease fee by 31 July each year. In July 2017 AOSMA paid $400 000. The land situated in the Adelaide Oval Core Area is leased by the SA Government from the Adelaide City Council for an equal term at $1 p.a.

AOSMA has licensed the SANFL the exclusive right to play football at the oval during the football season from 15 March to 7 October for a term of 20 years, with a right of renewal for three further 20-year terms. The licence enables the SANFL to enter into arrangements with the AFL and football clubs for the use of the oval. Likewise, AOSMA has licensed SACA the exclusive right to play cricket at the oval during the cricket season from 8 October to 14 March for a term of 80 years. The licence enables SACA to enter arrangements with CA for the use of the oval. The licences preserve AOSMA's right to hold ad hoc events, such as concerts, at the oval at any time provided sufficient notice is given to the SANFL and SACA.

The Adelaide City Council has also licensed the SA Government to use the area closely surrounding the stadium for a 20-year term for no fee, with a right of renewal for three further 20-year terms. The SA Government has sublicensed the use of this area to the SANFL, SACA and AOSMA for an equivalent term for a fee of $10 each p.a.

Commercial Operations Trust

In 2015-16, the COT was established and a company was set up and appointed as trustee to operate the Adelaide Oval roof climb in the Adelaide Oval Core Area. AOSMA licensed the COT to operate the roof climb from 1 July 2016 to 16 November 2031. The issuing of the licence was approved by the Minister. AOSMA also entered into a service agreement with the COT which enables AOSMA to manage the roof climb business on behalf of the COT. The associated licence and management fees as outlined in the agreements are recognised in the financial statements. Net ticket sales collected on behalf of the COT for the year were $1.25 million.

Insurance

AOSMA is required by the leasing and licensing requirements for the management of the Adelaide Oval to maintain certain insurance policies including public risk liability insurance and property insurance against material damage to the stadium. The required policies were in place for the year.

Adelaide Venue Management Corporation (AVMC)

Financial statistics

Income from trading activities:	$60.9 million
Profit from trading activities:	$11.4 million
Loss from property management activities:	$20.5 million
Net loss:	$9.1 million
Number of FTEs:	485

The following information on the number of events held and patrons attending these events was provided by AVMC and is unaudited.

	2018 Number	2017 Number
Adelaide Entertainment Centre:		
Events	106	93
Patrons	302 000	249 000
Coopers Stadium:		
Events	14	17
Patrons	175 000	191 000
Adelaide Convention Centre:		
Events/Functions	754	855
Patrons	292 000	262 000

Significant events and transactions

The redeveloped Adelaide Convention Centre opened in August 2017. The redevelopment cost $396.8 million, with $382.3 million funded from borrowings and $14.5 million from the Future Asset Replacement account.

Financial report opinion

Unmodified

Financial controls opinion

Unmodified

Functional responsibility

The AVMC was established by Regulations under the *Public Corporations Act 1993*. It is responsible to the Minister for Tourism.

The main function of the AVMC is to manage and operate the Adelaide Convention Centre, the Adelaide Entertainment Centre and Coopers Stadium. For details of the AVMC's functions refer note 2 of the financial report.

Scope of the audit

The audit program covered major financial systems to obtain sufficient evidence to form an opinion on the financial report and internal controls.

Specific areas of audit attention in 2017-18 included:

- revenue from events, restaurants, bars and car parks
- salaries and wages
- expenditure on supplies and services
- inventory.

Audit findings and comments

Communication of audit matters

Matters identified by the audit were detailed in a management letter to the Chief Executive Officer. While there were no major matters raised, we recommended that the AVMC implement some review processes over its time recording system. We received a positive response from the AVMC.

Interpretation and analysis of the financial report

Highlights of the financial report

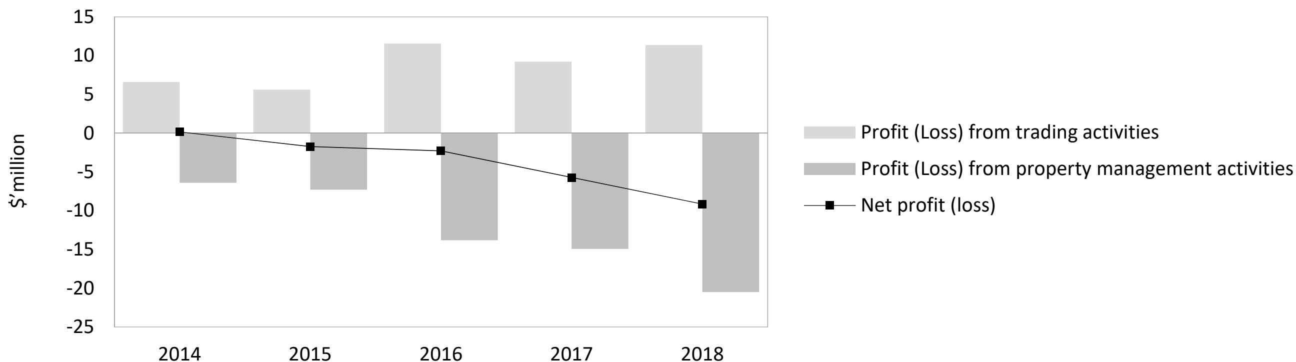
	2018 $'million	2017 $'million
Trading activities		
Expenses	50	41
Income	61	50
Profit (Loss) from trading activities	11	9
Property management activities		
Expenses	45	39
Income	25	24
Profit (Loss) from property management activities	(20)	(15)
Net profit (loss)	(9)	(6)
Other comprehensive income		
Change in asset revaluation surplus	10	-
Net cash provided by (used in) operating activities	30	27
Net cash provided by (used in) investing activities	(20)	(71)
Net cash provided by (used in) financing activities	(21)	49

	2018 $'million	2017 $'million
Assets		
Current assets	38	45
Non-current assets	653	649
Total assets	691	694
Liabilities		
Current liabilities	21	23
Non-current liabilities	388	388
Total liabilities	409	411
Total equity	282	283

Statement of Comprehensive Income

The AVMC recorded a net loss of $9.1 million for 2018.

The following chart shows the profits (losses) from trading and property management activities and the AVMC's net profits (losses) for the five years to 2018.



Profits from trading activities are not sufficient to cover the losses from property management activities.

Over the past three years of the five years represented, profits from trading activities have remained relatively steady while losses on property management activities have grown. The operations of the Adelaide Convention Centre became part of the AVMC from 2016.

The net loss for 2017-18 increased by $3 million to $9 million. The profit from trading activities has increased by $2 million to $11 million and the loss from property management activities has increased by $5 million to $20 million. The increase in the loss from property management activities is a result of the increased depreciation from the completed redevelopment of the Adelaide Convention Centre.

Profit from trading activities

The AVMC's income from trading activities totalled $61 million and mainly comprised catering revenue ($29.1 million) and venue hire revenue ($11 million).

Expenses from trading activities amounted to $49.6 million and mainly comprised employee benefits expenses ($29.2 million) and supplies and services expenses ($16 million).

Loss on property management activities

Expenses from property management activities were $45.5 million and mainly comprised depreciation ($13.8 million) and borrowing costs ($19.1 million).

The AVMC received $24.2 million in funding from the SA Government, which fully compensated borrowing costs and contributed to property management activities associated with the Adelaide Convention Centre site maintenance of the common areas and the Riverbank Precinct.

Statement of Financial Position

The main item in the AVMC's Statement of Financial Position is property, plant and equipment, representing 93% of total assets. The carrying value of property, plant and equipment is $640.9 million, which includes land and buildings of $617.4 million and plant and equipment of $20.7 million.

The AVMC revalued its land and buildings at 30 June 2018, resulting in a revaluation increment of $9.6 million.

The AVMC's main assets are the Adelaide Convention Centre and the Adelaide Entertainment Centre buildings. The redevelopment of the Adelaide Convention Centre cost $396.8 million, with $382.3 million funded from borrowings and $14.5 million from the Future Asset Replacement account. The redeveloped Adelaide Convention Centre opened in August 2017.

Liabilities as at 30 June 2018 totalled $409.3 million and mainly comprised borrowings of $382.3 million and payables of $6.4 million.

Statement of Cash Flows

Cash and cash equivalents reduced to $31.5 million ($38.3 million) at 30 June 2018.

The AVMC had a net cash inflow from operating activities of $29.9 million for the year while cash used in investing activities was $20.2 million, primarily for payments associated with the Adelaide Convention Centre redevelopment.

Cash used in financing activities was $20.7 million and comprised borrowing costs of $19.1 million and dividends paid to the SA Government of $1.6 million.

Dividends are paid in line with the AVMC's Performance Statement.

Administered items

The AVMC administers, but does not control, gross box office receipts from its ticketing agency. These receipts are held in separate event funds bank accounts. Settlement occurs after each event through the payment of funds held to promoters, the AVMC and other service providers. Total administered revenues for the year were $35 million and administered expenses were $27.3 million. The balance of funds held in trust as at 30 June 2018 was $15 million.

Attorney-General's Department (AGD)

Financial statistics

Employee benefits expenses:	$164 million
Net cost of providing services:	$117 million
Revenues from SA Government:	$111 million
Number of FTEs (includes administered):	1553.6
Administered income:	
Taxation revenue	$268 million
Fines and related fees	$91 million
Revenues from SA Government	$126 million
Victims of Crime levies	$39 million
Administered expenses:	
Payments to Consolidated Account	$347 million
National Redress Scheme payment	$146 million

Significant events and transactions

- $146.4 million was paid to SAicorp from the Victims of Crime Fund for the costs associated with South Australia participating in the National Redress Scheme people who have experienced institutional child sexual abuse.
- An additional $22 million was paid to the Legal Services Commission representing the 2018-19 State contribution to the Commission. The revised timing of this payment partially offsets the impact of reduced State funding to the Commission in 2018-19.
- The functions of the Office of the Police Ombudsman were transferred to the Office for Public Integrity from September 2017.
- SafeWork SA was transferred to the Department of the Premier and Cabinet from 1 July 2018.
- On 23 January 2018, the Governor of South Australia established a Royal Commission to investigate the operations and effectiveness of the Murray-Darling Basin system.

Financial report opinion **Unmodified**

Financial controls opinion	**Modified**
	Key issues: — No regular review or evidence of review of user access to a number of systems — No contract management plan established for the debt collection partner contracts with the Fines Enforcement and Recovery Unit — Key payroll reports not reviewed promptly and time attendance records not completed or approved promptly — Business processes in Consumer and Business Services and SafeWork SA require improvement

Functional responsibility

AGD is an administrative unit established under the *Public Sector Act 2009.*

The functions of AGD are to help create an inclusive, safe and fair South Australia. AGD promotes justice by protecting rights and holding people to account according to the law, improving safety and contributing to an efficient and fair justice system.

Notes 1, 2(c), 4 and A1 of the AGD's financial report provide further information on AGD.

Scope of audit

The audit program covered major financial systems to obtain sufficient evidence to form an opinion on the financial report and internal controls.

Specific areas of audit attention in 2017-18 included:

- cash and debtors
- non-current assets
- payroll and employee entitlements
- revenue
- taxation receipts
- statutory funds
- Crown Solicitor's Trust Account
- fines revenue and collection
- SafeWork SA
- financial accounting and reporting
- financial management performance program.

The audit took into account the controls and procedures performed by service providers including Shared Services SA (SSSA).

The work of AGD's internal auditors was also considered in planning and conducting the audit.

Audit findings and comments

Assessment of controls

In my opinion, the controls exercised by the Attorney-General's Department in relation to the receipt, expenditure and investment of money, the acquisition and disposal of property and the incurring of liabilities, except for all matters outlined under 'Communication of audit matters', are sufficient to provide reasonable assurance that the financial transactions of the Attorney-General's Department have been conducted properly and in accordance with law.

Communication of audit matters

Matters identified by the audit were detailed in management letters to the Chief Executive and other officers responsible for the governance of AGD's controlled and administered activities. The main matters raised and related responses are detailed below.

Payroll

Employee benefits expenses for both controlled and administered activities totalled $176 million for 2017-18, while employee benefits liabilities totalled $55 million as at 30 June 2018.

Key payroll reports not reviewed promptly

We found AGD's bona fide and leave return reports were not always reviewed promptly, signed or dated to evidence prompt review by the relevant manager. We also found instances where these reports could not be located. This finding is consistent with prior years. We note there were improvements in the prompt review of reports for some of the business units we tested.

The prompt review of bona fide and leave return reports provides assurance that:

- payments to employees are valid and authorised
- leave taken by employees is completely and accurately recorded.

AGD advised that it had reminded management of the need to review and certify bona fide and leave return reports promptly. AGD will also consider the option of targeted monitoring after implementation of the new bona fide and leave return reporting system developed by SSSA.

Time worked and leave requests not approved

Most AGD business units use TimeWise to record time worked and apply for leave. Our review of the Manager Reminder Report for the three most material pay points for the pay periods between 24 June 2017 to 2 March 2018 identified many instances where:

- timesheets were completed but not approved by the manager
- timesheets were not completed

- sick leave requests were not approved
- special leave requests were not approved.

Completing and approving timesheets and leave requests provides assurance that:

- time recorded by employees is accurate
- leave taken by employees is approved and accurately recorded.

A similar issue was raised last year.

AGD advised it is currently reviewing its time and attendance policy. Once completed HR will highlight to managers the need to certify attendance records promptly. AGD will also consider the possibility of targeted monitoring for compliance in this area.

Financial management

Policies and procedures

Treasurer's Instruction 2 'Financial Management' requires that policies and procedures are properly documented and regularly reviewed, revised where necessary and readily available to relevant staff.

Our review of policies and procedures across a number of business units identified:

- a number that were overdue for review
- a number that did not reflect current practices
- a number in draft format that were awaiting approval
- some that did not have an issue date or review date.

AGD advised it would review and update all outstanding policies and procedures, as well as updating, reviewing and signing its financial management policies and republishing them on its intranet. AGD also undertook to document any review or amendments made to these policies.

South Australian Government Radio Network (SAGRN)

No independent review of monthly financial reconciliation

The SAGRN asset management policy requires the SAGRN Manager, Operational Services Delivery to review and approve the monthly financial transactions reconciliation. This reconciliation ensures all asset acquisitions are capitalised and recorded in the asset register and is used to prepare monthly journals to record SAGRN transactions in the general ledger. We found that the monthly reconciliations were prepared but there was no evidence of independent review and approval. A similar issue has been raised in previous years.

AGD advised that the Manager Governance will be responsible for independently reviewing, signing and dating the monthly financial transactions reconciliation. The SAGRN asset management policy will be updated accordingly.

Crown Solicitor's Office (CSO)

Review of LawMaster user access

Our review of the LawMaster user access review process found:

- the LawMaster security procedure requires a monthly access review, but in practice the review is performed bi-monthly
- an employee list is used during the review, however it does not show employees who are on long-term leave or temporarily assigned to another business unit. This may result in these employees not having their access removed when they leave the CSO
- an access change request form is not completed when an employee leaves the CSO. Employee departures instead are identified through a monthly productivity report sent to managers. Managers check to ensure that employees on the report still require access to LawMaster. However, this is not the main purpose of the productivity report and no response is required.

AGD advised that CSO has updated the procedure to reflect the bi-monthly process, which is the current practice. CSO will establish a formal process to identify employees who are on long-term leave or in temporary positions to ensure access is removed promptly.

Timeliness of Victims of Crime (VOC) quarterly review

CSO Business Services performs a quarterly review of VOC payments by testing a sample of finalised claims to ensure the controls for the assessment and payment of claims have been appropriately applied. Business Services prepares a memorandum to the Crown Solicitor advising him of the outcome of testing.

Our review of the quarterly reviews completed at the time of the audit found that the review and subsequent memorandum to the Crown Solicitor was not completed promptly. We recommended the procedure for the quarterly review of payments be updated to specify a time frame for completion.

AGD advised that CSO has updated the procedure to specify that reviews are to be conducted by the end of the following quarter.

SafeWork SA

In 2017-18 licence fees collected by SafeWork SA totalled $6.8 million.

Our audit of SafeWork SA identified that:

- in 2016-17 the Point of Sales (POS) and InfoNet revenue collection system reconciliations were not performed after April 2016. This reconciliation ensures that payments receipted in POS are accurately recorded in InfoNET as there is no interface between the systems. In 2017-18 we found SafeWork SA were performing POS to InfoNet reconciliations and following up variances for 2016-17. At the time of our audit, April 2018, SafeWork SA had not yet commenced reconciliations for 2017-18

- the review of the InfoNet user access was inconsistent and it was unclear who was responsible for reviewing users for each area. The super user listing was reviewed by an officer with this type of access and there were no policies and procedures for reviewing user access to the BPoint and POS revenue collection systems
- a number of policies and procedures were overdue for review and draft procedures had been developed but were waiting approval.

AGD advised that the business improvement project to interface POS with InfoNET will be completed in November 2018. Work has started on clearing the backlog of reconciliations and this work is to be completed by December 2018.

AGD also advised that its policy and procedure for managing InfoNET users is under review and will be completed by September 2018. The procedure will specify that the manager is responsible for ensuring user access reviews are completed for their team and the super user listing will be reviewed by the Manager, Corporate Services.

SafeWork SA will ensure that procedures are regularly reviewed to align with current practices and work has commenced on registering all procedures to support this process.

Consumer and Business Services (CBS)

In 2017-18 licence and regulatory fees collected through the LOGIC revenue collection system totalled $26.7 million and the total collected for gaming and taxation revenue was $267.8 million. Total fees collected for issuing birth, death and marriage certificates through the Promadis revenue collection system were $6.3 million.

Our audit of CBS identified that:

- a number of policies and procedures were overdue for review, had no version control or did not reflect the current practices of CBS. In addition, we found there was no cross reference between applicable AGD corporate policies and CBS policies and procedures and there were overlaps between CBS policies
- reviews of user access for POS were not performed quarterly. After our inquiry in May 2018, a POS user access report review identified a number of employees who no longer required access to POS and employees who had not had their access suspended
- the LOGIC to general ledger reconciliation, which ensures revenue receipted in LOGIC is completely and accurately reflected in the general ledger, had not been prepared or reviewed promptly
- monthly gaming tax reconciliations to ensure all calculated tax is recognised in the AGD's financial reports were not always prepared promptly and not all supporting documentation was retained
- the independent reviewing officer does not check LOGIC to ensure that all data from the Independent Gambling Authority has been completely and accurately imported, as no supporting documentation is attached to the reconciliation. Further, this officer does not check that the tax rates entered into LOGIC for the calculation of the gaming tax are correct. These checks are important as the same officer loads the gambling revenue data in LOGIC and performs the gaming tax calculations.

AGD advised that:

- CBS will review and update the policies and procedures identified and conduct a broader review across the branch. CBS intends to develop a centralised storage and management system to ensure policies and procedures are readily available to staff, as well as routinely reviewed and updated as required
- the policy for the LOGIC to general ledger reconciliation will be updated to include a time frame for completion of reconciliations and staff will be reminded of the importance of timely reconciliations. CBS will continue to work with LOGIC developers to resolve the inaccurate reporting issue
- a hard copy of supporting documentation for the monthly gaming tax reconciliation will be maintained and attached to the reconciliation
- a screenshot of tax thresholds showing both the tax and net gambling revenue will be printed for the reviewer as evidence that tax thresholds were correctly entered.

Residential Tenancies Fund

As at 30 June 2018 total bonds lodged with the Residential Tenancies Fund were $196.7 million.

Bond Management System (BMS) user access reviews not performed

Our review of BMS user access in 2017-18 found that there was no evidence of user access reviews prior to January 2018, reviews were not completed promptly and users identified as no longer requiring access were not removed. We have previously raised these issues over a number of years.

AGD indicated that CBS has introduced the use of issue tracking and project management software that will track, maintain evidence and provide alerts when the next review is due.

Bond lodgement and refund audits not performed

Our review of bond lodgement and refund audits from July 2017 to February 2018 found that bond audits were not completed within 30 days of the end of each month and that the October 2017 audits were not reviewed until December 2017. These audits ensure that manual bond lodgement and refund details have been entered correctly in the BMS. If they are not performed there is an increased risk that incorrect processing of transactions in BMS may not be promptly identified and corrected. We have previously raised this issue over a number of years.

AGD responded that CBS would remind staff of the importance of preparing and reviewing bond audits promptly, in line with its policies. The policies will be updated to include the need for review by an independent officer.

Residential Tenancies Fund and Residential Parks bank reconciliation not reviewed promptly

The March 2018 Residential Tenancies Fund and Residential Parks bank reconciliations were not reviewed until May 2018 and the October 2017 Residential Parks bank reconciliation was not prepared and reviewed until December 2017. We raised similar issues last year.

In the absence of regular review, reconciliation variances may not be identified and addressed promptly.

AGD advised that CBS will remind staff of the importance of preparing and reviewing reconciliations promptly.

Unclaimed bonds

In 2016-17 we identified that CBS did not have a policy or procedure to provide guidance on when bonds should be recognised as unclaimed and how to manage unclaimed bonds. Our follow-up in 2017-18 found that no policy or procedure was developed. We note that as at March 2018, unclaimed bonds totalled $10.1 million.

We also found the March 2018 unclaimed bonds reconciliation included an unexplained variance of $74 000 which had been fluctuating since the introduction of the residential bond on-line system.

AGD advised that CBS has started to develop an unclaimed bonds policy outlining the method for calculating the liability and how unclaimed bonds should be managed. CBS is considering developing a public register to assist public access to unclaimed bonds. This will reduce the volume of unclaimed bonds over time.

We were also advised that the cause of the unexplained variance in the unclaimed bonds reconciliation has been identified. CBS will continue to work with the system developers to identify each individual transaction and eliminate this variance.

Fines Enforcement and Recovery Unit (FERU)

As at 30 June 2018, the balance of outstanding debt managed by the FERU was $404 million.

Debt collection contract management

In 2016, the Attorney-General entered into a debt collection deed with two debt collection companies (debt partners), Dun and Bradstreet and National Credit Management Limited. The contracts are managed by the FERU.

We reviewed the contract management process to determine if:

- a contract management plan had been established
- performance based debt distribution had commenced and performance targets established in line with the contract terms
- there are policies for when the FERU sends debt packages to debt partners
- debt partner contracts have been effective in reducing the level of long-term outstanding debt (including the debt originally transferred to the FERU).

Our review identified areas where the FERU could improve its contract management controls as:

- the FERU does not have a formal contract management plan in place. We identified that the FERU had developed a contract compliance checklist, however this only represents one element of contract management
- performance based debt distribution is not occurring. The debt partner contracts include assessing performance against key performance indicators and distributing debt packages between debt partners based on their performance. The FERU is internally monitoring performance, however KPIs used by the FERU have not been formally agreed and documented to assess debt partners' performance.

AGD advised that:

- the FERU is currently developing the following documents to support a complete and comprehensive contract management approach:
  - debt partners contract management plan
  - debt partners performance management plan
  - debt partners contract compliance guidelines
- the implementation of the new recovery management system on 18 June 2018 provides capacity for optimising debt distribution to the panel of debt partners. Due to the new system's implementation, there is no debt active with either of the debt partners. The FERU is negotiating key result areas and performance expectations with a view of recommencing referrals by early October 2018. To date debt partners have consistently maintained a return on investment equal to and exceeding $5 for every $1 of expenditure.

Shared Services SA – financial systems and transaction processing environments

SSSA processes financial transactions on behalf of AGD under service level determinations. The main systems and control environments include accounts payable, payroll and general ledger financial functions.

Our review and evaluation of controls for these systems concluded that controls were effective for 2017-18.

SSSA is discussed further in the commentary under 'Department of the Premier and Cabinet' in this Report.

Interpretation and analysis of the financial report

Highlights of the financial report – controlled items

	2018 $'million	2017 $'million
Expenses		
Employee benefits expenses	164	158
Supplies and services	70	68
Other expenses	17	17
Total expenses	251	243
Income		
Revenues from fees and charges	106	102
Recoveries	17	18
Other	11	8
Total income	134	128
Net cost of providing services	117	115
Revenues from SA Government	111	117
Net result	(6)	2
Total comprehensive result	(6)	2

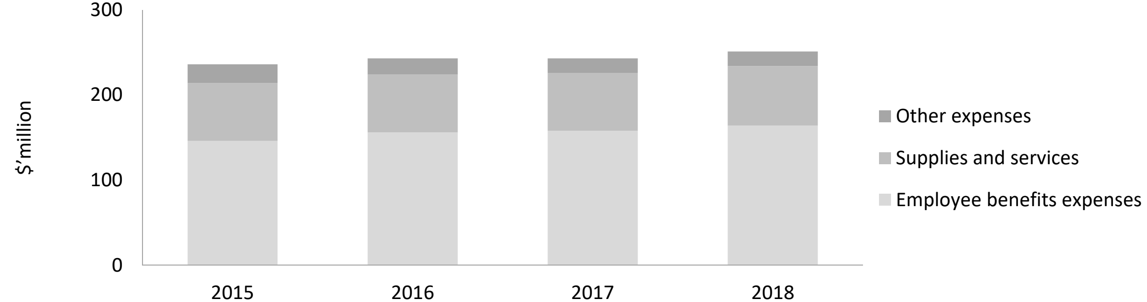
	2018 $'million	2017 $'million
Net cash provided by (used in) operating activities	(10)	15
Assets		
Current assets	45	57
Non-current assets	35	33
Total assets	80	90
Liabilities		
Current liabilities	30	33
Non-current liabilities	41	41
Total liabilities	71	74
Total equity	9	16

Statement of Comprehensive Income

Expenses

In 2017-18 total expenses increased by $8 million to $251 million. This is mainly due to an increase in employee benefits expenses of $6.4 million and an increase in supplies and services of $1.7 million.

The following chart analyses the main expense items for AGD for the four years to 2018.



Employee benefits expenses total $164 million and represent 65% of total expenditure. They increased by $6.4 million due mainly to the impact of enterprise bargaining agreement indexation, with increases in salaries and wages of $4.6 million and associated employment on-costs of $975 000. Salaries and wages include termination payments of $1.4 million which includes the former Chief Executive's pay-out on termination of her contract. Long service leave increased by $927 000 partly due to the transfer of employees from other government agencies with large outstanding balances.

Supplies and services expense is dominated by operating lease/accommodation costs of $23.9 million ($23.6 million) and ICT expenses of $17.7 million ($16.6 million), representing 59% (59%) of total supplies and services.

Income

AGD collected $106 million ($102 million) in fees and charges, which represents 79% (80%) of total income excluding revenues from the SA Government. Fees and charges collected in 2017-18 mainly comprise $60.2 million of licence and regulatory fees, $23.7 million in legal services fees and $12.5 million of network services fees.

The increase in fees and charges of $4.6 million is mainly due to the $3.4 million increase in licence and regulatory fees, with licence fees collected by CBS increasing by $870 000 and licence fees collected by SafeWork SA increasing by $2.5 million. In addition there was a $1.2 million increase in the recovery of expenditure as costs recovered from CBS were up $783 000 and costs recovered from the VOC Fund were up $365 000.

In 2017-18 $2.1 million of services were received free of charge from SSSA, as the SA Government ceased the intra-government charging model for services provided by SSSA to general government sector agencies.

Revenues from the SA Government decreased by $6.7 million to $110.7 million, mainly due to decreases in funding of:

- $2.2 million for efficiency dividends
- $2 million as SSSA ceased billing general government sector agencies
- $1 million due to the transfer of the Police Ombudsman function to the Office for Public Integrity from September 2017
- $900 000 in mid-year budget review savings
- $600 000 as salaries indexation was reduced to 1.5%.

Statement of Financial Position

Total assets decreased by $10 million to $79.9 million. This decrease is mainly due to a decrease in cash of $17.3 million. The decrease in cash was offset by increases in intangible assets, up $1.5 million, and receivables, up $5.6 million. Refer to commentary under 'Statement of Cash Flows' below for further explanation of the decrease in cash.

Intangible assets increased by $1.5 million due to additions to work in progress of $3.6 million, offset by amortisation of $2.2 million.

In 2017-18, $12.5 million was transferred from work in progress to computer software as the following systems became operational:

- $6.1 million for the Laboratory Information Management system used by Forensic Science SA
- $1.4 million for the Prosecution Management system used by the Office of the Director of Public Prosecution
- $3.5 million for the RMS Fines system used by the FERU
- $1.2 million for the system used by AGD for records management.

The increase in receivables of $5.6 million is mainly due to an outstanding $4.4 million recoup from administered CBS funds as at 30 June 2018.

Liabilities decreased by $3.2 million to $71.1 million mainly due to a decrease in payables of $3 million and lease incentive liability of $673 000. These decreases were offset by an increase in employee benefits of $759 000.

The decrease in payables is mainly due to a decrease in accrued expenses and creditors as at 30 June 2018 of $3.1 million. In 2016-17 accrued expenses included $1.1 million for the purchase of ICT hardware, $800 000 for records management system licensing and $800 000 for office lease rental.

The decrease in the lease incentive liability is due to the transfer of the Office of the Police Ombudsman accommodation to the Office for Public Integrity.

The increases in employee benefits liability included $109 000 for annual leave and $690 000 for long service leave. Annual leave and long service leave increased due to the transfer of employees from other government agencies and their accrued leave, as well as increases in rates of pay.

Statement of Cash Flows

The decrease in cash of $17.3 million was due to:

- a decrease in revenue received from the SA Government of $6.7 million due to budget saving initiatives of $3.1 million and a reduction in funding of $3.6 million. Refer to commentary under 'Income' above
- an increase in employee benefit payments of $7.6 million
- an increase in payments for supplies and services of $8.1 million
- an increase in the purchase of fixed assets of $1.6 million
- a decrease in other receipts of $1 million
- a decrease in fees and charges of $2.6 million.

Highlights of the financial statements – administered items

The administered items of AGD are identified in note A1 to the administered financial statements.

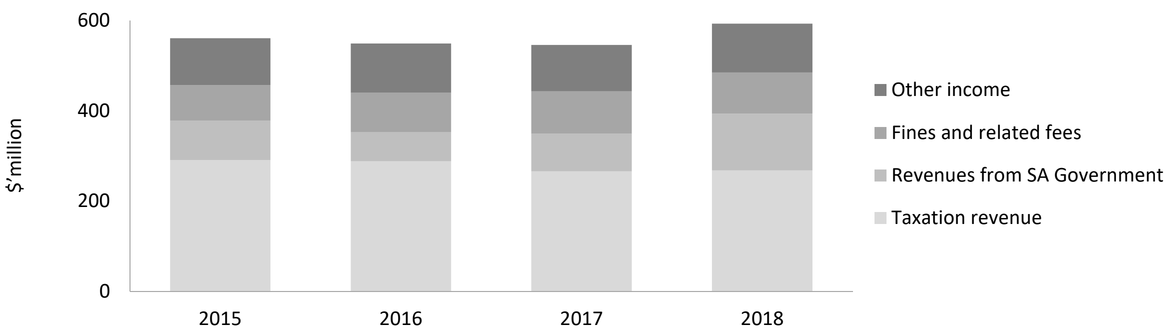
	2018 $'million	2017 $'million
Expenses		
Payments to Consolidated Account	347	348
National Redress Scheme	146	-
Grants and subsidies	67	46
Other expenses	107	104
Total expenses	667	498
Income		
Taxation revenue	268	266
Revenues from SA Government	126	83
Fines and related fees	91	94
Victims of Crime levies	39	42
Other income	69	61
Total income	593	546
Net revenue from (cost of) providing services	(74)	48
Total comprehensive result	(74)	48

	2018 $'million	2017 $'million
Net cash provided by (used in) operating activities	(65)	60
Assets		
Current assets	308	401
Non-current assets	97	77
Total assets	405	478
Liabilities		
Current liabilities	44	43
Non-current liabilities	2	2
Total liabilities	46	45
Total equity	359	433

Statement of Administered Comprehensive Income

Income

The following chart analyses the main sources of AGD's administered income for the four years to 2018.



Taxation revenue ($268 million) represents 45% of total administered income, with fines and related fees ($91 million) and VOC levies ($39 million) accounting for a further 22% of the total.

Total administered income increased by $47 million to $593 million ($546 million). The main components of this increase were as follows:

- Taxation revenue – increased by $2.1 million due to increased taxation from gaming machines. The tax is collected on behalf of the SA Government under the *Gaming Machines Act 1992*.
- Revenue from the SA Government – increased by $43.3 million as additional appropriation of $22 million was received for the 2018-19 State contribution to the Legal Services Commission. The revised timing of this payment partially offsets the impact of reduced State funding to the Commission in 2018-19. There was also an increase in appropriation for the SAGRN project of $13 million in 2017-18 which mainly reflects appropriation carried over from 2016-17.
- SAGRN recoveries – increased by $3.3 million mainly due to an increase of $2.7 million in usage and access charges from government agencies

- Recoveries and other income – increased by $4.5 million mainly due to:
  - an increase in sundry recoveries of $3 million representing the additional amounts recovered for SAGRN network services
  - confiscation of profits by South Australia Police increasing by $989 000. These amounts are deposited in the VOC Fund
  - recoveries from the use of the State Rescue Helicopter Services, which increased by $623 000
  - a decrease of $463 000 in gaming machine trading round revenue as less trading rounds were held in 2017-18.

These increases were offset by the following:

- Fines and related fees decreased by $3.1 million. This is mainly due to a decrease in fees collected on South Australia Police expiations and Court imposed fines of $1.1 million as more offenders entered into arrangements prior to fines being overdue. In addition, fines received from other entities decreased by $1.6 million.
- VOC levies income decreased by $3 million which directly reflects the decrease in fines and related fees, as more offenders entered into arrangements prior to fines being overdue.

Expenses

Total administered expenses increased by $170 million to $668 million. Payments to the Consolidated Account of $347 million (mainly for gaming taxation), $146 million payment for the National Redress Scheme and grants and subsidies of $67 million, principally paid to the Legal Services Commission, are AGD's largest administered expenses and represent 84% of total expenditure.

The increase in total expenses is mainly due to:

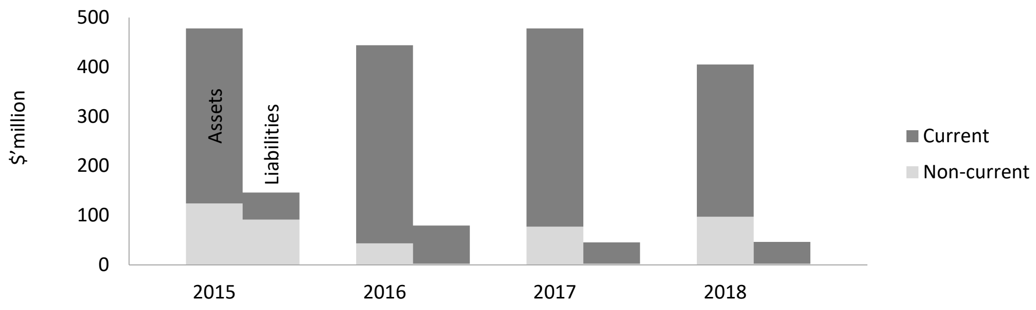
- a $146.4 million payment to SAicorp for the costs associated with South Australia participating in the National Redress Scheme for people who have experienced institutional child sexual abuse. This payment is discussed under 'Victims of Crime Fund' below
- a $20.7 million increase in grant and subsidies payments. This mainly relates to an additional payment of $22 million to the Legal Services Commission due to the change in timing of the State contribution payment as previously discussed. This increase was offset by a decrease in liquor subsidies of $1.2 million as the Cellar Door Liquor Subsidy Scheme ceased in 2016-17, a decrease in other grants of $1.3 million as payments for expensive criminal cases decreased by $601 000 and the domestic violence safety program of $664 000 which is now funded by the Department of Human Services
- an increase in VOC payments of $1.6 million due to an increase in the number and average value of compensation payments
- an increase in employment benefits expenses of $2.5 million largely due to an increase in salaries and wages of $642 000, long service leave of $1.1 million and annual leave of $281 000. This is mainly due to the establishment of the Murray-Darling Basin Royal Commission which included the transfer of employees from other government agencies
- an increase in net loss on disposal of non-current assets of $4.1 million that was due to the disposal of SAGRN assets as part of the SAGRN upgrade.

These increases were offset by decreases in:

- donated assets of $3.8 million as in 2016-17, $3.7 million of State Rescue Helicopter Services assets were transferred to South Australia Police
- other expenses of $910 000 mainly due to a decrease in suitor payments of $1.7 million and a decrease in native claim payments of $1.4 million. These decreases were offset by an increase in SAGRN expenditure of $2.1 million.

Statement of Administered Financial Position

The following chart analyses the administered assets and liabilities of AGD for the four years to 2018.



Total assets decreased by $72 million to $405 million. This was mainly a result of a decrease in cash and cash equivalents of $95 million, offset by an increase in receivables of $2.9 million and an increase in property, plant and equipment of $19.4 million.

The decrease in the cash position as at 30 June 2018 is mainly due to the $146.4 million National Redress Scheme payment and an increase in grant and subsidy payments of $20.7 million which includes the 2018-19 State contribution paid to the Legal Services Commission. This was offset by additional receipts from SA Government of $43.3 million. This is discussed further under 'Statement of Administered Cash Flows' below.

The major administered asset is the SAGRN. There is a major project underway to upgrade the SAGRN which resulted in additions to work in progress of $29.7 million. This increase was offset by depreciation of $5.5 million and the disposal of SAGRN assets of $4.8 million.

Other liabilities of $36 million ($33.6 million) represent 77% (76%) of total liabilities and are primarily made up of amounts owing to the Department of Treasury and Finance for gaming taxation, fines and other receipts. The increase in other liabilities of $2.4 million is mainly due to a $3 million increase in unearned revenue for the SAGRN. This was offset by a $1.4 million decrease in the holdings in the Crown Solicitor's Trust Account, with total funds held at 30 June 2018 being $2.8 million.

Statement of Administered Cash Flows

The net cash provided by operating activities decreased by $125 million, reflecting primarily an increase in cash used in operations of $168.2 million compared with the previous year. The major components of this increase were:

- $146.4 million paid to SAicorp for the National Redress Scheme

- additional grants payments of $20.7 million including the early payment of the 2018-19 State contribution to the Legal Services Commission.

This was offset by an increase in cash provided by operations of $43.2 million. This is mainly due to an increase in receipts from the SA Government of $43.3 million, as an additional $22 million was received from the SA Government for the early payment of the 2018-19 Legal Services Commission funding and an additional $13 million carry-over of funding for the SAGRN upgrade project.

Further commentary on operations

Fines Enforcement and Recovery Unit

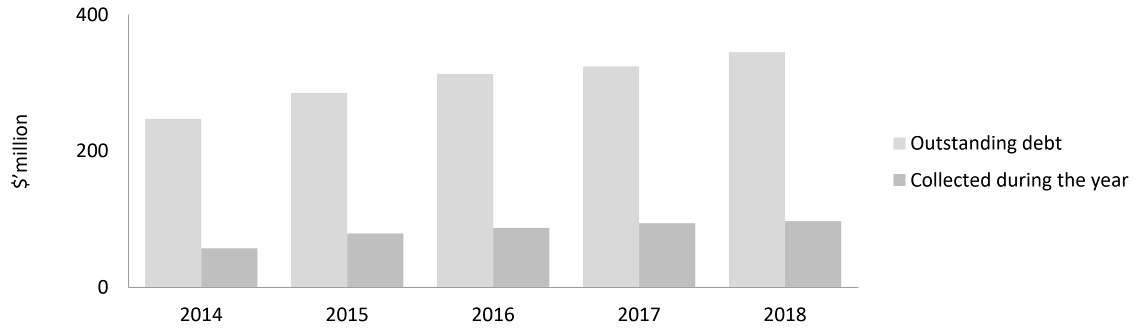
The FERU collects outstanding fines and related payments (suitor amounts and fees and charges associated with overdue amounts). The FERU performs this function for court fines, expiation fees (including overdue local government amounts referred) and other outstanding amounts, including VOC levies and third party suitor amounts.

As at 30 June 2018, the balance of debt managed by the FERU was $403.6 million ($379.1 million), which includes $39.5 million that is not yet due. This comprises:

- fines – $223.2 million ($207 million)
- VOC levies – $58.2 million ($54.6 million)
- FERU fees – $122.2 million ($117.4 million).

$139.7 million ($133 million) of the debt relates to Court penalties while $263.9 million ($246.1 million) relates to expiation notices.

The following chart shows the total outstanding debt from fines and related fees (excluding VOC levies) and total collections over the last five years.



The 2014 collections were undertaken by the Courts Administration Authority until February, and the FERU after that date.

The chart highlights that, while outstanding debts have continued to increase, the level of collections since the FERU was established increased significantly in 2015 with further increases in 2016 and 2017. The increased collections reflect different collections management by the FERU and the use of powers to suspend dealings with the Registrar of Motor Vehicles or drivers licences (amongst other powers available).

Outstanding amounts are not recorded in the Statement of Administered Financial Position as there is significant uncertainty about the amount that will be collected. Instead, revenue is recorded in the Statement of Administered Comprehensive Income when money is received.

In 2017-18 fines lodged with the FERU totalled $172.1 million ($171.2 million). These exclude fines that have been quashed as they should not have been raised. Total collections of $118.4 million ($124.5 million), including VOC amounts, included $102.5 million ($106.5 million) collected on behalf of the SA Government and $16 million ($18 million) on behalf of non-government entities, including local government councils.

In 2016-17 the FERU engaged a panel of external debt collectors to help collect outstanding amounts, particularly those that were more difficult to recover. Previously this service was provided by one debt collection agency. The total outstanding amounts collected by debt collection agencies is $15.9 million, with $11.7 million collected in the previous year.

Of the $403.6 million ($379.1 million) in total outstanding debt and related payments, $303.4 million ($306.5 million) is under active management, with $120.6 million ($125.8 million) subject to payment arrangements, $39.5 million ($40 million) subject to arrangements prior to fines being overdue and $39 million ($32.6 million) not owed to the State. $49.6 million ($24.9 million) of fines were referred to debt collection agencies in 2017-18. This increase was due to the full-year operation of the outsourced collection contracts and an increase in referrals to panellists prior to the implementation of the new system.

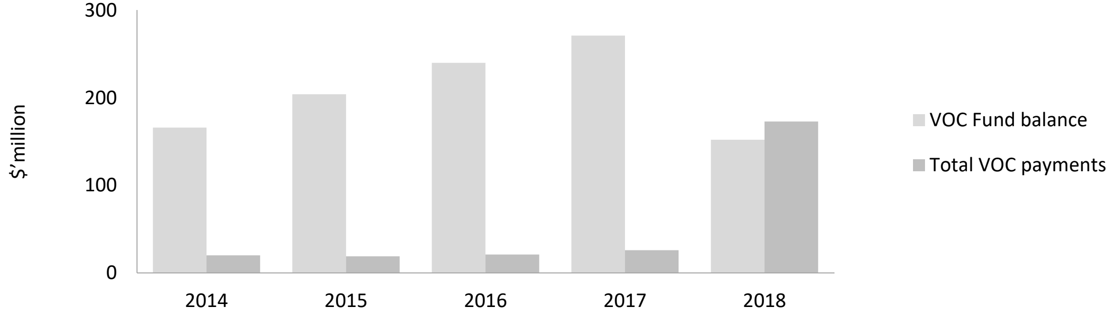
The FERU replaced its fines management system in 2017-18 with a commencement date of 19 June 2018.

Victims of Crime Fund (VOC Fund)

AGD is responsible for administering the *Victims of Crime Act 2001* (VOC Act). The VOC Fund is reported in AGD's administered financial statements.

The balance of the VOC Fund as at 30 June 2018 was $152.7 million ($270.6 million).

The following chart shows the balance of the VOC Fund and the value of total payments from the fund over the last five years.



The maximum compensation that can be awarded under the VOC Act is $100 000, in addition to costs and disbursements. A claim can succeed without a known offender.

Compensation is paid where an offence has been admitted or proven beyond reasonable doubt. In cases where no one has been charged with an offence, the applicant's evidence must be corroborated. Where an offence has not been established, the Attorney-General has discretion to make an ex gratia payment to the claimant.

Recoveries from offenders

The VOC Act empowers the Attorney-General to recover the cost of compensation payments from offenders who were convicted of the relevant offence. Recovery is difficult as most compensation claims are for unknown offenders. This is demonstrated by the following data:

- The amounts recovered directly from offenders during the year totalled $1.2 million ($807 000).
- Outstanding amounts at 30 June 2018 were $88.8 million ($90.7 million). $14.1 million ($27.1 million) of this amount is the subject of a judgement and is being actively managed. The remaining $74.7 million ($63.6 million) represents amounts paid in compensation for which no judgement has occurred or is likely to occur because the offenders have either not been identified or prosecuted as yet.

A further $2.8 million ($1.5 million) was recovered from offenders under the *Criminal Asset Confiscation Act 2005.*

A levy is imposed by the VOC Act on all people convicted of offences and on expiation notices. Total VOC income for 2017-18 was $54.8 million ($55.8 million) and included VOC levies of $39 million ($42 million) and revenues from the SA Government of $8.6 million ($8.4 million).

Payments from Victims of Crime Fund

Total VOC expenses for 2017-18 were $173.5 million ($25.7 million) and included:

- victims compensation and legal payments of $18.9 million ($17.3 million)
- grants of $4.4 million ($4.3 million)
- legal and other costs incurred in the administration of the VOC Fund of $3.7 million ($4.1 million)
- a $146.4 million payment to SAicorp for the National Redress Scheme.

The net cost for the VOC Fund in 2017-18 was $118.7 million.

National Redress Scheme for people who have experienced institutional sexual abuse

The Royal Commission into Institutional Responses to Child Sexual Abuse recommended the establishment of a National Redress Scheme for people who have experienced institutional child sexual abuse. The Commonwealth Government is leading the development of the scheme, which the States and non-government institutions are invited to participate in.

In May 2018 the SA Government agreed that South Australia would participate in the scheme.

The Commonwealth Department for Social Services commissioned independent modelling, performed by the Infinity Group and PricewaterhouseCoopers, into the likely cost of each State to opt into the National Redress Scheme.

Based on this work, the estimated cost to the SA Government of full participation in the scheme is $146.4 million. This figure includes monetary compensation, counselling, legal support and a contribution towards the administration of the scheme.

On 18 June 2018 a payment of $146.4 million was made from the VOC Fund to SAicorp, who will administer the scheme for South Australia. The payment was approved by the Attorney-General who, in line with section 31(1) of the VOC Act, has an absolute discretion to make payments to government and non-government organisations where the purpose of the payment is to advance the interests of victims of crimes.

Taxation

Taxation revenue for 2017-18 totalled $268 million ($266 million). This mainly comprises gaming machine taxes totalling $268 million ($265 million).

Gaming machine administration

Section 5 of the *Gaming Machines Act 1992* (GM Act) provides that the Liquor and Gambling Commissioner is responsible to the Independent Gambling Authority for scrutinising the operations of all licensees under the GM Act.

Under the GM Act, the operations of gaming machines in licensed premises must return winnings to players of not less than 85% in the case of machines installed before 31 May 2001, and 87.5% in the case of machines installed after that date. A prescribed percentage of the net gambling revenue is then paid to the Treasurer (Consolidated Account).

In July 2011 a trading system was introduced to allow eligible people to purchase and sell gaming machine entitlements. Full details are prescribed in the Gaming Machines Regulations 2005.

Under the new trading system the purchase price of a gaming machine entitlement is not fixed. This means that when a trading round is announced an eligible person can submit a written offer to:

- purchase a gaming machine entitlement and specify the highest price they would be willing to pay for the entitlement if their offer was accepted
- sell a gaming machine entitlement and specify the lowest price they would be willing to accept as payment for the entitlement if their offer was accepted.

The following table summarises gaming machine activity for the four years to 2018.

	2015 Number	2016 Number	2017 Number	2018 Number
Machines installed as at 30 June	12 377	12 337	12 210	12 142

	2015 $'million	2016 $'million	2017 $'million	2018 $'million
Turnover	8 055	8 000	7 595	7 576
Amount won	7 329	7 282	6 915	6 894
Net gambling revenue	726	719	680	682
Tax	287	284	265	268

Independent Gaming Corporation Limited (IGC)

Under section 25 of the GM Act, the Liquor and Gambling Commissioner granted the Gaming Machine Monitor licence to the IGC. Under this licence the IGC monitors the operations of gaming machine licensees.

Section 75 of the GM Act specifically provides for the accounts and operations of the IGC to be audited by the Auditor-General.

With respect to the 2017-18 operations, the audit of the IGC is complete and an unmodified Independent Auditor's Report was issued for its 2017-18 financial report.

Residential Tenancies Fund (RTF)

The *Residential Tenancies Act 1995* (RT Act) is administered by the Commissioner for Consumer Affairs. The RTF consists of amounts received by the Commissioner by way of security bonds and other amounts paid into the RTF under the RT Act. The Commissioner will refund security bonds from the RTF under the RT Act.

Income derived from investing the RTF is applied to the costs of administering and enforcing the RT Act, educating landlords and tenants about their statutory and contractual rights and obligations, and certain functions of the South Australian Civil and Administrative Tribunal (which undertakes the functions previously performed by the Residential Tenancies Tribunal).

Security bonds received by the Commissioner in 2017-18 increased by $5.3 million to $101.7 million ($96.4 million). Security bonds refunded for 2017-18 increased by $1.6 million to $88.6 million ($87 million).

The value of bonds held as at 30 June was $196.7 million ($188.5 million) and the value of unclaimed bonds was $8.6 million ($3.3 million).

Investment funds totalling $241.7 million are held by the Public Trustee in common funds. These are exposed to movements in the value of the underlying common fund assets. Investments increased by $22.2 million in 2017-18.

Murray-Darling Basin Royal Commission

On 23 January 2018, the Governor of South Australia established a Royal Commission to investigate the operations and effectiveness of the Murray-Darling Basin system.

The Royal Commission can obtain information for the inquiry by seeking relevant documents, taking evidence from people who have relevant experiences with the Murray-Darling Basin and receiving formal written submissions from people or organisations.

The Royal Commission is expected to report by 1 February 2019. Costs incurred to date for the Royal Commission totalled $2.5 million.

Public Trustee

Financial statistics	Profit before income tax equivalents:	$1.175 million
	Fees and charges revenue:	$22.6 million
	Number of FTEs:	184.2
	Number of estates under administration:	7834
	Total value of trust funds under administration:	$1.7 billion

Significant events and transactions

- The Public Trustee retired in March 2018 and an acting Public Trustee was appointed until 30 June 2019.
- An Independent Commissioner Against Corruption report on the Public Trustee was tabled in Parliament in September 2017. There were a number of recommendations made. A large number of them have been implemented, with a few actions still in progress.
- An additional $19.5 million was invested by the Consumer and Business Services funds and the Retail Shop Leases Fund.
- An additional $4.1 million was paid to Australian Super to ensure customers would receive the maximum financial benefits associated with superannuation.

Financial report opinion

Unmodified

Financial controls opinion

Modified

Key issues:

- The strategic plan and IT strategic plan were not updated at the time of the audit
- Masterpiece user access profiles assigned to some staff were incompatible with their job responsibilities
- The general ledger to payroll system reconciliation had not been performed since July 2017
- Limited support is available to Peoplesoft application and operating system environment
- Monitoring of user accounts with excessive access in Peoplesoft and HI Portfolio was not performed

Functional responsibility

The Public Trustee is a body corporate established under the *Public Trustee Act 1995*.

The powers and functions of the Public Trustee are established by the *Public Trustee Act 1995*. The Public Trustee administers the estates of deceased and protected people who need asset management assistance, prepares wills, provides investment services and arranges legal representation and advice.

Scope of the audit

The audit program covered major financial systems to obtain sufficient evidence to form an opinion on the financial report and internal controls.

The 2017-18 audit covered the corporate, trust and common fund operations of the Public Trustee. Specific areas of audit attention included:

- corporate governance
- expenditure
- payroll
- revenue
- cash and investments
- client assets
- fund manager reporting
- general ledger
- IT general controls.

Audit findings and comments

Assessment of controls

In my opinion, the controls exercised by the Public Trustee in relation to the receipt, expenditure and investment of money, the acquisition and disposal of property and the incurring of liabilities, except for all matters outlined under 'Communication of audit matters', are sufficient to provide reasonable assurance that the financial transactions of the Public Trustee have been conducted properly and in accordance with law.

Communication of audit matters

Matters identified by the audit were detailed in management letters to the Public Trustee. The main matters raised and the responses received are detailed below.

Governance arrangements

Public Trustee strategic plan

The Public Trustee's strategic plan for 2014-2017 expired on 31 December 2017. We found that at the time of the audit a new strategic plan had not been developed or implemented as the Public Trustee

was waiting on the SA Government's response to the an Independent Commissioner Against Corruption (ICAC) evaluation report and a change in leadership was pending due to the upcoming retirement of the Public Trustee. As a result the ICT strategic plan had also not been updated.

The Acting Public Trustee advised that by 30 June 2018 a new two-year strategic plan would be developed that focuses on the Public Trustee's purpose and objectives, including a set of measurable action items. The intention was to complete the ICT strategic plan by 31 August 2018.

We received a copy of the Public Trustee's 2018-2020 strategic plan and the ICT strategic plan in June 2018.

Policies and procedures

Treasurer's Instruction 2 'Financial Management' TI 2 clause 2.5 requires agencies to ensure that policies, procedures and systems are properly documented and regularly reviewed, revised where necessary and readily available to staff. In addition, the Public Trustee's policy framework states that documents are due for review and update at least every two years, or more often if impacted by changes to legislation, work practices or systems.

Our review of policies and procedures across a number of branches identified:

- a number that were overdue for review
- a number that did not reflect current practices
- that no procedures had been established for certain processes.

The Public Trustee advised that it would ensure that:

- all outstanding procedures would be reviewed and the senior management agenda would include a standing item to ensure all policies due for review are actioned
- those policies and procedures that were identified would be updated to reflect current practices
- where processes were not documented a policy or procedure would be developed.

Corporate services

Masterpiece – inappropriate user access profiles

Our review of Masterpiece user access found that user access profiles assigned to some staff were incompatible with their job responsibilities. Instances included:

- several corporate services staff and ICT network and support staff had system administrator access
- staff responsible for processing accounts payable and accounts receivable transactions had access to vendor maintenance and were also able to create journals
- most corporate services staff could make changes to the chart of accounts.

We found a similar issue in 2016-17.

The Public Trustee responded that it had identified segregation issues. It had also identified changes to profiles but were waiting on Shared Services SA (SSSA) to implement the changes prior to 30 June 2018. Once implemented there will be no corporate staff with administration rights and vendor maintenance will be separated from the accounts receivable and accounts payable functions.

The Public Trustee noted that there were mitigating controls to prevent unauthorised processing and inaccurate data, including:

- separate sign-off and independent review of vendor changes
- all journals are independently reviewed and approved
- general ledger transactions and variances to budget are reviewed as part of the month-end process.

Timeliness of payroll reconciliations

TI 2 requires regular and timely reconciliations between the general ledger and subsidiary systems.

We identified that the last completed and reviewed reconciliation between the Masterpiece general ledger and the Chris21 payroll system was July 2017. We also found that this reconciliation was not documented in any policy or procedure.

The Public Trustee responded that it would perform the reconciliation on a monthly basis from April 2018, develop a new procedure and the monthly corporate finance checklist would be updated to include the reconciliation.

The Public Trustee also advised that it had completed the year-to-date salary reconciliation and no material variances were identified.

Trust operations

Review of payment file audit logs

Each time a payment file is created in Peoplesoft, it is saved in a folder until it is loaded into CommBiz and paid. The accounts receivable supervisor reviews the audit log for the folder daily to identify any unusual activity, using an audit log report generated each night.

We were informed that the audit log storage system was full from 20 December 2017 to 9 January 2018, after which ICT resolved this issue with the service provider. During this period, there was no audit log of files saved to the payment file folder. As they could not be retrospectively generated, there was no review for unusual activity.

The Public Trustee responded that an alert will be put in place to advise ICT that the folder has reached capacity. ICT staff will then clear out the folder to ensure that there is sufficient storage capacity to generate audit logs. The audit log review will be monitored to ensure that it is conducted daily.

Real estate insurance review

To minimise the risk associated with customer assets the Public Trustee requires all insurable customer assets, including improved real estate, to be insured. At the end of the month two reports are generated, one listing all properties where no expiry date is recorded and the other listing all properties where insurance policies are expired.

We identified that these two reports were not run on a monthly basis, and there were inconsistencies in how Personal Estates and Deceased Estates reviewed the reports and reported on findings. We note that Personal Estates has a mitigating control as the annual review of estate files includes a review of insurance policy renewal.

In response, the Public Trustee advised that it will generate reports identifying cases with no insurance details monthly and this process would be included in the end of month action list.

We were also advised that the:

- procedures will be updated to ensure managers and team leaders are provided with monthly reports to review to ensure appropriate insurance coverage is held
- Manager Personal Estates and the Manager Estate Services will ensure that monthly reports for insurance are actioned by team leaders.

Information technology audit

Limited support applied to Peoplesoft application and operating system environment

Previous audit reviews of the Public Trustee's ICT environment have identified issues about outdated systems environments for its core business information system, Peoplesoft Financials and Customer Relationship Management. Software vendor maintenance for Peoplesoft expired in December 2010, with support limited to sustaining support.

These applications continue to reside on outdated operating systems.

The Public Trustee previously advised that the operating systems could not be updated until Peoplesoft is upgraded or replaced. We are aware that the Public Trustee has a number of partial mitigating controls and is continuing to pursue options to replace the Peoplesoft environment, but that this is contingent on funding.

The Public Trustee advised that, as part of its 2018-2020 ICT strategic plan, a review of long-term ICT priorities will be undertaken. Replacement of the systems and the associated business change is likely to require further investment. Work to further define business requirements and to explore possible market solutions will commence in 2018-19. Reforms using existing resources will be implemented as a first priority.

In the interim, the ICT area will improve business practices, implement system enhancements and manage cyber security risks in line with the SA Government's Information Security Management Framework.

Lack of segregation of duties for development and production

In 2016-17 we identified a lack of segregation of duties applied to developer accounts. We found that two Peoplesoft user accounts had the ability to develop system changes and then migrate these changes into the production environment. These users also had administrative functions in the production environment.

We recommended that the Public Trustee monitor the activities of user accounts with excessive access. The Public Trustee responded that it would review user accounts to ensure that access granted by roles is aligns with the responsibility required.

In 2017-18 we found that the annual review of user roles did not include the review of account activity for users with excessive access. Therefore, the risk associated with excessive access still existed.

We also found that two user accounts for HiPortfolio had access to both development and production environments, as well as access to perform administrative functions.

The Public Trustee responded that the current ICT environment does not allow for practical separation of duties in the Peoplesoft and HiPortfolio systems. The relevant accounts had been reviewed to ensure that access granted by roles is aligns with the responsibilities required.

Controls would be strengthened to identify all changes performed with separate privileged administrative accounts and to determine if automated controls can be implemented to monitor privileged user account activity.

Independent Commissioner Against Corruption evaluation

In 2017-18 ICAC evaluated the operations of the Public Trustee and the 'Evaluation of the Practices, Policies and Procedures of the Public Trustee' report was tabled in Parliament on 26 September 2017. There were a number of recommendations made which the Public Trustee has actioned in 2017-18.

As at 30 June 2018 the following actions had been completed by the Public Trustee:

- established a quality control position and commenced quality control reviews
- undertook an extensive staff engagement program
- established a Workplace Consultative Committee
- reviewed, simplified and consolidated procedures
- audited a sample of high risk/complexity files representing each operational aspect of the organisation
- finalised the ICT strategic plan and work plan
- engaged a procurement specialist to manage contracts and undertake business critical procurements
- developed a data breach and privacy policy
- improved initial customer contact practices

- developed a plan to address key findings from the employee culture and wellbeing report.

The following actions are currently in progress:

- developing a competency based training and induction program
- developing a reporting dashboard to monitor workloads, performance and equitable caseload allocation
- reviewing team structures
- developing idea generation forums to engage staff in business improvement programs.

Shared Services SA – payroll transaction processing environment

SSSA processes payroll transactions on behalf of the Public Trustee, as part of the overall arrangements for the Attorney-General's Department, under a service level determination.

Our review and evaluation of controls for the payroll system concluded that controls were effective for 2017-18.

SSSA is discussed further in the commentary under 'Department of the Premier and Cabinet' in this Report.

Interpretation and analysis of the financial report

Highlights of the corporate financial report

	2018 $'million	2017 $'million
Income		
Fees and charges	23	21
Other revenues	2	2
Total income	25	23
Expenses		
Employee benefits	16	15
Supplies and services	7	7
Other expenses	1	1
Total expenses	24	23
Profit (Loss) before income tax equivalents	1	-
Income tax equivalents*	-	-
Profit (Loss) after income tax equivalents and total comprehensive result	1	-
Net cash provided by (used in) operating activities	2	2
Assets		
Current assets	9	9
Non-current assets	24	23
Total assets	33	32

	2018 $'million	2017 $'million
Liabilities		
Current liabilities	4	3
Non-current liabilities	5	5
Total liabilities	9	8
Total equity	24	24

* Income tax equivalents expense of $352 000 in 2017-18 ($179 000).

Statement of Comprehensive Income

Income

The Public Trustee's main source of income is fees and charges, which principally comprise commissions from managing trusts and management fees for investing in common funds. During 2017-18 fees and charges income increased by $1.2 million to $22.6 million.

Common fund management fees are set at 1% p.a. (charged monthly) in line with the *Public Trustee Act 1995*, based on the level of funds invested. These fees have increased by $423 000 as a result of the increase in funds under management in Common Funds from $1.026 billion to $1.07 billion during 2017-18.

Commissions increased by $702 000 as the collection of commissions is directly affected by the types and number of estates being administered and the nature of the assets held.

Personal estate commissions increased by $466 000 and deceased estates commissions increased by $236 000. The number of personal estates administered and the funds under administration increased by 1%. Although the number of deceased estates administered decreased by 2.8%, the increase in commissions was due to the higher value of estates administered for the period.

Financial market movements in 2017-18 resulted in a $396 000 increase in the market value of financial assets due to favourable markets across all sectors. In 2017-18 there were gains in the Australian equities, the Fixed Interest sectors and Property sectors. Although there was an overall gain in the overseas equities sectors the gain was not as large as in 2016-17.

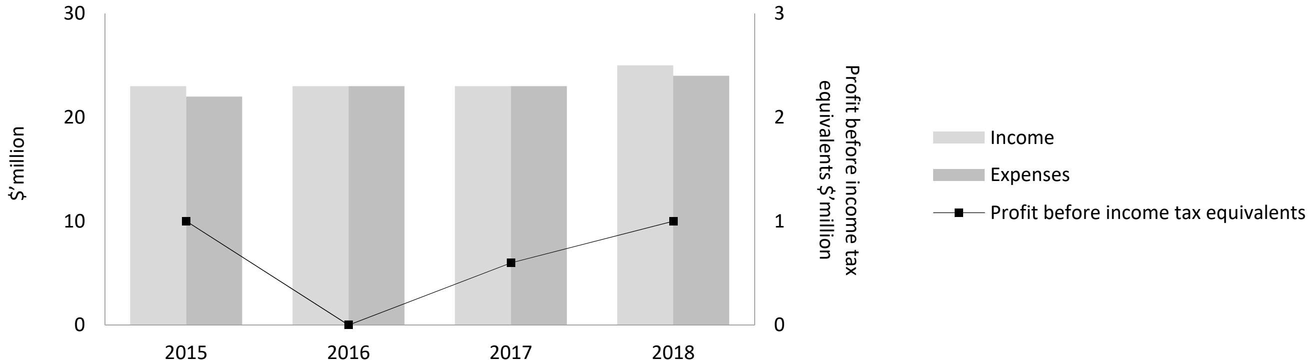
Expenses

Employee benefits account for 68% of total expenses and increased by $845 000 to $16.1 million in 2017-18. The increase in employee benefits is due the enterprise bargaining agreement increase and 10 additional temporary staff employed from February 2018.

Supplies and services increased by $72 000 to $6.6 million ($6.5 million). The increases was mainly due to an increase in resources seconded from SA Government of $193 000 to clear the back log of work within estate operations. There was also an increase in information technology costs of $42 000. This was offset by decreases in service contractors and other supplies and services of $282 000, as 2016-17 results included the costs associated with responding to a fraud in the personal estates area.

Net result

The following chart shows income, expenses and profit before income tax equivalents for the four years to 2018.



Profit before income tax equivalents of $1.1 million ($598 000) increased mainly due to higher fees and charges income and an increase in unrealised gains on financial assets. These increases were offset by higher supplies and services costs and employee benefits expenses.

Statement of Financial Position

Assets

Financial assets of $22 million represent 67% of total assets. Financial assets increased by $1.2 million, resulting from an increase in unrealised gains of $396 000 and an increase in the money deposited into the Corporate investment portfolio of $804 000.

This increase was offset by a decrease in the value of property, plant and equipment and intangible assets of $740 000. The decrease was mainly due to depreciation and amortisation expenses of $949 000, offset by purchases of plant and equipment and intangible assets of $210 000.

Liabilities

Employee benefits of $5.8 million represent 68% of total liabilities and payables of $2.1 million represent 25% of total liabilities.

The increase in employee benefits of $90 000 is mainly due to an increase in accrued salaries of $25 000 and annual leave of $137 000, as since February 2018 the Public Trustee has employed 10 additional temporary staff. These increases were offset by a decrease in long service leave of $72 000 due to the retirement of long standing employees and the transfer of employee leave balances to other government agencies.

Payables increased by $359 000 mainly due to an increase in trade creditors and accrued expenses of $313 000.

Statement of Cash Flows

Cash and cash equivalents decreased by $352 000 to $7.6 million in 2018. The main factors contributing to this decrease were:

- a $605 000 decrease in net cash provided by operating activities which was impacted by increases in cash outflows for employee benefits payments, up $742 000, tax equivalent payments, up $267 000, and GST remitted to the ATO, up $154 000; a decrease in investment income of $189 000 and tax equivalent receipts of $168 000; and offset by an increase in fees and charges of $879 000

- net cash used in investing activities increasing by $552 000 due to an $802 000 increase in the purchase of financial assets, offset by a $250 000 decrease in the purchase of plant and equipment and intangible assets

- net cash used in financial activities increasing by $842 000 due to the increase in the dividend paid to SA Government.

Interpretation and analysis of Statement of Trusts being Administered

The value of trust funds administered by the Public Trustee as at 30 June 2018 was $1.7 billion ($1.6 billion).

Detailed below are the number and value of trust funds under administration for the last two years.

	2017 Number	2018 Number	2017 $'000	2018 $'000
Deceased estates	1 331	1 297	181 540	211 928
Trusts	1 280	1 256	126 970	123 403
Administration matters	348	352	43 599	48 254
Court award orders	823	792	416 420	436 501
Protected estates	3 497	3 610	343 842	355 832
Workers compensation awards	6	7	323	348
Power of Attorney	296	284	55 457	61 531
Investors	246	236	384 568	421 677
	7 827	7 834	1 552 719	1 659 474

Of the total funds being administered, 62% (64%) were invested in the common funds with the remaining 38% (36%) represented by other estate assets.

The two largest categories of other estate assets are real estate assets of $358 million ($333 million) and superannuation of $150 million ($139 million).

Further commentary on operations

Common fund financial reports

The Public Trustee operates seven common funds through which client funds are invested. These funds are:

- Cash

- Short-term Fixed Interest
- Long-term Fixed Interest
- Overseas Fixed Interest
- Australian Shares
- Overseas Shares
- Property.

Analysis of common fund key figures

The common funds' assets in 2017-18 totalled $1.07 billion, increasing by $44 million from $1.026 billion in 2016-17.

Movements in common fund assets reflect movements in investment markets and in total funds invested as a result of changes to the number and value of estates under administration each year.

The following table summarises the annual net operating result and value of assets held for each common fund at 30 June 2018 and 30 June 2017.

	Net operating result		Assets	
	2017	2018	2017	2018
Common fund	$'000	$'000	$'000	$'000
Cash	9 201	9 395	*484 165	*534 289
Short-term Fixed Interest	1 032	689	56 505	59 867
Long-term Fixed Interest	779	1 212	93 245	96 931
Overseas Fixed Interest	861	557	54 341	54 948
Australian Shares	22 815	27 782	169 486	189 719
Overseas Shares	20 000	12 400	146 609	153 741
Property	4 988	7 962	103 919	106 577

* Includes $126 million ($82 million) deposited by other common funds.

The Public Trustee invests client money in the common funds by purchasing units in one of five standard investment strategies (SISs). Each SIS involves investments in the various common funds, with the proportion invested in each fund depending on the underlying investment strategy. Allocations for each SIS are the result of strategic asset allocation decisions that aim to provide appropriate strategies to match client circumstances with the SIS risk profiles.

In 2017-18 a further $19.5 million was invested in the Public Trustee from the Residential Tenancies Fund, the Agents Indemnity Fund and the Second-hand Vehicles Compensation Fund. The funds were received throughout the year, with $6.1 million invested in the Balanced SIS and $6.3 million invested in the Capital Stable SIS, and the remaining retained in cash. The $12.4 million was allocated across the following common funds: Cash ($1.4 million), Short-term Fixed Interest ($2.1 million), Long-term Fixed Interest ($2.2 million), Overseas Fixed Interest ($1.4 million), Australian Shares ($1.9 million), Overseas Shares ($1.7 million) and Property ($1.7 million).

The investment of Residential Tenancies Fund, Agents Indemnity Fund and Second-hand Vehicles Compensation Fund money was approved by the Attorney-General and the investment strategy adopted was approved by the Commissioner for Consumer and Business Services, who has responsibility for managing these funds.

The table below details the performance of each SIS and its performance against Public Trustee's established benchmarks as at 30 June 2018. These figures have been provided by Public Trustee and are unaudited.

Standard investment strategy		1 year %	3 years %	5 years %
Cash	Performance	1.79	1.94	2.33
	Benchmark	0.77	0.95	1.22
Capital stable	Performance	4.34	4.05	4.95
	Benchmark	3.78	3.45	4.34
Balanced	Performance	7.08	6.13	7.38
	Benchmark	6.34	5.23	6.70
Growth	Performance	9.32	7.58	9.05
	Benchmark	8.30	6.37	8.15
Equities	Performance	12.62	10.05	11.84
	Benchmark	12.27	8.49	10.76

The performance of each SIS against benchmarks for 2017-18 was good overall with all exceeding the established benchmark.

Net operating result

In 2017-18 all common funds achieved a net operating profit. However, the results when compared with the previous year were mixed, with the net result for some funds increasing while others decreased. This reflects the relative market performance of different asset classes.

In 2017-18 there was a change in the management fee calculation methodology. The management fee is now based on total assets (including cash) in each common fund, with the Cash common fund having its fee levied on total assets less cash attributable to other common funds. This resulted in an increase in management fees for each common fund, with a corresponding decrease in the Cash common fund. There was no overall dollar impact on the total management fees. The revised methodology will better reflect the management fee payable between each common fund. The change in methodology was attributable to the high levels of cash held in each common fund in recent years.

The net operating result for the Australian Shares common fund increased by $5 million, mainly due to the $4.8 million increase in trust distributions as a result of the strong performance of Australian shares. The return on Australian shares for the year was 18.77% compared to 16.21% the previous year.

The Overseas Shares common fund net operating result decreased by $7.6 million mainly due to a $2 million decrease in trust distributions as a result of the market performance of fund managers. There was also a $5.4 million decrease in net gains on financial assets held at fair value. The market performance in 2017-18 was not as good as in 2016-17. The return on overseas shares for 2017-18 was 10.11% compared with 17.44% the previous year.

The net operating result for the Property common fund increased by $3 million mainly due to an increase in the net gain on financial assets held for sale of $8.7 million, offset by a decrease in distributions of $5.4 million. The overall increase represented favourable market movements, with the rate of return for the Property common fund being 9.43% compared to 5.21% the previous year.

The rates of return figures were provided by the Public Trustee and are unaudited.

All investments for the common funds are valued at market value, being market price at the reporting date.

Auditor-General's Department

Financial statistics	Net cost of providing services:	$16.8 million
	Total appropriation:	$17.3 million
	Audit fees:	$14.8 million
	Average number of FTEs:	125
Financial report opinion	**Unmodified**	
Financial controls opinion	**Unmodified**	

Functional responsibility

The Auditor-General's Department operates to assist the Auditor-General in discharging his/her statutory audit mandate.

Audit findings and comments

Under section 35(1) of the *Public Finance and Audit Act 1987*, the Governor, on the Treasurer's recommendation, appointed Nexia Edwards Marshall as auditor of the Department.

Nexia Edwards Marshall advised in their audit completion letter that there were no matters to communicate to the Department for attention.

Interpretation and analysis of the financial report

Highlights of the financial report

	2018 $'million	2017 $'million
Expenses		
Employee expenses	12.9	12.2
Other expenses	4.0	3.8
Total expenses	16.9	16.0
Revenues from (Payments to) SA Government	16.3	17.0
Total assets	6.0	6.3
Total liabilities	5.7	5.4

Department for Child Protection (DCP)

Financial statistics	Employee benefit expenses:	$190 million
	Grants and subsidies expenditure:	$113 million
	Contracted out-of-home care services (commercial care):	$106 million
	Net cost of providing services:	$522 million
	Total revenues from SA Government:	$521 million
	Number of FTEs:	1995.6
	Number of children in care at 30 June 2018:	3672

Significant events and transactions

- An additional $40 million of funding from the Governor's Appropriation Fund was received in 2017-18, mainly to meet the increased costs of children in care.
- The first elements of the *Children and Young People (Safety) Act 2017* were enacted on 26 February 2018, which required more sharing of information with carers, children and other agencies. The new Act represents a significant revision of legislative requirements in relation to child protection in South Australia.
- The remaining elements of the *Children and Young People (Safety) Act 2017* will come into force on 22 October 2018. The new Act requires all employees who work with children to have a psychometric test.

Financial report opinion

Unmodified

Financial controls opinion

Modified

Key issues:

- Governance arrangements continue to need management focus
- Commercial care expenditure processes need improving
- Weaknesses in IT management controls for the Connected Client and Case Management System
- Ineffective review of payroll reports

Functional responsibility

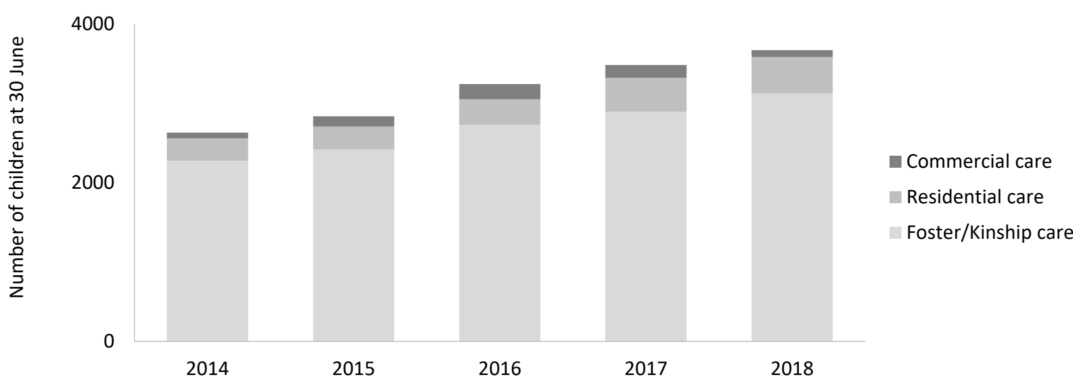
DCP was established on 1 November 2016

DCP commenced operations on 1 November 2016 and is an administrative unit established by the *Public Sector Act 2009*.

Functions

DCP's primary objective is to care for and protect children and young people who are at risk of abuse and neglect within their families, or whose families do not have the capacity to protect them.

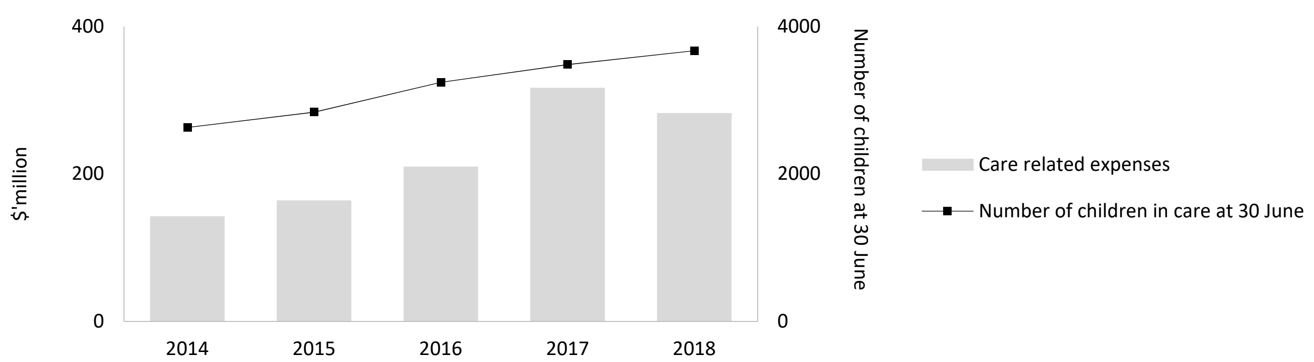
The graph below shows the number of children in care at 30 June for the last five years, separated by the type of care arrangement in place.



Source: Number of children at 30 June was sourced from the DCP website and is unaudited.

Of the children in care at 30 June 2018, 85% (83%) are in foster or kinship care, 13% (12%) are in residential care and 2% (5%) are in commercial care.

The number of children in care has risen by 40% in five years, while the total cost of care has almost doubled over the same period. The graph below shows the number of children in care at 30 June and the total care related expenditure for the past five years.



Source: Number of children at 30 June was sourced from the DCP website and is unaudited.

Scope of the audit

The audit program covered major financial systems to obtain sufficient evidence to form an opinion on the financial report and internal controls.

Specific areas of audit attention in 2017-18 included:

- governance arrangements
- accounts payable
- carer payments
- contracted out-of-home care services
- grant and subsidies
- incidental payments
- payroll
- purchase cards
- cash
- general ledger.

Audit findings and comments

Assessment of controls

In my opinion, the controls exercised by the Department for Child Protection in relation to the receipt, expenditure and investment of money, the acquisition and disposal of property and the incurring of liabilities, except for all matters outlined under 'Communication of audit matters', are sufficient to provide reasonable assurance that the financial transactions of the Department for Child Protection have been conducted properly and in accordance with law.

Communication of audit matters

Matters identified by the audit were detailed in management letters to the Chief Executive. The main matters raised and related responses are detailed below.

Governance arrangements continue to need management focus

We reviewed elements of DCP's governance arrangements. While we acknowledge that DCP has only existed as a separate entity for 20 months, we identified a number of areas needing management attention as a priority to ensure sound governance and accountability arrangements are firmly embedded within DCP's operations and culture.

No operational risk registers

We identified that DCP had established a risk management framework and policy, and documented its strategic risks, but there were no risk registers for the operational areas.

In our view, risks that are not appropriately identified and managed may impact DCP's ability to meet its objectives and could result in financial loss and other exposures. It is important for DCP to promptly establish structured processes to identify, assess, monitor and address all risks to ensure they are properly managed.

DCP responded that it was developing operational risk registers for key functions that are considered high risk with a view of having them in place by 30 June 2019.

Legal compliance processes have not been implemented

In November 2017 DCP's Senior Management Group approved a legislative compliance framework. This framework required:

- a central register of all legislation be established and maintained
- recording in the central register the divisions and personnel responsible for ensuring the legislation is complied with
- review processes, using a risk based approach, be implemented by responsible personnel.

We found:

- the central register had not been updated as significant legislative reforms around child protection, contained in the *Children and Young People (Safety) Act 2017*, had only been partly enacted
- divisions and personnel had not been assigned to the legislation in the central register
- there had not been a review of the processes implemented by responsible personnel.

DCP responded that it would ensure all areas of the legislative compliance framework, central register and responsibilities were allocated to the appropriate senior staff and would monitor compliance by 31 December 2018.

No external members on the DCP risk and audit committee

We noted that DCP did not have external members on its risk and audit committee.

The appointment of external committee members who can perform their role independently of the activities of management helps to ensure the audit committee acts objectively and impartially. This would enable DCP to receive advice and assurance from an independent perspective.

DCP advised it was undertaking a selection process for its risk and audit committee. It anticipated appointments would be made in late August 2018.

Policies and procedures need to be updated

DCP continued to apply a number of the Department for Education's (Education's) policies and procedures while developing and finalising its own policy documents. We were advised the process for DCP to establish its own policies and procedures may take up to two years, with finalisation targeted for late 2019.

DCP advised it would continue to work on developing its own policies and procedures.

Commercial care expenditure processes need improving

For 2017-18, the cost of contracted out-of-home care services or commercial care was $105.9 million and there were 86 children in commercial care at 30 June 2018.

Commercial care is an expensive care option and DCP has said it is working towards reduced reliance on this form of care. This is supported by the reduced number of children in commercial care in 2017-18. It is important that controls are in place and working effectively to ensure the proposed placement of a child in commercial care is appropriate and the projected cost impact is adequately considered by DCP.

All issues we identified in 2017-18 were repeat findings from 2016-17.

Commercial care placements and projected cumulative costs not always approved

Before children are placed in commercial care approval should be obtained, which involves calculating the projected cumulated costs of the placement.

We found a number of instances where commercial care placements were authorised a significant time after placements had commenced and payments were made.

DCP advised that on 1 July 2018 it implemented placement expiry reminder emails to be automatically sent from its case management system when a placement is due to end to ensure approvals are obtained before the end of the placement. The Financial Systems and Compliance Unit was also incorporating commercial care approval memorandums into its compliance program.

Cumulative commercial care costs are not always tracked

DCP's commercial care and accommodation approval process requires business support teams to accurately record cumulative projected and actual expenditure for each child in commercial care. This helps business support teams to track invoices for a child's commercial care placement against the approved estimated cost.

We found instances where:

- actual cumulative costs were not tracked or not regularly tracked
- the value of approved projected cumulative costs was not recorded
- a child's cumulative projected and actual expenditure was not being tracked.

DCP advised that from May 2018 the process of checking projected costs and recording and tracking cumulative costs has been performed by a central team, instead of the previous model which had various offices performing this task. This central team would be working to improve the management of both placements and costs by 30 June 2019.

Commercial care contracts have expired

DCP uses a panel of three contracted providers for the care of children and young people in commercial care.

These contracts expired on 31 December 2017.

Without a signed agreement, DCP does not have documented service levels and may not be able to recover payments made in instances where services provided do not meet DCP's expectations.

DCP advised that, as part of a broader reform process, it:

- would be moving to new models for care contracts
- has agreed to continue with the services under the same terms as the contracts that expired in December 2017 while it is moving to the new models for care contracts
- had commenced the process of renewing these contracts for a period of 12 months with a six-month extension option.

Weaknesses in IT management controls for the Connected Client and Case Management System (C3MS)

C3MS is a significant system used by DCP to support its operations, including recording investigations of child abuse or neglect, case management of children in care and determining payments for carers.

Data in C3MS is sensitive given the personal nature of case information recorded and tight controls are needed to properly protect and restrict access to this data to protect the privacy of clients.

We reviewed the management controls over the C3MS IT environments, which included following up the issues identified in a June 2016 internal audit report on C3MS requested by Education (when responsibility for child protection was part of Education).

We identified a number of areas that could compromise the integrity and security of C3MS:

- incomplete classification of C3MS data
- weaknesses in password configuration
- inappropriate assigning of user access
- no review of user access
- lack of database audit logs
- inadequate patch management
- lack of disaster recovery management
- weaknesses in vulnerability and threat management.

In response, DCP advised that its Chief Information Officer would lead the development of a program to address the identified areas of weakness in ICT general controls.

Ineffective review of key payroll reports

DCP had 1995.6 FTEs at 30 June 2018 and paid employee expenses of $190 million in 2017-18.

We reviewed a sample of bona fide certificates (BFCs) and monthly leave returns (MLRs) and found a significant proportion were not reviewed, or not promptly reviewed, by managers. We also found that most errors identified on BFCs related to incorrect reporting relationships in the payroll system, with many instances of staff being incorrectly included or excluded on BFCs.

Where BFCs and MLRs are not promptly checked, DCP has no assurance that only valid employees are paid, employees are paid correctly or leave balances recorded are accurate, impacting the reliability of associated liability balances.

In response DCP advised that Shared Services SA (SSSA) would distribute the new automated BFCs and MLRs from 22 June 2018, with DCP HR establishing a central monitoring and reporting process within four weeks of the distribution.

We understand the new automated BFCs and MLRs were implemented and we will review and evaluate the effectiveness of this process in 2018-19.

Shared Services SA – financial systems and transaction processing environments

SSSA processes financial transactions on behalf of DCP under service level determinations. The main systems and control environments include accounts payable, payroll and general ledger financial functions.

Our review and evaluation of controls for these systems concluded that controls were effective for 2017-18.

SSSA is discussed further in the commentary under 'Department of the Premier and Cabinet' in this Report.

Interpretation and analysis of the financial report

The comparative financial report for 2017 is for the eight months from 1 November 2016 to 30 June 2017.

Expenses and income from 1 July to 31 October 2016, for activities now performed by DCP, are included in Education's financial report comparative figures.

Highlights of the financial report

	2018 $'million	2017 $'million
Expenses		
Employee benefits expenses	190	112
Grants and subsidies	113	49
Contracted out-of-home care services	106	82
Supplies, services and other expenses	121	68
Total expenses	530	311
Income		
Commonwealth revenues, grants and contributions and other revenues	7	5
Revenues from fees and charges	1	1
Total income	8	6
Net cost of providing services	522	305
Revenues from SA Government	(521)	326
Net result	(1)	21
Total comprehensive income	(1)	23
Net cash provided by operating activities	7	16

	2018 $'million	2017 $'million
Assets		
Current assets	43	36
Non-current assets	40	41
Total assets	83	77
Liabilities		
Current liabilities	47	42
Non-current liabilities	44	42
Total liabilities	91	84
Total equity	(8)	(7)

Statement of Comprehensive Income (DCP and Education)

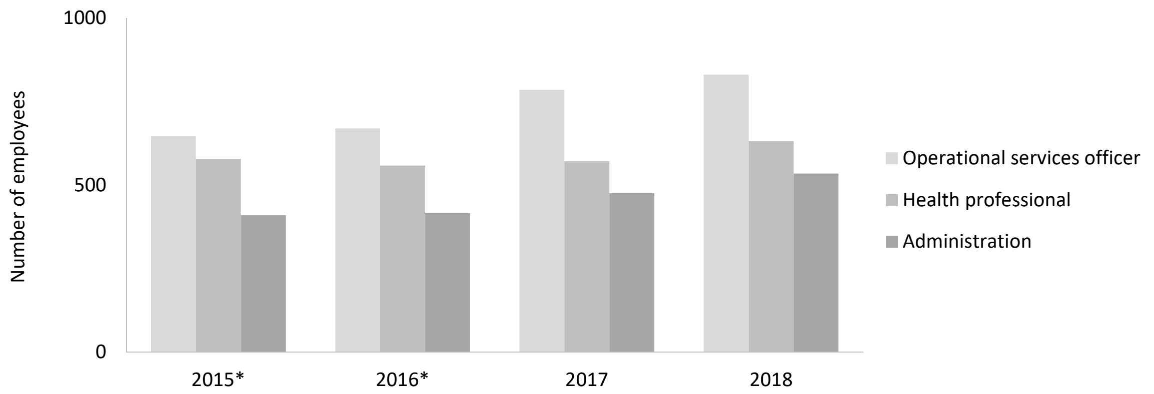
Expenses

Employee benefits expenses

Employee benefits of $190 million were DCP's main expense in 2017-18, accounting for 36% of total expenses.

There are currently 1995.6 FTEs. DCP budgeted to expand its workforce with an additional 463.9 FTEs to be recruited in 2017-18, but actually only recruited an additional 193.3 FTEs.

The following chart shows the number of FTEs by category over the last four years. Front line employees account for 73% of the total workforce, with the remaining 27% being administration employees. These percentages have remained constant even though the number of FTEs has increased.



* Number of child protection employees employed by Education when the child protection function was its responsibility.

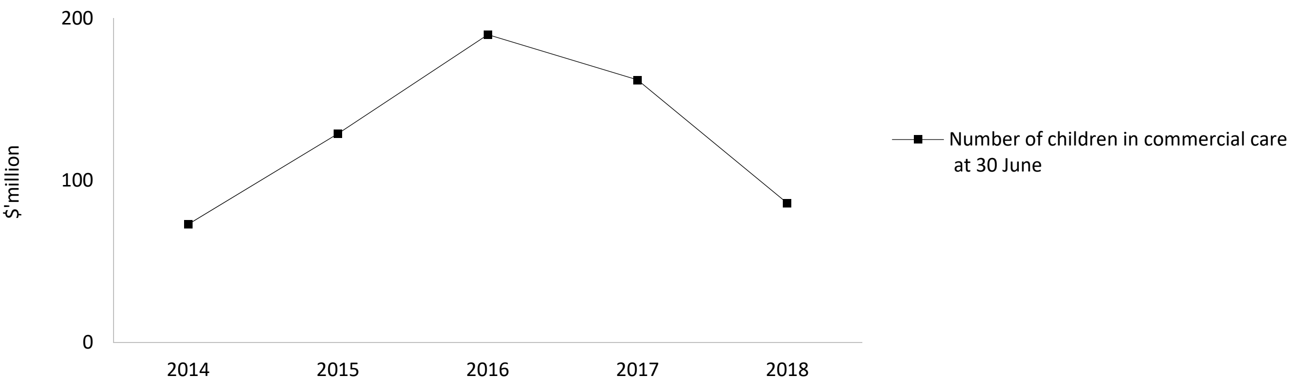
Grants and subsidies

Grants and subsidies of $113 million mainly consist of amounts paid to non-government organisations (NGOs) for residential based care, home based care, family group homes and other supported placement services. There was an increase of $65 million in these amounts in 2017-18, of which $51 million related to grants paid by Education in 2016-17 and the remaining $14 million related to CPI indexation of 2.5% and increased activity due to the increase in children in care.

Children in commercial care

Commercial care is a term that relates to payments made to commercial care service providers (the main contracted providers are Baptist Care (SA) Inc, Hessel Care Foundation Ltd and Hender Care Pty Ltd). Commercial care is provided at any suitable commercial premises, such as a private rental house or unit, and is staffed by carers who work shifts on a rotating 24 hour, 7 days a week work roster.

The actual number of children in commercial care fluctuates depending on need. At 30 June 2018 there were 86 children in commercial care placements. The graph below shows the number of children in commercial care at 30 June for the last five years.



Source: Number of children at 30 June was sourced from the DCP website and is unaudited.

At 30 June 2018 the number of children in commercial care placements fell by 76 children or 47% compared to the same point in 2017.

Contracted out-of-house care services expense

Total payments for contracted out-of-house care services include commercial care costs as well as some other costs for these carers to assist with other forms of care. Total expenses were $106 million in 2017-18. In 2016-17 $44 million was paid by Education, making the overall expense for the financial year $127 million. This means the cost of commercial care in 2017-18 fell by $21 million or 16%.

Supplies and services

Supplies and services increased by $50.9 million mainly due to:

- a $16 million increase in residential care expenses due to the movement of children from commercial care to residential care
- $34.7 million being paid by Education in 2016-17.

Income

DCP is predominantly funded by appropriation. Revenues from the SA Government were $521 million. In 2016-17 Education received $176 million in appropriation for DCP, bringing the total appropriation received in 2016-17 to $502 million.

Additional appropriations from the Governor's Appropriation Fund of $40 million and the contingency fund of $1 million were approved by the Treasurer and provided to DCP to offset cost pressures incurred mainly from the increased cost of children in care, particularly in commercial care as previously mentioned.

Statement of Financial Position

The following table shows the most significant items in the Statement of Financial Position at 30 June.

	2018 $'million	2017 $'million
Assets		
Property, plant and equipment	38	39
Cash and cash equivalents	38	32
Liabilities		
Employee benefits	52	46
Payables	26	22
Provisions	13	16
Net assets	(8)	(7)

Property, plant and equipment represents 46% of total assets, with cash and cash equivalents representing a further 46%. Property, plant and equipment mainly consists of residential accommodation housing of $19 million and land of $18 million.

Liabilities are made up of two main categories:

- employee related amounts, which include employee benefits, employee on-costs and workers compensation provisions, are 79.2% of total liabilities
- payables are 20.5% of total liabilities. Most payables relate to commercial care services provided but not paid at 30 June.

DCP has a negative net asset and total equity position at 30 June of $8.4 million. DCP's current liabilities are also $4.5 million higher than current assets. DCP works with the Department of Treasury and Finance on its cash requirements on an ongoing basis, as evidenced by the additional amounts of $41 million provided through the Governor's Appropriation Fund and contingency fund in 2017-18.

Statement of Cash Flows

Cash at 30 June is $37.9 million. This includes $8.5 million for accrual appropriations (while controlled by DCP the use of these funds must be approved by the Treasurer). DCP improved its cash position by $6.3 million in 2017-18.

Department for Correctional Services (DCS)

Financial statistics		
	Net cost of providing services:	$344 million
	Total appropriation:	$362 million
	Total prisoner numbers at 30 June 2018:	3001
	Number of FTEs:	2163

Significant events and transactions

- The contract with G4S to operate Mount Gambier Prison was renewed for five years, with an option to extend for a further five years, for a total value of $246 million.
- A number of contracts were awarded to non-government organisations for employment services and home detention services totalling $51 million.
- Prison capacity was increased by 128 prisoner beds, with capital works in progress to increase capacity by a further 200 beds.
- Surplus cash of $37 million was returned to the Consolidated Account.
- An equity contribution of $20 million was received in 2017-18 to fund capital projects.
- DCS recognised an additional compensation provision measured at $10.5 million, for a new enterprise agreement benefit to compensate staff who are injured at work.
- Workers compensation liabilities increased by $7.7 million.

Financial report opinion

Unmodified

Financial controls opinion

Modified

Key issue:

- Key procurement and contract management processes need strengthening

Functional responsibility

DCS is an administrative unit established by the *Public Sector Act 2009.*

The functions of DCS include contributing to public safety by safely, securely and humanely managing offenders and providing opportunities for their rehabilitation and reintegration. DCS provides:

- custodial services – secure containment and supervision for adults on remand and those sentenced to custodial sanction
- community based services – managing and supervising offenders in the community on probation, parole, home detention and supervised bail
- rehabilitation and reparation services – educational, vocational and rehabilitative activities to address offending behaviour.

Scope of the audit

The audit program covered major financial systems to obtain sufficient evidence to form an opinion on the financial report and internal controls.

Specific areas of audit attention in 2017-18 included:

- contract management
- payroll
- general ledger
- fixed assets
- workers compensation
- accounts payable
- revenue.

We obtained an understanding of internal audit activities to identify and assess the risks of material misstatement in the financial statements and to design and perform audit procedures.

Audit findings and comments

Assessment of controls

In my opinion, the controls exercised by the Department for Correctional Services in relation to the receipt, expenditure and investment of money, the acquisition and disposal of property and the incurring of liabilities, except for the matters outlined under 'Communication of audit matters', are sufficient to provide reasonable assurance that the financial transactions of the Department for Correctional Services have been conducted properly and in accordance with law.

Communication of audit matters

Matters identified by the audit were detailed in a management letter to the Chief Executive. The main matters raised and related response are detailed below.

Key procurement and contract management processes need strengthening

Procurement and contract management is a significant aspect of DCS's operations, with contracted expenses exceeding $37 million in 2017-18.

We identified the following matters for the sample of contracts that we reviewed:

- New panel contracts valued at $4.3 million for installing and maintaining electronic security system services were not approved by the Minister for Correctional Services until two weeks after the contract start date, and six weeks after the previous contracts had expired. This did not allow sufficient time for the Minister to consider DCS's procurement recommendations and ensure that a proper process was followed.

- DCS's contract for electronic monitoring services was not extended until more than six months after the previous contract expired. Contracts extensions should be arranged and authorised before existing contracts expire. Timely planning for contract renewals, extensions and new procurements helps to ensure that DCS obtains value for money from its contractual relationships and that its legal rights are protected.

- DCS was unable to demonstrate that its contract for the provision of home detention support services, valued at $17 million, was approved in line with Treasurer's Instruction 8 'Financial Authorisations' (TI 8). TI 8 requires that a Minister may only approve contracts over $15 million if the contract forms part of a public sector initiative that has been approved by Cabinet; if the scope of the contract is consistent with Cabinet approval; and where the consideration for the contract does not exceed any estimated cost provided to Cabinet in connection with its approval.

  While the contract was approved by the Minister, DCS had accepted that the 2016-17 State Budget process provided the necessary Cabinet approval. DCS was unable, however, to provide the information necessary to evidence compliance with TI 8.

DCS responded to these matters noting that it had recently engaged an external consultant to review its procurement and contract management governance processes, activity and organisational structures. The review and recommendations are currently under consideration by DCS and it anticipates that recommendations will be implemented in 2018-19. DCS also advised that it had amended other elements of its contract management processes to ensure compliance with TI 8.

Shared Services SA – financial systems and transaction processing environments

Shared Services SA processes financial transactions on behalf of DCS under service level determinations. The main systems and control environments include accounts payable, payroll and general ledger financial functions.

Our review and evaluation of controls for these systems concluded that controls were effective for 2017-18.

Shared Services SA is discussed further in the commentary under 'Department of the Premier and Cabinet' in this Report.

Interpretation and analysis of the financial report

Highlights of the financial report

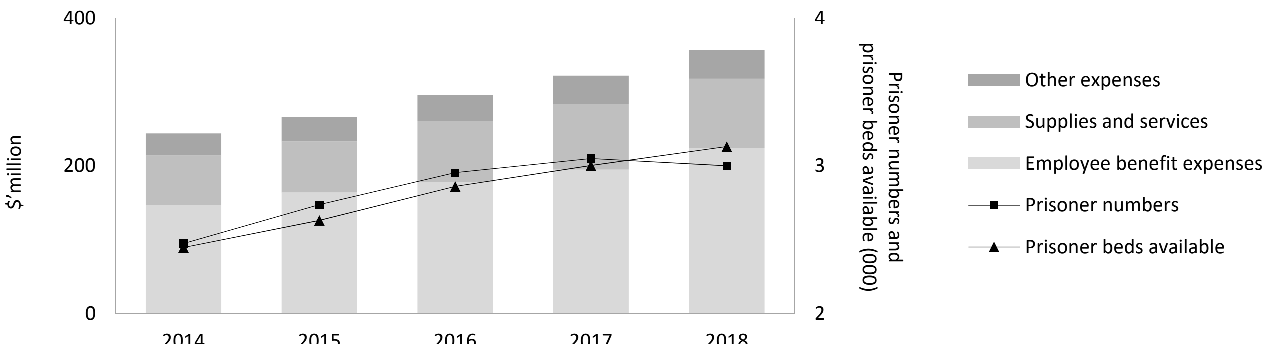
	2018 $'million	2017 $'million
Expenses		
Employee benefit expenses	224	195
Supplies and services	94	89
Other expenses	39	38
Total expenses	357	322
Income		
Income from prison labour and canteen and kitchen sales	6	6
Other income	7	5
Total income	13	11
Net cost of providing services	344	311
Revenues from SA Government	362	332
Payments to SA Government	(37)	-
Net result	(19)	21
Total comprehensive result	(8)	33
Net cash provided by (used in) operating activities	24	48
Net cash provided by (used in) investing activities	(67)	(51)
Net cash provided by (used in) financing activities	20	48
Assets		
Current assets	35	56
Non-current assets	627	571
Total assets	662	627
Liabilities		
Current liabilities	47	47
Non-current liabilities	61	39
Total liabilities	108	86
Total equity	554	541

Statement of Comprehensive Income

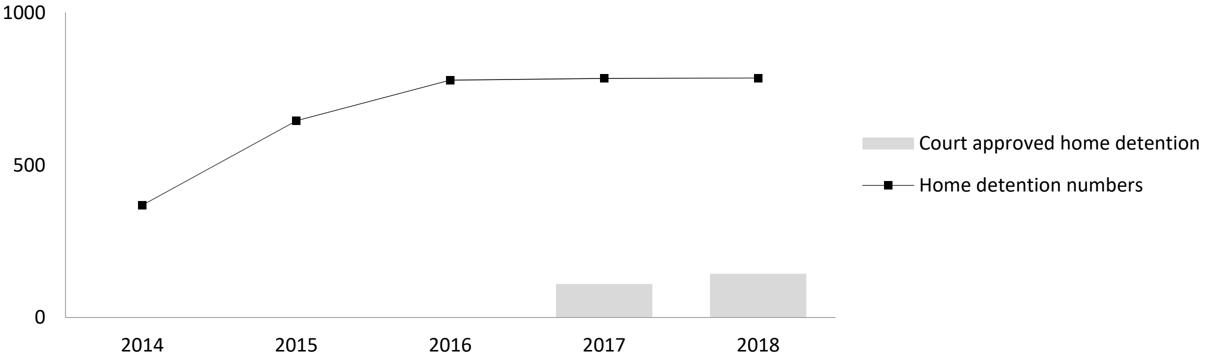
Expenses

A structural analysis of DCS's main expense items and total prisoner numbers for the five years to 2018 is shown in the following chart. Over this period total prisoner numbers as at 30 June have increased by 526 (21%) to 3001, while total expenses have increased by $113 million (46%). In 2017-18 total

prisoner numbers decreased marginally while total expenses increased by $35 million (11%), largely reflecting increases in employee benefit expenses. The prisoner numbers are at a point in time and may fluctuate during the year.



Home detention numbers have also increased from 368 at 30 June 2014 to 786 by 30 June 2018. In 2016 changes to the *Correctional Services Act 1982* and *Criminal Law (Sentencing) Act 1988* allowed the Courts to apply home detention orders. Prior to this only the DCS Chief Executive could release prisoners for home detention under certain conditions.



Employee benefit expenses

The significant increase in employee benefit expenses of $29.3 million is due mainly to:

- the introduction of a new injury and income protection policy (additional compensation provision) valued at $10.5 million (see 'Liabilities' below)
- an increase of $7.7 million in workers compensation provisions (see 'Liabilities' below)
- an increase in long service leave expenses of $2.2 million due to an increase in eligible employees
- a $5.9 million increase in salaries and wages arising from enterprise agreement salary increases and an increase of 78 FTEs associated with the 128 bed expansion at Port Augusta Prison.

Supplies and services expenses

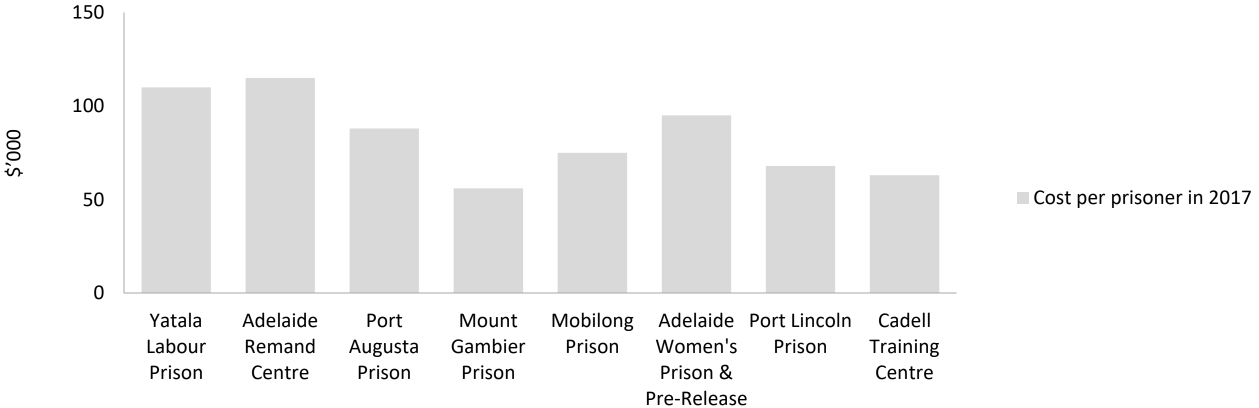
Supplies and services expenses increased by $5.7 million to $94.2 million mainly due to:

- a $2.3 million increase in contract expenditure due to the new bail support program ($1.8 million) and an increase in the costs of home detention electronic monitoring associated with an increase in the volume of activity and contract rates

- a $1.5 million increase in utilities charges due mainly to an increase in the amount charged under the new whole-of-government electricity contract.

Annual cost per prisoner per facility

The following chart shows the per prisoner cost of managing each facility in 2016-17. Figures include all direct and indirect operating costs. Indirect costs are allocated to prisons based on either a percentage of total salaries, a percentage of total beds or a percentage of total direct costs. Data was supplied by DCS and is unaudited.



DCS have advised that there several drivers influencing the costs of running South Australian prisons:

- Built environment of the prison. Ageing infrastructure at sites like Yatala Labour Prison can impact costs. For example, the design of prisoner accommodation, visitor centres and admissions areas can impact staffing levels, which then impact cost. Cell based accommodation as opposed to residential type accommodation also influences the cost per prisoner.
- Work practices and staffing levels vary at each site and have evolved over time. For example, there are variations at prison sites on the number of correctional officers required to escort prisoners within the facility, and the number of correctional staff required to monitor prisoners.
- The role and function of the prison that can vary based on factors including out of cell hours, level of industry activity at each site, level of prisoner employment, open campus (eg Mobilong) and security level of prisoners.

It is also important to note that South Australian prisons have varied security requirements rated as high, medium and low security. These requirements influence the cost of managing each facility, with higher security requirements generally increasing the cost of running a prison.

The chart illustrates the differences between facilities. The Adelaide Remand Centre cost $114 000 per prisoner in 2016-17, while the Yatala Labour Prison cost $110 000 per prisoner and the Mount Gambier Prison $56 000 per prisoner in the same period. These comparisons require consideration of the following points:

- Facilities such as the Adelaide Remand Centre and Yatala Labour Prison have mainly high and medium security prisoners.

- Cadell Training Centre (low security prisoners), Mobilong Prison (medium and low security prisoners), Mount Gambier Prison (medium and low security prisoners) and Port Lincoln Prison (medium and low security prisoners) have the lowest cost per prisoner.

- The Adelaide Women's Prison and Port Augusta Prison accommodate all security profiles.

Income

Revenues from the SA Government, DCS's primary income source, increased by $30 million to $362 million. This included $41 million received from the Consolidated Account for the upgrade of prison infrastructure. This increase in government funding was offset by the return of $37 million to the Consolidated Account, resulting from delays in progressing capital programs, particularly for the Port Augusta and Mount Gambier prisoner accommodation projects.

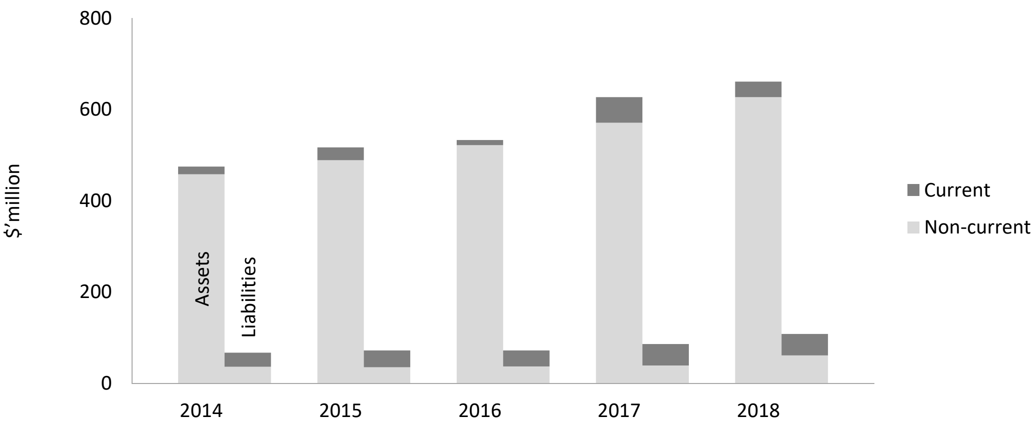
Resources received free of charge of $2 million were also recognised for the first time following the cessation of intra-government charging for services provided by Shared Services SA.

Equity contribution

In 2017-18 DCS received a capital contribution (or government equity contribution) from the SA Government of $20 million, a decrease of $28 million from the prior year, reflecting delays in capital programs.

Statement of Financial Position

For the five years to 2018, a structural analysis of assets and liabilities is shown in the following chart.



Assets

Cash and cash equivalents

DCS's current asset position declined in 2017-18, with total current assets of $35 million now exceeded by current liabilities of $47 million. Employee related leave liabilities and compensation

provisions represent 51% ($25 million) of current liabilities. The decrease in current assets is due mainly to a $23 million decrease in cash at 30 June 2018 attributable to the return of cash to the Consolidated Account.

Property, plant and equipment

The main item of DCS's Statement of Financial Position is property, plant and equipment, representing 94% of total assets.

Land and buildings represent 99% of total property, plant and equipment and were valued at $565 million as at 30 June 2018. The following chart shows asset values for DCS's land and buildings for the last two years.

The carrying value of land and buildings increased by $52 million due to:

- $59.7 million of completed capital works, due largely to additional accommodation (128 beds) and supporting infrastructure at Port Augusta Prison
- a revaluation increment of $11.4 million across all land and buildings
- partially offset by depreciation charges of $19.2 million.

Capital works in progress

As at 30 June 2018 capital works in progress totalled $53 million. This includes costs associated with the following prisoner accommodation projects in progress at 30 June 2018:

- $42 million for 160 additional beds at the Mount Gambier Prison
- $3 million for 40 additional beds at the Adelaide Women's Prison.

Liabilities

Total liabilities increased by $21.9 million to $108 million.

This increase is largely attributable to the $7.7 million increase in the provision for workers compensation and the introduction of a new additional compensation provision of $10.5 million.

A $2.6 million increase in long service leave liabilities also contributed to the increase in total liabilities, due to enterprise agreement salary increases and an additional 310 employees entitled to leave.

Provision for workers compensation

South Australia public sector employees who have suffered work-related injuries are entitled to benefits under the *Return to Work Act 2014* (RTW Act).

The workers compensation provision is based on an actuarial assessment of the outstanding liability as at 30 June 2018 provided by a consulting actuary engaged through the Office for the Public Sector. The liability increased by $7.7 million due mainly to:

- an increase in the estimate for serious injury worker (SIW) known claims of around $3.7 million
- a $3.3 million increase for incurred but not yet reported (IBNR) applications.

The increase in the estimate for known SIW claims was driven by the identification of a new seriously injured claim and an increase in assumed medical costs for known claims. The increase in the estimate for SIW IBNR claims was due to an increase in DCS's relative share of IBNR claims estimated by the actuary at a whole-of-government level.

There is a significant degree of uncertainty associated with estimating future claim and expense payments. The liability is impacted by agency claim experience relative to other agencies, average claim sizes and other economic and actuarial assumptions.

Additional compensation provision

Following changes to relevant public sector enterprise agreements, DCS has recognised an additional compensation provision as at 30 June 2018.

This new provision provides continuing benefits to workers who have suffered eligible work-related injuries and whose entitlements have ceased under the RTW Act. Eligible injuries are non-serious injuries suffered in circumstances which involve, or appear to involve, the commission of a criminal offence, or which arose from a dangerous situation.

The additional compensation provision as at 30 June 2018 was estimated by an actuary engaged by the Office for the Public Sector on behalf of all affected agencies across the public sector. The liability comprises an estimate for known claims and an estimate of IBNR applications.

There is a significant degree of uncertainty associated with the estimate of the additional compensation provision. In addition to the general uncertainties associated with estimating future claim and expense payments, the provision is impacted by the absence of claims history and the evolving nature of the interpretation of, and evidence required to meet, eligibility criteria.

Given these uncertainties the actuary has noted that the actual cost of additional compensation claims may differ materially from the estimate.

Statement of Cash Flows

The following table summarises the net cash flows for the five years to 2018.

	2014 $'million	2015 $'million	2016 $'million	2017 $'million	2018 $'million
Net cash flows					
Operating	11	23	6	48	24
Investing	(27)	(41)	(31)	(51)	(67)
Financing	13	28	8	47	20
Change in cash	(3)	10	(17)	44	(23)
Cash at 30 June	14	24	7	51	28

In 2017-18 cash decreased by $23 million largely reflecting capital expenditure totalling $67 million, partially offset by capital contributions from government of $20 million. Net cash generated by operating activities improved DCS's cash position by a further $24 million.

The table shows a history of investing cash outflows, representing the continual capital expenditures over the period relating primarily to additional prisoner accommodation. This expenditure has been funded in part through capital contributions from the SA Government, which are reflected in financing activities, and through the normal government appropriations received through operating cash flows.

Courts Administration Authority (CAA)

Financial statistics	Net cost of providing services:	$91.2 million
	Total appropriation:	$81.4 million
	Administered total expenses:	$64.4 million
	Number of FTEs:	
	Controlled	654.5
	Administered	87.1

Significant events and transactions

- The $31 million Higher Courts Redevelopment project commenced. Work undertaken included finalisation of the scope and design of the works and undertaking procurement processes for delivery for elements of the project.
- Work on the Electronic Court Management System project progressed during the year. Work undertaken included design of specifications, configuration of functionality and development of data interchanges.

Financial report opinion

Unmodified

Financial controls opinion

Modified

Key issues:

- Insufficient controls over payroll system user access
- Leave taken by employees not recorded promptly

Functional responsibility

The CAA was established under the *Courts Administration Act 1993.* It is constituted of the State Courts Administration Council, the State Courts Administrator and other staff of the State Courts Administration Council.

The function of the CAA, which is independent of the control of Executive Government, is to provide courts with the administrative facilities and services needed for the proper administration of justice. For more information about the CAA's objectives and priorities refer note 2 of its financial report.

Scope of the audit

The audit program covered major financial systems to obtain sufficient evidence to form an opinion on the financial report and internal controls.

Specific areas of audit attention in 2017-18 included:

- expenditure
- revenue and receipting
- payroll
- cash
- fixed assets
- financial accounting
- financial management compliance program
- trust accounts.

Internal audit activities were considered in designing audit procedures.

Audit findings and comments

Assessment of controls

In my opinion, the controls exercised by the Courts Administration Authority in relation to the receipt, expenditure and investment of money, the acquisition and disposal of property and the incurring of liabilities, except for all matters outlined under 'Communication of audit matters', are sufficient to provide reasonable assurance that the financial transactions of the Courts Administration Authority have been conducted properly and in accordance with law.

Communication of audit matters

Matters identified by the audit were detailed in a management letter to the State Courts Administrator. The main matters raised and related responses are detailed below.

Payroll

Employee benefits expenses totalled $55 million for 2017-18 and the liability for employee benefits at 30 June 2018 was $16 million.

Insufficient control over payroll system user access

Our review found that the controls over user access to the Chris21 payroll system were not sufficient. These included:

- review of Chris21 user access was not performed by an independent officer
- user access was granted without receipt of an authorised user access form.

As a result officers may have inappropriate access to Chris21.

In response the CAA indicated that it would take action to ensure:

- access to Chris21 is only provided on receipt of an authorised user access form
- annual review of user access is performed by an independent officer.

Leave taken by employees not recorded promptly

Our review identified instances where leave recorded in timesheets was not actioned in a timely manner in the payroll system. We also noted that leave reports are no longer provided to pay point managers for review. As a result, leave balances recorded in the payroll system and financial statements may be inaccurate.

In response the CAA indicated that it would remind managers and staff of the need to record leave promptly.

Interpretation and analysis of the financial report

Highlights of the financial report – controlled items

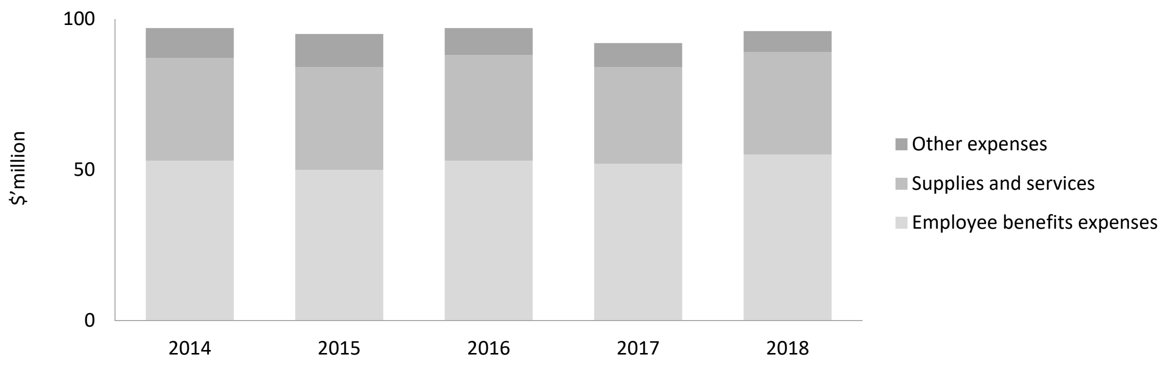
	2018 $'million	2017 $'million
Expenses		
Employee benefits expenses	55	52
Supplies and services	34	32
Other expenses	7	8
Total expenses	96	92
Income		
Revenues from fees and charges	4	3
Other revenues	1	1
Total income	5	4
Net cost of providing services	91	88
Revenues from (Payments to) SA Government	81	86
Net result	(10)	(2)
Total comprehensive result	(11)	(2)
Net cash provided by (used in) operating activities	(2)	4
Assets		
Current assets	51	60
Non-current assets	192	194
Total assets	243	254
Liabilities		
Current liabilities	13	11
Non-current liabilities	20	21
Total liabilities	33	32
Total equity	210	222

Statement of Comprehensive Income

The CAA's expenses reflect the costs of performing its statutory responsibilities, including collecting administered income such as fines and court fees on behalf of the SA Government. This income is directly credited to the Consolidated Account and is reported under administered income.

Expenses

The following chart shows the main expense items for the five years to 2018.



The chart shows that overall 2017-18 expenditure has increased, with increases in all categories except other expenses.

Employee benefits expenses are the major expense category for the CAA, accounting for 57% (56%) of total expenses. Employee benefits expenses increased by $3.5 million in 2017-18 with the following notable movements:

- salaries and wages increased by $1.5 million as a result of enterprise bargaining increases and additional staff employed for the Electronic Court Management System project
- long service leave expense increased by $1.3 million as a result of the revaluation of the long service leave liability caused by a higher level of accrued calendar days as at 30 June 2018.

Supplies and services account for 35% (35%) of total expenses and increased by $1.4 million in 2017-18. This was mainly due to a $971 000 increase in accommodation and service expenses, a result of increased electricity charges and minor projects works. Accommodation and services make up the highest expense of $15.1 million ($14.1 million), with computing and communications the next highest at $5.8 million ($5.5 million).

Other expenses decreased by $1.1 million mainly due to a decrease in workers compensation expenses of $1.3 million as a result of the revaluation of the workers compensation provision caused by a drop in claim payments as a result of the introduction of new legislation in 2015, offset by an increase for additional compensation provision of $403 000.

Income

Revenues from the SA Government are the major source of funding for the CAA, accounting for 94% (95%) of total income.

The following chart shows the level of revenues from the SA Government for the five years to 2018.

$'million
100
90
80
2014
2015
2016
2017
2018
Revenues from SA Government

Revenues from the SA Government decreased by $4.1 million in 2017-18 to $81.4 million. This was mainly due to a funding adjustment as a result of revised funding requirements for the Higher Courts Redevelopment project and the Electronic Court Management System project. Funding for these projects has been carried over to forward years.

Statement of Financial Position

Non-current assets mainly comprise land and buildings totalling $176 million ($178 million), which accounts for 92% (92%) of non-current assets.

Current assets mainly comprise cash and cash equivalents totalling $49 million ($58 million), which accounts for 96% (97%) of current assets.

Included in cash at 30 June 2018 are deposits with the Treasurer, including $40 million ($53 million) held in the Accrual Appropriation Excess Funds Account. The balance of these funds is not available for general use and can only be used with the Treasurer's/Under Treasurer's approval. Approval to use $13.2 million was provided by the Under Treasurer in September 2017 for the purpose of meeting capital expenditure for the Higher Courts Redevelopment project.

Court facilities planning

Last year we reported that as part of the 2017-18 budget, the CAA received a $31 million allocation to redevelop the Higher Courts precinct. This will fund the conversion of civil courts in the Sir Samuel Way building into three criminal courts, as well as the renovation of civil courts in the Supreme Court complex. In 2017-18 work undertaken included finalisation of the scope and design of the works and undertaking procurement processes for the delivery of elements of the project. As at 30 June 2018 total expenditure on this project was $1.5 million and is included in the capital work in progress balance.

Electronic Court Management System project

Last year we reported that the procurement process for the new electronic court management system was finalised. In 2017-18 work undertaken included design of specifications, configuration of functionality and development of data interchanges. As at 30 June 2018 total expenditure on the project was $5 million, with a total budget of $23.2 million. Probate activities are scheduled to go-live in November 2018.

Interpretation and analysis of the financial report for administered activities

Highlights of the financial report – administered items

	2018 $'million	2017 $'million
Expenses		
Judicial benefits expenses	42	39
Payments to the Consolidated Account	21	23
Other expenses	1	2
Total expenses	64	64
Income		
Revenues from SA Government	42	39
Court and transcript fees	21	21
Other income	1	4
Total income	64	64
Net and total comprehensive result	-	-
Net cash provided by (used in) operating activities	(9)	(4)
Assets		
Current assets	44	52
Total assets	44	52
Liabilities		
Current liabilities	39	49
Non-current liabilities	13	11
Total liabilities	52	60
Total equity	(8)	(8)

Statement of Administered Comprehensive Income

Expenses

Payments to the Consolidated Account totalling $21 million comprise mainly court and transcript fees.

Judicial benefits expenses were $42.1 million, an increase of $2.8 million from the previous year. Salaries and wages increased by $1.2 million as a result of a Remuneration Tribunal increase in base salaries and an additional Judicial officer. Long service leave expense increased by $920 000 mainly as a result of the revaluation of the long service leave liability caused by a higher level of accrued calendar days as at 30 June 2018.

Income

Court and transcript fees

Court and transcript fees are raised and collected by the CAA and paid directly to the Consolidated Account. The amount collected for 2017-18 was $21 million which is the same as the previous year.

Revenues from SA Government

Revenues from the SA Government are received by the CAA to fund employment expenses of the Judiciary. In 2017-18 revenues of $42 million ($39 million) were received from the SA Government to pay the recurrent expenditure associated with the Judiciary.

Statement of Financial Position

Total assets and liabilities both decreased by $8.5 million as a result of less cash held in trust accounts on behalf of parties involved in court matters.

Further commentary on operations

Total cost of services for the administration of justice through the courts system

The total cost of providing the services for the administration of justice through the courts system (CAA and Judicial Officers costs only) includes both the expenses and income in the controlled and administered financial reports. For 2017-18 total expenses were $160 million ($156 million) and total income, excluding revenues from the SA Government, was $27 million ($29 million). The SA Government provided $124 million ($125 million) towards the cost of administering justice.

Department for Education (Education)

Financial statistics

Net assets:	$4553 million
Net cost of providing services:	$2443 million
Total revenues from SA Government:	$2491 million
Total comprehensive result:	$48 million
Number of FTEs:	23 931
Number of school and preschool sites:	920
Number of FTE students enrolled in Education schools in term 1, 2018:	174 552

Significant events and transactions

- $144 million of the $250 million budget was spent to upgrade science, technology, engineering and mathematics (STEM) facilities at 139 government schools. All STEM works are due to be completed by the end of December 2018.
- $60 million was spent by 30 June 2018 on the new $100 million Adelaide Botanic High School (due to open in term 1, 2019).
- Two new Public Private Partnership schools announced for birth to year 12 students, with one in the Munno Para region and one in the Aldinga region. These schools are scheduled to be available for the start of the 2022 school year.
- $692 million to be spent over six years on improving, refurbishing and expanding capacity at 91 government schools through the Building Better Schools program. Some of these projects will provide facilities for year 7 students in high schools.

Financial report opinion

Unmodified

Financial controls opinion

Modified

Key issues:

- Controls for minor works and maintenance expenditure did not ensure all charges were valid and/or accurate
- Weaknesses in the recovery of salary overpayments
- Automatic updates to salaries did not occur for some employees
- Weaknesses in payroll system IT controls

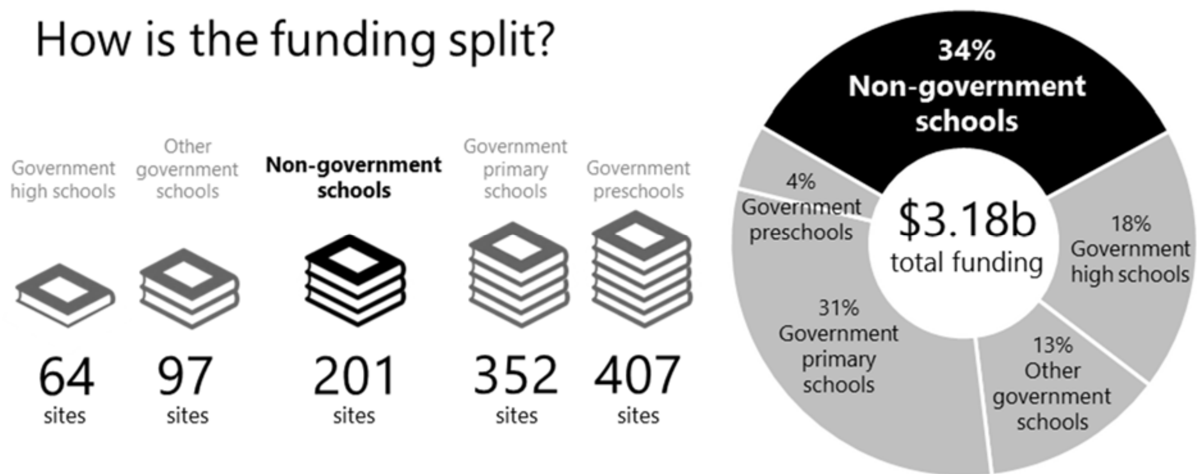
Functional responsibility

Education is an administrative unit established under the *Public Sector Act 2009* and responsible to the Minister for Education.

There are two main financial functions performed by Education:

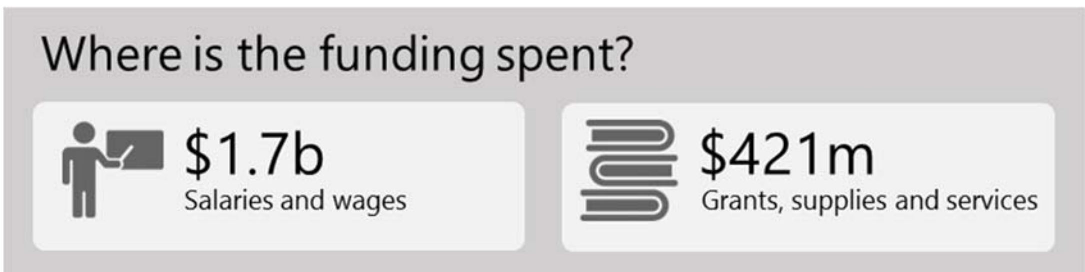
- providing funding to schools and preschools – in 2017-18 payments to and on behalf of 920 Education schools and preschools were $2.1 billion and payments to 201 non-government schools were $1 billion
- paying employees – employee benefits expenses, including schools and preschools, were $2.3 billion in 2017-18.

Funding to schools and preschools



Government schools and preschools

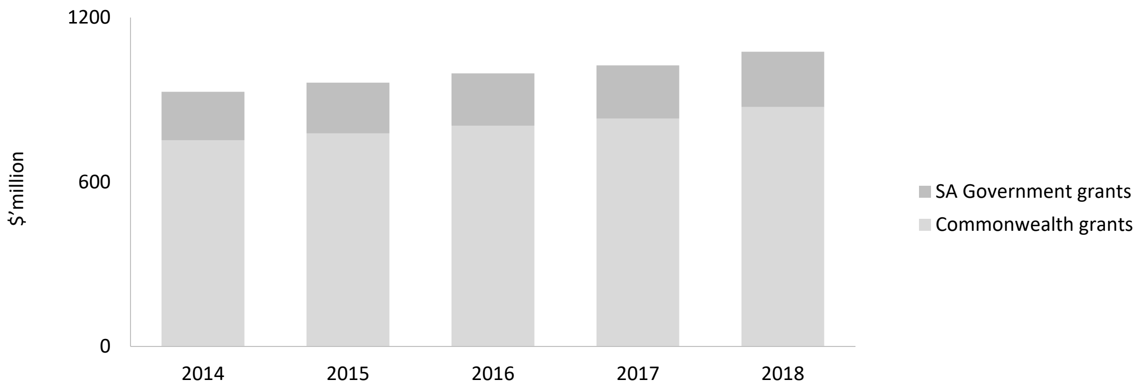
Payments to and on behalf of government schools and preschools relate to employee expenses, supplies and services and grants and subsidies within the controlled financial report. Employee benefits expenses account for 80% of the total amount provided to government schools and preschools.



In 2017-18 payments to and on behalf of government schools and preschools were funded by $1.7 billion in SA Government appropriation and $508 million in Commonwealth grants. Additional funds were also provided for capital works.

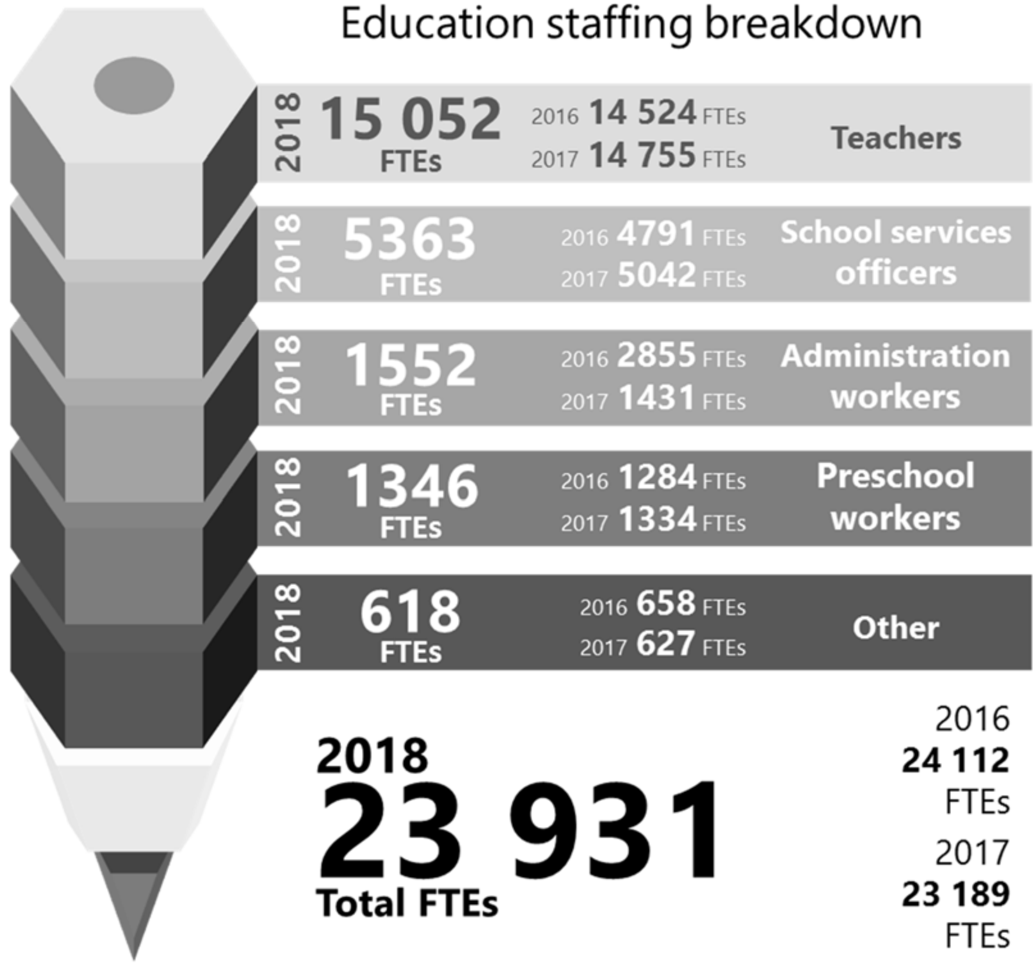
Non-government schools

Payments to non-government schools are paid as transfer payments from the administered financial report. There has been a gradual increase of 16% over five years in the transfer payments to non-government schools.



In 2017-18 transfers to non-government schools were funded by $202 million ($194 million) in SA Government grants and $873 ($831 million) in Commonwealth grants. All grants were based on the average annual enrolment of the school and the needs of the school and its students. The amount each non-government school receives from the Commonwealth is determined by the Commonwealth.

Employees



From 2016-17 there has been an increase of 3% in the number of teachers and school services officers, while the increase in the number of students enrolled in term 1 is 0.6%.

The number of administrative FTEs fell by 1424 in 2016-17 due to the transfer of 1763 administrative FTEs to the Department for Child Protection, offset by an increase of 339 in administrative FTEs.

Scope of the audit

The audit program covered major financial systems to obtain sufficient evidence to form an opinion on the financial report and internal controls.

Specific areas of audit attention in 2017-18 included:

- accounts payable
- minor works and maintenance expenditure
- payroll
- grants
- purchase cards
- cash
- general ledger
- payroll system IT controls
- teacher renewal scheme.

Internal audit activities were reviewed to assess the risk of material misstatement in the financial report and to design and perform audit procedures. We made use of internal audit's work for the audit of:

- school enrolment data used to determine the funding provided to each government school
- government schools audits, which were performed by contractors appointed, managed and monitored by internal audit.

The audit also considered controls and procedures performed by service providers including Shared Services SA (SSSA).

Audit findings and comments

Assessment of controls

In my opinion, the controls exercised by the Department for Education in relation to the receipt, expenditure and investment of money, the acquisition and disposal of property and the incurring of liabilities, except for all matters outlined under 'Communication of audit matters', are sufficient to provide reasonable assurance that the financial transactions of the Department for Education have been conducted properly and in accordance with law.

Communication of audit matters

Matters identified by our audit were detailed in management letters to the Chief Executive. The main matters raised and related responses are detailed below.

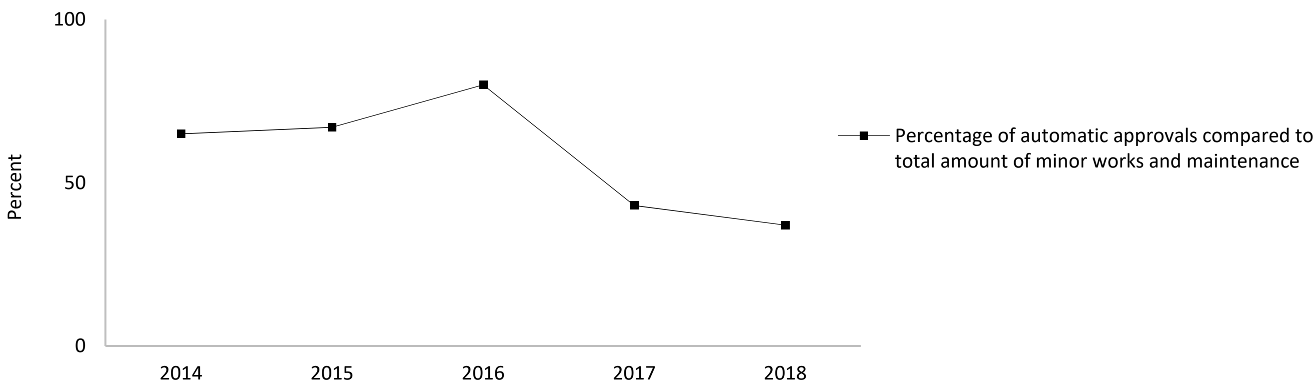
Minor works and maintenance expenditure

Education paid $167.6 million for minor works, maintenance and equipment in 2017-18. Minor works and maintenance are performed by contracted facilities managers through the Department of Planning, Transport and Infrastructure (DPTI), and recorded in DPTI's asset management system (FAMIS). Under the contractual arrangements with the facilities managers, if the charges recorded in FAMIS are not approved or disputed by sites within 30 days, they are automatically paid.

Controls for minor works and maintenance expenditures did not ensure all charges were valid and/or accurate

For a number of years we have raised the issue of automatic payments as there is an increased risk of paying for works not performed or being overcharged. In our view these payments also breach the Treasurer's Instructions, as no delegate has approved the payments.

A number of changes have been implemented by Education and DPTI that have contributed to a reduction in the number of automatic payments since 2015-16 to the lowest level in five years, as show below. The chart shows the percentage of automatic approvals out of total repairs and maintenance charges.



While there has been a significant improvement, there remains a substantial amount, $48 million for 2017-18, paid automatically without review and approval.

As we did last year, we contacted a number of schools with high levels of automatic payments to understand why sites were not approving these charges. Site staff advised us payments were not approved due to:

- FAMIS being difficult to use and access regularly being unavailable
- limited knowledge on, or access to, FAMIS
- staff not using FAMIS despite having established user accounts.

This year, Education advised us this continues to be a challenge and it has implemented formal notification to the Education Directors for those sites that repeatedly appear in the top 10 monthly sites with high automatic approval levels.

Payroll

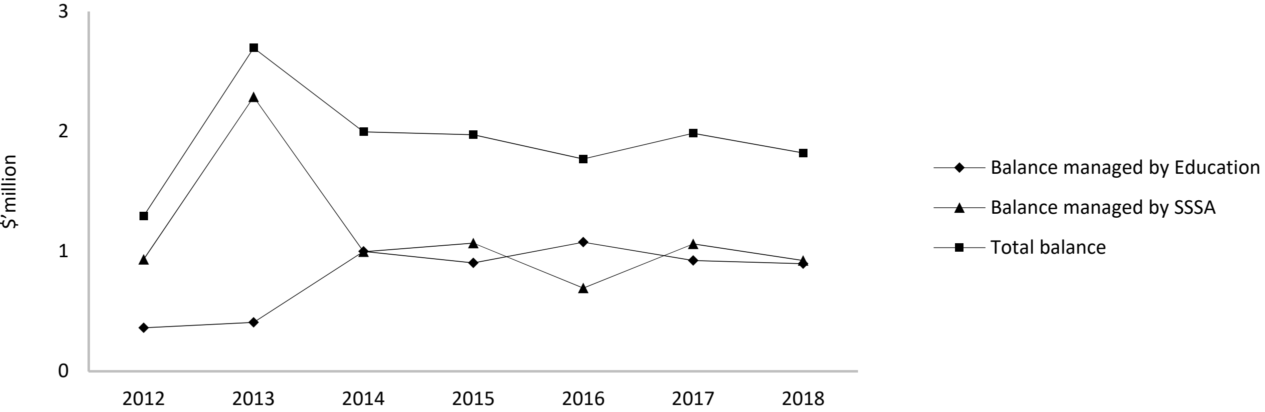
Total employee expenses were $2.34 billion in 2017-18, representing 72% of total expenses. Education had 23 931 controlled FTEs and 30 administered FTEs at 30 June 2018.

Weaknesses in the recovery of salary overpayments

Responsibility for the identification and recovery of salary overpayments is shared between Education and SSSA. Overpayments are initially managed by SSSA before being transferred to Education's Debt Recoveries Team.

We have previously reported that the causes and recovery of salary overpayments needed to be addressed by Education and SSSA.

In 2017-18 we noted there had been a number of improvements in the controls over the causes and recovery of salary overpayments, but this had not impacted the balance of the outstanding overpayments. The following chart shows salary overpayments at 30 June for the last seven years. The balances have remained fairly stable at just below $2 million since 30 June 2014.



We recommended Education and SSSA make further efforts to regularly monitor older debts and to record actions and decisions made.

We reviewed a sample of outstanding salary overpayments managed by Education and noted instances of delays in follow up, recovery actions and write off.

In response Education advised it would review the existing processes to ensure debts were pursued and/or written off promptly.

Automatic updates to salaries did not occur for some employees

One of the features of Education's payroll system is that it should automatically update each employee's pay rate to the next payment tier when the employee reaches their increment date.

We identified an instance where this did not occur and Education could not explain why. We did not identify any compensating control that would identify and correct this issue when it occurs.

Education advised it would investigate this system issue and the review would be completed by 20 July 2018. We understand the review remained ongoing in late July 2018.

Weaknesses in payroll system IT controls

Education's payroll system is Valeo. It is the largest system currently managed by Education and support services for the database and operating system are provided by NEC.

Weaknesses in password configuration settings

We compared Valeo's password configuration settings to the recommended setting in the Commonwealth Government's Information Security Manual (ISM) and found Education's password settings for the Valeo application, database and operating system could be strengthened.

Education advised it would make changes to align the Valeo application passwords with the ISM settings and would request that NEC implement default profiles for the database and operating system by 31 July 2018.

Inappropriately assigned privileged user access accounts

We reviewed the privileged user accounts across the Valeo application, database and operating system and identified a number of operating system privileged user accounts that were no longer appropriate.

Education advised the inappropriate access had been removed.

Inadequate patch management across the Valeo application system

We were advised that patching on the Valeo operating system – a process to update a system to update, fix or improve it – had not been applied frequently, with the last successful critical patch occurring in November 2015.

A recent attempt to apply critical operating system patches in the testing environment encountered problems and therefore was not applied to the production environment.

Education advised that the patching cycle had commenced after our audit, with the patches to be applied to the production environment by 13 July 2018. A three-monthly patching cycle had been added to the patching schedule.

Lack of disaster recovery management across the Valeo environment

We found Education had:

- no IT disaster recovery plan
- no secondary disaster recovery site for key business systems including Valeo
- not performed disaster recovery testing over the Valeo environment for an extended period of time.

Education advised it had requested NEC to provide a disaster recovery design and pricing for key business systems including Valeo. Once this was received ICT services would submit a business case to implement disaster recovery facilities for the key business systems, with a targeted completion date of 31 October 2018.

Shared Services SA – financial systems and transaction processing environments

SSSA processes financial transactions on behalf of Education under service level determinations. The main systems and control environments include accounts payable, payroll and general ledger financial functions.

Our review and evaluation of controls for these systems concluded that controls were effective for 2017-18.

SSSA is discussed further in the commentary under 'Department of the Premier and Cabinet' in this Report.

Interpretation and analysis of the financial report

Highlights of the financial report (Consolidated)

	2018 $'million	2017 $'million
Expenses		
Employee benefits expenses	2 340	2 270
Supplies and services	694	675
Other	206	282
Total expenses	3 240	3 227
Income		
Commonwealth revenues	509	478
Student and other fees and charges	169	161
Other	119	119
Total income	797	758
Net cost of providing services	2 443	2 469
Revenues from (Payments to) SA Government		
Revenues from SA Government	2 491	2 524
Net result	48	55
Other comprehensive income		
Changes in revaluation surplus	69	627
Total comprehensive income	117	682
Net cash provided by operating activities	179	167
Net cash used in investing activities	183	37
Assets		
Current assets	1 010	1 016
Non-current assets	4 695	4 533
Total assets	5 705	5 549
Liabilities		
Current liabilities	407	363
Non-current liabilities	745	750
Total liabilities	1 152	1 113
Total equity	4 553	4 436

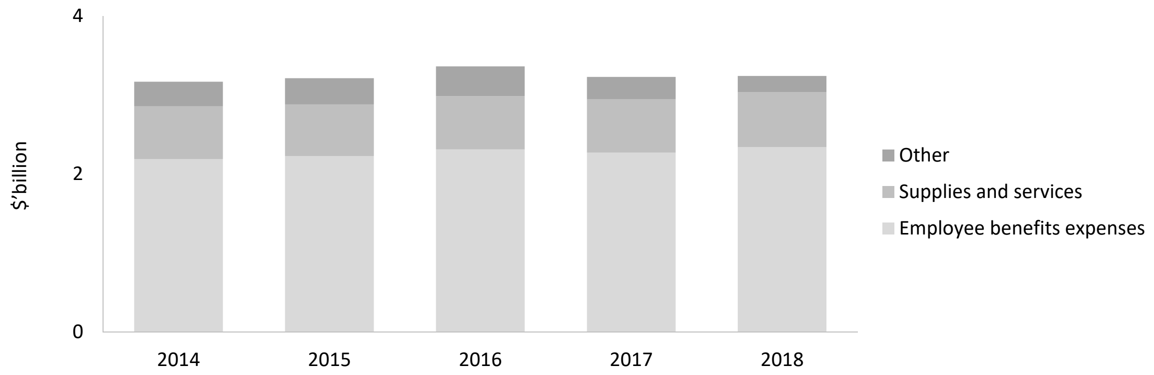
Transfer of Families SA to the Department for Child Protection (DCP) in 2016-17

Education's functions and responsibilities changed in 2016-17 due to the transfer of Families SA to the new DCP from 1 November 2016. As a result, some of the 2018 and 2017 figures are not directly comparable.

Statement of Comprehensive Income

Expenses

The main expense items for Education for the five years to 2018 is shown in the following chart.

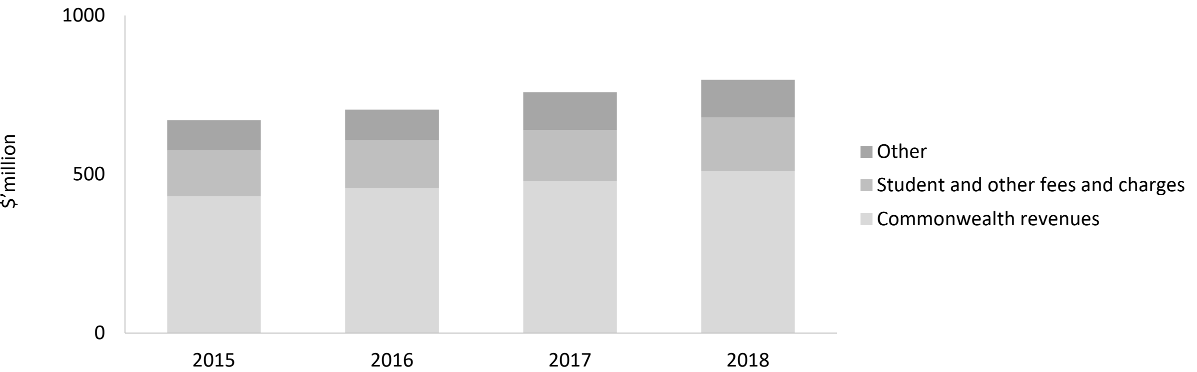


Total expenses increased in 2017-18 by $13 million (0.4%) to $3.24 billion. This comprised:

- a $70 million increase in employee benefits expenses reflecting:
  - a $28 million increase in long service leave expense, mainly reflecting that there was a significantly lower expense in 2017 as a result of an increase in the bond rate used to calculate the value of the long service leave liability reducing the expense. The bond rate used in 2018 was the same as in 2017
  - a $56 million increase in salaries and wages (including annual leave) that resulted from an increase of 742 employees and enterprise bargaining increases
  - offset by a $16 million decrease in workers compensation expenses as a result of a lower provision following a change in the allocation approach for this liability across government and a decrease in the liability for serious injury
- a $19 million increase in supplies and services mainly due to an increase in minor works, maintenance and equipment of $32 million offset by a general decrease due to DCP transferring out from 1 November 2016
- a $26 million increase in depreciation due to the impact of a revaluation increase of $557 million in 2016-17 mainly for buildings and improvements, with a higher amount being depreciated in 2018
- offset by a $104 million decrease in grants and subsidies primarily due to the transfer of Families SA to DCP in 2017, resulting in a reduction of $113 million in grants for this area, offset by an overall increase in other grants and subsidies.

Income

A structural analysis of the main income items for Education for the four years to 2018 is shown in the following chart.



In 2017-18 total income increased by $39 million (5%) to $797 million. This included:

- a $31 million increase in Commonwealth revenue due to an increase in National Education Reform Agenda funding, reflecting indexation under the funding arrangement and an increase of 1015 students
- an $8 million increase in student and other fees and charges, primarily due to a $4 million increase in student material and services charges and an increase in students.

Revenues from SA Government

Revenues from the SA Government decreased by $33 million (1%) to $2.5 billion, including a $169 million decrease due to the transfer of Families SA to DCP in 2017, partially offset by the receipt of additional funding of $143 million for capital projects, mainly for STEM works in government schools.

Statement of Financial Position

Assets

Current assets decreased by $6 million due to:

- a $6 million decrease in cash and cash equivalents and a $4.4 million decrease in assets held for sale due to the sale of land and buildings
- offset by a $5.7 million increase in receivables, due to an increase in GST recoverable from the ATO.

SA Schools Investment Fund (SASIF) cash balances

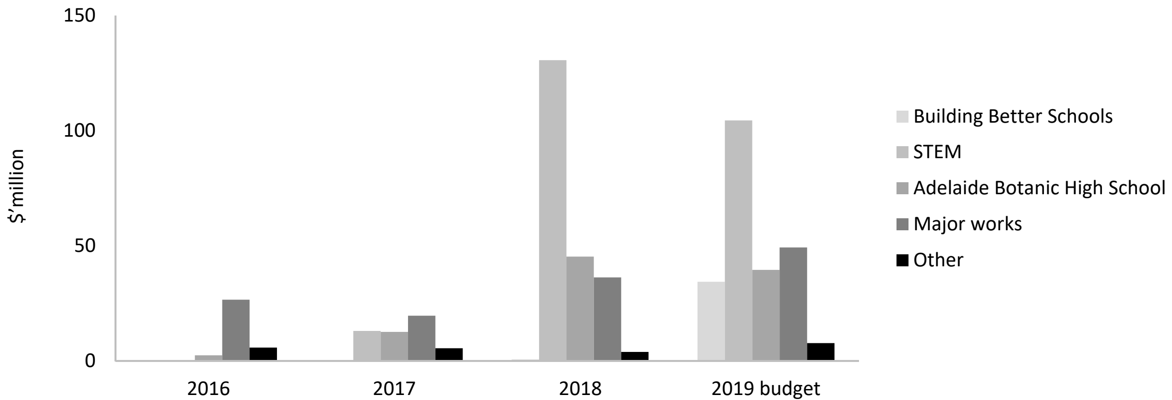
We have previously highlighted continued growth in school cash balances held in SASIF accounts. As at 30 June 2018, total physical SASIF balances for schools and preschools were $496.2 million ($491.9 million).

While there has been a marginal increase in total SASIF balances in 2018, Education will issue guidance on its expectations for SASIF balances, with Education indicating that a higher proportion of SASIF balances are expected to be allocated to specific projects in future years.

Property, plant and equipment increased by $162 million to $4.7 billion

The increase of $162 million in the value of property, plant and equipment was mainly a result of capital works additions, which increased by $166 million to $217.8 million.

Capital works will continue to increase over the next few years due to a number of programs and specific projects as outlined in the chart below.



In 2017-18 the increase in capital works additions of $166 million is mainly due to an increase of $118 million for STEM projects. STEM projects are due to be completed by 31 December 2018. There was also a $33 million increase in the total spent for the Adelaide Botanic High School which is due to open in January 2019. All major capital works projects are being managed by DPTI.

In 2018-19 capital works additions will increase again due to the Building Better Schools program. This program is for $692 million to be spent over six years on improving, refurbishing and expanding capacity at 91 government schools. It includes providing some facilities to move year 7 students from primary to high school, in line with government policy.

Liabilities

As at 30 June 2018 liabilities mainly comprise:

- employee benefits and related on-cost liabilities of $763 million ($738 million), making up 66% (66%) of total liabilities
- borrowings of $168 million ($169 million) relating to obligations under the finance lease for the schools' facilities Public Private Partnership agreement, comprising 15% (15%) of total liabilities
- the provision for workers compensation of $59 million ($72 million), which accounts for a further 5% (6%) of total liabilities.

The workers compensation provision has decreased steadily since 2013-14. Movements over the past five years are shown in the following table.

	2013-14 $'million	2014-15 $'million	2015-16 $'million	2016-17 $'million	2017-18 $'million
Payments	26.9	30.9	30.4	20.7	16.4
Balance of the provision	117.1	101.4	92.5	72.2	58.6

The closing balance of the workers compensation provision varies according to actuarial assessments undertaken each year and reduced by $20.3 million in 2016-17 mainly due to the transfer of Families SA staff to DCP.

The actuarial assessment reflects a range of items, including economic assumptions, experience of actual claims and the impact of any legislative changes to workers compensation arrangements. The decrease of $13.6 million in 2017-18 is mainly due to a change in the allocation approach across government and a decrease in the liability for serious injury.

Statement of Cash Flows

Education's cash position decreased by $6 million in 2017-18 mainly due to increased additions to capital works.

As at 30 June there was cash of $943 million ($949 million), which includes:

- deposits with the Treasurer in the Accrual Appropriation Excess Fund Account of $356 million ($441 million), which decreased due to a withdrawal of $85 million with the Treasurer's approval to fund capital works projects
- deposits with the Treasurer of $102 million ($40 million), which increased mainly due to the increase in capital creditors
- $447 million ($431 million) in cash held by schools in SASIF accounts, which increased by $16 million in 2017-18 due to schools not spending their full resource allocation.

Administered items

Education administers certain funds on behalf of the Minister for Education. Funds are received from the Commonwealth and SA Governments and used mainly to pay:

- transfers to non-government schools of $1075 million ($1025 million)
- family day care child care subsidies of $19 million ($20 million)
- subsidies of $13 million ($13 million) to DPTI for student travel concessions on metropolitan and country transport services
- an operating grant to the SACE Board of South Australia of $19 million ($20 million).

There was increased activity in a number of administered accounts for 2018 due to the *Children and Young People (Oversight and Advocacy Bodies) Act 2016* being enacted on 18 December 2017, which established the Commissioner for Children and Young People and the Guardian for Children and Young People, with both of these bodies reported in Education's administered activities.

Environment Protection Authority (EPA)

Financial statistics	Net assets:	$27.8 million
	Net revenue from providing services:	$16.8 million
	Total comprehensive result:	$4.9 million
	Number of FTEs:	216

Significant events and transactions

— $32 million of solid waste levies was transferred to the Green Industries Fund (Green Industries SA).

— Surplus cash of $12 million was returned to the SA Government under the cash alignment policy.

— EPA moved premises resulting in the:
- write-off of $1.8 million in leasehold improvements at its former premises
- recognition of $829 000 in leasehold improvements made available by the new landlord.

Financial report opinion — **Unmodified**

Financial controls opinion — **Unmodified**

Functional responsibility

The EPA is South Australia's primary environmental regulator for the control and minimisation of pollution and waste. It is responsible for the protection and enhancement of air and water quality, and control of pollution, waste and environmental noise.

The EPA financial reporting entity comprises the following:

- a statutory authority with an appointed board established by the *Environment Protection Act 1993* (the EP Act)
- an administrative unit, also named the EPA, established under the *Public Sector Act 2009*
- the Environment Protection Fund established under the EP Act.

The EP Act permits the statutory authority to make use of the services of the administrative unit's employees and facilities. The administrative unit is also responsible for radiation protection functions under the *Radiation Protection and Control Act 1982.*

Under the EP Act, the Chief Executive of the administrative unit is also taken to be the Chief Executive of the statutory authority. The Chief Executive is subject to the control and direction of the Minister in relation to the activities of the administrative unit, and is subject to the control and direction of the Board in giving effect to its policies and decisions under the EP Act.

Scope of the audit

The audit program covered major financial systems to obtain sufficient evidence to form an opinion on the financial report and internal controls.

Specific areas of audit attention in 2017-18 included:

- waste levies revenue
- licence fee revenue
- accounts payable
- payroll
- fixed assets
- purchase cards
- general ledger.

Audit findings and comments

Communication of audit matters

A number of minor matters identified by the audit were detailed in management letters to the Chief Executive. The EPA's responses indicated that appropriate action would be taken to address the matters raised.

Shared Services SA – financial systems and transaction processing environments

Shared Services SA processes financial transactions on behalf of the EPA under service level determinations. The main systems and control environments include accounts payable, payroll and general ledger financial functions.

Our review and evaluation of controls for these systems concluded that controls were effective for 2017-18.

Shared Services SA is discussed further in the commentary under 'Department of the Premier and Cabinet' in this Report.

Interpretation and analysis of the financial report

Highlights of the financial report*

	2018 $'million	2017 $'million
Expenses		
Employee benefits expenses	24	23
Supplies and services	9	8
Other expenses	4	2
Total expenses	36	33
Income		
Fees and charges	51	44
Other revenues	2	1
Total income	53	45
Net revenue from providing services	17	12
Net payment to SA Government	12	6
Net result	5	6
Net cash provided by (used in) operating activities	5	6
Assets		
Current assets	34	27
Non-current assets	4	6
Total assets	39	34
Liabilities		
Current liabilities	4	4
Non-current liabilities	7	7
Total liabilities	11	11
Total equity	28	23

* Table may not add due to rounding.

Statement of Comprehensive Income

Expenses

Total expenses increased by $3.1 million in 2017-18, due mainly to:

- a $1.8 million increase in other expenses due primarily to property, plant and equipment write-offs, most of which related to leasehold improvements at EPA's former premises
- an $890 000 increase in employee benefits expenses primarily resulting from increases in salaries and wages ($563 000), long service leave expense ($337 000) and superannuation on-costs ($269 000), offset by a decrease in workers compensation expense ($347 000).

  The increase in salaries and wages was due mainly to enterprise agreement salary increases.

The increase in long service leave expense reflects more leave taken or paid out on termination in 2017-18 compared to the previous year, and the increase in the long service leave liability.

The increase in superannuation on-costs reflects the increase in salaries and wages and employee benefits liabilities.

The decrease in workers compensation expense reflects the reduction in the workers compensation provision.

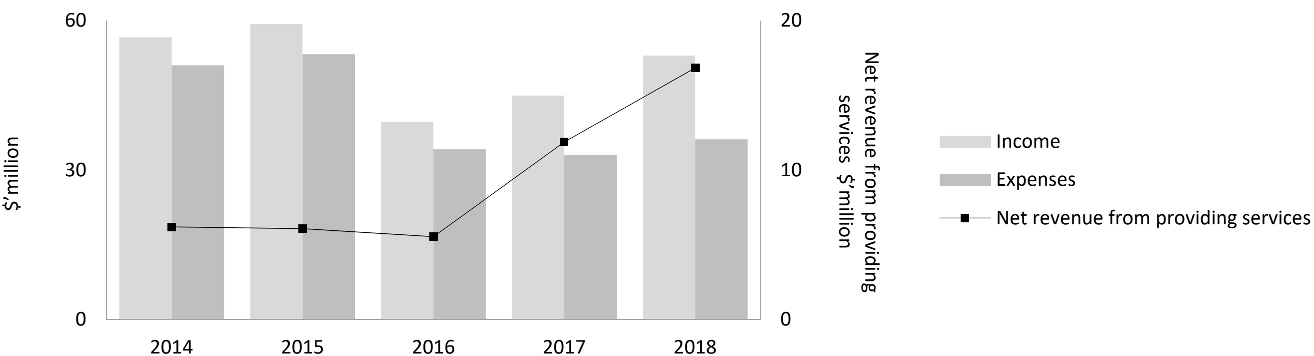
Income

Total income increased by $8 million in 2017-18 due primarily to a $6 million increase in waste levies recognised in revenues from fees and charges. Solid waste levies are discussed further under 'Further commentary on operations' below.

Net benefit of providing services

The chart below shows the income, expenses and net revenue from providing services for the five years to 2018.

Since 2014, the EPA has funded its operations by raising fees and charges and has not required any appropriation funding from the Consolidated Account. Over this period, under the cash alignment policy, the EPA has returned $36.8 million in surplus cash directly to the Consolidated Account.



Income and expenses in years 2014 and 2015 in this chart include solid waste levies received and transferred to the Green Industries Fund (Green Industries SA). In 2017 the EPA changed its reporting policy for solid waste levies. Since then levies that the EPA is required by law to transfer to the Green Industries Fund are recognised as an administered activity. More information on solid waste levies is provided under 'Administered items' below. The increase in net revenue from providing services since 2017 is driven by increases in solid waste levies.

Payments to SA Government

The EPA has achieved operating surpluses and generated surplus cash from operations for a number of years. It has returned $31.4 million to the Consolidated Account over the past four years.

The following table sets out payments to the SA Government and cash balances at 30 June for those years.

	2015 $'million	2016 $'million	2017 $'million	2018 $'million
Payments to SA Government	7.3	6.3	5.8	12.0
Cash	15.8	15.6	21.6	26.6

Statement of Financial Position

Current assets – cash and cash equivalents

Cash and cash equivalents, $27 million ($22 million), represent 78% (79%) of total current assets and 69% (64%) of total assets. They include the Environment Protection Fund deposit account of $8 million.

Use of the money held in the Environment Protection Fund requires the approval of the Minister and must be consistent with the requirements of the EP Act.

Non-current assets

Property, plant and equipment make up 6% (11%) of total assets. Furniture and fittings and plant and equipment are the dominant items.

Property, plant and equipment decreased by $1.4 million due mainly to:

- asset write-offs of $1.8 million, most of which related to leasehold improvements at EPA's former premises
- depreciation expense of $514 000
- the transfer of capital works in progress to intangibles of $126 000
- the recognition of $456 000 in leasehold improvements in EPA's new premises provided by the landlord as a lease incentive
- the recognition of $373 000 in leasehold improvements in EPA's new premises left by the former tenant
- additions of $277 000.

Intangible assets make up 6% (7%) of total assets. The licencing administration management program (LAMP), environment licencing forms (ELF) and general environment information (GENI) systems are the dominant items.

Administered items

The EPA's administered activities comprise:

- solid waste levies collected and transferred to the Green Industries Fund
- revenue arising from the litter provisions in the *Local Nuisance and Litter Control Act 2016.*

Transfer of solid waste levies to the Green Industries Fund (Green Industries SA)

The EPA receives solid waste levies from waste depots under section 113 of the EP Act. There was an increase in solid waste levy rates of 14% from 1 July 2017, compared to a 9% increase from 1 July 2016 and a further 23% from 1 September 2016. Section 17 of the *Green Industries Act 2004* requires the EPA to transfer 50% of these levies to the Green Industries Fund.

This fund may be applied by Green Industries SA in line with its approved business plan, or in any other way authorised by the responsible Minister for the purposes of the *Green Industries Act 2004.*

The EPA transferred $32 million ($27 million) to the Green Industries Fund during the year.

The balance of the Green Industries Fund at 30 June 2018 was $120.3 million ($108.3 million).

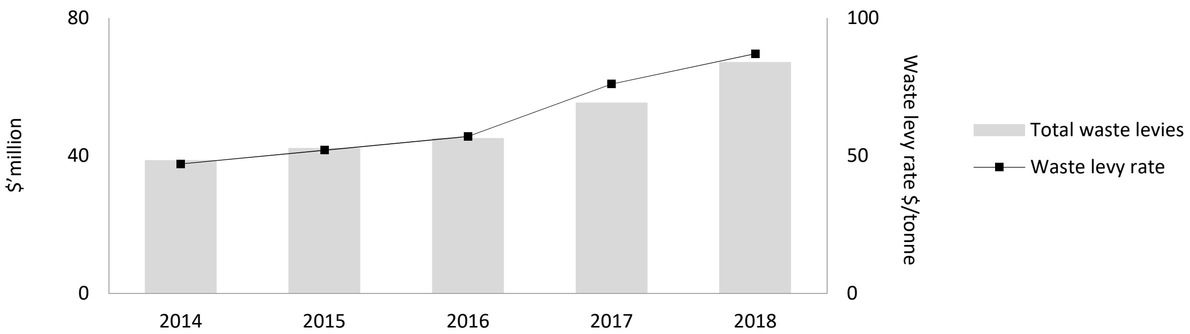
Further commentary on operations

Waste levies

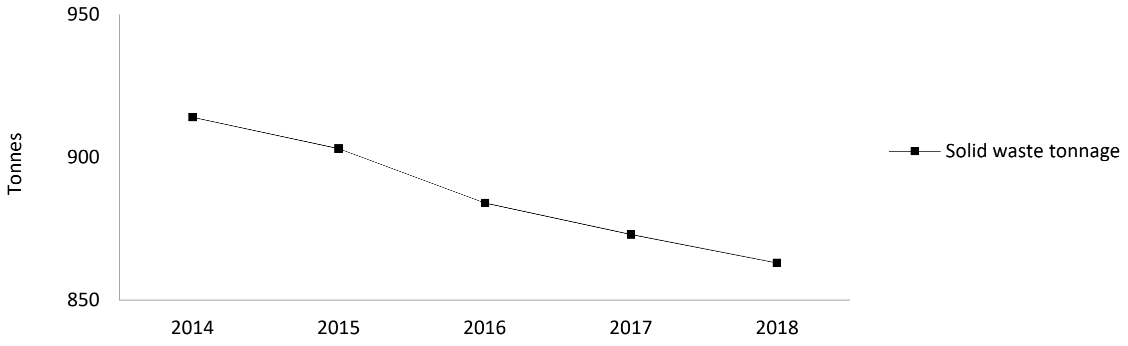
Waste levies collected by the EPA (controlled and administered) totalled $67.2 million ($55.4 million) (refer notes 10 and 36 of the EPA's financial report).

There has been an increasing trend in solid waste levy rates that has been offset by a decrease in solid waste tonnage reported as received by waste depots.

The following chart shows the amounts collected from waste levies from 2014 to 2018.



The following chart shows the decrease in solid waste tonnage reported by waste depots over the same period. This data was provided to us by the EPA.



Department for Environment and Water (DEW)

Financial statistics	Net cost of providing services:	$73.6 million
	Total appropriation:	$156.9 million
	Employee benefits expenses:	$158.5 million
	Property, plant and equipment:	$740 million
	Number of FTEs:	1517.9

Significant events and transactions

- Property, plant and equipment was revalued upwards by $32.5 million.
- Property, plant and equipment as at 1 July 2017 was increased by $24 million, mainly to recognise land gazetted as conservation parks in 2017 that DEW had not previously recorded.
- Property, plant and equipment valued at $12.5 million was transferred from administered items for $0 consideration.

Financial report opinion

Unmodified

Financial controls opinion

Modified

Key issues:

- Large numbers of incomplete and unapproved time attendance records
- Leave transactions for some branches and regions not reconciled to the payroll system since 2013-14
- Large numbers of reconciling items in the bank reconciliation
- DEW did not identify that it had been overcharged by $1.4 million for rent
- User access to the Masterpiece financial system was not reviewed effectively

Functional responsibility

DEW is an administrative unit established under the *Public Sector Act 2009*, and is responsible to the Minister for Environment and Water.

Effective from 17 May 2018, the Department of Environment, Water and Natural Resources was renamed the Department for Environment and Water. This change did not impact the purpose, objectives and structure of DEW.

DEW has significant responsibilities in managing the State's natural environment for the prosperity and wellbeing of current and future generations of South Australians. To support this DEW:

- safeguards the State's natural environment through sustainable management, evidence based decision-making and service delivery, with the focus on the community and stakeholders
- connects and involves people with nature by opening up parks and places
- unlocks the potential of the State's natural environment to contribute to the economic development and prosperity of South Australia.

Scope of the audit

The audit program covered major financial systems to obtain sufficient evidence to form an opinion on the financial report and internal controls.

Specific areas of audit attention in 2017-18 included:

- fees and charges revenue
- water licence and levy revenue
- grant revenue
- accounts payable
- grants and subsidies expenditure
- payroll
- cash
- fixed assets
- purchase cards
- general ledger.

We also reviewed IT general controls in relation to DEW's Masterpiece application.

Audit findings and comments

Assessment of controls

In my opinion, the controls exercised by the Department for Environment and Water in relation to the receipt, expenditure and investment of money, the acquisition and disposal of property and the incurring of liabilities, except for all matters outlined under 'Communication of audit matters', are sufficient to provide reasonable assurance that the financial transactions of the Department for Environment and Water have been conducted properly and in accordance with law.

Communication of audit matters

Matters identified by the audit were detailed in management letters to the Chief Executive. The main matters raised and related responses are detailed below.

Accounts payable

Review of Basware user access was not effective

Shared Services SA (SSSA) provides DEW's Finance and Business Services (FBS) branch with quarterly reports that detail user access and financial authorisation limits in the Basware payment processing system. DEW is required to review the validity of the information on the reports and provide SSSA written confirmation of the validity of information, and details of any changes required.

Our review of this process identified the following matters:

- DEW's review of the September 2017 quarter user access report did not identify 16 users whose employment had terminated
- confirmation of the validity of information on the September 2017 quarter user access report and details of required changes was not provided to SSSA until 23 January 2018. Delays in reviewing user access increases the risk of invalid user access and processing error.

DEW responded that details of the 16 identified users have since been forwarded to SSSA to deactivate their Basware access.

DEW also advised that it has agreed a revised approach to completing quarterly user access reviews with SSSA. DEW's business units will now advise SSSA directly of any changes they identify, with DEW's FBS branch receiving a copy of requested changes as evidence of the review performed. The FBS branch will follow up with business units that have not completed their review.

DEW is confident that the revised approach will address delays resulting from the collation of review results from Business Managers.

Payment of incorrect accommodation charges

In May 2016 DEW entered into a new lease with the Department of Planning, Transport and Infrastructure (DPTI) for accommodation in the Adelaide CBD. The lease agreement with DPTI included a lease incentive in the form of a rental rebate over the first five years of the lease.

We noted that DPTI had not reduced its rental charges for the value of this rebate since inception of the lease. DEW had not identified the overcharge, which we estimated was $1.4 million for the period May 2016 to April 2018.

DPTI has subsequently adjusted the lease arrangements to ensure DEW receives the value of the lease incentive and these adjustments were recognised at 30 June 2018.

Payroll

Employee benefits expenses were $159 million in 2017-18 and the liability for leave entitlements at 30 June 2018 was $50 million.

The findings identified below are consistent with those reported in prior years, indicating that past action taken by DEW has not resulted in any notable improvement in the control environment. We have therefore recommended that DEW's Organisational Performance (OP) branch (Human Resources) monitor compliance with these controls and that non-compliance is reported to DEW's executive management team for their information and action.

Bona fide report certification

The DEW bona fide policy requires pay point delegates to review and certify fortnightly bona fide reports. This provides DEW with assurance that only valid employees are paid and that employees are paid correctly. Certified bona fide reports are recorded on a central register.

We noted that 8.6% of bona fide reports for the financial year were not recorded as certified on the register as at 6 February 2018.

DEW responded that:

- the bona fide register will be monitored by the OP branch and reminders sent to branches with outstanding certifications
- a reminder reinforcing the need to comply with DEW's bona fide policy will be sent to Business Managers for distribution to pay point delegates
- a new program to monitor bona fide report certification will be established by the OP branch. Non-compliance will be reported to DEW's executive management team for their information and action.

Large numbers of incomplete and unapproved attendance records

DEW uses the TimeWise system to monitor employee attendance and approve leave taken. We noted:

- 356 TimeWise attendance records were yet to be completed by DEW employees, some dating back to August 2017
- 549 completed TimeWise attendance records were yet to be reviewed and approved, some dating back to August 2017.

We also noted that the reconciliation of leave transactions recorded in TimeWise with leave records in the CHRIS payroll system had not been performed for all branches/regions, with some of the outstanding reconciliations relating to 2013-14.

DEW relies on these controls to ensure all leave taken is deducted from an employee's leave entitlement. If they are not operating effectively DEW's leave liabilities may be overstated. Further, without accurate CHRIS leave records, managers may approve leave in excess of actual entitlement, resulting in salary overpayments.

DEW responded that:

- a reminder reinforcing the need to comply with DEW's time and attendance recording procedures will be sent to all employees
- the OP branch will continue to monitor the extent of incomplete and unapproved TimeWise records and report non-compliance to DEW's executive management team for their information and action
- the OP branch will investigate whether TimeWise reports can be enhanced to assist with follow-up of non-compliance
- the OP branch has allocated resources to ensure all outstanding TimeWise to CHRIS reconciliations up to December 2017 are completed by 30 June 2018. DEW is also negotiating with SSSA to ensure that they allocate adequate resources to ensure any required adjustments are made promptly.
- a program will be established by the OP branch to ensure TimeWise to CHRIS reconciliations are being regularly performed by branches/regions and non-compliance will be reported to DEW's executive management team for their information and action.

DEW advised that it had completed all TimeWise to CHRIS reconciliations up to December 2017.

TimeWise leave and overtime approval

Managers have access to the TimeWise system to check and approve leave and overtime requests. This approval is required to ensure that the overtime is necessary and that occupational health and safety requirements are considered.

We noted, however, that the TimeWise user access profile structure is not consistent with DEW's delegations of authority. Some TimeWise users have access to approve leave and overtime requests in excess of their delegated authority.

In 2017-18 we noted numerous instances where overtime and long service leave was approved in TimeWise by officers in excess of their delegated authority. For a sample of TimeWise entries made between 1 July 2017 and 31 December 2017 we identified:

- 553 overtime entries out of 1997 instances were approved by officers with insufficient delegation
- 62 long service leave entries out of 158 instances were approved by officers with insufficient delegation.

Most of the exceptions associated with overtime relate to a small number of TimeWise workgroups.

These statistics are consistent with observations we have made in prior years, with DEW responding that it would educate staff to ensure they understand their responsibilities.

In 2018 DEW responded that:

- the OP branch will investigate and implement, where possible, changes in TimeWise that will bring to managers' attention the delegated level required to approve leave

- it is considering an internal compliance program to ensure managers understand their delegations, including those relating to overtime and leave approvals
- as part of the next review of delegation levels, it will review the delegations allocated to the workgroups to ensure they align with current business practice.

Cash

Clearing of reconciling items

We noted 36 028 reconciling items totalling $1.7 million in the DEW bank reconciliation for February 2018. They were due mainly to issues associated with transactions processed through DEW's Hospitality and Leisure Point of Sale, Bookeasy, Desert Park Passes and Parks Passes systems.

DEW responded that a number of permanent system solutions were being tested and that the existing reconciling items would be cleared prior to the preparation of its 2017-18 financial report.

When reviewing DEW's 2017-18 financial report we noted that, while the number and value of reconciling items had decreased, DEW had not resolved all matters in its June 2018 bank reconciliation. Over 26 000 reconciling items totalling $822 000 remained unresolved.

The bank reconciliation is a fundamental control to ensure the completeness and accuracy of DEW's financial statements. The difficulty in promptly clearing all reconciling items on DEW's bank reconciliation has been a recurring issue and it is disappointing that it has been unable to resolve this matter.

Design of the DEW bank reconciliation

The DEW bank account is used by 16 separate entities and 22 funds (bureau entities) established to support specific Commonwealth and SA Government programs.

The bank reconciliation is a fundamental control for both DEW and its bureau entities. Performed regularly, it helps to confirm the integrity of accounting records and identify errors or irregularities requiring action.

SSSA performs the bank reconciliation but requires DEW's assistance, particularly in relation to revenue.

We noted the bank reconciliation does not separately identify or classify reconciling items between DEW and its bureau entities. Without this level of detail SSSA cannot assess the impact that reconciling items have on DEW's, or its bureau entities', financial reporting.

DEW responded that it had developed a report that separately identifies and classifies all reconciling items between DEW and its bureau entities.

For the June 2018 bank reconciliation, we noted that DEW had prepared a report that classifies transactions recorded in the bank account but not yet agreed to general ledger records. DEW had not prepared a similar report that classifies transactions recorded in the general ledger but not yet agreed to bank records. There were transactions valued at $927 000 that may impact the accuracy of cash recognised by DEW and its bureau entities.

While DEW was able to provide evidence that most of these transactions relate to DEW activities, the absence of an effective bank reconciliation increases the risk that errors in bureau entity financial statements are not resolved.

Fixed assets

Excluding land and capital works in progress, DEW controlled fixed assets valued at $373 million as at 30 June 2018. These assets comprise approximately 16 000 individual assets reported across 13 different asset classes in DEW's financial statements.

Matters arising from the audit of fixed assets are detailed below.

No schedule of planned asset stocktakes for the current five-year cycle

DEW's asset stocktake procedure requires stocktakes to be completed over a five-year rolling period to enable planning for remotely located assets.

We noted that DEW had not developed an asset stocktake schedule that ensures all assets are verified within the five-year stocktake cycle. As a result, DEW officers could not confirm whether all required asset classes will be verified in the current cycle.

If asset stocktakes are not performed, the existence and condition of assets cannot be confirmed, which may result in a material error in DEW's financial statements.

DEW responded that asset stocktake schedules covering on-park assets over a three and five-year time frame will be developed. These schedules will be discussed, reviewed and agreed to by relevant business units. Stocktake schedules for all other asset classes will be revised, updated and developed where required, to ensure stocktakes are completed for all asset classes within a five-year cycle.

DEW's stocktake procedure does not clearly outline which assets are covered

We noted the current DEW asset stocktake procedure does not clearly outline which DEW fixed asset classes it covers. This has resulted in inconsistencies between the actual stocktake practice and DEW's asset stocktake procedure.

DEW responded that the wording of the asset stocktake procedure will be revised to ensure it clearly reflects DEW's desired stocktake processes, time frames and the asset classes subject to stocktake. This process will include reviewing the role of independent valuers in confirming the existence of assets at the time of undertaking asset revaluations.

General ledger

User access to the Masterpiece financial system not reviewed effectively

SSSA provides DEW with quarterly reports that identify Masterpiece users and their access level. DEW is required to review the validity of the user information on the reports, including the level of access, and provide details of any changes required to SSSA for actioning.

We were advised that staff reviewing the reports only check the validity of DEW users and not the appropriateness of access levels assigned to them.

DEW responded that the quarterly Masterpiece user access review will now include a review of the appropriateness of access levels assigned to users.

Other areas

Risk management

Risk management, including the identification, monitoring and reporting of risks, is an integral part of DEW's internal control environment and provides assurance that DEW is managing risk effectively.

Last year we noted that DEW's risk management policy was past its review date. We also noted that DEW was developing a new risk management framework.

In December 2017, DEW's Risk and Performance Committee (RPC) endorsed the draft risk management framework, together with a work plan to implement the framework. Both the framework and the work plan were referred to DEW's executive for approval.

In June 2018 we noted that:

- while neither the risk management framework or the work plan had been approved by DEW's executive, the draft risk management framework was being implemented across DEW
- the risk management policy had been reviewed and the revised policy had not been submitted to the RPC for endorsement.

DEW responded that the framework will be updated to reflect the outcome of the DEW executive strategic risk workshop in October 2018 and presented to executive for approval in December 2018.

DEW also advised that the revised risk management policy will be endorsed by the RPC and submitted to the Chief Executive for approval by December 2018.

Annual internal audit plan not endorsed by the RPC or approved by the Chief Executive

The internal audit charter requires the Risk and Audit Team to prepare an annual internal audit plan and for the plan to be approved by the Chief Executive on the recommendation of the RPC.

While the RPC considered potential areas for internal audit review and endorsed the performance of specific reviews, the 2017-18 internal audit plan was not formally endorsed by the RPC or approved by the Chief Executive.

Internal audit provides the Chief Executive with assurance as to the effectiveness and efficiency of DEW's financial and operational controls. It is important that the RPC and the Chief Executive evidence that they are satisfied that the plan provides them with the level of assurance they require in response to the agency's identified risks.

DEW responded that the 2018-19 internal audit plan will be endorsed by the RPC and approved by the Chief Executive by December 2018. In future years, the annual internal audit plan will be finalised by 30 June for the next financial year, with any revision to the plan to be endorsed by the RPC.

IT general control (ITGC) review – Masterpiece application

In 2017-18 we reviewed the ITGCs operating within and around DEW's Masterpiece application. This included password management, privileged user access, audit logging, patch management, change management, backup and disaster recovery management.

Our review identified there was:

- inappropriate assignment of privileged user access accounts
- inadequate Masterpiece patching processes. Patching is a process to update, fix or improve a system.

These findings increase the likelihood of unauthorised access and/or unauthorised changes to the Masterpiece environment.

DEW responded positively to our findings and agreed to take appropriate remedial action.

Shared Services SA – financial systems and transaction processing environments

SSSA processes financial transactions on behalf of DEW under service level determinations. The main systems and control environments include accounts payable, payroll and general ledger financial functions.

Our review and evaluation of controls for these systems concluded that controls were effective for 2017-18.

SSSA is discussed further in the commentary under 'Department of the Premier and Cabinet' in this Report.

Interpretation and analysis of the financial report

Highlights of the financial report*

	2018 $'million	2017 $'million
Expenses		
Employee benefits expenses	158	155
Supplies and services	73	93
Grants and subsidies	34	32
Depreciation and amortisation expense	24	25
Other expenses	6	13
Total expenses	296	319
Income		
Fees and charges	103	97
Grants revenues	97	59
Other income	23	3
Total income	222	159
Net cost of providing services	74	160
Revenues from (Payments to) SA Government	157	141
Net result	83	(19)

	2018 $'million	2017 $'million
Other comprehensive income	32	49
Total comprehensive income	116	30
Net cash provided by (used in) operating activities	94	25
Assets		
Current assets	199	162
Non-current assets	746	641
Total assets	945	803
Liabilities		
Current liabilities	56	52
Non-current liabilities	56	58
Total liabilities	112	110
Total equity	832	693

* Table may not add due to rounding.

Statement of Comprehensive Income

Expenses

Total expenses decreased by $23 million. The major items causing this change were:

- a $20 million (21%) decrease in supplies and services reflecting:
  - a $6.8 million (34%) decrease in fee-for-service, due mainly to the completion of the Greater Artesian Basin Sustainability Initiative (GABSI)
  - a $5.5 million (54%) decrease in minor works, maintenance and equipment. Last year's expenditure included remedial work to address damage caused by severe storm events to DEW assets
  - a $2.1 million (50%) decrease in bore drilling services, due mainly to the completion of the GABSI
  - a $2 million (16%) decrease in general administration following a $1.6 million decrease in legal fees, most of which related to the South East Flows Restoration project
  - a $1.5 million (11%) decrease in accommodation and property management, due mainly to a $905 000 credit note issued by DPTI as a rental rebate
  - a $1.4 million (23%) decrease in sand replenishment, reflecting additional expenditure in 2016-17 for urgent restorative works to address damage caused by severe storms in September 2016
- a $6.8 million (52%) decrease in other expenses, due mainly to a $6.4 million decrease in assets transferred to other entities for $0 consideration, offset by $3.1 million for settlement of legal claims
- a $1.9 million (8%) decrease in depreciation and amortisation expense reflecting:
  - a $1.6 million (32%) decrease in depreciation of buildings and improvements – 96 buildings being fully depreciated in 2016-17

  - a $1.5 million (39%) decrease in depreciation of park infrastructure, due mainly to 639 park infrastructure assets being fully depreciated in 2016-17
  - a $1.3 million (22%) decrease in depreciation of roads, tracks and trails – 1606 roads, tracks and trails assets being fully depreciated in 2016-17
  - a $2 million (89%) increase in depreciation of groundwater monitoring wells, due mainly to their revaluation as at 30 June 2017
- a $3.1 million (2%) increase in employee benefits due mainly to:
  - a $1.4 million (60%) increase in long service leave expense, reflecting more leave taken or paid out on termination in 2017-18 compared to last year, and the increase in the long service leave liability
  - a $1.2 million (1%) increase in salaries and wages, reflecting enterprise agreement salary increases, offset by the implementation of the vacancy management strategy in January 2018, which involved prioritising work and applying alternative methods to filling roles in the latter half of 2017-18, and a 44.2 decrease in average FTEs compared to 2016-17
- a $2.4 million (8%) increase in grants and subsidies, due mainly to a $3.3 million increase in funding to the Murray-Darling Basin Authority (MDBA), $1.1 million in funding for the South East Confined Aquifer Well Rehabilitation and $1.3 million in funding for other grant programs, offset by a $1.7 million decrease in funding for the Nilpena Station Ediacaran Fossil site and a $900 000 decrease in funding for the Coorong, Lower Lakes and Murray Mouth long-term plan.

Income

Total income increased by $63 million. The major items causing this change were:

- a $38 million (65%) increase in grant revenues primarily due to:
  - a $21.5 million increase in funding from the Commonwealth for the SA Riverland Floodplain Infrastructure program following a variation in the timing of the milestone payments in the funding agreement
  - a $14.7 million increase in funding from the Commonwealth for the Murray Futures – Riverine Recovery program due to a change in timing for the program for factors such as high water flows
  - a $4.9 million increase in funding from the Commonwealth for the Flows for the Future program
  - a $4.4 million increase in funding from the Commonwealth for the Coorong, Lower Lakes and Murray Mouth long-term plan
  - a $4.3 million decrease in funding from the Commonwealth for the GABSI
- $19.8 million in resources received free of charge, comprising property, plant and equipment ($15.4 million) and services provided by SSSA ($4.4 million).

Statement of Financial Position

DEW's assets comprise two main items: property, plant and equipment and cash.

Non-current assets – property, plant and equipment

Property, plant and equipment is $740 million and represents 78% of total assets.

Property, plant and equipment includes land valued at $301 million, which comprises national, conservation and recreation parks and wilderness protection areas and reserves. In addition, related park infrastructure amounts to $24.2 million and roads, tracks and trails total $31.7 million.

Property, plant and equipment increased by $104 million due mainly to additions of $59.3 million, a $32.5 million adjustment on revaluation of sand pumping infrastructure, waste disposal stations and regulators and embankments, a $24 million error correction to recognise assets for the first time and $15.4 million in assets received for $0 consideration (donated assets), all partially offset by $22.8 million in depreciation charges. Donated assets included $12.5 million in Crown land proclaimed as new parks and additions to existing parks and reserves.

Refer note 22 of DEW's financial report for an analysis of this significant disclosure item.

Current assets – cash

Cash of $184 million ($144 million) represents 92% (89%) of total current assets, and 19% (18%) of total assets. DEW's cash at 30 June 2018 comprised operating deposit accounts of $107 million ($78 million) and an Accrual Appropriation Excess Funds Account of $77 million ($66 million). Access to the latter account is subject to the Treasurer's/Under Treasurer's approval.

The large operating deposit account balance reflects unspent grant funding, which at 30 June 2018 totalled $86.4 million ($76.5 million).

Liabilities

Total liabilities increased by $2.6 million (2%) to $112 million. The major items causing this change were:

- a $4 million increase in creditors due mainly to costs incurred but unpaid at the end of the year on major capital works programs, including the South East Flows Restoration, Murray Futures – Riverine Recovery and West Beach seawall reconstruction
- a $1.3 million decrease in the lease incentive liabilities, reflecting 12 months of amortisation charges.

Administered items

DEW's administered activities include:

- the National Landcare Program (South Australia)
- the Natural Resources Management Fund
- the State's joint interest in the MDBA.

National Landcare Program (South Australia)

The National Landcare Program is administered by the Commonwealth and SA Governments under section 19(2) of the *Natural Heritage Trust of Australia Act 1997* (Cwlth) and section 5 of the *Natural Resources Management (Financial Assistance) Act 1992* (Cwlth).

The National Landcare Program items administered by DEW include grant revenues from the Commonwealth Government of $13.7 million ($13.6 million), grant expenses of $13.8 million ($13.7 million) and a cash balance of $337 000 ($431 000).

Natural Resources Management Boards (NRMBs) and Natural Resources Management Fund

DEW has primary responsibility for helping the Minister to administer the *Natural Resources Management Act 2004* (NRMA). The main purpose of the NRMA is to promote sustainable and integrated management of the State's natural resources and to protect these natural resources.

The NRMA provides for a range of entities with specific responsibilities, including eight regional NRMBs.

Water levies are collected by DEW for prescribed water resources within specific natural resources management regions under section 101 of the NRMA. The levies are subsequently paid to the regional NRMBs under section 116(1)(a)(ii)(A).

In 2017-18, $17.3 million ($17.1 million) in water levies, penalties and expiation fees were raised on behalf of the NRMBs. DEW also received $4.6 million ($2.5 million) in appropriation funding for transfer to the NRMBs.

Payments to NRMBs from the Natural Resources Management Fund during the year were $22 million ($19.5 million). These payments relate to water levies invoiced and collected by DEW. The NRMA requires the Minister to issue the levies and collect the revenue into the Natural Resources Management Fund. The Minister then distributes funds collected to the NRMBs based on receipts.

Murray-Darling Basin Authority

The MDBA is established under the *Water Act 2007* (Cwlth). It assumed all functions of the former Murray-Darling Basin Commission in December 2008.

The MDBA's functions are to:

- prepare, implement, monitor and enforce the Basin Plan
- implement the decisions of the Ministerial Council and Basin Officials Committee.

DEW has recognised the State's joint interest in the MDBA infrastructure assets and water rights as an interest in a joint operation in its administered financial statements. The State's interest in the arrangement is 26.67%.

The recognition of MDBA infrastructure assets and water rights is in line with the following agreements signed by the Commonwealth, NSW, Vic, SA, the ACT and the MDBA on 12 June 2009:

- asset agreement for River Murray Operations assets
- further agreement on addressing water over-allocation and achieving environmental objectives in the Murray-Darling Basin – control and management of Living Murray assets.

The State's interest in the arrangement was valued at $874.5 million ($876.5 million).

Health sector overview

Structure of this section of the Report

Collectively the Department for Health and Wellbeing (DHW), the local health networks (LHNs) and the SA Ambulance Service Inc (SAAS) are known as SA Health or the Health sector.

This section of the Report discusses the following matters:

- some significant health sector events and challenges
- an overview of governance arrangements
- unaudited health sector staffing and patient activity data.

Health sector – significant events and challenges

Total expenses for the consolidated SA Health sector in 2017-18 were $6.5 billion, an increase of $767 million (13.4%) over 2016-17.

Financial sustainability and budget

We have previously reported on continued hospital expenditure growth, failure to achieve savings targets and risks associated with the financial sustainability of the public health care system.

Note 35 of the DHW financial report provides some budgetary reporting information, including explanations of major variances between DHW's original budget provided to Parliament and actuals reported in the financial statements. Total actual expenses exceed the 2017-18 State Budget allocation to Health by $438 million, while total income exceeded the 2017-18 State Budget by $59 million. The net result is a deterioration of $379 million against the original budget. It is important to note that the budget data is not subject to audit.

Recent State Budgets have provided substantial additional funding to meet the growth in health costs. In the past two State Budgets $847.8 million was provided over the forward estimates to address shortfalls in original estimates:

- 2016-17: additional Health operating funding of $526.8 million (over four budget years)
- 2017-18: savings targets were reduced by $321 million across the forward estimates.

In 2017-18 we again looked at health sector budget and performance management, including its reported outcomes against budget and savings targets. I intend to table a separate Report on this. It will include commentary on budget outcomes and monitoring for 2017-18, and make some observations on governance and accountability in the public health system in light of proposed governance changes.

Future governance and accountability changes

The SA Government has announced its intention to amend governance arrangements across SA Health. The first part of these changes was completed in August 2018 when the *Health Care (Governance) Amendment Act 2018,* which will operate from 1 July 2019, was proclaimed.

The amendments change the role of the Chief Executive, DHW to remove direct control and responsibility for the administration of incorporated hospitals. The amendments also provide for the LHNs to be governed by a board. Governing boards will be established for each of the LHNs as they are currently constituted, except for the Country Health SA Local Health Network Incorporated (CHSALHN) which will be replaced by six regional LHNs. The creation of these LHNs is discussed under 'New regional country local health networks' below.

Governing boards will be appointed by the Minister for Health. The people appointed are to collectively have, in the opinion of the Minister, the knowledge, skills and experience necessary to enable the board to effectively carry out its functions. The SA Government intends LHN boards will be fully operational by 1 July 2019.

The SA Government has stated it will establish a new governance and accountability framework for the public health system that will be reflected in legislation to be introduced into Parliament later in 2018 or early next year.

These reforms present the most significant changes in the governance of SA Health since the introduction of the *Health Care Act in 2008* (HC Act) in 2018 and the introduction of LHNs in 2011.

The amended Act requires health services to be provided as part of an integrated system that achieves an effective balance between local decision-making at LHNs and health system planning, integration and management. Achieving this balance through a functional governance and accountability framework will be challenging but very important, and will require care and diligence. The success of the changes will be highly dependent on how well the framework supports the roles of DHW, the boards and the Minister and creates accountabilities throughout the sector.

The time frame for establishing legislation and frameworks and appointing people to boards and key management positions by 1 July 2019 will also be challenging and requires careful management.

New regional country local health networks created in August 2018

In August 2018 the following six new regional incorporated hospitals (LHNs) were proclaimed under the HC Act:

- Barossa Hills Fleurieu Local Health Network Incorporated
- Eyre and Far North Local Health Network Incorporated
- Flinders and Upper North Local Health Network Incorporated
- Riverland Mallee Coorong Local Health Network Incorporated
- South East Local Health Network Incorporated
- Yorke and Northern Local Health Network Incorporated.

They will take over the functions of providing health services from CHSALHN from 1 July 2019.

The changes are particularly significant for CHSALHN and will present challenges, particularly given the relatively small size of some of the regions and existing centralised processing and control frameworks.

Continued high turnover of senior executive positions

DHW and the LHNs again experienced significant turnover of their chief executives including:

- DHW – a new Chief Executive in May 2018
- Southern Adelaide Local Health Network Incorporated (SALHN) – a new Chief Executive Officer in March 2018

- Women's and Children's Health Network Incorporated (WCHN) – a new Chief Executive Officer in April 2018
- Northern Adelaide Local Health Network Incorporated (NALHN) – a new Interim Chief Executive Officer in April 2018
- SAAS – new Interim Chief Executive Officer in September 2018.

The new Royal Adelaide Hospital (RAH)

From 14 August 2017 clinical services progressively commenced at the new RAH. Patients were moved from the old RAH to the new RAH between 4 September 2017 and 6 September 2017. The emergency department opened on 5 September 2017.

Outstanding matters and operational disputes

While the new RAH commenced operations from September 2017, there are a number of outstanding works, action items, defects and modifications that await resolution. There are also a number of disputes relating to the operation of the hospital.

Part A of this Report under 'New Royal Adelaide Hospital update' discusses these matters including the status of:

- outstanding defects
- commercial acceptance outstanding items
- modifications
- legal proceedings initiated by the builder
- significant facility failures since operational commencement
- process suspension deeds entered into to resolve issues arising from operating the facility.

My Supplementary Report for the year ended 30 June 2017 'New Royal Adelaide Hospital: March 2018' outlined significant matters relating to the completion of works and hand-over of the facility to the State.

I intend to table another separate Report on the new RAH project. It will provide observations on the arrangements implemented by the State to manage the Project Agreement for the operating term, along with commentary on the June 2018 process suspension deed discussed in Part A of this Report.

Impact on the financial reports of CALHN and SA Health

The new RAH is recognised in the financial reports of the Central Adelaide Local Health Network Incorporated (CALHN) and SA Health. Liabilities of $2.76 billion and assets of $2.809 billion were reported as at 30 June 2018. SA Health has included details of the total commitments for the new RAH.

When the effect of discounting is excluded, the total nominal cost of the new RAH arrangements to the State over the term to June 2046 is $11.41 billion.

Further commentary on the arrangements, legal action and financial impact are included in the section of this Report titled 'Central Adelaide Local Health Network Incorporated'.

Repatriation General Hospital (RGH) site

The RGH was closed and decommissioned in November 2017.

Following the State election in March 2018, the contract to sell the RGH to the Aged Care and Housing Group Incorporated was officially terminated in May 2018.

An expression of interest for 'Reactivating the Repat Health Precinct' was released in August 2018 seeking submissions from the private sector and non-government organisations interested in partnering with SA Health to deliver a variety of health focused services at the site.

Further comments on the RGH decommissioning and reactivation are included in the section of this Report titled 'Southern Adelaide Local Health Network Incorporated'.

Oakden Older Persons Mental Health Facility

In February 2018, the Independent Commissioner against Corruption published a report that found NALHN had engaged in maladministration in public administration regarding the management of the Oakden Older Persons Mental Health Facility. All residents were moved out of the Oakden facility by the end of September 2017 and it was closed. Further comments on the Oakden facility are included in the section of this Report titled 'Northern Adelaide Local Health Network Incorporated'.

Information technology and system change

Over a number of years, DHW has developed and progressively implemented IT systems used to support financial and health related services, such as patient administration and clinical functions. Many of these systems and their dependencies are critical for the successful operations of the health system.

Enterprise Patient Administration System (EPAS)

In March 2018, the EPAS rollout was paused pending an independent review. Since the announcement, the EPAS Program has been refocused on delivering functional and reporting improvements requested by clinicians as well as updating the software to the latest version.

Enterprise Pathology Laboratory Information System (EPLIS)

EPLIS implementation concluded in 2017-18 and the system is operational in all major metropolitan and regional hospitals where SA Pathology laboratories are situated, including some Patient Collection Centres.

Following the implementation, concerns were raised regarding the timeliness of pathology results. SA Health established a Taskforce to respond to these concerns. The Taskforce recommended and oversaw remediation activities, including additional staffing, with the aim to return turnaround times to pre-EPLIS levels. It also confirmed the need to undertake further system, process and workflow optimisation activities. DHW advised us that these activities are underway.

Further commentary on the EPLIS project, its budget and costs are included in the section of this Report titled 'Central Adelaide Local Health Network Incorporated'.

Legacy systems

SA Health continues to operate a number of legacy systems including patient administration and revenue systems. These legacy systems present a number of support and security challenges.

Governance arrangements (existing throughout 2017-18)

Under 'Future governance and accountability changes' above we discussed the SA Government's intention to amend governance arrangements across SA Health from 1 July 2019. This section of the Report provides commentary on the arrangements that existed throughout 2017-18 and that we anticipate will continue through 2018-19.

Health care legislation

The HC Act provides the legislative framework for the operation of the South Australian health sector. Provisions in the HC Act cover hospitals and other health services administration and consultative councils; systems to support the provision of high quality health outcomes; licensing systems for ambulance services and private hospitals; providing laboratory services and facilities associated with veterinary science; and other purposes.

Minister for Health and the Chief Executive have specific functions and responsibilities

The Minister for Health and the Chief Executive have specific functions in connection with the operation of the HC Act.

The Minister's functions include to:

- ascertain the community's health and health services requirements and how to meet those requirements to the best advantage of the community
- plan, implement or support a system of health services that is comprehensive, coordinated and readily accessible to the public
- establish health services within the community
- ensure that hospitals established under the HC Act, or hospitals or other health services established, maintained or operated by or with the assistance of the SA Government, are operated in an efficient and economical manner
- ensure resources are properly allocated to health services established under the HC Act
- establish mechanisms to keep the policies and standards of health and health services developed by DHW under evaluation and review.

The Chief Executive, DHW's functions include to:

- assist the Minister in administering the HC Act and exercising the statutory powers conferred by the HC Act
- be responsible to the Minister for the overall management, administration and provision of health services within the Minister's portfolio
- assume direct responsibility for administering incorporated hospitals
- ensure that DHW has a leadership role in administering health services

- ensure appropriate standards of patient care and service delivery are adopted and applied in delivering of health services
- facilitate the efficient and economic operation of the public health system
- advise the Minister on the operation or administration of the HC Act, the provision of health services within the State, or the protection or promotion of public health within the State.

Neither the Minister or the Chief Executive, DHW can give a direction about a person's clinical treatment.

The Chief Executive, DHW may, by instrument in writing, appoint a specified person, or a person occupying a specified office or position, as the chief executive officer of an incorporated hospital. LHN and SAAS chief executive officers are subject to the control and direction of the Chief Executive, DHW.

The Department for Health and Wellbeing

DHW is an administrative unit established under the *Public Sector Act 2009*. Under section 26(b) of that Act the Department's title changed from the Department for Health and Ageing to the Department for Health and Wellbeing in May 2018.

DHW is a funder or service purchaser, policy setter and strategic planner and provider of services.

DHW is charged with a broad ranging policy and administrative responsibilities associated with health.

Local health networks

National Health Reform Agreement (NHRA)

In August 2011 the Commonwealth, State and Territory Governments entered into the NHRA. The NHRA establishes governance, funding and financial management arrangements for delivering public hospital services and other health services.

The NHRA required the States to establish LHNs to directly manage the delivery of public hospital and other health services. An LHN can contain one or more hospitals, and is usually defined as a business group, geographical area or community. Every Australian public hospital is part of an LHN. These requirements were to place responsibility and accountability for health service delivery to local health areas.

South Australian LHNs

LHNs are incorporated hospitals and bodies corporate established under the HC Act. They are responsible to the Minister for Health and the Chief Executive, DHW.

Chief executive officers at LHNs have significant accountabilities

The Chief Executive, DHW has appointed chief executive officers at the LHNs. They work to an annual service level agreement (SLA) that assigns accountability for the high level outcomes required for the term of the agreement. It also sets out the parties' respective statutory and other legal functions and obligations.

The SLAs are comprehensive agreements. Some key financial management responsibilities are:

- the LHN chief executive officers are responsible for providing safe, high quality health care services within agreed financial parameters and managing the LHN budget and performance outcomes as determined by DHW in line with the SLA
- the Chief Executive, DHW is responsible for allocating the financial resources provided by the SA Government to the health service providers and support service providers in a transparent way
- where an LHN chief executive officer considers they cannot manage within their budget constraints they must report this through the mechanism outlined in the SA Health performance framework.

LHN Health Advisory Councils have a statutory advocacy role

LHNs have Health Advisory Councils appointed under section 15(1) of the HC Act. These councils have an advocacy role, on behalf of the community, to provide advice and to perform other functions as determined under the HC Act.

LHNs operating in South Australia

In 2017-18 the following LHNs operated in South Australia:

- Central Adelaide Local Health Network Incorporated

  The principal units within CALHN were the RAH, The Queen Elizabeth Hospital, Hampstead Rehabilitation Centre, GP Plus Health Care Centres and primary, subacute and mental health services located in the local area. CALHN also includes state-wide clinical support services covering pharmacy, medical imaging and pathology.

- Southern Adelaide Local Health Network Incorporated

  The principal units within SALHN were the Flinders Medical Centre, RGH, Noarlunga Hospital, GP Plus Health Care Centres and primary, subacute and mental health services located in the local area.

- Northern Adelaide Local Health Network Incorporated

  The principal units within NALHN were the Lyell McEwin Hospital, Modbury Hospital, GP Plus Health Care Centres and primary, subacute and mental health services located in the local area.

- Country Health SA Local Health Network Incorporated

  CHSALHN provided a network of hospitals and health services located throughout regional South Australia.

- Women’s and Children’s Health Network Incorporated

  The principal unit within WCHN was the Women’s and Children’s Hospital.

SAAS has operated since 1992 as the principal provider of emergency ambulance services in South Australia.

The following table highlights total expenditure and total assets of the SA Health entities.

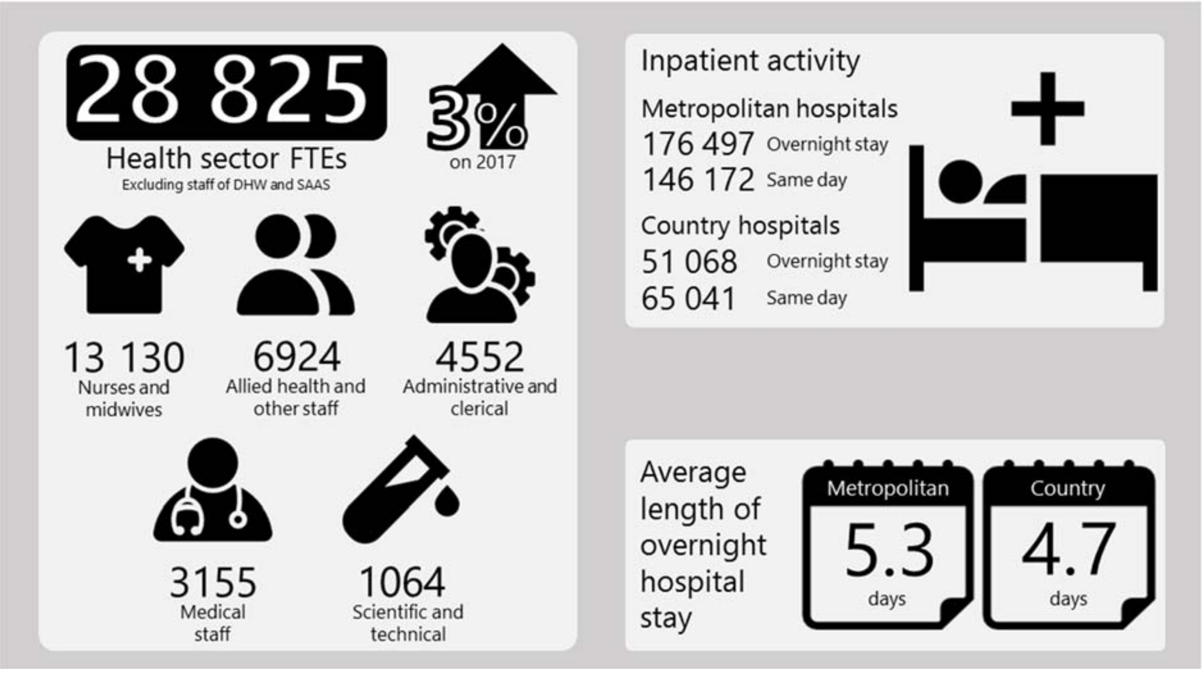
	*DHW $'million	CALHN $'million	SALHN $'million	CHSALHN $'million	NALHN $'million	WCHN $'million	SAAS $'million
Total expenses	5 774	2 717	1 070	912	685	465	315
Total assets	595	3 766	831	1 024	476	410	171

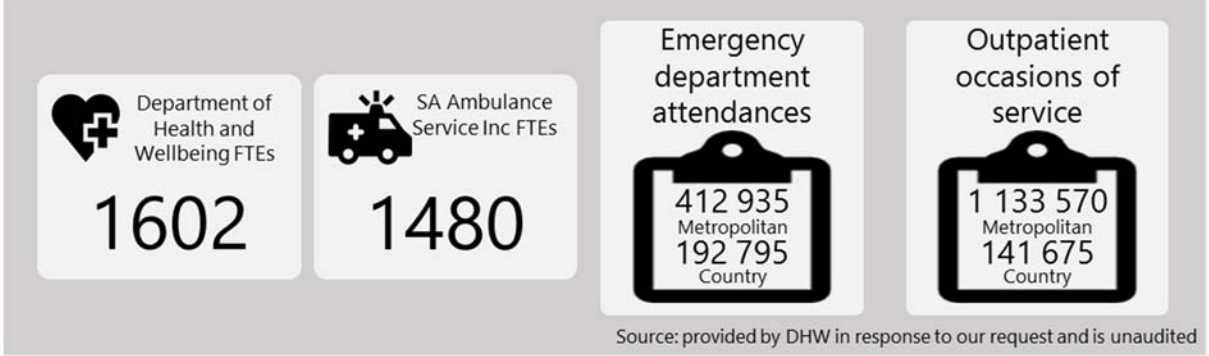
* Includes grants to incorporated hospitals of $5 billion.

Consolidated financial statements

In line with AASB 10 'Consolidated Financial Statements', DHW prepared financial statements for the consolidated entity which comprises DHW, the LHNs and SAAS.

Health sector staffing and patient activity data – unaudited





The following staffing and patient activity information was provided by DHW in response to our request and is unaudited.

Health sector staffing statistics

The following table details the staffing levels as at 30 June in the health sector, excluding staff of DHW and SAAS, for the past three years.

Health sector FTE mix (unaudited)

	2016 Number	2017 Number	2018 Number
Staff categories:			
Nurses and midwives	12 471	12 578	13 130
Medical staff	2 938	3 020	3 155
Scientific and technical	1 092	1 065	1 064
Administrative and clerical	4 168	4 491	4 552
Allied health and other staff	6 689	6 760	6 924
Total staff	27 358	27 914	28 825
Increase (Decrease)	(316)	556	911
Percentage increase (decrease)	(1.1%)	2%	3.3%

Department for Health and Wellbeing staffing statistics

The following table details the staffing levels of DHW as at 30 June for the past three years.

Department for Health and Wellbeing FTEs (unaudited)

	2016 Number	2017 Number	2018 Number
Total staff	2 036	1 702	1 602

SA Ambulance Service Inc staffing statistics

The following table details the staffing levels of SAAS as at 30 June for the past three years.

SA Ambulance Service Inc FTEs (unaudited)

	2016 Number	2017 Number	2018 Number
Total staff	1 244	1 349	1 480

Part of the increase in SA Ambulance FTEs is attributable to an increase in frontline services staff as funded through the December 2017 State Budget mid-year budget review.

Hospital activity statistics

The tables below indicate the trends over past years in inpatient activity (unweighted), length of hospital stay, and casualty and outpatient activity (unweighted).

The data in the tables was sourced from DHW's reporting systems and has not been audited. DHW advised that its processes to collate activity data for 2017-18 were not complete at the time of this Report and the figures presented are not final. Accordingly the activity statistics below are at a point in time and subject to change.

Inpatient activity (unaudited)

	2016 Number	2017 Number	2018 Number
Metropolitan hospitals:			
Overnight stay	176 845	177 959	176 497
Same day	153 975	148 101	146 172
Total	330 820	326 060	322 669
Country hospitals:			
Overnight stay	51 641	51 443	51 068
Same day	56 419	60 068	65 041
Total	108 060	111 511	116 109

Average length of overnight hospital stay (unaudited)

	2016 Days	2017 Days	2018 Days
Metropolitan hospitals	5.4	5.3	5.3
Country hospitals	5.0	4.6	4.7

Emergency Department and public outpatient activity (unaudited)

	2016 Number	2017 Number	2018 Number
Metropolitan hospitals:			
Emergency Department attendances	394 948	403 893	412 935
Outpatient occasions of service	1 058 846	1 122 092	1 133 570
Country hospitals:			
Emergency Department attendances	179 116	183 573	192 795
Outpatient occasions of service	140 094	143 215	141 675

Department for Health and Wellbeing (DHW)

Financial statistics	Total expenses:	$5774 million
	Net cost of providing services:	$3973 million
	Revenue from SA Government:	$3986 million
	Employee benefits liability and related on-costs:	$61 million
	Workers compensation liability:	$1 million
	Number of FTEs:	1602

Significant events and transactions

- The *Health Care (Governance) Amendment Act 2018* was proclaimed in August 2018 and will operate from 1 July 2019. It changes governance arrangements including the Chief Executive, DHW's responsibilities and establishes that LHNs will be governed by a board.
- The Department's name changed from the Department for Health and Ageing to the Department for Health and Wellbeing.
- The consolidated net cost of providing services was a $379 million deterioration from the original budget.
- A new Chief Executive commenced in May 2018.

Financial report opinion

Unmodified

Financial controls opinion

Modified

Key issues:

- A large proportion of SA Health supplies and services expenditure is not subject to formal contractual arrangements
- Contract management processes require improvement
- Probity advisor not required to formally report
- Processes not adequate to ensure consistent and appropriate management of medical officers' professional development leave and reimbursements
- Employee payroll and leave management information was not reviewed appropriately
- Expenditure system approval profiles were not regularly reviewed
- Legal compliance framework not fully implemented

Functional responsibility

DHW is an administrative unit established under the *Public Sector Act 2009.* Under section 26(b) of that Act, its name changed from the Department for Health and Ageing to the Department for Health and Wellbeing in May 2018.

DHW is a funder or purchaser of health services, policy setter and strategic planner and provider of services. Note 2 of DHW's financial report provides details about its objectives.

DHW is charged with broad ranging policy and administrative responsibilities associated with the provision of health care in South Australia. The *Health Care Act 2008* (HC Act) makes the Chief Executive, DHW responsible for ensuring the proper allocation and use of resources between health regions and health services incorporated under the HC Act*.*

In line with AASB 10 'Consolidated Financial Statements', consolidated financial statements have been prepared comprising DHW, the local health networks (LHNs) and SA Ambulance Service Inc (SAAS).

Collectively DHW, the LHNs and SAAS are known as SA Health or the Health sector.

Governance changes

The SA Government has announced its intentions to amend governance arrangements across SA Health. The first part of these changes was completed in August 2018 when the *Health Care (Governance) Amendment Act 2018,* which will operate from 1 July 2019, was proclaimed.

The amendments change the role of the Chief Executive, DHW to remove direct responsibility for the administration of incorporated hospitals and provide for LHNs to be governed by a board from 1 July 2019. The Chief Executive, DHW will remain responsible for the overall management, administration and provision of health services within the Minister's portfolio to ensure that DHW undertakes a leadership role in the administration of health services.

The SA Government has stated it will establish a new governance and accountability framework for the public health system which will be reflected in further changes to legislation to be introduced into Parliament later in 2018 or early next year.

Scope of the audit

The audit program covered major financial systems to obtain sufficient evidence to form an opinion on the financial report and internal controls.

Financial services are provided through a mix of:

- central services provided by DHW for LHNs and SAAS
- services provided by Shared Services SA (SSSA).

Specific areas of audit attention in 2017-18 included:

- payroll

- accounts payable
- procurement
- contract management
- cash
- general ledger
- funding to health services
- funding to non-government organisations
- interstate transfers
- non-current assets
- inventory management
- revenues from the Commonwealth
- insurance services
- IT systems controls
- professional development entitlements.

Internal audit activities were considered in designing and conducting audit procedures.

Audit findings and comments

Assessment of controls

In my opinion, the controls exercised by the Department for Health and Wellbeing in relation to the receipt, expenditure and investment of money, the acquisition and disposal of property and the incurring of liabilities, except for all matters outlined under 'Communication of audit matters', are sufficient to provide reasonable assurance that the financial transactions of the Department for Health and Wellbeing have been conducted properly and in accordance with law.

Communication of audit matters

Matters identified by the audit were detailed in management letters to the Chief Executive, DHW. The main matters raised and related responses are detailed below.

Procurement and contract management

The following section contains our findings and comments about a number of DHW procurement and contract management areas. Similar issues were raised with DHW in previous years.

A large proportion of SA Health goods and services expenditure is not subject to contractual arrangements

DHW's analysis of SA Health's 2016-17 expenditure found it spent approximately $209 million p.a. on goods and services that were not governed by documented contractual arrangements. High levels of uncontracted spend may cause lost opportunities for savings. It may also reduce the effectiveness of procurement and supply chain management including SA Health's ability to ensure accountability and transparency in procurement operations. We recommended DHW continue to work towards increasing the proportion of expenditure subject to documented contractual arrangements.

In response DHW advised its procurement activities had increased the total expenditure under formal contract from 64% in June 2016 to 78% in June 2017. It also indicated pending procurement projects will result in 81% of expenditure being under formal contractual arrangements by 31 January 2019.

Procurement of centralised contracts for hotel services

In 2017-18 DHW established centralised contracts for hotel services. Hotel services cover various non-clinical support services including help desk, cleaning, distribution and patient services, catering/food, ward/department support services and grounds and garden maintenance.

Prior to the new contractual arrangements, hotel services at major metropolitan hospitals were provided through a mixture of fully outsourced, partially outsourced and fully insourced operations. These services were largely through independent contracts between individual hospital sites and the supplier.

The procurement resulted in contracts with two major service providers across certain metropolitan hospital sites. The SA Government approved the financial authorisation to enter into the contracts on 7 May 2018. The contracts are for three years with the option to extend for further three-year and two-year periods. The anticipated total cost of the procurement including the extensions was $486 million, with projected savings of $20 million over the eight-year term.

We reviewed the procurement documentation against the mandated requirements of the State Procurement Board and found that DHW complied with most requirements. We found the following areas that needed improvement.

Improvements needed in risk management planning

Our review of the acquisition documents found that the risk management plan developed for the hotel services procurement did not document:

- the allocation of risk management responsibilities
- how risks will be monitored and managed on an ongoing basis
- an outline of how risks were identified and analysed.

Where risk management and monitoring responsibilities are not documented there is reduced accountability and mitigation strategies may not be applied consistently and as intended.

We recommended these elements be addressed in risk management plans developed for future procurements. DHW responded with its intended actions to ensure the areas identified are included in any future risk management plans.

No formal reporting from the probity advisor

The appointed probity advisor did not provide a report communicating his findings. We found the probity plan intended that the advisor would report prior to the purchase recommendation, however the requirement was not included in the contractual arrangement with the advisor. Where a probity advisor does not provide a report, there is an increased risk any actions required to meet probity standards will not be identified before the key elements of the procurement process are progressed. We raised a similar issue last year.

DHW advised it had subsequently obtained a probity report for the hotel services procurement which would be provided to the Executive Director Procurement and Supply Chain Management by October 2018. It also indicated it had reiterated with its staff the need to ensure contracts with probity advisors include a requirement to report.

Inventory procurement and management

Uncontracted purchase of inventory supplies

DHW annually spends around $100 million on medical, surgical and laboratory inventory through its distribution centre and bulk stores. Last year we reported a significant portion of inventory purchases was not subject to any formal contractual arrangements. Our review in 2017-18 found improvement, with a higher proportion of purchases for the period July 2017 to February 2018 under formal contracts. This improvement is partly attributable to some large procurement processes, including new orthopaedics and cardiovascular prosthesis contracts.

While acknowledging this progress, we found there is room for further improvement. We reviewed catalogue items with an expected annual spend of more than $250 000 and found only 44% were subject to a current formal contract. High levels of uncontracted spend may cause lost opportunities for savings and may impact SA Health's ability to ensure accountability and transparency in procurement processes.

We recommended DHW continue to work towards increasing the proportion of inventory expenditure subject to formal contractual arrangements. We also recommended DHW establish thresholds that require particular procurement approaches and contractual arrangements when estimated annual expenditure reaches certain dollar limits.

DHW responded that of approximately 150 000 individual product items in its catalogue, 125 000 or 83% were supported by formal contracts. The response provided information regarding its current and planned strategic medical and surgical consumables procurement projects which aim to increase the portion of its spend that is contracted. DHW indicated it determines its procurement approaches on a case-by-case basis.

Potential for incorrect prices on purchase orders

The order price of common (catalogue) medical, surgical and laboratory supplies is based on price records in the Oracle inventory management system. A separate system, the Catalogue Management System, is used to maintain prices and supplier details. We found that reconciliations between the two systems only occur on an ad hoc basis and are not performed regularly. This increases the risk that items are ordered outside the contracted or otherwise managed price.

DHW responded that it was working to develop a report to enable regular reconciliation between Oracle and the Catalogue Management System. It indicated in the interim it would continue to rely on ad hoc manual reconciliations.

Our stock counts found variances between system records and physical stock

Our sample stock counts at the Flinders Medical Centre's bulk store found variances between system records and physical stock. While staff provided potential reasons for the variances, they were generalisations and not specific to the particular discrepancies. We recommended DHW investigate

processes and systems at the Flinders Medical Centre's bulk store to ensure the existence, completeness and accuracy of the inventory records.

DHW responded that it was reviewing processes at that site to isolate the cause of the count discrepancies.

Inventory adjustments made without adequate investigation

Our review of inventory management at DHW considered whether all adjustments to inventory records were investigated appropriately, to ensure the inventory balances are accurate. Our testing of adjustments found that in most cases, documentation was not sufficient to show that inventory officers had investigated the cause of the variance. We recommended DHW ensure the causes of inventory discrepancies are investigated and documented, prior to approval of system adjustments, to help prevent errors or misappropriation of stock.

DHW indicated it had developed a checklist for documenting the investigation of discrepancies of more than $300.

Orthopaedics and cardiovascular prosthesis and associated consumables – contract management

In 2016-17 DHW implemented State-wide contracts for orthopaedics and cardiovascular prosthesis and associated consumables. The panel contracts with numerous suppliers cover over 120 000 separate items. The contracts are for three years with the option to extend for a further two, two-year periods. The anticipated total costs for the contracts, including the extension options, is $568 million (including GST).

In 2017-18 we reviewed DHW's management of these contracts. Expenditure on them in 2017-18 exceeded $57.5 million. Our review identified the following areas that needed improvement.

Systems data not sufficient to manage contract prices and savings

The price paid for goods under the contracts is dependent on the suppliers' market share. Generally, the larger the market share, the lower the price. These arrangements were put in place to decrease the number of suppliers through standardisation of medical practices to achieve greater saving over the life of the contracts.

Our review found expenditure system reports provided unreliable figures and resulted in many discrepancies from supplier provided information. Consequently, the contract manager was reliant on client purchase records in determining and managing market share and its impact on price. We recommended DHW review its expenditure system Oracle and associated reporting to develop reliable data that can be used to confirm market share and pricing and track contract benefits.

DHW responded that its Oracle data was immature in the first half of 2017-18 due to large non-catalogue orders by LHNs. It indicated that from January 2018, Oracle spend data was used to confirm supplier records. It also responded that it would develop quarterly variance reports by January 2019 and its SA Health Digitisation Project aims to electronically manage market share in Oracle by December 2020.

Market share arrangements

We noted a number of instances where market share volume was consistently outside the market share arrangements. The arrangements and prices had not changed for these instances. Where volume is lower than market share agreements suppliers can request price increases. Where volume is higher than the market share agreements DHW can enforce lower prices. Our analysis found that purchases volumes outside the market share arrangements can have significant impact on the cost of prostheses and associated consumables.

DHW responded that suppliers may request a modified price where SA Health fails to maintain market share in any two consecutive quarters. It indicated that it manages this risk through negotiation with the supplier who had opted to maintain the existing market share price banding. It also indicated it would report the opportunity cost of not achieving market share expectations to LHN chief executive officers.

Management of day to day contract performance needs improvement

The contract management plans acknowledge the important role hospital staff play in assisting the contract manager to monitor performance. We found hospital staff involved in the day-to-day management:

- did not have a clear understanding of their role in monitoring performance. We noted their responsibilities were not included in the contract management plan
- had little or no communication with contract managers.

We recommended DHW amend its contract management plan to document the role and responsibilities of all relevant hospital staff and to describe how the contract manager should obtain information required to determine key performance indicators. DHW responded that it would expand its contract management plan in line with our recommendations.

Arrangements for consignment stock not agreed

We found hospitals did not have consignment lists, consignment agreements or other documentation outlining the processes for reconciling, ordering and restocking consignment stock. Agreed and managed levels of consignment stock are important to prevent shortages of items of clinical importance.

DHW responded it would review its contract management plans to ensure responsibilities for consignment stock are clearly outlined. It also indicated it would advise all parties of their responsibilities and centrally monitor these activities.

Contracted items on the Oracle purchasing catalogue

Our audit noted instances where requisitioning staff did not have access to, or had trouble locating, items on the Oracle purchasing catalogue. Where contracted items are not on the catalogue, or not easily found on the catalogue, they will be ordered as a non-catalogue purchase. There is a higher risk that non-catalogue purchases are made with uncontracted suppliers or outside of the contracted price.

DHW responded that it would review its orthopaedic and cardiovascular prosthesis and associated consumables catalogue in Oracle for potential missing products to ensure the catalogue is complete.

Savings achieved as a result of the contract not adequately assessed

At the time of our review in May 2018, SA Health had not undertaken sufficient analysis to understand the level of saving actually achieved since the contract commenced. DHW responded that the contract manager had developed a savings tracker to monitor savings. It also indicated that by the end of January 2019 it would develop two quarterly reports on savings that:

- compare total spend against budget and projected savings
- measure savings based on actual product expenditure (volume based) by comparing pre-contract price to current contracted price.

Contract management

SA Health's records show it spends more than $1.1 billion on contracted supplies and services each year.

In addition to our focused review of DHW's management of its orthopaedics and cardiovascular prosthesis and associated consumables, we also considered SA Health's compliance with the State Procurement Board's contract management policy including frameworks and policies.

We found there is scope for DHW to improve its contract management processes. The key findings are summarised below.

Contract manager's role in certifying payments

The State Procurement Board's contract management policy lists the key roles of a contract manager, including certifying payments to the supplier for work done (where applicable). We found, when describing the role of the contract manager, SA Health's contract management framework does not address the manager's role in certifying payments. We consider that where certification of payments is done in isolation of the contract management processes, there is an increased risk of payments for goods or services that were not received or where other terms were not met.

DHW responded that it would update its contract management framework to provide a more detailed description of the role of the contract manager in certifying the payment of goods and services.

Information on the contract register not reliable or complete

We identified instances where information in the Procurement and Contract Management System was unreliable. This could prevent management from monitoring contract end dates and identifying when to commence new procurement activities. We also noted instances where current contracts were not on the system.

DHW responded that it would design and implement a new reporting process targeted to identifying, reviewing and rectifying inaccuracies.

Supply arrangements continued beyond contractual term

Our review of contract management considered the extent to which supply arrangements continued beyond the expiry of contracts. Our testing found that for 15% of our sample of contracts, the arrangements continued beyond their contracted terms. Any period without a formal, documented

contract potentially impacts DHW's ability to manage contractual obligations and conditions including price. We recommended DHW identify and respond to instances where supplier arrangements continue beyond the end of the contracted term.

DHW responded that it will report six monthly on contracts due to expire within two years, indicating the report would be used to determine appropriate actions including whether to approach the market in a procurement process or extend or terminate contracts.

Waiving competitive procurement processes in favour of direct negotiation

Our review of procurement processes included testing of a sample of contracts established through a direct negotiation approach; that is, they did not involve competitive procurement. We found:

- one instance where the requirement for competitive procurement processes was waived in favour of direct negotiation solely due to time constraints
- one instance where the contract was extended multiple times outside of the contracted terms due to delays in procurement processes for the new tender.

Waiving competitive processes to address timing concerns may compromise DHW's ability to obtain value for money. We consider that in only exceptionally urgent circumstances should time constraints be used as the sole reason for waiving competitive process.

DHW responded that it will communicate to the LHNs and departmental business units the importance of appropriately justifying direct negotiations and that time constraints are to be used in exceptional circumstances only.

Accounts payable

Accounts payable services are provided to DHW, the LHNs and SAAS by SSSA under service level determinations.

System-based expenditure approval profiles not regularly reviewed

Our review of the Basware payment processing system found financial delegations assigned to users within the system were not regularly compared to financial delegations. Consequently, management may not detect employees with Basware approval powers that exceed the authority provided to them by the financial delegations, resulting in the potential for invalid or unauthorised payments. This issue has been raised for several years.

DHW responded with its actions to address the recommendations including escalating non-performance to management.

Concerns over vendor master data quality

In recent years we reported that our testing of accounts payable data found multiple instances of invalid, incomplete and/or duplicate vendor information in the vendor masterfile, highlighting the need to improve vendor management controls.

Our testing of accounts payable data in 2017-18 found similar concerns.

Where vendor details in the system are incomplete or inaccurate there is an increased risk that the vendor might not be a valid supplier, potentially allowing invalid or duplicate payment transactions to occur.

In its response DHW indicated it was undertaking a data cleansing exercise to address the quality of vendor data.

Governance and accountability

Legal compliance framework not in place

Last year we reported that while DHW had developed and approved a legislative compliance policy directive and guidelines, it was not implemented across SA Health. Our follow-up found that DHW made progress towards implementing its legislative compliance framework across SA Health in 2017-18. At the time of our audit, legislative compliance registers were being developed but were not finalised at all LHNs.

We recommended DHW implement the framework across SA Health, including developing compliance registers and certification processes. DHW responded that business units are required to complete their legislative compliance certification by 1 September each year. It also indicated that it is likely the legislative compliance framework will be reviewed in the context of the SA Government's changes to governance arrangements, including establishing governing boards.

Medical officer professional development (PD)

SA Health's enterprise agreements establish medical officers' PD entitlements. They include paid leave and reimbursement of expenses incurred in obtaining PD. Entitlements vary under each enterprise arrangement. For example, certain medical officers are entitled to:

- up to 20 days PD leave over any two-year period
- a cumulative reimbursement, for eligible PD expenditure over any two-year period, up to a maximum of $44 000.

Since 2015-16 we have reported concerns about SA Health's management of PD entitlements.

In 2017-18 we followed up DHW's actions to address the matters raised. We found DHW had not addressed the concerns raised and could improve its management of PD in the following areas.

Inadequate central direction to LHNs for consistent and adequate management of medical officers' PD entitlements

Since 2015-16 we have recommended that DHW establish an SA Health-wide central policy framework that provides direction to LHNs for consistent and adequate PD control processes. Our follow-up found DHW had not developed this central framework.

DHW responded it was seeking to develop a new policy guideline for approving PD claims for LHNs, SAAS and State-wide Clinical Support Services to use and which will support an intended database to record PD reimbursement.

No central record of employees PD leave entitlements

Since 2015-16 we have reported that SA Health did not maintain a record of employee PD leave entitlements on the payroll system or in any other centralised record.

Our 2017-18 review of PD leave entitlement records at LHNs indicated PD leave entitlement records and monitoring was inadequate and resulted in medical officers taking leave in excess of their entitlements.

DHW responded that it had investigated adding a leave code to the payroll system to record PD leave but indicated that further work was necessary with a target completion date of 31 March 2019.

Payroll

Employee benefit expenses are a significant cost, totalling $189 million for DHW and $3.9 billion across the consolidated entity in 2017-18.

Payroll services are provided through a combination of:

- central payroll services provided by DHW for SA Health
- central payroll services provided by SSSA for SA Health
- payroll activities located in each LHN.

A summary of our findings for payroll activities in LHNs can be found under 'Communication of audit matters' in the sections of this Report for each LHN.

Findings relating to the central and DHW specific payroll services provided by DHW are reported below.

Payroll (relating to DHW and LHNs)

Delays in approval of employment contracts

Our review considered how quickly the payroll system is updated to reflect employee contract alterations. We found that for the period 1 July 2017 to 30 November 2017, across SA Health 39.9% of alterations to contracts were approved after the date the change was to take effect. This may result in incorrect payments and the potential for back pay. We recommended DHW ensure all contracts, including alterations to existing contracts, are approved and updated to the payroll system prior to the date that the contract takes effect.

DHW responded it was reviewing its processes and is monitoring the preparation of contracts to ensure they are finalised prior to the effective date.

Insufficient review of payroll information

Many SA Health employees are paid standard hours without direct reference to actual time records. In this environment it is important to ensure regular management review of individual employee payments and leave records. In recent years we have reported deficiencies in management's review of bona fide and leave reports.

In November 2017, a new bona fide and leave reporting process was introduced where managers/team leaders log on to the payroll system and review a report to confirm the bona fide nature of employee payments and leave taken. We reviewed five pay runs in the two months after the implementation of the new process. We found managers had not reviewed 74% of bona fide certificates and leave taken reports across SA Health. In one run, 85% of bona fide and leave taken reports were not reviewed, equating to approximately $29 million in salary and wages without the required review.

DHW responded that it had identified anomalies in its reports and was working with SSSA to address the problem. It also responded that it was reviewing its procedures with the intention of providing managers/team leaders a longer time to review and approve the reports.

Delegations and authorisations not reviewed as intended

Over recent years we have reported that DHW's instrument of HR delegations and authorisations had not been updated and approved since November 2012. DHW had advised its intention to finalise delegations in November 2017. Our follow-up review in December 2017 found this did not occur as expected.

DHW responded that it had developed draft HR delegations and had anticipated they would be approved in March 2018. At the time of this Report the delegations were not yet endorsed.

Payroll (relating to DHW only)

CHRIS access profiles not regularly reviewed

Our review found that CHRIS payroll system user assess was not reviewed quarterly by an appropriate delegate in line with SSSA's user access policy guideline. This issue was raised over the last two years.

Failure to detect inappropriate user access permissions may allow processing of unauthorised transactions, potentially resulting in financial loss. We recommended DHW review quarterly CHRIS user access profiles to ensure user access is limited to the functionality required to meet an individual's responsibilities and to ensure incompatible duties are segregated.

DHW responded that it had developed a series of reports to distribute every three months for review.

IT general controls review

In 2017-18 we conducted an IT general controls review of SA Health's Oracle Corporate System and Enterprise Patient Administration System (EPAS). The key controls tested for both environments related to password management, user access, patch management, change management, backup and disaster recovery management.

We found that SA Health's controls over patch and backup management for these ICT system environments were generally satisfactory.

Oracle Corporate System

Our assessment identified the following findings:

- conflicts in the segregation of duties of business roles and responsibilities

- database server privileged user access is not regularly reviewed
- privileged account management of the database could be strengthened
- instances exist of users with unnecessary access to sensitive business functions
- user access responsibilities need to be reassessed
- active privileged user access was assigned to terminated employees
- network password configuration settings were weak.

SA Health responded positively to these findings with details of proposed remediation action expected to be completed by January 2019.

EPAS

Our assessment identified the following findings:

- password configuration settings were weak
- inappropriately assigned privileged user access
- weakness in user on-boarding and off-boarding processes
- change management process weaknesses.

SA Health responded positively to these findings with details of remediation action expected to be complete by December 2019.

Shared Services SA – financial systems and transactions processing environments

SSSA processes financial transactions on behalf of DHW. The main systems and control environments include accounts payable and payroll financial functions.

Our review and evaluation of controls for these systems conclude that the controls were effective for 2017-18. SSSA is discussed further in the commentary under 'Department of the Premier and Cabinet' in this Report.

Interpretation and analysis of the financial report

Highlights of the financial report – Department for Health and Wellbeing (parent)

	2018 $'million	2017 $'million
Expenses		
Employee benefit expenses	189	190
Supplies, services and other expenses	557	535
Grants, subsidies and client payments	5 028	4 403
Total expenses	5 774	5 128
Income		
Fees and charges	344	360
Grants and contributions	1 428	1 350
Other	29	31
Total income	1 801	1 741
Net cost of providing services	3 973	3 387

	2018 $'million	2017 $'million
Revenues from SA Government	3 986	3 401
Net result	13	14
Other comprehensive income	(2)	-
Total comprehensive result	11	14
Net cash provided by (used in) operating activities	8	25
Assets		
Current assets	483	480
Non-current assets	112	132
Total assets	595	612
Liabilities		
Current liabilities	171	212
Non-current liabilities	161	147
Total liabilities	332	359
Total equity	263	253

Statement of Comprehensive Income – Department for Health and Wellbeing (parent)

Expenses

Employee benefit expenses

Employee benefit expenses decreased by $1 million to $189 million. During the year 60 employees transferred from DHW's People and Culture division to LHNs, SAAS and the Department of the Premier and Cabinet.

The number of employees whose remuneration received/receivable exceeded base executive level ($149 000) totalled 77 (79), comprising 36 (37) executive, 25 (31) non-medical and 16 (11) medical, nursing and operational employees. Total remuneration for these employees was $18 million ($18 million).

Supplies and services expenses

Supplies and services expenses amounted to $514 million ($479 million). Significant components of supplies and services were:

- contract of services – $105 million ($100 million)
- cost of goods sold to incorporated health services – $101 million ($96 million)
- computing costs – $97 million ($75 million). Contributing to the increase was the cost of outsourced end user computer and related services previously provided internally and additional costs relating to networks at the new Royal Adelaide Hospital (RAH)
- insurance – $53 million ($28 million). The increase is due mainly to an increase in the medical malpractice provision for new claims of $5.4 million and revision of the actuarial assessment of future claims estimate of $18.8 million

- interstate patient transfers – $37 million ($45 million). The decrease mainly reflects large interstate patients' expenditure accruals in 2016-17 which included the impact of revised estimates for prior years
- repairs and maintenance – $21 million ($20 million)
- consultants – $4 million ($14 million). The decrease is mainly due to reduced costs for consultants engaged for the Transforming Health program.

Revenues

Income

Income for 2017-18 amounted to $1.8 billion ($1.7 billion) and principally comprised Commonwealth Government National Health Reform Agreement funding of $1.335 billion ($1.253 billion). DHW receives Commonwealth Government grants paid from the State Pool account in line with the revised funding agreement under the National Health Reform Agreement rather than from the Department of Treasury and Finance through SA Government appropriation.

Revenues from the SA Government

Included with revenues from the SA Government was appropriation of $3967 million, including contingency funds from the Department of Treasury and Finance of $105 million and targeted voluntary separation package (TVSP) recoveries of $10 million. These appropriations were approved as follows:

- $3749 million original appropriation – *Appropriation Act 2017*, 2017-18 State Budget
- $132 million provided through the December 2017 mid-year budget review to support the transition to the new RAH and to meet ongoing growth in the health system
- $17 million approved budget variations including TVSP recoveries of $10 million and various other items
- $70 million provided at the end of the year and announced in the 2018-19 State Budget to ensure the health system continued to provide the necessary services required by the community.

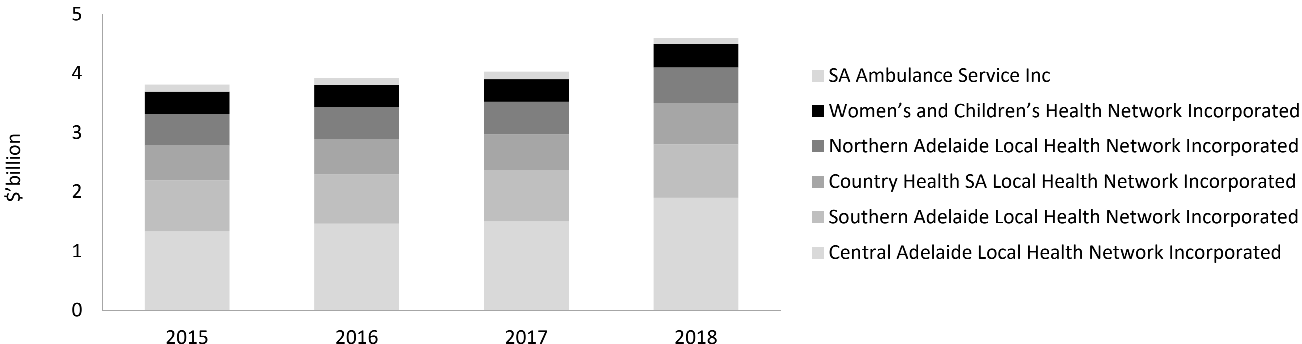
Revenues from the SA Government increased by $586 million to $4 billion (17%). Significant to this increase was funding to meet:

- increased finance lease borrowing costs of $249 million which relate to interest on the public private partnership agreement for the new RAH
- increased public private partnership contractual delivery of operations services of $60 million (security, cleaning, maintenance, food supplies) at the new RAH.

Recurrent funding to incorporated health services

Recurrent funding to incorporated health services increased by $676 million to $4.7 billion (16.8%). Recurrent funding is provided to health services to meet their cost of services. The Central Adelaide Local Health Network Incorporated (CALHN) received an increase of $449 million in 2017-18. Commentary on the cost of services of LHNs is included in the sections of this Report for each LHN.

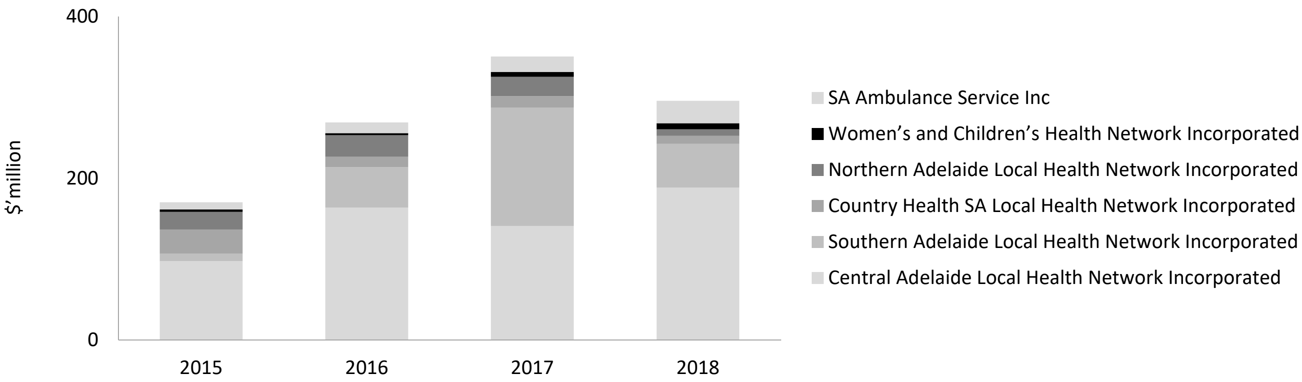
The following chart shows a significant increase in total recurrent funding to incorporated health services in 2017-18, particularly at CALHN.



Total recurrent funding has increased over the four years, from $3.8 billion in 2015 to $4.7 billion in 2018 (refer note 5.1 of DHW's financial report). The three largest increases were at Central Adelaide Local Health Network Incorporated, $449 million (30%), Northern Adelaide Local Health Network Incorporated, $72 million (13%), and Southern Adelaide Local Health Network Incorporated, $74 million (9%).

Capital funding to incorporated health services

The following chart shows capital funding to incorporated health services for the four years to 2018.



In 2018 total capital funding decreased by $55 million to $296 million. The decrease in capital funding was due mainly to Flinders Medical Centre and Noarlunga Health Services redevelopment projects nearing completion (refer note 5.1 of DHW's financial report).

Statement of Financial Position – Department for Health and Wellbeing (parent)

Assets

Current assets increased by $3 million to $483 million as at 30 June 2018 and included cash and cash equivalents of $293 million.

Liabilities

DHW's total liabilities were $332 million at 30 June 2018, a decrease of $27 million from the previous year. Significant components of liabilities were:

- payables, $147 million ($181 million) – the decrease is mainly related to a reduction in accruals relating to major capital projects

- provision for insurance, $119 million ($105 million) – the increase is due mainly to the revision of the actuarial assessment of future claims estimate
- employee benefits liabilities and related on-costs, $61 million ($63 million).

The provision for insurance estimates DHW's liability for professional indemnity (including medical malpractice) and general public liability. The determination of the insurance provision was carried out through an actuarial assessment in line with AASB 1023 'General Insurance Contracts' and takes into account prudential margins, inflation, taxes, claims incurred but not reported and current claim values (refer note 27.2 of DHW's financial report).

Equity

As at 30 June 2018, DHW had a net assets position of $263 million ($252 million). DHW did not receive any equity contribution from the SA Government in 2017-18 ($57 million in 2016-17).

Highlights of the financial report – consolidated entity

The consolidated entity comprises:

- Department for Health and Wellbeing
- Central Adelaide Local Health Network Incorporated
- Country Health SA Local Health Network Incorporated
- Northern Adelaide Local Health Network Incorporated
- SA Ambulance Service Inc
- Southern Adelaide Local Health Network Incorporated
- Women's and Children's Health Network Incorporated.

	2018 $'million	2017 $'million
Expenses		
Employee benefit expenses	3 916	3 643
Supplies, services and other expenses	2 023	1 863
Borrowing costs	263	15
Depreciation and amortisation	256	174
Grants and subsidies	43	39
Total expenses	6 501	5 734
Income		
Fees and charges	589	592
Grants and contributions	1 769	1 709
Other	121	104
Total income	2 479	2 405
Net cost of providing services	4 022	3 329
Revenues from SA Government	3 986	3 401
Net result	(36)	72
Other comprehensive income		
Changes in property plant and equipment asset revaluation surplus	349	(6)
Gains or losses recognised directly in equity	2	40
Total other comprehensive income	351	34
Total comprehensive result	315	106

	2018 $'million	2017 $'million
Net cash provided by (used in) operating activities	388	282
Net cash provided by (used in) investing activities	(232)	(292)
Assets		
Current assets	1 047	946
Non-current assets	6 193	5 896
Total assets	7 240	6 842
Liabilities		
Current liabilities	1 055	997
Non-current liabilities	3 607	3 582
Total liabilities	4 662	4 579
Total equity	2 578	2 262

Statement of Comprehensive Income – consolidated entity

Expenses

Total expenses increased by $767 million to $6.5 billion (13%) and principally comprised employee benefit expenses of $3.9 billion and supplies and services expenses of $1.9 billion.

Employee benefit expenses

Employee benefits expense increased by $272 million to $3.9 billion. Contributing to this increase were:

- a $170 million increase in salaries and wages and superannuation to $3.4 billion (5.2%). Contributing to this was a 3% rise in FTEs to 31 907 and salaries and wages rises associated with various enterprise agreements
- a $53 million increase in long service leave expense
- a $25 million increase in workers compensation expense. Contributing to this increase was a $15 million expense to bring to account for the first time the new non-statutory provisions for certain work related injuries as part of enterprise bargaining arrangements and industrial awards introduced in 2017-18.

The number of employees whose remuneration received/receivable exceeded base executive level ($149 000) totalled 3232 (3222), comprising 104 (107) executive, 136 (136) non-medical and 2992 (2979) medical, nursing and operational employees.

Total remuneration for these employees was $861 million ($836 million).

The following table summarises the remuneration of employees for 2017-18 included in note 3 of DHW's financial report.

	Executive Number	Non-medical Number	Medical Number	Nursing Number	Operational Number	Total Number
$147 001 - $209 000	57	122	933	202	327	1 641
$209 001 - $309 000	37	13	542	-	44	636
$309 001 - $409 000	6	-	425	-	4	435
$409 001 - $509 000	1	-	303	-	-	304
$509 001 - $609 000	2	-	148	-	-	150
$609 001 - $709 000	-	1	54	-	-	55
$709 001 - $809 000	-	-	8	-	-	8
$809 001 - $909 000	1	-	2	-	-	3
Total	104	136	2 415	202	375	3 232

Supplies and services expenses

Supplies and services increased by $179 million to $1.9 billion. Significant components of supplies and services were:

- medical, surgical and laboratory supplies – $309 million ($298 million)
- drug supplies – $226 million ($250 million)
- contract of services – $132 million ($124 million)
- fee-for-service – $169 million ($137 million)
- contractors – agency staff – $99 million ($69 million)
- public private partnership operating expenses – $62 million ($2 million)
- electricity, gas and fuel – $54 million ($35 million)
- insurance – $55 million ($31 million)
- computing – $109 million ($82 million)
- housekeeping – $83 million ($92 million).

Income

Income for 2017-18 amounted to $2.5 billion ($2.4 billion) and principally comprised Commonwealth Government National Health Reform Agreement grants of $1.3 billion ($1.3 billion) and revenue from fees and charges of $589 million ($592 million).

DHW receives Commonwealth Government grants paid from the State Pool account in line with the revised funding agreement under the National Health Reform Agreement rather than from the Department of Treasury and Finance through SA Government appropriation.

Comparison of actual expenses to original budget

For 2017-18, the net cost of providing health services exceeded the original budget by $379 million. Note 35 of DHW's financial report provides budgetary reporting information, including some explanations of major variances between DHW's original budget provided to Parliament and actuals reported in the financial statements.

In summary, the key items reported (all exceeding budget) are:

	Variance $'million
Total expenses	438
Total income	59
Net cost of providing services	379
Revenues from SA Government	225
Net result	154

Note 35 states that the unfavourable variance of $438 million in total expenses compared with the original budget is mainly due to the increased cost of providing hospital services. Most of these costs are incurred across a large range of areas and are not separately disclosed in this note because of the number and breadth of areas involved. Some specific items that have contributed to the variance are described. The three largest items are:

- increased operational expenses predominantly due to the readiness, transition and site works associated with the new RAH of $44.2 million
- increased drug costs in administering a new Hepatitis C medication under the Pharmaceutical Benefits Scheme of $27.6 million
- increased costs associated with enterprise agreements finalised throughout 2017-18 of $27.9 million.

The main elements of budget variances were:

	Over (Under) budget $'million
Expenses:	
Employee benefit expenses	191
Supplies and services	236
Income:	
Revenues from fees and charges	(36)
Grants and contributions	67

Statement of Financial Position – consolidated entity

As at 30 June 2018, the consolidated entity had a net assets position of $2.6 billion.

Liabilities

Employment liabilities make up $1.3 billion of the consolidated entity's total liabilities at 30 June 2018, comprising:

- employee benefits liabilities and related on-costs, $1.3 billion ($1.2 billion)

- provision for workers compensation, $109 million ($88 million). The worker compensation provision was estimated by an independent actuary as at 30 June 2018. The provisions include non-statutory provisions for certain work related injuries as part of enterprise bargaining

- arrangements and industrial awards introduced in 2017-18. As at 30 June 2018 the consolidated entity recognised a workers compensation non-statutory provision of $15 million for the first time. There is a high degree of uncertainty about the value of the provision because of the absence of claims experience. Note 27.1 of DHW's financial report provides information on the actuarial assessment.

Assets

The consolidated entity's financial position is dominated by non-current property, plant and equipment assets, representing 83% of total assets.

The carrying value of property, plant and equipment increased by $317 million to $6 billion. Key movements during the year were:

- a $332 million valuation increment resulting from an independent revaluation as at 1 June 2018, of which $350 million was recognised in other comprehensive income and $18 million in net result. Unobservable inputs and the significant extent of professional judgement required in valuing these assets is discussed further in note 23.2 of DHW's financial report
- additions of $229 million including $211 million capital works in progress additions
- depreciation and amortisation of $234 million.

The main categories of property, plant and equipment were:

- land, $344 million
- buildings, $2.5 billion
- buildings under public private partnership, $2.6 billion
- capital works in progress, $67 million
- leasehold improvements $41 million
- plant and equipment, $254 million
- plant and equipment under public private partnership, $251 million.

In 2017-18 certain land and buildings at the former RAH site were transferred to the Urban Renewal Authority for $0 consideration.

Central Adelaide Local Health Network Incorporated (CALHN)

Financial statistics

Total expenses:	$2717 million
Net cost of providing services:	$2128 million
Revenues from SA Government:	$2133 million
Staff benefits liability and related on-costs:	$463 million
Workers compensation liability:	$26 million
Number of FTEs:	11 222

Significant events and transactions

— The new Royal Adelaide Hospital (RAH) opened on 5 September 2017.

— The new RAH was recognised in CALHN's financial report at a value of $2.809 billion. This comprised a leased building asset of $2.551 billion and leased furniture, fixtures and equipment of $258 million.

— The builder has initiated legal action in the Federal Court of Australia against Celsus (previously SA Health Partnerships Nominees Pty Ltd), the independent certifier and the State. This and other matters related to the construction of the new RAH are ongoing.

— Quarterly service payments of $350 million for the new RAH were paid in line with the Project Agreement.

— Effective 6 June 2018, Celsus renegotiated its finance for the new RAH and this resulted in a $5 million credit to CALHN for the June 2018 quarterly service payment, in line with the Project Agreement.

— CALHN incurred a $29 million expense in 2017-18 to reduce the remaining value of land and buildings at the old RAH site that were now included in an expanded group of assets to be transferred to the Urban Renewal Authority. This expense reflects that SA Health will no longer have control over these assets and will not receive any income on transfer.

- The Enterprise Pathology Laboratory Information System was implemented in all major metropolitan and regional hospitals where SA Pathology laboratories are situated. Following implementation a Taskforce was established to address concerns about the impact of the system on the timeliness of pathology results.
- An independent revaluation of land and buildings as at 1 June 2018 (excluding the new RAH) resulted in a net $30 million valuation increment.
- The *Health Care (Governance) Amendment Act 2018* was proclaimed in August 2018 and will be operational from 1 July 2019. It changes governance arrangements, including that CALHN will be governed by a board from that date.

Financial report opinion	**Unmodified**
Financial controls opinion	**Modified** Key issues: — Inadequate review of employee payroll and leave management information — No process to ensure nurses' and medical officers' timesheets were always approved prior to payment — Weaknesses in processes to ensure the completeness of revenue and prompt debt collection — Patient billing has been delayed due to system changes — No reviews of user access for a number of systems — Retrospective approval of SA Pharmacy expenditure through purchase orders — Duplicate invoices processed and paid

The new Royal Adelaide Hospital (RAH)

New RAH public private partnership (PPP) arrangement

The new RAH opened in September 2017 and has been delivered through a PPP project that commenced in May 2011. The estimated total value of the contractual arrangement provided for a nominal capital cost for design and construction of $1.85 billion. The budget for State funded works is $588 million, of which $553 million had been spent as at 30 June 2018. The total nominal cost of the project was $2.4 billion.

Commencement of service delivery and quarterly service payments

Commercial acceptance was achieved on 13 June 2017, signalling the transfer of control of the new RAH to the State. It also marked the start of repayments to Celsus including new RAH servicing costs through quarterly service payments.

As at 30 June 2018 quarterly service payments of $350 million had been made.

Legal action in progress

On 1 August 2017, the builder (Hansen Yuncken Pty Ltd and CPB Contractors Pty Ltd (formerly Leighton Contractors Pty Ltd)) filed legal proceedings against Celsus, independent certifier Donald Cant Watts Corke Pty Ltd and the State of South Australia for alleged breaches of contract and other matters in relation to the construction of the new RAH. At the time of this Report the arbitration process was still in progress.

On 5 June 2018, Spotless issued Celsus with three Notices of Dispute relating to operational matters. On the same day, Celsus issued corresponding Notices of Dispute to the State. At the time of this Report, the parties were discussing these operational matters.

Financial impact of the completion of the new RAH

The new RAH arrangements have a significant impact on CALHN's financial report as outlined below.

Framework for the recognition of the new RAH

The new RAH is accounted for as a finance lease arrangement under Australian Accounting Standards. In broad terms, this requires CALHN to recognise

- the liabilities for the repayments to Celsus over the life of the agreement
- the new RAH building and leased equipment as assets on the date of commercial acceptance.

Substantial liabilities associated with the new RAH

CALHN's financial report includes total liabilities of $2.76 billion as at 30 June 2018 which are associated with the new RAH. This is split between current and non-current finance lease liabilities of:

- current – $61 million
- non-current – $2.69 billion.

These liabilities represent the present value of the future minimum lease payments for the new RAH building and equipment. The future payments represent payments to Celsus for the design, construction and financing of the new RAH building and the furniture, fittings and equipment that Celsus has provided to the State as part of the arrangement.

Also included in these payments are amounts for the planned maintenance of the building and planned maintenance or replacement of items of furniture, fittings and equipment through the life of the contract. These payments are termed lifecycle costs and represent the projected costs the State has agreed to pay Celsus to maintain the facility in the condition required by the arrangements until the new RAH is handed back to the State in June 2046.

Significant future commitments for operating costs of the new RAH

In addition to the assets and liabilities discussed above, CALHN has disclosed details of the commitments for payments to Celsus for the provision of services including security, maintenance and cleaning at the new RAH for the term of the arrangements. The total nominal cost of these arrangements is $2.984 billion.

The committed amounts are not recognised as a liability as the State is only liable to pay them once the services have been delivered and the State has been invoiced for the costs. Accordingly, they will be recognised as expenses for each year of operation of the new RAH until 2046.

The total payments to Celsus over the term for these commitments will also vary depending on, among other factors, the number and types of patients in the new RAH and the quantity of maintenance required.

Refinancing event

The new RAH Project Agreement provides for the refinancing of the project a number of times over its 30-year life. The first refinancing event was scheduled for seven years from the signing of the Project Agreement in 2011.

Under the arrangement, refinancing gains are to be shared with CALHN in one of the following forms:

- a lump sum payment
- adjusting the quarterly service payment
- a combination of the above.

Effective 6 June 2018, Celsus renegotiated its finance and achieved a reduced interest rate for a period of two years. Celsus will provide credits as part its quarterly service payment invoices in line with the Project Agreement.

Changes in the interest rates are treated as contingent rents by CALHN which means that they are excluded from the lease calculation and recognised in the period in which they are incurred. The reduction in interest rate will lower the quarterly service payments for the next two years. For the period from 6 June 2018 to 30 June 2018, the refinancing resulted in a credit being received by the State for $5 million on the June quarterly service payment.

Total nominal cost of the new RAH arrangements

The liabilities recognised for the new RAH in CALHN's financial report are the present value of the minimum lease payments to Celsus. This figure is determined by discounting the nominal payments to Celsus using the discount rate (interest rate) that is implicit in the arrangements. The discount rate used for the new RAH is 9.929%.

When the effect of discounting is excluded, the total nominal cost of the new RAH arrangements to the State over the term to June 2046 is shown in the following table.

	Finance lease $'million	Operations and maintenance $'million	Total $'million
Nominal payments over the life of the lease (until June 2046)	8 426	2 984	11 410

As mentioned above, these costs will change over the course of the arrangements for the operations and maintenance element due to changes in the number of patients in the new RAH and other factors. These amounts are disclosed as commitments (refer notes 29.3 and 29.4 of CALHN's financial report).

The composition of the payments to Celsus will vary over the term according to the planned maintenance schedule (lifecycle) costs and variations in the levels of maintenance and other operational costs incurred. The State will make quarterly service payments to Celsus noting that the amount paid in any given year will vary, as previously explained, including for the effects of any refinancing which occurs.

The arrangements provide for the indexation of the lifecycle costs and the pass through of operating and maintenance costs based on volume. The lifecycle costs will therefore change over the course of the arrangement through the effects of indexation.

At the time of this Report, negotiations were continuing with Celsus to resolve matters that may result in reductions (abatements) in payments.

Further reporting on the new RAH

I intend to table a further separate Report on the new RAH project. It will provide observations on the arrangements implemented by the State to manage the Project Agreement for the operating term, along with further commentary on the June 2018 process suspension deed. The deed is discussed in Part A of this Report under 'New Royal Adelaide Hospital update'.

Enterprise Pathology Laboratory Information System (EPLIS)

EPLIS was designed to provide SA Pathology, which forms part of CALHN, with a consolidated laboratory information system and replace legacy systems previously in use.

EPLIS was implemented in all major metropolitan and regional hospitals where SA Pathology laboratories are situated by 20 April 2018, including some Patient Collection Centres.

The original approved budget for the project was $30.65 million, made up of a feasibility phase and an implementation phase. Delays in the project resulted in an increased budget to $34.5 million and an extension of the original schedule of 11 months. Delays were the result of:

- procurement of new pathology equipment
- additions to scope
- the increase in requirements before 'Go Live'
- the tight planning time frame
- changes in program staffing.

The project changed from its original baseline in the final business case from May 2015 and, as a result, benefits expected to be realised as part of the project were not achieved including:

- staff savings – reduced from $5.2 million to $0
- printing costs – reduced from $250 000 to $0
- recurrent costs – increased from $3.1 million to $7.1 million.

SA Pathology continues to report each quarter to eHealth Systems on the realisation of benefits with the possibility that benefits may be achieved in the future when full electronic ordering is achieved.

Following the implementation of EPLIS, concerns were raised about the timeliness of pathology results.

A Taskforce was established in response to these concerns and it recommended a number of initiatives, including additional staffing, to return pathology turnaround times to pre-EPLIS levels. The Taskforce confirmed the need to undertake further system, process and workflow optimisation activities which are underway. SA Pathology updated the EPLIS benefits realisation plan which revised the expected benefits to include no staff savings (a reduction of eight FTE was projected) and an increase of 40 FTEs.

The additional 40 FTEs are required to assist in data entry processes to ensure pathology processing times achieve the levels required.

One of the challenges to achieving ongoing efficiency in the use of EPLIS has been the pause in the rollout of the Enterprise Patient Administration System (EPAS). The delay in implementing electronic ordering from EPAS to EPLIS has reduced the efficient use of EPLIS.

Functional responsibility

CALHN is established under the *Health Care Act 2008.*

The powers and functions of CALHN are to establish, provide, maintain and enhance hospital, medical and allied health services in its local area.

Under the *Health Care Act 2008* the Chief Executive, Department for Health and Wellbeing (DHW) assumes direct responsibility for administering incorporated hospitals. This includes appointing the Chief Executive Officer of CALHN. The Chief Executive, DHW cannot give a direction about a person's clinical treatment.

Governance changes

The new SA Government has announced its intention to amend governance arrangements across SA Health. The first part of these changes was completed in August 2018 when the *Health Care (Governance) Amendment Act 2018* was proclaimed and will operate from 1 July 2019.

The amendments abolish the former function of the Chief Executive, DHW to assume direct responsibility for the administration of incorporated hospitals. The amendments provide for CALHN to be governed by a board. The SA Government intends the board to be fully operational by 1 July 2019.

The SA Government has stated it will establish a new governance and accountability framework for the public health system which will be reflected in legislation to be introduced into Parliament later in 2018 or early next year.

Scope of the audit

The audit program covered major financial systems to obtain sufficient evidence to form an opinion on the financial report and internal controls.

Financial services for CALHN are provided through a combination of:

- central services provided by DHW through an integrated finance service model
- finance services located within CALHN
- services provided by Shared Services SA (SSSA).

The audit included review of systems at DHW's central services, CALHN and SSSA.

Audit findings across health services fall into the following categories:

- common findings reflecting central services and/or systems
- matters for individual health services
- SSSA matters.

Specific areas of audit attention in 2017-18 included:

- SA Pharmacy
- SA Pathology
- inventory
- property, plant and equipment
- general ledger
- private practice revenue
- payroll
- expenditure and accounts payable
- patient billing and sundry revenue
- accounts receivable and other revenue
- grants and contributions revenue
- cash and online banking.

Internal audit activities were reviewed to assess the risks of material misstatement in the financial report and to design and perform audit procedures.

Audit findings and comments

Assessment of controls

In my opinion, the controls exercised by the Central Adelaide Local Health Network Incorporated in relation to the receipt, expenditure and investment of money, the acquisition and disposal of property and the incurring of liabilities, except for all matters outlined under 'Communication of audit matters', are sufficient to provide reasonable assurance that the financial transactions of the Central Adelaide Local Health Network Incorporated have been conducted properly and in accordance with law.

Communication of audit matters

Matters identified by the audit were detailed in management letters to the Chief Executive Officer, CALHN and copied to the Chief Executive, DHW. SSSA matters were reported to the Chief Executive, Department of the Premier and Cabinet.

A summary of our findings for centralised processes performed by DHW and SSSA can be found in the section of this Report titled 'Department for Health and Wellbeing' under the heading 'Communication of audit matters'. The main matters raised with CALHN and related responses are detailed below.

Payroll

Payroll related costs for CALHN are significant, with more than $1.4 billion in staff benefit expenses paid in 2017-18 and $435 million in staff benefit liabilities at 30 June 2018. Payroll controls are therefore a key focus of our audit each year.

No regular review of payroll information by CALHN

Consistent with our previous findings, we found CALHN did not have an effective process to ensure the accuracy of employee-level pay information. In particular we found:

- the validity of payments to employees was not certified
- there was no regular review of employee classification levels
- the validity of long-term allowances was not reviewed.

As part of the Chris21 payroll system upgrade, a bona fide report was introduced to verify employee level pay information. We found that the report covers auto-pay employees which only represent about 40% of CALHN's staff. We were also informed that the review process had not been implemented due to data quality issues.

CALHN noted the findings and advised that it was progressively identifying the system issues and advising SSSA. CALHN advised a number of issues were not yet finalised and it was working through a process to implement alternate solutions for bona fide reports for non-auto pay employees.

Inadequate leave management processes

Leave should only be granted where the employees have accumulated adequate entitlements and all leave taken should be recorded.

Consistent with our previous findings in 2017-18, we found CALHN did not have an effective central mechanism to ensure leave management reports were reviewed as required by policies and procedures. We noted increases in both the number and hours of employees with negative and excessive annual leave in 2017 -18.

Our review identified 261 (197) CALHN employees with negative leave balances and 1580 (662) with excessive annual leave balances, the highest being 2114 hours, reinforcing the need to improve leave management. Total negative leave hours had increased by 1104 to 1807 hours.

CALHN noted the findings and advised that an investigation of the negative and excessive annual leave balances had begun. CALHN advised it would meet with SSSA each fortnight to determine whether processing errors were contributing to the issue. CALHN also noted reports identifying excess leave balances and negative leave balances would be sent to managers to ensure leave plans were in place within four weeks of receiving the report and make sure no further leave was granted to employees with negative balances.

Nurses’ timesheets were not always approved prior to payment

We have previously reported that not all timesheets for nursing, midwifery and patient services staff were approved prior to payment as required by CALHN policy. We noted an average of 90% of timesheets were approved prior to payment which was consistent with previous years. This issue is mainly a result of adjustments made to approved timesheets, meaning the timesheets require re-approval.

CALHN noted the findings and advised it would reinforce to Nursing Directors that all timesheets are to be approved prior to payment, including adjusted timesheets.

No process to ensure all medical officers’ timesheets were approved and submitted

Consistent with our previous findings, there remained no process to ensure all medical officers submit timesheets and accompanying leave forms for approval. We found that managers were not informed when employees had not submitted expected timesheets and therefore did not monitor and follow up missing timesheets.

The complete review of timesheets and associated leave ensures correct payments will be made to staff and leave taken captured in the payroll system. We consider this is particularly important where staff are automatically paid in the payroll system, regardless of whether a timesheet is submitted, which is typically the case for medical officers. While they are automatically paid, medical officers’ timesheets identify allowances they are entitled to, meaning the accuracy of total payments requires completed timesheets to be processed promptly.

CALHN responded that it would investigate with SSSA to determine if regular reports of outstanding timesheets can be produced. CALHN advised it would also discuss the issue of outstanding timesheets with relevant Business Managers.

Expenditure

CALHN paid over $849 million for supplies and services in 2017-18. A large proportion of these expenses are approved for payment using online approval functions in SA Health's key financial systems, Oracle and Basware.

Invoices were not always matched to purchase orders

When goods or services are received and receipted against an Oracle purchase order, an expense and matching liability is recognised in the general ledger. If goods or services received are not matched against the purchase order this can result in the duplication of expenses and liabilities. We noted there was a $1.3 million liability for unmatched receipted purchase orders as at 30 June 2018.

Not matching invoices with their corresponding purchase orders prior to payment can result in an overstatement of liabilities and associated expenses. There is also an increased risk of payments being made for goods or services not received or at a price inconsistent with the agreed purchase order.

CALHN acknowledged that not all invoices were matched to purchase order receipts. Staff would be reminded that supplies ordered through purchase orders are to be receipted in Oracle when the goods are received and not through Basware.

Duplicate invoices were processed and paid

Our analysis of invoice data identified potential duplicate invoices across eight high risk categories for CALHN. Our review of 26 pairs of invoices identified 12 duplicate payments. CALHN has started action to recover these specific overpayments. We note, however, there was no process in place to proactively identify duplicate payments within CALHN.

CALHN responded that SSSA had various mechanisms to detect and cancel duplicate invoices, however errors were still occurring. CALHN advised it would meet with SSSA to conduct a root cause analysis to reduce the number of suppliers who send duplicates. This would include, but not be limited to, supplier engagement, improvements to procurement process, moving to e-invoicing and reducing errors such as the creation of duplicate vendors.

CALHN also undertook to establish a periodic review process to identify duplicate invoices and, when they are identified, seek to recover any overpayment.

Contracts not established where regular services are provided

Our review identified significant expenditure that was not supported by formal contracts between the supplier and CALHN. Negotiating and documenting a contract with suppliers of large amounts of goods/services provides opportunities to reduce prices or improve service delivery.

CALHN responded that it had contracts in place for most suppliers and it would remind staff to adhere to current procurement policies and procedures. CALHN would also review vendor spend profiles and, if necessary, contact staff to ensure that contracts were in place and liaise with SA Health's Procurement and Supply Chain Management group to help establish contracts to define service and price expectations.

Intellectual property (IP) register

Each local health network (LHN) is responsible for maintaining its own IP register as there is no central IP register for SA Health. CALHN could not provide its register at the time of our audit.

In my opinion CALHN requires an up-to-date IP register to effectively manage IP rights and obligations, which in turns helps to determine IP claims.

CALHN responded that the CALHN Research unit had recently developed an IP register that was now up to date and could be reviewed in 2018-19.

SA Pharmacy

SA Pharmacy operates pharmacies for all LHNs and spent more than $214 million on drug supplies in 2017-18.

Stocktakes of controlled drugs are not performed monthly

SA Pharmacy's stock management policy requires drugs of dependence and restricted drugs to be counted each month. At the Flinders Medical Centre pharmacy store we noted that the manual registers used to record controlled drug stocktakes were not completed each month.

We confirmed that there was currently no review process in place to ensure that monthly counts were performed for each drug.

SA Pharmacy noted our finding and advised it would investigate establishing an education program focusing on inventory management principles.

Requisition forms for drugs of dependence not always returned

Wards complete a requisition form for drugs of dependence from the pharmacy. Pharmacy staff record all requisition forms received from the wards in the drugs of dependence receipt log. Two staff at the ward then receive drugs and sign the requisition form and return it to the pharmacy. We noted that pharmacy staff did not follow up requisition forms that were not received back from the wards. As a result there is no assurance that all drugs of dependence issued have been received by the appropriate people.

SA Pharmacy acknowledged and agreed with this issue and advised it would communicate with pharmacy staff at the Flinders Medical Centre about the requirement to follow up instances where the requisition forms for drugs of dependence had not been returned.

Monitoring access to pharmacies requires improvement

We have previously identified that monitoring swipe card access and after-hours access to pharmacies needed to improve to ensure access was restricted and stock was safe.

SA Pharmacy has previously agreed that, although reviews started to occur in the second half of 2016-17, there was no procedure in place to support the consistent review of pharmacy access. SA Pharmacy advised it would develop an after-hours pharmacy access policy to provide guidance to all sites.

For 2017-18, we noted that the procedure was still being developed and the RAH pharmacy stores were working with Spotless to develop monthly access reports to ensure only appropriate personnel had access.

SA Pharmacy advised it was continuing to establish a procedure and was working with Spotless to obtain an appropriate system report for access at the new RAH pharmacy.

No independent review of the return of drugs

SA Pharmacy policy requires all returns of drugs of dependence to be recorded in a log book. Two pharmacists or a pharmacist and a registered nurse must sign the log book on receipt of the drugs of dependence. The Controlled Substances (Poisons) Regulations 2011 require information to be recorded about a drug of dependence immediately after its destruction.

At The Queen Elizabeth Hospital (TQEH) site we noted that the log book was not regularly reviewed by an independent officer to ensure details were correctly recorded and certified by appropriate personnel. We reviewed the log book for January 2018 and noted that the processing details for two drugs were not recorded, with no evidence that this had been followed up.

We were advised that the Team Leader had since followed up the identified discrepancies and advised that the two drugs were destroyed in May 2018, with the log book updated in late May 2018.

SA Pharmacy advised it would investigate establishing an education program focusing on inventory management principles.

No independent review of the drugs of dependence movement report

At the new RAH, drugs of dependence are kept in a safe in the main pharmacy and at ward level they are stored in Automated Dispensing Cabinets (ADCs). Movements between the main stores and ADCs are tracked by an internal system. The system requires authorised users to perform a count every time an item is added or removed. Where there are variances on the report the pharmacist will examine each exception and follow up with the relevant ward when required.

We noted that this report was not being independently reviewed to ensure that these checks are performed promptly.

SA Pharmacy acknowledged the finding and advised it would require an independent officer to review the system reconciliation to ensure that the control was performed as intended.

Entry to pharmacies with generic access cards is not reviewed against manual registers

SA Pharmacy reviews the security access reports to pharmacy stores each month to ensure only authorised personnel have access and every attempted entry to the pharmacy can be investigated where required. If the stores were accessed by a generic card, the report shows the card number and name of the card.

We noted that not all generic cards that had accessed the pharmacy store had a manual register of users. Rather, generic cards had been allocated to wards or Spotless. The lack of control over these cards increases the risk that pharmacy stores are accessed by inappropriate personnel, meaning access to drug supplies cannot be monitored effectively.

SA Pharmacy acknowledged the finding and advised it would work with LHN business units regarding the importance of maintaining security card registers. SA Pharmacy also noted that accountability for the LHN business unit register resides with the LHN, not with SA Pharmacy.

Retrospective authorisation of purchase orders

Treasurer's Instruction 8 'Financial Authorisations' (TI 8) requires authorised delegates to approve expenditure before it is incurred, including purchases. We found that the authorisation for pharmaceutical purchases was, in most instances, provided after the purchase order had been placed with the supplier.

SA Pharmacy's previous responses to this issue have acknowledged the TI 8 requirements but noted that delaying electronic orders until the authorisation was complete could result in substantial delays, potential shortages and patient harm.

We requested that SA Pharmacy investigate changes to its processes and delegations to align them with TI 8 requirements. We noted that throughout 2017-18 this issue remained but SA Pharmacy worked to resolve it through discussions with DHW and DTF.

SA Pharmacy responded that it acknowledged the recommendation and had updated its delegations to comply with TI 8 effective 1 July 2018.

Pharmaceutical Benefits Scheme (PBS) revenue reconciliations are incomplete

SA Pharmacy implemented a standard procedure from June 2017 to undertake PBS reconciliations. The reconciliations ensure payments have been received from Medicare for all applicable prescriptions. PBS claims technicians follow up any discrepancies between the estimated rebate and the actual rebate from Medicare. Medicare will not provide a reimbursement for claims that have been closed for over 90 days, meaning it is crucial for the LHNs to investigate the discrepancies promptly.

Consistent with last year, we found some reconciliations had not been performed, others had no evidence of independent review and some had unexplained variances that were being investigated. Consequently, LHNs cannot be certain they have received all PBS subsidies they are entitled to.

We acknowledge that a manual claim form can be submitted after the 90-day claim period but these are for exceptional circumstances, require additional supporting documentation and take more time to complete.

SA Pharmacy acknowledged and accepted this recommendation. It advised it would communicate with the SA Pharmacy PBS Officers Group to ensure PBS reconciliations were completed promptly.

SA Pathology

SA Pathology patient fees for public and private patients totalled more than $113 million for 2017-18.

Delayed or incomplete billing (EPLIS)

Consistent with issues raised in previous years, we found no specific processes existed to ensure all fees for the provision of SA Pathology services were billed.

EPLIS was implemented in 2017-18 and there was a significant increase in the number of errors that had prevented transactions from being processed in the billing system (PBRC). Errors included:

- items raised in EPLIS but not billed in PBRC
- items raised in EPLIS but rejected by PBRC
- EPLIS items rejected by Medicare/health funds.

SA Pathology advised that it was working with Hospital Revenue Services to understand any delayed or incomplete billing in EPLIS. Once the system was better understood, SA Pathology would develop policy and procedure documents to support this process. The EPLIS Optimisation Project will also consider SA Pathology billing.

Delayed or incomplete billing (ULTRA)

Consistent with prior years we found improvements were needed to ensure billing was complete and accurate. We found SA Pathology did not effectively:

- monitor or follow up pathology services completed that had not been invoiced
- reconcile its laboratory system (Ultra) records to revenue system records.

We noted in previous years that while the billing system will send invoices and reminder notices, a system issue did not allow the final and demand notices to be sent.

Unbilled pathology charges that are not followed up may result in delayed or lost revenue.

SA Pathology advised that Hospital Revenue Services had been provided with a system solution to allow final and demand notices to be sent to outstanding debtors. A plan for system solution testing and implementation was being determined, with an intention that sending final notices would be possible from December 2018.

Pathology system access

For a number of years, we have raised concerns about SA Pathology's review of user access to Ultra. Consistent with last year, our review found that issues about system access, user profiles, monitoring and reporting for Ultra and EPLIS remained.

We noted that issues raised in previous years were not progressed due to significant operational issues encountered when EPLIS was implemented system-wide. We understand SA Pathology has been focused on addressing these significant operational issues and is working to address remaining issues under direction from an internally managed task force.

SA Pathology advised:

- it reviews Ultra access when positions are created or when staff leave or revert to a substantive position
- staff that leave or revert from a senior position have their access removed as part of the exit process
- it will maintain a list of employed staff and their level of access to Ultra and EPLIS and review this each quarter to ensure access profiles are correct.

No reconciliation between PBRC and the laboratory system

In previous years we have highlighted that a reconciliation between PBRC and the laboratory system had not been performed and were advised by SA Pathology that this was due to system limitations. SA Pathology expected that once EPLIS was fully implemented, a reconciliation between the systems would be possible to ensure that all information was completely and accurately invoiced.

EPLIS was fully implemented in 2017-18 and our follow-up revealed that a reconciliation between EPLIS/Ultra and PBRC was not yet developed.

SA Pathology advised that the system limitations that do not allow the Ultra laboratory system to be reconciled will be overcome after EPLIS implementation and once the data warehouse was able to facilitate these reports.

Patient billing

CALHN's revenue from patient and client fees was over $238 million in 2017-18, with a further $36 million recorded in private practice fees controlled by CALHN. In addition, $65 million was collected on behalf of medical officers and DHW in administered revenue from private practice arrangements.

Inadequate review of revenue system access levels

Last year we found that no complete review of user access profiles was performed for EPAS as required by policy. Our review this year noted that CALHN had performed a review of EPAS users with access to the billing module. However, this review did not consider users with access to the clinical module of EPAS at TQEH. As such, no complete review of user access to EPAS was performed.

Without a regular review of EPAS user access and profiles there is a risk of inappropriate access, which could result in inaccurate or unauthorised changes being made to data or unauthorised access to patient information.

CALHN acknowledged the finding and advised it would allocate a resource to perform a review of clinical access to EPAS. CALHN would also implement a regular process of access review to ensure only current employees had access and access privileges were appropriate.

Invoices with double billed line items

We were advised that both TQEH and the new RAH have noticed duplicate charges on patient invoices. This duplication error has been raised with the EPAS support team and no solution was yet available.

As a workaround, CALHN billing teams were manually checking every invoice to ensure the charges were correct. Manually checking each invoice decreases any efficiencies gained by having an automated invoicing system.

CALHN responded that revenue staff would continue to manually check every invoice and log errors as they are identified until the issue is resolved. EPAS defects and changes are discussed and reviewed bi-monthly at the EPAS Patient Billing Work Group, with a range of higher priority changes being progressed.

No policy or procedure for the coding of patient treatments and significant delays in coding

The coding unit at CALHN reviews patient files in EPAS to identify procedures undertaken and apply a code for each treatment. EPAS will not generate an invoice until a patient's treatment has been coded. This process is not documented in a policy or procedure.

Our review of the Hospital Billing Accruals report noted that most patients discharged from March 2018 onwards had not been coded. We understand from discussions with CALHN staff that the delays were caused by:

- the transition to EPAS and lack of staff knowledge of the new system
- the non-clinical rollout of EPAS at the new RAH, which has placed reliance on manual client files for coding and there have been issues with locating files and a backlog of unfiled treatments in doctor notes.

CALHN responded that it was required to complete all clinical coding on a monthly basis with submission for the current month by the 16th of the following month. CALHN had been unable to achieve this due to a shortage of clinical coding staff and the impacts of the EPAS system. It recently completed the 2017-18 financial year backlog and was working on the current financial year. With the assistance of external coding support, increased internal resources and an overall improvement strategy for clinical coding, CALHN is nearing business as usual.

Prostheses invoices had not been billed since September 2017

Our past audits have identified issues about the completeness of invoices for prostheses services, including charging for prosthetic devices used. In following up these matters we were advised the proposed scanning system which was to be implemented at the new RAH had now been assessed as inadequate and there had been no billing for prosthetics from September 2017 for the financial year. Prostheses billing is estimated to be $4 million annually.

CALHN responded that a new prostheses billing system was implemented on 1 July 2018. A new dedicated position has been created to perform prostheses billing and the back-billing was progressing and was to be completed by January 2019.

Private practice billing

Private practice revenues are billed on behalf of salaried medical officers and subsequently distributed to the LHNs, DHW and salaried medical officers according to private practice agreements.

Private practice audits

We have previously noted that specialist private practice agreements allow for the Chief Executive, DHW, through DHW, the LHNs or the engagement of an independent auditor, to review and audit:

- specialists' private practice
- amounts transferred to CALHN under a private practice agreement
- accounts rendered by a specialist or on behalf of a specialist.

CALHN has previously responded that a risk based approach would be considered but a regular program of review or audit of specialists' private practice had not been established.

In May 2018, CALHN performed a review to identify where specialists had a Medicare provider number at an offsite address that was not included or disclosed on their private practice agreement. This process identified 36 specialists, 11 at TQEH and 25 at the new RAH, where further information was needed to confirm the arrangements were in line with approved private practice agreements.

Clinicians were asked to provide a written response to CALHN on the identified matters but as at July 2018 only 17 responses had been received.

We recommended CALHN continue to develop and document a risk based approach to reviewing/auditing specialist private practice arrangements, as provided for in private practice agreements.

CALHN responded that it would continue to adopt a risk based approach to reviewing/auditing specialists' private practice arrangements and noted it was still following up outstanding responses from its earlier review.

Private practice – system difficulties

Under the rights of private practice, salaried medical officers and clinical academics are able to treat private patients and charge them for services. If CALHN staff administer the billing function, CALHN receives a 9% administration fee on total revenue. We noted that revenue had decreased during the year and were informed that the reduction related to the introduction of EPAS.

CALHN noted that the invoice duplication issue discussed above and difficulties in getting some report information had resulted in an increase in Medicare rejections, with manual processes required to follow up and correct the errors.

As noted above, CALHN advised it would continue to identify and report issues as they occur and discuss these issues bi-monthly at the EPAS Patient Billing Work Group meetings.

Interpretation and analysis of the financial report

Highlights of the financial report

	2018		2017	
	Consolidated $'million	Parent $'million	Consolidated $'million	Parent $'million
Expenses				
Staff benefit expenses	1 415	1 407	1 336	1 330
Supplies and services	849	845	738	735
Depreciation and amortisation	124	124	47	47
Borrowing costs	261	261	13	13
Other expenses	68	68	77	76
Total expenses	2 717	2 705	2 211	2 201
Income				
Revenue from fees and services	356	346	326	317
Grants and contributions	183	184	204	204
Other income	50	48	44	43
Total income	589	578	574	564
Net cost of providing services	2 128	2 127	1 637	1 637
Revenues from SA Government	2 133	2 133	1 637	1 637
Net result	5	6	-	-
Other comprehensive income	47	47	(7)	(7)
Total comprehensive result for the year	52	53	(7)	(7)
Assets				
Current assets	262	253	192	181
Non-current assets	3 503	3 497	3 497	3 491
Total assets	3 765	3 750	3 689	3 672
Liabilities				
Current liabilities	359	357	304	303
Non-current	2 971	2 971	3 004	3 003
Total liabilities	3 330	3 328	3 308	3 306
Net assets	435	422	381	366

Statement of Comprehensive Income

Expenses

In 2017-18 the consolidated entity's total expenses increased significantly by $506 million to $2.7 billion.

Staff benefit expenses

Staff benefit expenses, $1.4 billion, represent more than 50% of CALHN's total expenses and increased by $79 million in 2017-18.

The increase in staff benefit expenses is due to:

- a $52 million increase in salaries and wages, mainly from wage rises associated with enterprise agreements
- an increase in long service leave expenses of $4 million due to assumptions relating to timing of cash flows, staff turnover and enterprise bargaining agreement increases
- an increase in annual leave expense of $8 million
- a $7 million increase in workers compensation reflects an increase in actuarial assumptions and new workers compensation non-statutory liability of $2.7 million introduced in 2017-18 through various enterprise bargaining agreements and awards.
- an increase of $7 million in targeted voluntary separation packages of $9 million ($1.5 million) that were paid to 101 (13) employees.

The number of employees whose remuneration received/receivable exceeded the base executive level ($149 000) totalled 1185 (1170), comprising 1013 medical, 85 non-medical, 64 nursing and 23 executive employees. Nursing remuneration included in these figures decreased by 26 employees and $5 million as a result of there being an extra pay run in the previous year. Total remuneration for these employees was $338 million ($329 million).

Supplies and services expenses

Supplies and services expenses increased by $111 million (15%) to $849 million. Significant components of supplies and services expenses were:

- drug supplies, which increased by $8 million (4%) to $214 million
- medical, surgical and laboratory supplies, which increased by $4 million (3%) to $162 million
- PPP expenses, which increased by $60 million to $62 million related to the operations of the new RAH (security, cleaning, maintenance, food supplies).

Other expenses

Overall other expenses reduced by $9 million to $68 million. Significant components of other expenses were:

- impairment expenses of $14 million mostly related to the write-down in value of the old RAH car park, recognising it will transfer to the Urban Renewal Authority in 2018-19 for $0 consideration
- land revaluation decreases of $18 million that were expensed due to the revaluation reserve being exhausted from previous old RAH decrements
- donated assets of $15 million relating to transfers of other buildings at the old RAH site to the Urban Renewal Authority for $0 consideration
- royalty payments of $10 million.

Revenues

CALHN is dependent on revenue from the Commonwealth and SA Governments.

CALHN received $2.133 billion in funding from the SA Government in 2017-18. This included capital funding of $189 million, an increase of $48 million (34%).

Commonwealth grants and contributions received directly by CALHN decreased by $24 million to $163 million, due to a decrease of $24 million in the PBS Commonwealth subsidies to $158 million relating to a reduction in claims for drug treatments.

Statement of Financial Position

Property, plant and equipment

Property, plant and equipment represent 91% of total assets.

The carrying value of property, plant and equipment remained at $3.4 billion.

Significant movements in property, plant and equipment in 2017-18 were:

- revaluation decrements, donated assets and impairment losses associated with surplus assets totalling $46 million, mostly related to the write-down in value of the old RAH and Glenside sites
- revaluation increments of $47 million relating to buildings, mostly at TQEH, and medical equipment
- depreciation and amortisation expenses increasing by $70 million to $114 million due to commissioning of the new RAH and associated plant and equipment.

There were also transfers from capital works in progress totalling $35 million to CALHN's intangible assets in 2017-18. These additions include amounts associated with developing software and ICT systems for the new RAH, the ESMI medical imaging system and EPLIS.

Liabilities

Current liabilities increased by $55 million to $359 million during the year and exceeded current assets of $262 million at 30 June 2018. CALHN works with DHW to ensure sufficient funding is provided to CALHN to meet expected cash flows for its administration and program delivery. Cash and cash equivalents of $159 million are sufficient to meet current payables of $96 million.

Staff benefits are the largest element of current liabilities, totalling $193 million at 30 June 2018, and include leave entitlements expected to be taken within 12 months.

Total liabilities increased by $22 million to $3.3 billion, reflecting increases in staff benefit liabilities and workers compensation offset by payments against the finance lease liabilities associated with the new RAH.

Staff liabilities and associated on-costs make up $490 million of CALHN's total liabilities at 30 June 2018, comprising:

- staff benefits liabilities and related on-costs, $464 million ($431 million)
- provision for workers compensation, $26 million ($22 million).

Staff benefits liabilities were impacted by increases in assumptions about the timing of future cash flows, leave taken in service and enterprise bargaining increases offset by a slight increase in the bond yield that decreased the liability.

The increase in the provision for workers compensation reflects changes to relevant public sector enterprise agreements and CALHN has recognised an additional compensation provision as at 30 June 2018.

Country Health SA Local Health Network Incorporated (CHSALHN)

Financial statistics

Total expenses:	$911 million
Net cost of providing services:	$685 million
Revenues from SA Government:	$661 million
Staff benefits liability and related on-costs:	$172 million
Workers compensation liability:	$9 million
Number of FTEs:	5843

Significant events and transactions

— An independent revaluation of land and buildings as at 1 June 2018 resulted in a $61 million valuation increment.

— The *Health Care (Governance) Amendment Act 2018* was proclaimed in August 2018 and will be operational from 1 July 2019. It changes governance arrangements, including that local health networks (LHNs) will be governed by boards from that date.

— In August 2018 six new regional incorporated hospitals (LHNs) were proclaimed under the *Health Care Act 2008.* Each will be governed by a board and will take over the functions of providing health services from CHSALHN from 1 July 2019.

Financial report opinion

Unmodified

Financial controls opinion

Modified

Key issues:

— Contracts with general practitioners need updating to reflect new overarching agreements

— Specialists working in CHSALHN hospitals without contractual agreements

— System access not restricted to ensure incompatible tasks are segregated

Functional responsibility

CHSALHN is established under the *Health Care Act 2008.*

The powers and functions of CHSALHN are to provide health services in rural areas of South Australia.

Under the *Health Care Act 2008* the Chief Executive, Department for Health and Wellbeing (DHW) assumes direct responsibility for administering incorporated hospitals. This includes appointing the Chief Executive Officer of CHSALHN. The Chief Executive, DHW cannot give a direction about a person's clinical treatment.

The consolidated accounts of CHSALHN include the assets, liabilities, revenues and expenses of the Health Advisory Councils (HACs). The HACs were established under the *Health Care Act 2008* to undertake an advocacy role on behalf of the community, to provide advice about the provision of health services, health issues, goals, priorities, plans and other strategic initiatives, and to perform other functions as determined under the *Health Care Act 2008.*

Governance changes

The new SA Government has announced its intention to amend governance arrangements across SA Health. The first part of these changes was completed in August 2018 when the *Health Care (Governance) Amendment Act 2018* was proclaimed and will operate from 1 July 2019.

The amendments change the role of the Chief Executive, DHW to remove direct responsibility for the administration of incorporated hospitals. The amendments also provide for the LHNs to be governed by a board. The SA Government intends the boards to be fully operational by 1 July 2019.

The SA Government has stated it will establish a new governance and accountability framework for the public health system which will be reflected in legislation to be introduced into Parliament later in 2018 or early next year.

New regional local health networks created in August 2018

In August 2018 the following six new regional incorporated hospitals (LHNs) were proclaimed under the *Health Care Act 2008*:

- Barossa Hills Fleurieu Local Health Network Incorporated
- Eyre and Far North Local Health Network Incorporated
- Flinders and Upper North Local Health Network Incorporated
- Riverland Mallee Coorong Local Health Network Incorporated
- South East Local Health Network Incorporated
- Yorke and Northern Local Health Network Incorporated.

These LHNs will take over the functions of providing health services from CHSALHN from 1 July 2019.

Scope of the audit

The audit program covered major financial systems to obtain sufficient evidence to form an opinion on the financial report and internal controls.

Financial services for CHSALHN are provided through a mix of:

- central services provided by DHW through an integrated finance service model
- finance services located within CHSALHN
- services provided by Shared Services SA (SSSA).

CHSALHN continued to operate some legacy systems. Consequently, our audit included the review of new and legacy systems and completing audit work at DHW's central services, CHSALHN and SSSA.

Audit findings across health services fall into the following categories:

- common findings reflecting central services and/or systems
- matters for individual health services
- SSSA matters.

A Chartered Accounting firm assisted the Auditor-General with the audit of CHSALHN.

Specific areas of audit attention in 2017-18 included:

- payroll
- accounts payable
- patient revenue including accounts receivable
- Enterprise Patient Administration System (EPAS) revenue at Port Augusta
- fee-for-service
- property, plant and equipment
- cash
- general ledger.

Internal audit activities were considered in designing and performing audit procedures.

Audit findings and comments

Assessment of controls

In my opinion, the controls exercised by the Country Health SA Local Health Network Incorporated in relation to the receipt, expenditure and investment of money, the acquisition and disposal of property and the incurring of liabilities, except for all matters outlined under 'Communication of audit matters', are sufficient to provide reasonable assurance that the financial transactions of the Country Health SA Local Health Network Incorporated have been conducted properly and in accordance with law.

Communication of audit matters

Matters identified by the audit were detailed in a management letter to the Chief Executive Officer, CHSALHN and copied to the Chief Executive, DHW.

A summary of our findings for centralised processes performed by DHW can be found in the section of this Report titled 'Department for Health and Wellbeing' under the heading 'Communication of audit matters'.

The main matters raised with CHSALHN and related responses are detailed below.

Payments to medical practitioners – fee-for-service

CHSALHN pays medical practitioners in line with the terms of the South Australian Rural Fee Agreement. Our review identified a number of opportunities to improve control processes relating to fee-for-service payments.

Contracts with general practitioners (GPs) need updating to reflect new overarching agreements

In December 2017 CHSALHN established new agreements with the Australian Medical Association (AMA) and the Rural Doctors Association of South Australia (RDA). These agreements require GPs and GP registrars who provide public inpatient medical services to enter into a fee-for-service agreement with CHSALHN.

Our review of fee-for-service agreements with GPs and GP registrars found many were not updated to reflect current terms and conditions established under the new overarching agreements.

CHSALHN responded that due to the unique nature of the contracts it was considering a number of alternatives for implementing our recommendation.

Specialists working in CHSALHN hospitals without contractual agreements

Specialist doctors (specialists) provide public medical services at CHSALHN hospitals and charge CHSALHN on a fee-for-service basis. We found there were a number of specialists operating in CHSALHN without contractual agreements. We also noted there were no overarching agreements between CHSALHN, AMA and RDA defining terms and conditions for contracts between CHSALHN and specialists. We recommended CHSALHN ensure agreements are in place with specialists.

CHSALHN responded that it was awaiting AMA (SA Branch) readiness to commence negotiations for developing an agreement for contracted specialists.

Chiron system access restrictions insufficient

Our review of fee-for-service and patient billing in Chiron found opportunities to improve segregation of duties through independent review processes or restricting user access.

CHSALHN responded that systems limitations prevent it from restricting access to certain system menus and options. It was reviewing access to ensure staff have appropriate access in line with their roles.

Staff can override fee-for-service rates on the system

Fee-for-service payments are generated automatically by Chiron based on code rates maintained in the system. We found staff can manually override these code rates, increasing the opportunity for error or fraud. We acknowledge there are circumstances where manual changes to fees are necessary where fees are based on length of time. However, it is important that code rates cannot be overridden.

We also found staff not involved in fee-for-service processing had access to the fee-for-service module. We recommended that where possible CHSALHN should introduce system based preventative controls. Where these are not possible we recommended CHSALHN introduce additional review processes to identify and action any manual overrides. This matter has been raised for a number of years.

CHSALHN responded that system limitations prevent it from controlling and restricting access, indicating it would consider the requirements of a new system when replacing Chiron. It also advised that is conducted random audits on fee data entry.

Supplies and services expenditure

Invoices received are not always matched to purchase orders

Our review of payments noted instances where invoices were not matched to purchase orders prior to payment. Where this occurs there is an increased risk that payments may be made for goods or services not received or not at the agreed price. In addition the associated expense records may be overstated. This matter was also raised last year.

CHSALHN indicated that it reduces the risk of overstating expenditure by reviewing and actioning records of goods received but not matched against an invoice over 90 days old. It also indicated it would continue to provide training to staff.

Revenue

Policies and procedures

In recent years we have reported to CHSALHN that policies and procedures for patient invoicing, aged care residential fees and sundry invoicing processes were not documented. Our follow-up of actions taken found opportunities for improvement remain. We also found instances where control practices were inconsistently performed. CHSALHN responded it was reviewing work processes and finalising work instructions.

EPAS revenue – Port Augusta

EPAS is operational at the Port Augusta Hospital and Health Service.

Billing officers can access billing data at other hospitals

Our review of EPAS systems access found that Port Augusta billing officers had access to modify billing data at other hospitals using EPAS and vice versa. We recommended CHSALHN ensure that access rights controls are in place to restrict access to the user's specific area of responsibility.

CHSALHN responded that it was unable to modify or restrict access due to limitations in EPAS. To manage the associated risk, CHSALHN indicated it had implemented a manual review of all adjustments.

Need to restrict access to make billing changes

Compensable and private patients are invoiced through EPAS based on a number of different variables including admission and discharge dates, patient elections and admission type. We found access to make changes to these inputs is not adequately restricted. We also found management did not review

reports or audit trails of changes made. Where management does not detect inappropriate or unauthorised changes to invoices or invoicing master files there is an increased risk of fraud or error. We recommended CHSALHN restrict access to make changes or introduce additional review processes to identify and assess changes made. These issues were raised last year.

CHSALHN responded that the issue is with DHW's eHealth Systems division for resolution, indicating it will monitor its progress.

Shared Services SA – financial systems and transactions processing environments

SSSA processes financial transactions on behalf of CHSALHN. The main systems and control environments include accounts payable and payroll financial functions.

Our review and evaluation of controls for these systems concluded that the controls were effective for 2017-18. SSSA is discussed further in the commentary under 'Department of the Premier and Cabinet' in this Report.

Interpretation and analysis of the financial report

Highlights of the financial report

	2018		2017	
	Consolidated $'million	Parent $'million	Consolidated $'million	Parent $'million
Expenses				
Staff benefit expenses	551	551	521	521
Supplies and services	319	319	302	302
Depreciation and amortisation	35	20	34	19
Other expenses	6	13	5	8
Total expenses	911	903	862	850
Income				
Revenue from fees and services	80	80	75	75
Grants and contributions	135	137	131	133
Other income	11	8	8	3
Total income	226	225	214	211
Net cost of providing services	685	678	648	639
Revenues from SA Government	661	661	618	618
Net result	(24)	(17)	(30)	(21)
Other comprehensive income	61	44	-	-
Total comprehensive result for the year	37	27	(30)	(21)
Assets				
Current assets	151	132	138	121
Non-current assets	873	461	836	433
Total assets	1 024	593	974	554
Liabilities				
Current liabilities	195	195	181	181
Non-current liabilities	113	113	114	114
Total liabilities	308	308	295	295
Net assets	716	285	679	259

Statement of Comprehensive Income – Consolidated

Expenses

In 2017-18 total expenses increased by $49 million to $911 million.

Staff benefit expenses

Staff benefit expenses increased by $30 million to $551 million mainly due to:

- an increase in salaries and wages of $20 million to $446 million
- an increase in long service leave expense of $8 million to $16 million due to the impact of actuarial assessments of the associated liability in 2016-17 and 2017-18.

Staff benefit expenses represent 60% of CHSALHN's total expenses. The number of employees whose remuneration received/receivable exceeded base executive level ($149 000) totalled 122 (132), comprising 67 (65) medical (excluding nursing), 37 (52) nursing, 14 (12) executive and four (three) non-medical employees. Total remuneration for these employees was $32 million ($36 million).

Supplies and services expenses

Supplies and services expenses increased by $16 million to $319 million.

Significant components of supplies and services were:

- fee-for-service payments to medical practitioners – $86 million ($75 million). Contributing to the increase were increased locum costs, $5 million, and increased rates for fee-for-service of $2 million
- medical, surgical and laboratory supplies – $46 million ($43 million)
- contractors – agency staff – $10 million ($14 million)
- patient transport – $20 million ($19 million)
- repairs and maintenance – $27 million ($25 million).

Revenues

Revenues from SA Government

CHSALHN is principally funded by DHW. In 2017-18, funding of $661 million comprised recurrent funding of $651 million and capital funding of $10 million.

Statement of Financial Position – Consolidated

Property, plant and equipment

Property, plant and equipment represents 85% of CHSALHN's total assets. The carrying value of

property, plant and equipment increased by $37 million to $866 million. This increase was primarily due to:

- a $61 million valuation increment resulting from an independent revaluation of land and buildings as at 1 June 2018. Notes 19 and 22 of CHSALHN's financial report provides further information on the valuation
- additions of $11 million including capital work in progress of $9 million
- depreciation and amortisation of $34 million.

Liabilities

Current liabilities of $195 million exceeded current assets of $151 million at balance date.

Cash and cash equivalents of $35 million were not sufficient to meet current payables of $38 million. CHSALHN is funded to meet expected cash flows for its current program delivery.

Staff related liabilities make up $181 million of CHSALHN's total liabilities at 30 June 2018, comprising:

- staff benefits liabilities and related on-costs, $172 million ($161 million)
- provisions for workers compensation, $9 million ($14 million).

Note 26 of CHSALHN's financial report provides further information on the independent actuarial assessments of provisions for workers compensation, including that there is a high level of uncertainty as to their valuation.

Northern Adelaide Local Health Network Incorporated (NALHN)

Financial statistics

Total expenses:	$684 million
Net cost of providing services:	$647 million
Revenues from SA Government:	$627 million
Staff benefits liability and related on-costs:	$137 million
Workers compensation liability:	$6 million
Number of FTEs:	3583.3

Significant events and transactions

— In February 2018 the Independent Commissioner Against Corruption published his report on the Oakden Older Persons Mental Health Facility, a part of NALHN. Titled 'Oakden: A Shameful Chapter in South Australia's History', the report made findings against NALHN, which was found to have engaged in maladministration in public administration.

— Northgate House, which opened after Oakden was closed, was accredited by the Australian Council on Healthcare Standards in July 2018.

— An independent revaluation of land and buildings as at 1 June 2018 resulted in a $16 million valuation increment.

— Due to the continuing reconfiguration of health services, 151.5 staff moved from the Central Adelaide Local Health Network Incorporated to NALHN in 2017-18 – 79.2 nursing FTEs, 17.6 medical officer FTEs and 54.7 administrative FTEs.

— The *Health Care (Governance) Amendment Act 2018* was proclaimed in August 2018 and will be operational from 1 July 2019. It changes governance arrangements, including that NALHN will be governed by a board from that date.

Financial report opinion

Unmodified

Financial controls opinion	**Modified**
	Key issues: — Inadequate review of payroll information — Improvements needed in how allowances are managed — Patient billing processes can be improved — Contracts were not established for some regular services — Some duplicate invoices were paid and there was inadequate matching of invoices to purchase orders — Management of professional development leave can be improved

Functional responsibility

NALHN is established under the *Health Care Act 2008*.

The powers and functions of NALHN are to establish, provide, maintain and enhance hospital, medical and allied health services in its local area.

Under the *Health Care Act 2008* the Chief Executive, Department for Health and Wellbeing (DHW) assumes direct responsibility for administering incorporated hospitals. This includes appointing the Chief Executive Officer of NALHN. The Chief Executive, DHW cannot give a direction about a person's clinical treatment.

Governance changes

The new SA Government has announced its intention to amend governance arrangements across SA Health. The first part of these changes was completed in August 2018 when the *Health Care (Governance) Amendment Act 2018* was proclaimed and will operate from 1 July 2019.

The amendments abolished the former function of the Chief Executive, DHW to assume direct responsibility for the administration of incorporated hospitals. The amendments provide for NALHN to be governed by a board. The SA Government intends the board will be fully operational by 1 July 2019.

The SA Government has stated it will establish a new governance and accountability framework for the public health system that will be reflected in legislation to be introduced into Parliament later in 2018 or early next year.

Scope of audit

The audit program covered major financial systems to obtain sufficient evidence to form an opinion on the financial report and internal controls. Financial services for NALHN are provided through a mix of:

- central services provided by DHW through an integrated finance service model
- finance services located within NALHN
- services provided by Shared Services SA (SSSA).

NALHN continues to operate some DHW legacy systems. Consequently, our audit included the review of new and legacy systems and completing audit work at DHW's central services, NALHN and SSSA.

Audit findings across health services fall into the following categories:

- common findings reflecting central services and/or systems
- matters for individual health services
- SSSA matters
- governance.

Specific areas of audit attention in 2017-18 included:

- governance
- payroll, medical officer allowances and rostering practices
- expenditure and accounts payable
- property, plant and equipment
- patient billing
- medical officer professional development
- cash and online banking
- medical, surgical and laboratory supplies inventory
- general ledger and financial accounting.

Review of the financial management compliance program was addressed through the audit of DHW.

Internal audit activities were reviewed to assess the risks of material misstatement in the financial report and to design and perform audit procedures.

Audit findings and comments

Assessment of controls

In my opinion, the controls exercised by the Northern Adelaide Local Health Network Incorporated in relation to the receipt, expenditure and investment of money, the acquisition and disposal of property and the incurring of liabilities, except for all matters outlined under 'Communication of audit matters', are sufficient to provide reasonable assurance that the financial transactions of the Northern Adelaide Local Health Network Incorporated have been conducted properly and in accordance with law.

Communication of audit matters

Matters identified by the audit were detailed in management letters to the interim Chief Executive Officer, NALHN and copied to the Chief Executive, DHW. SSSA matters were reported to the Chief Executive, Department of the Premier and Cabinet.

A summary of our findings for centralised processes performed by DHW and SSSA can be found in the section of this Report titled 'Department for Health and Wellbeing' under the heading 'Communication of audit matters'. The main matters raised in our audit of NALHN are detailed below.

Inadequate review of payroll information

Payroll related costs for NALHN are significant, with $463 million in staff benefits paid in 2017-18 and $137 million in staff benefit liabilities and related on-costs as at 30 June 2018. Payroll controls are therefore a key focus of our audit each year.

Bona fide reports and leave return certificates not reviewed for auto-pay staff

NALHN implemented bona fide report and leave return certificates for the review of employee level payroll information for auto-pay staff in 2017-18. These controls cover approximately 37% of NALHN's total payroll. While this was a positive improvement in the control environment, we found that only 47% of bona fide reports and 37% of leave return certificates had been reviewed and approved between November 2017 and March 2018.

NALHN responded that it would send a memo to all Divisional Directors and Managers reminding them of their responsibility to review and approve bona fide reports and leave return certificates within the required time frames by December 2018. A procedure would also be developed to cover processes for monitoring these controls and escalating approvals.

No regular review of employee level payroll information for non-auto pay staff

While NALHN implemented reviews of employee level payroll information for auto-pay staff in 2017-18, these controls do not extend to non-auto pay staff. Consistent with prior years, there was no regular process to review the validity, accuracy and completeness of pay information for these staff.

Failure to ensure payroll information is valid, accurate and complete may result in fraudulent or incorrect payments.

NALHN advised it would partner with SSSA to investigate whether non-auto pay staff could all be accommodated on the ProAct rostering and time recording system. NALHN advised this process would be undertaken by June 2019.

Nurses' timesheets were not always approved prior to payment

The ProAct system is used to initiate payroll payments to nurses across the various areas of NALHN. We found that ProAct timesheets were not always approved prior to submission to SSSA for processing into the Chris21 payroll system. Our analysis revealed that 1698 (4%) of all timesheets processed between July 2017 and March 2018 had not been authorised. Processing unauthorised timesheets into Chris21 increases the risk that staff are paid for hours not worked.

NALHN responded that it would create a report to identify month-on-month and year-to-date unauthorised ProAct timesheets by December 2018. NALHN also advised a memo would be sent to all Divisional Directors and Managers reminding them of their responsibility to review all unauthorised or modified ProAct timesheets prior to payment.

Inconsistent medical rostering practices across divisions

We reviewed medical rostering practices and noted there were inconsistent approaches across the three divisions we sampled. As there was no rostering system for medical officers, and no central training for staff preparing rosters, varying local practices had developed. The inconsistencies in rostering approaches increase the risk of different interpretations of complex enterprise agreements emerging between divisions.

NALHN advised it would partner with SSSA to investigate whether non-auto pay staff could all be accommodated on the ProAct rostering and time recording system. NALHN advised this process would be undertaken by June 2019, with SSSA helping to develop a project plan for ProAct to be rolled out more widely.

NALHN advised that any roll-out project would include the development of project tools and staff education packages regarding the use of the system.

Improvements needed in how allowances are managed

Recall allowances are a significant feature of total payroll for NALHN, accounting for $4.7 million in 2017-18.

Recall allowances are not consistently reviewed for accuracy and some were unsubstantiated

Our review of recall allowances paid in 2017-18 identified the degree of review for recall allowances varied according to divisions and individual payments. There was no consistent practice of reviewing these allowances for accuracy. As a result, there is a risk that NALHN is paying recall allowances in circumstances where they should not be paid.

SA Health policy requires a range of information to be recorded on a medical officer’s timesheet to support recall allowances. This information is required to validate the accuracy of the recall. We identified five examples, from a sample of 15, that did not meet these SA Health policy requirements but were still paid.

NALHN advised that it would develop and implement a procedure for reviewing and substantiating recall allowance claims and payments by December 2018.

Recalls performed at other local health networks (LHNs) not validated

We noted many medical officers’ timesheets included recalls for work performed at other LHNs. These recall amounts are paid by NALHN, although no verification of these recall allowances was undertaken.

As noted above, NALHN advised it aimed to have a procedure for the review of all recall allowances, including those performed at other LHNs, in place by December 2018.

Medical officer on-call allowances were not reviewed and were not always consistent with actual rostering frequency

The SA Health Medical Officers Enterprise Agreement 2017 states that a consultant, other than a casual employee, who participates in a regular on-call roster will be paid an annual allowance based on their annual salary and the frequency of the on-call arrangements.

We found that NALHN did not have a consistent process in place to ensure these allowances were reviewed. We also identified an instance where a medical officer's actual rostering frequency differed from their on-call allowance in Chris21, resulting in an approximate overpayment of $4000 for the eight months ended February 2018.

NALHN responded that a six-monthly process to review on-call percentages against rosters to ensure the correct rates were applied in Chris21 would be implemented by December 2018, along with procedures to support it.

Patient billing processes can be improved

NALHN received $17.4 million in patient fees and charges in 2017-18. Patient fees include, among others, compensable revenue amounts that are recoverable through compulsory third party arrangements for motor vehicle accidents, or through the Return to Work Corporation of South Australia for workplace related injuries.

Ineffective identification of compensable charges

We reviewed the processes implemented by NALHN to ensure all compensable revenue was identified at the Lyell McEwin Hospital and Modbury Hospital outpatient clinics, and the Lyell McEwin Hospital emergency department. We found that processes to identify compensable visits varied significantly and that there was potential for compensable revenue activity not to be identified. For example, we observed either no or limited enquiries were made with visiting outpatients to determine whether their appointment related to a compensable injury claim.

NALHN advised it would develop a procedure to educate and train outpatient clinic reception staff on the importance of confirming the compensable status of each appointment by March 2019.

Patient billing reviews were not completed or were not evidenced

We reviewed inpatient and outpatient billing processes and identified that some key reports used to ensure the completeness of revenue had either not been reviewed (for some outpatient activity) or there was no evidence of the review process performed for more than 12 months (for some inpatient activity). Gaps in these review processes raise the potential of financial loss for NALHN in a financial environment already under significant budgetary pressure.

NALHN responded that the review of outpatient and inpatient billing reporting would be spread evenly across three revenue supervisors to ensure the continual review of reporting by March 2019. Procedures would also be updated to require revenue supervisors to maintain evidence of their review on file.

Expenditure and accounts payable

NALHN paid $193 million for supplies and services in 2017-18. A large proportion of these expenses are approved for payment using online approval functions in SA Health's key financial systems, Oracle and Basware.

Contracts were not established with significant suppliers

We found that NALHN had not entered into contracts with four suppliers who were paid in excess of $4.5 million between July 2017 and February 2018. The absence of contracts for significant expenditure increases the risk of inaccurate or disputed charges and payments.

NALHN advised that two of the identified suppliers had recently been subject to an SA Health Procurement and Supply Chain Management (PSCM) tender process which was close to finalisation.

The remaining two contracts were not part of any planned tender process. However, NALHN advised that the PSCM forward procurement plans indicate that state-wide tendering for the services associated with these contracts would occur in the future.

Inadequate matching of invoices to Oracle purchase order receipts

Consistent with prior years, we found that, as at 31 March 2018, 578 purchase order receipts over 40 days old had not been matched to an invoice. These invoices totalled more than $349 000. While it was likely that NALHN had paid the associated invoices, failure to match invoices when goods/services are received increases the risk that payments are made for goods/services not received, or at a price that is inconsistent with the purchase order price.

NALHN responded that by August 2018 PSCM would be engaged to provide ongoing training to requisitioners and approvers across NALHN. Training would be supported by periodic reviews of long outstanding open purchase orders.

Duplicate invoices processed and paid

Our analysis of NALHN's invoice data identified 385 pairs of high risk potential duplicate invoices. Our review of 10 of these pairs identified seven duplicate invoice pairs. These were confirmed to be duplicates by NALHN.

NALHN responded that it would look to improve controls to limit duplicate payments, although it did not believe that its current control environment was ineffective in preventing and identifying material overpayments, and that processes had been established to recoup these overpayments.

Management of professional development leave can be improved

SA Health salaried medical officers are entitled to up to 10 days of professional development leave a year.

No central record of professional development leave entitlements

As we have found in the past, there remains no central record of professional development leave entitlements for medical officers. The absence of a central record of leave balances results in divisions

maintaining, in some cases, multiple leave records. This results in leave approval without reference to remaining leave entitlements.

NALHN advised that a project led by DHW, with all LHNs participating, aimed to develop a central system for the recording, approval and monitoring of professional development leave and expenditure, with substantial development completed by May 2019. In the interim, a memo would be sent to Divisional Directors reminding them of their responsibility to ensure adequate leave balances existed prior to approving leave. Divisional Directors would also be reminded to monitor this leave until a central system was operational.

Staff taking more professional development leave than they were entitled to

We identified five medical officers from our testing who had, according to Chris21 records, taken more professional development leave than they were entitled to over the past two years.

NALHN advised it will investigate all instances to verify the explanation for the excessive leave by May 2019.

Interpretation and analysis of the financial report

Highlights of the financial report*

	2018 $'million	2017 $'million
Expenses		
Staff benefit expenses	463	414
Supplies and services	193	172
Depreciation and amortisation expense	28	27
Other expenses	-	3
Total expenses	684	616
Income		
Revenue from fees and charges	27	26
Grants and contributions	3	3
Other income	7	5
Total income	37	34
Net cost of providing services	647	582
Revenues from SA Government	627	572
Net result and total comprehensive result	(20)	(11)
Assets		
Current assets	38	29
Non-current assets	438	441
Total assets	476	470
Liabilities		
Current liabilities	80	74
Non-current liabilities	77	73
Total liabilities	157	147
Net assets	319	323

* Table may not add due to rounding.

Statement of Comprehensive Income

Expenses

In 2017-18 total expenses increased by $68 million (11%) to $684 million.

Staff benefit expenses

Staff benefit expenses of $463 million represent 68% of NALHN's total expenses. These costs have increased by $49 million which is mainly attributable to:

- a 2017-18 move of staff from the Central Adelaide Local Health Network Incorporated to NALHN of 79.2 nursing FTEs, 17.6 medical officer FTEs and 54.7 administrative staff FTEs – $19.5 million
- CPI salary and allowance increases following the successful finalisation of the SA Health Medical Officers Enterprise Agreement 2017, which includes nursing staff – $13 million
- an increase of $10 million in long service leave expenditure associated with the actuarially assessed revaluation of the liability conducted for 30 June 2018.

The number of staff whose remuneration received/receivable exceeded base executive level ($149 000) totalled 380 (335), comprising 338 (300) medical officers, six (four) executives, 34 (29) nursing staff and two (two) non-medical staff. Total remuneration of these staff was $108 million ($95 million).

Supplies and services

Supplies and services expenditure increased by $21 million (12%) in 2018 to $193 million. Significant components of supplies and services were:

- medical, surgical and laboratory supplies, which increased by $7.1 million (14%) to $57.9 million. The increase is mainly attributable to the increased cost of prosthesis and implants ($3.4 million), imaging recharges ($2.5 million) and increases in radiology charges ($500 000)
- contractors – agency staff, which increased by $4.6 million (35%) to $17.7 million. This increase is mainly attributable to rises in nursing agency staff demand due to staff shortages and vacancy rates. Notable increases included registered nurses ($2.4 million), nursing personal care assistants ($328 000) and undergraduate nursing students ($822 000)
- security, which has increased by $2.4 million (39%) to $8.4 million. This is mainly due to increases in the cost of security services, additional security for the Oakden site and an increased security presence at both NALHN emergency departments.

Revenues

Revenues from SA Government

NALHN is principally funded through recurrent and capital funding from DHW. In 2018, NALHN received recurrent funding of $619.3 million and capital funding of $8.1 million mainly for the finalisation of the Modbury Hospital and Lyell McEwin Hospital (Stage C) Transforming Health redevelopments.

Recurrent funding increases were largely driven by additional DHW appropriations required to meet increases in costs from other SA Health entities paid by NALHN and as a result of increased activity due to the reconfiguration of health services.

Statement of Financial Position

Property, plant and equipment

Property, plant and equipment assets represent 92% of total assets.

The carrying value of property, plant and equipment decreased by $3.9 million to $436 million. The decrease was mainly attributable to a revaluation increment of $16.2 million, as well as $7.7 million in additions, being mainly offset by depreciation expenditure of $27.9 million.

Liabilities

Current liabilities increased by $6 million to $80 million during the year and exceeded current assets of $38 million at 30 June 2018. NALHN works with DHW to ensure sufficient funding is provided to NALHN to meet expected cash flows for its administration and program delivery. Cash and cash equivalents of $28 million are sufficient to meet current payables of $20 million.

Staff liabilities make up $142 million (91%) of NALHN's total liabilities at 30 June 2018, comprising:

- staff benefits liabilities and related on-costs of $137 million ($124 million)
- workers compensation provisions of $5 million ($8 million).

The increase in staff liabilities is mainly the result of a $6 million increase in non-current long service leave as a consequence of an actuarially assessed revaluation of the liability conducted for 30 June 2018, which included an increase in the estimated retirement age and additional staff who had moved from CALHN.

This increase was partially offset by a reduction in the non-current provision for workers compensation of $1.4 million (29%) as a consequence of an actuarially assessed revaluation of the liability as at 30 June 2018.

Further commentary on operations

Changes to NALHN's Older Persons Mental Health approach in 2017-18

At the time of my Report last year, the Independent Commissioner Against Corruption had announced a maladministration investigation into the Oakden Older Persons Mental Health Facility in May 2017. His report, 'Oakden: A Shameful Chapter in South Australia's History', was released in February 2018. One of the findings of that report was that NALHN, as a corporate entity, had committed maladministration in public administration in relation to the management of the Oakden facility.

All residents were moved out of the Oakden facility by the end of September 2017.

NALHN continued to provide older persons mental health services following the closure of Oakden, most notably through services provided at Northgate House. Northgate House has the capacity for 16 residents and was used to transfer some of the former residents of Oakden.

While Oakden was formerly operated as a Commonwealth accredited aged care facility, Northgate House is run as a health facility and is not an accredited aged care facility.

Northgate House received full accreditation from the Australian Council on Healthcare Standards for three years in July 2018.

The Oakden facility continues to form part of NALHN's assets as at 30 June 2018. The future use of this site, whether by NALHN or SA Health more broadly, had not been determined at the time of this Report.

SA Ambulance Service Inc (SAAS)

Financial statistics

Total expenses:	$315 million
Net cost of providing services:	$175 million
Revenues from SA Government:	$165 million
Staff benefits liability and related on-costs:	$110 million
Workers compensation liability:	$15 million
Number of FTEs:	1480

Significant events and transactions

- SAAS led the move of inpatients to the new Royal Adelaide Hospital in September 2017.
- An independent revaluation of land and buildings as at 1 June 2018 resulted in a $28 million valuation increment.
- MedSTAR employees who were previously paid by the Central Adelaide Local Health Network Incorporated and recognised as contracted agency staff transferred to SAAS.
- A new non-statutory workers compensation provision added $9 million to liabilities. There is a high level of uncertainty in the value because of the lack of claims experience.

Financial report opinion

Unmodified

Financial controls opinion

Modified

Key issues:

- Improvements are needed to confirm the accuracy and completeness of timesheets submitted
- Financial authorities in the payment system did not always match delegations
- Improvements are necessary to ensure transport charges are completely and accurately raised

Functional responsibility

SAAS is a body corporate constituted under the *Health Care Act 2008.*

SAAS is the principal provider of ambulance services in South Australia. It delivers:

- out of hospital emergency care and transport
- non-emergency patient care and transport
- emergency and major event management
- medical retrieval services.

Under the *Health Care Act 2008* the Chief Executive, Department for Health and Wellbeing (DHW) assumes direct responsibility for administering SAAS. This includes appointing the Chief Executive Officer of SAAS. The Chief Executive, DHW cannot give a direction about a person's clinical treatment.

The SA Government has stated it will establish a new governance and accountability framework for the public health system which will be reflected in legislation to be introduced into Parliament later this year or early next year.

Scope of the audit

The audit program covered major financial systems to obtain sufficient evidence to form an opinion on the financial report and internal controls.

Financial services for SAAS are provided through a mix of:

- central services provided by DHW through an integrated finance service model
- finance services located within SAAS
- services provided by Shared Services SA (SSSA).

Our audit included the review of new and legacy systems and completing audit work at DHW's central services, SAAS and SSSA.

Audit findings across health services fall into the following categories:

- common findings reflecting central services and/or systems
- matters for individual health services
- SSSA matters.

A Chartered Accounting firm assisted the Auditor-General in the audit of SAAS.

Specific areas of audit attention in 2017-18 included:

- payroll
- accounts payable
- revenue
- accounts receivable
- property, plant and equipment

- cash
- general ledger.

Internal audit activities were considered in designing and performing audit procedures.

Audit findings and comments

Assessment of controls

In my opinion, the controls exercised by the SA Ambulance Service Inc in relation to the receipt, expenditure and investment of money, the acquisition and disposal of property and the incurring of liabilities, except for all matters outlined under 'Communication of audit matters', are sufficient to provide reasonable assurance that the financial transactions of the SA Ambulance Service Inc have been conducted properly and in accordance with law.

Communication of audit matters

Matters identified by the audit were detailed in a management letter to the Chief Executive Officer of SAAS and copied to the Chief Executive, DHW. The main matters raised and related responses are detailed below.

A summary of our findings for centralised processes performed by DHW can be found in the section of this Report titled 'Department for Health and Wellbeing' under the heading 'Communication of audit matters'.

Revenue

Improvements necessary to ensure transport charges are completely and accurately raised

SAAS runs legacy revenue systems that require considerable manual processing, including manual card records and associated data entry. Our review of these processes found improvements are necessary to ensure:

- management raises invoices for all relevant dispatches
- data is completely and accurately interfaced between its dispatch and invoicing systems.

Similar concerns were raised last year. SAAS responded that its project team had developed processes to ensure the completeness of revenue. It expects to implement them by October 2018.

Improvements necessary to ensure the validity of changes made to patient transport charges

Our review of revenue resulted in the following recommendations to ensure the validity of changes made to patient transport charges:

- prevent billing officers from amending invoice details such as number of kilometres and fees charged per kilometre
- ensure all adjustments to revenue information are independently reviewed.

SAAS responded that it would quality review invoice details such as number of kilometres entered, the call out fee, and the fee charged per kilometre.

Invoice system not regularly reconciled to the general ledger

Our review found SAAS had not regularly reconciled its invoicing system to its general ledger to ensure revenue information was completely and accurately recorded in the general ledger and financial reports. SAAS responded that it would ensure the reconciliation is completed on a timely basis.

System user access rights not regularly reviewed

We recommended SAAS regularly review user access rights to its invoice system to ensure access levels are compatible with job functions. SAAS responded with its intention to implement a regular review by October 2018.

Supplies and services expenditure

Purchase orders created outside of mandated financial system

SA Health's requisition, purchase order and invoice management policy mandates that purchase orders be created in the Oracle financial system. Consistent with concerns we reported last year, we found that the fleet services team raises manual, Excel-based purchase orders that do not benefit from the system-based controls built into Oracle.

SAAS responded that it would work with its fleet services area and the SA Health procurement team to review alternatives for where urgent purchases are required.

Financial authorities in the payment system did not always match delegations

Our review of financial authorities assigned to users in the Basware payment authorisation system noted instances where they did not match the authorities in the Chief Executive Officer's instrument of delegation. Consequently, invoices may be paid without the required authority and outside of Treasurer's Instructions requirements. SAAS agreed with our recommendation to regularly review the financial authorities in Basware to the instrument of delegation.

Invoices received are not always matched to purchase orders

Our review of payments noted instances where invoices were not matched to purchase orders prior to payment. Where this occurs there is an increased risk that payments may be made for goods or services not received or not at the agreed price. In addition the associated expense records may be overstated. This has been raised for a number of years.

SAAS's response indicated that as this was an SA Health-wide issue it would work with central teams to find a system-based solution. It indicated that in the interim it would continue to educate staff on processing invoices related to Oracle purchase orders.

Documentation supporting new purchase cards requires improvement

Our review of forms supporting the issue of purchase cards found instances where:

- an approved delegate did not sign to approve the use of a purchase card

- cardholders' declarations were missing or not signed
- receipt of the card was not signed by the cardholder.

SAAS responded that it would action our recommendations to ensure cards are only issued where approved by an authorised delegate and that cardholders complete and sign the declarations required by Treasurer's Instruction 12 'Government Purchase Cards'.

Payroll

Improvements needed to confirm the accuracy and completeness of timesheets submitted

Operational staff are paid two weeks in advance based on their contracted hours and roster cycle. Penalties, overtime hours and leave are processed in the payroll system only once a manual timesheet is provided to SSSA. Our review noted the following opportunities to improve timesheet processing:

- there were no processes in place to ensure all timesheets are received for processing
- there were no processes in place to ensure team leaders follow up timesheet errors
- there were 67 instances of staff members submitting five or more timesheets at the same time. The greatest number of timesheets lodged by a staff member at one time was 38
- management did not validate certain types of overtime and allowances recorded on manual timesheets.

SAAS responded with its intention to interface its roster system with its payroll system which would address some of the issues and risks identified above. It indicated it was developing a business case and consulting with SAAS Workforce and SSSA. It also responded that an internal audit, which had commenced, would help to identify actions to address the concerns raised by our audit.

Insufficient review of payroll information

Consistent with last year, we found SAAS supervisors or team leaders did not always review payroll reports to ensure the accuracy and completeness of staff payments. In November 2017 a bona fide report process was introduced whereby managers and team leaders log into the payroll system and review a report to confirm the bona fide nature of employees paid. We found SAAS did not follow up managers and team leaders who had not completed the review. At the time of the audit we found that 279 out of 740 bona fide reports were not approved.

Failure to ensure payroll information is valid and accurate may result in fraudulent or incorrect payments.

SAAS responded that it was reinforcing with its managers their responsibilities to review the reports. It also indicated it was exploring options to escalate outstanding reports.

Shared Services SA – financial systems and transactions processing environments

SSSA processes financial transactions on behalf of SAAS. The main systems and control environments include accounts payable and payroll financial functions.

Our review and evaluation of controls for these systems conclude that the controls were effective for 2017-18. SSSA is discussed further in the commentary under 'Department of the Premier and Cabinet' in this Report.

Interpretation and analysis of the financial report

Highlights of the financial report

	2018 $'million	2017 $'million
Expenses		
Staff benefit expenses	220	194
Supplies and services	63	71
Depreciation and amortisation expense	13	11
Other expenses	19	20
Total expenses	315	296
Income		
Revenue from fees and charges	129	126
Other income	11	9
Total income	140	135
Net cost of providing services	175	161
Revenues from SA Government	165	150
Net result	(10)	(11)
Other comprehensive income	31	40
Total comprehensive result for the year	21	29
Assets		
Current assets	34	37
Non-current assets	138	97
Total assets	172	134
Liabilities		
Current liabilities	64	62
Non-current liabilities	69	54
Total liabilities	133	116
Net assets	39	18

Statement of Comprehensive Income

Expenses

In 2017-18 total expenses increased by $19 million (6%) to $315 million. This was due mainly to a $26 million increase in staff related expenses, a $2 million increase in depreciation and amortisation and a $9 million decrease in supplies and services.

Staff benefit expenses

Staff benefit expenses of $220 million represented 70% of SAAS's total expenses.

Salaries and wages rose $14 million (9%) to $158 million. Contributing to the increase was $6 million for MedSTAR employees who were previously paid by the Central Adelaide Local Health Network Incorporated (CALHN) and recognised as contracted agency staff.

Long service leave expense increased by $7 million to $10 million mainly due to the impact of changed actuarial assumptions used to estimate the associated liability, including predicted wage growth and the impact of increased liability for MedSTAR employees.

The number of staff whose remuneration received/receivable exceeded the base executive level ($149 000) totalled 388 (475) comprising 356 (465) operational, 20 (0) medical, eight (nine) executive and four (one) administration staff. The decrease in operational staff exceeding the base level executive level was partly caused by significant back pays to those staff last year. The increase in medical staff was caused by MedSTAR staff reclassified from contracted agency staff. Total remuneration for staff across the categories was $72 million ($86 million).

Supplies and services expenses

Supplies and services expenses decreased by $9 million to $63 million. Significant components of supplies and services were:

- contractors – agency staff – $5 million ($16 million). The decrease mainly relates to $10 million for MedSTAR staff included in 2016-17 as contractors (recharged from CALHN) who are now paid through employee benefits
- patient transport – $18 million ($17 million)
- motor vehicle expenses – $5 million ($5 million)
- medical, surgical and laboratory supplies – $4 million ($4 million)
- communication – $3 million ($3 million).

Revenues

Revenues from SA Government

SAAS is dependent on revenue from the SA Government which comprises 54% of total revenue.

In 2017-18 total revenues from DHW increased by $16 million to $165 million and comprised recurrent funding of $137 million and capital funding of $28 million.

Capital funding was primarily for construction of new stations and a rescue retrieval and aviation base and the purchase of ambulances, stretchers and loaders.

Revenues from fees and charges

Revenues from fees and charges increased by $3 million to $129 million. Significant components of revenues from fees and charges were:

- ambulance cover – $27 million ($25 million)

- ambulance transport – $94 million ($93 million).

Ambulance cover revenue is from member subscriptions to the SAAS ambulance cover scheme to cover against the cost of ambulance transport. Ambulance transport revenue is earned from patient transport services to the general public, $67 million, and local health networks, $27 million.

Statement of Financial Position

Property, plant and equipment

Property, plant and equipment represents 80% of SAAS's total assets. The carrying value of property, plant and equipment increased by $42 million to $136 million. This increase was primarily due to:

- a $28 million valuation increment resulting from an independent revaluation of land and buildings as at 1 June 2018
- $25 million in additions to capital work in progress which mainly relate to construction of new stations, a rescue retrieval and aviation base and the purchase of ambulances, stretchers and loaders
- depreciation and amortisation of $12 million.

Liabilities

Staff liabilities make up $125 million (94%) of SAAS's total liabilities at 30 June 2018, comprising:

- staff benefits liabilities and related on-costs, $110 million ($96 million)
- provision for workers compensation, $15 million ($10 million).

Staff benefits liabilities increased significantly by $12 million to $104 million due mainly to:

- a $6 million increase in long service leave liabilities. Contributing to this was a $1.4 million increase in liabilities for MedSTAR employees recognised for the first time and the impact of changed actuarial assumptions relating to predicted salary inflation causing an increase of $3 million
- a $4 million increase in annual leave liabilities.

Provisions for workers compensation increased by $5 million to $15 million. Workers compensation provisions are based on independent actuarial assessments. The provisions included non-statutory provisions for certain work related injuries as part of enterprise bargaining arrangements and industrial awards introduced in 2017-18. As at 30 June 2018 SAAS recognised a workers compensation non-statutory provision of $9 million for the first time. There is a high level of uncertainty about the value of the provision because of the absence of claims experience. Note 24.1 of SAAS's financial report provides information on the actuarial assessment.

Current liabilities, $64 million, exceeded current assets, $34 million, at 30 June 2018. SAAS is funded to meet expected cash flows for its current program delivery. Note 1.5 of the financial report provides information about the continuity of operations.

Southern Adelaide Local Health Network Incorporated (SALHN)

Financial statistics

Total expenses:	$1070 million
Net cost of providing services:	$994 million
Revenues from SA Government:	$996 million
Staff benefits liability and related on-costs:	$239 million
Workers compensation liability:	$39 million
Number of FTEs:	5473

Significant events and transactions

- The Repatriation General Hospital (RGH) was closed and decommissioned on 9 November 2017 with the last patients moved to new SALHN facilities.
- Following the State election in March 2018, the contract to sell the RGH to the Aged Care and Housing Group Incorporated was officially terminated in May 2018.
- As the first step in reopening the RGH as a health precinct, the hydrotherapy pool was reopened in May 2018.
- An expression of interest for 'Reactivating the Repat Health Precinct' was released in August 2018 seeking submissions from the private sector and non-government organisations interested in partnering with SA Health to deliver a variety of health focused services at the RGH site.
- An independent revaluation of land and buildings as at 1 June 2018 resulted in an $83 million revaluation increment.
- A new rehabilitation building, a new older persons mental health facility and a new multi-deck car park were completed at the Flinders Medical Centre in 2017-18.
- SALHN continued to experience turnover in key executive positions, with a new Chief Executive Officer commencing on 26 February 2018.
- The *Health Care (Governance) Amendment Act 2018* was proclaimed in August 2018 and will be operational from 1 July 2019. It changes governance arrangements, including that SALHN will be governed by a board from that date.

Financial report opinion	**Unmodified**
Financial controls opinion	**Modified** Key issues: — Inadequate review of payroll information and leave management reports — No process to ensure all medical officers' timesheets are approved and submitted — Nurses' timesheets were not always approved prior to payment — Allowances paid to staff were not always reviewed. — Delegations in key financial systems were not always consistent with the approved financial delegations — Contracts not established with some significant suppliers — No complete review of EPAS user access was performed — Weaknesses in hospital billing — Control weaknesses around the completeness of private practice income — Management of professional development entitlements needs to improve

Functional responsibility

SALHN is established under the *Health Care Act 2008*.

The powers and functions of SALHN are to establish, provide, maintain and enhance hospital, medical and allied health services in its local area.

Under the *Health Care Act 2008* the Chief Executive, Department for Health and Wellbeing (DHW) assumes direct responsibility for administering incorporated hospitals. This includes appointing the Chief Executive Officer of SALHN. The Chief Executive, DHW cannot give a direction about a person's clinical treatment.

Governance changes

The new SA Government has announced its intention to amend governance arrangements across SA Health. The first part of these changes was completed in August 2018 when the *Health Care (Governance) Amendment Act 2018* was proclaimed and will operate from 1 July 2019.

The amendments abolish the former function of the Chief Executive, DHW to assume direct responsibility for the administration of incorporated hospitals. The amendments provide for SALHN to be governed by a board. The SA Government intends the board to be fully operational by 1 July 2019.

The SA Government has stated it will establish a new governance and accountability framework for the public health system that will be reflected in legislation to be introduced into Parliament later in 2018 or early next year.

Scope of the audit

The audit program covered major financial systems to obtain sufficient evidence to form an opinion on the financial report and internal controls.

Financial services for SALHN are provided through a mix of:

- central services provided by DHW through an integrated finance service model
- finance services located within SALHN
- services provided by Shared Services SA (SSSA).

SALHN continued to operate a legacy revenue system at the Flinders Medical Centre (FMC). Consequently, our audit included the review of new and legacy systems and completing audit work at DHW's central services, SALHN and SSSA.

Audit findings across health services fall into the following categories:

- common findings reflecting central services and/or systems
- matters for individual health services
- SSSA matters.

Specific areas of audit attention in 2017-18 included:

- governance
- payroll, including medical officer allowances
- expenditure and accounts payable
- professional development entitlements
- patient billing
- cash and online banking
- medical, surgical and laboratory supplies inventory
- general ledger
- property, plant and equipment
- infrastructure changes.

Review of the financial management compliance program was addressed through the audit of DHW.

Internal audit activities were reviewed to assess the risks of material misstatement in the financial report and to design and perform audit procedures.

Audit findings and comments

Auditor's report on the financial report

Assessment of controls

In my opinion, the controls exercised by the Southern Adelaide Local Health Network Incorporated in relation to the receipt, expenditure and investment of money, the acquisition and disposal of property and the incurring of liabilities, except for all matters outlined under 'Communication of audit matters', are sufficient to provide reasonable assurance that the financial transactions of the Southern Adelaide Local Health Network Incorporated have been conducted properly and in accordance with law.

Communication of audit matters

Matters identified by the audit were detailed in management letters to the Chief Executive Officer, SALHN and copied to the Chief Executive, DHW. SSSA matters were reported to the Chief Executive, Department of the Premier and Cabinet.

A summary of our findings for centralised processes performed by DHW and SSSA can be found in the section of this Report titled 'Department for Health and Wellbeing' under the heading 'Communication of audit matters'. The main matters raised in our audit of SALHN are detailed below.

Payroll

Payroll related costs for SALHN are significant, with $736 million in staff benefit expenses paid in 2017-18 and $223 million in staff benefit liabilities at 30 June 2018. Payroll controls are therefore a key focus of our audit each year.

No regular review of payroll information by SALHN

Consistent with prior years, we found SALHN did not have a mechanism to ensure employee-level pay information in the payroll system was valid and accurate. At the time of our review, the Chris21 payroll system could not reliably generate bona fide reports for SALHN.

While there were pre-processing checks in place to validate payments before they were processed, there were no processes in place to ensure the information processed by the payroll system was valid and accurate.

We consider the failure to ensure payroll information is valid and accurate may result in fraudulent or incorrect payments, resulting in a financial loss to SALHN or additional processing costs where overpayments occur and/or manual payments are required.

SALHN advised that, following the audit, bona fide reports were implemented for 370 of its staff. SALHN responded that the remaining staff who were paid automatically each fortnight, totalling around 2840 staff, continue to complete timesheets for approval. SALHN advised it was impractical to implement a process to check these transactions for all staff given the complexity of timesheets and the volume processed.

Inadequate leave management processes

As we have identified previously, SALHN did not have a consistent process to ensure staff leave management reports were reviewed and actioned. In particular, there remained no central mechanism to ensure prompt review of these reports was occurring.

There were 186 SALHN staff members with negative leave balances and 277 with excessive annual leave balances.

When leave reports are not promptly reviewed, there is an increased risk that details of leave taken are not appropriately recorded in the payroll system. This could result in leave balances in excess of the staff member's entitlement being recorded and taken and a potential overstatement of leave liabilities in the financial statements.

In response SALHN advised that a draft SA Health policy had been developed, which was subject to consultation.

SALHN also advised that our recommendation to implement a central mechanism to monitor the review of leave reports was impractical as there were in excess of 7000 staff members. SALHN further advised that managers are responsible for the review.

In our view, while managers are responsible for performing the review, a central monitoring role could be implemented, which would provide assurance that all managers were performing the required review and allow for targeted follow-up where this was not occurring.

No process to ensure all medical officers' timesheets are approved and submitted

Consistent with our previous findings, there remained no process to ensure all medical officers submit timesheets and accompanying leave forms for approval. We also noted there were still no documented policies or procedures about the processes to check medical officers' attendance records at SALHN, although SALHN had previously advised a strategy and process would be identified.

Where there is no complete review of outstanding timesheets and associated leave forms, incorrect payments may be made to staff or leave taken may not be captured. We consider this is particularly important where staff are automatically paid in the payroll system, regardless of whether a timesheet is submitted, which is typically the case for medical officers. While they are automatically paid, medical officers' timesheets identify allowances they are entitled to be paid, meaning the accuracy of total payments requires completed timesheets to be processed promptly.

SALHN responded that it had sent out communications and published information on its intranet about employees' and managers' responsibilities for time and attendance recording. SALHN also advised that it was waiting for SA Health's policy to be finalised to underpin its instructions.

Nurses' timesheets were not always approved prior to payment

We have previously identified that nursing staff timesheets could be submitted to SSSA for payment without approval. We noted that the percentage of approved timesheets during our review in March 2018 had dropped by 11% from the prior year results in March 2017. In our view there remains a risk that staff may be paid for time not actually worked.

In response SALHN advised that the March 2018 data was distorted by an early pay run due to Easter and was not representative of the progress made with timesheet sign-off across the year. SALHN further advised that the SALHN requirement for timesheets to be signed prior to completion of the fortnight was not supported by managers. SALHN would review reporting time frames and its current policy.

On-call allowances

We noted that SALHN had not performed reviews of on-call allowances in 2017-18, which was consistent with SA Health internal audit findings from November 2017.

SALHN is required by the SA Health Salaried Medical Officers Enterprise Agreement 2017 to review these allowances at least twice a year. In the absence of a review, SALHN cannot ensure that the on-call percentages established in Chris21 are valid and accurate. This may result in systemic overpayments or underpayments of allowances.

From our testing of allowances, we found multiple instances where the allowance paid was incorrect, further supporting the need for regular reviews.

In response SALHN advised that a process had been implemented to ensure reviews of allowances were undertaken as required. SALHN would also follow-up the instances of incorrect payments and process the necessary adjustments where required.

Accounts payable

SALHN paid over $296 million for supplies and services in 2017-18. A large proportion of these expenses are approved for payment using online approval functions in SA Health's key financial systems, Oracle and Basware.

Delegations in key financial systems were not always consistent with the approved financial delegations

Last year we identified that while Basware delegations were reviewed, they were not checked to ensure they agreed to SALHN's approved financial delegations. We also identified that there were a number of inconsistencies between the SALHN approved financial delegations and the approval limits established in Oracle and Basware.

SALHN's response stated that system delegations would be reviewed against the SALHN approved financial delegations and a procedure would be documented.

Our 2017-18 review found that SALHN was in the process of undertaking a comprehensive review of the delegations in the authorisations against system delegations in Basware and Oracle and was developing and implementing a procedure. This was still ongoing in March 2018 and our review found a number of inconsistencies between the approved financial delegations and the delegations established in the two systems.

Where established delegations in online systems are not adequately reviewed, or do not agree to the approved delegations, unauthorised or inappropriate payments could be made.

In response, SALHN advised that it would use Basware as the primary record for delegations instead of maintaining a separate register. SALHN would also develop clearer guidance on how to apply for delegations and how they are to be updated.

Contracts were not established with some significant suppliers

We have identified in previous years that SALHN had spent significant amounts with a number of suppliers that did not have existing contract arrangements in place. In 2017-18 there were still a number of significant suppliers whose arrangements were not covered by current contracts, either through SALHN-specific contracts or whole-of-health arrangements. We were advised by SALHN that negotiation of these contracts was in progress and they were in development, evaluation or contract development stages.

We consider that negotiating contracts with major suppliers would provide opportunities to reduce prices or improve service delivery.

SALHN advised it produces a biannual report from Oracle detailing the spend profile by supplier and item. This report is used to identify items or spend categories that should have a contract in place.

No evidence charges were checked to pricing schedules

Consistent with previous years, we identified that amounts invoiced were not always agreed to established contract rates to check that the correct price was charged. From our sample testing, we found instances where there was no evidence that the approver had checked the contract rates and pricing prior to approving the invoice for payment.

Where invoice rates are not agreed to contracts (or contract summaries), SALHN may be paying more than is required for the goods or services provided. This could result in financial loss to SALHN.

SALHN advised that all staff would be provided with a link to the whole-of-health contracts information page. SALHN would also remind officers to check pricing of invoices against contract prices.

Hospital billing

Our audit covered the major financial functions for hospital billing (including administered private practice). The Enterprise Patient Administration System (EPAS) was used for patient billing at the Repatriation General Hospital (RGH), prior to its decommissioning and is used at Noarlunga Hospital, with Homer used for most patient billing at the FMC.

SALHN's revenue from patient and client fees was over $28 million in 2017-18, with a further $4 million recorded in private practice fees controlled by SALHN. In addition, a further $16 million was collected on behalf of medical officers and DHW in administered revenue from private practice arrangements.

No complete review of EPAS user access

In previous years, we found that there was no complete review of EPAS user access and no policy or procedure covering the review of user access to EPAS.

In 2017-18, SALHN implemented a work instruction from September 2017 and performed a review of EPAS users with access to the billing module in February 2018. We found that the review did not consider all EPAS users and excluded all users with access to the clinical module. The review identified:

- user access was not restricted by site, allowing non-SALHN employees to make adjustments in the billing module
- hospital billing staff had access to the clinical and billing modules of EPAS enabling them to generate charges, create and make adjustments to invoices without independent review.

We understand that hospital billing staff require some access to the EPAS clinical module for the management of billing functions. As there has not been a complete review of all user access, there remains a risk that staff have access to EPAS information that is not relevant to their role, or which may provide inappropriate access to patient information.

SALHN advised it would review the work instruction to include the introduction of an annual EPAS user review process for all EPAS modules. SALHN would also work with SA Health on further changes to ensure users have appropriate access for their roles.

Inconsistent billable charges between EPAS and HOMER

Following the closure of the RGH in November 2017, services previously provided there were transitioned to new buildings at the FMC. These services continue to use EPAS, resulting in two patient administration systems operating at FMC. Patients moving between FMC wards and the previous RGH services must to be discharged from one system and readmitted into the other.

Hospital Billing has established processes to ensure all billable activity is captured from the two systems.

In 2017-18, we tested a sample of 10 revenue transactions for the period from July 2017 to February 2018. From this we identified two instances where Hospital Billing did not identify discrepancies between billable charges associated with the dual systems, which resulted in incorrect invoice charges.

The use of two systems increases the risk of incorrect or incomplete transfer of patient information between the systems. Transposition errors may result in incorrect treatment plans, incorrect patient elections and inaccurate billed charges resulting in the loss of revenue to SALHN.

SALHN advised that it now reviews all billable charges for accuracy and completeness where patients transfer between systems.

No review of backdated billing transaction reports for 2017-18

We have previously identified that backdated patient discharge reports could not be generated from EPAS to highlight amendments that may result in changed billing for discharged patients. In 2017-18, we found that a report can now be generated from EPAS, enabling Hospital Billing to invoice for amended billed charges.

Due to the backlog, at the time of our review in April 2018 no transactions had been reviewed for 2017-18. Additionally, SALHN had not established policies or procedures to direct Hospital Billing officers about the review of the report.

Unresolved amendments to billed charges may result in not billing patients and increases the risk of not recovering long outstanding revenue from others. This may result in a loss of revenue for SALHN.

SALHN's response indicated that backdated transaction reports were run each week and reviewed for amendments to billed charges. SALHN also noted training material would be updated to include the new report.

Some patient election forms were incomplete or missing

In 2017-18, we reviewed hospital billing processes to confirm patient election forms were complete. Patient election forms are used for a patient to nominate to be treated as a private patient. Our review of data from July 2017 to February 2018 identified:

- two of 10 patient election forms were incorrect
- two election forms were not fully completed
- one election form was missing.

We understand Hospital Billing has a process to review patient election forms and, where discrepancies are identified, an email is sent to Patient Liaison Officers for follow-up with the patient. If election forms are not fixed, Hospital Billing will change the patient status from private back to public, resulting in lost revenue.

Incomplete, incorrect or missing patient election forms may result in delays in invoicing charges or a loss of revenue to SALHN (where charges are changed to public patient status). The loss of revenue from billable charges we identified that were not raised was $26 462.

SALHN advised that it would remind relevant staff of the importance of correct and complete election forms and would continue to report discrepancies to the relevant areas.

Ineffective identification of compensable charges

We visited three outpatient clinics at the FMC to confirm that questions designed to ensure all compensable visits are identified were being asked of patients. From our observations, we noted staff did not always comply with SALHN's procedure, as some patients were not asked the relevant questions required to identify a compensable visit.

When compensable patient visits are not identified and captured, SALHN may not receive all of the revenue it is entitled to.

SALHN advised that it would remind key staff in outpatient services about the need to identify if the patient visit is compensable. SALHN would also develop and place appropriate signage in clinics where there is a high probability of compensable patient visits.

Ineffective debtor management processes

Our review of SALHN's debtor management practices found that debtor balances in HOMER could not be separated between insured and uninsured debt. Any claims older than two years are highly unlikely to be recovered from health insurers, due to time limitations associated with billing arrangements.

The inability to separately identify insured debtors prevents effective debt recovery processes as the required data to support a claim cannot be provided. As at 31 May 2018 the balance of long outstanding debtors greater than 24 months was $1.5 million.

SALHN advised that new account codes had been created to separately identify insured and uninsured debts from July 2018. SALHN would continue to provide the minimum data set for all debts to health funds to assist in minimising delays in payment. SALHN would also seek regular status updates on long outstanding debts from SA Health's Debt Management Service, which has central responsibility for insured debt management.

Private practice arrangements

Inadequate recording and monitoring of Rights of Private Practice (ROPP) doctors who perform offsite billing

Consistent with our previous findings, there remain issues with the recording and monitoring of doctors who perform offsite billing under private practice arrangements. Our review in 2017-18 identified:

- the ROPP master list as at 6 December 2017 was inaccurate as it included a doctor from the Royal Adelaide Hospital who had been providing services to the FMC and the RGH since 2014 without having a ROPP agreement with SALHN
- the ROPP master list did not identify doctors that have an approved non-employee agreement
- a register listing all offsite areas that require approval was not maintained
- policies or procedures were not established to support the review process.

Without robust processes to record and monitor ROPP doctors who perform offsite billing, SALHN cannot ensure it is receiving all receipts under the arrangements. This may result in a loss of revenue to SALHN and potential misstatement in financial statements.

SALHN advised that significant changes had been implemented to address the identified issues. SALHN would also include additional information in the register to assist with offsite reviews.

No private practice audits were conducted

Consistent with prior years, we noted no private practice audits were conducted in 2017-18 as allowed under the private practice agreements. SALHN instead sent statutory declaration forms to ROPP doctors seeking confirmation and/or disclosure of their private practice services and offsite billing arrangements. While this process allows each ROPP doctor the opportunity to review their offsite arrangements to ensure compliance with their agreement and helps SALHN identify any arrangements that may have been missed, an annual program of audits would provide greater assurance to SALHN about the completeness of revenue from ROPP arrangements.

In response SALHN advised that it would engage with DHW to establish a risk-based framework for reviewing private practice that would be applied across SA Health.

Management of professional development entitlements

The SA Health Salaried Medical Officers Enterprise Agreement 2017 provides an allowance to medical officers to claim up to $44 000 over a two-year period for professional development expenses. SALHN paid $14.5 million for professional development expenses over the two-year professional development period from 14 April 2016 to 13 April 2018.

In addition, salaried medical officers are entitled to up to 10 days of professional development leave a year.

No monitoring of medical officers' professional development leave entitlements

We found that SALHN had not established processes to monitor professional development leave. Professional development leave is applied for and approved using a manual form. There is no consistent record maintained of the professional development leave entitlement balance as the process used does not have the ability to record leave taken and a remaining balance.

The absence of effective controls to monitor professional development leave balances increases the risk that medical officers will apply for, and be granted, leave without reference to remaining leave entitlements, and could take more leave than they were entitled to.

SALHN advised it would ensure Clinical Divisions advise managers approving professional development leave to confirm leave totals for the individual seeking approval, prior to an application being approved. A biannual report would also be provided to the Executive Director Medical Services advising leave levels for each clinician eligible for professional development leave.

Professional development leave taken in excess of entitlement

In 2017-18, we reviewed the Chris21 payroll transaction records for the period from 14 April 2016 to 13 April 2018. We identified 11 medical officers who exceeded their professional development leave entitlements over this period. This data reinforces the need for SALHN to implement active monitoring of professional development leave taken and the remaining entitlement.

SALHN advised that DHW was leading a project to implement a standard software solution for the management of professional development across SA Health.

Professional development reimbursements for more than the maximum allowed

We reviewed accounts payable data for the period from 14 April 2016 to 13 April 2018 and found 24 employees had exceeded their professional development allowance over the two-year period.

Payments for professional development expenses above the cap established in enterprise agreements may result in financial loss to SALHN.

SALHN advised it had developed a database that captured all elements associated with professional development reimbursement. SALHN would revisit the processes for managing the database to ensure it accurately monitors professional development allowances.

Interpretation and analysis of the financial report

Highlights of the financial report

	2018 $'million	2017 $'million
Expenses		
Staff benefit expenses	736	676
Supplies and services	296	269
Depreciation and amortisation	32	31
Other expenses	6	6
Total expenses	1 070	982
Income		
Revenue from fees and charges	57	60
Grants and contributions	5	7
Other income	14	13
Total income	76	80
Net cost of providing services	994	902
Revenues from SA Government	996	1 015
Net result	2	113
Other comprehensive income	82	1
Total comprehensive result for the year	84	114
Assets		
Current assets	55	66
Non-current assets	776	656
Total assets	831	722
Liabilities		
Current liabilities	143	135
Non-current liabilities	163	145
Total liabilities	306	280
Total equity	525	442

Statement of Comprehensive Income

Expenses

In 2017-18 total expenses increased by $88 million (9%) to $1.07 billion.

Staff benefit expenses

Staff benefit expenses of $736 million represent 69% of SALHN's total expenses. These costs have increased by $60 million in 2017-18 mainly due to:

- a $21.5 million increase in salaries and wages expense to $568 million, mainly from wage rises associated with enterprise agreements
- an $18.1 million increase in long service leave expense mainly due to the changes in the actuarial assessment and increased long service leave payments to staff

- a $4.5 million increase in annual leave expense for payments of additional hours and overtime hours worked in 2017-18
- $3 million for targeted voluntary separation package payments to 60 staff
- workers compensation expenses increasing by $8.8 million mainly due to changes in the actuarial assessment arising from an increase in serious injury claims in SALHN from six to nine cases in 2017-18.

The number of staff whose remuneration received or receivable exceeded the base executive level ($149 000) totalled 586 (554), comprising 537 medical officers, 34 nursing staff, nine executives and six non-medical staff. Total remuneration for these staff was $163 million ($152 million).

Supplies and services expenses

Supplies and services expenses increased by $27 million (10%) to $296 million in 2017-18. Significant components in supplies and services were:

- medical, surgery and laboratory supplies, which increased marginally to $88 million
- fee-for-service costs, which increased by $3.4 million (10%) to $36.3 million mainly due to billing from Flinders Private Hospital for orthopaedic services during the transition of services from the RGH to the FMC
- contractors – agency staff, which increased by $5.8 million (38%) to $21 million mainly due to additional temporary nursing staff and medical officers assisting in the transition of the RGH to the FMC
- repairs and maintenance, which increased by $6.7 million (59%) to $17.9 million mainly due to major repairs and upgrades to facilities at the FMC to accommodate the transition of RGH activity to the FMC.

Revenue

SALHN is dependent on revenue from the Commonwealth and SA Governments.

Revenues from SA Government

Revenue from the SA Government comprises capital and recurrent funding. In 2017-18, overall revenues decreased by $18.7 million (2%) to $996 million due to decreased capital funding of $92.5 million, which was offset by increased recurrent funding of $73.8 million.

Capital funding decreased by $92.5 million (63%) to $54 million mainly due to the completion of key capital works at the FMC and the Jamie Larcombe Centre at Glenside in 2017-18.

Recurrent funding increased by $73.8 million (9%) to $942 million mainly due to increased funding for the decommissioning of the RGH and payments to Statewide services (SA Medical Imaging (SAMI) and SA Pharmacy).

Revenues from fees and charges

Revenues from fees and charges decreased by $3.3 million (6%) from:

- a $1.4 million (27%) decrease in private practice fees received by SALHN due to the transfer of SAMI rights of private practice from SALHN to the Central Adelaide Local Health Network Incorporated
- a $2.1 million (10%) decrease in recoveries mainly for the recovery of salary and wages expenses paid by SALHN for staff working for other local health networks.

Statement of Financial Position

Property, plant and equipment

Property, plant and equipment represents 92% of SALHN's total assets. The carrying value of property, plant and equipment increased by $118 million to $767 million. This increase is due mainly to:

- additions of $51 million for new facilities at the FMC and for other infrastructure projects including the veterans' mental health precinct, Jamie Larcombe Centre and Noarlunga Hospital capital works
- reclassification of the RGH from held for sale, following the State election
- a revaluation increment of $83 million comprising a $13 million increment for land and a $70 million increment for buildings
- offset by depreciation expenses of $32 million.

Liabilities

Current liabilities increased by $8 million to $143 million during the year and exceeded current assets by $88 million at balance date. SALHN works with DHW to ensure sufficient funding is provided to SALHN to meet expected cash flows for its administration and program delivery. Cash and cash equivalents of $33 million are sufficient to meet current payables of $32 million.

Total liabilities increased by $26 million to $306 million.

Staff liabilities make up $277 million (91%) of SALHN's total liabilities at 30 June 2018, comprising:

- staff benefits liabilities and related on-costs of $239 million ($221 million)
- workers compensation provisions of $38 million ($26 million).

The movement in staff liabilities is mainly due to:

- a $9 million (7%) increase in long service leave liabilities primarily resulting from changes to the assumptions associated with the duration of the liability, offset by the increase in the discount rate applied to the liability calculation
- a $12 million (47%) increase in workers compensation provisions reflecting changes in the actuarial assessment arising from the increase in serious injury claims in SALHN from six to nine cases in 2017-18.

Further commentary on operations

SALHN infrastructure changes

Flinders Medical Centre redevelopment

The total budget for this build is $185.5 million. The SA Government approved a $170.5 million budget for the redevelopment in August 2015. A further $15 million of funding for two additional levels of car parking was approved in August 2016.

The FMC redevelopment works were completed in 2017-18. The completed works included the:

- 55 bed rehabilitation building, including a palliative care unit, with total spend of $83 million
- Older Persons Mental Health Service unit, with total spend of $32.7 million
- multi-deck car park delivering 1820 car spaces, with total spend of $59 million.

As at 30 June 2018, further redevelopment works remained in progress. To date, these separate projects have incurred costs of $20 million and include:

- a new 50 cot neonatal unit
- a new ophthalmology clinic
- a new infusion centre.

Repatriation General Hospital decommissioning and reactivation

On 9 November 2017, the RGH was closed and decommissioned with the last patients moved to new facilities across SALHN. We were advised that the total direct costs of decommissioning the RGH were approximately $5.8 million. SALHN further advised that this amount potentially excluded other costs incurred that were incidental to the decommissioning process.

Following decommissioning, further costs were incurred to secure and maintain the vacant RGH site.

Following the State election in March 2018, the previous SA Government's decision to sell the RGH to the Aged Care and Housing Group Incorporated was cancelled. The contract of sale was terminated in May 2018 at no extra cost.

To recommence providing health services at the RGH site, the hydrotherapy pool was reopened in the last week of May 2018. Planning to reactivate the RGH for the delivery of potential health services from the site, through a staged stakeholder consultation and engagement process, also commenced in June 2018.

SA Health released an expression of interest for 'Reactivating the Repat Health Precinct' in August 2018 seeking submissions from the private sector and non-government organisations interested in partnering with SA Health to deliver a variety of health and wellbeing focused services in reactivating the RGH site.

Women's and Children's Health Network Incorporated (WCHN)

Financial statistics	Total expenses:	$465 million
	Net cost of providing services:	$415 million
	Revenues from SA Government:	$413 million
	Staff benefits liability and related on-costs:	$110 million
	Workers compensation liability:	$13 million
	Number of FTEs:	2705

Significant events and transactions

- The SA Government established a taskforce to develop a fully costed plan to build a new Women's and Children's Hospital co-located with the Royal Adelaide Hospital.
- An independent revaluation of land and buildings as at 1 June 2018 resulted in a $117 million valuation increment.
- The *Health Care (Governance) Amendment Act 2018* was proclaimed in August 2018 and will be operational from 1 July 2019. It changes governance arrangements, including that WCHN will be governed by a board from that date.

Financial report opinion

Unmodified

Financial controls opinion

Modified

Key issues:

- Improvements necessary to ensure all private practice revenue is received
- Nurses' time records not always approved

Functional responsibility

WCHN is an incorporated hospital established under the *Health Care Act 2008*.

The functions of WCHN include the provision of health services to women and children. The principal unit within WCHN is the Women's and Children's Hospital.

Under the *Health Care Act 2008* the Chief Executive, Department for Health and Wellbeing (DHW) assumed direct responsibility for administering incorporated hospitals including WCHN. This included appointing the Chief Executive Officer of WCHN. The Chief Executive, DHW cannot give a direction about a person's clinical treatment.

Governance changes

The new SA Government has announced its intention to amend governance arrangements across SA Health. The first part of these changes was completed in August 2018 when the *Health Care (Governance) Amendment Act 2018* was proclaimed and will operate from 1 July 2019.

The amendments change the role of the Chief Executive, DHW to remove direct responsibility for the administration of incorporated hospitals. The amendments provide for the WCHN to be governed by a board. The SA Government intends the board to be fully operational by 1 July 2019.

The SA Government has stated it will establish a new governance and accountability framework for the public health system that will be reflected in legislation to be introduced into Parliament later in 2018 or early next year.

Scope of the audit

The audit program covered major financial systems to obtain sufficient evidence to form an opinion on the financial report and internal controls.

Financial services for WCHN are provided through a mix of:

- central services provided by the DHW through an integrated finance service model
- finance services located within WCHN
- services provided by Shared Services SA (SSSA).

Consequently, our audit included the review of new and legacy systems and completing audit work at DHW's central services, WCHN and SSSA.

Audit findings across health services fall into the following categories:

- common findings reflecting central services and/or systems
- matters for individual health services
- SSSA matters.

A Chartered Accounting firm assisted the Auditor-General with the audit of WCHN.

Specific areas of audit attention in 2017-18 included:

- payroll
- accounts payable
- revenue
- patient revenue including accounts receivable
- property, plant and equipment
- cash
- general ledger.

Internal audit activities were considered in designing and performing audit procedures.

Audit findings and comments

Assessment of controls

In my opinion, the controls exercised by the Women's and Children's Health Network Incorporated in relation to the receipt, expenditure and investment of money, the acquisition and disposal of property and the incurring of liabilities, except for all matters outlined under 'Communication of audit matters', are sufficient to provide reasonable assurance that the financial transactions of the Women's and Children's Health Network Incorporated have been conducted properly and in accordance with law.

Communication of audit matters

Matters identified by the audit were detailed in a management letter to the Chief Executive Officer, WCHN and copied to the Chief Executive, DHW.

A summary of our findings for centralised processes performed by DHW can be found in the section of this Report titled 'Department for Health and Wellbeing' under the heading 'Communication of audit matters'.

The main matters raised with WCHN and related responses are detailed below.

Payroll

Insufficient review of payroll information

Consistent with last year we found WCHN managers or team leaders did not always review payroll reports to ensure the accuracy and completeness of staff payments. In November 2017, a new bona fide report process was introduced whereby managers and team leaders log into the payroll system and review a report to confirm the bona fide nature of employee payments. We found WCHN did not follow up managers and team leaders who had not completed the review. At the time of the audit in April 2018, we found that 730 of 1705 bona fide reports were not approved.

Failure to ensure payroll information is valid and accurate may result in fraudulent or incorrect payments. We recommended WCHN monitor and follow up to ensure managers and team leaders promptly review payroll bona fide reports to ensure the accuracy and completeness of staff payments.

WCHN responded that since March 2018 bona fide reports had been automatically generated and delivered to managers. It also intended to establish compliance reporting by September 2018.

Nurses' time records not always approved

Timesheets for nurses are created in the ProAct rostering timesheet system. Managers are required to electronically authorise timesheets in ProAct before they are uploaded to the CHRIS payroll system for payment.

Consistent with last year we noted instances where the ProAct file was uploaded to CHRIS without all timesheets being authorised. We recommended WCHN ensure all ProAct timesheets are approved before to being uploaded to CHRIS for payroll processing.

WCHN responded it had begun reporting on unapproved ProAct timesheets to allow monitoring and where appropriate referral to divisional directors for corrective action.

Controls over access to ProAct require improvement

Our audit considered management's processes to ensure only authorised people have access to ProAct. We recommended WCHN regularly review ProAct user access with a view to removing staff who no longer require access. This issue was raised last year.

WCHN accepted the recommendation and responded with its intended actions, including establishing a cyclical review of access.

Supplies and services expenditure

Financial authorities in payment system did not always match delegations

Our review of financial authorities assigned to users in the Basware payment authorisation system noted instances where user position descriptions did not match the authorities in the Chief Executive Officer's instrument of delegation. Incorrect approval limits in Basware increase the risk of invalid, unbudgeted or unapproved expenditure.

WCHN indicated that while the position descriptions in Basware differed from those in the delegation instrument, the delegated authority was generally the same. WCHN agreed with our recommendation and had established a regular review of financial authorities in Basware against delegations.

Patient billing

Revenue system access rights not reviewed

In past years we reported that management did not review a complete list of user access rights in the Homer revenue system. Our follow-up in 2017-18 found that although WCHN had developed a report for the Chief Finance Officer's review, it did not contain sufficient information and was not reviewed. Without regular management review WCHN may not detect inappropriate levels of access within Homer, increasing the risk of inaccurate or unauthorised changes to revenue transactions.

WCHN responded that it had developed a report as part of its July 2018 software upgrade and each person's access rights were now being reviewed. It indicated the reports will be examined by its Revenue Manager and signed off by the Chief Finance Officer.

Improvements necessary to ensure all private practice revenue is received

Some medical officers employed by WCHN have a right of private practice under agreements with SA Health. The private practice arrangements require these medical officers to complete a statutory declaration confirming their complete disclosure of private practice revenues. We found that of 140 requests for declarations, only nine responses were received.

Medical officers are required to contribute a percentage of income earnt through their private practice over a specific threshold to schemes administered by SA Health. Medical officers' failure to disclose all private practice revenue may result in a loss of revenue. We recommended WCHN monitor and ensure it received all statutory declarations.

WCHN responded that it would seek to ensure all rights of private practice revenue are declared by way of a questionnaire and a statutory declaration where required.

Shared Services SA – financial systems and transactions processing environments

SSSA processes financial transactions on behalf of WCHN. The main systems and control environments include accounts payable and payroll financial functions.

Our review and evaluation of controls for these systems conclude that the controls were effective for 2017-18. SSSA is discussed further in the commentary under 'Department of the Premier and Cabinet' in this Report.

Interpretation and analysis of the financial report

Highlights of the financial report*

	2018 $'million	2017 $'million
Expenses		
Staff benefits expenses	350	323
Supplies and services	107	107
Depreciation and amortisation expense	8	8
Other expenses	-	2
Total expenses	465	440
Income		
Revenue from fees and charges	32	36
Grants and contributions	9	7
Other income	9	9
Total income	50	52
Net cost of providing services	415	388
Revenues from SA Government	413	384
Net result	(3)	(4)
Changes in assets revaluation surplus	117	-
Total comprehensive result for the year	114	(4)

	2018 $'million	2017 $'million
Assets		
Current assets	37	26
Non-current assets	373	256
Total assets	410	282
Liabilities		
Current liabilities	58	52
Non-current liabilities	73	63
Total liabilities	131	116
Net assets	279	166

* Table may not add due to rounding.

Statement of Comprehensive Income

Expenses

In 2017-18 total expenses increased by $26 million to $465 million.

Staff benefit expenses

Staff benefits expenses, $350 million, represent 75% of WCHN's total expenses. The number of staff whose remuneration received/receivable exceeded the base executive level ($149 000) totalled 261 (249), comprising 231 (211) medical, 15 (24) nursing, eight (eight) administration and seven (six) executive staff. Total remuneration for these staff was $72 million ($67 million).

Supplies and services expenses

Supplies and services expenses were $107 million, the same as last year. Significant components of supplies and services were:

- medical, surgical and laboratory supplies – $25 million ($26 million)
- drug supplies – $8 million ($9 million)
- contractors – agency staff – $9 million ($8 million)
- housekeeping – $10 million ($10 million).

Revenues

Revenues from SA Government

WCHN is principally funded by DHW. In 2017-18, funding of $413 million comprised recurrent funding of $405 million and capital funding of $7 million.

Statement of Financial Position

Property, plant and equipment

Property, plant and equipment represents 86% of WCHN's total assets. The carrying value of property, plant and equipment increased by $116 million to $353 million. This increase was primarily due to:

- $117 million valuation increment resulting from an independent revaluation of land and buildings as at 1 June 2018. Unobservable inputs and the significant extent of professional judgement required in valuing the building assets is discussed in note 22.2 of WCHN's financial report
- $7 million additions to capital work in progress
- depreciation and amortisation of $8 million.

In 2017-18 the SA Government established a taskforce to develop a fully costed plan to build a new Women's and Children's Hospital co-located with the Royal Adelaide Hospital.

Liabilities

Current liabilities increased by $5 million to $58 million during the year and exceeded current assets of $37 million at balance date. Cash and cash equivalents of $28 million are sufficient to meet current payables of $13 million.

Staff benefits are the largest element of current liabilities, totalling $42 million at 30 June 2018. They mainly comprise leave entitlements expected to be taken within 12 months.

Staff liabilities make up $123 million of WCHN's total liabilities at 30 June 2018, comprising:

- staff benefits liabilities and related on-costs, $110 million ($101 million)
- provision for workers compensation, $13 million ($7 million).

HomeStart Finance (HomeStart)

Financial statistics	Loans and advances:	$2 billion
	Short-term borrowings: Long-term borrowings:	$251 million $1.6 billion
	Profit before income tax:	$19 million
	Dividends paid:	$19.1 million
	Number of FTEs:	110
	Number of loans outstanding at 30 June:	13 254
Significant events and transactions	— Dividends of $19.1 million were paid after a recommendation from the Board and approval by the Minister and the Treasurer. — Loans and advances increased by $169 million due mainly to the growth in fixed rate and graduate loans.	
Financial report opinion	**Unmodified**	
Financial controls opinion	**Unmodified**	

Functional responsibility

HomeStart is a statutory corporation established by Regulation under the *Urban Renewal Act 1995*. It has a Board of Management appointed by the Minister for Transport, Infrastructure and Local Government and is subject to the control and direction of the Minister.

HomeStart's functions include:

- lending money or providing other financial assistance to facilitate home ownership for people who would otherwise have difficulty obtaining finance
- providing, marketing and managing home finance products
- providing, managing or facilitating finance for housing schemes or housing associations and for mortgage relief schemes within South Australia
- providing, managing or facilitating finance for the development, ownership or operation of aged care residential accommodation or facilities.

Scope of the audit

The audit covered major financial systems to obtain sufficient evidence to form an opinion on the financial report and internal controls.

Specific areas of audit attention in 2017-18 included:

- lending, including arrears management and allowance for impairment
- investment
- purchases and payments
- payroll
- treasury
- regulatory framework
- general IT controls.

We also considered the work of HomeStart's internal auditors in planning and conducting the audit.

Audit findings and comments

Communication of audit matters

A small number of minor control matters identified by the audit were outlined in a management letter to the Chair of the HomeStart Audit Committee.

HomeStart provided a satisfactory response to these matters.

Interpretation and analysis of the financial report

Highlights of the financial report*

	2018 $'million	2017 $'million
Interest income	101	96
Interest expense	(38)	(35)
Net interest income	63	61
Other income	11	12
Other expenses	(26)	(26)
Government guarantee fee	(29)	(27)
Profit (Loss) before income tax equivalents	19	20
Income tax equivalents expense	(6)	(6)
Profit (Loss) after income tax equivalents expense	13	14
Other comprehensive income	1	2
Total comprehensive result	15	17
Assets		
Loans and advances	2 011	1 842
Other assets	66	73
Total assets	2 077	1 915

	2018 $'million	2017 $'million
Liabilities		
Borrowings	1 898	1 730
Other liabilities	17	20
Total liabilities	1 915	1 750
Total equity	162	165

* Totals may not add due to rounding.

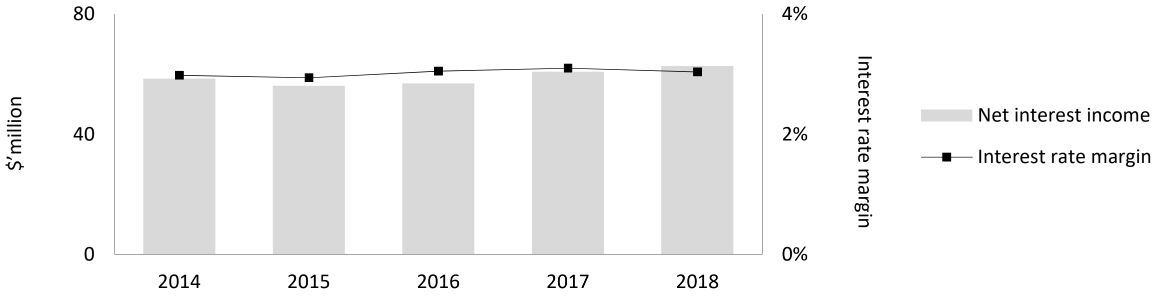
Statement of Comprehensive Income

Profit for the year

Profit before income tax equivalents decreased by $1.4 million to $19 million. The analysis below outlines the main factors contributing to this result.

Net interest income

The following chart compares the net interest income to the interest rate margin between loans and cost of funds, excluding the cost of the government guarantee fee.



Net interest income increased by $1.9 million (3%) to $62.7 million. The increase mainly reflects a 9% increase in net loans and advances during the year.

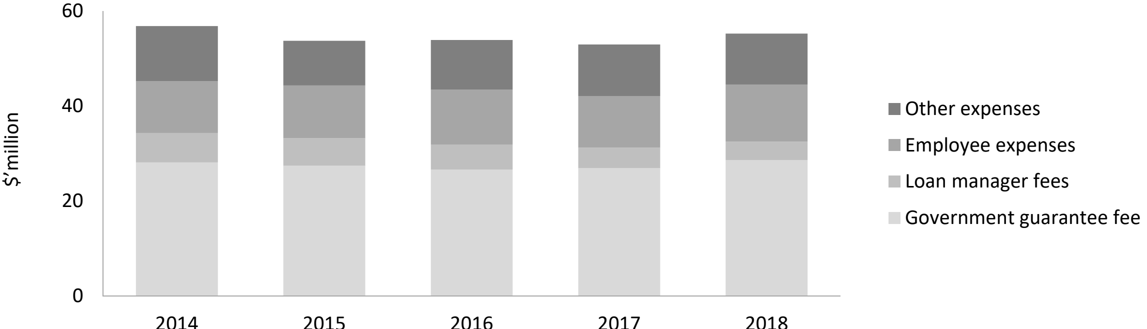
The chart shows that the interest rate margin between loans and cost of funds has remained stable at around 3% over the last five years.

Other income

Other income decreased by $1.1 million to $11.4 million due mainly to reduced growth in the unrealised gain in breakthrough loans of $654 000. Investment income was also $837 000 lower in 2017-18 following the maturing of available-for-sale investments in 2016-17. These financial assets were not reinvested. The decreases in other income were partially offset by a $328 000 increase in the community service obligation (CSO) subsidy from the Department of Treasury and Finance for the provision of advantage loans and for the administration of the Nunga loan program.

Expenses other than interest

The movement in expenses other than interest over the last five years is illustrated in the following chart.



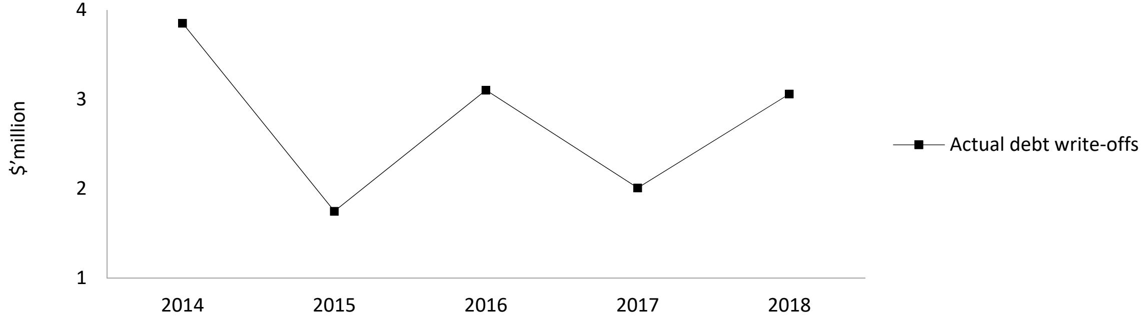
Expenses have declined slightly since 2014, with expenses increasing by $2.3 million in 2017-18. More significant movements in 2018 were:

- an increase in the government guarantee fee of $1.7 million attributable to the increase in the value of borrowings and the increase in the government guarantee fee rate to 1.88% for loans written from 1 July 2017. A guarantee fee rate of 1.56% applied for loans written in 2016-17 and 1.6% for legacy borrowings prior to this date
- employee benefits expenses increasing by $1.1 million as a result of a 1.5% increase in enterprise agreement salaries rates and a 3 FTE increase in staff numbers
- loan manager fees decreasing by $454 000 reflecting the transition to using brokers (rather than loan managers) in writing new loans. Commissions paid to brokers are lower than for loan managers.

Bad and impaired loans expense

HomeStart's bad and impaired loans expense for the year was $2.4 million ($2.9 million). The decrease reflects changes in loan provisioning from the prior year.

The total provision for impairment as at 30 June 2018 was $17.5 million ($18.2 million). The following chart shows the actual debt write-offs through the provision and the Statement of Comprehensive Income for the last five years.



The chart demonstrates the relative volatility of debt write-offs over the past five years, reflecting the impact of the economic circumstances of borrowers.

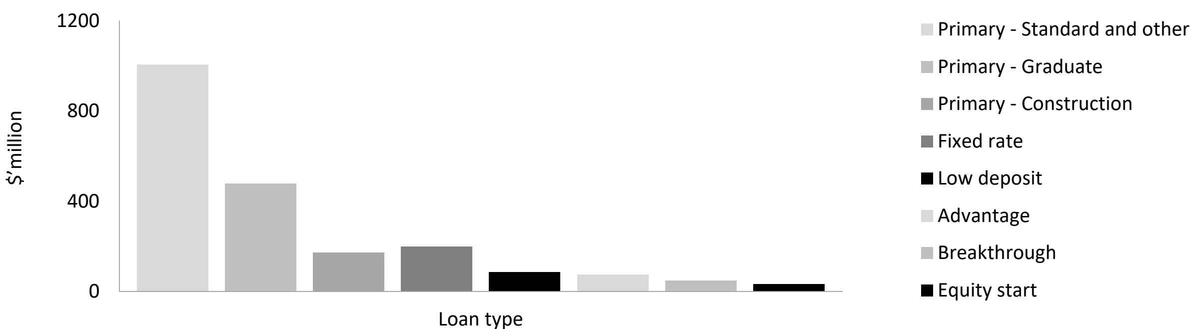
The increase in bad debt write-offs for 2018 was mainly attributable to losses on the disposal of properties held following an increase in mortgagees in possession.

Statement of Financial Position

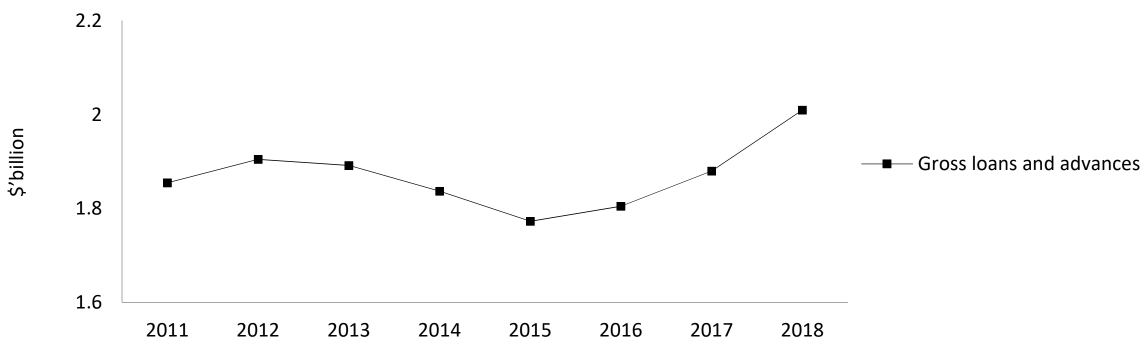
Loans and advances

As at 30 June 2018 gross loans and advances totalled $2.1 billion, an increase of $163.4 million from the previous year. This increase was due mainly to a $104.9 million increase in fixed rate loans and a $98.8 million increase in graduate loans, both partially offset by a decrease in variable loans of $40.7 million.

The following chart shows the value, by loan type, of HomeStart's loan portfolio at 30 June 2018.



The following chart shows the value of gross loans and advances over the past eight years.



The decrease in gross loans over the three years to 2015 reflected higher levels of loan discharges driven by:

- refinancing as a result of lower market interest rates from other lenders
- higher loan repayments and discharges due to lower interest rates allowing faster repayment of outstanding principal amounts.

The increase in gross loans from 2015 is primarily the result of the growth in graduate loans. HomeStart changed the lending criteria for these loans in 2015, allowing students with a TAFE SA certificate III qualification to be eligible for a graduate loan.

Breakthrough loans and shared equity option loans

Breakthrough loans and shared equity option loans are comprised of two components:

- a standard loan component with standard interest rates and repayments

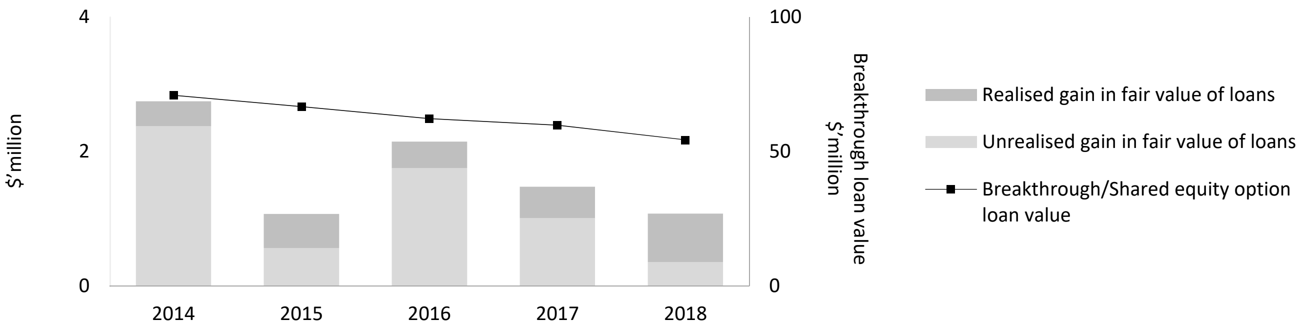
- a shared appreciation component where the loan is repaid along with a percentage of the increase in property value when the property is sold.

The shared appreciation component of these loans is recognised as a financial asset at fair value through profit and loss, while the standard loan component is recognised at amortised cost.

These loans represent a relatively small portion of total loans and advances, with the breakthrough and shared equity loans representing 3% of HomeStart's total loan portfolio. The impact that the shared appreciation component has on HomeStart's operating result, however, has meant that HomeStart has implemented specific risk management strategies for these loans. One of those strategies is placing a cap on the total value of these loans that will be written or outstanding at any given time.

In 2018 a net $1.1 million gain ($1.5 million gain) was recognised for these loans, comprising a $355 000 gain ($1 million gain) recognised from revaluation and a $722 000 gain ($468 000 gain) recognised on discharge of breakthrough loans. The movement in the value of the shared appreciation component, and the impact of these loans on the operating result, follows general property market movements for the areas in which the properties are located.

The chart below shows the impact of the breakthrough loans on HomeStart's operating result and the total value of loans since 2014.



The breakthrough loan product was withdrawn from December 2017, with the new shared equity option loan released in April 2018.

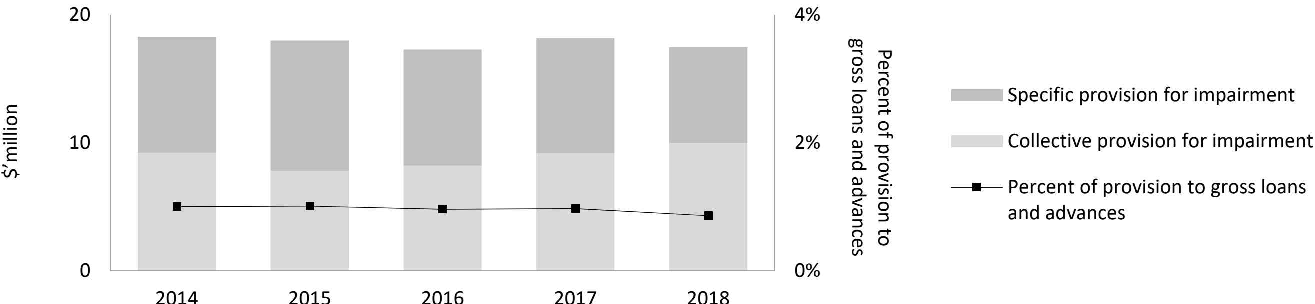
Provisions for impairment

HomeStart assesses whether there is objective evidence that a financial asset or a portfolio of financial assets is impaired at each balance date.

The total provision for impairment decreased by $709 000 to $17.5 million. It has two components:

- the specific provision – representing loans and advances that are individually assessed as impaired. As at 30 June 2018 this was $7.5 million ($9 million)
- the collective provision – this arises where HomeStart determines that no objective evidence of impairment exists for an individually assessed financial asset. As at 30 June 2018 this was $10 million ($9.2 million). To calculate this provision, assets are included in a group of financial assets with similar credit risk characteristics and collectively assessed for impairment.

The following chart shows the level of the total provisions and their composition over the past five years.



The chart shows that the overall level of provisioning has remained consistent, relative to total gross loans and advances, over the period.

In 2018, the overall decrease in the provision resulted from a decrease in the specific provision, offset by an increase in the collective provision. The decrease in specific provision is due mainly to a reduced number of loans in arrears greater than three months and the increased number of loans written off on realisation of properties. The increase in the overall collective provision is due mainly to the growth in the loan portfolio.

The Australian Accounting Standards Board issued a new accounting standard AASB 9 'Financial Instruments' which HomeStart will adopt from 1 July 2018. The standard contains a new classification and measurement approach for financial assets and will impact on impairment requirements and other elements. HomeStart has estimated that the adoption of the new standard will reduce equity by approximately $500 000.

General reserve for credit losses

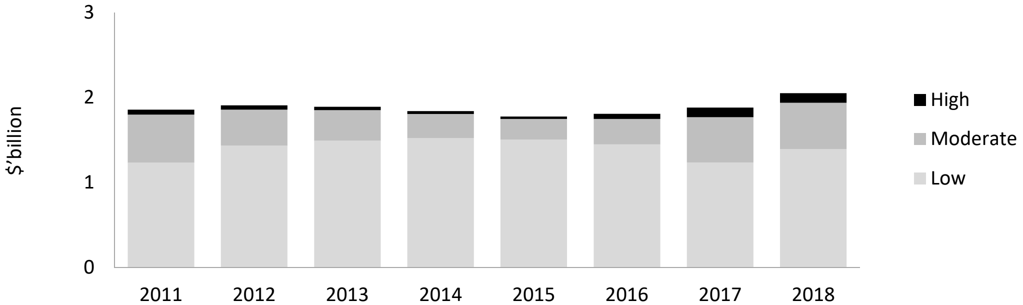
The use of a general reserve for credit losses, to set aside additional funds in excess of the specific and collective provisions, as per HomeStart's charter, is consistent with the Australian Prudential Regulation Authority's prudential risk management requirement to retain sufficient retained earnings for capital adequacy purposes. The charter requires that a capital adequacy ratio of 12% be maintained. As at 30 June 2018, HomeStart maintained a 13.7% capital adequacy ratio.

The balance of the reserve at 30 June 2018 was $8.1 million ($8.3 million) reflecting a decrease in estimated potential credit losses. HomeStart last had an actuarial assessment performed over potential credit losses as at 31 December 2017.

The combined provisions for impairment and general reserve for credit losses take the total amount set aside for potential losses to $25.6 million ($26.5 million), representing 1.25% (1.4%) of gross loans and advances.

Loan quality

HomeStart has assessed the gross value of loans and advances to customers by credit risk grading. The following chart summarises that assessment.



The chart shows that the proportion of high and moderate credit risk category loans reduced until 2015, with most loans assessed as low credit risk. There was an increase in high and moderate credit risk loans from 2016 mainly as a result of changes to the credit risk classifications based on credit scores. This resulted in more loans being classified as high credit risk. This has not adversely impacted the provision required.

Risk management for loans

HomeStart's risk profile for its loans has a higher inherent risk than a commercial lender's loan portfolio. Key differences include:

- generally HomeStart customers have lower incomes and borrow a greater percentage of their home value
- there is a significant concentration of lending in regional South Australia and outer metropolitan suburbs
- customers are not required to take out mortgage insurance because HomeStart self-insures losses incurred.

There are geographic areas with a greater concentration of HomeStart loans, with 33% of loans by value secured against properties in the City of Playford and the City of Salisbury. A further 22% of loans by value are secured against properties outside of the Adelaide metropolitan area.

HomeStart manages the risks associated with these concentrations of lending through its general lending policies, including loan to valuation ratios and limits on lending in some instances. As HomeStart lends only to individual owner-occupiers, it holds collateral against the value of the loans outstanding through mortgages on the associated properties.

HomeStart's principal exposure is to the risk of a borrower not being able to repay the loan. Where this occurs, the property may be subject to sale as a mortgagee in possession, with HomeStart seeking to recover outstanding amounts by selling the property. In this situation HomeStart is exposed to market risk that the price achieved for the property's sale does not cover the outstanding balance. HomeStart manages this risk by monitoring property valuations annually and complying with loan to valuation ratios for new loans.

As discussed above, HomeStart seeks to manage the risks associated with loan quality by maintaining a specific provision, a collective provision and a general reserve for credit losses. HomeStart also seeks to maintain appropriate capital reserves to cover any significant losses arising from loan defaults.

Investments

HomeStart's financial investments decreased by $6 million to $55 million ($61 million). This was due mostly to a decrease in the fair value of breakthrough loans, which are designated as investments at fair value through profit and loss. Breakthrough loans will continue to decline as they are no longer offered to customers (from December 2017) and have been replaced by the shared equity option loan (from April 2018).

The shared appreciation component of the breakthrough loan product was valued at $54.2 million ($59.8 million). The discharge of a breakthrough loan is at the discretion of the property owner through refinancing or sale. Consequently, HomeStart cannot liquidate these investments to meet any future potential funding requirements.

Liabilities

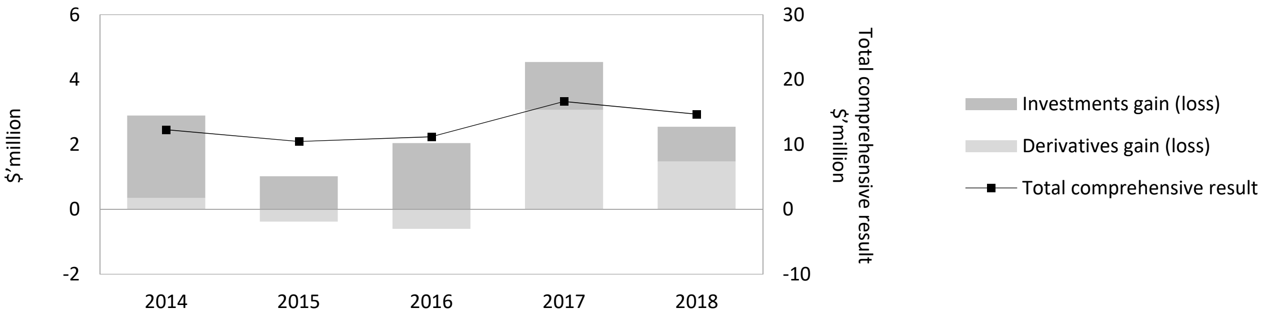
Borrowings at 30 June 2018 were $1.9 billion ($1.7 billion) and represent 99% (99%) of HomeStart's liabilities. HomeStart is required to use the South Australian Government Financing Authority (SAFA) as its sole counterparty for all funding transactions. At 30 June 2018, HomeStart had a current approved borrowing limit of $2.1 billion ($2.1 billion). All of HomeStart's borrowings from SAFA mature within five years, with $312 million of SAFA debt maturing over the next 12 months.

Fair value and comprehensive result

HomeStart recognises derivatives and certain investments, including breakthrough loans and the shared equity option loan products, at fair value. The changes in market value of these items can impact HomeStart's Statement of Financial Position and Statement of Comprehensive Income.

Derivatives are used to hedge (protect against) changes in interest rates. Whilst these hedges remain effective (as defined by the accounting standards), changes in the fair value of hedges do not affect profit as they are recognised in the derivatives valuation reserve within equity. However, the realised and unrealised changes in investments at fair value are recorded in other expenses or income in the Statement of Comprehensive Income.

The impact of all these changes is included in the total comprehensive result reported in the Statement of Comprehensive Income. HomeStart's total comprehensive result decreased by $1.9 million to $14.7 million. The chart below shows the impact of the changes in the fair value of derivatives and investments on HomeStart's total comprehensive result for the last five years.

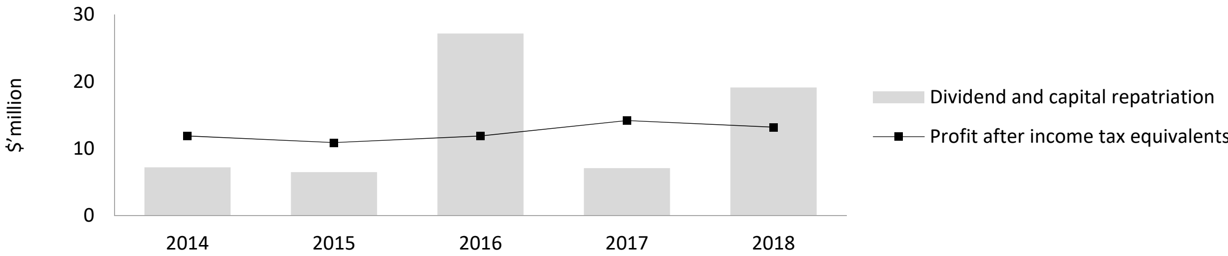


It is important to appreciate that the financial report combines the financial assets and financial liabilities measured at either fair value or at cost. The fair value of net financial assets is $153.2 million ($154.3 million), while the carrying value of net financial assets is $158.2 million ($160.6 million). The

slight decrease in the margin between fair value and carrying value is mainly due to an improvement in the market value position of HomeStart's borrowings.

Distributions to government

The following chart shows profit after income tax equivalents and distributions for the past five years, highlighting HomeStart's sustained profit performance over that period.



In June 2018 the Treasurer approved the payment of a dividend of $19.1 million, noting the remaining dividend from HomeStart's final operating result would be paid in 2018-19. The dividend is comprised of:

- a dividend adjustment of $1.4 million to account for the difference between the forecast profit after tax and the final tax profit in 2016-17
- a dividend of $7.7 million relating to 60% of HomeStart's forecast after tax profit for 2017-18 in line with its 2017-18 performance statement
- an interim dividend of $10 million that was declared as part of the 2017-18 mid-year budget review.

HomeStart recognised a dividend payable of $212 000 ($1.4 million) at 30 June 2018 for the difference between the forecast profit after tax and the final tax profit in 2017-18, which is not included in the chart above.

HomeStart aims to return dividends to the SA Government regularly, in line with its established performance statement and the requirements of the *Public Corporations Act 1993*. Dividends are recommended by the Board and then approved by the Treasurer.

HomeStart's payments to the SA Government include dividends, guarantee fees and income tax equivalents. HomeStart also receives CSO funding for advantage loans and for the administration of the Nunga loan program.

The following table summarises these transactions with the SA Government for the four years to 2018.

	2015 $'million	2016 $'million	2017 $'million	2018 $'million
SA Government:				
Dividend	7	27	7	19
Tax	5	5	5	6
Government guarantee fee	27	27	28	29
Total to SA Government	39	59	40	54
CSO income	(6)	(6)	(6)	(7)
Net amount provided to SA Government	33	53	34	47

HomeStart's charter, approved by the Treasurer and the Minister for Transport, Infrastructure and Local Government, provides for an annual dividend calculated at 60% of profit after tax. In 2018 HomeStart was directed to pay a further interim dividend of $10 million. A further interim dividend was also required in 2016.

Statement of Cash Flows

Net cash flows

The following table summarises the net cash flows for the four years to 2017.

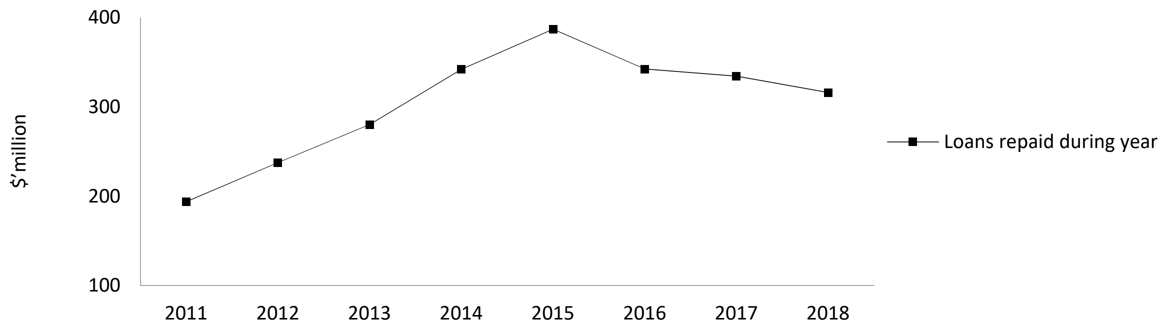
	2015 $'million	2016 $'million	2017 $'million	2018 $'million
Net cash flows:				
Operating	6	10	12	10
Investing	71	(29)	(19)	(161)
Financing	(78)	19	10	149
Change in cash	(1)	-	3	2
Cash at 30 June	2	2	5	3

Investing activities relate primarily to the provision of loans to customers. In 2018 there was a net $166.7 million cash outflow for customer loans, which corresponded to the increase in gross loans and advances. The net financing cash inflow of $149 million reflects new SAFA borrowings ($468 million), offset by repayment of borrowings ($300 million).

Customer loans repaid

From 2016 new lending has increased while discharges have decreased in comparison to prior years. Discharges in 2018 were $244 million ($246 million).

The following chart shows loan repayments, including discharges, since 2011.



Customer repayments increased substantially between 2011 and 2015. The increase was due largely to the reduction in interest rates resulting in:

- customers choosing to repay more debt or refinance with other institutions to take advantage of more suitable loan arrangements
- fixed repayment loan products repaying proportionately more principal.

HomeStart operating parameters

HomeStart is required to operate within financial parameters set down in its charter and performance statement approved annually by the Treasurer and the Minister for Transport, Infrastructure and Local Government.

HomeStart's performance targets compared to actual results are detailed below.

	Cabinet approved operating parameters	Performance statement target for 2018	2017 result	2018 result
Operating profit before tax	n/a	$15.5 million	$20.3 million	$18.9 million
Return on equity	9%	9.4%	12.57%	11.52%
Cost to income ratio	55%	52.6%	49.96%	53.33%
Capital adequacy ratio	12%	15%	15.6%	13.7%

The most significant factor contributing to HomeStart's above-parameter return on equity in 2018 was its strong net interest income.

The Treasurer has approved HomeStart's borrowing limit of $2.105 billion.

Department of Human Services (DHS)

Financial statistics	Net cost of providing services:	$1.2 billion
	Revenues from SA Government:	$1.3 billion
	Total assets:	$466 million
	Number of FTEs:	3931.3

Significant events and transactions

- Disability clients continued to transition to the National Disability Insurance Scheme (NDIS), with all clients between the ages of 18 and 64 eligible to transition from 1 July 2017. All DHS eligible clients were to transition to the scheme by 30 June 2018. At this date approximately 25% of clients due to transition in 2017-18 were yet to transition.
- In February 2017 the SA Government approved significant changes to how disability and domiciliary care services will be provided in South Australia in response to Commonwealth disability and aged care reforms. One change was to transition domiciliary care services to non-government management. On 29 June 2018 domiciliary care services transitioned from DHS to the Royal District Nursing Service South Australia and eligible employees transferred across.
- An employee-led mutual was set up as a company limited by guarantee on 8 February 2018. From 1 October 2018 responsibility for the provision of early childhood early intervention services under the National Disability Insurance Scheme will transition from the Child and Youth Services division of DHS to the employee-led mutual.

Financial report opinion

Unmodified

Financial controls opinion

Modified

Key issues:

- Weaknesses in brokerage care services controls and processes
- Outstanding concessions issues from prior years

Functional responsibility

DHS is an administrative unit established under the *Public Sector Act 2009.*

The *Public Sector (Administrative Units-Alteration of Titles) Proclamation 2018* changed the name from the Department for Communities and Social Inclusion to DHS on 17 May 2018. DHS now reports to the Minister for Human Services.

DHS is committed to ensuring that all South Australians, particularly the most vulnerable and disadvantaged, have access to high quality services that protect and enhance the community's wellbeing and provide support to people when they need it. DHS is committed to delivering better and more connected services to the vulnerable and disadvantaged in our community, and to building engaged, socially inclusive, strong and vibrant communities.

DHS also functions as a service provider to the South Australian Housing Trust (SAHT) through its Housing SA division. From 1 July 2018, Housing SA employees were transferred to the employment of the Chief Executive SAHT.

For more information about DHS's objectives and functions refer note 2 of its financial report.

Scope of the audit

The audit program covered major financial systems to obtain sufficient evidence to form an opinion on the financial report and internal controls.

Specific areas of audit attention in 2017-18 included:

- follow-up of issues raised in 2016-17
- National Disability Insurance Scheme (NDIS) governance and financial arrangements
- disability and aged care reform taking place within DHS
- compliance with legislation and other government requirements
- expenditure, including expenditure on grants, concessions and brokerage care services
- payroll
- revenue
- cash and general ledger
- fixed assets
- client trust accounts.

The audit considered control processes performed by both DHS and Shared Services SA (SSSA).

We also considered DHS's internal audit coverage when designing and performing audit procedures.

Audit findings and comments

Assessment of controls

In my opinion, the controls exercised by the Department of Human Services in relation to the receipt, expenditure and investment of money, the acquisition and disposal of property and the incurring of

liabilities, except for matters outlined under 'Communication of audit matters', are sufficient to provide reasonable assurance that the financial transactions of the Department of Human Services have been conducted properly and in accordance with law.

Communication of audit matters

Matters identified by the audit were detailed in a management letter to the Chief Executive. The main matters raised and related responses are detailed below.

Brokerage care services

In 2017-18 DHS paid $195.1 million ($180.9 million) to care service providers who were engaged through brokerage arrangements.

Weaknesses in brokerage care services controls and processes

For a number of years we have recommended that DHS improve its controls to ensure that brokerage care services invoiced by non-government organisations (NGOs) were received by clients prior to DHS making payment. The importance of improving controls in this area was highlighted in 2015-16. DHS identified that an NGO, which had been providing care and support services to Disability SA clients through brokerage funded arrangements for a number of years, was being investigated as to whether services had been provided in line with payments made by DHS.

In 2016-17 DHS advised us that responsibility for providing brokerage care services would transfer from DHS to the National Disability Insurance Agency (NDIA) when the NDIS was fully implemented in South Australia. This was planned to occur by 30 June 2018. Consequently, DHS was not planning to commit significant resources to addressing known control weaknesses. DHS did advise that a number of controls were in place to try to prevent fraud against DHS while it was responsible for providing brokerage care services.

Our review in 2017-18 identified that due to a high turnover of staff in the brokerage care services area, a number of controls implemented in prior years were not being performed, or were not being performed as intended. We also noted that DHS had identified a number of potential billing anomalies with a service provider over a number of years. A letter was sent to this service provider in April 2018 requesting that a review of this matter be performed by the service provider and the outcome advised to DHS. DHS advised that a final response has not been received from the service provider and it is working closely with them regarding invoicing processes.

DHS advised us that they expect all DHS eligible clients will transition to the NDIS in 2018-19. Therefore, some level of brokerage care services will continue to be paid by DHS in 2018-19. If controls over the provision of these services do not operate as intended, DHS may pay for brokerage care services that are not received or are not of a standard required by contracts in place with NGOs, resulting in financial loss or reputational risks to DHS.

Concessions payments

In 2017-18 DHS made concessions payments of $160.6 million ($152.8 million).

Outstanding concessions issues from prior years

In prior years we have performed a comprehensive review of concessions administered by DHS. This included a data analytics review of concessions in 2015-16 which resulted in a Supplementary Report to Parliament. As part of this data analytics review, and a follow-up review performed in 2016-17, we identified and reported a number of issues and recommended improvements to the way DHS administers concessions, including the systems used.

In 2016-17 DHS advised us that an external review of its ConcessionsSA business would be performed on the concession systems, processes and scheme design. In April 2018, an external contractor was appointed to perform the review between 1 May 2018 and 30 June 2018. The findings of the review may significantly impact how DHS administers concessions. Because of other resourcing priorities, DHS advised that a number of issues we raised in prior years are being resolved, or are on hold until the review findings are received. These include the following.

Issues with concessions data quality in the Concessions and Rebate Tracking System (CARTS)

We have previously raised concerns about the quality of data in CARTS and recommended that DHS systematically check all records. DHS has previously advised that resourcing priorities do not support systematic checking processes for all records but some records are checked and updated where a discrepancy or error is identified.

DHS advised it is implementing a data warehouse to allow for exception reporting and ad hoc analysis of CARTS data, and this will be operational in 2018-19.

Limited validation of water and sewerage concession payments to pensioners prior to payment

We have previously identified and reported there is limited validation of water and sewerage concession payments to pensioners prior to payment. DHS advised it is considering options for increasing the extent of validation of these payments in the future.

DHS and energy retailers operating outside of the established energy concession scheme

We previously identified that DHS and energy retailers are operating outside of the established SA Government Customer Concession Scheme for Energy. DHS has previously advised that although it believes it adheres to the intent of the scheme, it does not follow certain aspects of it as it considers it impractical to do so.

To partially mitigate the risk of operating outside of the scheme, DHS has issued letters to energy retailers outlining each party's responsibilities. Based on legal advice this acts as a contractual agreement. Despite this, DHS agreed in 2016-17 that the scheme should be updated following the completion of the external review.

Status of the Cost of Living Information System (COLIN)

The project to implement COLIN for paying the cost of living concession is not completed. DHS has not assessed whether the expected tangible and intangible benefits from the project were fully realised. It advised us that the project will be completed in 2018-19.

If the issues we have raised are not adequately addressed, inappropriate concessions payments may be made resulting in financial loss or reputational risks to DHS.

We asked DHS for a copy of the findings from the external review of the ConcessionsSA business once the review has been finalised. We also asked DHS to advise us how it plans to address the findings of the external review and whether any planned changes to the ConcessionsSA business will address the issues we have raised in prior years.

DHS advised it had received the final report of the external review. The review recommendations propose program analysis and policy review, which will be used to identify opportunities for streamlined and efficient concessions policy and associated IT enhancements. We will continued to monitor developments.

Shared Services SA – financial systems and transaction processing environments

SSSA processes financial transactions on behalf of DHS under service level determinations. The main systems and control environments include accounts payable, payroll and general ledger financial functions.

Our review and evaluation of controls for these systems concluded that controls were effective for 2017-18.

SSSA is discussed further in the commentary under 'Department of the Premier and Cabinet' in this Report.

Interpretation and analysis of the financial report

Highlights of the financial report – controlled items

	2018 $'million	2017 $'million
Expenses		
Employee benefits expenses	389	377
Supplies and services	305	286
Grants, subsidies and client payments	642	567
Other expenses	186	110
Total expenses	1 522	1 340
Income		
Revenues from fees and charges	125	117
Commonwealth revenues	116	75
Other revenues	43	28
Total income	284	220
Net cost of providing services	1 238	1 120
Revenues from (Payments to) SA Government	1 258	1 126
Net result	20	6
Other comprehensive income	-	-
Total comprehensive result	20	6
Net cash provided by (used in) operating activities	74	10

	2018 $'million	2017 $'million
Assets		
Current assets	273	202
Non-current assets	193	202
Total assets	466	404
Liabilities		
Current liabilities	165	121
Non-current liabilities	79	81
Total liabilities	244	202
Total equity	222	202

Statement of Comprehensive Income

Expenses

In 2017-18 total expenses increased by $181.6 million to $1.5 billion. This included increases in grants, subsidies and client payments ($74.8 million), other expenses ($76.7 million), supplies and services ($18.8 million) and employee benefits expenses ($11.7 million).

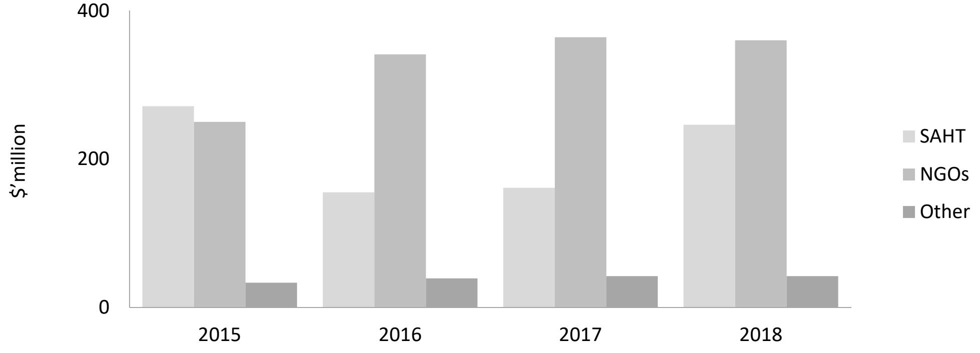
Grants, subsidies and client payments

Grants, subsidies and client payments of $641.9 million ($567.1 million) are DHS's largest expenditure category. The major grant recipients by program in 2017-18 include:

- disability grants $262.8 million ($281.2 million), which fell because of the impact of the NDIS transition
- SAHT, $245.7 million ($161.4 million) which increased by $84.3 million, largely because of the reinstatement of tax equivalent regime funding that has not been paid since 2016
- specialist homelessness services, $65.4 million ($63.4 million).

Note 7 of DHS's financial report discloses a detailed list of grants, subsidies and client payments by program and recipient type.

The following chart shows grants, subsidies and client payments by recipient type for the four years to 2018.



Funding to NGOs decreased by $3.4 million in 2017-18 to $360.1 million. Refer note 7.3 of DHS's financial report for a detailed list of NGO payments by organisation. Grants to NGOs will decrease

significantly in future years as disability clients fully transition to the NDIS and as other disability and aged care reforms transfer the provision of these services from DHS to the non-government sector. The discussion under 'Disability and aged care reform' below provides more information on this.

Other expenses

The increase in other expenses of $76.7 million is largely due to a $57.9 million increase in NDIS payments. This increase is due to the continuing transition of clients to the NDIS in 2017-18, with funding associated with these clients transferred from DHS to the NDIA. Transition eligibility was:

- children aged between zero and 14 years from 1 July 2013 (based on age)
- young people aged between 15 and 17 from 1 January 2017
- adults between the ages of 18 and 64 from 1 July 2017.

Other expenses increased due to an $18.4 million increase in aged care and disability services reform payments to the Commonwealth, up from $59.4 million in 2016-17 to $77.8 million. This payment to the Commonwealth is for services provided by the Commonwealth to clients that are the responsibility of the State under the Transition to a National Disability Insurance Scheme bilateral agreement. In 2017-18 this amount includes a payment of $25.9 million for the transition of clients over the age of 65 years to the Commonwealth Continuity of Support program.

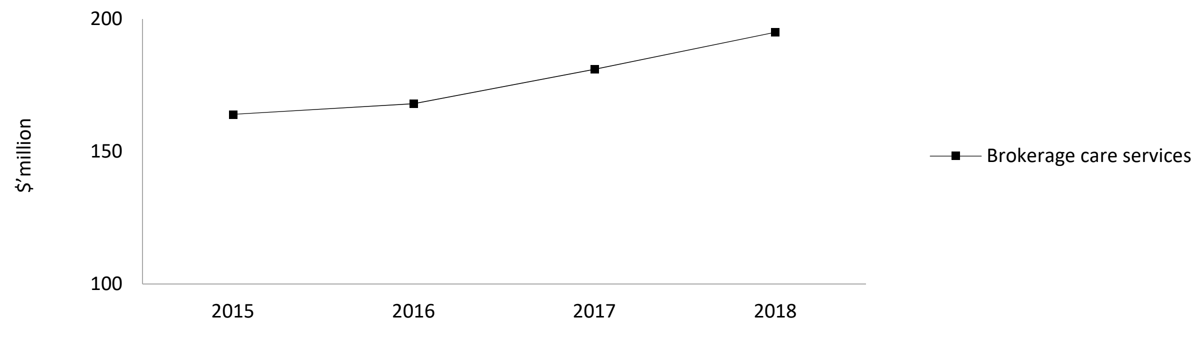
Supplies and services

In 2017-18 supplies and services expenses increased by $18.8 million to $304.6 million. Brokerage care services expenses of $195.1 million account for 64% of this total and increased by $14.3 million from 2016-17.

Previously we have reported that we expected brokerage care services expenses would significantly decrease as eligible disability clients transitioned to the NDIS. Given all eligible disability clients were due to transfer by 30 June 2018, we expected that brokerage care services expenses would decrease in 2017-18. We were advised that this was not the case because:

- there were delays in eligible adults transitioning to the NDIS in 2017-18. Although all existing clients were due to transition by 30 June 2018, we were advised there were approximately 6700 existing clients that will transition to the NDIS in 2018-19
- those existing clients that are yet to transition are more complex, higher cost clients. DHS continues to pay the costs associated with these clients
- there is constantly increasing demand for brokerage care services.

The following chart highlights the growing demand for brokerage care services and the associated expenses for the four years to 2018.



Employee benefits expenses

Employee benefits expenses increased by $11.7 million to $388.6 million in 2017-18. This is mainly due to:

- a $4.5 million increase in eligible termination payments. This is due to sector retention payments to eligible employees who transferred from DHS to the Royal District Nursing Service South Australia (RDNS SA) as part of the transition of domiciliary care services to non-government management on 29 June 2018. The discussion under 'Transfer of domiciliary care services to non-government management' below provides more information.

  This amount also includes termination payments to three executives in 2017-18
- a $2.6 million increase in long service leave expenses
- a $1.7 million increase in salaries and wages primarily due to general pay increases throughout the year
- a $1.7 million increase in targeted voluntary separation package payments. 28 employees had packages paid out in 2017-18 compared to 12 in 2016-17.

Income

In 2017-18 total income increased by $64.2 million to $284.1 million. This included increases in Commonwealth revenues ($40.7 million), revenues from fees and charges ($8.6 million), other income ($7.9 million) and resources received free of charge ($6.8 million).

Commonwealth revenues

Commonwealth revenues increased to $115.9 million in 2017-18 from $75.2 million. This increase of $40.7 million is primarily due to DHS receiving for the first time in 2017-18 revenue from the DisabilityCare Australia Fund totalling $33 million. Revenue raised by the Commonwealth for the July 2014 increase to the Medicare levy has been received into the DisabilityCare Australia Fund for the purposes of reimbursing governments for NDIS expenditure. This payment in 2017-18 is for the State's share of Medicare levy increases for entitlements from previous years.

DHS also received for the first time funding of $6.7 million for the Continuity of Support program, which is for providing services to disability clients over the age of 65 years who are the responsibility of the Commonwealth under the Transition to a National Disability Insurance Scheme bilateral agreement.

Revenues from fees and charges

Revenues from fees and charges increased by $8.6 million to $125.4 million largely due to a $7.2 million increase in recoveries. This increase was mainly made up of an additional $5.1 million in disability recoveries of unspent grant funds.

Other income

Other income increased by $7.9 million in 2017-18, primarily due to a payment from RDNS SA on 29 June 2018 for the transfer of domiciliary care services from DHS to the RDNS SA. The discussion under 'Transfer of domiciliary care services to non-government management' below provides more information.

Resources received free of charge

Resources received free of charge increased by $6.8 million in 2017-18 due to services received free of charge from SSSA. This is because for the first time this year the appropriation amount paid to agencies was reduced by the amount payable to SSSA and this amount was paid directly to SSSA by the Department of Treasury and Finance (DTF).

Revenues from and payments to SA Government

Revenues from the SA Government increased by $146.5 million to $1.3 billion, offset by a $14.8 million increase in payments to the SA Government.

Revenues from the SA Government increased due to a $138.1 million increase in appropriations from the Consolidated Account and an $8.4 million increase in contingency funding.

The increase in appropriations from the Consolidated Account primarily relates to net increases in grants paid for the SAHT and funding from the DisabilityCare Australia Fund paid through DTF appropriation.

The $8.4 million increase in contingency funding primarily relates to $4.5 million in funding for Multicultural Community Infrastructure Investment Fund grants and $2.7 million in funding for enterprise bargaining agreement supplementation.

The $14.8 million payment to the Consolidated Account relates to the return of proceeds for asset sales, including at Magill and Cavan, and for asset sales at Elizabeth and Park Holme associated with the transfer of domiciliary care services from DHS to the RDNS SA on 29 June 2018. The discussion under 'Transfer of domiciliary care services to non-government management' below provides more information.

Statement of Financial Position

Assets

Cash and cash equivalents of $228 million and property, plant and equipment of $168.2 million represent 85% of DHS's total assets.

Total assets increased from $404.3 million to $466.5 million as at 30 June 2018, largely due to an $82 million increase in DHS's cash and cash equivalents balance. This is due to additional cash held for material NDIS and Commonwealth invoices to be paid in July 2018. DHS's cash balance also includes $142.9 million ($124.2 million) held within the Accrual Appropriation Excess Funds Account, which is not available for general use but can only be used in line with the Treasurer's/Under-Treasurer's approval.

The increase in DHS's cash balance was offset by a $12.5 million decrease in property, plant and equipment due to disposals and depreciation and an $8.9 million decrease in non-current assets classified as held for sale as four properties were sold during the year.

Liabilities

Total liabilities increased by $41.8 million to $243.8 million. This was largely due to a $41.8 million increase in payables resulting from a $25.9 million payable to the Commonwealth for the Continuity of Support program and a $10 million payable to DTF’s Consolidated Account for the repayment of proceeds for asset sales throughout the year.

Highlights of the financial report – administered items

	2018 $’million	2017 $’million
Expenses		
Grants, subsidies and client payments	202	187
Client trust payments	13	13
Other expenses	5	5
Total expenses	220	205
Income		
Grants and contributions	11	10
Client trust receipts	12	14
Other income	2	1
Total income	25	25
Net cost of providing services	195	180
Revenues from (Payments to) SA Government	197	191
Net result	2	11
Total comprehensive result	2	11
Assets		
Current assets	71	68
Non-current assets	26	29
Total assets	97	97
Liabilities		
Current liabilities	11	13
Total liabilities	11	13
Total equity	86	84

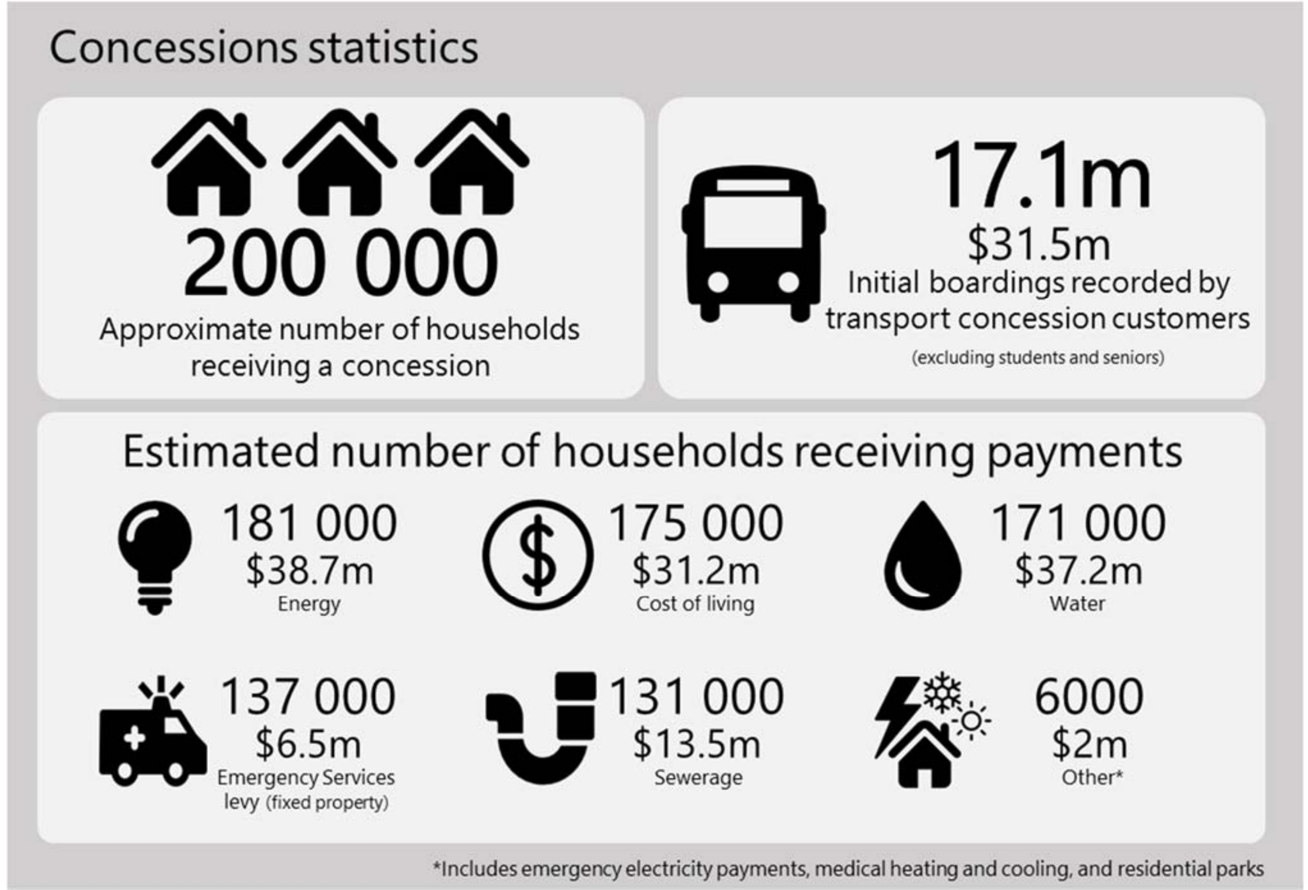
Statement of Administered Comprehensive Income

Administered expenses

Grants, subsidies and client payments of $201.7 million represent 92% of total administered expenses. This balance is largely made up of concession payments (80%).

Concession payments increased by $7.8 million to $160.6 million. This is due to a $4.1 million increase in energy concessions and a $3.5 million increase in water and sewerage rate concessions, due in part to annual CPI increases. DHS continued making supplementary payments to energy retailers who updated the details of concession holders who had previously been denied payment due to DHS’s client records differing from those of the energy retailer.

The following chart highlights concession payments by number and value in 2017-18.



DHS advised that approximately 200 000 households received an SA Government concession in 2017-18. Most of these households received more than one concession type during the year and therefore one household may show up in more than one concession type above.

Further commentary on operations

National Disability Insurance Scheme

2017-18 Stage 2 of NDIS Implementation and Governance Review

The NDIS is a new insurance based scheme designed to change the way that support and care is provided to people with permanent and significant disabilities. It seeks to create opportunities for people with disability to live 'an ordinary life' and provides support in line with defined and agreed criteria.

The NDIS has been gradually rolled out across Australia since 2013 and it was expected all eligible existing South Australian specialist disability clients would transition to the NDIS by 30 June 2018. Due to delays this is now expected to occur in 2018-19.

The primary role of South Australia under the bilateral agreement with the Commonwealth is to plan, assist, encourage and manage eligible participants to transition to the NDIS. The NDIS involves contractual payments between the Commonwealth and SA Governments to fund the scheme.

Annual expenditure on disability services in South Australia is currently $760 million and will rise significantly to $1.5 billion by 2019-20 (indexed annually), with $723.1 million provided by the SA Government.

The State's bilateral contribution to the NDIS scheme in 2017-18 was forecast to be $305 million. However, due to the delays in the transition of existing South Australian specialist disability clients, the actual NDIS payment to the Commonwealth in 2017-18 was $96 million ($161 million in contributions less $31.3 million cash ceiling adjustments and $32.9 million DHS 'in-kind services,' for example the supported accommodation DHS continues to provide to disability clients).

In 2017-18, the total expenditure for the NDIS Reform division is $646.5 million. This consists of $190.3 million supplies and services expenditure (predominantly brokerage care expenses) and $264.3 million grant expenditure, mainly relating to the funding of disability services to the NGOs existing clients who have not yet transitioned to the NDIS. There are also bilateral agreement payments of $96 million for NDIS payments for clients who have transitioned and $77.8 million for Aged Care and Disability Services Reform payments to the Commonwealth. The remainder of the NDIS Reform program expenditure relates to employee benefits expenses of DHS employees, NDIS projects and initiatives and depreciation and amortisation.

Our 2017-18 audit considered the role of DHS in the transition to the NDIS. From 1 July 2017 adults aged 18 to 64 were able to enter the scheme (depending on geographical location). The scope of the review included:

- DHS actions to address the issues we raised in 2016-17. We found all issues from the previous year were satisfactorily addressed
- understanding current governance structures in place to manage the transition
- understanding the risks for DHS and the State due to the delay in transition to the NDIS and any unplanned or unforeseen issues that have arisen and DHS's response
- identifying the impact of the NDIS transition on DHS's 2017-18 financial statements.

There were no audit findings from our review, however we identified areas of significance for the State's transition to the NDIS. Commentary on these areas can be found in Part A of this Report under 'National Disability Insurance Scheme'.

Disability and aged care reform

On 7 February 2017 the SA Government approved a number of significant changes to the way disability and domiciliary care services will be provided in South Australia, in response to Commonwealth disability and aged care reform. These changes, along with the continuing transition to the NDIS, had a significant impact on DHS's operations, structure and finances in 2017-18 and will continue to do so in future years. Key aspects of this reform to date are detailed below.

Transfer of domiciliary care services to non-government management

In late 2016-17 DTF's Commercial Projects Group, in conjunction with DHS, started processes to appoint a non-government provider of domiciliary care services in South Australia. In November 2017

it was announced that RDNS SA, part of the Silver Chain Group, had been appointed as the new provider. Provision of these services transferred from DHS to RDNS SA on 29 June 2018. The transfer did not include any of the in-home care services provided by the Country Health SA Local Health Network Incorporated or the Aged Care Assessment Program delivered by SA Health.

As part of the transfer agreement RDNS SA paid DHS for the transfer of this business, including the sale of land and building assets associated with the business at Elizabeth and Park Holme. As part of the transaction, DHS also paid RDNS SA to take on the leave liabilities of the employees who transferred from DHS to RDNS SA on 29 June 2018. All eligible transferring employees were also paid a sector retention payment by DHS for transferring to RDNS SA to encourage them to remain in the sector to ensure continuity of care for clients.

DHS will continue to provide some administrative services to RDNS SA in the short-term in line with the Transitional Services Agreement in place between the two entities.

Establishment of Supported Community Accommodation Services public corporation

On 21 November 2017 the Public Corporations (Supported Community Accommodation Services) Regulations 2017 established a new Supported Community Accommodation Services public corporation. A Chief Executive was appointed in March 2018, and a Board and Audit and Risk Committee were established. The provision of supported community accommodation services was due to transfer from DHS to this new public corporation in 2018-19 once governance structures were established.

The new SA Government, elected in March 2018, decided not to go ahead with the new public corporation and the Public Corporations (Supported Community Accommodation Services) (Dissolution and Revocation) Regulations 2018 dissolved the public corporation, effective 16 August 2018. We have been advised that the provision of these services will remain with DHS in the interim. DHS will gradually withdraw from service provision and clients will receive services from the non-government sector.

The employment contract of the Chief Executive was terminated effective 29 June 2018 and the remaining term of her five-year contract was required to be paid out by the SA Government.

All financial transactions of the Supported Community Accommodation Services public corporation entered into during the year have been reported as part of DHS's 2017-18 financial report.

Establishment of employee-led mutual for early childhood early intervention (ECEI) services

An employee-led mutual was set up as a company limited by guarantee on 8 February 2018 for the provision of ECEI services under the NDIS. The employee-led mutual will be established separate from the public sector to deliver the ECEI services through a cooperative or mutual governance structure, whereby members of the organisation can be involved in decision-making. The NDIA provided funding of $2.2 million to support the establishment of the new service provider.

A grant agreement was signed between the SA Government and the NDIA for the provision of ECEI services in South Australia, which runs from 1 March 2018 to 31 December 2022. This agreement will initially be delivered by DHS's Child and Youth Services division while the employee-led mutual is established. The agreement, however, requires that the mutual must be established and the

agreement with the NDIA novated to the mutual by 30 September 2018. When this occurs, those DHS employees who have agreed to transfer to the mutual will become employees and members of the mutual. This arrangement is designed to result in the mutual operating as a private company in the NGO sector. It will have a service and funding relationship with and be accountable to the NDIA, not the SA Government. If the mutual is not established by 30 September 2018 and the agreement is not novated, DHS will be required to provide ECEI services for a further 12 months under the agreement.

We have been advised that all eligible DHS employees transferring to the mutual will be paid a sector retention payment by DHS for transferring to the mutual to encourage them to remain with the mutual to ensure continuity of care for clients.

Other planned disability and aged care reforms

Other planned disability and aged care reforms impacting DHS in the future include:

- the transfer of ASSIST therapy services to the disability services provider Minda by the end of 2018
- the market process to transfer domiciliary equipment services to the non-government sector in 2018-19.

Machinery of government changes

The election of a new SA Government in March 2018 resulted in a number of changes to DHS, including a name change from the Department for Communities and Social Inclusion effective from 17 May 2018, and machinery of government transfers related to Housing SA and Multicultural Affairs, effective from 1 July 2018.

In relation to Housing SA, the Public Sector (Reorganisation of Public Sector Operations – South Australian Housing Trust) Notice 2018, gazetted on 28 June 2018, transferred all employees from Housing SA within DHS to the SAHT, effective 1 July 2018.

In relation to Multicultural Affairs, the Public Sector (Reorganisation of Public Sector Operations) Notice 2018, gazetted on 14 June 2018, transferred 11 employees from DHS to the Department of the Premier and Cabinet, effective 1 July 2018.

Any budget transfers associated with the above changes were also effective from 1 July 2018.

Independent Commissioner Against Corruption (ICAC)

Financial statistics	Net cost of providing services:	$13 million
	Revenues from SA Government:	$14 million
	Number of FTEs:	54.5

Significant events and transactions

- The functions of the Office of the Police Ombudsman were transferred to the Office for Public Integrity as at September 2017.
- The Commissioner released two major reports in 2017-18: 'The Evaluation of the Practices, Policies and Procedure of the Public Trustee' and 'Oakden: A Shameful Chapter in South Australia's History'.

Financial report opinion — **Unmodified**

Financial controls opinion — **Unmodified**

Functional responsibility

The Independent Commissioner Against Corruption (the Commissioner) and the Office for Public Integrity (the OPI) are established under the *Independent Commissioner Against Corruption Act 2012*.

The activities of both the Commissioner and the OPI are included in the financial report as they constitute a single entity, ICAC, for financial reporting purposes.

The primary functions of the Commissioner are to identify and investigate corruption in public administration and prevent or minimise corruption, misconduct and maladministration in public administration through referral of potential issues, education and evaluating practices, policies and procedures.

The primary function of the OPI is to receive and assess complaints and reports about public administration, corruption, misconduct and maladministration and to make recommendations for taking action on them.

Note 2 of the ICAC financial report further explains the objectives and functions of the Commissioner and the OPI.

Scope of the audit

The audit program covered major financial systems to obtain sufficient evidence to form an opinion on the financial report and internal controls.

Specific areas of audit attention in 2017-18 included:

- corporate governance
- expenditure
- payroll
- assets
- general ledger.

Internal audit activities were considered in designing and performing audit procedures.

Audit findings and comments

Communication of audit matters

A management letter was sent to the Commissioner raising a number of minor areas where controls over purchasing, payroll and asset management could be improved. ICAC responded that it would take action to address all our concerns.

Shared Services SA – financial systems and transaction processing environments

Shared Services SA processes financial transactions on behalf of ICAC under service level determinations. The main systems and control environments include accounts payable, payroll and general ledger financial functions.

Our review and evaluation of controls for these systems concluded that controls were effective for 2017-18.

Shared Services SA is discussed further in the commentary under 'Department of the Premier and Cabinet' in this Report.

Interpretation and analysis of the financial report

Highlights of the financial report*

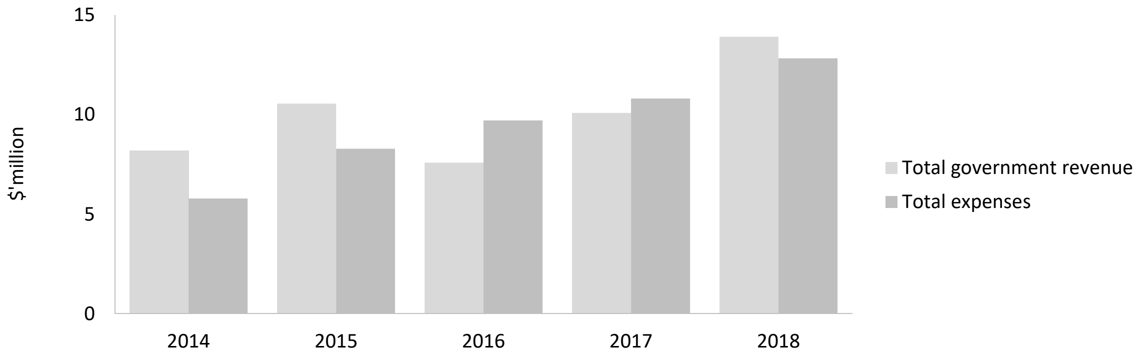
	2018 $'million	2017 $'million
Expenses		
Employee benefits expenses	8	7
Supplies and services	4	3
Other expenses	1	1
Total expenses	13	11
Net cost of providing services	13	11

	2018 $'million	2017 $'million
Revenues from SA Government	14	10
Net result and total comprehensive result	1	(1)
Net cash provided by (used in) operating activities	3	1
Net cash provided by (used in) investing activities	(1)	(1)
Assets		
Current assets	6	3
Non-current assets	5	5
Total assets	11	8
Liabilities		
Current liabilities	3	2
Non-current liabilities	1	1
Total liabilities	4	3
Total equity	7	6

* Table may not add due to rounding.

Statement of Comprehensive Income

The following chart shows total expenses and total government revenue over the past five years.



The chart shows that both expenses and government revenue increased significantly over the period reflecting ICAC's increased level of activity, particularly in 2018 when two major reviews were undertaken.

Expenses

ICAC's expenses increased by $2 million to $12.8 million.

Employee benefits expenses increased by $944 000 due to an increase in the number of employees as the Office of the Police Ombudsman (OPO) transferred to OPI in 2017-18.

Supplies and services also increased by $811 000 mainly due to increased operating lease payments, up $131 000, as a result of the OPO transfer and increased legal fees, up $514 000, due to the engagement of external legal services to assist in investigations into maladministration in public administration, in particular the Oakden review.

Income

ICAC relies on revenues from the SA Government, which increased by $3.8 million to $13.9 million in response to ICAC's operating and investing costs.

Statement of Financial Position

Assets

ICAC's assets increased by $2.7 million to $11.1 million. This is mainly due to an increase in cash of $2.3 million. Refer to comments under 'Statement of Cash Flows' below for details of the increase.

Liabilities

ICAC's liabilities increased by $1.5 million to $4.3 million. The major items causing this change were:

- employee benefit liabilities increasing by $369 000 to $1.8 million, due mainly to increases in annual leave of $111 000 and long service leave of $243 000 as a result of the transfer of OPO employees and their associated leave entitlements
- payables increasing by $1.2 million to $1.8 million due primarily to creditors for office fitout costs of $1.2 million.

Statement of Cash Flows

Cash and cash equivalents at 30 June 2018 were $5.5 million ($3.2 million). Net cash provided by operating activities was $2.8 million, an increase of $2.2 million from 2017 due mainly to an increase in revenues from the SA Government of $3.8 million, partially offset by increases in employee benefits payments, up $963 000, and supplies and services payments, up $556 000.

Lifetime Support Authority of South Australia (LSA)

Financial statistics	Provision for future costs of current participants:	$398 million
	Lifetime Support Scheme Fund levy net of duty:	$136 million
	Investments:	$598 million
	Net assets:	$199 million
	Number of FTEs:	50.1
	Number of interim participants as at 30 June:	89
	Number of lifetime participants as at 30 June:	77

Significant events and transactions

- The provision for future cost of caring for current participants increased by $92 million.
- The total number of participants increased from 113 in 2016-17 to 166 in 2017-18.
- The LSA made an operating surplus of $42 million and has net assets totalling $199 million, meaning the Lifetime Support Scheme remains fully funded at 30 June 2018.

Financial report opinion

Unmodified

An emphasis of matter was included in the financial report opinion relating to significant inherent uncertainty surrounding the estimate of the provision for participants’ treatment, care and support services because of the long-term nature of the provision and limited participants’ experience to date.

Financial controls opinion

Unmodified

Functional responsibility

The LSA is established under the *Motor Vehicle Accidents (Lifetime Support Scheme) Act 2013* (the LSS Act).

The LSA administers the Lifetime Support Scheme (LSS or the Scheme) and the LSS Fund established by the LSS Act to support people who suffer very serious injuries in motor vehicle accidents in South Australia, regardless of fault. A person can be accepted as an interim or lifetime Scheme participant depending on their eligibility under the LSS rules.

Lifetime Support Scheme Fund

Levies on motor vehicle registrations to pay for the Scheme expenses are collected by the Registrar of Motor Vehicles and paid into the LSS Fund. The LSA invests the levies with the Superannuation Funds Management Corporation of South Australia (Funds SA) until needed to pay for participants' treatment, care and support and other costs of operating the Scheme.

Scope of the audit

The audit program covered major financial systems to obtain sufficient evidence to form an opinion on the financial report and internal controls.

Specific areas of audit attention in 2017-18 included:

- processes for determining applications from people injured in motor vehicle accidents
- procurement of service providers
- payment for service providers according to service plans tailored to the needs of each participant
- employee benefits and other administrative expenses
- investments
- service level agreements with other SA Government agencies.

Internal audit activities were considered in planning and conducting the audit.

Audit findings and comments

Auditor's report on the financial report

The following is an extract from the Independent Auditor's Report issued for LSA's 2017-18 financial report, which is unmodified but notes a significant inherent uncertainty relating to the provision for participants' treatment, care and support services.

Opinion

In my opinion, the accompanying financial report gives a true and fair view of the financial position of the Lifetime Support Authority of South Australia as at 30 June 2018, its financial performance and its cash flows for the year then ended in accordance with the Treasurer's Instructions issued under the provisions of the Public Finance and Audit Act 1987 *and Australian Accounting Standards.*

Significant inherent uncertainty – provision for participants' treatment, care and support services

Without qualification to the opinion expressed above, attention is drawn to note 20 of the financial report. There is significant inherent uncertainty surrounding the estimate of the provision for participants' treatment, care and support services because of the long-term nature of the provision and limited participants' experience to date. This uncertainty will remain until sufficient participants' experience is available.

Communication of audit matters

Matters identified by the audit were detailed in a management letter to the Chief Executive Officer. While there were no major matters raised, we recommended that the LSA develop and implement payroll policies and procedures; review payroll reconciliation reports; review user access to its Salesforce participant management system; and implement a review over vendor file changes. A positive response was received from LSA.

Shared Services SA – financial systems and transaction processing environments

Shared Services SA processes financial transactions on behalf of the LSA under service level determinations. The main systems and control environments include accounts payable, payroll and general ledger financial functions.

Our review and evaluation of controls for these systems concluded that controls were effective for 2017-18.

Shared Services SA is discussed further in the commentary under 'Department of the Premier and Cabinet' in this Report.

Interpretation and analysis of the financial report

Highlights of the financial report

	2018 $'million	2017 $'million
Expenses		
Participant treatment, care and support expenses	130	114
Duty on LSS Fund levy	15	15
Other	13	9
Total expenses	158	138

	2018 $'million	2017 $'million
Income		
LSS Fund levy	151	149
Investment revenue	49	33
Other	-	23
Total income	200	205
Net result from operating activities	42	67
Total comprehensive result	42	67
Net cash provided by operating activities	107	116
Net cash used in investing activities	107	116
Assets		
Current assets	4	3
Non-current assets	598	465
Total assets	602	468
Liabilities		
Current liabilities	41	28
Non-current liabilities	362	283
Total liabilities	403	311
Total equity	199	157

Statement of Comprehensive Income

This is the fifth year of operation of the LSA and the fourth year of the LSS. The level of financial activity of the LSA rose as more participants entered the Scheme and the investment base increased.

Net result

The LSA achieved a surplus of $42.1 million ($66.9 million). Actual outcomes in 2017-18 were:

- the LSS Fund levy received was $3.1 million over the $147.6 million estimate
- actual LSS costs were $158.2 million, including a $115.3 increase in the provision for participant care costs.

The LSA's net result depends significantly on the interdependence between the LSS Fund levy set before the start of the year and the movement in the provision for the cost of participants' treatment, care and support services determined at the end of the year. Both the levy and the provision are determined using reports prepared by an independent actuary appointed by the LSA (refer to commentary under 'Liabilities' and 'Required fund contribution' below).

The net result was also impacted by investment revenues of $49.5 million ($32.8 million) and a reduction in insurance recoveries of $22.5 million.

Expenses

The LSA's expenses of $158.2 million ($137.8 million) comprised:

- $130.2 million ($113.5 million) for participants' treatment, care and support expenses, of which $115.3 million was the increase in the estimate of future expenses for participants injured in motor vehicle accidents up to 30 June 2018

- $15 million ($14.8 million) paid to the SA Government for the 11% duty on the LSS Fund levy payable under the *Stamp Duties Act 1923*
- $2.8 million ($3.2 million) for brokerage fees and premiums paid to reinsurers who provide cover for significantly larger than expected liabilities for estimated future participant care costs
- $10.2 million ($6.3 million) for general operating expenses including $4.8 million ($3.1 million) for employee benefits, and $2.5 million ($581 000) for research, education and programs.

Income

The LSA's income of $200.3 million ($204.6 million) mainly comprised:

- $150.7 million ($148.9 million) of LSS Fund levy on South Australian motor vehicle registrations. No GST is payable on the levy
- $49.5 million ($32.8 million) of investment revenue. The result reflected favourable investment markets. There were no changes in LSS Fund strategy during the financial year.

Statement of Financial Position

The LSA's financial position depends significantly on the value of its investments exceeding the provision for participants' treatment, care and support services. The LSA's net assets increased by $42.1 million to $198.9 million and reflect the net result from operations discussed under 'Net result' above.

Assets

The LSA's assets of $602.2 million consist mainly of cash, investments and receivables. A reduction in receivables of $22.7 million relates to there being no recoveries expected this financial year from the LSA reinsurance program.

Investments

At 30 June 2018 the LSA had $597.8 million invested with Funds SA in line with the investment strategy approved by the LSA Board.

The LSA must maintain investments to fund its present and likely liabilities for participants' treatment, care and support services. The LSA investment strategy takes into account its current risk appetite and the need to match investment returns to the long-term nature and timing of payments associated with the needs of Scheme participants.

The LSA's investments with Funds SA earned a nominal return of 9.4% in 2017-18 compared to its target of 6.25%.

Liabilities

The LSA's liabilities of $403.3 million consist mainly of the provision for participants' treatment, care and support services.

Provision for participants' treatment, care and support services

The provision was estimated to be $397.8 million at 30 June 2018, a rise of $92 million.

The main reason for the increase was the rise in the number of participants during the year from 113 in 2016-17 to 166 in 2017-18. The inflation rate and investment return rate used in the actuarial calculation remained the same as in 2016-17. Other assumptions such as the weighted mean term (estimated length of claim) changed only marginally over 2016-17. Refer note 20 of the LSA's financial report for further details.

The LSA appointed an independent actuary to estimate the liabilities of the Scheme, measured as the present value of the expected future payments for claims incurred up to 30 June 2018, including claims incurred but not yet reported. The LSA Board approved the valuation prepared by the scheme actuary after also considering the report from the peer review actuary.

Information relating to the actuarial estimation is provided in note 20 of the LSA's financial report.

Significant inherent uncertainty in the provision

The LSA's financial report refers to the significant inherent uncertainty surrounding the actuarial estimation and the sensitivities of the estimation to changes in key assumptions, and comments on the long-term nature of the liabilities and volatility around the number of participants and their injury severity. In estimating the liability at 30 June 2018, the actuary noted that the LSS is in its infancy and limited experience exists to assess the reasonableness of initial LSS costings. The actuary also noted that, due to the very long-term nature of the LSS, the actual experience in the short period since 1 July 2014 tells very little about the Scheme and is not sufficient, in isolation, to inform long-term future assumptions.

The independent actuary referred to the significant inherent uncertainty in the projected outcomes of future claim costs for long-term claims. The main areas of uncertainty identified were the:

- adequacy of benchmarks for defining the lifetime care and support needs of participants, including models of expected cash flows for an individual of a specific age with a specific injury
- future inflation levels for services, especially increases in attendant care hourly rates. Changes in best practice treatment also mean liabilities could increase significantly
- final stable severity for each participant's injury. The current assessment for each participant is at very early duration since injury.

The sensitivity analysis in note 20 of the LSA's financial report illustrates that relatively small changes to key assumptions in the estimate can result in changes in the order of millions of dollars.

For example, a 1% increase in the mortality improvement assumption can increase the provision by $23 million and a 1% increase in the long-term discount rate can increase the provision by $68.9 million.

Note 20 of the LSA's financial report also indicates the time frame over which the LSA must manage claims. The uninflated, undiscounted weighted mean term is 21.1 years.

Independent reviewing actuary

The LSA had the actuarial estimate confirmed by an independent reviewing actuary, who noted that the valuation results were not unreasonable in the circumstances and early development of the Scheme.

Having an independent reviewing actuary is prudent given the long-term purpose of the Scheme and the critical role actuarial expertise has in setting the levy annually and estimating the outcome at the end of each year.

The Scheme is not an insurance scheme

The LSA determined the provision under AASB 137 'Provisions, Contingent Liabilities and Contingent Assets' and not AASB 1023 'General Insurance Contracts'. The latter is more prescriptive in the permitted choice of the rate of investment return (discount rate) to be adopted in deriving the present value of liabilities. It also requires risk margins to be added to the central estimate of the liability, increasing the liability. Consistent with similar interstate schemes, the LSA has not applied a risk margin to its central estimate.

Probability of sufficiency

As at 30 June 2018 the probability of sufficiency for the LSS was 78%. The LSA has a target minimum probability of sufficiency of 70% (the chance that the capital of the LSS is expected to be adequate to cover actual outcomes) through a solvency margin in excess of actuarial provisions.

Current liabilities

At 30 June 2018 current liabilities exceeded current assets by $37.5 million. Most of the balance of current liabilities is the $36.7 million provision for participants' treatment, care and support services. The LSA can access funds from its Funds SA investments if required.

Required fund contribution

The LSA must determine, before the beginning of each financial year, an amount it considers is required to be contributed to the LSS Fund to meet expenses for the period. This amount is to:

- fund the present and likely future liabilities for participants who enter the Scheme in the period
- meet payments from the LSS Fund that exceed previously provided amounts estimated
- pay stamp duties
- provide for other matters in connection with any LSA liability under the LSS Act, including paying for any past liability that would otherwise be unfunded.

That determination is made in line with a report from an independent actuary engaged by the LSA after consulting the Treasurer. The LSA must report its determination to the Minister before the beginning of each financial year.

The Minister must, on receiving a report and taking into account such matters (including matters not covered by the report) as the Minister thinks fit, and after consulting the Treasurer, determine an amount to be paid to the LSA for contribution to the LSS Fund for the relevant period (the required fund contribution).

If the Minister makes a determination that is inconsistent with the LSA's determination, the LSA must report that in its annual report.

Setting levies at an appropriate level is critical to the LSS. If break-even levies are charged each year and if all underlying assumptions used to set the levy eventuate, the LSS will always be fully funded. If the levy is set too low each year, liabilities will eventually exceed assets causing the LSS to be under-funded.

Annual contribution and levy

The estimated levy of $147.6 million including duty was required to cover the costs of operating the Scheme in 2017-18 and probable liability at 30 June 2018.

The following table sets out the required fund contribution and levy for the past three years.

	2017	2018	2019
Required fund contribution:			
LSA recommended ($'million)	145.8	147.6	154.7
Minister approved	Yes	Yes	Yes
Average levy ($)	102.54	102.54	104.59
Average increase per vehicle over previous year ($)	0.05	-	2.05

The actuary's estimates used to set the levy are, as with the estimated provision, sensitive to the number of LSS participants and the severity of their injuries. Small changes in these numbers can impact significantly on the estimates.

2017-18 levy

The estimated 2018-19 levy was based on an actuarial estimate at 31 December 2017.

Statement of Cash Flows

The Statement of Cash Flows reflects the investment of $107.2 million with Funds SA using the LSS Fund levy of $151 million. The LSA will use these investments to meet the costs of treatment, care and support services over the life of the Scheme participants.

Motor Accident Commission (MAC)

Financial statistics	Outstanding claims liability:	$853 million
	Other financial assets:	$1012 million
	Return of capital:	$359 million
	Net result:	$143 million
	Number of FTEs:	30.28
	MAC Fund assets exceeded the targeted solvency level by $143 million (116% of the targeted level).	
Significant events and transactions	— MAC sold its investment property portfolio for $565.5 million on 31 July 2017. — MAC paid $359.4 million to the Highways Fund in June 2018 as a return of capital. — The outstanding claims liability reduced by $344 million.	
Financial report opinion	**Unmodified**	
Financial controls opinion	**Unmodified**	

Functional responsibility

MAC is established under the *Motor Accident Commission Act 1992* (the MAC Act).

MAC's main functions are to promote road safety awareness and manage the run-off of claims against compulsory third party (CTP) insurance policies issued to motor vehicle users in South Australia before 1 July 2016.

MAC's responsibility to perform the functions of the nominal defendant transferred to the CTP insurance regulator (the CTP Regulator) from 1 January 2017.

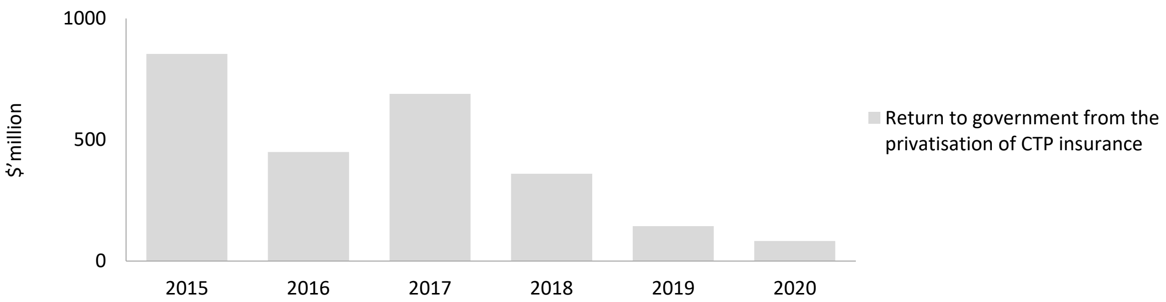
Return of capital – payment to the Highways Fund

The 2014-15 State Budget identified that, after ceasing to be the sole provider of CTP insurance for South Australia, MAC would be able to return surplus net assets to the Highways Fund to improve road safety.

In June 2018 MAC paid $359.4 million ($688.2 million) to the Highways Fund. This payment was made out of the net assets in excess of the level required for sufficient solvency of the MAC Fund. The Treasurer directed, consistent with section 26(2) of the MAC Act, that the payment be made to the Highways Fund, which is administered by the Department of Planning, Transport and Infrastructure.

As the payment has been made from MAC's surplus net assets as directed by the Treasurer, it was treated as a return of capital in the financial report and recorded as a reduction in MAC's assets and total equity. As such, this payment is not reflected in MAC's total comprehensive result for 2017-18.

The following chart demonstrates the 2017-18 State Budget projection that a total of $2.5 billion will be returned to government by MAC by 2019-20. MAC has already paid $2.35 billion, including the payment of $359.4 million in 2017-18.



Further capital returns are projected

MAC's solvency position provides a margin of $142.7 million more than the established sufficient solvency target at 30 June 2018. The projected return of a further $135 million, as outlined in the 2017-18 State Budget, will reduce this margin. This is expected to be offset by reductions in the outstanding claims actuarial estimate as claims continue to settle and there is greater certainty of the remaining liability.

It will be important for MAC to continue to focus on managing claims within the established estimates to maintain a margin above solvency, and to provide for further returns in future years.

Scope of the audit

The audit program covered major financial systems to obtain sufficient evidence to form an opinion on the financial report and internal controls.

Specific areas of audit attention in 2017-18 included:

- investment assets

- claim payments
- outstanding claims liability
- return of capital.

Audit findings and comments

Communication of audit matters

Our audit did not identify any matters that required formal communication to the Chief Executive.

Shared Services SA – financial systems and transaction processing environments

Shared Services SA processes financial transactions on behalf of MAC under service level determinations. The main systems and control environments include accounts payable, payroll and accounts receivable functions.

Our review and evaluation of controls for these systems concluded that controls were effective for 2017-18.

Shared Services SA is discussed further in the commentary under 'Department of the Premier and Cabinet' in this Report.

Interpretation and analysis of the financial report

Highlights of MAC's consolidated financial report

	2018 $'million	2017 $'million
Net claims	128	259
Net investment returns and fees	(7)	37
Road safety expenses	(14)	(13)
Management expenses	(26)	(34)
Total revenue	14	14
Net result before market value movements	95	263
Investment market value movements	48	98
Total comprehensive result	143	361
Net cash inflows (outflows) from operating activities	349	668
Assets		
Current assets	1 024	1 587
Non-current assets	3	4
Total assets	1 027	1 591

	2018 $'million	2017 $'million
Liabilities		
Current liabilities	266	369
Non-current liabilities	616	861
Total liabilities	882	1 230
Equity	145	361

Return of capital

In June 2018 MAC paid $359.4 million ($688.2 million) to the Highways Fund. The payment has been treated as a return of capital in the financial report and is recorded as reductions in MAC's assets and total equity. For further information about this payment refer to 'Return of capital – payment to the Highways Fund' above.

Sale of investment property portfolio

MAC's property portfolio was offered for sale through an expression of interest in 2015-16, with the properties classified as assets held for sale.

On 6 July 2017, following SA Government approval, the Minister for Finance directed MAC, under section 5(3) of the MAC Act, to approve the sale of its property portfolio for $565.5 million. The sale was finalised on 31 July 2017, with the sale price reflected as the fair value of the assets held for sale at 30 June 2017.

The property portfolio was sold because of the need for the MAC Fund to have greater liquidity during the claims run-off process. MAC's revised role requires a transition to a higher proportion of defensive assets in its investment portfolio, to protect capital, while achieving a portfolio of investments with characteristics that are sufficiently liquid to allow MAC to meet identifiable claims as and when they are due.

Road safety funding

In July 2016 MAC entered into a funding arrangement with the CTP Regulator. Funding of $13.9 million ($13.5 million) was provided to MAC in 2017-18 to perform its road safety functions. These activities were previously funded from MAC's premium revenues but are now specifically funded through the CTP Regulator as a component of CTP premiums. As required by MAC's charter, transactions related to road safety activities are maintained by MAC in a separately established Road Safety Fund.

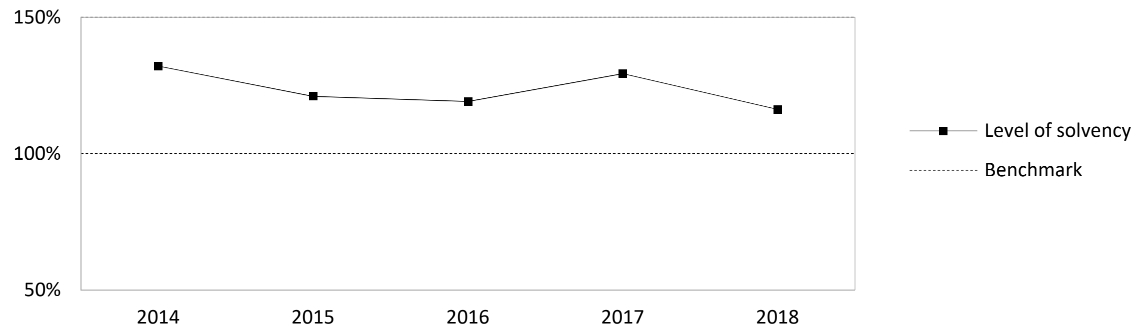
Solvency level is above the target level

Section 13A of the MAC Act requires MAC to seek to achieve and maintain a sufficient level of solvency for the MAC Fund using a formula determined by the Treasurer.

The formula issued by the Treasurer on 7 December 2016 specifies the MAC Fund will have a sufficient level of solvency if its assets exceed its liabilities. Full details are included in note 25 of MAC's financial report.

As at 30 June 2018 the target level of assets was $881.2 million. The MAC Fund's assets as at that date were $1023.9 million, $142.7 million above the target level. This equates to 116.2% (129.3%) of the targeted solvency level.

The following chart shows the level of solvency achieved over the past five years.



As discussed above, the level of solvency has increased importance given MAC has ceased writing new CTP policies and is now running off existing claims. Any shortfalls or deterioration in claims experience cannot be met by future premiums, although MAC's liabilities are guaranteed by the Treasurer under section 21 of the MAC Act.

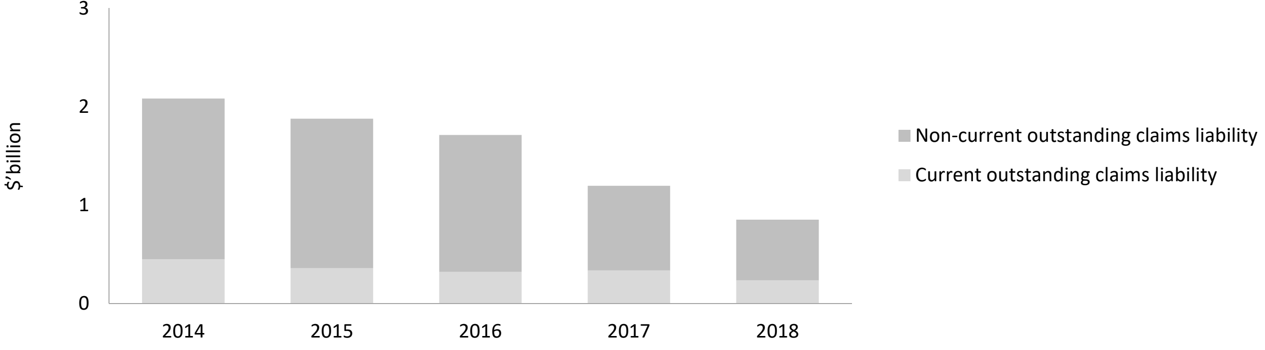
Outstanding claims liability

MAC's primary liability is for outstanding claims from the period before 1 July 2016. The liability covers claims reported but not yet paid, claims incurred but not yet reported, the anticipated direct and indirect costs of settling those claims and estimated reinsurance and other insurance costs.

Calculating the liability is an estimation process and a range of factors, including economic assumptions, affect the calculation. As a result, professional actuaries need to perform the calculation and, for reporting purposes, detailed disclosure of the assumptions needs to be included in the notes of the financial report.

In 2017-18 MAC's primary independent actuary was Finity Consulting Pty Ltd (Finity), consistent with the prior year. Details of the actuary's calculations and assumptions are provided in note 16 of MAC's financial report.

The following chart shows the outstanding claims liability for the five years to 2018, with the continuing decrease a reflection of the run-off process since 1 July 2016.



Factors considered by the actuary that impact the estimate of amounts required to settle claims include the:

- number of claims incurred
- length of time taken to settle the claim
- average amount of claim payments
- inflation and discount rates used.

The outstanding claims liability consists of the 'old scheme' for claims prior to 1 July 2013, and the 'new scheme' for claims from that date to 30 June 2016. Legislative reform from 1 July 2013 changed scheme entitlements and, as a result, the two schemes are considered separately by Finity.

The new scheme introduced thresholds for economic and non-economic loss and placed caps on legal fees. Compensation for non-economic loss under the new scheme is based on a severity of injury scale, with an indexed maximum cap on damages.

Examples of the potential impact of changes to these assumptions are included in note 16 of MAC's financial report. Some of these are shown in the table below.

	Impact on provision %	Financial impact $'million
Average size of large claims increased by 43% (old scheme)	8.1	68.5
Average size of large claims increased by 43% (new scheme)	5.3	44.9
Discount rate increased from 2.5% to 3% p.a.	(1.3)	(11.2)

The risk margin achieves 80% probability the provision is adequate

Also impacting on the outstanding claims liability calculation are the solvency requirements determined by the Treasurer under the MAC Act that require a risk margin to be included in the provision to achieve an 80% probability the provision is adequate. This requirement exceeds the Australian Prudential Regulation Authority's nominated target of 75% probability, as set out in Prudential Standard GPS 320 'Actuarial and Related Matters'.

$344 million reduction in the outstanding claims liability

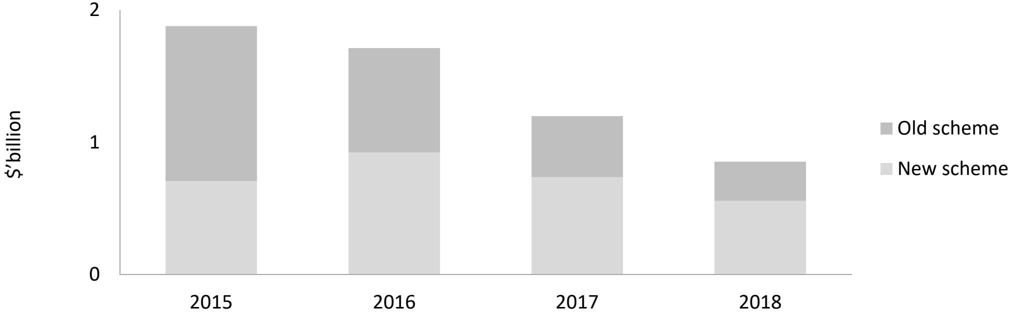
The $344 million decrease in the liability at 30 June 2018 was due to payments totalling $216 million made to settle claims in 2017-18 and changes to a range of assumptions in the actuarial calculations, particularly:

- a $101 million reduction due to a reduced number of expected future claim payments due to:
  - a decrease of $48 million in expected payments based on claims experience
  - the reduced estimated number of settlements for the new scheme of $32.5 million
  - saving on the allowance for large claims of $30.3 million
  - a decrease of $11.5 million due to economic assumption changes including a lower allowance for wage inflation (now 3% p.a., down from 3.25%)
  - offset by an increase of $20 million due to fewer smaller claim (below cap) settlements and low payment volumes for larger claims (above cap)

- a $44 million reduction in the risk margins, which remain at the same percentages as the 2017 valuation, following claim payments and other decreases in expected future claims

- offset by a reduced discount to present value of $17 million due to claims being a year closer to expected settlement.

The chart below shows the proportion of outstanding claims for the new and old schemes for the last four years.



As at 30 June 2018, CTP claims under the new scheme represent 65% (62%) of the outstanding claims liability. Claim numbers and values have so far been lower than expected under the new scheme and the outstanding claims liability calculation has therefore been adjusted to reflect this.

While the higher proportion of new scheme claims has a role in the reduction of the outstanding claims liability, as expected after introducing scheme reform, there is a higher level of uncertainty about these claims due to the limited claims experience to date. Accordingly, MAC has included a higher risk margin for the new scheme compared to the risk margin applied to the older claims, increasing the estimated liability when calculating the outstanding claims liability.

The claim estimate process is externally peer reviewed

As was the case in 2017, in 2018 the claims liability calculation was subject to external peer review by Taylor Fry Consulting Actuaries. The independent reviewing actuary reported that:

- nothing had come to their attention that would lead them to believe the actuarial assessment conducted by Finity was unreasonable

- while the 2018 actuarial assessment conducted by Finity had considerably reduced the outstanding claims liability, the reduction was based on recent claims experience and did not appear unreasonable

- the valuation provides a balance between optimistic and cautious assumptions and therefore represents a reasonable central estimate

- the claims handling expense assumption and risk margin are reasonable but are likely to increase as payments run off.

Estimated timing of the settlement of claims

The estimated timing of payments to settle claims is shown in the following table.

Up to 1 year $'million	2-4 years $'million	5-9 years $'million	10-14 years $'million	15-19 years $'million	Total $'million
237	449	117	37	9	850

Statement of Comprehensive Income

MAC's financial performance is significantly influenced by two interrelated aspects of its business:

- net claims – influenced by the number of claims and the estimated costs of settling those claims
- investment result – investment operations are an integral part of any insurance business as the estimated return on invested funds is a significant component of the business strategy.

AASB 1023 'General Insurance Contracts' requires market value accounting to be adopted when valuing investments. This means the investment result includes not only interest and related income received, but also changes in the market values of investments held at balance date. Changes in the market values of investments can be subject to wide fluctuations and it is important to emphasise that investment market value movements recognised in MAC's financial report are unrealised. That is, until the investments are sold, no gain or loss is actually received or incurred by MAC.

Net claims

There has been no premium income since MAC ceased issuing new policies from 1 July 2016.

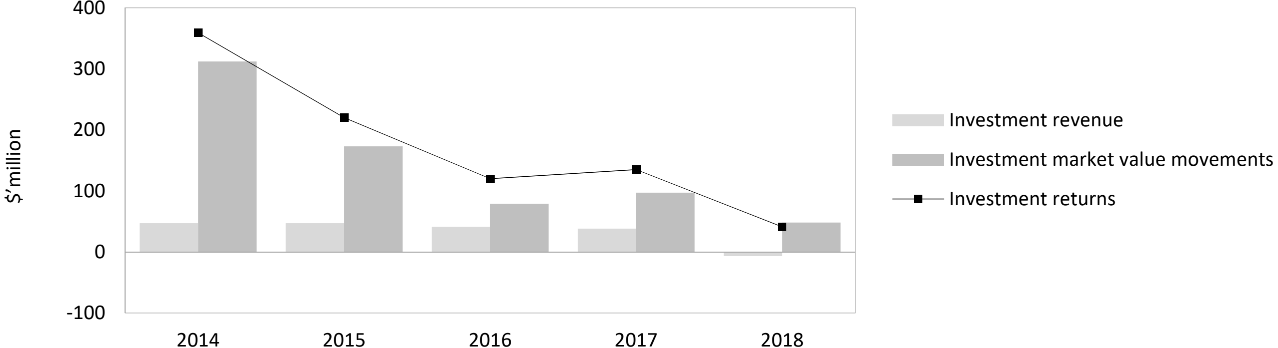
The overall net claims result of $128 million is a combination of actual claim payments and the movement in the outstanding claims liability. The $131 million reduction in net claims in 2017 is mainly from a $171 million decrease in the movement of the outstanding claims provision, which is explained further under 'Outstanding claims liability' above. There was also a decrease of $39 million in gross claim payments to $216 million ($255 million).

Investment result

MAC uses the Superannuation Funds Management Corporation of South Australia (Funds SA), the SA Government's investment body, to manage most of its investment portfolio. MAC holds investments in unit trusts within Funds SA where the majority of income is derived through movements in the value of unit holdings rather than through direct receipt of interest and dividend income.

MAC's investment returns this financial year resulted in a surplus of $41 million compared with $135 million the previous year. The investment result is a combination of investment revenue and investment market value movements, offset by Funds SA management fees and direct operating costs. Investment returns decreased by $94 million due mainly to a $49 million decrease in the market value movement, reflecting the reduced amounts invested, and a decrease in investment revenue of $45 million due to the sale of the investment property portfolio on 31 July 2017.

An analysis of MAC's investment result for the five years to 2018 is shown in the following chart.



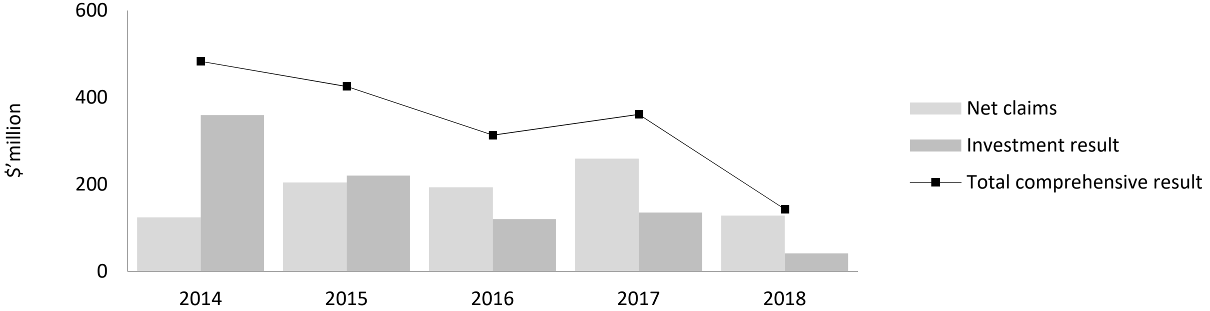
Note 19(6) of MAC's financial report explains market risk and illustrates the effect of market movements. An example of the impact of market risk is if interest rates move by (1%) the financial impact would be $30.8 million.

In considering the impact of market movements on investments, it should be noted that the total invested is expected to reduce significantly over the next two years in line with projected claim settlements.

Total comprehensive result

MAC's total comprehensive result for 2018 was a profit of $143 million compared to a $361 million profit in the previous year. The $218 million decrease is a result of a number of factors as previously mentioned.

The following chart provides a breakdown of the contribution of the net claims and investment results to the total comprehensive result.

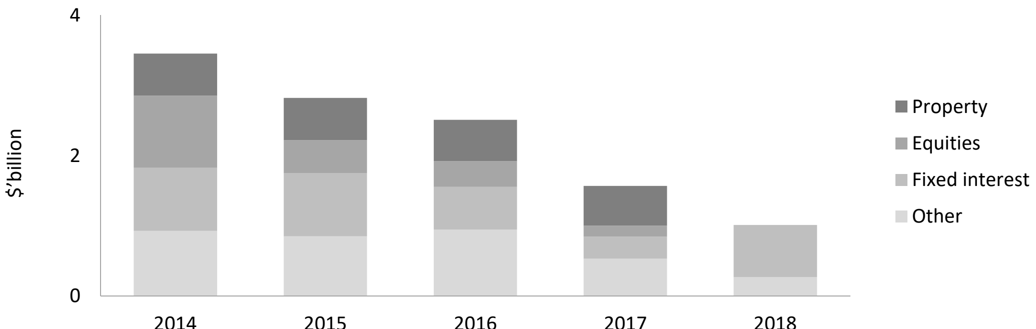


Statement of Financial Position

Investments

MAC does not directly hold investments in equities but rather has interests in Funds SA's pooled investment portfolios. MAC is responsible for setting the investment objectives and strategic asset allocation for the various investment sectors. Funds SA is responsible for managing the investment portfolios in line with the agreed asset allocations and regularly reporting investment performance.

For the five years to 2018 a structural analysis of investment assets (excluding cash) is shown in the following chart.



The chart shows the steady decline in total investment assets, excluding cash, from $3.5 billion in 2014 to $1 billion in 2018. The decrease of $555 million in 2018 was principally due to:

- the return of capital of $359 million
- claim payments of $216 million (as there is no longer any premium income to offset these expenses).

The chart also shows the move to more defensive assets in 2017 and 2018, as discussed further below.

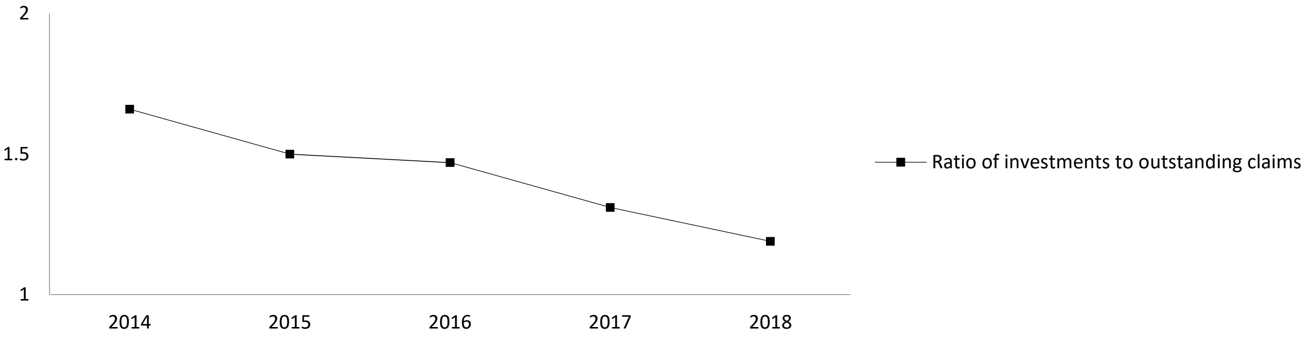
MAC increases the proportion of defensive assets

In June 2017 the Treasurer approved MAC's 2017-18 asset allocation, which was revised to a 10% (20%) allocation to growth assets and 90% (80%) to defensive assets. In July 2018 the Treasurer approved MAC's 2018-19 asset allocation, which was revised to 100% defensive assets. At 30 June 2018 the actual asset allocation of investments managed by Funds SA was a 100% allocation to defensive assets, with an associated reduction in the targeted rate of return.

The move to an increased allocation of defensive assets reflects the need to carefully manage existing holdings while running down the outstanding claims.

Investments exceed estimated liability

The investments (excluding cash) to outstanding claims ratio shows the value of MAC's investments is sufficient to cover the value of its outstanding claims at 30 June 2018. The decrease in the ratio in 2018 reflects the $555 million decrease in the value of investments relative to the smaller $344 million reduction in outstanding claims liability. This further highlights the need to carefully manage existing holdings while running down the outstanding claims. The ratio of investments, excluding cash, to outstanding claims liability is shown in the following chart.



Statement of Cash Flows

MAC's cash position decreased by $10 million. This reduction was $10 million less than 2017 due to:

- a $319 million decrease in net operating cash flows, resulting mainly from:
  - a $1042 million decrease in interest and other investment income (predominantly relating to the redemption of Funds SA investments to fund claim payments in 2017, the $688.2 million return of capital in June 2017 and the $105 million payment for distributions to four private insurance and the CTP Regulator)
  - offset by the $565.5 million proceeds from the sale of the direct property portfolio
- a $329 million decrease in net cash flows used in financing activities, relating to the lower return of capital in 2018 compared to 2017.

Department of Planning, Transport and Infrastructure (DPTI)

Financial statistics

Total expenses:	$1778 million
Commonwealth grants income:	$743 million
Net revenue from providing services:	$134 million
Net revenues from SA Government:	$960 million
Equity contributions from SA Government:	$262 million
Capital expenditure:	$1157 million
Total non-current assets:	$26 billion
Number of FTEs (excluding Rail Commissioner):	2386
Administered	
Total income:	$1172 million
Disbursements to third parties:	$1014 million
Payments to Consolidated Account:	$113 million

Significant events and transactions

- $359 million was received from the Motor Accident Commission and paid into the Highways Fund.
- Commonwealth grants increased by $186 million to $743 million mainly to fund road and rail projects.
- Property, network assets and plant and equipment assets were revalued upwards by $281 million.
- The State Valuation Office transferred to the Department of Treasury and Finance (DTF) on 1 July 2017 and the Office of the Registrar-General transferred to DTF on 1 February 2018. Both offices transferred back to DPTI on 1 July 2018.

Financial report opinion

Unmodified

Financial controls opinion

Modified

Key issues:

- Procurement, contract management and project delivery require further improvement
- Across government facilities management arrangements require improvement

Functional responsibility

DPTI is an administrative unit established under the *Public Sector Act 2009* and is responsible for transport systems and services, infrastructure planning and provision, sporting infrastructure and strategic land use for South Australia.

Scope of the audit

The audit program covered major financial systems to obtain sufficient evidence to form an opinion on the financial report and internal controls.

Specific areas of audit attention in 2017-18 included:

- accounts payable
- payroll
- bus contracts
- grants and subsidies
- fees and charges, including motor registrations, drivers licences and Metrotickets
- income and expenditure for maintenance, property rental and building construction services
- accounts receivable
- bank reconciliation
- general ledger
- governance including risk management and legal compliance
- project delivery and management
- procurement and contract management
- fixed assets including capital works, network assets, land, buildings and facilities, and plant and equipment.

In addition, we considered internal audit activities to identify and assess the risks of material misstatement in the financial report and to design and perform audit procedures.

Audit findings and comments

Assessment of controls

In my opinion, the controls exercised by the Department of Planning, Transport and Infrastructure in relation to the receipt, expenditure and investment of money, the acquisition and disposal of property and the incurring of liabilities, except for all matters outlined under 'Communication of audit matters', are sufficient to provide reasonable assurance that the financial transactions of the Department of Planning, Transport and Infrastructure have been conducted properly and in accordance with law.

Communication of audit matters

Matters identified by the audit were detailed in management letters to the Chief Executive. The main matters raised and related responses are detailed below.

Further opportunities to improve procurement and contract management

Procurement and contract management is a significant aspect of DPTI's operations, with DPTI spending over $2 billion on goods, services and construction annually.

Since August 2014 DPTI has undergone significant organisational restructure and has reformed its operations, including its procurement and contract management processes.

In response to recommendations made by an independent consultant in 2016, and as part of its procurement modernisation project, DPTI developed an implementation plan with 48 separate projects. The plan was largely focused on organisational change to develop and align procurement and contract management activities with contemporary practice.

Since then we have reported on DPTI's progress in implementing these changes. Our 2016-17 Report commented that about half of the recommendations were outstanding.

Reform progress in 2017-18

DPTI closed the procurement modernisation project in February 2018, having completed most of its intended changes. Responsibility for the remaining items was transferred to DPTI's Procurement and Contract Management Directorate. DPTI has now implemented:

- a single executive accountable for all procurement and contract management activity across DPTI
- a new procurement and contracting structure
- a defined category management framework
- strategies for actively engaging with industry and suppliers
- spend analytics, opportunity assessment and analysis for potential savings, and active monitoring of savings and benefits
- a centralised structure for procurement and contract management
- a training and development program, capability framework and feedback opportunities.

The following actions were incomplete:

- developing a suite of effective procurement policies (see below)
- implementing IT systems for procurement processes, supplier relationship management and contract lifecycle management
- establishing an online catalogue and work flow process for goods and services procurement.

Now that DPTI has largely reformed its procurement and contract management processes, it must also update its large volume of documented policies and procedures. As at July 2018, of DPTI's:

- six policies, one needs review and three were pending approval
- 95 procedures, 66 need review and 20 were either under review or pending approval
- 242 templates, 228 need review and nine were either under review or pending approval.

DPTI advised us that it expects to complete its review of policies and procedures by 30 June 2019.

Internal audits identified concerns with contract management

DPTI has made significant efforts to improve procurement and contract management practices over the past two years and has allocated internal audit resources to review and identify areas for further improvement. In 2017-18 DPTI's internal audit function performed reviews over aspects of procurement and contract management and made the following important observations.

Contract management: $4 million – $10 million

In September 2017 internal audit completed a review of contract management for contracts valued between $4 million and $10 million. Internal audit raised the following significant matters:

- the absence of governance and management oversight and ongoing formal reporting on contract progress and compliance
- existing policies and procedures often lacked relevance, completeness or sophistication and were outdated, and there was an absence of documented guidance and better practice examples. The audit observed that:
  - DPTI had not established standard requirements for contract management meetings and other communication, and formal contract performance meetings were not routinely held with contractors or were often not adequately documented
  - there was little guidance on the approvals required for varying non-financial elements of a contract (eg timing, scope, quality), and when additional approval or legal advice should be obtained
- a lack of consistent practices for managing contracts observing that:
  - contract management staff were not managing similar types of contracts in a consistent manner across DPTI, and in some business units there was a general lack of clarity regarding roles and responsibilities for contract management
  - eight of the 12 contracts reviewed by internal audit had no contract management plans prepared, and two of the plans were of a poor standard. In addition, DPTI's policies did not specify that contract management plans were required for building and construction contracts
  - there was varying use of the Contract Management System. A range of other methods and systems were used across the DPTI
  - a range of systems and processes were used to document variations and the lack of system integration prevented effective recording of contract information across DPTI. It was noted where variations were undertaken, documentation was sometimes recorded in multiple locations or systems.

In general these observations demonstrate the need for DPTI to update its policy framework to reflect new practice. The volume of change required to DPTI's policies and procedures is not unexpected, given the significance of the reform program.

In my opinion, the success of DPTI's reform program depends on staff having a clear understanding of management's expectations as they relate to procurement and contract management. It is therefore important DPTI prioritises action to ensure that up-to-date policies, procedures and processes are communicated, readily available and supported by relevant training.

DPTI advised that it has established a plan to address internal audit's findings. It includes developing a contract management framework and responsibility assignment matrix to clearly outline roles and responsibilities within DPTI.

City Tramline Extension internal audit – procurement and contract management observations

In June 2018 internal audit reported on its review of the City Tramline Extension project. Internal audit's observations about procurement and contract management included:

- concerns with the weightings used in the evaluation process
- inappropriate allocation of risks between DPTI and the construction contractor
- poor timing in procuring the contract manager for the construction contract and a delay in signing the contract with the contract manager
- a lack of clarity over roles and responsibilities of the contractors and DPTI, including responsibility for project management and contract management, and the responsibilities of the outsourced contract manager
- the absence of a contract management plan to manage the outsourced contract manager appointed to manage the construction contract
- the absence of key performance indicators and documented milestones for key agreements
- difficulty that internal audit experienced in obtaining documentation because it was not centrally stored and because a number of different systems were used to store information.

In September 2018 DPTI advised us that it would develop an action plan to respond to these observations for future projects.

Findings from our review of procurement and contract management

We reviewed aspects of procurement and contract management. Our review was limited to assessing DPTI's compliance with documented or accepted practice and focused on ensuring key documents were developed, or evidence was maintained, that important processes were performed. We did not evaluate contract performance or risks for any individual contract.

We noted that:

- DPTI was unable to easily locate and provide procurement and contract documents for our review, with DPTI unable to locate conflict of interest forms for one tender process we reviewed. This observation is consistent with internal audit's findings and indicates the need to improve records management. Besides the delays caused in the audit process, the difficulties in locating key documents for audit could compromise DPTI's contract management practice
- DPTI has not documented its policies and procedures for maintaining a contract register. The contract register was incomplete and inaccurate, which could impact the efficient and effective management of contracts
- contract management plans for selected contracts were in draft format and did not include some important information describing governance arrangements, risk and performance management

- policies and procedures needed review. As noted earlier DPTI had already identified this requirement and plans to complete its review of all policies and procedures by June 2019
- one example where contract variations for construction work performed for another government agency were not approved in line with the Treasurer's Instructions.

DPTI accepted the findings and indicated it will:

- revisit records management
- review processes for capturing and recording information in the contract register, update the incomplete information and undertake regular reviews to ensure the information is updated
- ensure all officers responsible for managing significant contracts understand that a complete contract management plan is required for all significant contracts
- implement measures to ensure all variations are approved in line with the Treasurer's Instructions.

Our review also noted instances where DPTI had started works and/or paid its contractors before the formal instrument of arrangement (FIA) was signed. DPTI's internal audit made a similar observation in the review of the City Tram Extension project, noting that the contract manager contract was not signed until April 2018, 12 months after the letter of acceptance and work commenced.

We have noted delays in finalising signed contracts before, commenting that these delays increase the risk that parties to the arrangements are unclear on their respective rights and obligations, especially as the complexity of the arrangements increase. We recommended that DPTI develops a policy and/or procedure that specifies the circumstances under which FIA's are required before initiating work or making payments.

DPTI noted that it may enter a contract arrangement either through an FIA or by issuing a letter of acceptance, and that for all contracts we identified a letter of acceptance was signed by both parties before progress payments were made. DPTI does not believe a documented policy or procedure is required. DPTI further advised a letter of acceptance will only be issued at the discretion of the General Manager, Procurement and Contracting, and where extenuating circumstances are present.

Further improvements required in project governance and project delivery

Project delivery is a core component of DPTI's operations that warrants a strong control environment. In 2017-18, DPTI spent about $1.2 billion on constructing and purchasing assets, and $387 million on building projects for other SA Government agencies.

DPTI has previously identified gaps in how it manages project and program delivery

DPTI reviewed its approach to managing project and program delivery in 2015, with an external consultant's report making a range of recommendations to improve project delivery governance arrangements across all aspects of DPTI's operations, including projects delivered on behalf of other SA Government agencies.

Since that date DPTI has made significant changes to how it manages project delivery and notes that further changes are anticipated.

Recent progress

Portfolio, Program and Project Management Office (3PMO) developments

The 3PMO establishes the minimum governance, monitoring and reporting requirements applicable to all projects and provides an independent review of compliance with those requirements. Over the last two years DPTI has made the following significant changes in the governance processes of the 3PMO:

- established program owners, program structure and roles to coordinate, direct and oversee a set of related projects, subprograms and other program activities to obtain benefits not available from managing them individually
- established management phases for initialisation, preliminary business case, pre-delivery, procurement, delivery and realisation
- implemented a project governance framework and created tools and templates
- created a benefits framework to measure DPTI performance by identifying portfolio level benefit categories, key performance indicators and target measures aligned to the DPTI Strategic Plan
- developed risk register and issues register templates to improve the management of risks and issues
- categorised programs and projects based on financial categories and non-financial categories to ensure that the correct level of governance is achieved for projects
- developed a Gateway Review Process to provide transparency of decision-making
- established a post-implementation review process to improve planning and lessons learnt for future projects.

DPTI anticipates that the framework will be further refined over the next 12 months to ensure:

- further development of policies, standards and guidelines
- focus on tools, communication and capability of staff to improve the application of the project management framework to programs and projects
- continued implementation of a new project portfolio management tool.

Revised approach to delivering capital projects

The Capital Initiatives Program is DPTI's new approach for delivering capital projects. DPTI established a new directorate to manage new capital projects. As part of this new approach DPTI held an industry briefing session in August 2017 and provided information on upcoming capital works projects and proposed delivery models in August 2017. The session advised a forward program of about $9.5 billion and detailed a forward work plan to 2020-21.

All tenders for individual and bundled projects were targeted for release by October 2017, with contracts signed and works started by December 2017.

Internal audit reported the outcomes of its review of the management and governance of the implementation of the new capital initiatives approach in March 2018. Internal audit assessed the project controls were adequate, meeting the industry standard for project management and governance. The audit found inadequate project documentation version control, including approvals not being reflected within some of the project documentation.

In September 2018 DPTI advised that project documentation, including approvals, has been reviewed and updated within DPTI's records management system and that the 3PMO will continue to closely monitor the achievement of the capital initiatives program.

Changes in governance committees

In 2017-18 DPTI's Portfolio Management Committee and High-Risk High Value Category 1 Committee were dissolved and a new Project Review Panel (PRP) was established. The PRP provides assurance to the Chief Executive that programs and high-risk high value projects are on time, within scope and budget and risks are being managed effectively. The PRP is chaired by an independent member. PRP meetings are scheduled monthly and programs and projects are brought to the PRP as required but at least every quarter.

The PRP was initially established to cover projects undertaken by the Capital Initiatives Directorate. The PRP terms of reference were updated in July 2018 to cover the projects previously governed by the High-Risk High Value Category 1 Committee.

Gateway review

DPTI started performing gateway reviews in 2017-18. A gateway review is a short, independent review of a program or project undertaken at key decision points in the project's lifecycle.

A gateway review is not an audit and has no decision-making authority.

Gateway reviews are performed by a team of mostly external specialised consultants and aim to provide an independent perspective on opportunities, risks and issues facing the program or project. They provide the project's senior responsible officer with timely and independent reporting on the progress of a program or project and assurance that it can proceed successfully to the next stage.

Gateway reviews were performed for selected projects (Category 1 projects), with 19 reviews performed and a further five reviews scheduled as at July 2018.

An internal audit review of the gateway review process was completed in March 2018. The review found:

- policy and principles governing gateway reviews need further refinement, including requiring that recommendations are appropriately addressed, tailoring reviews for smaller projects, establishing criteria for project review selection and providing for project manager involvement
- the absence of a clearly defined governance framework for the escalation of findings, recommendations and actions arising from gateway reviews, including the absence of requirements for follow-up and reporting against each recommendation

- the absence of complete documentation of how DPTI initiates, manages and delivers the gateway review process. DPTI has not specified:
  - the documentation required to support a gateway review
  - the process to capture lessons learnt for future reviews
  - that project expenditure be compared to the business case throughout the project lifecycle
  - clear and objective confidence assessment and priority ratings
- the management and follow-up of gateway reviews relied on manual systems such as Excel spreadsheets, Word documents and emails.

In September 2018 DPTI advised us it had prepared and was monitoring a plan to address the above issues.

Gateway reviews are an important tool to ensure that projects have the best opportunity for success. In my opinion the matters raised by internal audit are significant and, if not addressed, may compromise the effectiveness of these reviews.

City Tramline Extension internal audit – project management observations

Internal audit completed a review of the City Tramline Extension project in June 2018. Internal audit's observations about project management included:

- *Governance*: A business case was not prepared for the project; lessons learnt from previous similar projects were not formally considered during the initiation stage; and internal audit had some difficulty obtaining documentation.
- *Project planning*: Some upfront planning activities did not occur due to restricted time frames and a lack of resources; some project components were not fully understood until construction commenced; some requirements were not referenced in the project plan; and the acquisition plan for one contractor did not include a detailed analysis of the engagement model.
- *Roles and responsibilities*: Roles and responsibilities were not defined, resulting in a duplication of effort and some key activities not being performed.
- *Management reporting*: The financial reporting in the early stages of the project was incorrect, and the reporting system limited the number of risks reported to three.
- *Risk management*: DPTI's project risk register was not updated throughout the project.

In September 2018 DPTI advised us that lessons learnt from the internal audit report will be used as part of DPTI's continuous improvement process.

Findings from our review of project delivery and management

We reviewed aspects of project delivery and management. This was limited to assessing DPTI's compliance with documented or accepted practice and focused on ensuring key project documents were developed, or evidence was maintained that important processes were performed. We did not evaluate project performance or risk management for any individual project.

We noted the following matters:

- Project management plans were not approved for some of the projects we sampled.
- DPTI has not documented procedures for the regular review of project risk registers and our review of a sample of risk registers was unable to verify the registers were reviewed on a timely basis.
- The IT system used to report project status to senior management limits the number of reportable risks to three.
- Some issue registers we reviewed were missing key information.
- Lessons learnt registers were not maintained for most projects we reviewed.
- DPTI was unable to provide some project definition reports we requested, while others were not signed or had some important information gaps.
- DPTI was unable to quickly provide some key project documents, indicating poor records management.

These issues increase the risk that projects are not managed effectively.

DPTI advised it will review the processes for reviewing and approving project management plans and project definition reports, evidencing project risk register reviews and maintaining issues registers. In addition, DPTI advised it has:

- enabled the reporting tool to link to key documents, including the risk management plan and risk register
- created a guidance document on how the lessons learnt register should be maintained and used
- reminded staff of the requirement to appropriately store relevant project information.

Across government facilities management arrangements (AGFMA)

DPTI is responsible for managing the AGFMA. These arrangements provide SA Government agencies with access to planned and unplanned maintenance, minor works and other services and are managed by DPTI's AGFMA unit. In 2017-18 these services amounted to $287 million and were provided by:

- an outsourced contractor for the central and northern Adelaide regions ($161 million)
- DPTI's Facilities Services for the southern Adelaide region and country South Australia ($126 million).

Improvement required for contract management practices for the AGFMA

We found some processes and practices to ensure key contract requirements are met need further refinement. Our main findings were as follows:

- DPTI did not regularly review and monitor the contract management plan and there was no evidence of a specific risk management plan and regular review of contract risks, increasing the risk that contract obligations and risks are not managed effectively.

- Independent audits to ensure charges for work performed by the facilities management providers are accurate and valid did not include all types of work performed and did not assess the procurement process. About 50% of financial activity was not subject to DPTI's audit coverage, increasing the risk that performance issues and incorrect charging are not identified and actioned.
- The results of the independent audits of the facilities management providers were not reported to the governance group responsible for oversight of the AGFMA. As a result, risks raised from the audits may not be addressed.
- The controls for preparing key performance indicators did not detect some errors, resulting in the risk of incorrect information being reported to the governance group responsible for oversight of the AGFMA.

DPTI advised us that it had, or would, implement appropriate corrective actions including reviewing the contract management plan and risks, increasing the scope of audits, reporting the results of audits to the governance group and implementing controls to check the preparation of key performance indicators.

Facilities Services improvements required

Facilities Services manages jobs for southern Adelaide and country South Australia regions, with expenditure of $126 million in 2017-18. Our review of Facilities Services noted that:

- a key reconciliation to ensure that payments to contractors have been recovered from the AGFMA unit was not performed
- responsibility for payment approval, data entry and checking invoice processing was not segregated at regional offices, increasing the risk of invalid or incorrect payments not being identified and actioned
- information was missing from the database used to manage small contractors. DPTI uses this database to ensure contract information is current and that service providers are adequately qualified.

DPTI responded that it planned to complete all reconciliations by December 2018 and that additional controls over payment processing at regional offices would be implemented from November 2018. DPTI also advised it was developing a new system for the management of contractors for implementation in October 2019, with procedures to be developed by November 2018 to cover the interim period.

Payroll controls did not ensure all payments were bona fide and accurate, and that all leave was recorded

In 2017-18 DPTI's employee benefits expenses amounted to $226 million, with related liabilities amounting to $95 million.

Payroll processing services are provided by Shared Services SA (SSSA) in line with a service level determination. While SSSA is responsible for the complete and accurate processing of the payroll data it receives, DPTI is responsible for ensuring payroll transactions are valid, accurate and complete.

Our previous audits have identified weaknesses in DPTI's controls for monitoring the validity, completeness and accuracy of SSSA payroll processing, including that checking processes did not ensure that all relevant payroll details for employees were checked, followed up and discrepancies appropriately actioned.

In 2017-18 DPTI implemented a new payroll verification process comprising a quarterly review of employee details (staff establishments report) and a monthly review of employee pay variations, time recording and leave (staff exceptions report).

DPTI engaged an external contractor to review these new controls. This review, which was completed in June 2018, noted:

- the approval of key reports was either outstanding or late, with 44% of staff establishment reports and 47% of staff exception reports tested outstanding
- some employees were incorrectly allocated in the reports, resulting in ineffective review of those reports
- examples where exceptions were identified but not actioned in a timely manner.

DPTI advised that it has implemented an escalation process for outstanding reports and will review the report distribution and approval functionality to streamline processes, provide additional training to managers and review the process for capturing staffing changes in the reports.

Accounts payable controls did not ensure all system access and delegations were reviewed.

Our audit noted that DPTI's check of user delegation limits did not consider purchase order approval delegations and new users. Approximately 40% of the value of DPTI's transactions are processed through purchase orders.

DPTI accepted the findings and indicated it would implement controls to address them.

Administration of Office of Recreation, Sport and Racing (ORS) grants requires improvement

Our audit noted:

- the endorsement of grant recommendations by the responsible assessment committee and ORS executive was not adequately evidenced, reducing the perceived transparency of the process for awarding grants
- some grant agreement obligations were overdue, increasing the risk that grant outcomes are not achieved.

ORS responded it would update policies and procedures to require assessment panel and ORS executive to evidence endorsement of grant recommendations, and manage overdue grant agreement obligations.

ICT and control for selected systems

We reviewed password management, privileged user access, audit logging, patch management, change management, backup and disaster recovery management for the following systems:

- Adelaide Fare Collection system (Metrocard)
- Masterpiece financial system (Masterpiece)
- motor registration and licensing system (TRUMPS).

Our review identified areas where DPTI's information security controls were inadequate, notably:

- password configuration settings were weak, increasing the risk that unauthorised users could gain access to the system (Masterpiece and Metrocard)
- documentation to support system changes was not maintained, increasing the risk of unauthorised changes to the system (Masterpiece and Metrocard)
- segregation of duties conflicts existed for some system changes, increasing the risk of unauthorised changes to the system (all three systems)
- inadequate application or database patching, increasing the risk that system vulnerabilities may be exploited (Masterpiece and Metrocard)
- lack of disaster recovery testing, increasing the risk that systems and data are unable to be recovered timely in the event of a disaster or system failure (Masterpiece and Metrocard).

DPTI responded positively to our findings with details of remediation action and time frames.

Shared Services SA – financial systems and transaction processing environments

SSSA processes financial transactions on behalf of DPTI under service level determinations. The main systems and control environments include accounts payable, payroll and general ledger financial functions.

Our review and evaluation of controls for these systems concluded that controls were effective for 2017-18.

SSSA is discussed further in the commentary under 'Department of the Premier and Cabinet' in this Report.

Other commentary

Adelaide Oval redevelopment

On 29 September 2011 the *Adelaide Oval Redevelopment and Management Act 2011* (the AORM Act) came into operation. The primary purpose of the AORM Act is to facilitate the redevelopment of Adelaide Oval and to provide for the future care, control and management of Adelaide Oval. DPTI has the principal construction management role and responsibility for the redevelopment project.

The AORM Act also requires financial supervision of the project by the Auditor-General and provides for the Auditor-General to report to Parliament on specific financial matters associated with the redevelopment and the ongoing management of Adelaide Oval. Six-monthly reports are provided to

the Parliament discharging the requirements of the AORM Act. The first Report was provided to the Parliament on 29 February 2012 and the most recent Report was on 31 August 2018.

Interpretation and analysis of the financial report

Highlights of the financial report*

	2018 $'million	2017 $'million
Expenses		
Employee benefits expenses	226	222
Supplies and services	907	897
Depreciation and amortisation	427	429
Grants and subsidies	176	131
Other expenses	42	77
Total expenses	1 778	1 756
Income		
Fees and charges	642	625
Commonwealth revenues	743	557
Sale of goods and services	166	151
Rental income	222	214
Other income	139	152
Total income	1 912	1 699
Net revenue from (cost of) providing services	134	(57)
Revenues from (Payments to) SA Government		
Revenues from SA Government	990	1 604
Payments to SA Government	(30)	(61)
Total revenues from (payments to) SA Government	960	1 543
Net result	1 094	1 486
Other comprehensive income		
Changes in revaluation surplus	281	101
Total comprehensive result	1 375	1 587
Net cash provided by (used in) operating activities	1 507	1 951
Net cash provided by (used in) investing activities	(1 145)	(979)
Assets		
Current assets	4 142	3 538
Non-current assets	26 059	25 096
Total assets	30 201	28 634
Liabilities		
Current liabilities	299	341
Non-current liabilities	141	156
Total liabilities	440	497
Total equity	29 761	28 137

* Table may not add due to rounding.

The following chart shows the breadth and scale of DPTI's activities, identifying 2017-18 operating expenses by activity and the value of fixed assets held to support these activities.

Activity

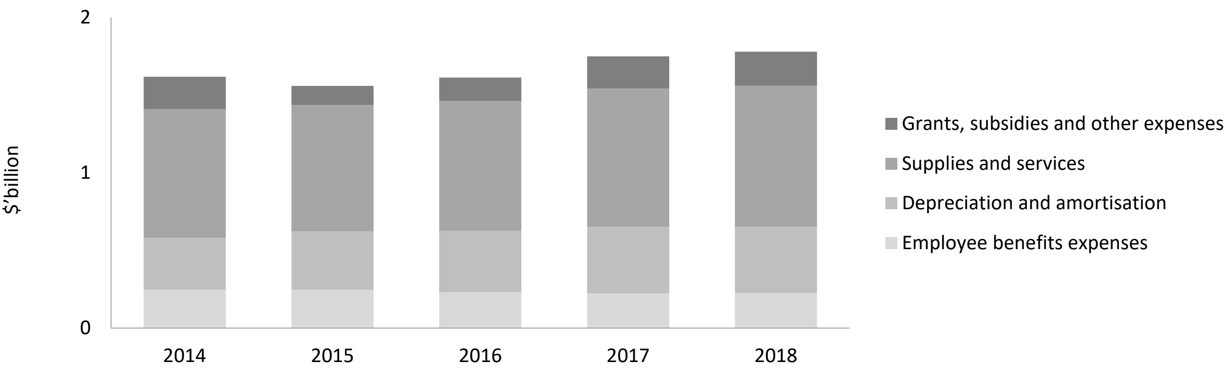
Activity	Operating expenses	Fixed assets
Roads and marine	$545m in operating expenses	$21.5b in fixed assets
Public transport	$584m in operating expenses	$2.8b in fixed assets
Infrastructure planning and management	$481m in operating expenses	$1.3b in fixed assets
Recreation, sport and racing	$85m in operating expenses	$281m in fixed assets
Other activity	$89m in operating expenses	$4m in fixed assets

Note: The net loss or gain on the disposal of non-current assets is recognised by activity in the chart above.

Statement of Comprehensive Income

Expenses

For the five years to 2018, a structural analysis of DPTI's major expense items is shown in the following chart.



Expenses for the year totalled $1778 million ($1756 million) and are mainly attributable to:

- supplies and services expenses of $907 million (51%), of which $212 million was for bus service contract payments, $159 million was for operating costs of major infrastructure maintenance and other service contracts, $167 million was for operating lease expenses and $140 million was for property expenses
- depreciation and amortisation expense of $427 million (24%), of which $290 million was for network assets, $60 million was for plant and equipment and $71 million was for buildings and facilities

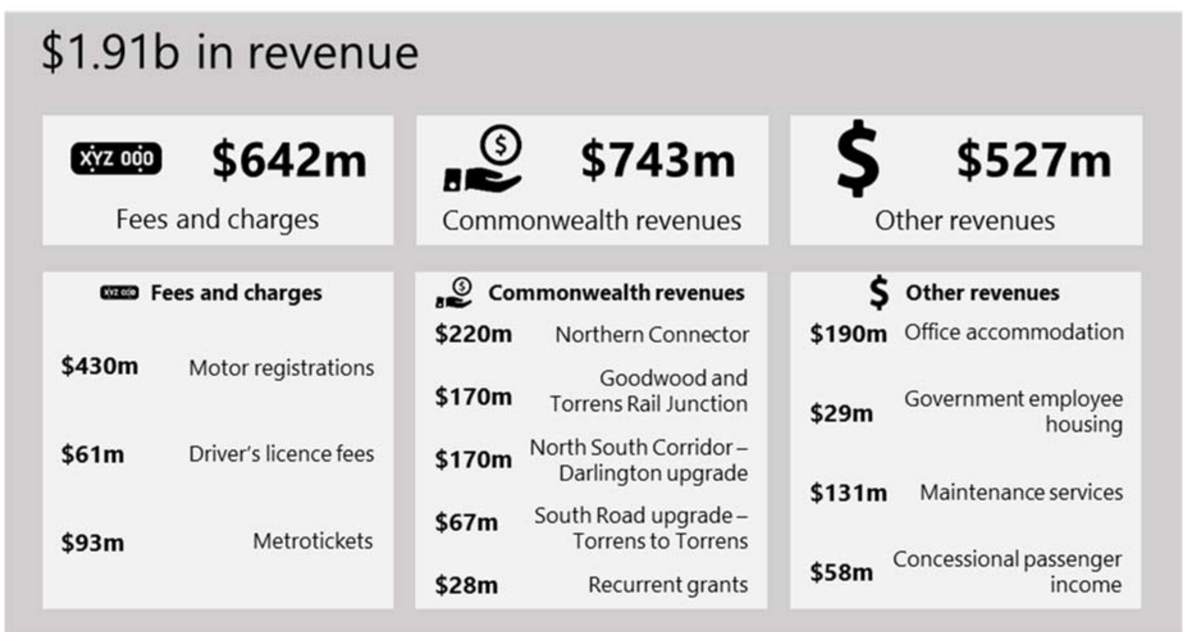
- employee benefits expenses of $226 million (13%)
- grants and subsidies of $176 million (10%).

Total expenses increased by $22 million (1%), with the more notable movements including:

- grants and subsidies increasing by $45 million due mainly to $32 million in taxi industry assistance grants paid for the first time
- a $10 million increase in bus service contract expenses attributable to contract indexation increases and additional services
- property expenses increasing by $18 million due mainly to additional minor and refurbishment works for Country Health and Education
- other expenses decreasing by $33 million due mainly to 2016-17 expenses including the cost of donating assets valued at $51 million to the South Australian Water Corporation (SA Water). The assets were constructed as part of the North-South Corridor Darlington Upgrade and the Torrens to Torrens Project
- other service contracts expense decreasing by $19 million due mainly to 2016-17 including relocation works funded by SA Water of $13 million, and additional costs of emergency response to road works associated with storm damage of $9 million
- while total depreciation and amortisation expenses remained consistent with 2017:
  - network asset depreciation increased by $14 million due mainly to the capitalisation of new assets (rail track and road assets) and revaluation of road assets
  - plant and equipment depreciation decreased by $14 million due mainly to revaluation decrements and the reduction in useful lives of rolling stock assets.

Income

Income (excluding revenues from SA Government) totalled $1912 million. DPTI's revenue sources are shown in the following chart, which demonstrates the importance of Commonwealth revenues (used largely for capital projects) and the significance of fees charged for motor registrations.

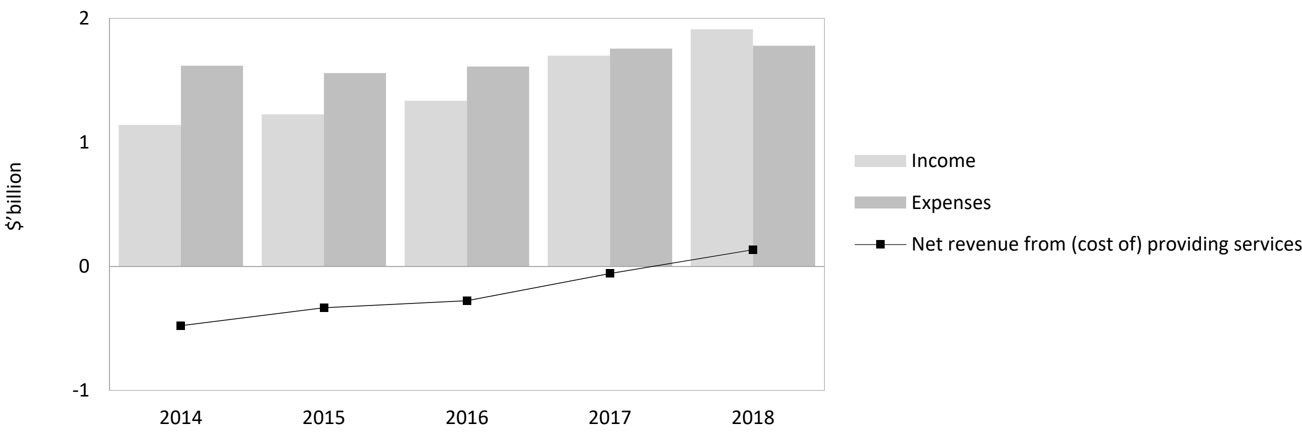


Total income (excluding revenues from the SA Government and changes in the revaluation surplus) increased by $213 million (13%) to $1912 million due mainly to the following movements:

- Commonwealth funding increasing by $186 million predominantly for road projects (refer to the chart above)
- resources received free of charge decreasing by a net $16 million, due mainly to the once off transfer of the Leigh Creek township valued at $21 million in 2016-17, offset by the recognition of $5 million in services now provided free of charge by SSSA
- an $18 million increase in maintenance services revenue, due mainly to additional minor and refurbishment works performed for Country Health and Education.

Net cost of providing services

The following chart shows the income, expenses and net revenue from or cost of providing services for the five years to 2018.



DPTI has recorded a net revenue from providing services for the year of $134 million (net cost of $57 million). A significant factor in the change was the level of Commonwealth funding received, which increased by $186 million to $743 million. Commonwealth funding was mainly for capital projects and is reported as income in the year it is received.

Revenues from (Payments to) SA Government

Net revenues from the SA Government decreased by $583 million to $960 million, due mainly to:

- a decrease of $329 million received from the Motor Accident Commission. Further details are provided under 'Cash' below
- DPTI receiving a once off contribution in 2017 of $259 million from the Department of Treasury and Finance, representing the initial fee paid by private insurers to participate in the compulsory third party insurance scheme.

Payments to the SA Government totalled $30 million ($61 million) including $26 million ($56 million) return of surplus cash under the SA Government's cash alignment policy.

In 2018 DPTI received an equity contribution from the SA Government under the *Appropriation Act 2017* of $262 million ($169 million). Equity contributions are recognised in the Statement of Changes in Equity.

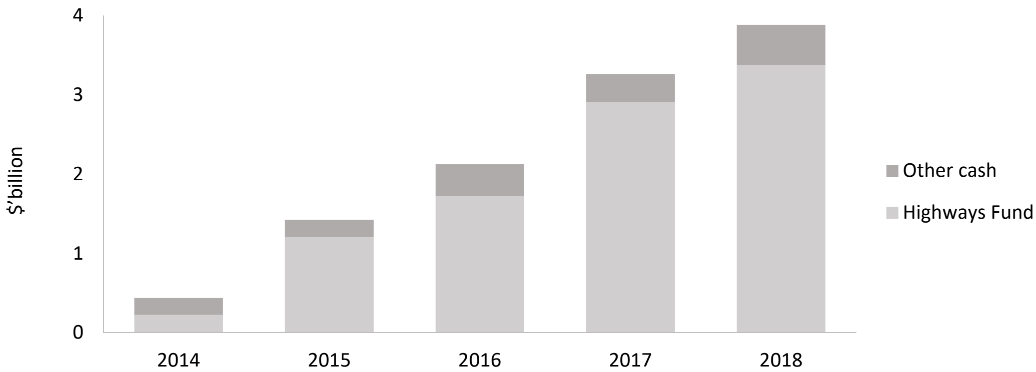
Statement of Financial Position

DPTI's total assets as at 30 June 2018 were $30.2 billion ($28.6 billion), and include network assets of $20.8 billion ($20.2 billion), land, buildings and facilities of $2.7 billion ($2.7 billion) and cash of $3.9 billion ($3.3 billion).

DPTI's liabilities amounted to $440 million ($497 million) and mainly comprised payables of $241 million ($292 million), employee benefits of $95 million ($99 million) and lease incentives of $43 million ($50 million). Payables decreased mainly because of changes in the timing of payments for capital projects.

Cash

DPTI's cash amounted to $3.9 billion ($3.3 billion) and includes $3.4 billion ($2.9 billion) held in the Highways Fund established under *Highways Act 1926*. The balance of the Highways Fund and other cash is shown in the following chart.

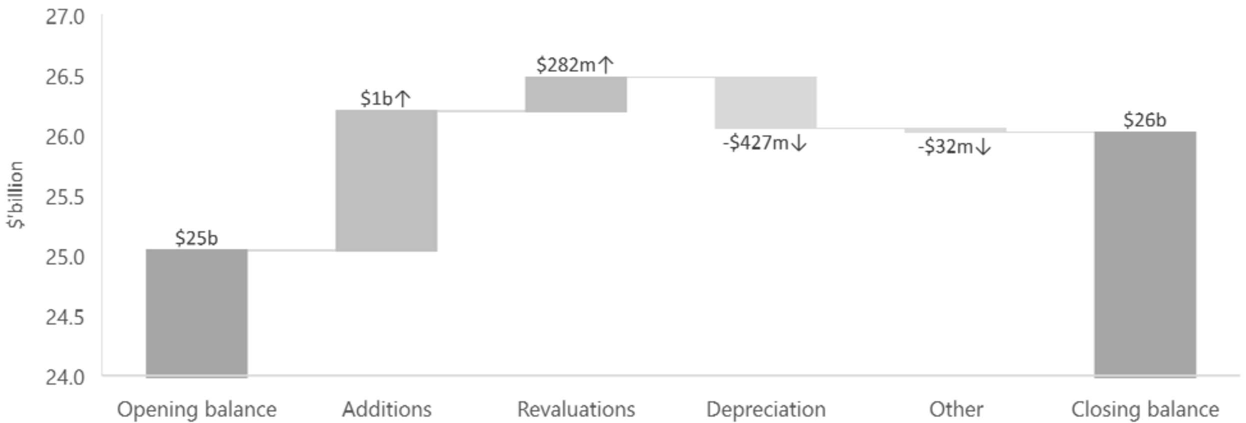


The marked increase in amounts held in the Highways Fund since 2014 largely reflects the following transfers in this period:

- surplus funds from the Motor Accident Commission totalling $2.4 billion. Further details on the transfer from the Motor Accident Commission are included in the commentary under 'Motor Accident Commission' in this Report
- money from private insurer participation in compulsory third party arrangements amounting to $259 million.

Fixed assets

DPTI's fixed assets include network assets of $20.8 billion ($20.2 billion), land, buildings and facilities of $2.7 billion ($2.7 billion), capital work in progress of $1.9 billion ($1.4 billion) and plant and equipment of $610 million ($670 million). The following chart shows the movement in fixed assets during the year.



Network assets

Network assets amounted to $20.8 billion and represented 80% of total non-current assets. Network assets comprise roads with a written down value of $16.3 billion (79%), structures with a written down value of $2.3 billion (11%) and rail and bus track assets with a written down value of $2.2 billion (10%).

The written down value of network assets increased by $539 million to $20.8 billion. The main movements were:

- capitalisation of network projects totalling $545 million, comprising $160 million for roads, $32 million for structures and $353 million for rail and bus track assets
- a net revaluation upwards of $290 million, comprising a $217 million increment for roads and $73 million increment for structures
- depreciation charges of $290 million, comprising $179 million for roads, $45 million for structures and $66 million for rail and bus track assets.

Capital works in progress

The value of capital works in progress increased by $516 million to $1.9 billion. The major movements in capital works are shown in the following table.

Projects	Carrying amount 01.07.17 $'million	Additions $'million	Transfer to assets $'million	Closing balance 30.06.18 $'million
Torrens to Torrens Project	439	154	22	571
Northern Connector	235	248	1	482
North-South Corridor Darlington Upgrade	217	161	-	378
Torrens Rail Junction	77	163	222	18
O-Bahn Extension	129	27	156	-
Tram Extension to the old RAH	9	77	-	86
Gawler Line Modernisation	-	37	-	37
Railcar overhaul	23	10	-	33
Festival Precinct Plaza	17	13	-	30
Port Bonython Jetty Refurbishment	25	3	28	-
Bald Hill and Southern Freeway Intersection	22	-	22	-
Oaklands Rail Crossing	-	21	-	21

Land, buildings and facilities

While the value of land, buildings and facilities remained largely unchanged at $2.7 billion, the main movements were:

- asset additions from purchases, transfers from capital works in progress and assets received free of charge amounting to $62 million, which included $28 million for the Port Bonython Jetty Refurbishment
- depreciation charges of $72 million
- revaluation upwards of $22 million, attributable mainly to increases in the value of owned SA Government office buildings of $53 million offset by a reduction in the value of bus depots and facilities of $24 million.

Plant and equipment

Plant and equipment totalled $610 million, a decrease of $60 million from the previous year. The main movements for the year were:

- asset additions and transfers from capital works in progress of $31 million, including $8 million for the bus purchase program
- a revaluation downwards of $30 million mainly for diesel electric rail cars acquired between 1987 and 1996
- depreciation expense of $60 million.

Statement of Cash Flows

Cash increased by $620 million to $3.9 billion. The main contributing factor was the receipt of $359 million from the Motor Accident Commission.

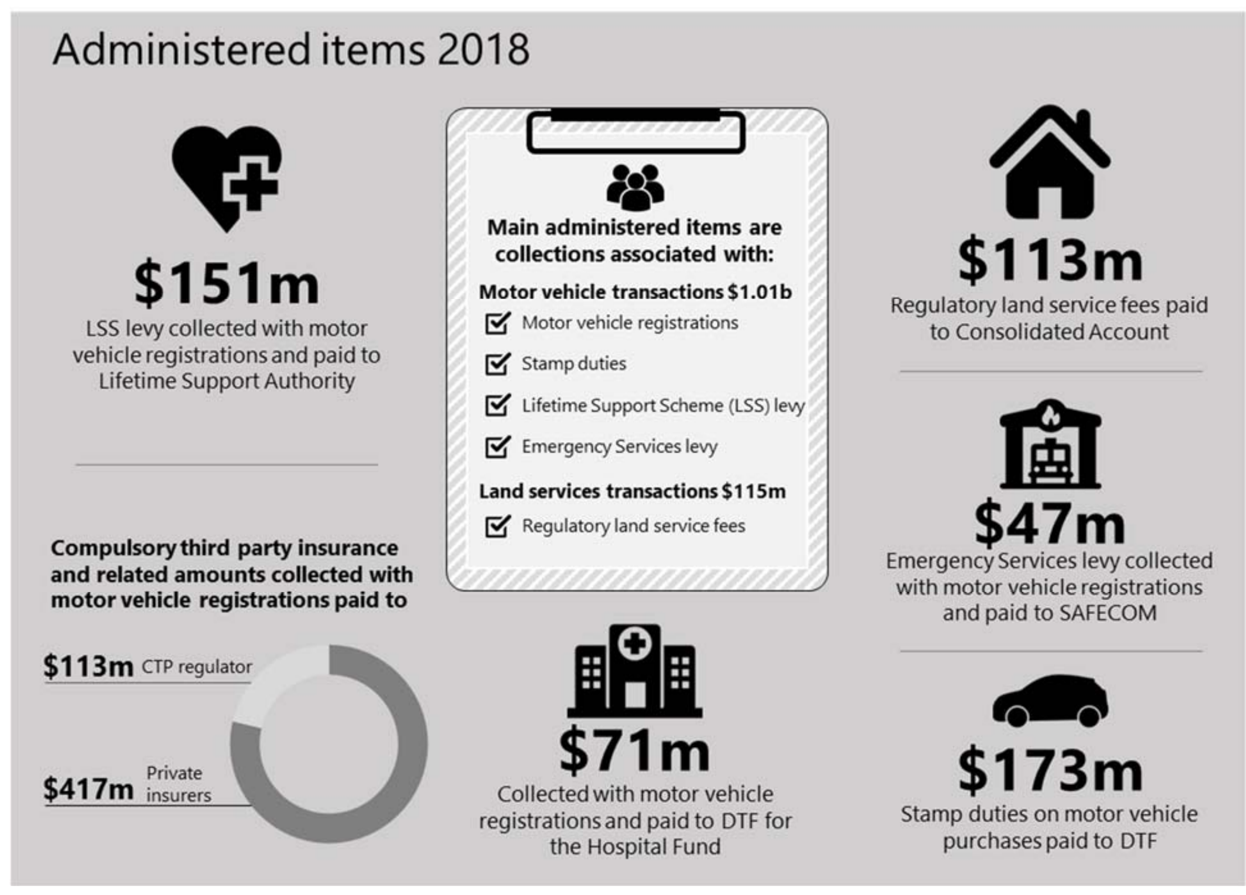
The cash used in investing activities increased by $175 million to $1.2 billion, reflecting an increase in DPTI's capital works program.

The net cash flows from financing activities increased by $92 million to $258 million, due mainly to an increase in the equity contribution from the SA Government from $169 million to $262 million.

Gross cash inflows from the SA Government amounted to $1.3 billion ($1.8 billion) including the transfer of $359 million ($688 million) from the Motor Accident Commission, operating appropriations of $600 million ($640 million) and equity contributions of $262 million ($169 million).

Administered items

DPTI is responsible for managing a range of activities on behalf of the SA Government. These activities are identified as administered items and reported separately where, for example, DPTI does not control these activities but is responsible for transferring amounts to other eligible beneficiaries. In 2018 DPTI was responsible for administering the following activities.



DPTI's administered revenue and expenses totalled $1.2 billion, which remained consistent with 2017 amounts but reflected:

- an increase in collections associated with motor vehicles of $29 million (3%) reflecting small rate and volume increases
- a decrease in regulatory land services fees from $188 to $115 million due mainly to machinery of government changes that transferred the responsibility for this activity to the Department of Treasury and Finance. This function was returned to DPTI on 1 July 2018.

Department of the Premier and Cabinet (DPC)

Financial statistics	Net cost of providing services:	$373 million
	Total appropriation:	$397 million
	Number of FTEs:	1723.54

Significant events and transactions

- The Chief Executive and a Deputy Chief Executive had their contracts terminated in March 2018.
- The South Australian Grid-Connected Battery Facility project agreement was executed in July 2017. Commencing in December 2017, the facility will seek to support power system security, integrity and stability for the South Australian electricity network.
- A Short Term Capacity Contract was executed in July 2017 for managing electricity generation capacity required to meet peak demand in South Australia on days of extreme heat. Costs incurred to date under this contract are $82.2 million.
- In November 2017 the SA Government executed a contract to purchase the assets associated with the Short Term Capacity Contract at a cost of $226.8 million.

Financial report opinion

Unmodified

Financial controls opinion

Modified

Key issues:

- Basware payment processing system financial authorisations were not updated in a timely manner
- Insufficient controls over the annual price update in the ICT billing system
- Grant agreements established under the PACE Gas grant program did not comply with the requirements of Treasurer's Instruction 15
- No separately documented evaluation plan or evaluation report for the Renewable Technology Fund
- Contract extensions significantly increased the value of original contracts without testing the market

Functional responsibility

DPC is an administrative unit established under the *Public Sector Act 2009*.

DPC's responsibilities include providing specialist policy advice, supporting the Cabinet process, leading implementation of the SA Government's strategic priorities and policy commitments, and providing a range of other government services. Details are contained in note 2 of DPC's financial report.

Scope of the audit

The audit program covered major financial systems to obtain sufficient evidence to form an opinion on the financial report and internal controls.

Specific areas of audit attention in 2017-18 included:

- accounts payable
- revenue
- bank reconciliations
- fixed assets
- financial accounting
- Shared Services SA (SSSA)
- Service SA
- PACE Gas grants
- Renewable Technology Fund
- Contract extensions and single offer market approaches.

The audit also considered the nature of the review work undertaken by internal audit.

Audit findings and comments

Assessment of controls

In my opinion, the controls exercised by the Department of the Premier and Cabinet in relation to the receipt, expenditure and investment of money, the acquisition and disposal of property and the incurring of liabilities, except for the matters raised in relation to corporate operations outlined under 'Communication of audit matters', are sufficient to provide reasonable assurance that the financial transactions of the Department of the Premier and Cabinet have been conducted properly and in accordance with law.

Communication of audit matters

Matters identified by the audit were detailed in management letters to the Chief Executive. The main matters raised and related responses are detailed below.

Corporate operations

Accounts payable

Our review identified that approved financial authorisations effective from 1 July 2017, were not updated into the Basware payment processing system in a timely manner. We also identified that Basware quarterly user access reviews were not performed in a timely manner and that not all user details were reviewed. This increases the risk of officers approving payments that are not within their authorised delegation limit.

In response DPC stated it would change its procedure manual and include a requirement to promptly update Basware for changes to financial delegations. DPC also stated that efforts will be made to complete future Basware user reviews within or as near to the dates nominated by SSSA eProcurement Systems Support.

ICT revenue from government agencies

DPC received $37.7 million in ICT revenue from various SA Government agencies for ICT services.

Our review found that there were insufficient controls over the annual price update in the Telecommunication Billing System (TBS). We found:

- no evidence was maintained to show that the 2017-18 price list was verified against the approved minute before updating prices into TBS and import files
- changes to prices for transmission services were not independently reviewed in a timely manner
- no evidence that changes to hosting and internet charges were independently reviewed.

This increases the risk that clients may be charged incorrectly.

In response DPC advised that all recommendations will be actioned as part of the 2018-19 price changes and the work instruction will be updated.

Our review also found instances where invoices raised were not approved by an appropriate officer or not approved at all. This increases the risk of incorrect or inappropriate invoices being sent out.

In response DPC stated that the Office for Technology has addressed this finding with all relevant staff instructed that only staff with appropriate income recognition delegation are permitted to approve invoices. DPC also advised that delegation levels have been reviewed and all invoice batch header approvals are monitored by the responsible team leader.

PACE Gas grants

Our review of grant funding agreements established under the PACE Gas grant program found that they did not include all reporting requirements as specified in Treasurer's Instruction 15 'Grant Funding'. This increases the risk the grant agreement will not establish an appropriate level of accountability on entities that receive grant funding.

In response the Department for Energy and Mining (DEM), which now has responsibility for this area, stated that sufficient compensating controls and accountability mechanisms are in place to minimise any exposure intended to be managed as outlined by Treasurer's Instruction 15.

Renewable Technology Fund

The Renewable Technology Fund was established as a key component of South Australia's energy plan announced in March 2017. The fund provides grants and loans to private sector entities to support the integration of renewable technologies and demand management technologies in South Australia. We reviewed activities of the grant and loan funding program.

Our review identified there was no separately documented evaluation plan outlining the process to be undertaken to evaluate proposals, and no evaluation report documenting the outcome of the evaluation process that we could access. This increases the risk of reducing transparency in evaluating and approving grant applications.

In response DEM, which now has responsibility for the fund, advised that specific evaluation plans and reports will be prepared for future grant programs.

Our review also found that there was no documented evidence to support actions taken to manage conflicts of interest. This increases the risk that proposals may not receive equitable treatment.

In response DEM advised that it will ensure appropriate documentation of such actions is made for future projects and programs through meeting minutes.

We also found that the Energy Plan Implementation Committee meeting minutes did not clearly indicate which proposals were recommended to and endorsed by the Committee. This increases the risk of reducing transparency of the grant and loan award process.

In response DEM advised that it will endeavour to ensure the recommendations and endorsement of proposals are more clearly documented in future minutes.

Contract extensions and single offer market approaches

Our review of a sample of contract extensions and single offer market approaches found:

- a contract extension that increased the value of original contract from $220 000 to $2.2 million
- instances where the justification for single offer market approaches was not appropriate.

This increases the risk of DPC not receiving value for money in its procurement activities and non-compliance with State Procurement Board guidelines.

At the time of this Report we had not received a response to our findings.

Shared Services SA – financial systems and transaction processing controls

SSSA processes financial transactions on behalf of a large number of SA Government agencies under service level determinations. The main systems and control environments include accounts payable, accounts receivable, payroll and general ledger financial functions.

Our review and evaluation of controls for these systems concluded that controls were effective for 2017-18. We did, however, find areas where controls could be improved.

Shared Services SA – payroll controls

SSSA processes payroll transactions specific to the Chris21 payroll system on behalf of a large number of SA Government agencies under service level determinations.

Our 2017-18 audit considered the controls over Chris21, including the payroll process and internal controls of SSSA and the external bureau provider of the Chris21 payroll service to SSSA, Frontier.

SSSA payroll functions include:

- payroll maintenance comprising processing changes to employee master data and salaries
- processing employee pays through Chris21
- calculating payroll payments (via Chris21)
- disbursing payroll payments (via CommBiz banking)
- identifying and managing overpayments
- calculating termination payments.

The SSSA teams that perform these functions comprise the following functional streams: work management, payroll data input, quality assurance, customer service, pay run processing and technical specialist.

Our review did not identify any significant control deficiencies within the Chris21 payroll environment. We did, however, find some issues that we communicated to DPC.

Integrity of data in reports

We found a number of variances in the data used in reports to identify variances in employee pays from each pay run. This increases the risk of variances in employee pays not being identified.

In response DPC stated that Technical Specialist Officers were reminded of the requirement to complete the 'variation register' for all transactions that have been processed after reports have been generated.

Pay run activities not completed prior to generating pay run variance reports

We identified instances where required pay run activities were not completed prior to generating pay run variance reports. This increases the risk that any changes to pays are not reviewed, resulting in inaccurate payments.

In response DPC stated that Pay Run team members were reminded of their responsibility to ensure that all pay run activities are completed in correct sequence in line with current documented procedures.

Shared Services SA – accounts payable controls

SSSA processes payments on behalf of SA Government agencies. The SSSA accounts payable function employs several systems to make these payments, including:

- the e-Procurement system for ordering, receiving and invoice processing
- the Masterpiece (MPAP) system for payment transaction processing through EFT and cheques and general ledger maintenance.

Our review did not identify any significant control deficiencies within the accounts payable environment. We did, however, find some issues that we communicated to DPC.

Manual payments

Our review of the manual payment process identified that duplicate payments had been made and that internal controls could be improved. This included a duplicate payment of $76.4 million made by SSSA on behalf of the South Australian Local Government Grants Commission to the Local Government Financing Authority, which was subsequently recovered.

We recommended:

- implementing a system control within the MPAP platform to remove the need to manually assign a payment ID
- implementing a monitoring system to check that all manual payments are updated in Basware within 48 hours of payment.

In response DPC stated that:

- it had commenced developing and implementing a new system control and this work has progressed to the testing stage
- SSSA was reviewing the urgent payments procedure to ensure the requirement that all manual payments are created in Basware within 48 hours is incorporated into the procedure. This will be supported by the implementation of a control report for periodic review by the Operational Team Leader to ensure that this time frame is being met for all applicable transactions.

External feed files

Our review found that secure file transfer protocols were not implemented for external feed files for a number of agencies. This increases the risk of data being modified prior to importing into MPAP.

In response DPC stated that SSSA was working with these agencies to implement a secure file transfer protocol for external feed files.

Vendor maintenance

Our review of vendor maintenance identified a number of findings requiring improvement. We found:

- the independent reviewer was able to make changes to vendor details in the Vendor Wizard while reviewing vendor details
- changes to vendor details could be made directly into MPAP, bypassing independent review processes
- the vendor masterfile was not periodically reviewed to identify redundant or duplicated vendors
- banking details in the vendor masterfile were updated by the vendor maintenance team on advice from the payment team without supporting documentation.

In response DPC advised it would:

- develop a new report to identify any vendor record changes made by reviewers. Reports will be reviewed on a periodic basis to ensure that all changes made by the reviewers are appropriate

- introduce a new control report for periodic review that highlights all vendor detail updates made directly into MPAP
- assign project resources to develop and document a new process for periodic review of vendor masterfiles
- review current procedures for vendor masterfile changes to ensure that the requirement for supporting documentation relating to any banking detail updates is more clearly articulated.

Shared Services SA – IT general controls

We reviewed key financial systems managed by SSSA to assess the adequacy of IT general controls. Our testing covered:

- password management
- privileged user access
- audit logging
- user onboarding/offboarding
- user access review
- change management
- patch management
- backup management
- disaster recovery management.

We identified the following control deficiencies.

Chris21

Our review identified the following issues:

- the user access request form process was not adequately followed
- quarterly user access reviews were not performed by all SSSA business units
- not all user access amendments were processed
- inadequate change management processes
- lack of regular payroll application upgrades
- no disaster recovery testing conducted for the Chris21 application since September 2016.

In response DPC stated that:

- customer service officers were reminded of their responsibility to ensure that all parts of the user access request forms are completed in full. In addition a communication will be sent out to all authorised officers reminding them to ensure all parts of the forms are completed
- this matter will be escalated to the Senior Leadership Team at its monthly Risk and Compliance meeting to ensure that all business unit quarterly reviews are completed within 10 days
- customer service officers were reminded of their responsibility to ensure that all amendments to user access profiles are accurately performed as requested by the respective payroll units
- SSSA acknowledges that the documented testing procedures do not fully reflect practices currently being applied and that the overarching change management process is due for review and update. A review and update of the current testing procedures will be undertaken to ensure alignment between practice and documentation, including developing controls to ensure the revised process is consistently applied across all change requests

- SSSA has completed negotiations with Frontier to provide a new application version pathway which is expected to result in a major upgrade in late 2018
- SSSA is currently planning with Frontier to conduct a major disaster recovery exercise in October – November 2018.

Basware

Our review identified the following issues:

- current password configuration settings do not incorporate appropriate requirements for password complexity and length
- user access exceptions
- change management testing exceptions.

In response DPC stated that:

- SSSA would implement the DPC password standards (or our recommendations where appropriate) for Basware in both the SA Government general and SA Health environment
- SSSA will issue a communication to internal and external stakeholders, reminding them of their obligation to request deactivation of user accounts for terminated employees
- SSSA is undertaking a comprehensive review of its change management procedure.

Masterpiece

Our review identified the following issues:

- current password configuration settings do not incorporate appropriate requirements for password complexity and length
- database privileged user access exceptions
- user access testing exceptions
- change management testing exceptions
- no mainframe disaster recovery testing for SYS1 (general government) and SYSH (Department of Human Services and Housing SA).

In response DPC advised that:

- SSSA would implement the DPC password standards (or our recommendations where appropriate) for Masterpiece in both the SYS1 and SYSH environments
- SSSA will conduct a review of the users listed and make appropriate changes to current access as required
- SSSA will communicate with applicable staff to remind them to comply with requirements set out in the Masterpiece user access management procedure
- SSSA is undertaking a comprehensive review of its change management procedure
- SSSA will consult with DPC ICT and other relevant stakeholders to identify when the next whole-of-government mainframe test is expected to occur. Once confirmed this will be incorporated into the SSSA business continuity recovery testing schedule.

CommBiz

Our review identified the following issues:

- SSSA CommBiz user accounts were not reviewed
- inadequate termination of payroll users with network access to financial services sensitive files
- user access changes were not processed timely.

In response DPC stated that:

- communication will be issued to the Directors of each SSSA line of business to reinforce the importance of ensuring that access is only retained by specific individuals who require it
- communication will be issued to the Director, Payroll Services to reinforce the importance of ensuring that network access to sensitive files is reviewed on an ongoing basis and any necessary changes implemented expeditiously
- the procedure was updated to reflect achievable time frames for processing CommBiz user access forms.

Interpretation and analysis of the financial report

DPC's 2017-18 financial report includes the full 12-month impact of the transferred employees from the following business units of the Department of State Development (DSD) to DPC effective from 1 April 2017:

- Mineral Resources Division
- Energy Resources Division
- Energy Markets and Programs Division
- Resource Infrastructure and Investment Task Force (with the exception of the Case Management Function)
- Strategy and Governance Unit
- Office of the Economic Development Board.

Highlights of the financial report – controlled items

	2018 $'million	2017 $'million
Expenses		
Employee benefits	184	148
Supplies and services	248	124
Grants and subsidies	89	42
Other expenses	11	9
Total expenses	532	323

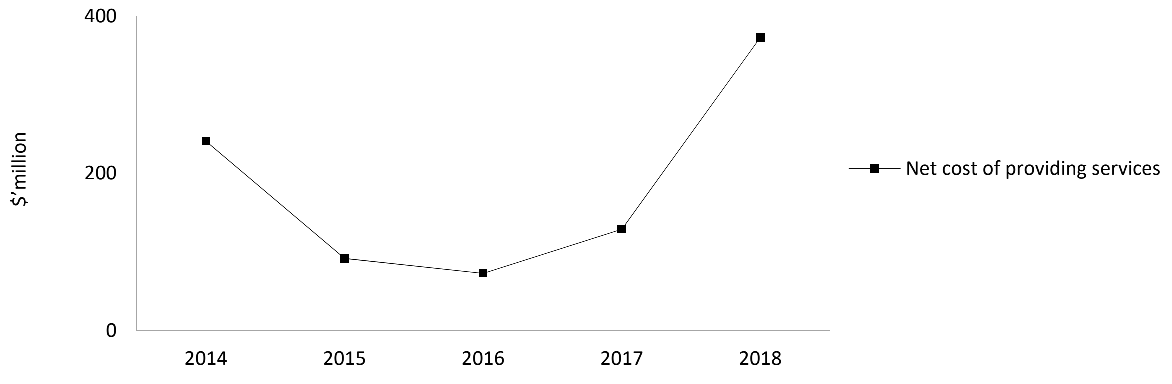
	2018 $'million	2017 $'million
Income		
Fees and charges	141	189
Grants	5	1
Resources received free of charge	4	-
Other	9	4
Total income	159	194
Net cost of providing services	373	129
Revenues from (Payments to) SA Government		
Revenues from SA Government	397	153
Payments to SA Government	-	(5)
Total revenues from (Payments to) SA Government	397	148
Net result and total comprehensive result	24	19
Net cash provided by (used in) operating activities	19	62
Net cash provided by (used in) investing activities	(10)	(9)
Net cash provided by (used in) financing activities	4	6
Assets		
Current assets	161	160
Non-current assets	83	79
Total assets	244	239
Liabilities		
Current liabilities	62	86
Non-current liabilities	48	47
Total liabilities	110	133
Total equity	134	106

Statement of Comprehensive Income

Net cost of providing services

The machinery of government transfer from DSD and the implementation of the previous SA Government's energy plan resulted in an increase in the net cost of providing services. This follows the increase in the previous year due to machinery of government changes.

The following chart shows the net cost of providing services for the five years to 2018.



Expenses

As a result of the DSD transfer and the implementation of the energy plan, total expenses for the year increased by $208.7 million (65%). The total increase in expenses attributable to the DSD transfer was $68.6 million.

Employee benefits expense increased by $36.8 million (25%). This is mainly due to an increase in salaries and wages costs of $28.6 million. The amount of the increase attributable to the DSD transfer for salaries and wages is $21 million.

Supplies and services increased by $123.7 million (100%). The amount of the increase attributable to the DSD transfer is $21.5 million. The following highlights the material movements in individual expense items:

- Short-term emergency electricity supply expenses of $82.2 million relate to costs incurred to secure the supply of electricity as part of the SA Government's energy plan. There were no costs in the prior year.
- General administration and consumables increased by $5.7 million. The increase is a result of the impact of DSD for the full year ($2.3 million), and an increase in fuel costs of $1.9 million as a result of the SA Government's energy plan.
- Contractors increased by $8.6 million. The increase is a result of the impact of DSD for the full year ($4.4 million), and an increase in general contractors of $4.2 million, including $2.8 million for energy plan implementation.
- Promotion and marketing expenses increased by $4.5 million as a result of an increased number of campaigns, including Fund My Neighbourhood, Job Accelerator Grant, Jobs SA, Public Education and Health Infrastructure Communications campaign.
- Intra government transfers increased by $7.3 million. The increase is a result of the impact of DSD for the full year ($4.3 million), and an increase in payments to agencies of $3 million for various purposes.
- Service fees expenses of $2.3 million relate to costs incurred for the battery storage project as part of the SA Government's energy plan. There were no costs in the prior year.
- Energy supply fuel and lubricants expenses increased by $4.2 million as a result of the impact of DSD for the full year.

Grants and subsidies increased by $46.3 million to $88.5 million. The increase is a result of the impact of DSD for the full year ($16.6 million), and a number of new grant programs introduced in 2017-18 ($27.3 million).

The significant grant programs included:

- $24 million under the PACE Gas grant program (round 2). This program aims to accelerate investment in gas projects in South Australia that help to secure new incremental and significant gas supplies.

  The four PACE Gas grant projects comprise:

  - $6.89 million for the Santos Moomba Heat Recovery Steam Generator project

- $6.89 million for the Beach Energy Limited Dombey Conventional Gas Exploration Well in the Otway Basin
- $4.95 million for the Otway Energy and Vintage Energy New Gas Exploration Well in the Otway Basin
- $5.26 million for the Senex Energy Gemba Conventional Tight Gas project

- $18.6 million under the Fund My Neighbourhood program. Launched in August 2017, this program provided funding for communities to support projects between $10 000 and $150 000 that would improve their neighbourhood or bring communities together. As at 30 June 2018 grants were paid to a total of 149 grant recipients, with the largest recipient being the City of Tea Tree Gully with $1.2 million
- $9.7 million Energy Productivity Program. This program aims to assist large energy using businesses in the State to reduce their energy usage and related costs, and contribute energy supply benefits to the State. In 2017-18 a total of 400 grants were paid, with the largest amount paid being $1.1 million
- $6.8 million Renewable Technology Fund program. The Fund was established as one of the key components of the previous SA Government's energy plan announced in March 2017. The objectives of the Fund were to catalyse private sector investment to support further integration of renewable technologies and demand management technologies in South Australia. As at 30 June 2018 a total of eight grant payments had been made to successful applicants.

Income

Total income (excluding revenues from the SA Government) for the year was $158.8 million, a decrease of $35.6 million (18%) from the previous year.

Fees and charges decreased by $47.7 million to $141.3 million. The decrease is mainly due to SSSA revenue decreasing by $84.4 million due to DPC receiving funding through appropriation for services provided to agencies. This decrease was offset by increases in mining and petroleum application fees, rentals and licences ($16.1 million), industry license fees ($7.7 million), sale of electricity – remote areas ($3.3 million) and other ($8.7 million). These increases were the result of the impact of DSD for the full year.

Commonwealth revenues increased to $1.1 million which principally relates to $1 million received from Geoscience Australia for the Coompana Drilling program.

Grants increased by $3.9 million to $5 million. This is mainly as a result of $3 million received from DSD for trade mission support funding.

Resources received free of charge increased by $3.7 million to $3.8 million. This is mainly as a result of donated assets received by DPC from the Department of Planning, Transport and Infrastructure for the fitout at Port Adelaide ($2.9 million).

Other income increased by $3.4 million to $6.4 million. This increase was the result of the impact of DSD for the full year.

Net revenues from the SA Government increased by $248.6 million to $396.8 million. The increase includes additional appropriations of $33.3 million for the impact of DSD for the full year, and $87.9 million funding for SSSA. Contingency provisions increased by $127.4 million to fund additional initiatives including implementation of the energy plan.

Statement of Financial Position

Net assets increased by $28 million (26%). This was mainly due to a decrease in total liabilities of $22.5 million.

As at 30 June 2018 total assets increased by $5.5 million to $244.5 million. Cash and cash equivalents of $140.4 million make up 57% of the total asset balance. The cash balance includes an amount of $7.4 million held in the Accrual Appropriation Excess Funds Account. The balance of these funds is not available for general use and can only be used with the Treasurer's/Under Treasurer's approval.

Total liabilities decreased by $22.5 million to $110.2 million. This was the result of a decrease in payables of $24.2 million caused by a reduced creditors balance as at 30 June. The June 2017 creditors balance had a large number of outstanding payments made in relation to PACE Gas grants ($22 million) in early 2017-18.

Highlights of the financial report – administered items

	2018 $'million	2017 $'million
Expenses		
Disbursements on behalf of third parties	355	359
Payments to SA Government	237	66
Other expenses	7	3
Total expenses	599	428
Income		
Collections on behalf of third parties	355	359
Royalties	237	66
Revenues from SA Government	3	2
Fees and charges	4	1
Total income	599	428
Net result	-	-
Total comprehensive result	-	-
Net cash provided by (used in) operating activities	9	7
Net cash provided by (used in) financing activities	-	11
Assets		
Current assets	37	34
Total assets	37	34
Liabilities		
Current liabilities	35	32
Total liabilities	35	32
Total equity	2	2

Statement of Administered Comprehensive Income

Disbursements and collections on behalf of third parties

DPC, through Service SA, collects various fees on behalf of third parties and disburses them to the responsible recipient agency. The main amounts collected and disbursed related to registrations, licences and other fees collected on behalf of the Department of Planning, Transport and Infrastructure ($342 million) and expiation notices and firearms licences on behalf of South Australia Police ($11 million).

Royalties

As a result of the DSD transfer, DPC receives royalties levied on minerals and petroleum production on behalf of the SA Government. The royalties received are paid into the Consolidated Account. Total royalties received and paid during the year were $237 million ($66 million).

Department of Primary Industries and Regions (PIRSA)

Financial statistics	Net cost of providing services:	$136 million
	Net revenues from SA Government:	$87 million
	Commonwealth revenues:	$26 million
	Advances and grants revenue:	$57 million
	Grants and subsidies expense:	$83 million
	Number of FTEs:	890.3

Significant events and transactions

- A full revaluation of PIRSA's land and building assets was performed as at 30 June 2018 by Liquid Pacific. This resulted in a $14.2 million increase to the asset revaluation surplus and a $4.8 million expense for assets with downward revaluation movements in excess of amounts held in the asset revaluation surplus for those assets.
- PIRSA continued to deliver the $265 million South Australian River Murray Sustainability (SARMS) program. $25 million was received from the Commonwealth in 2017-18 and $45.9 million was paid out in grants for SARMS projects during the year.
- PIRSA continued to support projects and initiatives through the Regional Development Fund (RDF). $15.2 million was paid out in grants for RDF projects in 2017-18. With a change in State Government in March 2018, the RDF was repurposed as the Regional Growth Fund. How this fund will be spent in the future will be determined by the Minister for Primary Industries and Regional Development.

Financial report opinion

Unmodified

Financial controls opinion

Modified

Key issues:

- Improvements required to the RDF grant application and evaluation processes
- Bona fide and leave return reports not promptly reviewed
- Improvements required to system access review processes

Functional responsibility

PIRSA is an administrative unit established under the *Public Sector Act 2009*.

PIRSA's objective is to grow primary industries and drive regional growth in South Australia.

For more information about PIRSA's objectives and activities refer note 2 of its financial report.

Scope of the audit

The audit program covered major financial systems to obtain sufficient evidence to form an opinion on the financial report and internal controls.

Specific areas of audit attention in 2017-18 included:

- follow-up of 2016-17 audit findings
- governance
- compliance with Treasurer's Instructions
- payroll
- revenue, including sundry revenue, licence revenue, South Australian Research and Development Institute (SARDI) grant revenue and SARMS program Commonwealth revenue
- expenditure including supplies and services and grant expenditure for the SARMS and RDF programs
- cash and general ledger
- concessional loans schemes
- fixed assets.

The audit considered control processes performed by both PIRSA and Shared Services SA (SSSA).

We also considered PIRSA's internal audit coverage when designing and performing audit procedures.

Audit findings and comments

Assessment of controls

In my opinion, the controls exercised by the Department of Primary Industries and Regions in relation to the receipt, expenditure and investment of money, the acquisition and disposal of property and the incurring of liabilities, except for all matters outlined under 'Communication of audit matters', are sufficient to provide reasonable assurance that the financial transactions of the Department of Primary Industries and Regions have been conducted properly and in accordance with law.

Communication of audit matters

Matters identified by the audit were detailed in management letters to the Chief Executive. The main matters raised and related responses are detailed below.

Regional Development Fund

Total payments from the RDF for the year were $15.2 million ($18.4 million).

Improvements required to the RDF grant application and evaluation processes

In 2016-17 we recommended a number of improvements to the RDF grant application and evaluation processes. Our follow-up review in 2017-18 identified that although there were significant improvements to these processes for funding applications assessed in 2017-18, a number of areas for additional improvement were identified to further strengthen them.

Approach followed may not allow all potential applicants equitable access to funding

In 2017-18 no rounds of funding were publically offered to potential applicants as was the case in previous years. Rather, potential applicants who had previously contacted the Minister for Regional Development or PIRSA to query funding availability, or potential applicants that regional coordinators were aware of because of the work they perform, were invited to submit an application for grant funding from the RDF.

Although this approach was approved by the former Minister for Regional Development, and PIRSA considers that all applicants with projects in a position to be funded were aware of the funding process, we believe this approach may not allow all potential applicants equitable access to RDF grant funding. This may create reputational risks if potential applicants become aware that funding was available but were not aware they could apply.

Short time frames for the assessment panel to review applications

We noted that the assessment panel meetings to review applications submitted for funding were held only a few days after the closing dates for applications. These short time frames for reviewing applications may prevent a proper and equitable assessment of all applications by the assessment panel, particularly when there are a large number of applications to assess. This may result in funding being awarded to applicants that do not satisfy the assessment criteria. We understand that these shorter time frames were approved by the former Minister for Regional Development.

Improvements required to the information included in the assessment evaluation plan

A panel assessment document was prepared in 2017-18 in response to our 2016-17 recommendation that an evaluation plan be developed for the assessment panel to follow when assessing applications. This document outlines the assessment criteria to be used by panel members when reviewing and ranking applications. Our review of the document identified that it could be improved by including additional important information such as how to assess the eligibility criteria; key decision points and time frames; approval and reporting processes; and how to manage appeals. We believe a more comprehensive evaluation plan for the RDF grant funding program would help ensure that all assessment panel members are aware of their roles and responsibilities and reduce subjectivity in the assessment process.

In response PIRSA advised that although the findings were acknowledged, the former Minister for Regional Development had total discretion over the processes to be applied on spending the fund and was the decision maker on expenditure from the fund. PIRSA noted that under the new government the RDF has been repurposed as the Regional Growth Fund and how these funds will be distributed in the future will be decided by the Minister for Primary Industries and Regional Development.

While PIRSA considered the approach adopted in 2017-18 for assessing RDF proposals to be fair, objective and clearly understood by applicants and assessment panel members, it acknowledged that there are opportunities for improvement to funding application, assessment and evaluation processes.

PIRSA is also currently preparing an across-department grant management framework, which will incorporate our recommendations and will ensure consistent practices across the various grant funding programs.

Payroll

Employee benefits expenses for the year were $95.1 million ($92.1 million).

Bona fide and leave return reports not promptly reviewed

Our review in 2017-18 identified instances of bona fide and leave return reports that were not reviewed and approved in line with the time frames outlined in PIRSA's procedures.

For example, our review of bona fide reports for three material pay points identified an instance of a report that took 49 days to be reviewed. Bona fide reports should be reviewed and approved within five business days. Our review of leave return reports for the same pay points also identified an instance of a report that took 84 days to review, when these reports should be reviewed and approved within seven days.

If bona fide and leave return reports are not promptly reviewed and approved, payroll errors may not be identified and corrected and inappropriate payments may be made.

PIRSA responded that this issue would be addressed by continuing to issue reminders to bona fide and leave return report approvers about the time frames outlined in PIRSA's procedures. The relevant Executive Directors will write to those officers identified as having not complied with policy requirements, reinforcing their responsibilities, while business managers in each division will be required to undertake additional, proactive checking of compliance with the policy within their division.

This was also raised as an issue with PIRSA in prior years.

System access

Improvements required to system access review processes

We reviewed system access for various systems across PIRSA, which are used to record both financial and non-financial transactions. This identified that there is no consistent PIRSA-wide approach to reviewing system access periodically and that a number of improvements are required to current practices.

We also identified areas for improvement in the system access review processes for the Primary Industries Information Management System (PIIMS), the Standard Invoicing System (SIS), Sharepoint, Planview, and the Rural Finance Information System (RUFIS). These areas for improvement included:

- no evidence of the periodic reviews was maintained and therefore we were unable to confirm that the reviews had occurred (PIIMS, Sharepoint, Planview and RUFIS)

- the appropriateness of users was reviewed, however no review of user access levels was performed (PIIMS and Planview). As a result, our review of PIIMS users identified a number of employees with inappropriate system access levels for their positions
- no evidence that all users were included in the review (PIIMS, SIS and Sharepoint)
- not all responses were received back from areas required to complete the reviews (PIIMS and SIS)
- there was no process in place to ensure employees who left PIRSA had their system access removed between reviews (SIS)
- no evidence of the review of financial delegations was maintained (SIS).

If system access review processes are not appropriate, users may have incorrect access, access levels or delegations set up in PIRSA's systems. This could result in the processing of unauthorised or invalid transactions or inappropriate changes to the information maintained in these systems. We recommended that PIRSA review the current system access review processes across PIRSA and develop a PIRSA-wide policy for reviewing system access periodically.

PIRSA responded that relevant system owners had been reminded of their responsibilities for reviewing system access, and that no unauthorised transactions or inappropriate changes were identified in relation to the issues raised. PIRSA also noted that the areas identified for improvement will be incorporated in the relevant procedures to have a more consistent and integrated approach to how access is given, reviewed, monitored and revoked across PIRSA to strengthen existing controls.

Shared Services SA – financial systems and transaction processing environments

SSSA processes financial transactions on behalf of PIRSA under service level determinations. The main systems and control environments include accounts payable, payroll and general ledger financial functions.

Our review and evaluation of controls for these systems concluded that controls were effective for 2017-18.

SSSA is discussed further in the commentary under 'Department of the Premier and Cabinet' in this Report.

Interpretation and analysis of the financial report

Highlights of the financial report – controlled items

	2018 $'million	2017 $'million
Expenses		
Employee benefits	95	92
Supplies and services	51	50
Grant and subsidies	83	89
Other expenses	17	8
Total expenses	246	239

	2018 $'million	2017 $'million
Income		
Fees and charges	14	14
Advances and grants	57	55
Commonwealth revenues	26	57
Other income	13	9
Total income	110	135
Net cost of providing services	136	104
Revenues from (Payments to) SA Government		
Revenues from SA Government	107	127
Payments to SA Government	(20)	(6)
Net result	(49)	17
Other comprehensive income	14	-
Total comprehensive income	(35)	17
Net cash provided by (used in) operating activities	(37)	24
Assets		
Current assets	142	184
Non-current assets	152	138
Total assets	294	322
Liabilities		
Current liabilities	51	52
Non-current liabilities	50	42
Total liabilities	101	94
Total equity	193	228

Statement of Comprehensive Income

Expenses

Employee benefits expenses

Employee benefits expenses increased by $3 million to $95.1 million largely due to increases in:

- salaries and wages of $1.6 million primarily due to general pay increases throughout the year
- long service leave expenses of $719 000 due to movements in the valuation of the long service leave liability.

Grants and subsidies expense

Total grants and subsidies decreased by $6.8 million to $82.6 million, mainly due to:

- a $3.2 million decrease in grant payments made from the RDF (see discussion under 'Regional Development Fund' below)
- a $2.9 million decrease in grants paid under the South East Forestry Partnership program given there were no milestone payments made in 2017-18
- a $2.1 million decrease in payments for natural disaster recovery programs

- a $1.5 million decrease in grants paid out of the Riverland Sustainable Futures Fund
- a $1.1 million decrease in industry development and restructuring initiative grants.

These decreases were offset by a $4.4 million increase in grants paid under the SARMS program (see discussion under 'South Australian River Murray Sustainability program' below).

South Australian River Murray Sustainability program

In August 2013 a National Partnership Agreement between the Commonwealth and SA Governments was signed, allocating $265 million in Commonwealth funding to the SARMS program over six years, with the aim of returning 40 gigalitres of water to the River Murray. Of the $265 million, $240 million has been allocated to the Irrigation Industry Improvement program and $25 million to the Regional Economic Development program. These components are designed to provide a comprehensive set of programs supporting regional research, economic diversification and development in River Murray communities.

– *Irrigation Industry Improvement program (3IP)*

3IP is a competitive grants program created by industry to support the restoration of a healthy Murray-Darling Basin environment. It supports SA River Murray irrigators to remain at the forefront of irrigation practices, and also helps irrigators and the wider community respond to the Murray-Darling Basin Plan and be more resilient to the effects of fluctuating water availability.

Since 3IP's inception, PIRSA has entered into the following grant funding agreements:

- round one (2014-15) – 108 grant funding agreements for $102.5 million to return 19.8 gigalitres of water to the River Murray
- round two (2014-15) – 53 grant funding agreements for $60.9 million to return 13.1 gigalitres of water to the River Murray
- round three (2015-16) – 21 grant funding agreements for $12.7 million to return 1.9 gigalitres of water to the River Murray
- round four (2017-18) – 71 grant funding agreements for $32.7 million to return 4.5 gigalitres of water to the River Murray. There were still three contracts yet to be executed as at 30 June 2018.

PIRSA advised that as at 30 June 2018, $186.2 million has been paid out in grants for 3IP projects and 35 gigalitres of water has been returned to the River Murray. It also advised that no further rounds of the 3IP are planned.

– *Regional Economic Development program*

Funding of $25 million for the Regional Economic Development program has been allocated across three areas as follows:

- $12.5 million for the Regional Development and Innovation Fund – to date there has been $11 million in grants awarded to support 17 projects across four rounds of funding. There was no round of funding offered in 2017-18

- $5 million for the Industry-Led Research Sub-Program – to date there has been $2.9 million in grants awarded to support nine projects across two rounds of funding. There were no rounds of funding offered in 2016-17 or 2017-18
- $7.5 million for the Loxton Research Centre redevelopment.

The Loxton Research Centre redevelopment commenced in February 2016 and it was officially opened on 3 February 2017. Although most work was completed in 2016-17, some minor works and upgrades were completed in 2017-18 and some will continue into 2018-19. As part of the redevelopment, existing facilities were refurbished, including the reception area, offices, kitchen, meeting rooms and laboratories. The redevelopment also involved the construction of a new building that provides a state-of-the-art conference facility, meeting areas, a demonstration kitchen and flexible working spaces.

Total SARMS grant payments for the year for both 3IP and the Regional Economic Development program were $45.9 million ($41.5 million) as funds are not paid on approval, but over time as project milestones are achieved. $25 million ($52.5 million) in Commonwealth SARMS funding was received in 2017-18 to support this grant program.

Regional Development Fund

Grant funding from the RDF supported efforts to grow stronger, more sustainable and competitive regions. Grants are intended to support economic growth, improved infrastructure and job creation in the regions.

Since the RDF's inception, PIRSA has entered into the following grant funding agreements:

- round one (2014-15) – $17.6 million for 39 projects. These projects involve direct investment of around $330 million and aim to create 637 direct, ongoing FTE jobs
- round two (2015-16) – $13.9 million for 24 projects. These projects involve direct investment of around $152 million and aim to create 273 direct, ongoing FTE jobs
- round three (2016-17) – $13.6 million for 22 projects. These projects involve direct investment of around $147 million and aim to create 417 direct, ongoing FTE jobs
- unsolicited requests for funding in 2017-18 – $10.3 million for 29 projects. These projects involve direct investment of around $67 million and aim to create 367 direct, ongoing FTE jobs.

Total payments from the RDF for the year were $15.2 million ($18.4 million) as funds are not paid on approval, but over time as project milestones are achieved.

With a change in State Government in March 2018, the RDF was repurposed as the Regional Growth Fund. How this fund will be spent in the future will be determined by the Minister for Primary Industries and Regional Development.

Other expenses

Other expenses increased by $8.8 million to $9.9 million largely due to:

- a $2.8 million increase in workers compensation liability revaluation expense. This was due to an increase in PIRSA's workers compensation liability as at 30 June 2018 resulting from a review of the liability by a new consulting actuary in 2018-19

- a $4.8 million revaluation expense in 2017-18. A full revaluation of PIRSA's land and building assets was performed as at 30 June 2018 by Liquid Pacific. This expense is for assets with downward revaluation movements in excess of amounts held in the asset revaluation reserve for those assets, given PIRSA takes revaluation adjustments to the asset revaluation surplus on an individual asset basis rather than on an asset class basis. The largest downward movements relate to the Clare Research Centre ($2.1 million) and the Lincoln Marine Science Centre ($1.8 million) which was transferred from the Flinders University to PIRSA in 2015-16.

Income

Advances and grants

Advances and grants revenue increased by $2.2 million to $56.7 million. This was largely due to a $5.1 million increase in grants from industry, offset by a $1.6 million decrease in Commonwealth grants and a $1.5 million decrease in grants received from SA Government entities.

Commonwealth revenues

Commonwealth revenues decreased by $30.8 million largely due to a $27.5 million decrease in SARMS program funding. The amount of Commonwealth SARMS funding received in 2017-18 of $25 million ($52.5 million) is in line with the funding schedules in the National Partnership Agreement on South Australian River Murray Sustainability Program Part A and Part B, taking into account any approved variations to the funding schedules. See more discussion on the SARMS program under 'South Australian River Murray Sustainability program' above.

Commonwealth funding to undertake a feasibility study funded from the National Water Infrastructure Development Fund also decreased by $2.7 million.

Resources received free of charge

Resources received free of charge increased by $2.6 million in 2017-18 largely due to a $1.9 million increase in services received free of charge from SSSA. This is because for the first time this year the appropriation amount paid to agencies was reduced by the amount payable to SSSA and this amount was paid directly to SSSA by the Department of Treasury and Finance (DTF).

Revenues from (Payments to) SA Government

Revenues from the SA Government decreased by $19.8 million to $107 million. This decrease reflects the funding impacts from changes in government priorities, carry overs across the years and budget initiatives and savings strategies.

Payments to the SA Government increased by $14.6 million to $20.3 million, largely due a $20.1 million return of surplus cash under the cash alignment policy in 2017-18. This was offset by a $5.6 million decrease in other payments to the Consolidated Account due to the one-off return of proceeds from the sale of land and buildings at Flaxley and Lenswood in 2016-17.

Statement of Financial Position

Assets

Total assets decreased by $28.1 million to $293.5 million. This decrease was primarily due to a $41.9 million decrease in cash offset by a $7.9 million increase in property, plant and equipment.

PIRSA held cash of $123.7 million ($165.6 million) as at 30 June 2018. The main components of cash held were:

- funds held in the Accrual Appropriation Excess Funds Account – $16.8 million
- funds held under the *Rural Industry Adjustment and Development Act 1985* and other State and Commonwealth schemes for rural financial assistance – $57.5 million
- external funds held in the nature of grants or under cooperative agreements where unspent funds may be returned to the funder – $18.5 million
- Commonwealth funds held for the SARMS program – $8.7 million
- Commonwealth funds held for the various concessional loans schemes – $10.2 million
- deposits with the Treasurer held as working capital – $12 million.

The decrease in cash is largely represented by a $25.6 million decrease in Commonwealth funds held for the SARMS program and a $25.2 million decrease in deposits with the Treasurer held as working capital which are subject to DTF budget and cash alignment policies.

The decrease in funds held for the SARMS program is largely due to grants paid out under the SARMS program totalling $45.9 million in 2017-18, whereas only $25 million in Commonwealth revenue was received during the year.

The decrease in PIRSA's cash held as working capital during 2017-18 is largely due to a $20.1 million return of surplus cash under DTF's cash alignment policy.

Property, plant and equipment increased by $7.9 million in 2017-18 to $121.9 million ($113.9 million). A full revaluation of PIRSA's land and building assets was performed as at 30 June 2018 by Liquid Pacific. This resulted in a $14.2 million increase to the asset revaluation surplus and a $4.8 million expense for assets with downward revaluation movements in excess of amounts held in the asset revaluation surplus for those assets.

Liabilities

Total liabilities increased by $6.6 million to $100.9 million ($94.3 million). This increase was largely due to a $5.3 million increase in borrowings. See discussion under 'Concessional loans schemes' below for more information on this.

Concessional loans schemes

PIRSA's borrowings balance of $31 million is largely made up of borrowings associated with the following concessional loans schemes:

- Farm finance concessional loans scheme
- Drought concessional loans scheme
- Drought recovery concessional loans scheme
- Dairy recovery concessional loans scheme
- Farm business concessional loans scheme.

The Commonwealth pays funds for the above loans schemes in advance in agreed amounts and these funds are held in a special deposit account until paid to approved applicants. When the loans schemes are closed to new applicants, any amounts that are not paid to loan recipients are returned to the Commonwealth.

Farm finance concessional loans were made available to applicants to restructure their debt. This scheme closed on 30 June 2015.

Drought concessional loans were made available to applicants for debt refinancing, operating expenses and to meet the costs of drought recovery and readiness activities. Applications for round one of the scheme closed on 30 June 2015 and applications for round two of the scheme closed on 31 October 2016.

Drought recovery concessional loans were made available to applicants for new debt for planting and restocking activities or refinancing of an existing drought concessional loan. This scheme closed on 31 October 2016.

Dairy recovery concessional loans were made available to dairy farm businesses affected by the May 2016 decision of Murray Goulburn and Fonterra to reduce farm gate milk prices. They were for debt restructuring or new debt, operating expenses and costs associated with productivity enhancement measures. This scheme closed on 31 October 2016.

Farm business concessional loans are made up of drought assistance concessional loans, dairy recovery concessional loans and business improvement concessional loans. Round one of this scheme commenced in December 2016 and closed on 30 June 2017 for drought assistance and dairy recovery concessional loans. Loan payments for round one were paid to eligible applicants in 2017-18 and any unpaid amounts were returned to the Commonwealth.

The Commonwealth requested that States and Territories continue to deliver the farm business concessional loans scheme until 30 June 2018. Round two of the scheme included a new loan measure, business improvement concessional loans, in addition to the continuation of the drought assistance concessional loans and dairy recovery concessional loans. Loans were made to eligible applicants in 2017-18 and will continue into 2018-19 and any unpaid amounts will be returned to the Commonwealth in 2018-19.

We have been advised by PIRSA that from 1 July 2018 applications for farm business concessional loans will be made to the Commonwealth Government's single national administrator, the Regional Investment Corporation.

Concessional loans drawn down as at 30 June 2018 totalled $19.5 million, made up of the following amounts:

- Farm finance concessional loans scheme – $400 000
- Drought concessional loans scheme – $2.1 million (round one)
- Drought concessional loans scheme – $4.1 million (round two)
- Drought recovery concessional loans scheme – $800 000
- Dairy recovery concessional loans scheme – $7 million
- Farm business concessional loans scheme – $4.1 million (round one)
- Farm business concessional loans scheme – $1 million (round two).

As at 30 June 2018 there were no impaired loans and all amounts are expected to be repaid in line with the repayment schedules.

Administered items

PIRSA administers 17 funds that are reported in its administered financial report. The main administered revenues are industry contributions and aquaculture and fishing licence fees. These are then paid out as grants and subsidies to support promotion, research and development, and other activities to benefit the different groups that have paid the contributions.

Total fees and charges revenue, including industry contributions and aquaculture and fishing licences, was $29.5 million ($30.1 million) and grants and subsidies paid out during the year totalled $33.6 million ($30.8 million). The Fisheries Research and Development Fund paid $13.4 million to carry out research, exploration and experiments for the conservation and management of living resources found in waters.

PIRSA also received $5.5 million ($4.7 million) in revenues from the SA Government for the administered activities. $4.8 million of this amount was for payments to South Australian Forestry Corporation for community service obligations including native forest management and fire protection.

Cash of $20.8 million ($22.6 million) is the main asset recognised for the administered activities.

Return to Work Corporation of South Australia (RTWSA)

Financial statistics

Total comprehensive result:	$26.7 million
Premium revenue:	$521 million
Net claims paid:	$305 million
Outstanding claims liability:	$2.7 billion
Net assets:	$527.5 million

As at 30 June 2018 the number of workers receiving income support for a year or more increased by 10.46%, and for less than a year decreased by 15.2%.

The number of seriously injured claimants in the Return to Work Scheme as at 30 June 2018 was 518 (432), an increase of 20%.

The average premium rate was 1.8% in 2017-18, a 0.15% decrease from the 2016-17 rate of 1.95%.

Number of FTEs:	256.4

Significant events and transactions

- The provision for outstanding claims increased by $289.2 million.
- Net investment profit was $218.9 million.
- RTWSA achieved a funding ratio of 119%, meaning that the Return to Work Scheme is fully funded.
- In line with section 203(1) of the *Return to Work Act 2014* an independent review of the Act and its administration and operation was required to be undertaken, three years after its commencement in December 2014. The report on the outcome of the review was tabled in Parliament in July 2018.

Financial report opinion

Unmodified

An emphasis of matter was included in the financial report opinion relating to inherent uncertainty in the estimate of the outstanding claims liability and the funding ratio.

Financial controls opinion

Unmodified

Functional responsibility

RTWSA was established under the *Return to Work Corporation of South Australia Act 1994*.

RTWSA administers the Return to Work Scheme (the Scheme) under the *Return to Work Act 2014* (RTW Act). The Scheme compensates injured workers and helps them return to work using premium and investment income from the Compensation Fund.

Legislative changes

Legislative changes have impacted significantly on the Scheme. The changes aim to get injured workers back to work more promptly and reduce the cost of the Scheme. This will lead to reductions in the Scheme's net liability and premium rates.

On 4 December 2014 the RTW Act was proclaimed, with most provisions commencing on 1 July 2015 and some commencing earlier. The RTW Act replaced the *Workers Rehabilitation and Compensation Act 1986* on 1 July 2015.

The legislative changes separate claims into two categories:

- short-term claims for injured workers with less than 30% whole person impairment (WPI) – will receive income support for up to two years and treatment costs for up to three years. The legislation also introduces a new lump sum benefit for economic loss available to workers with a WPI of at least 5%
- serious injury claims for injured workers with 30% or higher WPI – will receive income support until retirement age, and treatment and other care costs for life.

The Scheme will focus on getting short-term claimants back to work and, in the case of serious injury claimants, providing lifetime care.

Under transitional arrangements, claimants injured before 1 July 2015 with a WPI below 30% received income support until 30 June 2017, unless they exited the Scheme earlier.

Under previous legislation, a worker's income support was reduced by 10% at 13 weeks and a further 10% at 26 weeks, equating to 80% of their pre-injury earnings. Under current legislation, a worker's income support will not be reduced until 52 weeks, at which point it will be reduced to 80% of their pre-injury earnings. This means workers will receive more income support in their first year under current legislation.

The following table shows the percentage of claimants back at work at key intervals after the date of their injury:

Year	4 weeks	13 weeks	26 weeks	52 weeks
2013-14	73%	81%	86%	88%
2014-15	75%	83%	86%	88%
2015-16	75%	83%	86%	88%
2016-17	75%	83%	87%	88%
2017-18	79%	87%	90%	93%

The numbers shown in this chart were provided by RTWSA and are unaudited.

Legislative review

In line with section 203(1) of the RTW Act an independent review of the RTW Act and its administration and operation was required to be undertaken, three years after its commencement in December 2014. The review was completed in June 2018 and the final report was tabled in Parliament in July 2018. The review concluded that the Scheme is still in a transitional phase and that there was no need for comprehensive change at this time.

Overview of Return to Work Scheme

Employers must pay a premium to RTWSA based on remuneration provided to their workers. RTWSA invests the premium revenue until needed to pay compensation and other costs of operating the Scheme, including the claim management fees of two claims agents for managing workers compensation claims. Very small employers are not required to pay a premium, while self-insured employers must pay a fee instead of a premium.

Scope of the audit

The audit program covered major financial systems to obtain sufficient evidence to form an opinion on the financial report and internal controls.

Specific areas of audit attention in 2017-18 included:

- agent assurance framework
- premiums
- investments
- actuarial estimates of outstanding claims liabilities
- determination of claims for workers compensation
- workers compensation payments such as income support, lump sums and medical costs
- general operating expenses
- ICT infrastructure and systems.

Internal audit activities were reviewed to help plan and conduct the audit of RTWSA's control environment.

Audit findings and comments

Auditor's report on the financial report

The following is an extract from the Independent Auditor's Report on RTWSA's 2017-18 financial report, which is unmodified but notes a significant inherent uncertainty relating to the outstanding claims provisions and funding ratio implications.

Opinion

In my opinion, the accompanying financial report gives a true and fair view of the financial position of the Return to Work Corporation of South Australia as at 30 June 2018, its financial performance and its cash flows for the year then ended in accordance with the Treasurer's Instructions issued under the provisions of the Public Finance and Audit Act 1987 *and Australian Accounting Standards.*

Inherent uncertainty – outstanding claims liability and funding ratio

Without qualification to the opinion expressed above, attention is drawn to notes 4, 9 and 10 of the financial report. There is significant uncertainty surrounding the financial impact of legislative reforms which will only become clearer as outstanding claims experience emerges in future financial periods. If in future years the actual cost of claims described in notes 9 and 10 are greater than the balances recorded in the financial statements, this will adversely impact the funding ratio described in note 6.

Communication of audit matters

Our audit did not identify any matters that required communication to RTWSA.

Interpretation and analysis of the financial report

Highlights of the financial report

	2018 $'million	2017 $'million
Underwriting result		
Premium revenue from registered employers	521	517
Net claims paid	(305)	(355)
Decrease (Increase) in net outstanding claims liability	(294)	6
Claim management fees	(62)	(66)
Other underwriting expenses	(16)	(16)
Underwriting result	(156)	86
Net investment and other income		
Net investment profit	219	210
Other income	13	12
Net investment profit and other income	232	222
Operating expenses		
Employee benefits expenses	(30)	(37)
Other expenses	(28)	(27)
Total operating expenses	(58)	(64)
Result from operating activities before tax equivalents	(18)	244
Tax equivalents	-	(73)
Other comprehensive income		
Re-measurements of defined benefits liability	9	4
Total comprehensive result	27	175
Net cash provided by (used in) operating activities	121	115
Net cash provided by (used in) investing activities	(123)	(70)

	2018 $'million	2017 $'million
Assets		
Investments	3 231	2 992
Other assets	75	83
Total assets	3 306	3 075
Liabilities		
Outstanding claims	2 749	2 460
Other liabilities	29	114
Total liabilities	2 778	2 574
Total equity	528	501

Statement of Comprehensive Income

Total comprehensive result

RTWSA's comprehensive result depends significantly on:

- premium rates being set before the start of the financial year with the aim of ensuring premium revenue and investment income will at least cover the cost of new claims incurred during the financial year and administrative costs. The premium setting process depends significantly on the actuarial estimate of the cost of new claims likely to be received in the coming year and other factors determined by RTWSA's Board of Management
- the actuarial estimate of the outstanding claims provision
- movements in the market value of its investments.

The total comprehensive result for the year was a profit of $27 million ($175 million). The decrease of $148 million in the total comprehensive result was due mainly to a $251 million increase in the cost of claims. The increase in the net outstanding claims liability of $294 million was the major contributor to the increased cost of claims (refer to commentary under 'Liabilities' below).

The increase in the cost of claims was partially offset by:

- an increase in net investment profit of $9.3 million
- an increase in premium revenue of $3.9 million
- a decrease in claims management fees of $4.2 million
- a decrease in general operating costs of $5.7 million.

In 2016-17 the total comprehensive result also included $73.4 million in tax equivalents required to be paid under Treasurer's Instruction 22 'Tax Equivalent Payments'. The *Return to Work Corporation of South Australia Act 1994* restricts the application of tax equivalents to financial years in which RTWSA has achieved both a funding level of at least 100% (with its outstanding claims liabilities at a 75% probability of sufficiency) and a profit from insurance operations. Under the tax equivalents regime, the corporate tax rate (30%) is applied to the operating profit. In 2017-18 RTWSA made a loss on its insurance operations and therefore were not required to pay any tax equivalents.

The following chart shows RTWSA's total comprehensive result for the five years to 2018.

Over the five years the comprehensive result has been relatively stable other than in 2015, when there was a significant increase. This was due to the introduction of the new legislation in July 2015 which resulted in a significant decrease in the net outstanding claims liability.

Underwriting result

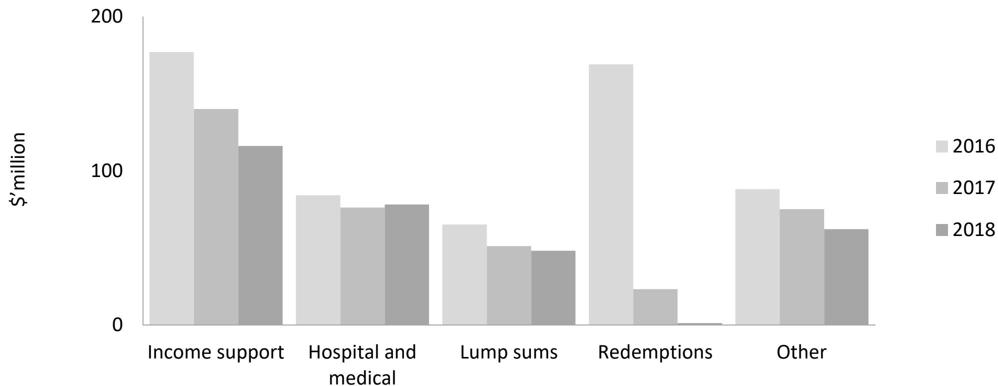
The underwriting result is essentially registered employer premium revenue less claims expense. Investment income does not form part of the underwriting result. AASB 1023 'General Insurance Contracts' requires the underwriting result to be shown separately in the Statement of Comprehensive Income to help show the extent to which underwriting activities rely on investment income for the payment of claims.

The underwriting result was a loss of $156 million, compared to a profit of $86 million in 2016-17. The $242 million downturn reflects a $251 million increase in the cost of claims mainly as a result of:

- a $294 million increase in the net outstanding claims liability
- a $45 million decrease in claims payments due mainly to:
  - income support decreasing by $22 million to $116 million as a result of fewer claimants receiving income support, due mainly to RTWSA's initiatives to get claimants back to work sooner
  - redemptions paid to claimants decreasing by $22 million as a result of the cessation of the redemption program
- a $4 million increase in premiums due mainly to higher levels of remuneration reported by employers
- a $4 million decrease in claim management fees.

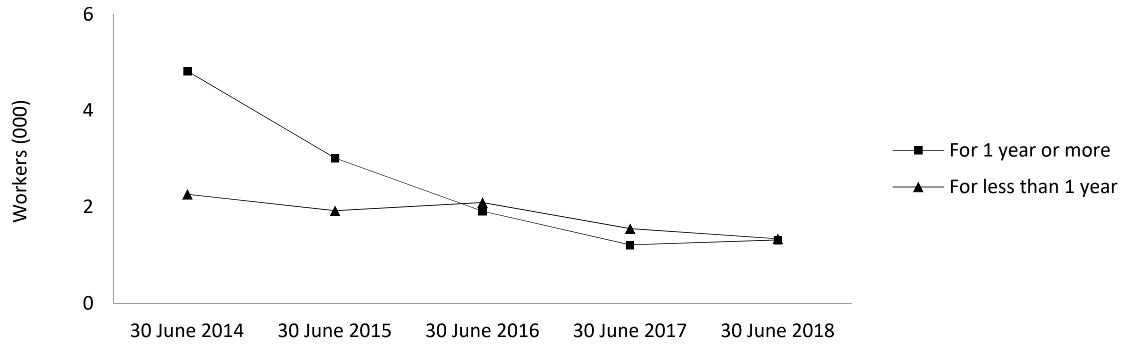
Claim payments

The following chart analyses claim payments for the three years to 2018.



The chart shows the downturn in income support payments in 2018 ($22.2 million) due mainly to RTWSA's focus on early intervention by mobile case managers to get claimants back to work sooner. The payment of redemptions was brought forward in 2016 and consequently redemptions were lower in 2017. The redemptions program finished in 2018.

The change in the number of workers receiving income support for the five years to 2018 is reflected in the following chart.

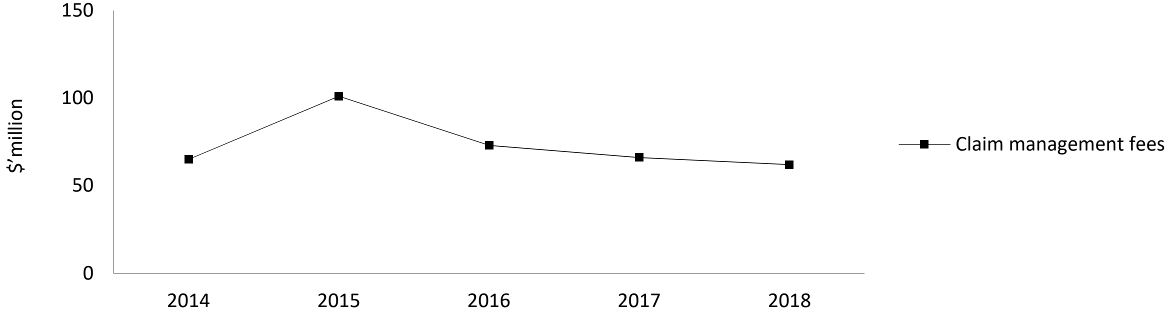


The numbers shown in this chart were provided by RTWSA and are unaudited.

The chart shows that the number of workers receiving income support started decreasing in 2015. In 2018 the number of workers receiving income support for a year or more (long-term claims) decreased by 10.46%, and for less than a year increased by 15.2%.

Claim management fees

The following chart shows claim management fees for the five years to 2018.



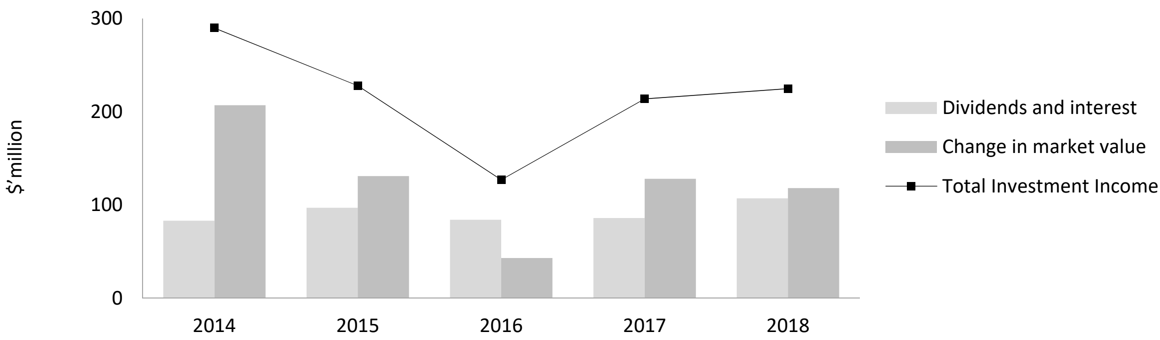
Claim management fees are paid to RTWSA's two claims agents for managing workers compensation claims.

Claim management fees increased in 2015 due mainly to new incentives for managing RTWSA's initiatives for getting claimants back to work, as well as additional payments being made to cover the extra costs incurred by the agents due to Scheme reform. In 2018, claim management fees decreased by $4 million to $62 million, partly as a result of the cessation of transitional allowance payments to agents as part of the Scheme reform.

Investment profits

RTWSA's investment profits have fluctuated significantly over recent years as a result of changes in the market value of its investments, which depend on financial market conditions and macroeconomic influences.

The following chart shows RTWSA's investment income for the five years to 2018.

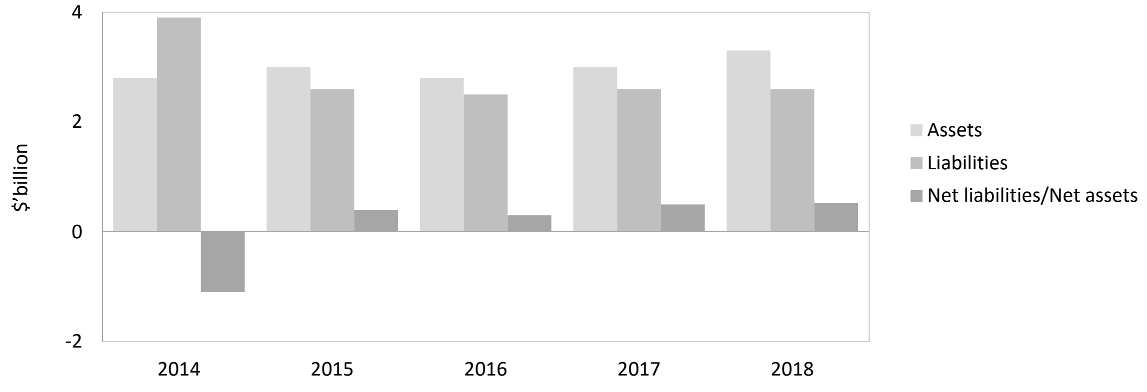


As shown, dividend and interest income has remained relatively stable with gradual growth over the past three years. The market values of RTWSA's investments have significantly increased since 2016 as a result of the upturn in investment markets and this is reflected in total investment income since that time.

Statement of Financial Position

In 2018 there was an increase in net assets of $27 million, due mainly to investments increasing by $239 million to $3.231 billion as a result of increases in the market values of investments and no requirement to pay income tax equivalents this financial year compared to $73 million paid in 2017. This was offset by an increase in the provision for outstanding claims totalling $289 million.

The following chart analyses RTWSA's assets and liabilities for the five years to 2018.



The chart reflects the impact on RTWSA's financial position of the 2014 legislative changes and its initiatives to get claimants back to work sooner. In 2014-15 the Scheme became fully funded for the first time in many years. The funding ratio (assets divided by liabilities) was 119% in 2017-18 compared to 119.5% in 2016-17.

Liabilities

Outstanding claims – Compensation Fund

Outstanding claims for the Compensation Fund comprised 96% (96%) of RTWSA's liabilities. The outstanding claims liability covers expected future payments including those related to claims reported but not yet paid, incurred but not yet reported and incurred but under-reported.

The liability is determined by RTWSA's management and Board of Management considering and assessing a comprehensive actuarial review of claims exposures by an independent actuary. Information about the actuarial estimation of outstanding claims liabilities is provided in notes 4 and 9 of RTWSA's financial report.

The net central estimate of outstanding claims liabilities was $2.275 billion at 30 June 2018. The net outstanding claims provision was $2.616 billion at 30 June 2018, including a risk margin of $341 million intended to achieve a 75% probability of sufficiency.

The net central estimate of outstanding claims liabilities has increased from $2.017 billion at 30 June 2017. The $258 million increase can be attributed to:

- a $471 million increase in claims incurred less payments made in 2017-18
- a $43 million increase due to economic assumptions reflecting decreases in risk free long-term discount rates. A decrease in the discount rate leads to an increase in the liability. Although changes to discount and inflation rate assumptions are impacted by events outside of RTWSA's control, the actuary determines the rates with reference to market practice. The actuary decreased the discount rate from 3.87% in 2017 to 3.33% in 2018
- a $381 million decrease due to expected payments for current and prior year claims
- a $125 million increase due to a more unfavourable claims experience than was projected for both short-term claims and serious injury claims.

The liability for long-term claims may extend for many years beyond the current year, causing the liability to grow. The reduction in short-term claims has resulted in long-term claims becoming a greater proportion of total claims. This is reflected in the weighted average expected term to settlement of claims remaining at 15 years in 2018 (refer note 9(a) of RTWSA's financial report).

Sensitivity to changes in key assumptions

The sensitivity analysis in note 9(f) of RTWSA's financial report illustrates that relatively small changes to key assumptions in the estimate can result in changes in the order of millions of dollars.

For example, a 1% decrease in the real discount rate would lead to an increase in the net outstanding claims provision of $152 million. There is also significant uncertainty regarding the serious injury claims cost arising from factors such as life expectancy, superimposed inflation and the ultimate number of claims. The actuary's sensitivity analysis suggest changes to each of these assumptions could change the net outstanding claims provision in the order of $100 million to $500 million.

Impact of outstanding claims liability on funding ratio and premiums

As a result of legislative changes and RTWSA's initiatives to get claimants back to work sooner, the Scheme became fully funded for the first time in many years in 2014-15. The funding ratio (assets divided by liabilities) was 119.5% in 2016-17 and 119% in 2017-18.

RTWSA reduced the average premium rate from 1.95% in 2016-17 to 1.8% in 2017-18.

Legislative reform and other developments affecting the uncertainty of the outstanding claims liability

The actuarial estimation is primarily based on the anticipated impact of new legislation. The impact will only become clearer as actual claims experience emerges under the legislation. Further, note 9 of RTWSA's financial report specifies the nature of a number of key uncertainties associated with the actuarial estimation and the sensitivities of the estimation to changes in key assumptions. Of particular note are the uncertain actual experience for short-term claims and serious injury claims and WPI assessments. The independent actuary noted the following:

- Interpretation and legal challenge – the RTW Act has elements that are subject to interpretation and legal challenge. The outcome of any challenges and the potential impact on the Scheme are unknown.
- WPI assessments – are the gateway to lifetime benefits for serious injury claimants and new lump sum benefits for economic loss. The robustness of the WPI assessment rules under the legislation has not been tested in practice. If these rules do not operate as intended, the cost implications may be significant.
- Future cost escalation – future cost growth in medical treatment and personal care is a particular risk for the lifetime benefits payable to serious injury claimants.
- Return to work – the potential improvements to Scheme culture as a result of new hard boundaries may encourage earlier return to work for short-term claims. Counter to this, the potential for benefits to continue while claims are in dispute may encourage further disputes and worsen return to work experience up to the two year cut-off.
- Outcomes for claims with current disputes – the valuation basis assumes a high level of success on currently disputed claims.

We note there are a number of key cases currently before the Courts where the outcomes may have a significant impact on the Scheme.

Audit approach to the estimate of outstanding claims liability

Due to the nature and significance of the Scheme estimate of outstanding claims liability, our audit approach has included focused review of the Scheme actuary's projections by an independent professional actuary engaged by the Auditor-General. The nature and impact of the legislative changes continued to warrant a high level of audit scrutiny, particularly at the start of the new Scheme arrangements.

Our audit did not identify any issues or variations from expected practice that would suggest the estimate of outstanding claims liability is unreasonable or that the estimate for 30 June 2018 should be adjusted in any material way. The inherent uncertainty associated with the new Scheme arrangements, however, prevents the degree of certainty over the estimate that would warrant no comment or clarification to the audit opinion.

The key valuation uncertainties in this valuation are: potential legal challenges; the unwind of legislative changes; the eventual outcomes from operational strategies; resolution of existing disputes; future cost growth in medical and treatment related expenditure items for long-term claims; actual experience for two-year income support claims; and WPI assessments and actual experience for serious injury claims. The uncertainties may have favourable as well as unfavourable outcomes for the Scheme.

Probability of sufficiency

As disclosed in note 9 of RTWSA's financial report, the estimate of outstanding claims liability is determined by reference to a 75% probability that the provision for outstanding claims will be adequate. Given the greater uncertainty with the estimate, RTWSA has maintained the risk margin at 15% as at 30 June 2018 (the same as 2017), so that the net liability is adequately provided to approximately a 75% probability of sufficiency. RTWSA's performance statement, authorised by the Treasurer, requires it to estimate its claims liabilities using a risk margin with at least 65% probability of sufficiency for the net liability. The Australian Prudential Regulation Authority sets a minimum of 75% in Prudential Standard GPS 320 'Actuarial and Related Matters'. Public sector entities are not bound by this requirement but the parameters adopted by RTWSA are consistent with the requirements of the standard.

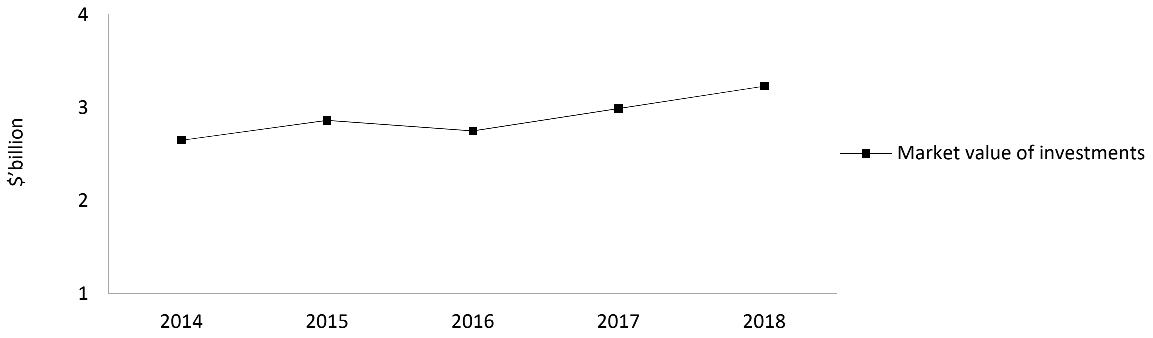
Investments

RTWSA's investment portfolio of $3.231 billion ($2.991 billion) mainly comprises investments in pooled funds, discrete mandate funds and fixed-term deposits. RTWSA has appointed the National Australia Bank to be custodian of the pooled funds and discrete mandate funds.

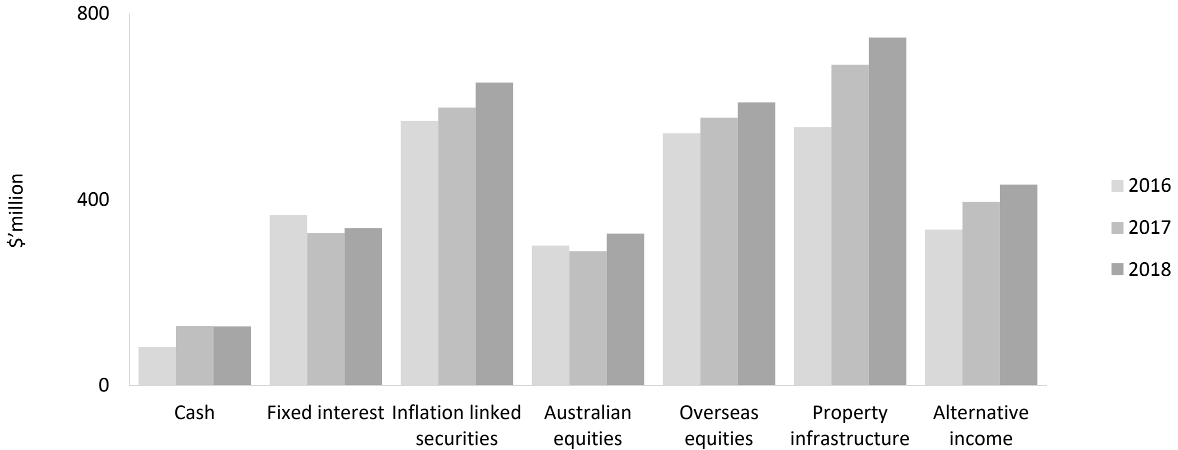
Investment decisions

RTWSA investment officers implement its investment strategy, which involves rebalancing the investment portfolio held in pooled funds, discrete mandate funds and fixed-term deposits to minimise risk and achieve target returns. The investment officers also receive expert advice on investment matters from an external consultant.

The following chart shows the market value of RTWSA's investments for the five years to 2018.



The following chart shows the RTWSA's investments by asset class for the three years to 2018.



According to RTWSA, the return on investments measured in line with Australian Investment Performance Standards for the last five years to 2018 were as shown in the following table.

	2014	2015	2016	2017	2018
Return on investments	12.6%	8.6%	4.6%	7.7%	7.5%
RTWSA Board of Management approved targeted return	6.5%	5.0%	4.5%	4.9%	4.6%

The current long-term objective for the investment program is a return of CPI plus 2.5% as approved by RTWSA's Board of Management. The actual return on investments has exceeded these targets.

South Australia Police (SAPOL)

Financial statistics

Employee benefits expense:	$750 million
Net cost of providing services:	$891 million
Total net revenues from SA Government:	$841 million
Property, plant and equipment:	$340 million
Employee benefits liability and related on-costs:	$306 million
Provisions including workers compensation liability:	$121 million

Number of active FTEs:	
Police Act 1998 employees	4845
Unsworn employees	913
Protective Security	125
Total	5883

Administered items:	
Revenue from expiation fees	$68 million
Revenue from Victims of Crime levy	$11 million

Significant events and transactions

- The Injury and Income Protection Policy was ratified by the SA Employment Tribunal in November 2017 and now forms part of the Police Officers Award. SAPOL's liability is now known as an additional compensation provision.
- The additional compensation provision increased by $46 million due to an increase in the number of successful claims and increases in the projected number of successful future claims. Estimating this provision is subject to significant uncertainty.
- SAPOL replaced its legacy payroll system with Chris21 in November 2017.
- Work to implement a new district policing model progressed. SAPOL is merging the six Local Service Areas into four districts.
- $35 million was returned to the Consolidated Account under the cash alignment policy.

Financial report opinion

Unmodified

Financial controls opinion

Modified

Key issues:

- Leave taken by non-commissioned officers not recorded in the payroll system

Functional responsibility

SAPOL is an administrative unit established under the *Public Sector Act 2009* and operates under a legislative framework prescribed by the *Police Act 1998*.

The functions of SAPOL are to:

- uphold the law
- preserve the peace
- prevent crime
- assist the public in emergency situations
- coordinate and manage responses to emergencies
- regulate road use and prevent vehicle collisions.

Scope of the audit

The audit program covered major financial systems to obtain sufficient evidence to form an opinion on the financial report and internal controls.

Specific areas of audit attention in 2017-18 included:

- payroll
- workers compensation
- cash
- expiation revenue
- revenue from fees and charges
- expenditure
- government purchase cards
- procurement and contract management
- police records management system – Shield Business Transformation program.

Audit findings and comments

Assessment of controls

In my opinion, the controls exercised by South Australia Police in relation to the receipt, expenditure and investment of money, the acquisition and disposal of property and the incurring of liabilities, except for all matters outlined under 'Communication of audit matters', are sufficient to provide reasonable assurance that the financial transactions of South Australia Police have been conducted properly and in accordance with law.

Communication of audit matters

Matters identified by the audit were detailed in management letters to the Commissioner of Police. The main matters raised and related responses are detailed below.

Payroll – leave recording

For 2017-18 employee benefits liabilities and related on-costs totalled $306 million.

Leave taken by non-commissioned officers, who use the Workforce Central system (WFC) to record time worked and attendance, is not recorded in the payroll system until an approved leave form is received. Similarly, leave taken by unsworn personnel, who submit timesheets through the Electronic Timesheet Management System (ETMS), is not recorded in the payroll system until an approved leave form is received.

To ensure the completeness and accuracy of the payroll system, it is important that SAPOL ensures timesheets and leave forms are submitted and approved for both non-commissioned officers and unsworn staff.

Commissioned officers do not submit timesheets due to the nature of their role. To ensure leave taken by commissioned officers is completely and accurately recorded in the payroll system, SAPOL expects supervisors to certify the leave records of their assigned staff every four weeks.

Our review of SAPOL's controls to ensure the timely submission and processing of leave forms identified the following matters.

Leave taken by non-commissioned officers not recorded in the payroll system

We identified a significant difference in the volume and value of employee leave records recorded in WFC and leave records in the payroll system.

Before the Chris21 payroll system was implemented in November 2017, leave taken by non-commissioned officers was not recorded in the payroll system until an approved leave form was submitted. The processing of all leave forms was therefore critical to ensure the completeness and accuracy of leave records in the payroll system.

Before February 2017 Shared Services SA (SSSA) used an outstanding leave forms report, produced from the HRMS payroll system, to identify outstanding leave forms. SSSA staff used this report to process the outstanding leave records directly into the HRMS system.

In May 2017 we wrote to SAPOL noting that:

- from February 2017 SSSA stopped processing leave reported on the outstanding leave forms report
- neither SSSA or SAPOL were adequately reviewing the report for further action.

At that time, we reported the risk that leave taken by non-commissioned officers was not being recorded in HRMS and recommended that SAPOL implement a regular review of the outstanding leave forms report.

SAPOL transitioned its legacy HRMS payroll system to Chris21 in November 2017, and leave forms are no longer used. All employees are now required to apply for leave in Chris21, with managers approving leave applications online. We were advised that Chris21 does not produce an outstanding leave report and that neither SAPOL or SSSA regularly reconciles leave records in WFC with those recorded in Chris21.

At our request, SAPOL reconciled leave recorded in WFC with leave recorded in the payroll system between October 2017 and February 2018. This identified 79 612 hours of leave recorded in WFC that was not recorded in the payroll system. We estimated the value of this leave at $3.4 million.

It is likely that this control breakdown was caused by the cessation of leave processing using the outstanding leave forms report from February 2017. In May 2018 we recommended that SAPOL immediately reconcile the value of leave taken since February 2017 in WFC with the value of leave recorded in the payroll system and process all outstanding leave transactions.

We also recommended that SAPOL implement controls to ensure all outstanding leave records are updated into Chris21, noting that this may require SAPOL to introduce a regular reconciliation of leave recorded in the WFC system with leave recorded in Chris21.

In August 2018 SAPOL responded that:

- it had corrected most of the discrepancies identified for the period October 2017 to March 2018, reducing SAPOL's leave liabilities – adjustments valued at $300 000 remain outstanding
- a preliminary review of leave not processed over the period from February 2017 to September 2017 had identified about $1.4 million of employee entitlements that need to be corrected in 2018-19
- it is developing a mismatch tool to identify any inconsistencies between leave applications in WFC and Chris21, with SSSA to then action any items identified.

Information and communications technology and control

Police records management system – Shield Business Transformation program (Shield program) status

In 2017-18 SAPOL progressed its program to implement a new police records management system, Niche RMS, now referred to as the Shield program. The program included the implementation of Stage 1 (custody management and criminal associations) for an approved budget of $13 million. A further $45 million is budgeted to implement Stages 2 to 4.

At the time of our review Stage 1 was completed, with work continuing on Stages 2 to 4.

As at 30 June 2018 investment expenditure on the Shield program totalled $27 million, while operating and recurrent expenditure totalled $12 million.

The remaining budget for investment expenditure is $11 million, while the remaining budget for operating and recurrent expenditure is $5 million.

Shield program follow-up review

In 2017-18 we completed a follow-up review of the Shield program to track the progress of Stages 2 to 4. We noted that there have been continuing delays to the project schedule caused by system development delays, remediation of defects and SAPOL resourcing. This is magnified by a number of internal SAPOL activities, including the organisational reform project that requires coordination with the roll-out of Shield.

Matters identified by our review were detailed in a management letter to the Commissioner of Police that noted the following:

- SAPOL has not developed and documented a benefits realisation plan for the Shield program. It will need to do this to ensure the benefits associated with implementing the Shield program are achieved.
- There were many items recorded on the risk and issues register that had no clear action plans and time frames for resolution. In addition, some issues have remained unresolved for an extended period of time, which may further impact the program schedule.
- SAPOL has an escrow agreement with the Shield vendor that requires the vendor to deposit all and any updated versions of source code with the escrow agent to accurately reflect all modifications, amendments, updates and new releases made to or in respect of the licensed software every six months.

  We identified that the most recent deposit was in early-December 2015. Since this time Shield has been subject to a number of changes, including a build released into production in August 2017 to resolve a large number of high priority production defects.

SAPOL responded that:

- it will start to develop a benefits realisation plan
- it would make the following changes to risk and issues processes:
  - all new registered issues and risks will require a target date for resolution
  - critical and major issues and risks will continue to be monitored fortnightly
  - issues will be reviewed quarterly with commentary added to update their status
- the vendor has recently submitted their latest Shield software code to the Public Trustee for escrow. SAPOL also advised that the vendor has scheduled further escrow deposits in October 2018 and March 2019.

Shared Services SA – financial systems and transaction processing environments

SSSA processes financial transactions on behalf of SAPOL under service level determinations. The main systems and control environments include accounts payable, payroll and general ledger financial functions.

Our review and evaluation of controls for these systems concluded that controls were effective for 2017-18.

SSSA is discussed further in the commentary under 'Department of the Premier and Cabinet' in this Report.

Interpretation and analysis of the financial report

Highlights of the financial report*

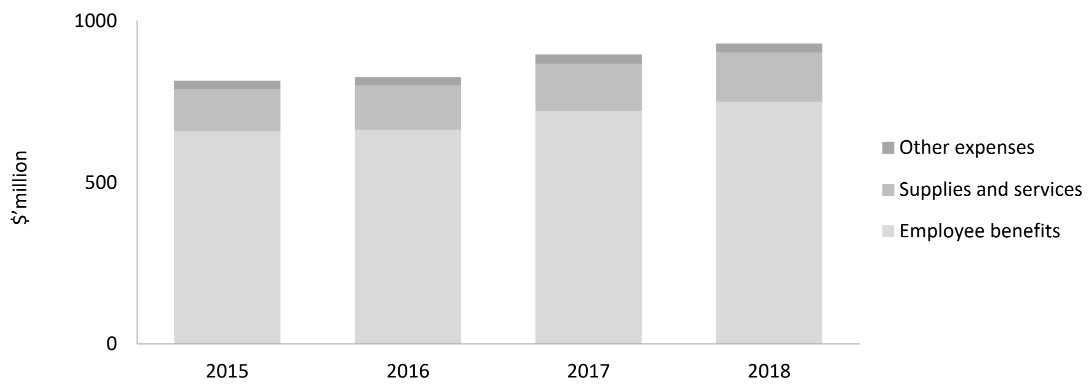
	2018 $'million	2017 $'million
Expenses		
Employee benefits	750	721
Supplies and services	152	146
Other expenses	28	29
Total expenses	930	896
Income		
Fees and charges	27	27
Other revenues	12	11
Total income	39	38
Net cost of providing services	891	858
Revenues from (Payments to) SA Government	841	853
Net result	(50)	(5)
Other comprehensive income	5	-
Total comprehensive income	(45)	(5)
Net cash provided by (used in) operating activities	(1)	78
Assets		
Current assets	174	194
Non-current assets	378	377
Total assets	552	571
Liabilities		
Current liabilities	126	130
Non-current liabilities	327	298
Total liabilities	453	428
Total equity	99	144

* Table may not add due to rounding.

Statement of Comprehensive Income

Expenses

The following chart shows SAPOL's main expense items for the four years to 2017-18.



Supplies and services expenses increased by $6 million (4%) in 2017-18, driven mainly by:

- an increase in communication and computing expenses of $4 million, due mainly to additional software licences and hosting services
- an increase in motor vehicle related expenses of $2 million, due mainly to an increase in motor vehicle leases, higher fuel costs and more services and repairs
- an increase in utilities of $1.5 million, due mainly to increased electricity costs.

Employee benefits account for 81% of total expenses and increased by $29 million in 2017-18. This movement was due mainly to increases in salaries and wages ($28 million) and the additional compensation provision ($32 million), offset by a decrease in workers compensation ($29 million).

Salaries and wages increased by $28 million to $522 million, due mainly to enterprise agreement salary increases, increases in penalties and allowances and an increase in accrued salaries and wages.

Additional compensation provision

Following the commencement of the *Return to Work Act 2014* on 1 July 2015, the Police Association of South Australia (PASA) campaigned for additional insurance arrangements for police officers. In February 2017 the SA Government and PASA reached an agreement on a new compensation benefit. In November 2017 a negotiated agreement was ratified by the SA Employment Tribunal and the benefit now forms part of the Police Officers Award (clause 4.17 'Additional Compensation for Certain Work Related Injuries or illnesses').

Under the additional compensation provision, eligible police officers who are injured in circumstances detailed in the award will be provided with the financial support and/or medical expenses detailed in the award, where the following applies:

- they have not been assessed as having a 30% or more Whole Person Impairment
- they have not made a return to work within the meaning of the *Return to Work Act 2014*
- they are temporarily or permanently incapacitated for work and have exhausted their entitlements under the *Return to Work Act 2014*.

The additional compensation liability increased by $46 million to $61 million, due mainly to:

- an increase in the number of known claims
- a significant increase in the projected number of successful future claims, reflecting the additional claims experience.

The increases in known and projected claims are influenced by the following differences in the entitlements included in clause 4.17 of the Police Officers Award, compared to those previously included in the Injury and Income Protection Policy (IIPP):

- The IIPP causation criteria for an eligible injury referred to an injury being caused by a criminal act directed at the police officer. The causation criteria in the award removed the reference to 'directed at' and now refers to an injury caused by a criminal act or an act that appears to be criminal. This change is likely to lead to a broader interpretation of the link between an injury and a criminal act.

- Under the IIPP, if an officer made a return to the workplace they were ineligible for any entitlements. This eligibility test was removed from the award, which now enables entitlements to medical expenses.
- Former officers and cadets whose employment commenced on or after 30 September 1987 are now defined as eligible officers under the award.

Significant uncertainly with the estimated additional compensation provision

There is a significant degree of uncertainty associated with the estimate of the additional compensation provision. In addition to the general uncertainties associated with estimating future claim and expense payments, the provision is impacted by the absence of a meaningful claims history and the evolving nature of the interpretation of, and evidence required to meet, eligibility criteria.

Given these uncertainties the actuary has noted that the actual cost of additional compensation claims may differ materially from the estimate.

Workers compensation provision

The decrease in workers compensation expense reflects the movement in the workers compensation liability. The liability decreased by $22 million in 2018 due mainly to a decrease in:

- the number of known claims
- assumed medical costs for known claims
- SAPOL's relative share of incurred but not reported claims estimated by the actuary at a whole-of-government level.

This decrease followed an increase in the liability of $5 million in 2017. The accumulated impact of these movements explains the decrease in the workers compensation expense for 2018.

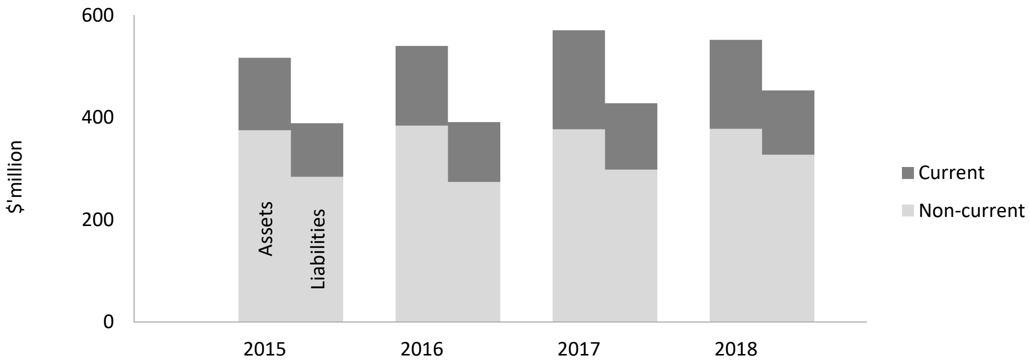
There is a significant degree of uncertainty associated with estimating future claim and expense payments. The liability is impacted by agency claim experience relative to other agencies, average claim sizes and other economic and actuarial assumptions.

Income

SAPOL receives government funding based on annual budgeted expenditure, less estimated revenues from fees and charges and other sources. Net revenues from the SA Government decreased by $12 million to $841 million, reflecting an increase in appropriations largely to fund salary and wage increases, offset by a return of $35 million to the Consolidated Account. Returns to the Consolidated Account under the Cash Alignment Policy reflect the build-up of surplus cash.

Statement of Financial Position

For the four years to 2017-18, a structural analysis of assets and liabilities is shown in the following chart.

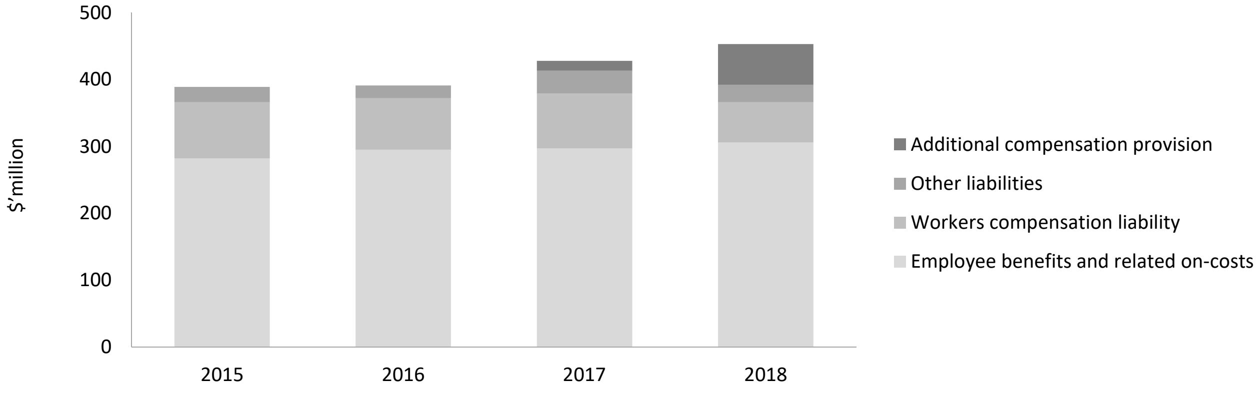


Assets and liabilities

Current assets decreased by $20 million, driven by a similar reduction in cash.

The decrease in cash reflected a $35 million payment to the Consolidated Account under the Cash Alignment Policy and an $8 million decrease in creditors and accrued expenses, both partially offset by a $21 million increase in revenue from the SA Government. The decrease in creditors was due mainly to the recognition in 2017 of an $8 million payable for superannuation and payroll tax. The comparable costs for 2018 were paid before 30 June 2018.

The significance of employee related liabilities compared to total liabilities is shown in the following chart.



Total liabilities increased by $25 million (6%) due mainly to a $24 million increase in provisions, a $12 million increase in employee benefits liability and an $11 million decrease in payables.

Provisions increased predominately as a result of a $46 million increase in an actuarial estimate for the additional compensation provision, partially offset by a $22 million decrease in SAPOL's workers compensation liability.

The employee benefits liability increased due mainly to a $6 million increase in accrued salaries and wages, reflecting differences in the timing of payments in June 2017 and June 2018, and a $4 million increase in the long service leave liability.

Total payables decreased by $11 million reflecting the timing of payments for superannuation and payroll tax in 2017 and 2018. In 2018 SAPOL identified an error in the calculation of employment on-costs recognised in payables as at 30 June 2017. The subsequent correction of this error in 2018 largely explains the $4 million decrease in the non-current employment on-costs.

Administered items

Expiation fees

Expiation fees are collected by SAPOL on behalf of the SA Government. SAPOL treats the collection of expiation revenue under the *Expiation of Offences Act 1996* as an administered item and pays the revenue to the Consolidated Account. Expiation fees collected increased by $1 million to $68 million in 2017-18.

Victims of Crime levy

SAPOL collects money associated with the *Victims of Crime Act 2001* from the expiation of offences included on expiation notices issued by police officers and other authorised officers. The *Victims of Crime Act 2001* provides for the payment of compensation to people who suffer injury as a result of criminal acts and recovering the money from offenders.

SAPOL collects money and remits it to a special interest bearing deposit account managed by the Attorney-General's Department.

In 2017-18, Victims of Crime levy receipts paid to the Attorney-General's Department totalled $11 million.

Further commentary on operations

Staffing

SAPOL employed the following active FTEs by category as at 30 June for the past two years.

	2018 FTEs	2017 FTEs
Police Act 1998 employees	4 845	4 816
Unsworn employees	913	921
Protective Security	125	132
Total	5 883	5 869

Source: FTE data was supplied by SAPOL and is unaudited.

South Australian Fire and Emergency Services Commission (SAFECOM)

Financial statistics	Consolidated net cost of providing services:	$319 million
	Total consolidated contributions from the Community Emergency Services Fund:	$251 million
	Employee benefits liability and related on-costs:	$61 million
	Workers compensation liability:	$75 million
	Number of FTEs (SAFECOM consolidated):	1283

Significant events and transactions

- The workers compensation liability increased by $38 million due to a significant increase in the number of long-term claims under firefighter presumptive cancer compensation arrangements, and the resulting increase in incurred but not reported claim estimates.
- The sector recognised a new provision for additional compensation arising from changes to enterprise agreements. Changes to enterprise agreements provide continuing benefits to workers whose entitlements have ceased under the statutory workers compensation scheme. This new liability was estimated at $18 million but is subject to significant measurement uncertainty.
- In January 2018 the Alert SA App experienced significant performance issues. As a result the App was decommissioned and written off.

Financial report opinion

Unmodified

Financial controls opinion

Modified

Key issues:

- No legal compliance program
- No internal audit function
- Bona fide and leave return reports not reviewed or incomplete
- Inadequate review of reporting on manual payments

Functional responsibility

SAFECOM is established by the *Fire and Emergency Services Act 2005*.

The functions of SAFECOM include responsibility for corporate services across the emergency services sector. SAFECOM supports and allocates sector resources and has a leadership role in state-wide emergency management.

SAFECOM administers the Community Emergency Services Fund (the Fund), the main source of funding for all emergency services sector agencies.

Scope of the audit

The audit program covered the major financial systems to obtain sufficient evidence to form an opinion on the financial report and internal controls.

The audit included access to systems and information maintained by SAFECOM and the emergency services organisations (ESOs) to conduct relevant financial transaction and control compliance tests. The ESOs are made up of the:

- South Australian Metropolitan Fire Service (SAMFS)
- South Australian Country Fire Service (SACFS)
- South Australian State Emergency Service (SASES).

Specific areas of audit attention in 2017-18 included:

- expenditure
- payroll
- revenue
- non-current assets, including capital works in progress and vehicle management
- cash at bank
- financial accounting
- workers compensation
- governance
- the Fund.

Audit findings and comments

Assessment of controls

In my opinion, the controls exercised by the South Australian Fire and Emergency Services Commission in relation to the receipt, expenditure and investment of money, the acquisition and disposal of property and the incurring of liabilities, except for all matters outlined under 'Communication of audit matters', are sufficient to provide reasonable assurance that the financial transactions of the South Australian Fire and Emergency Services Commission have been conducted properly and in accordance with law.

Communication of audit matters

Matters identified by the audit were detailed in management letters to the Chief Executive and chief officers responsible for the governance of SAFECOM and the ESOs. The main matters raised and related responses are detailed below.

Governance

The *Fire and Emergency Services Act 2005* requires SAFECOM to develop and implement a framework of sound corporate governance across the emergency services sector.

Good governance practice is a foundation for the effective performance of public sector entities. Public sector governance encompasses leadership, direction, control and accountability, and helps an entity to achieve its outcomes in such a way as to enhance confidence in the entity, its decisions and its actions. Good public sector governance is about getting the right things done in the best possible way, and delivering this standard of performance on a sustainable basis.

The importance of sound corporate governance is reinforced through Treasurer's Instructions, with every chief executive having a responsibility to establish and maintain an appropriate internal control environment in line with Treasurer's Instruction 2 'Financial Management'.

We have identified the need for SAFECOM to strengthen its corporate governance across the sector in the following areas.

Internal audit

While SAFECOM has established an independent Audit and Risk Committee for the sector, it does not have an internal audit function. Internal audit provides an independent and objective review and advisory service to provide assurance to the Chief Executive that the entity's financial and operational controls designed to manage the organisation's risks and achieve its objectives are operating effectively. While we appreciate SAFECOM must consider and assess its specific assurance needs, the absence of an internal audit function is not demonstrative of sound corporate governance.

Legal compliance

SAFECOM does not have a formal legislative compliance framework or program to assist in monitoring the sector's compliance with its legal and regulatory obligations. An effective legal compliance framework includes identifying relevant legislative and regulatory requirements, assigning responsibility for compliance, review processes to ensure legislative and regulatory requirements are complied with, and mechanisms for dealing with non-compliance. This should include periodic reporting to senior management and SAFECOM.

SAFECOM responded to these observations by noting that it has extremely limited resources and made a decision to redirect resources from compliance activities to IT, which required work to address the emerging risk of cyber security. Following progress in this area and because of the issues we raised, SAFECOM will seek to reinstate an internal audit position in 2019.

SAFECOM also advised that it would re-establish a formal legislative compliance framework to help monitor the sector's compliance with its legal and regulatory obligations.

Payroll

Employee benefits expenses totalled $225 million and the employee liabilities and related on-costs at 30 June 2018 were $61 million.

Bona fide and leave return reports not reviewed or incomplete

SAFECOM's bona fide certificates and leave returns procedure requires each payment delegate to review and certify fortnightly bona fide and leave return reports. Certification of these reports provides SAFECOM with assurance that:

- only valid employees are paid
- employees are paid in line with the terms of their employment
- all leave taken is recorded in the payroll system and therefore deducted from the employee's leave balance.

We noted that SAFECOM's bona fide certificates and leave returns procedure does not specify the time frame within which the review must be completed.

Our review of a sample of eight bona fide reports identified seven instances where the reports were not reviewed, or not reviewed within one month (a time frame that is consistent with other public sector agencies). In particular, we noted the following:

- Two of the four SAFECOM bona fide reports tested were not reviewed because the pay point manager was unable to access the report in the CHRIS payroll system. One bona fide report tested was not signed or dated as reviewed, and another was not reviewed until nine months after the end of the pay period.
- Of the four SACFS bona fide reports tested, one was not signed or dated as reviewed and another two were not reviewed within one month.

Our review of a sample of 10 leave return reports identified seven instances where the reports were not reviewed or not reviewed within one month. In particular, we noted the following:

- Two of the three SAFECOM leave return reports we tested were reviewed at the time of our request, many months after the pay run date. One of the leave return reports was not reviewed because the pay point manager was unable to access the return in CHRIS.
- Two of the three SACFS leave return reports we tested were not reviewed.
- Two of the four SASES leave return reports we tested were not reviewed. We note that employee was on leave, but did not review the reports on their return.

We also noted that while the SASES had implemented a register to monitor the review of bona fide and leave return reports, SAFECOM and the SACFS had not.

SAFECOM responded that a new automated bona fide and leave return report solution will be implemented across the emergency services sector in 2018-19. This new automated process will enable delegates to view and approve reports within the payroll system and result in a more efficient process. It is anticipated that the introduction of a paperless control will improve compliance with SAFECOM procedures for the review and certification of bona fide and leave return reports.

In the interim, SAFECOM will ensure that managers receive regular emails to remind them to complete the review of bona fide certificates and leave return reports in line with the its procedure.

The bona fide certificates and leave returns procedure is being updated to insert the recommended time frame of one month for completing reviews. It is anticipated that the updated procedure will be completed by end of August 2018.

No control to ensure validity of Shared Services SA (SSSA) processing for SAMFS

Last year we noted that the SAMFS had not implemented a control designed to ensure that only valid employees were paid in line with the terms of their employment. Promotions, position reclassifications, terminations, overtime, allowances and penalties are manually processed by SSSA. While SSSA maintains controls to ensure the completeness and accuracy of payroll processing, it does not check the validity of information provided to it.

The SAMFS responded that it would use the GARTAN time management system to check the validity of SSSA processing

Follow up this year found that the SAMFS was unable to use the GARTAN system as intended, meaning that it has yet to implement a check of the validity of SSSA processing for operational staff (97% of staff).

We also noted that a planned review of bona fide certificates for public sector employees has not started.

The SAMFS responded that, in partnership with SSSA, is has engaged a consultant to review the end to end payroll processes. This review will identify opportunities for improvements in HR/payroll processes between both the SAMFS and SSSA, which may provide assistance in this area.

The SAMFS also advised that at the time of our testing, it had started using the bona fide and leave return process for salaried employees in line with the approved SAFECOM procedure. Training was being arranged for managers to familiarise themselves with the process and procedure.

Inadequate review of manual payments

For the year to 31 March 2018, SSSA had processed $4.5 million in manual payments on behalf of SAFECOM and the ESOs.

To ensure the validity and approval of all manual payments processed, each month SSSA provides SAFECOM a report for its review. It details all manual payments processed by SSSA during the month.

SAFECOM and the ESOs can request SSSA to process manual payments on their behalf. Manual payments mainly comprise the payment of foreign currency invoices associated with the purchase of non-current assets, urgent/manual payments for reimbursement of travel and training expenses incurred by volunteers, and replenishing petty cash to stations. Manual payments are not subject to the same validation checks that apply to payments processed and approved through the Basware payment processing system.

We noted that SAFECOM does not have a documented procedure on how to check manual payments in the manual payments report. SAFECOM staff advised that transactions are reviewed on a sample basis according to value for each category. We noted that for the March 2018 review:

- only $28 000 of a total of $557 000 in foreign currency transactions were reviewed
- no review of the 10 most financially significant payments was performed.

We recommended that SAFECOM limit the use of manual payments to foreign currency transactions and other genuinely urgent circumstances, and ensure that either:

- all manual payments are checked for validity, or
- a procedure is developed to support a risk-based review of a sample of manual payments.

SAFECOM responded that the testing performed on the March 2018 report was not appropriately documented. A project is currently underway to streamline finance processes for volunteers with SAFECOM aiming to reduce the volume of manual payments.

Shared Services SA – financial systems and transaction processing environments

SSSA processes financial transactions on behalf of SAFECOM under service level determinations. The main systems and control environments include accounts payable, payroll and general ledger financial functions.

Our review and evaluation of controls for these systems concluded that controls were effective for 2017-18.

SSSA is discussed further in the commentary under 'Department of the Premier and Cabinet' in this Report.

Interpretation and analysis of the financial report

Highlights of the financial report – consolidated emergency services sector*

	2018 $'million	2017 $'million
Expenses		
Employee benefits expenses	225	155
Supplies and services	83	74
Depreciation and amortisation	22	21
Other expenses	5	3
Total expenses	334	252
Total income	14	15
Net cost of providing services	319	237
Revenues from SA Government	254	247
Net result and total comprehensive result	(66)	10
Net cash provided by (used in) operating activities	23	32
Net cash provided by (used in) investing activities	(29)	(26)

	2018 $'million	2017 $'million
Assets		
Current assets	32	37
Non-current assets	360	354
Total assets	393	391
Liabilities		
Current liabilities	53	42
Non-current liabilities	99	42
Total liabilities	152	84
Total equity	241	307

* Table may not add due to rounding.

Statement of Comprehensive Income

Expenses

Total expenses increased by $82 million to $334 million mainly as a result of a $70 million increase in employee expenses and a $9 million increase in supplies and services.

Employee benefits expenses

Expenses largely comprised employee benefits expenses of $225 million ($155 million), which represent 67% of total expenses. In 2017-18, employee benefits expenses increased by $70 million due mainly to the following:

- Workers compensation expense increased by $41 million. Workers compensation expenses are impacted by movements in the workers compensation provision (liability), which in 2018 increased by $38 million. The increase in the provision for 2018 was impacted by a significant increase in the number of long-term claims under firefighter presumptive cancer compensation arrangements and increases in incurred but not reported claims (see comments under 'Statement of Financial Position' below).
- A new additional compensation provision valued at $18 million was introduced. It provides additional injury and income protection for injured workers with non-serious injuries incurred after 1 July 2015 who have exhausted their entitlements under the *Return to Work Act 2014*. These provisions have been included in public sector enterprise agreements and the Firefighting Industry Employees Award (see comments under 'Statement of Financial Position' below).
- Salaries and wages increased by $7 million following enterprise agreement salary increases and the employment of an additional 45 FTEs across the sector. See commentary under 'Further commentary on operations' for an explanation of this increase in FTEs.

The number of employees whose normal remuneration is equal to or greater than the base executive remuneration level requiring disclosure this year was 134 (98). The aggregate remuneration paid or payable for those employees was $22.4 million ($16.9 million). The change largely reflects an additional 34 SAMFS officers now included in the disclosure.

Supplies and services

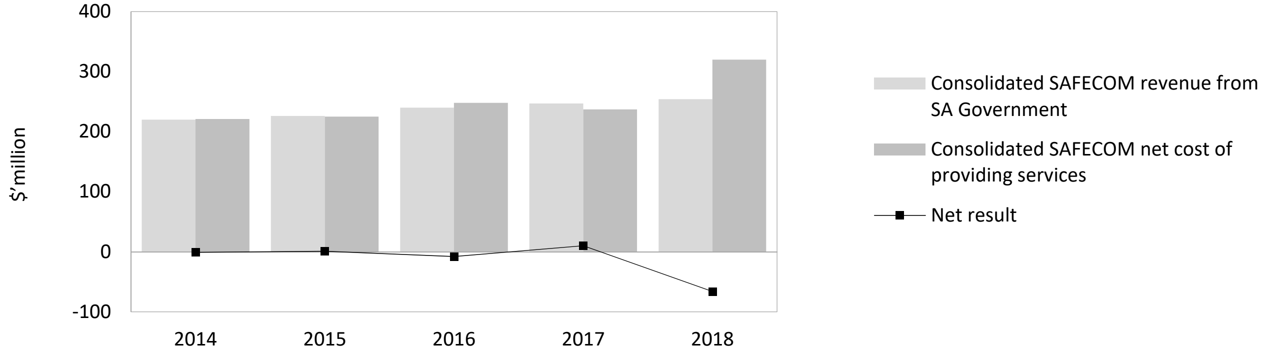
Supplies and services expenses increased by $9 million to $83 million mainly due to a:

- $2.8 million increase in aerial firefighting costs associated with an increased number of incidents
- $2.3 million increase in personal protective clothing for SACFS volunteers
- $1.6 million increase in repairs and maintenance of firefighting vehicles
- $1.3 million increase in the SA Government Radio Network costs due to increased electricity costs.

Revenue

The main source of revenue for the consolidated sector is contributions from the Fund of $251 million ($245 million), which account for 94% of total income.

The following chart shows the funding received by the consolidated sector from the SA Government (including the Fund), the net cost of providing services and the net result for the past five years. It illustrates that revenue from the SA Government has largely been sufficient to meet the net cost of providing services. The $66 million shortfall in 2018 is due mainly to the increase in the workers compensation provision and the introduction of the new additional compensation provision, both of which have a non-cash impact on the net result.



Statement of Financial Position

At 30 June 2018 current liabilities of $53 million exceeded current assets of $32 million. While a deficiency in working capital can be of concern, the consolidated sector is funded principally from the Fund. The sector works with the Fund to determine cash flows associated with its government approved program of work to ensure funding meets the expected cash flows. The consolidated sector receives its funding monthly, which significantly reduces the risk.

Assets

Property, plant and equipment assets of $360 million represent 92% of total assets. The main asset classes held are land ($65 million), buildings ($113 million) and vehicles ($129 million).

Property, plant and equipment increased by $7 million during the year due mainly to acquisitions of $30 million for fire and rescue vehicles, Adelaide SAMFS station upgrade and Loxton SASES unit upgrade, all partially offset by depreciation expense for the year of $21 million.

Liabilities

Total liabilities increased by $68 million to $152 million.

This large increase in liabilities is attributable to the $38 million increase in the provision for workers compensation and the introduction of a new additional compensation provision of $18 million. There was also an increase of $6 million in employee benefits liabilities and related on-costs due to employee agreement salary increases and an additional 45 employees entitled to leave. In 2018, the SAMFS identified an error in the proportion of long service leave liability taken as leave percentage for 30 June 2017. The subsequent correction of this error in 2018 explains the $2 million increase in employment on-costs.

Provision for workers compensation

Workers compensation liability increased by $38 million to $57 million. The workers compensation provision is based on an actuarial assessment of the outstanding liability as at 30 June 2018 provided by a consulting actuary engaged through the Office for the Public Sector. The increase in the workers compensation liability in 2018 was impacted by an increase in the:

- number of known seriously injured firefighter cancer claims
- allowance for incurred but not yet reported firefighter cancer claims estimated by the actuary.

The increase in the estimate for seriously injured firefighter cancer claims was driven by the identification of 27 new claims in 2017-18. The presumptive workers compensation coverage for firefighters had only identified a total of 27 in the previous four years. The actuary increased the allowance of incurred but not yet reported firefighter cancer claims estimated from 10 to 70 in the current year.

There is a significant degree of uncertainty associated with estimating future claim and expense payments. The liability is impacted by agency claim experience, average claim sizes and other economic and actuarial assumptions.

Provision for additional compensation

Following changes to relevant public sector enterprise agreements, the sector has recognised a new $18 million additional compensation provision as at 30 June 2018.

Under the additional compensation provision, eligible employees who are injured in circumstances detailed in the public sector enterprise agreements and the SAMFS Firefighting Industry Employees Award will be provided with the financial support and/or medical expenses detailed in the award, where the following applies:

- they have not been assessed as having a 30% or more Whole Person Impairment
- they have not made a return to work within the meaning of the *Return to Work Act 2014*
- they are temporarily or permanently incapacitated for work and have exhausted their entitlements under the *Return to Work Act 2014*.

The additional compensation provision is based on an actuarial assessment of the outstanding liability as at 30 June 2018 provided by a consulting actuary engaged by the Office for the Public Sector. The liability is comprised of an estimate for known claims and an estimate of incurred but not reported applications.

Significant uncertainty with the estimated additional compensation provision

There is a significant degree of uncertainty associated with this estimate. In addition to the general uncertainties associated with estimating future claim and expense payments, the additional compensation provision is impacted by the absence of claims history and the evolving nature of the interpretation of, and evidence required to meet, eligibility criteria.

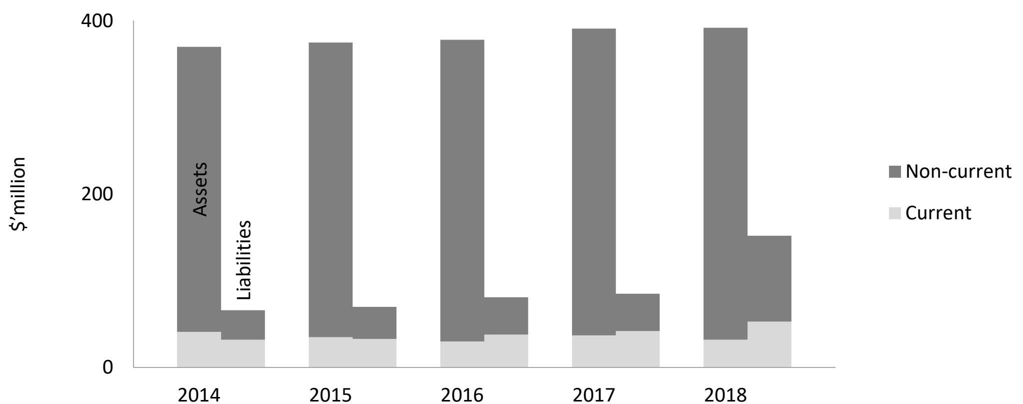
Given these uncertainties, the actual cost of additional compensation claims may differ materially from the estimate.

SACFS leave dispute

In 2016-17 the SACFS was in negotiation with the Public Service Association to resolve a dispute with a small number of SACFS employees resulting from over-accruing leave entitlements. The value of leave accrued in excess of entitlement was $638 000.

In March 2018, the Chief Officer received legal advice that the excess leave accrued did not constitute a debt under Treasurer's Instruction 5 'Debt Recovery and Write Offs'. The Chief Officer used his authority to take no further action and employee leave balances will remain unaffected.

For the five years to 2018, a structural analysis of assets and liabilities is shown in the following chart, which demonstrates the impact of the workers compensation and additional compensation provisions on total liabilities in 2018.



Statement of Cash Flows

Net cash provided by operating activities decreased by $9 million in 2018 due mainly to increased employee benefits expenses and supplies and services, offset by additional contributions from the Fund of $6 million. Investing cash outflow increased by $3 million to $29 million following an increase in cash payments for the acquisition of property, plant and equipment across the sector.

The following table summarises the consolidated sector's net cash flows for the five years to 2018.*

	2014 $'million	2015 $'million	2016 $'million	2017 $'million	2018 $'million
Net cash flows					
Operating	22	24	26	32	23
Investing	(22)	(31)	(29)	(26)	(29)
Change in cash	-	(7)	(2)	6	(6)
Cash at 30 June	32	25	23	29	23

* Table may not add due to rounding.

Highlights of the financial report – SAFECOM*

	2018 $'million	2017 $'million
Expenses		
Employee benefits expenses	8	7
Supplies and services	7	5
Other expenses	5	3
Total expenses	20	16
Total income	3	3
Net cost of providing services	17	13
Revenues from SA Government	15	15
Net result and total comprehensive result	(2)	2
Net cash provided by (used in) operating activities	2	1
Assets		
Current assets	7	7
Non-current assets	2	2
Total assets	9	9
Liabilities		
Current liabilities	4	2
Non-current liabilities	3	2
Total liabilities	6	4
Total equity	2	4

* Table may not add due to rounding.

Statement of Comprehensive Income

Revenues from SA Government

The main source of funds for SAFECOM is revenue from the SA Government of $15 million, which accounts for 83% of revenues.

Expenses

Employee benefits expenses are SAFECOM's main expense category and totalled $8 million ($7 million), which is 41% of total expenses.

Supplies and services totalled $7 million ($5 million). The increase is due mainly to increased costs associated with a new training and administrative system for volunteers, and the development of a business case for a new AlertSA website and mobile App.

Highlights of the financial report – administered items*

	2018 $'million	2017 $'million
Expenses		
Contributions to SA Government administrative units	279	272
Grants and subsidies	6	4
Other expenses	8	8
Total expenses	293	283
Income		
Revenues from levy sources	300	293
Other revenues	2	2
Total income	301	295
Net result and total comprehensive result	9	12
Net cash provided by (used in) operating activities	8	(12)
Assets		
Current assets	32	24
Total assets	32	24
Liabilities		
Current liabilities	1	1
Total liabilities	1	1
Total equity	32	23

* Table may not add due to rounding.

Community Emergency Services Fund

Contributions, by way of levies, are made by all land owners (including State and Local Governments) for fixed and mobile property to fund the provision of emergency services. Levies are collected in line with the *Emergency Services Funding Act 1998*. The levies are set to cover the budgeted emergency services expenditure for the coming financial year.

The levy on fixed properties is collected by RevenueSA and applies to capital values adjusted for location and land use. The levy on mobile properties is collected by the Department of Planning, Transport and Infrastructure using the vehicle registration system. Once collected, these levies are paid into the Fund.

In addition, the SA Government has made direct contributions to the Fund in the form of remissions of levies (both fixed and mobile property) and concession subsidy payments through the Department of Human Services for eligible people.

The costs of collecting levies and expenses relating to administration are also met from the Fund.

Statement of Administered Comprehensive Income

For the year ended 30 June 2018 the Fund's net result was a surplus of $9 million ($12 million).

This surplus reflects $8 million in levy collections for 2017-18 not used for budgeted SACFS presumptive workers compensation.

Administered revenue

Levies and other revenues are collected in line with the *Emergency Services Funding Act 1998* to fund the budget of SA Government administrative units, grants and subsidies to various bodies and other payments approved by the Minister for providing emergency services. Emergency services levies increased by $6 million to $300 million.

The increase in levy revenue and changes in remissions are shown in the table below.

	2014 $'million	2015 $'million	2016 $'million	2017 $'million	2018 $'million
Fixed property collections	101	191	199	216	221
Fixed property remissions*	96	20	26	25	25
Mobile collections	33	41	43	43	44
Mobile remissions*	12	4	3	3	3
Government concessions	7	7	7	6	6
	249	263	278	294	300

* Remissions are provided by the SA Government.

The increase in fixed property collections reflects an increase in the budget to reflect growth in the base expenditure and additional funding for new initiatives, including SASES and SAMFS call response systems, new protective clothing for SAMFS firefighters and delivery of training to volunteer marine rescue members and SASES volunteers.

In the 2014-15 State Budget, the SA Government removed general remissions for all property owners except eligible concession recipients. All non-concessional property owners were required to pay their full levy from 1 July 2014. This had the following impact:

- remissions paid by the SA Government decreased by $84 million
- fixed property collections paid by property owners increased by $90 million
- mobile collections paid by property owners increased by $8 million.

In the 2018-19 State Budget the SA Government announced the reintroduction of general remissions for fixed property collections and its commitment to funding the anticipated $90 million funding shortfall.

Administered expenses

The following table shows the contributions made by the Fund to SA Government administrative units over the past five years.

	2014 $'million	2015 $'million	2016 $'million	*2017 $'million	*2018 $'million
SAMFS	121	124	136	137	139
SACFS	68	74	74	76	77
South Australia Police	20	21	21	21	22
SASES	15	15	16	20	20
SAFECOM	10	11	11	12	15
Other SA Government entities	4	5	6	6	6
	238	250	264	272	279

* Refer note A3 of SAFECOM's financial report for the year ended 30 June 2018.

Over the period contributions paid have increased by $41 million, with most of the increase being received by the SAMFS ($18 million) and the SACFS ($9 million).

In 2018, contributions to SA Government administrative units increased by $7 million to $279 million, representing a 2.5% increase.

Grants and subsidies of $6 million were paid to Surf Life Saving South Australia, Volunteer Marine Rescue and Shark Beach Patrol. An increase in funding to Surf Life Saving South Australia was as a result of the redevelopment of the Chiton Rocks Surf Life Saving Club.

Other expenses of $7 million were paid to RevenueSA for collection costs under the *Emergency Services Funding Act 1998* for administering the collection of fixed property levies. The Department of Planning, Transport and Infrastructure was paid $1 million in collection costs for collecting the mobile property levies.

Statement of Administered Financial Position

Net assets for the Fund at 30 June 2018 were $32 million ($23 million).

At 30 June 2018, current assets totalled $32 million ($24 million), predominately comprising cash and cash equivalents. The increase in cash and cash equivalents of $8 million relates to reduced expenditure related to unrequired workers compensation in the SACFS.

Further commentary on operations

Staffing

SAFECOM and the ESOs employed the following active FTEs as at 30 June for the past two years.

	*2017 FTEs	*2018 FTEs
SAFECOM	64	65
SAMFS	965	995
SACFS	150	153
SASES	59	70
Total	1 238	1 283

* FTE data was supplied by SAFECOM and is unaudited.

The increase in SAMFS FTEs related to the Firefighters Enterprise Agreement 2017, which provided for an additional 22 FTEs in 2017-18 and 32 FTEs in 2018-19. Due to the time frames required to recruit and train firefighters, the SAMFS's strategy is to recruit more than required in the agreement to accommodate attrition and the new additional FTEs.

The increase in SASES FTEs relates mainly to additional funding received for the following initiatives:

- marine compliance
- emergency responses and rescue improvements
- implementation of the Burns review recommendations.

Volunteers

The SACFS and SASES had the following active volunteers as at 30 June for the past two years.

	*2017 FTEs	*2018 FTEs
SACFS	13 550	13 275
SASES	1 501	1 549
Total	15 051	14 824

* Volunteer data was supplied by SAFECOM and is unaudited.

South Australian Government Financing Authority (SAFA)

Financial statistics	Profit before income tax equivalents:	$113 million
	Total loans on issue:	$20.9 billion
	Total bonds, notes and debentures on issue:	$17.8 billion
	Outstanding insurance claims:	$390 million
	Fleet vehicles (including held for sale):	$170 million
	Number of fleet vehicles (including held for sale):	7276

Significant events and transactions

- The $50 million SA Venture Capital Fund commenced on 1 July 2017, with the fund being managed by Blue Sky Venture Capital.
- SAFA received funding of $146.4 million to pay for claims under the National Redress Scheme for those who have experienced institutional child sexual abuse.
- Payments totalling $35.5 million had been advanced under the school loans scheme as at 30 June 2018. Total amounts approved to that date were $80 million.

Financial report opinion — **Unmodified**

Financial controls opinion — **Unmodified**

Functional responsibility

SAFA, a body corporate, was established under the *Government Financing Authority Act 1982* (SAFA Act).

SAFA is the central borrowing authority for the State of South Australia, and is responsible for managing most of the State's debt and for implementing the SA Government's debt management policy as determined by the Treasurer.

Under section 15 of the SAFA Act, SAFA's liabilities are guaranteed by the Treasurer.

SAFA also administers the SA Government's:

- insurance and risk management arrangements through its insurance division, trading as SAicorp
- passenger and light commercial vehicle fleet operations through Fleet SA.

Scope of the audit

The audit program covered the major financial systems to obtain sufficient evidence to form an opinion on the financial report and internal controls.

Specific areas of audit attention in 2017-18 included:

- cash
- financing
- treasury
- general ledger.

Internal audit activities were reviewed to assess the risks of material misstatement in the financial report and to design and perform audit procedures. We considered the work performed by SAFA's compliance unit and internal audit function for elements of our program, in particular:

- quarterly reporting by SAFA's compliance unit
- internal audit's review of interest rate and foreign exchange risk management.

Audit findings and comments

Communication of audit matters

A small number of low risk matters identified by the audit were communicated to the General Manager with a satisfactory response received.

Interpretation and analysis of the financial report

Highlights of the financial report

	2018 $'million	2017 $'million
Interest revenue	1 036	957
Interest expense	(1 034)	(969)
Net interest revenue	2	(12)

	2018 $'million	2017 $'million
Net gain (loss) on financial instruments and derivatives	88	109
Leasing and hire revenue	57	58
Insurance premium revenue	55	52
Recoveries	22	20
Other income (including net gain on sale of property, plant and equipment)	12	9
Vehicle operating costs (including depreciation and impairment)	(66)	(66)
Insurance claims	(35)	(55)
Other expenses	(22)	(23)
Profit before income tax equivalents	113	92
Income tax equivalent expense	(34)	(28)
Profit after income tax equivalents and total comprehensive result	79	64
Assets		
Cash, short-term assets and investments	6 883	6 442
Loans	20 906	20 665
Derivatives receivable	199	125
Property, plant and equipment (including held for sale)	170	166
Other assets	56	53
Total assets	28 214	27 451
Liabilities		
Deposits and short-term borrowings	9 241	8 681
Bonds, notes and debentures	17 782	17 913
Outstanding claims	390	383
Derivatives payable	166	51
Payables and other liabilities	215	55
Total liabilities	27 794	27 083
Total equity	420	368

Statement of Comprehensive Income

Interest revenue and expense

Interest revenue and expense are recognised on a market value accounting basis and accrued in line with the terms and conditions of the underlying financial instruments. Both have increased slightly compared to the prior year.

The slight increase in interest revenue and expense reverses a trend that saw both decrease proportionately in recent years as a result of the downward trend in market interest rates. Interest revenue and expense are also impacted by the timing of maturities and settlements for financial instruments, including derivatives.

Net gain on financial instruments and derivatives

SAFA's 2017-18 operating result includes a net gain of $88 million on financial instruments and derivatives. This gain represents the profit to SAFA from movements in the prices of financial instruments and derivatives it held mostly as a result of changes in market rates.

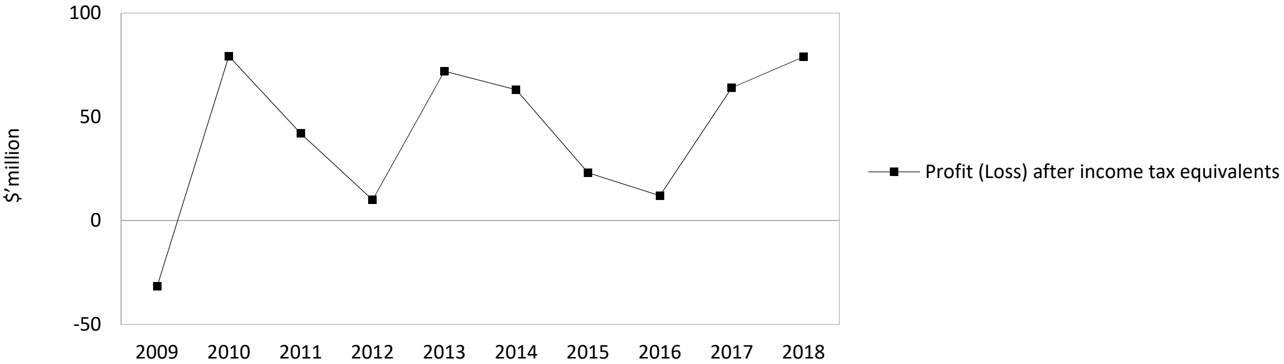
Leasing and hire revenue and recoveries

Leasing and hire revenue reflects the fees charged to other government agencies for leasing fleet vehicles, whereas recoveries include the recovery of fuel costs and unscheduled maintenance charges for the fleet vehicles.

Profit (Loss)

SAFA's profit before income tax equivalents was $113 million. Under Treasurer's Instruction 22 'Tax Equivalent Payments' SAFA is required to pay the Treasurer an income tax equivalent. The income tax liability is calculated by applying a tax rate of 30% to profit or loss before tax.

The 10-year trend in SAFA's profit or loss after income tax equivalent expense is illustrated in the following chart.



The chart highlights the volatility in SAFA's results, which comes from the financial performance of SAFA's insurance activities.

The 2018 profit after income tax equivalents of $79 million is primarily attributable to profit on SAFA's insurance activities of $55 million and treasury activities of $15 million.

Insurance activity impact on profit (loss)

SAFA's insurance activities are designated into three funds (Fund 1, Fund 2 and Fund 3). SAFA's result after income tax equivalents is, in net terms, only affected by Fund 1 results, as SAFA is indemnified by the Treasurer against any operating profit or loss arising from the activities of Funds 2 and 3.

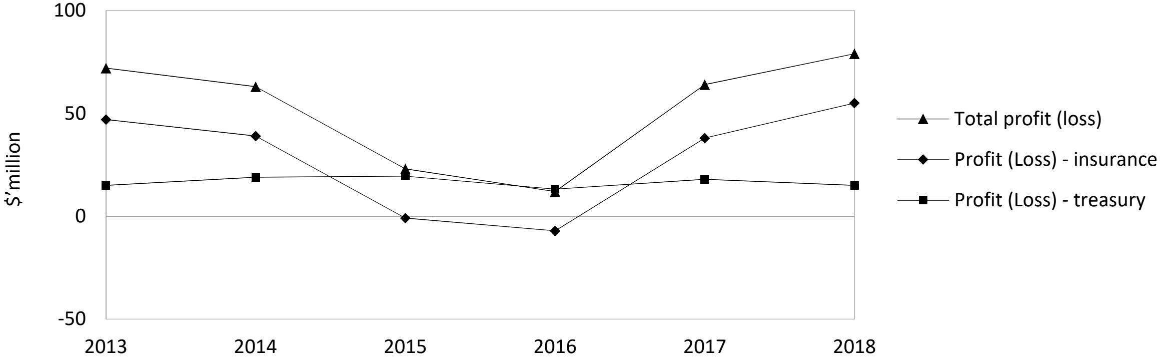
Fund 2 is used to fund liabilities arising from insurable incidents that:

- occurred before 1 July 1994
- involve claims under the building warranty indemnity reinsurance arrangements up to 30 June 2013
- involve the former State Government Insurance Commission residual claims and workers compensation claims previously managed by the former South Australian Asset Management Corporation
- some historical workers compensation and asbestos claims previously managed by other SA Government entities.

Fund 3 is used to fund liabilities arising from claims under the building indemnity insurance scheme effective from 1 July 2013.

All of SAFA's remaining insurance activities are funded through Fund 1.

The impact of SAFA's insurance activities on its profit or loss after income tax equivalent expense is highlighted in the following chart.



SAFA's insurance activities reported a 2017-18 profit after tax of $55 million (profit of $38 million). The increase in the insurance profit was mainly a result of a $19.5 million reduction in claim expenses. This reduction was mainly due to $18 million less being paid for claims in 2017-18. Other major factors impacting the valuation of the outstanding claims liability were:

- the closure of two large claims with no payments ($16 million reduction)
- fewer new claims over the year (ie no major weather events)
- favourable settlements from older years resulting in substantial releases from outstanding claims liabilities.

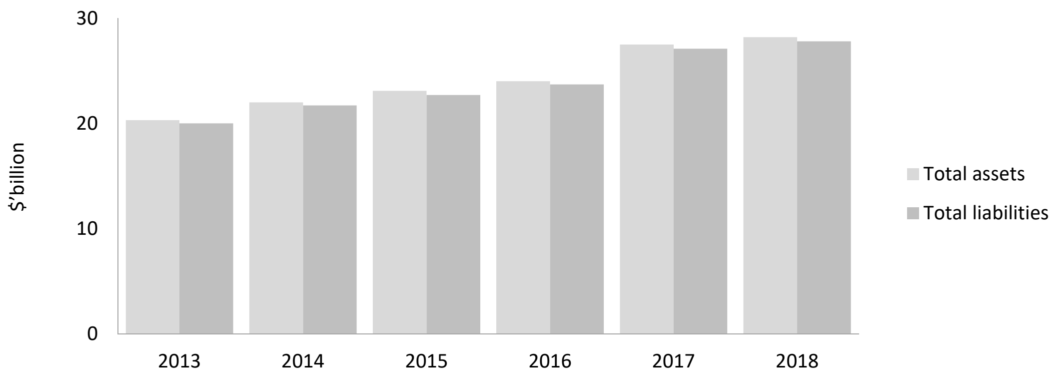
These changes highlight the inherent volatility of insurance activities, and the impact on SAFA's financial performance.

Additional insurance activity in future years is anticipated for the National Redress Scheme for those who have experienced institutional child sexual abuse. SAFA received funding of $146.4 million in June 2018 that is intended to fund compensation under the National Redress Scheme in South Australia. It is anticipated the Scheme will become operational in the next 12 months following the finalisation of State and Commonwealth legislation. It is also anticipated that this activity will be undertaken through a fourth SAFA insurance fund (Fund 4) once the legislation is finalised.

Statement of Financial Position

Assets and liabilities

A structural analysis of assets and liabilities for the six years to 2018 is shown in the following chart.



The chart illustrates the gradual increase in SAFA’s assets between 2013 and 2016. Over the same period SAFA’s total liabilities increased by a corresponding amount, reflecting its activities in financial markets to fund the accumulated deficits and loans to public authorities.

The vast majority of SAFA’s financial assets used for treasury operations relate to financial liabilities financed by market borrowings. The remaining balance of financial assets is funded from SAFA’s equity ($420 million as at 30 June 2018).

In 2017, there was a significant spike in SAFA’s total assets and liabilities. This is mainly due to increases in investment assets ($2.9 billion) and bonds, notes and debentures liabilities ($2.8 billion). These increases are primarily attributable to changes in SAFA’s liquidity policy. SAFA sought to increase its liquidity to ensure greater alignment with market best practice and regulator and rating agencies’ guidelines. To increase the amount of liquid funds available, new select line bonds were issued, with the proceeds placed in investments.

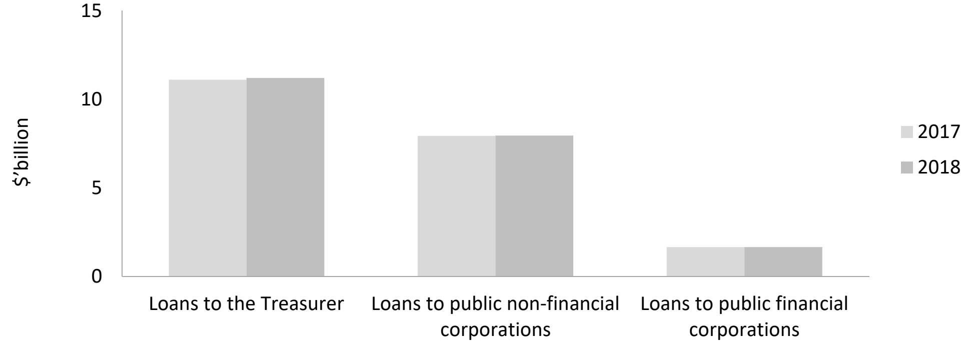
In 2018 there was a gradual increase in SAFA’s borrowings, with assets increasing by a corresponding amount.

Loans to government agencies

Total assets include loans of $20.9 billion, comprising SAFA’s loans to the Treasurer to fund accumulated Consolidated Account deficits and loans to other public authorities.

At 30 June 2018 SAFA’s loans to the Treasurer totalled $11.2 billion, an increase of $174 million since 30 June 2017. The Treasurer also has funds on deposit with SAFA totalling $7 billion ($6.5 billion) as at 30 June 2018.

The chart below highlights SAFA’s current and prior year government sector loan composition.



There was a small current year increase in loans to the Treasurer, while loans to public non-financial and financial corporations remained steady. The increase in loans to the Treasurer was primarily to fund the deficit in the Consolidated Account for 2017-18 ($119 million).

The main loans to public non-financial corporations were to the South Australian Water Corporation (SA Water), the Urban Renewal Authority and the Adelaide Venue Management Corporation.

Capital and distributions

At 30 June 2018 SAFA’s capital reserves were represented solely by its retained earnings, which stood at $420 million ($368 million). A $26 million ($23 million) dividend distribution was made to the Treasurer in 2017-18.

This dividend payment was made under section 12(2) of the SAFA Act, which states that any surplus of funds remaining after SAFA's costs have been met in any financial year must be paid into the general revenue of the State or otherwise dealt with as the Treasurer determines. The Treasurer approved SAFA's dividend payment in June 2018.

Statement of Cash Flows

SAFA's cash position fluctuates in line with the net effects of its various operating, investing and financing activities. Cash balances have been maintained in line with liquidity requirements.

Further commentary on operations

SAFA Advisory Board

The SAFA Act provides that SAFA is 'constituted of the Under Treasurer' and establishes the South Australian Government Financing Authority Advisory Board (the Advisory Board). The Advisory Board comprises up to seven members, one of whom is the Under Treasurer who is also Presiding Member.

The SAFA Act provides that the Under Treasurer may request advice from the Advisory Board and consider any advice given. The Advisory Board may provide advice, as it sees fit, to the Treasurer or SAFA. SAFA's annual report must include details of any advice from the Advisory Board that the Treasurer or SAFA has decided not to follow and the reason for that decision.

Business risk management

Operational risk management

SAFA has a number of mechanisms to manage operational risks, including:

- an annual risk assessment facilitated by the contracted internal auditors addressing changes to SAFA's operating environment and the financial markets it transacts with. This assessment is used to determine the scope of the internal audit program
- a policy manual that details parameters within which SAFA pursues its core objectives, including dealings with financial markets, reporting requirements and managing assets and liabilities. This manual is reviewed annually and subject to the Treasurer's approval
- a central procedures manual that provides a high level summary of the actions that SAFA expects to be maintained within the treasury, insurance, fleet and operational support units. The procedures manual is also subject to annual review
- the compliance unit performing daily, weekly, monthly and quarterly reviews to ensure compliance with policy requirements. The compliance unit's work is reviewed and tested by SAFA's contracted internal auditor
- a Risk and Performance Committee comprising two independent members appointed by the Under Treasurer at 30 June 2018 (a third is intended to be appointed in early 2018-19).

SAFA's treasury portfolio structure

To help manage SAFA's treasury function and its associated risks, its balance sheet is separated into distinct portfolios. The portfolio structure and related procedures contribute to transparency of operations, risk identification and management and performance measurement and reporting. SAFA's portfolio structure consists of:

- SAFA's principal portfolios
- the Treasurer's cost of funds portfolio
- client asset/liability management portfolios.

SAFA's principal portfolios

SAFA maintains the following principal portfolios:

- funding
- liquidity
- foreign exchange hedging service.

The funding portfolio contains all of SAFA's term loans to clients, around $9.7 billion in assets. Its major function is to provide funding to clients on a defined maturity and rate basis.

The liquidity portfolio contains:

- all of SAFA's liquid assets and the funding that supports them
- deposits of excess cash from clients
- transactions relating to the cash loan to the Treasurer
- the Treasurer's deposit with SAFA.

The liquidity portfolio holds liabilities and assets and hedging instruments (including derivatives). It is run on a basis where mismatches between assets and liabilities are managed within risk parameters, with assets of $13.1 billion at 30 June 2018. These parameters are managed on a daily basis within the guidelines stipulated in the policy manual.

The foreign exchange hedging service portfolio covers all transactions associated with the service SAFA provides to public sector clients relating to the hedging of foreign currency exposures, mainly associated with purchases and sales of goods and services. The portfolio had a net asset position of $10 242 at 30 June 2018.

Any profits or losses from the operations of the principal portfolios are recorded in SAFA's Statement of Comprehensive Income.

Treasurer's cost of funds portfolio

The Treasurer's cost of funds portfolio is the primary portfolio for the Treasurer. It contains liabilities and assets managed against a benchmark range. The main management task for this portfolio is to minimise interest rate risk within the portfolio relative to the policy benchmark range set by the Treasurer. The net expenses of this portfolio are borne by the Treasurer.

There are transactions in the Treasurer's cost of funds portfolio that are not measured and reported against the benchmark range, such as new Royal Adelaide Hospital transactions. The interest rate exposure on the new Royal Adelaide Hospital transactions is managed by fixing the interest rate for a defined term.

Client asset/liability management portfolios

The client asset/liability management portfolios do not reside on SAFA's Statement of Financial Position and only impact on SAFA's profit and loss through fee income received. This includes SA Water's Financial Bureau Services Agreement.

SA Water manages its own debt. SAFA's role is to develop and document, in conjunction with SA Water and within strict policy guidelines, a risk management strategy for SA Water's exposures. The strategy must have regard to the likely impact of interest rate exposures on SA Water's results, an assessment of SA Water's ability to carry interest rate risk and SA Water's regulatory framework.

The Treasurer also makes loans directly to government entities and other bodies, including loans by the Treasurer to government departments and statutory authorities. SAFA administers these loans on behalf of the Treasurer. In 2017-18 this included administering the Future Jobs Fund and Economic Investment Fund which were established as a result of the 2016-17 State Budget. The activities of these Funds are recognised in the Treasurer's statements and are listed as loans to the Treasurer in SAFA's financial statements.

General market risk management

SAFA is the State's central borrowing authority and manages most of the State's debt. It lends funds raised from financial markets to a number of South Australian public sector clients, including the Treasurer who borrows on behalf of public sector agencies to support their operational requirements.

SAFA's Risk Appetite Statement indicates it performs its treasury, insurance and fleet functions with a low risk appetite, protects the interests of its owners and clients and protects its reputation as a provider of services consistent with its strategic direction.

A low risk appetite approach means some exposure to identified risk is tolerated that is within well defined, approved parameters consistent with the organisation's strategic direction and business objectives.

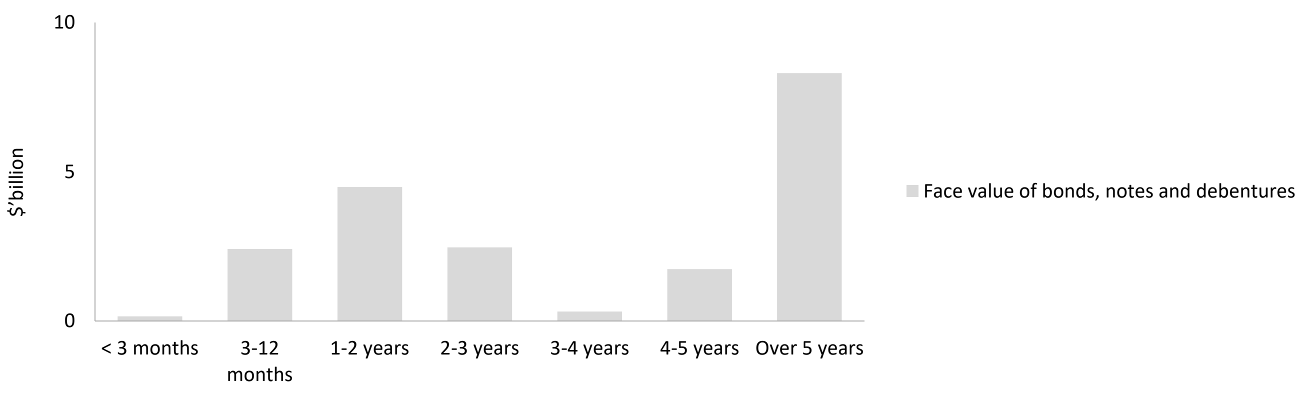
Funding risk management

SAFA raises funds from domestic and international financial markets to support the SA Government's budgetary funding requirements.

Funding risk refers to the prospect of SAFA either being unable to raise funds when required, or only being able to raise funds at a higher cost. Accordingly, SAFA's objective for funding risk is to ensure that it is not exposed to a significant refinancing or funding risk within any financial year. Guidelines for funding risk are set by the Under Treasurer.

A maturity profile of the undiscounted principal and interest repayment amounts for SAFA's bonds, notes and debentures as at 30 June 2018 is presented in the following chart. Bonds, notes and

debentures include SAFA's core funding issue of select lines and floating rate notes.



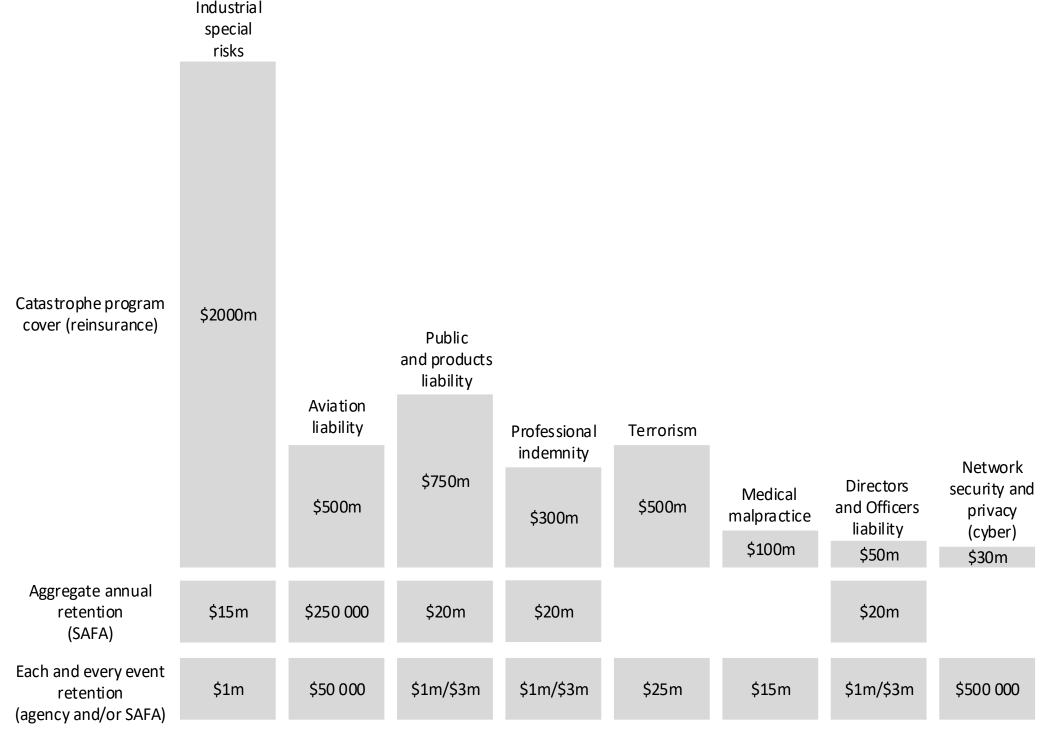
The chart illustrates that SAFA's principal and interest repayments vary each year for the next four years. From 2024, SAFA will have $8.3 billion of principal and interest repayments.

The chart does not include expectations for the SA Government's early refinancing or future financing requirements.

Catastrophe reinsurance program

The SA Government is fundamentally a self-insurer. However, to protect the State's finances against a very large loss or claim or a series of large losses or claims in a year, a commercial catastrophe reinsurance program is placed in the international insurance market. The reinsurance program is renewed annually and then approved by the Treasurer (formerly the Minister for Finance) after consideration by the Advisory Board.

The structure of SAFA's catastrophe reinsurance program for 2017-18 is shown in the following diagram.



SAFA’s catastrophe reinsurance premium expense for 2017-18 was $8.3 million ($7.7 million), an increase of 8%. The increased cost in 2017-18 reflected increased levels of cover for industrial special risks and terrorism.

SAFA reviews its coverage levels annually. While various factors influence its final choice of cover, key drivers in this evaluation are the market’s willingness to accept risk for SAFA’s preferred coverage, and SAFA’s internal value-for-money assessments of the prevailing insurance market.

School loans scheme

As part of the 2016-17 State Budget, the SA Government established a new $250 million low interest loan scheme to help non-government schools upgrade infrastructure and facilities.

Loans of between $500 000 and $10 million per school will be made available over five years, with loan terms up to 15 years. All non-government schools are eligible to apply and access will be granted based on highest need, taking into account a school’s Socio Economic Status score. Priority will be given to projects that invest in science, technology, engineering and maths, as well as early years facilities.

Since the scheme’s inception there have been four funding rounds.

The first loan was drawn down under the scheme in February 2017. Total funds advanced to non-government schools as at 30 June 2018 were $35.5 million, made up of $32.3 million (face value) in loans and $3.2 million in overdraft facilities. As at 30 June 2018, $1 million had been paid back.

The total value of approved school loans at 30 June 2018 was $80 million, with $43.5 million not yet drawn down.

SA Venture Capital Fund

On 1 July 2017 SAFA entered into an agreement to establish a $50 million SA Venture Capital Fund with the object of assisting early-stage South Australian companies to attract private sources of co-investment from national and international investors.

Blue Sky Venture Capital was appointed as the fund manager for the SA Venture Capital Fund and will provide investment and management services. To be eligible for funding, there are a range of criteria that need to be met, including requirements for assets and staff to be located in South Australia within 12 months of the initial investment date.

In 2017-18 there were two investments made totalling $4.3 million at 30 June 2018.

National Redress Scheme for Institutional Child Sexual Abuse funding

On 25 May 2018 the SA Government approved South Australia’s participation in the National Redress Scheme for Institutional Child Sexual Abuse (the Scheme) and for SAicorp to administer all payments associated with South Australia’s participation in the Scheme. On 6 June 2018 the Premier signed an Intergovernmental Agreement confirming South Australia’s participation in the Scheme.

It is anticipated the Scheme will become operational within the next 12 months when Commonwealth and State legislation is finalised. The estimated start date for the Scheme is February 2019 and it will operate for 10 years.

The Treasurer approved the transfer of $146.4 million from the Victims of Crime Fund to SAicorp on 24 June 2018 to meet the cost of paying claims made under the Scheme. The Scheme will be administered through a separate fund, Fund 4, once the legislation has been finalised. The full amount of funding received for the Scheme is recognised as a liability, reflecting that the amount will be paid out for, or in relation to, compensation, or returned to the Victims of Crime Fund.

Insurance settlement paid to Mr Henry Keogh

The Budget and Finance Committee of the Legislative Council is examining the $2.57 million payment that was made to Henry Keogh. The Legislative Council has given authority for the Committee to hold public hearings.

In those circumstances, our review of this payment was limited to verifying the correct authority for the payment and whether the payment decision was made having received relevant advice.

SAicorp acts as the State Government's insurer, including providing insurance against legal judgements and settlements. SAicorp, as a division of SAFA, has functions provided by section 11(2) of the SAFA Act that allow it to settle matters, with the approval of the Treasurer, related to insurance activities.

It is consistent with these functions that, following the receipt of correspondence from lawyers representing Mr Henry Keogh and working in conjunction with other State Government agencies, SAicorp provided a memo in May 2018 to the Treasurer seeking his approval to negotiate a settlement with Mr Keogh's legal representatives.

The Treasurer approved the memo setting out the parameters for the settlement. Following legal negotiations a Deed of Settlement and Release, which was consistent with the memo, was signed on 29 June 2018. It provided that the State pay Mr Keogh a total of $2.57 million, including payments for legal costs he incurred. The payment was finalised in July 2018.

The Deed of Settlement and Release, which has been made available through the Parliament of South Australia website, releases the State from potential claims related to the matters subject to the settlement.

South Australian Housing Trust (SAHT)

Financial statistics	Net cost of providing services:	$278 million
	Rental income:	$251 million
	Rental property expenses:	$375 million
	Total revenue from SA Government:	$183 million
	Value of rental property:	$7.1 billion
	Number of lettable rental properties:	34 706

Significant events and transactions

- Property, plant and equipment was revalued upwards by $418 million.
- Property and tenancy management for 4003 public housing properties valued at $1.1 billion transferred to the community housing sector on 23 September 2017, with a further 47 transferred on 24 March 2018.
- The SAHT received an additional $70 million land tax equivalent reimbursement from the Treasurer as a result of a decision to reverse the reduction in funding approved in the 2017-18 Budget.
- The agreement to replace the SAHT's ageing legacy systems was executed. Total implementation cost for this program is estimated at $45 million.

Financial report opinion

Unmodified

Financial controls opinion

Modified

Key issues:

- Further action is required to finalise a strategic asset management plan
- The SAHT's policy framework does not detail the circumstances when management should consult with the Board when formulating and approving new initiatives and policies
- The SAHT has been unable to effectively apply key performance measures in housing maintenance when monitoring multi-trade contractor performance due to concerns with the reliability of quality performance data

Functional responsibility

The SAHT continued in existence under the *South Australian Housing Trust Act 1995* (SAHT Act).

The functions of the SAHT include:

- the construction, purchase, ownership and management of houses and units for tenant occupation
- managing SAHT tenancies and housing grant programs.

The SAHT did not employ staff in the year ended 30 June 2018 but relied on the Urban Renewal Authority (URA) and the Department of Human Services (DHS), through its Housing SA (HSA) division, to deliver services on its behalf.

The SAHT had service level administrative arrangements with:

- the URA to provide asset and maintenance strategy services, develop and deliver projects to renew the SAHT's housing stock and manage not-for-profit community housing growth strategies and transfers, including relevant financial management
- DHS to deliver social housing services (including property maintenance) through HSA.

Prior to the State election in March 2018 the SAHT was subject to the control and direction of the then Minister for Housing and Urban Development, with the then Minister for Social Housing responsible for selected functions under the *Housing Improvement Act 2016* and the SAHT Act to provide social housing services (including property maintenance) and other housing programs.

From March 2018 all responsibilities under the SAHT Act and other relevant acts were assigned to the Minister for Human Services.

SAHT to operate independently

As a result of the new SA Government's plan to change the SAHT's governance arrangements, from 1 July 2018 the SAHT began operating independently of DHS and the URA. Existing service level arrangements with these entities have been dissolved and the employment of about 1000 DHS and URA staff has transferred to the SAHT.

Scope of the audit

The audit program covered major financial systems to obtain sufficient evidence to form an opinion on the financial report and internal controls.

Specific areas of audit attention in 2017-18 included:

- revenue including raising rent, recoveries and debt write-offs
- accounts payable
- staffing costs

- maintenance
- council and water rates
- fixed assets including rental properties and capital works
- private rental assistance
- house sales
- general ledger
- project management, procurement and contract management
- fees received from community housing providers under the Master Community Housing Agreement
- billing of council and water rates for properties where tenancy and property management has transferred to the community housing sector in 2018.

Internal audit activities were considered to identify and assess the risks of material misstatement in the financial report and to design and perform audit procedures.

In addition, some services, including payroll and accounts payable processing, were undertaken by Shared Services SA (SSSA) and these were reviewed as part of our audit of SSSA.

Audit findings and comments

Assessment of controls

In my opinion, the controls exercised by the South Australian Housing Trust in relation to the receipt, expenditure and investment of money, the acquisition and disposal of property and the incurring of liabilities, except for all matters outlined under 'Communication of audit matters', are sufficient to provide reasonable assurance that the financial transactions of the South Australian Housing Trust have been conducted properly and in accordance with law.

Communication of audit matters

Matters identified by the audit were detailed in management letters to the Chief Executive, URA and from 1 July 2018, the Interim Chief Executive, SAHT. The main matters raised and related responses are detailed below.

Governance arrangements require improvement

We noted that:

- further action was required to finalise SAHT's strategic asset management plan (SAMP)
- improvement was required to the SAHT's policy framework to ensure proper and reasonable consultation with the SAHT Board when formulating and approving new policies.

Strategic asset management planning

Last year we noted that while the SAHT had a Housing and Accommodation Strategy that provided strategic guidelines and a decision-making framework for asset management, it had identified the need for a documented SAMP. A SAMP is an important tool to support the efficient management of public housing and should ideally address the following questions:

- What assets does the SAHT control and what is their condition?
- What are the community's current and anticipated demand for these assets?
- How does the SAHT plan to meet current and future demand?

A SAMP should articulate and prioritise the delivery of community needs for public housing.

Our follow-up in 2018 noted that while the SAHT has developed a draft SAMP, it:

- does not reflect a completed asset condition assessment
- has not been approved by the SAHT Board
- needs updating to reflect the SAHT's new governance arrangements.

The SAHT responded that:

- an ongoing asset inspection program started in March 2018 and as at 31 July 2018, 2343 inspections had been completed. The SAHT is incorporating asset information from these inspections into the asset strategy decision-making process
- a new SAHT Board was appointed following changes to governance arrangements approved by the new SA Government and that the SAMP will be provided to the SAHT Board after November 2018 when the new members meet for the first time
- the SAMP has now been updated to reflect the new governance arrangements of the SAHT under the Minister for Human Services.

Updates required to the SAHT Board policy framework

Under the governance arrangements in place in 2017-18, the SAHT Board had delegated its authority to approve SAHT policy to the URA General Manager and Housing SA Directors.

Recognising the important role that the SAHT Board has in setting policy direction, we have previously recommended that the Board update its policy framework to detail the circumstances under which consultation with the Board is required when management formulates and approves new policies.

While the SAHT has previously responded that the policy framework would be updated to require SAHT Board approval for significant policy changes, the Board had not defined the circumstances that would result in a significant policy change.

The need to clarify the Board's role in approving policy arrangements was demonstrated through our review of SAHT's debt management.

Over the last two years the SAHT has written off over $9.5 million in tenant and ex-tenant debt under two large debt reviews. While these debt reviews were approved in line with SAHT delegations, they

resulted in a temporary change to the SAHT's existing debt policy framework. Further commentary on these debt reviews is provided under 'Debt management' below.

While we appreciate that the Board was aware of these two debt reviews, the reviews were not explicitly approved by them and it is not clear that the Board was provided with a detailed explanation of their nature and scope.

Recognising the significant value of debt foregone because of these two debt reviews, we recommended that the SAHT Board update its policy framework and link the approval of new initiatives and policy changes with expenditure authority.

The SAHT's Interim Chief Executive has accepted this recommendation and responded that a revised policy framework, which aligns approval of policy changes with expenditure authority, will be provided to the Board for approval.

Debt management initiatives implemented by the SAHT

As at 30 June 2018 the SAHT was owed $26 million in outstanding debt. Of this total, 92% relates to tenant and non-tenant debt (former tenants and customers on private rental assistance). About 86% of customer debt is subject to an arrangement to pay, with the average weekly repayment amount being $31 for tenants and $17 for non-tenants.

Because of difficulties faced by the SAHT in recovering tenant and non-tenant debt, an $18 million allowance for doubtful debts has been recognised as at 30 June 2018.

Over the last two years the SAHT has performed the following debt management reviews:

- large debt review – focus on domestic violence and associated financial hardship
- statute of limitations review – focus on financial hardship based on the age of customers.

These reviews, including their scope and criteria, were approved by Housing SA's Housing and Homelessness Leadership Group (HHLG), which was chaired by the Executive Director, Housing SA.

The two reviews resulted in the write-off of debt with a value of more than $9.5 million.

Large debt review (LDR)

The SAHT's debt write-off procedure allows Housing SA officers to write off debt where evidence of domestic violence is verified. Housing SA staff are also authorised to write off debt where there is evidence of financial hardship. The SAHT's writing off a debt procedure specifies the evidence that Housing SA officers must obtain to verify claims of domestic violence and circumstances of financial hardship.

Stage one of the LDR was completed in 2017 and involved the review of debtors with the largest debt who had a recorded history of domestic violence and associated financial hardship. While the SAHT's existing debt policy was applied when validating and writing off debt for reasons of domestic violence, it was not applied for writing off debt for reasons of financial hardship. The SAHT's policy framework for managing debt requires Housing SA officers to obtain reasonable evidence of long-term financial hardship before writing off debt for this reason. Reasonable evidence may include information on income and expenditure, financial counsellor's reporting or other supporting evidence.

The HHLG approved a temporary change to this policy framework for the purpose of stage one of the LDR. Stage one of the LDR required Housing SA officers to obtain evidence to substantiate claims of domestic violence when writing off debt for this reason. Where evidence of domestic violence was established and indicators of financial hardship were on record, the debtor was placed on an affordable repayment plan, with a revised debt figure payable over three years. The revised debt was calculated using a formula approved by the HHLG specifically for the purposes of the LDR. All remaining debt was written off because of financial hardship, regardless of whether the debtor was making debt repayments under a previously approved repayment plan.

Stage two of the LDR involved reviewing customers over 50 years of age with large debt.

Again, the HHLG approved a temporary change to the SAHT's existing debt policy framework and did not require Housing SA officers to obtain detailed evidence to confirm the customer's financial hardship before writing off debt. Customers were placed on an affordable repayment plan with debt payable over three or six years based on their age. Applicable customers 65 years and over are required to repay their new debt balance over three years, while customers aged between 50 and 65 years are required to repay in six years.

Any debt exceeding the amount owed under the new repayment plan was written off because of financial hardship, regardless of whether the customer was making repayments under a previously approved repayment plan.

Stage one of the LDR resulted in $5.6 million of debt write-offs.

Stage two has resulted in $2.5 million of debt write-offs since September 2017.

Statute of limitations review (SOLR)

The SAHT faces significant difficulty in pursuing long outstanding debt.

As part of the SOLR ,the HHLG approved the writing off of debt older than six years, regardless of whether a customer was making repayments under a previously approved repayment plan.

About $1.4 million in debt was written off under the SOLR between July 2017 and May 2018.

Our review of these debt management initiatives and SAHT's general debt management procedures noted the following.

Lack of evidence to support decisions relating to the debt management initiatives

We evaluated Housing SA's decision to proceed with these debt initiatives using the principles outlined in Treasurer's Instructions 17 'Evaluation of and Approvals to Proceed with Public Sector Initiatives' (TI 17) and associated guidelines. Our review noted that Housing SA:

- did not clearly identify the net benefit to the SAHT of these initiatives, and did not perform a detailed cost versus benefit analysis or risk analysis to support them
- did not perform a post-implementation review of the LDR or the SOLR to determine whether these initiatives achieved their objectives
- was unable to provide evidence that supported the use of new affordable repayment terms of three and six years when writing off debt under the debt initiatives.

I understand that the SAHT is responsible for providing affordable, secure and appropriate housing for its customers, many of whom are in vulnerable financial circumstances or at risk of homelessness. The SAHT has a difficult task in balancing its role in supporting these clients while demanding payment from them.

In my opinion it is therefore important that SAHT staff are well supported by good policy and procedures that guide decision-making when formulating new initiatives and policies. The use of business cases, cost versus benefit analysis and risk analysis are all important tools in supporting objective, evidenced based decisions. We recommended that the SAHT use these tools to support future major projects and initiatives.

The SAHT responded that:

- it will consider analysing future major projects and initiatives using the principles outlined in TI 17, including cost versus benefit analysis and risk analysis, as part of a planned review of SAHT policies due to the establishment of the new SA Housing Authority
- a post-implementation review of the debt initiatives will be undertaken
- the new affordable repayment terms were based on a broad assessment of affordability and capacity to pay. The post-implementation review will consider if the affordable repayment plans will be used on an ongoing basis.

Non-compliance with the SAHT's debt policies and procedures

We reviewed a sample of 15 debts written off under the SAHT's existing policies and procedures (not written off as part of the LDR or the SOLR) and identified five instances of non-compliance. Of these we noted:

- three instances where the debt write-off was approved by a Housing SA officer in excess of their delegated authority
- four instances where the Housing SA officer did not comply with SAHT procedure and obtain the evidence required to support the decision to write off the debt.

We also noted that one Housing SA region was not reconciling debts written off in the accounts receivable system with local records to ensure the validity, completeness and accuracy of system processing.

The SAHT responded that it would remind regional staff of their roles and responsibilities in managing and writing off customer debt, and outsourcing the collection of customer debt.

Maintenance

In October 2013 the SAHT implemented a multi-trade contractors (MTCs) model under which MTCs now manage most job orders issued by the SAHT for responsive, vacancy, programmed and capital upgrade maintenance within defined geographical areas. The SAHT's contracts with five MTCs are estimated to cost $912 million over eight years (including renewals).

Last year we noted that the SAHT has not implemented a reliable method of measuring MTC performance against the key performance indicators in MTC contracts. The SAHT responded that it

had developed a new performance management framework that MTCs were considering, with a trial of the new framework planned for October 2017. It replaces the six-monthly abatement (financial penalty) with a monthly abatement, based on the assessed degree of non-conformance. The monthly abatement assessment is aimed to reduce the level of contestability and provide a fairer and more reasonable approach to assessing performance.

Our 2018 review noted that the SAHT had not finalised and implemented the new performance management framework.

While the SAHT applied the existing framework in 2018, it has not been able to effectively apply key performance indicators when measuring MTC performance due to concerns with the reliability of quality performance data. Specifically, we noted that the SAHT has not:

- met its inspection targets for one MTC contract region for both contract management reporting periods in 2018, compromising the accuracy of the quality compliance benchmark
- applied abatements because an MTC has challenged the accuracy and validity of the data used by the SAHT to calculate the performance compliance score.

We also noted that the SAHT has not:

- developed procedures outlining the circumstances where abatements are to be applied
- obtained independent expert advice on its sampling methodology.

The SAHT responded that it has:

- concluded an internal review of the performance management framework and proposed further changes to timeliness and quality key performance indicators, with an external consultant engaged to review these changes against models applied in other jurisdictions. In the interim, the SAHT will address issues affecting the accuracy of data by increasing compliance/audit activity. The revised framework is planned to be finalised in 2018-19
- developed an IT solution (mobile application or ‘app’) to enable in-field compliance assessment of MTC performance for non-conformance. The app is scheduled for release in October 2018, at which time the new abatement methodology will be trialled. The procedures to support this methodology are currently in draft, awaiting trial outcomes. Following a successful trial and variation to MTC contracts, the procedures will be finalised. This is planned to occur in 2018-19
- approached a consultant to provide independent expert advice on the SAHT’s sample size and the selection methodology used to measure the MTC’s quality performance.

The SAHT has advised us that any changes to the performance management framework and abatement methodology will require the agreement of MTCs and a contract variation.

Management of SAHT properties transferred to community housing providers

The SAHT has recognised $2.5 billion worth of land and buildings managed by community housing providers (CHPs) under the following arrangements:

- CHPs with legal title to 4300 former SAHT properties that are managed by CHPs in line with a Master Community Housing Agreement. While legal title has transferred, Australian Accounting Standards require that these assets are recognised by the SAHT because of the level of control maintained.

- CHPs responsible for tenancy and property management for about 5000 SAHT properties using a concurrent lease and deed model. The SAHT retains legal title to these properties.

Our review of these two arrangements noted the following.

Annual fees not charged in line with the Master Community Housing Agreement

Under the Master Community Housing Agreement each CHP is required to pay the SAHT a fixed annual fee indexed for CPI on 1 July each year.

We reviewed a sample of five quarterly invoices for 2018 and identified four instances where the full CPI increase was not applied. We were advised that this was because of an approved adjustment to billing arrangements made in about 2012-13. We noted, however, that:

- the existing Master Agreement was implemented in 2016 and only provides for full CPI increases
- the SAHT was unable to provide evidence that the reduced CPI increases were approved in line with SAHT delegations.

We estimated the total value of CHP fees forgone for 2018 at about $153 000.

The SAHT responded that the full CPI increases have been applied to fix payment amounts under the Master Agreement for 2018-19 and that charging the CHPs an annual fee is under review.

Process to approve the write-off of debt owed by CHPs was inadequate

The SAHT transferred tenancy and property management for 4003 SAHT properties to five CHPs on 23 September 2017. This followed the transfer of management for 1086 SAHT properties in October 2015.

The lease agreement requires the CHPs to pay for all outgoings and charges for services during the term of the lease, and allows for the recovery of any outgoings that are paid by the SAHT on behalf of the CHPs during the lease term.

The SAHT paid all council rates and water charges for the quarter ending 30 September 2017. Under the lease terms the CHPs were responsible for all outgoings from 23 September 2017, meaning that the SAHT was legally entitled to recover the charges paid on behalf of the CHPs for the eight days between 23 and 30 September 2017.

We noted that the SAHT did not seek to recover these outgoings but instead wrote off an estimated $137 000 in council and water charges owed by the CHPs. The SAHT’s reasons for this write-off included a recognition of the administrative burden placed on the SAHT in calculating the amounts owed.

While we appreciate the importance of administrative efficiency, and acknowledge that the write-off was approved in line with SAHT delegations, it is not clear that the SAHT took all reasonable action to recover the amounts owing. The SAHT did not estimate the administrative cost of accurately calculating the amounts owed or consult with the CHPs to agree an efficient approach to estimating amounts owed. As a result, the SAHT has forgone the recovery of these costs without taking all reasonable action.

We recommended that the SAHT implement procedures to consult and agree with CHPs on the recovery of council and water charges (supply, sewerage and usage) for any future transfers of property and tenancy management to CHPs.

The SAHT responded that the decision to write-off these costs included the consideration of the materiality of the cost, the administrative complexity of recovery and the need for all parties to show flexibility and forbearance on a very complex set of transactions. The decision was documented and made within appropriate contract delegations. The SAHT also responded, however, that it will implement procedures to consult and agree with CHPs on the recovery of any future council and water charges.

Other comments

Review of the Renewing Our Streets and Suburbs (ROSAS) initiative

The SA Government has implemented the ROSAS initiative to rejuvenate older SAHT homes and improve the supply of affordable housing for rent or purchase while stimulating the construction sector. The following programs are key to the ROSAS initiative:

- construction of 1000 new homes in 1000 days commencing in December 2015
- renewal of 4500 older SAHT homes within 10 kms of the city by 2020
- transferring responsibility for property and tenancy management for over 5000 SAHT properties to CHPs by 2018.

The ROSAS initiative will be mostly self-funded through the sale of SAHT properties, together with a $65 million housing stimulus package from the SA Government.

The following summarises progress against each of the ROSAS programs as at 30 June 2018. This information was provided by the SAHT and is unaudited.

1000 homes in 1000 days

Tenders to build 1000 homes have been released to the market, 440 homes were under construction and 398 completed. The SAHT advised that the remainder of the program will be completed by April 2020, with 960 homes scheduled for completion by October 2019. The SAHT noted that delays in the program resulted from delays in tenant relocations, the desire to achieve innovative housing design and other factors affecting large-scale housing programs, including planning approvals, demolitions and weather.

Renewing 4500 older SAHT homes by 2020

2247 homes were released to the market to renew through various programs and expressions of interest, 361 homes were under construction and 442 new or refurbished homes completed. The SAHT advised that it is not expecting to complete this program within its original scheduled timeline, with the delays impacted by the complexity of the projects.

Transfer of property and tenancy management to CHPs

The responsibility for property and tenancy management for over 5000 SAHT properties transferred to CHPs in two tranches. The first tranche of 1086 SAHT properties (valued at about $184 million) was transferred to two CHPs in October 2015. The second tranche of 4003 SAHT properties (valued at about $1.1 billion) transferred to five CHPs in September 2017. A further 47 properties transferred in March 2018 (valued at about $13 million).

The SAHT has applied a concurrent lease and deed model to these transfers. The leases for the first tranche have three-year terms, expiring on 23 October 2018, with optional extensions of 20 years. Unlike the first tranche, the leases for the second tranche have 20-year terms and require the CHPs to implement a stock renewal program.

An objective of the CHP transfers is to create better quality social housing stock through:

- rents increasing by the amount of Commonwealth rent assistance to fund housing stock improvements. CHP tenants are eligible for Commonwealth rent assistance whereas SAHT tenants are not
- CHPs using their additional rental income to improve the quality of housing stock by implementing a stock renewal program and increasing programmed maintenance.

CHPs must also comply with the SAHT's tenancy conditions, ensuring the tenancy conditions of transferred tenants remain the same. Due to the lease and deed arrangements the housing stock remains recognised in SAHT's Statement of Financial Performance, classified as assets under arrangement.

The SAHT has started negotiations for contract extension with the two CHPs responsible for the first tranche of properties. Negotiations are subject to continued satisfactory performance over the remaining period of the current arrangements. Any extension of these leases will require SA Government approval.

The SAHT is in discussions with the five CHPs responsible for the second tranche of properties regarding the Final Investment and Asset Management Plan that supports the stock renewal program. The agreed plan will form the basis of seeking SA Government approval of an overall development program.

Triennial review

Section 43 of the SAHT Act requires the Minister, once in every three years, to cause a report to be prepared on the operations and administration of the SAHT.

The triennial review for the period 2013-14 to 2016-17 was presented to Parliament on 4 July 2018. Performed by an external consultant, it included several significant observations on the governance arrangements that support SAHT operations. Some of the more notable findings included:

- the SAHT currently has no clear performance framework set out through Ministerial direction or funding arrangements
- year on year funding under the State budget process has varied which impacts the SAHT's ability to develop and deliver long-term plans
- the new Commonwealth funding agreement (National Housing and Homelessness Agreement) that commenced on 1 July 2018 requires the State to develop a housing strategy
- property condition profiles have not been kept up to date by the SAHT in recent years and this has resulted in an unclear picture of the maintenance backlog. The SAHT has started but not yet finished inspecting the condition of its properties
- underutilisation and overcrowding figures indicate properties do not meet changing tenant profile needs. The SAHT has undertaken strategies to redevelop properties, including transferring properties to the community housing sector for redevelopment.

The triennial review also identified the following areas in which the SAHT needed to improve its operations and administration:

- To support a modern housing system, a business model should be developed that enables policy objectives to be achieved in the most effective and sustainable manner.
- Improved benchmarks and indicators should be implemented to measure strategic targets and operational performance.
- The SAHT should evolve its service and asset delivery to meet the needs of its growing primary tenant cohort of single aged households.
- Options to increase rental revenue include looking to a 30% household income cap like some other jurisdictions or tailoring the rental policy to encourage employment and mobility within the housing system.

The Minister for Human Services responded in Parliament that the SAHT will operate under a new governance framework and structure. A key deliverable of the new SAHT is the development of a new housing and homelessness strategy.

Shared Services SA – financial systems and transaction processing environments

SSSA processes financial transactions on behalf of the SAHT under service level determinations. The main systems and control environments include accounts payable, payroll and general ledger financial functions.

Our review and evaluation of controls for these systems concluded that controls were effective for 2017-18.

SSSA is discussed further in the commentary under 'Department of the Premier and Cabinet' in this Report.

Business System Transformation program status update

The SAHT established the Business System Transformation program to replace its ageing legacy IT systems. This program will result in the acquisition of a core system replacement solution, comprising housing and software implementation services that cover broad business services including property management, tenancies management, procurement and contract management, and financial service requirements.

Total implementation costs for the program are estimated at $45 million, which includes a contract for program implementation, and cloud and related services. This cost will be funded from existing SAHT resources.

On October 2017 the Cloud and Related Services (CARS) Agreement with Northgate Public Services Pty Ltd (NPS) was executed. Under this agreement NPS will provide a commercial off-the-shelf housing management solution to replace existing SAHT legacy systems. The initial term of the contract is seven years and two months which includes five years of support, and a five-year extension option. A subcontracting arrangement was also entered into through NPS for the provision of hosting services to run the software of the new housing management solution.

The program's implementation stage started in late January 2018, with go-live anticipated to occur in April 2020. Following the implementation of the new CARS solution, the SAHT's existing mainframe legacy system will be decommissioned and the support licence will cease.

SAHT management reporting indicates that the business system transformation program is tracking on time and within the approved budget.

We will conclude our review of the procurement of these services in 2019 and continue to monitor the phased rollout of the program.

Revised Commonwealth funding agreements

From 1 July 2018 the National Housing and Homelessness Agreement will replace the former National Partnership Agreement on Homelessness (NPAH), National Affordable Housing Agreement (NAHA) and the National Affordable Housing Specific Purpose Payment (NAHSPP). The NPAH was previously administered by the Department of Human Services, however from 1 July the SAHT will be responsible for administering any responsibilities relating to homelessness.

The National Housing and Homelessness Agreement requires state housing authorities to have a publicly available housing strategy that indicates the level of housing supply to respond to projected demand and outlines the reforms and initiatives that will contribute to meeting this need, as well as a publicly available homelessness strategy that addresses priority areas of need.

The National Partnership Agreement on Remote Housing expired on 30 June 2018. The State is currently in negotiations with the Commonwealth regarding a new agreement.

Interpretation and analysis of the financial report

Highlights of the financial report*

	2018 $'million	2017 $'million
Expenses		
Staffing costs	73	74
Maintenance	108	114
Council rates and water rates	76	79
Land tax equivalent	190	180
Depreciation and amortisation	90	88
Grants and subsidies	33	37
Other expenses	92	90
Total expenses	662	662
Income		
Rental income	251	279
Commonwealth revenues	75	74
Other	58	55
Total income	384	408
Net cost of providing services	278	254
Revenues from SA Government	183	88
Net result	(95)	(166)
Other comprehensive income	408	127
Total comprehensive result	313	(40)

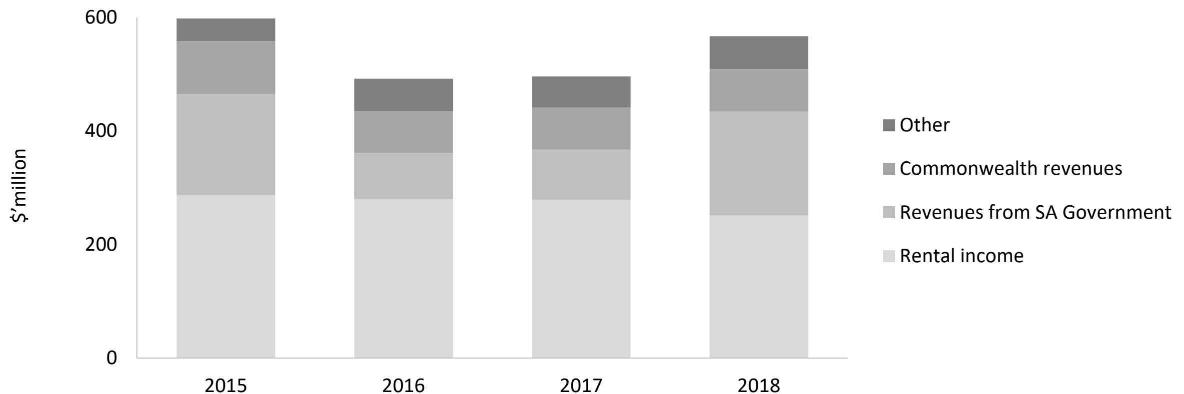
	2018 $'million	2017 $'million
Net cash provided by (used in) operating activities	(27)	(200)
Assets		
Current assets	350	390
Non-current assets	10 253	9 890
Total assets	10 603	10 280
Liabilities		
Current liabilities	73	71
Non-current liabilities	20	20
Total liabilities	93	91
Total equity	10 510	10 189

* Table may not add due to rounding.

Statement of Comprehensive Income

Income

A structural analysis of the SAHT's income for the four years to 2018 is presented in the following chart.



Total income (including revenues from the SA Government) increased by $71 million to $567 million in 2018 reflecting:

- SA Government revenues increasing by $95 million to $183 million, comprising increases in both recurrent and capital funding:
  - Recurrent funding increased by $85 million resulting from an increase in the tax equivalent reimbursement by $95 million, which included $70 million arising from the Treasurer's decision to reverse the reduction in funding approved in the 2017-18 Budget, offset by a $9 million decrease in the reimbursement of emergency management grants. Grants were received in 2017 to provide support for South Australians affected by the extreme weather and loss of power event in September 2016.
  - Capital funding increased by $10 million due mainly to the once-off transfer of the Housing Loans Redemption Fund from the Department of Treasury and Finance following the repeal of the *Housing Loans Redemption Act 1962*

- an increase in other income of $3 million due to a $14 million increase in the gain on disposal of non-current assets, offset by decreases in recoveries and interest revenue:
  - The gain on disposal of non-current assets in 2018 reflected a significant increase due mainly to the receipt of a $7 million revenue share from the sale of land in Playford which was owned jointly with the URA, the higher volume of developed properties disposed through the SAHT's housing renewal and capital programs, and a greater average gross profit margin being achieved. Further comment on the disposal of properties is provided below.
  - Recoveries decreased by $8 million due mainly to a $5 million reduction in recoveries from tenants for water usage. Tenant recoveries are impacted by debt write-off practices, the transfer of tenancy and property management to CHPs and seasonal fluctuations in water usage.
  - Interest revenue decreased by $3 million due to the timing of cash received, with the $70 million land tax equivalent reimbursement received in late June 2018
- a decrease in rental income of $28 million to $251 million. This decrease reflects the transfer of property and tenancy management for 4050 public housing properties to the community housing sector in 2018.

Proceeds from the disposal of non-current assets support the SAHT's financial viability strategy and its housing renewal and capital programs. Proceeds from the disposal of non-current assets in 2018 totalled $134 million, comprising property sales totalling:

- $59 million to support the SAHT's financial viability strategy
- $75 million to support the SAHT's housing renewal and capital programs.

The cost of sales, including the carrying amount, for non-current assets disposed totalled $117 million, leaving a net gain on disposal of $17 million.

Rental operations

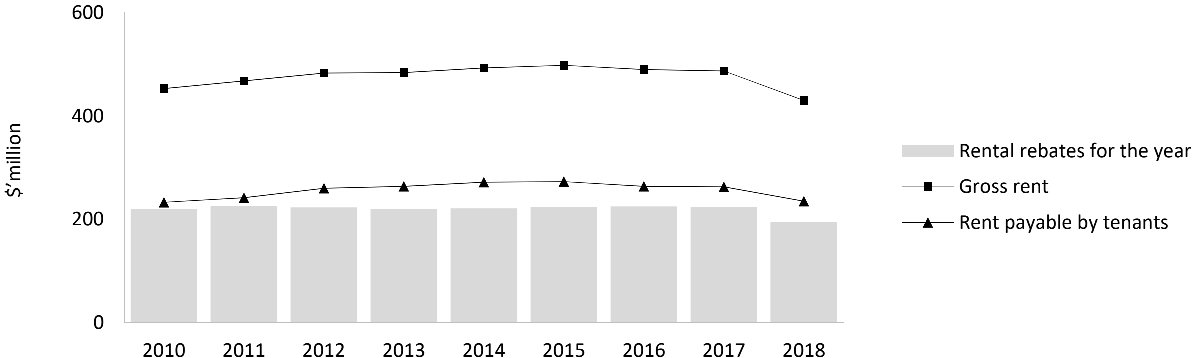
The following table shows the level of housing stock, excluding unlettable properties, as at 30 June for the past five years.

	2014	2015	2016	2017	2018
	Number	Number	Number	Number	Number
Properties	42 847	41 726	39 855	39 074	34 706

The table highlights that housing stock decreased by 4368 in 2018. This decrease arose mainly from the transfer of property and tenancy management for a further 4050 public housing properties to the community housing sector in 2018.

Information provided by the SAHT records that 87% (92%) of tenants pay reduced (rebated) rent. The amount of rent rebates depends on each tenant's circumstances, with rent payable capped at 25% of household income or market rent, whichever is lower. In addition to changes in an individual tenant's financial circumstance, the improvement in the percentage of tenants on reduced rent is also attributable to the transfer of tenancy and property management for 4050 properties to the community housing sector, which included tenants on rent rebates.

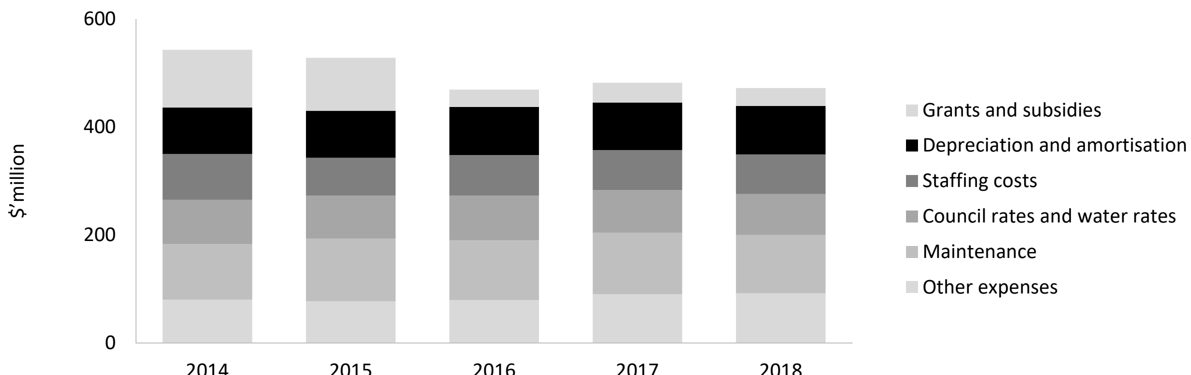
Data relating to housing stock levels and tenancies was provided by the SAHT and is unaudited. The trend of rents and rebates is illustrated in the following chart.



The chart highlights that gross rent steadily increased to 2015 due to increases in market rents. While market rents have continued to increase since then, gross rent has reduced following the transfer of responsibility for tenancy management of 1086 properties to the community housing sector in 2016. A further 4050 properties were transferred in 2018. The rent on these properties is retained by the community housing sector.

Expenses

For the five years to 2018, the major expense items for the SAHT, other than land tax equivalent expenses, are shown in the following chart.



The chart shows a downward trend in expenses since 2014.

In 2018 total expenses (excluding land tax equivalent expenses) decreased by $10 million to $472 million due mainly to:

- grants and subsidies decreasing by $4 million due mainly to:
  - an $8 million reduction in emergency management grants. Grants were paid to provide support for South Australian's affected by the extreme weather and loss of power event in September 2016, partially offset by a $2 million increase for the CBD Respite Facility
  - a $3 million increase in the National Partnership Agreement on Remote Indigenous Housing grants paid as a result of additional housing upgrades and new builds
- maintenance expenses decreasing by $6 million following the transfer of tenancy and property management to the community housing sector

- supplies and services decreasing by $3 million due mainly to a $2 million reduction in business-as-usual ICT expenditure as a result of the Business System Transformation program
- impairment expenses increasing by $6 million, resulting from an increase in asset write-offs due to property demolitions relating to the SAHT's housing renewal programs, specifically the Better Neighbourhoods program and the 1000 Homes in 1000 Days program.

Land tax reimbursements

Effective 30 June 2013 the Commonwealth Government agreed to write off $320 million of South Australian public housing debt as part of a package to stimulate the housing construction sector. The Treasurer subsequently forgave $320 million of SAHT loans.

The SA Government has reduced reimbursements for land tax equivalents expense to recoup the loans forgiven and achieve budget savings.

In 2018 the land tax expense was $190 million, with $167 million reimbursed by the SA Government resulting in $23 million returned to the State Budget. Included in the land tax reimbursement is $70 million that was received on 28 June 2018 from the Treasurer as a result of the decision to reverse the reduction in funding approved in the 2017-18 Budget.

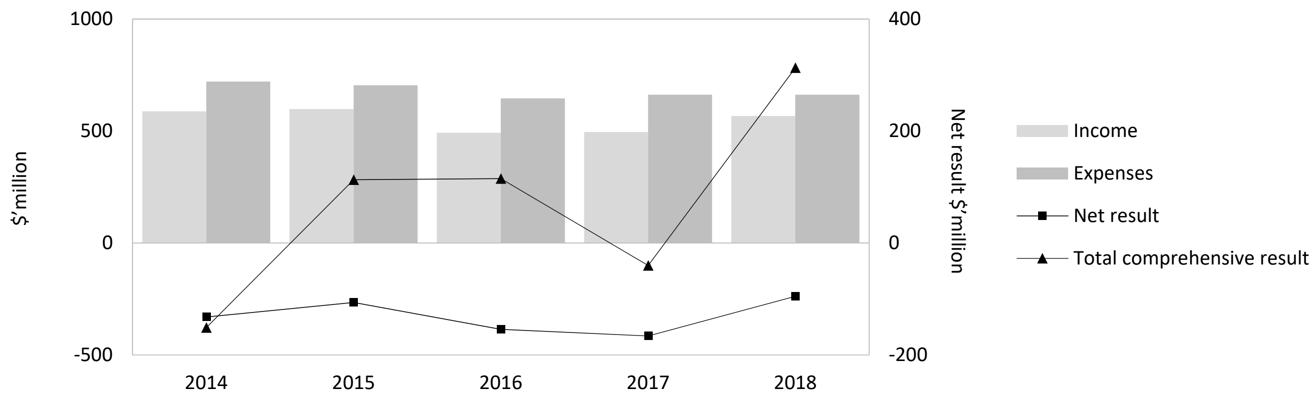
Since introducing this arrangement five years ago, the SAHT has returned $404 million to the State budget, which exceeds the $320 million SAHT loans forgiven by the Treasurer. A further $14 million is expected to be returned in 2019.

The following table shows the amount returned to the State budget by the SAHT for the past five years.

	2013 $'million	2014 $'million	2015 $'million	2016 $'million	2017 $'million	2018 $'million
Land tax equivalent expense	181	178	176	178	180	190
Tax equivalent reimbursement	181	99	87	72	73	167
Amount returned to State budget	-	79	89	106	107	23

Net result and total comprehensive result

The following chart shows the income and expenses (including income tax equivalent but excluding administrative restructure), net result and total comprehensive result for the five years to 2018.



The chart shows that the SAHT has been in deficit since 2014. SAHT's total comprehensive result, which includes the impact of fixed asset revaluations, improved to $313 million reflecting a $418 million revaluation upwards for total property, plant and equipment.

The net result for 2018 improved by $72 million from the previous year as a result of an increase in revenues received from the SA Government. This is due mainly to the $70 million land tax reimbursement that was receipted by the Treasurer on 28 June 2018. The reduced deficit in 2015 was due to $65 million received in June 2015 from the SA Government for public housing stimulus.

The SAHT last achieved a surplus in 2013, when the Treasurer forgave $320 million of SAHT loans.

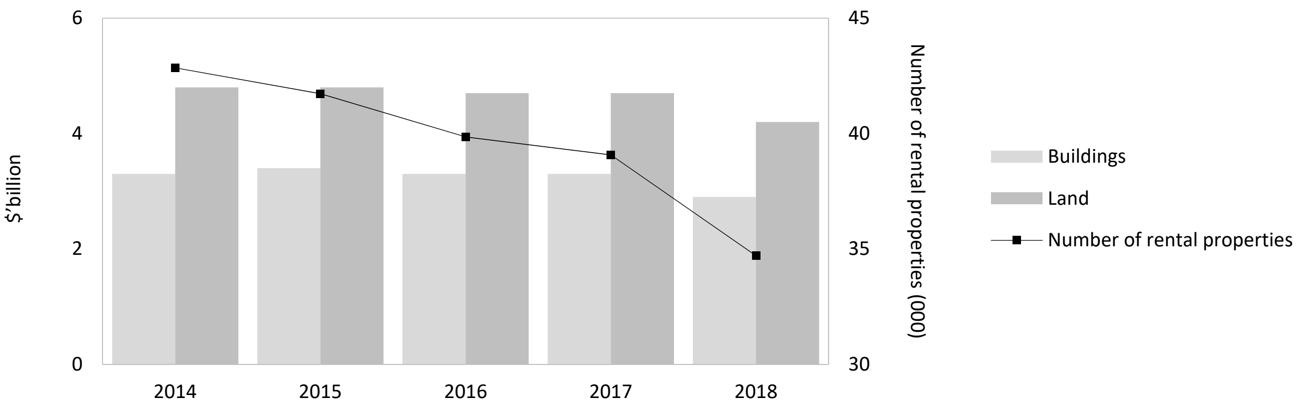
Statement of Financial Position

The SAHT's financial position is dominated by non-current property, plant and equipment assets. Current assets and liabilities are, while significant in their own right, not material relative to non-current assets. Notwithstanding, at 30 June 2018 current liabilities amounted to $73 million ($71 million), while current assets were $350 million ($390 million).

Rental properties

SAHT's rental properties are estimated to be worth $7 billion and comprise 69% of the SAHT's property, plant and equipment of $10 billion.

The following chart shows the movements in the number and value of the SAHT's rental properties over the past five years.



The chart shows that while the value of rental properties has remained relatively constant between 2014 and 2017, maintained mainly through upward revaluations of individual properties and capital upgrades, the level of housing stock is reducing. The average value of an SAHT rental property, based on the totals, changed from $189 000 in 2014 to $205 000 in 2018.

In 2018 the level of housing stock largely reduced by 4368 properties to 34 706. This reduction was due mainly to the transfer of property and tenancy management of public housing properties to the community housing sector. This transfer followed the first tranche of CHP property transfers in 2016.

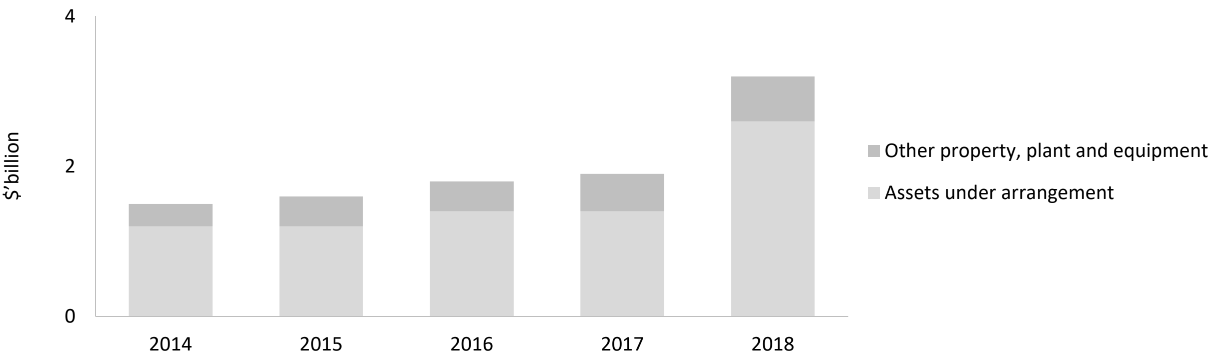
These properties are now classified as assets under arrangement and included in the commentary under 'Other property, plant and equipment' below.

In 2018 the value of rental properties decreased by $878 million to $7 billion. The decrease reflects transfers to other asset categories of $1.2 billion (principally to assets under arrangement), disposals of $66 million and depreciation expense of $61 million. These impacts were partially offset by an upward revaluation of land and buildings of $339 million, and additions of $124 million including completed capital works and maintenance upgrades.

It is important to note that the SAHT revalues most land and buildings annually using the Valuer-General's values. Because of the timing of the update of the Valuer-General's database and the SAHT's financial reporting obligations, reported values lag current market values. The values for 2018 were issued by the Valuer-General as at 1 July 2017. This policy has been consistently applied and reflects the practicality of valuing a very large housing stock. The Valuer-General has published a notice in The South Australian Government Gazette advising that the average percentage change in site values is 6.2% as at 1 July 2017 for 2017-18 and 4.6% as at 1 July 2018 for 2018-19.

Other property, plant and equipment (excluding rental properties)

The following chart shows the value of the SAHT's other property, plant and equipment assets over the past five years.



The SAHT's other property, plant and equipment rose sharply in 2018 due mainly to:

- assets under arrangement increasing by $1.1 billion due mainly to the transfer of the responsibility for property and tenancy management of 4050 properties to the community housing sector in 2018. These properties are no longer classified as rental properties
- capital works in progress increasing by $104 million to $296 million reflecting the increased activity in the SAHT's housing renewal programs.

Current assets

Current assets have decreased by $40 million to $350 million due mainly to decreases in cash and current receivables. The decrease in cash is explained under 'Statement of Cash Flows' below.

Current receivables decreased by $6 million due mainly to:

- a $4 million decrease in net receivables (receivables less allowance for doubtful debts) impacted by a reduction in water recoveries from tenants for water usage, debt write-offs under the LDR and SOLR debt management reviews, and the transfer of property and tenancy management to the community housing sector

- accrued revenues decreasing by $2 million due to the reduction in accrued recoveries from tenants for water usage.

Current liabilities

Current liabilities increased by $3 million to $73 million due mainly to a $6 million increase in sale deposits held, offset by a $2 million decrease in accrued expenses relating to payments made under the National Rental Affordability Scheme.

Statement of Cash Flows

In 2018 the SAHT recorded a decrease in cash of $28 million compared to a decrease of $192 million in the previous year. This change of $164 million was due mainly to:

- a $124 million decrease in payments for land tax equivalents. In 2017, the land tax equivalents paid were for 2017 and three quarters of 2016. In 2018, land tax equivalents paid were for 2018
- a $26 million decrease in rent received as a result of the transfer of property and tenancy management for 4003 public housing properties to the community housing sector in September 2017, with a further 47 transferred in March 2018
- a $37 million increase in proceeds from sales of rental properties
- a $56 million increase in development costs as a result of increased activity in the SAHT's housing renewal programs.

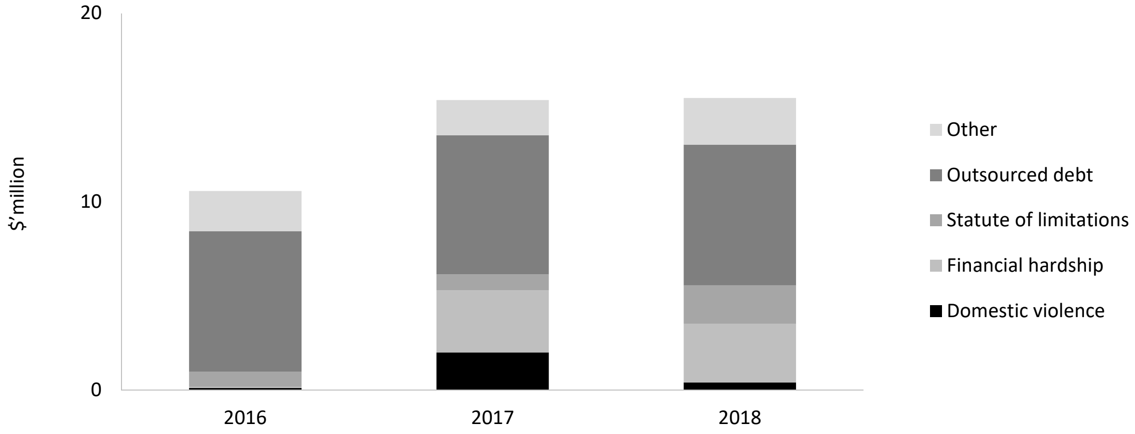
Further commentary on operations

Debt write-offs

Since 2016 the SAHT has performed the following debt management reviews:

- large debt review
- statute of limitations review.

The following chart shows the value of debts written off over the past three years.



The SAHT's total debt write-offs rose sharply in 2017 due mainly to the implementation of stage one of the LDR. This is evidenced by the large increases in debt write-offs for reasons of domestic violence and financial hardship in that year. The revised debt policy framework resulted in debt write-offs increasing by $5 million to $15 million.

While the chart shows that total debt write-offs are consistent in 2017 and 2018 at $15.5 million, debts written off under the statute of limitations reason increased significantly in 2018. This is due mainly to the implementation of the SOLR, which included reviewing debt older than six years.

Debts written off for reasons of financial hardship have remained consistent over the past two years following the conclusion of stage one of the LDR and commencement of stage two in September 2018. Stage two involved reviewing customers over 50 years of age with large debt who had a history of financial hardship.

Installation of solar panels and Tesla batteries on SAHT properties

On 4 February 2018 the SA Government announced a plan to roll out a network of at least 50 000 home solar and battery systems across South Australia, working together to form the world's largest virtual power plant. Beginning with a trial of 1100 SAHT properties, a solar panel system and Tesla battery will be installed at no charge to the household and financed through the sale of electricity. Following the trial, systems are set to be installed at a further 24 000 SAHT properties.

As at 30 June 2018, 100 solar panel systems and Tesla batteries have been installed on SAHT properties in the first phase of the project. The SAHT advised that a further 1000 solar panels and Tesla batteries are scheduled to be installed on SAHT properties by 30 June 2019 as part of the second phase.

We will continue to monitor the progress of the project in 2019.

South Australian Tourism Commission (SATC)

Financial statistics	Net cost of providing services:	$99 million
	Total appropriation:	$101 million
	Number of FTEs:	136
Significant events and transactions	— SATC held the 2018 Adelaide 500, which attracted a reported 273 500 patrons across the four-day event. This is 29 150 more patrons than the 2017 event. — SATC held the 2018 Santos Tour Down Under, which attracted a reported 46 000 event specific visitors. This is 3000 more patrons than the 2017 event.	
Financial report opinion	**Unmodified**	
Financial controls opinion	**Unmodified**	

Functional responsibility

SATC is established by the *South Australian Tourism Commission Act 1993* and is a body corporate.

The functions of SATC include promoting South Australia as a tourist destination and further developing and improving the State's tourism industry. SATC aims to achieve this by:

- ensuring a coordinated approach to promoting South Australia
- attracting, developing, owning and supporting major and strategic tourism events
- developing tourism resources to maintain and preserve South Australia's environmental and cultural heritage.

Scope of the audit

The audit program covered major financial systems to obtain sufficient evidence to form an opinion on the financial report and internal controls.

Specific areas of audit attention in 2017-18 included:

- income from sponsorships and event entrance fees
- employee benefits expenses
- expenditure on events, advertising and industry assistance
- general ledger processing.

Audit findings and comments

Communication of audit matters

No significant matters were identified by the audit.

Shared Services SA – financial systems and transaction processing environments

Shared Services SA processes financial transactions on behalf of SATC under service level determinations. The main systems and control environments include accounts payable, payroll and general ledger financial functions.

Our review and evaluation of controls for these systems concluded that controls were effective for 2017-18.

Shared Services SA is discussed further in the commentary under 'Department of the Premier and Cabinet' in this Report.

Interpretation and analysis of the financial report

Highlights of the financial report*

	2018 $'million	2017 $'million
Expenses		
Employee benefits expenses	15	15
Advertising and promotion	40	34
Industry assistance	22	19
Event operations	44	39
Other	10	10
Total expenses	131	117
Income		
Revenues from SA Government	102	89
Other	32	27
Total income	134	116
Net result	3	(1)
Other comprehensive income	6	-
Total comprehensive result	9	(1)
Net cash provided by (used in) operating activities	4	1

	2018 $'million	2017 $'million
Assets		
Current assets	17	13
Non-current assets	18	12
Total assets	35	26
Liabilities		
Current liabilities	8	8
Non-current liabilities	2	2
Total liabilities	10	10
Total equity	24	16

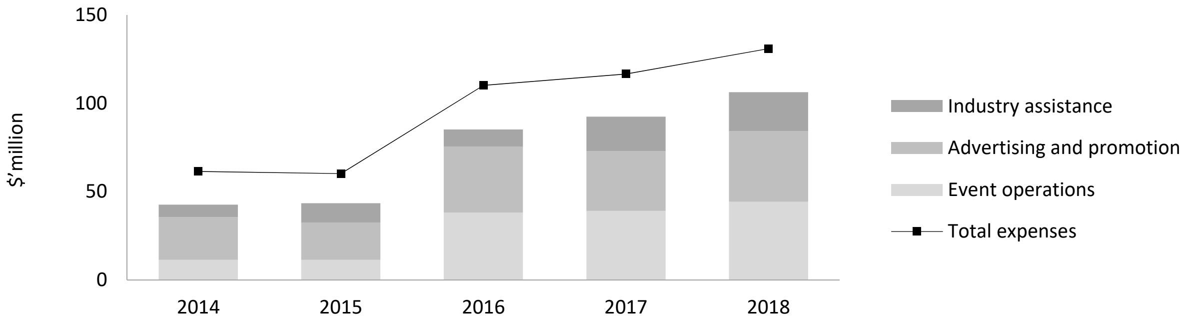
* Table may not add due to rounding.

Statement of Comprehensive Income

SATC relies on SA Government funding as its major revenue source to fund its operations. The level and timing of SATC's financial activities vary from year to year depending on the planned mix of marketing, destination development and events supported, and the extent to which specific identified opportunities are funded. The main events managed by SATC are the Adelaide 500, Santos Tour Down Under, Bridgestone World Solar Challenge, Credit Union Christmas Pageant, Tasting Australia and the Adelaide Fashion Festival.

Expenses

The following chart shows a structural analysis of the main expense items for the five years to 2018.



Total expenses increased by $14 million to $131 million in 2017-18 mainly as a result of:

- event operation expenses increasing by $5 million due mainly to the increased expenditure on catering, entertainment, venue hire, civil works and event contractors for the Adelaide 500, Bridgestone World Solar Challenge, Tasting Australia and Santos Tour Down Under
- advertising and promotion expenses increasing by $6 million due mainly to increased television productions and film shoots for the China Brand Ambassador Campaign and other television promotions
- industry assistance expenses increasing by $3 million due mainly to event sponsorships and tourism development grants including $1 million for the FIM Asia Road Racing Championship, $1 million for the Tailem Bend Motor Sport Park Supercars event and $900 000 for enhancements to the Port Adelaide Passenger Terminal.

Total expenses increased by $50 million in 2016 following the transfer of activities of the former South Australian Motor Sport Board (SAMSB) to SATC.

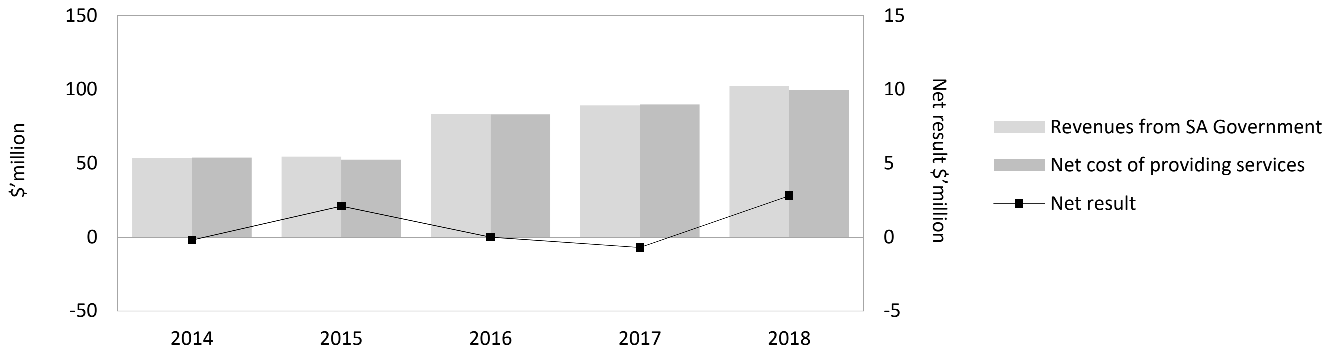
Income

Income for the year totalled $134 million ($116 million). Revenue from the SA Government was $102 million ($89 million) and represented 76% (77%) of total income. The SA Government provided extra funding of $13 million in 2017-18 mainly for the Adelaide 500, Australian Tourism Exchange, Tailem Bend Motor Sport Park and Port Adelaide Passenger Terminal.

Other income increased by $5 million to $32 million due mainly to increased income from sponsorships and event entry fees. The main events contributing to the increase in income were the Adelaide Fashion Festival, Tasting Australia and Bridgestone World Solar Challenge.

Net result

The following chart shows revenues from the SA Government, the net cost of providing services and the net result for the five years to 2018.



The chart shows that funding from the SA Government exceeded the net cost of services by $3 million in 2017-18, due to additional funding received from the Governor's Appropriation Fund. The additional funding was mainly to support international motor bike racing at Tailem Bend, once-off concert support for the Adelaide 500, office fitouts and expected higher operating costs.

Other comprehensive income

Other comprehensive income of $6 million related solely to a revaluation increment on motor sport infrastructure assets revalued by SATC at 30 June 2018. Infrastructure assets include buildings, barriers and fencing.

Statement of Financial Position

Current assets and liabilities

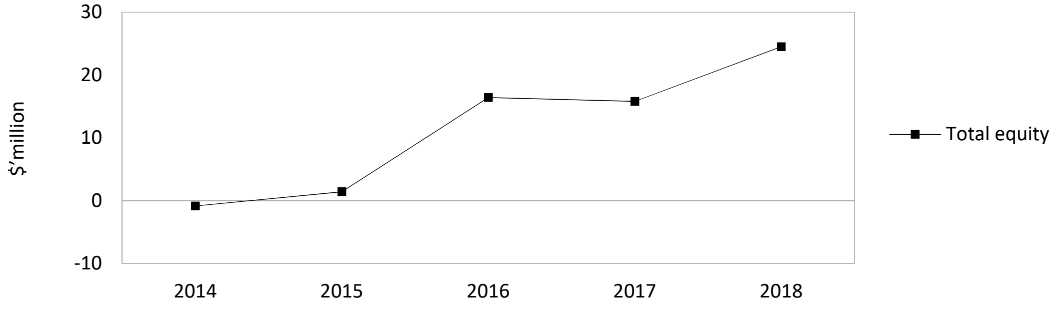
At 30 June 2018 current assets were $17 million ($13 million), exceeding current liabilities of $8 million ($8 million). Current assets increased due mainly to a $3 million increase in cash held. Cash provided by the SA Government of $102 million plus cash generated from operations of $39 million exceeded cash used in operations of $137 million. The increase in cash held reflected unspent funding from the SA Government to cover expected higher operating costs.

Non-current assets

At 30 June 2018 plant and equipment was $18 million ($12 million). The $6 million increase in plant and equipment was due mainly to a $6 million revaluation increment on motor sport infrastructure assets and office fitouts of $1 million (SATC moved premises in July 2018). The increase was offset by depreciation expense of $2 million.

Equity (net assets)

The following chart shows total equity as at 30 June for the past five years.



Total equity (net assets) increased by $9 million in 2017-18 due to a $6 million revaluation increment on motor sport infrastructure assets and a positive net result of almost $3 million. The $15 million increase in total equity in 2015-16 was due to the transfer of the former SAMSB on 1 July 2015.

Further commentary on operations

Naming rights sponsor for Adelaide 500

The naming rights sponsorship for the Adelaide 500 concluded after the 2017 event. This was a significant portion of SATC's sponsorship revenue. SATC is consulting with potential new naming rights sponsors for the 2019 event and beyond. In 2017-18 the SA Government provided extra funding for the event.

South Australian Water Corporation (SA Water)

Financial statistics	Water and sewer rates and charges:	$1.17 billion
	Community service obligations:	$145 million
	Borrowing costs:	$330 million
	Profit before income tax:	$202 million
	Infrastructure, plant and equipment:	$13.9 billion
	Borrowings:	$6.5 billion
	Net assets:	$5.5 billion
	Number of FTEs:	1492.4

Significant events and transactions

- SA Water's profit before tax increased by 7% to $202 million, mainly attributable to a 19 gigalitre increase in the volume of water sold and a 2.1% increase in rates charged for residential water use.
- Work started on the $155.6 million Northern Adelaide Irrigation Scheme with $20.5 million spent in 2017-18.
- Work continued on the $119.9 million upgrade of Kangaroo Creek Dam safety with $28.8 million spent in 2017-18 bringing the total spent so far to $56.6 million.
- Infrastructure, plant and equipment was revalued upwards by $99 million, mainly as a result of increases in the values of water and sewer infrastructure assets.

Financial report opinion — **Unmodified**

Financial controls opinion — **Unmodified**

Functional responsibility

SA Water is established under the *South Australian Water Corporation Act 1994*. It is responsible to the Minister for Environment and Water.

The primary functions of SA Water are to provide services for the storage, treatment and supply of water and removal and treatment of wastewater.

The *Public Corporations Act 1993* applies to SA Water and requires a charter and performance statement to be prepared by the Minister and the Treasurer after consultation with SA Water.

SA Water is a for-profit entity under Accounting Policy Framework II 'General Purpose Financial Statements Framework', APS 2.4.

Scope of the audit

The audit program covered major financial systems to obtain sufficient evidence to form an opinion on the financial report and internal controls.

Specific areas of audit attention in 2017-18 included:

- revenue raising, collection, receipting and banking
- procurement and contract management
- operating and capital expenditure
- payroll
- financial accounting
- non-current asset recording, valuation and depreciation
- borrowing and finance leases
- governance arrangements
- general IT controls.

The work of SA Water's internal auditors was also considered in planning and conducting the audit.

Audit findings and comments

Communication of audit matters

Matters identified by our audit were detailed in management letters to the Chief Executive. The main matters raised and related responses are detailed below.

Ellipse system controls need strengthening

Ellipse is SA Water's expenditure payment system which processed approximately $878 million in payments in 2017-18

Ellipse IT controls

SA Water's Ellipse domain is maintained by an external provider. We reviewed IT controls relevant to Ellipse and identified weaknesses in:

- application, database and operating system password configurations for contractor administrator accounts
- administrator account logging, monitoring and oversight, recommending that SA Water strengthen monitoring of privileged user account activities.

SA Water responded that it would request its service provider align privileged user password configuration settings with those documented in SA Water's Password Security Standard and request the service provider log privileged and administrator account activity as appropriate.

Review of Ellipse delegations not performed as required

We noted the need to clarify management's expectations on the checks staff are required to perform when reviewing Ellipse delegations.

Business units are required to check the validity of user access to Ellipse twice yearly. When performing this review, business units are expected to assess the accuracy and appropriateness of access levels and ensure the delegation limits in Ellipse reflect the Board's approved delegations of authority. Where discrepancies are identified business units are expected to take action to correct the error.

We identified instances where:

- a delegate's payment limit in Ellipse did not reflect their approved delegation of authority
- changes to delegations of authority were not approved in line with SA Water procedures.

Our discussions with SA Water staff concluded that these issues arose because some business units were unclear on the extent of checks they were required to perform when complying with SA Water's Ellipse delegation review instructions.

We recommended SA Water review Ellipse instructions to clarify staff responsibilities when reviewing Ellipse delegations and making changes to delegations of authority.

SA Water advised that all discrepancies in Ellipse delegations have been corrected and that it would update the Ellipse delegation review instructions.

Cash and financing

No bank account transaction limits

The electronic banking system allows SA Water to set payment limits at either the individual bank account, group consolidated bank account and/or user level. The use of payment limits provides a system control to limit financial exposure arising from error or fraud.

We noted that while SA Water had established a range of controls to prevent fraud and error in daily banking, including the use of dual authorisation for electronic payments, its transaction limits were set at the group consolidated account level.

We recommended that SA Water establish individual bank account payment limits and user limits that reflect the likely value of daily processing for each of SA Water's bank accounts.

SA Water responded that it would implement the necessary changes.

Interpretation and analysis of the financial report

Highlights of the financial report*

	2018 $'million	2017 $'million
Income		
Water and sewer rates and charges	1 166	1 076
Community service obligations	145	136
Other	186	158
Total income	1 497	1 369
Expenses		
Depreciation and amortisation expense	357	327
Borrowing costs	330	337
Operational and service contracts	185	185
Employee benefits expense	127	128
Other expenses	296	204
Total expenses	1 295	1 181
Net profit before income tax equivalents expense	202	189
Income tax expense	58	54
Net profit after income tax equivalents expense	143	134
Other comprehensive income (net of tax)	73	68
Total comprehensive result	216	202
Net cash inflows (outflows) from operating activities	487	395
Assets		
Current assets	237	249
Non-current assets	14 080	13 946
Total assets	14 317	14 195
Liabilities		
Current liabilities	293	293
Non-current liabilities	8 518	8 483
Total liabilities	8 810	8 776
Total equity	5 507	5 419

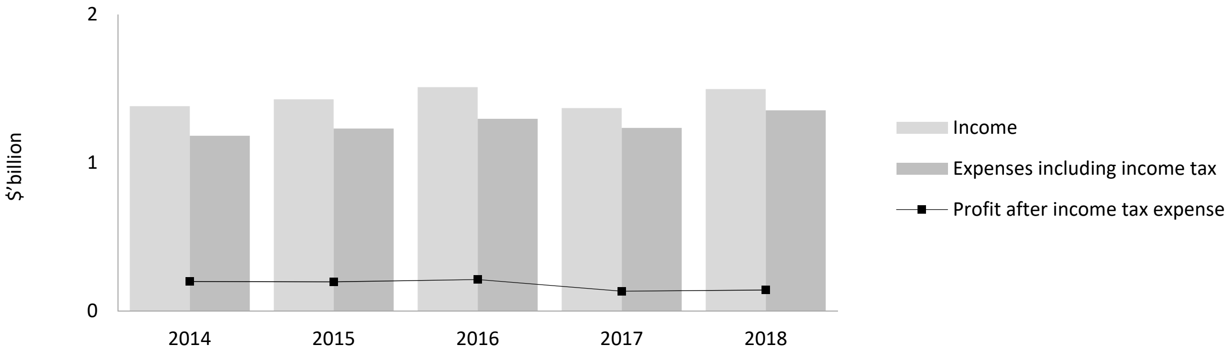
* Table may not add due to rounding.

Statement of Comprehensive Income

Operating result

SA Water's profit after income tax equivalents expense (income tax) increased by $9 million to $143 million.

The following chart shows the income, expenses (including income tax) and profit after income tax for the five years to 2018.

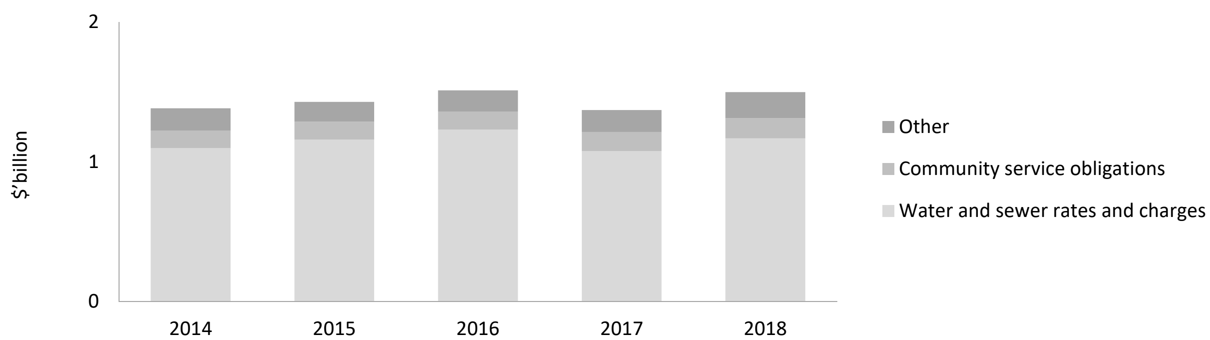


Since 2014 the Essential Services Commission of South Australia (ESCOSA) has regulated the revenue that SA Water can earn from the provision of drinking water and sewerage retail services. ESCOSA determines the revenue (not price) that SA Water may derive from these services, with SA Water setting annual water and sewerage charges to achieve the revenue limits determined by ESCOSA, and ESCOSA then monitoring SA Water's performance. Further information on ESCOSA's role in making price determinations is provided below under 'Further commentary on operations'.

The chart shows that since 2014 SA Water's profit after income tax has increased from each prior year, except in 2017 when SA Water experienced an 11% decrease in water usage. Further explanation of the movements in income and expenses is provided below.

Income

The following chart shows the main sources of income for SA Water for the five years to 2018.



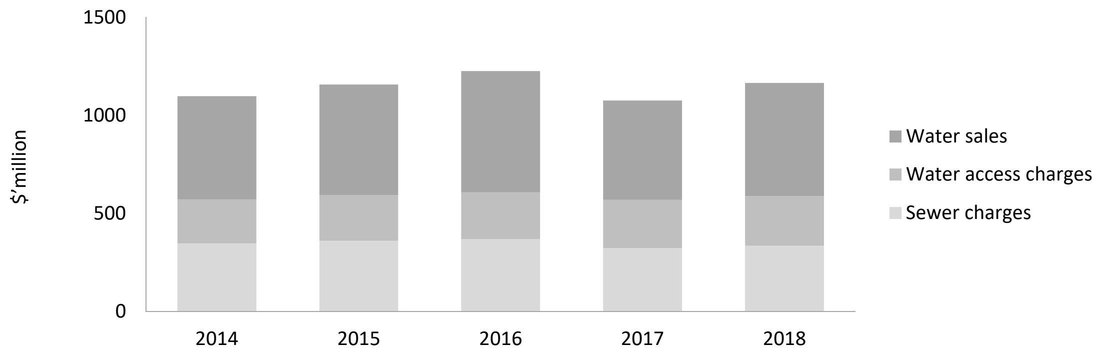
The chart shows total income generally increasing to 2018 (except in 2017), with income from water and sewer rates and charges in that year at the lowest level of the previous five years. Total income increased by $127 million to $1.5 billion in 2018. Factors that impact this trend are discussed below.

Water and sewer rates and charges

The major source of SA Water's income is water and sewer rates and charges. These mainly comprise:

- sewer charges, mainly set on property values
- water access charges, mainly set at a fixed amount
- water sales, charged by volume of water used.

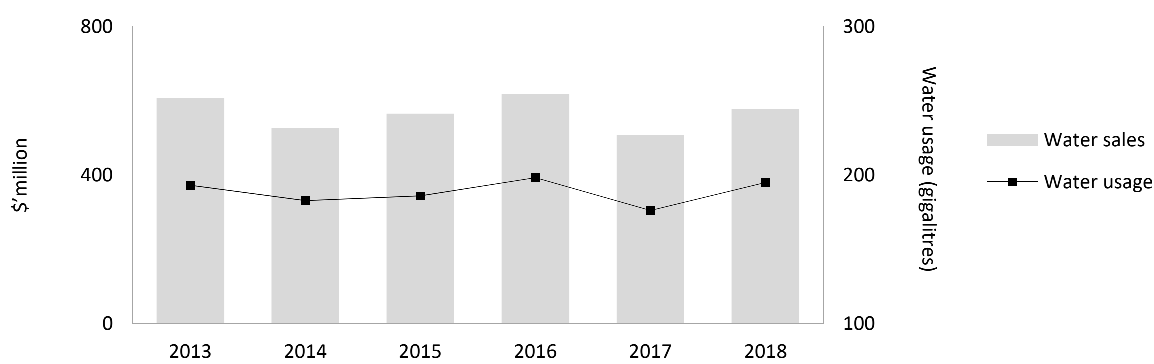
The following chart shows these components for the past five years.



The main factors affecting water and sewer rates and charges revenue are changes in price and water consumption. Water sales increased by $70 million in 2018 due to a 2.1% price increase and an increase in the demand for water. Demand for water is discussed further in the next chart. In 2017 water pricing decreased by an average of 3% and customers lowered their water usage.

Sewer charges increased by $11 million to $334 million also due to a 2.1% price increase and an increase in customer growth of $4.7 million. Water access charges increased by $8 million to $253 million mainly as a result of customer growth and pricing.

The following chart shows the relationship between water usage and water sales income.



Water usage decreased in 2014 due primarily to higher rainfall in that year compared to the previous. Water usage increased in 2015 and 2016, which SA Water attributed to hotter and drier weather conditions, especially for 2016. In 2017 water usage fell to 176.2 gigalitres, down from 198.3 gigalitres in the previous year. This reflected above average rainfall and below average temperatures in South Australia in 2017. In 2018 water usage again increased to 195 gigalitres due to hotter and drier weather conditions, resulting in a $70 million increase in revenue from the previous year.

The factors affecting water and sewer prices are discussed further under 'Further commentary on operations' below.

Community service obligations (CSOs)

SA Water is required to provide a number of non-commercial services to the community on behalf of the SA Government. The SA Government provides SA Water with CSO funding to compensate for these non-commercial activities. CSO revenue increased by $9 million to $145 million in 2018, mainly due to a $5.5 million increase in funding for relocating the waste water pump station at the Osborne naval shipyard, $1.8 million for the acquisition of the Leigh Creek water supply system and $1.2 million to aid safe drinking water to the APY lands. The main CSOs are to compensate SA Water for:

- the shortfall in recovery of costs associated with country water and sewer services (due to the requirement for state-wide pricing). SA Water received $108 million ($108 million) for this CSO in 2018
- the provision of water and sewer exemptions and concessions to certain properties including charities and public schools. SA Water received $18 million ($18 million) for this CSO in 2018
- other payments such as the administration of the Pensioner Concession Scheme, South Australian Government Radio Network and emergency management services, and maintaining water and sewerage services in remote communities.

CSOs are provided under SA Water’s financial ownership framework agreed with the Department of Treasury and Finance.

Other income

Other income increased by $29 million to $186 million.

Other income includes contributed assets and recoverable works, which can vary from year to year depending on economic conditions and government initiatives. The increase in other income for 2018 was due mainly to an increase in the net gain on the disposal of renewable energy certificates of $12 million, following a decision to use carbon offsets instead of renewable energy certificates. Other increases were for recoverable works ($6 million increase for the Riverina program) and fees and charges ($5 million increase) for higher connection volumes associated with strong building applications.

Expenses

Total expenses increased by $114 million to $1.3 billion. The major contributing components were:

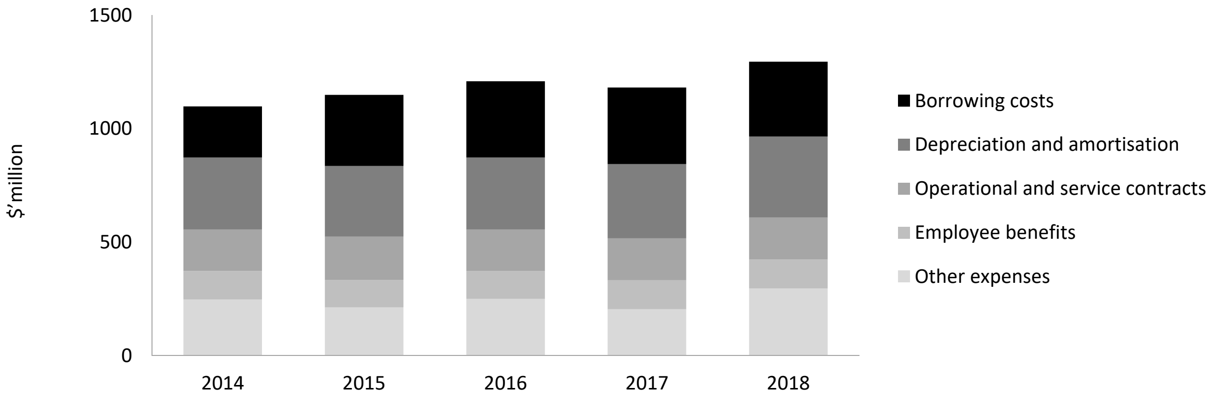
- an increase in services and supplies of 45% or $73 million. This increase mainly reflects:
  - a $38 million write-down in seasonal water allocations. In 2008-09 and 2009-10 the SA Government granted approval for SA Water to purchase temporary seasonal water allocations to be used for critical human water needs for future years in response to the Millennium Drought. In 2017-18 due to a shortage of water held in the Murray-Darling Basin, SA Water was advised by the Department for Environment and Water that the temporary seasonal water allocations were no longer available to carry forward. In 2017-18 a permanent reduction in the remaining water allocation of 120 gigalitres was recognised as an expense

— the write-down of property, plant and equipment increasing by $17 million, due largely to the abandonment of water and sewer mains

— an increase in the ESCOSA license fee of $5 million

- an increase in electricity charges of $19 million due mainly to the removal of electricity charging from the Allwater contract, with a corresponding decrease in operational and service contract expenses. This change was made to eliminate the premium earned by Allwater on electricity charging. Electricity costs also increased due to an underlying increase in price and volume following additional pumping
- an increase in depreciation and amortisation of 9% or $30 million, due mainly to asset revaluations and additions
- a reduction in borrowing costs of $7 million to $330 million due to lower market rates.

The following chart analyses SA Water's main expense items, excluding income tax expense, for the five years to 2018.



Since 2014 expenses have increased by $197 million (18%). Major factors affecting expenses have been:

- increased borrowing costs of $105 million due mainly to the increase in borrowings as a result of a change in SA Water's capital structure. SA Water maintains a debt to asset ratio of 45%
- a $39 million increase in depreciation and amortisation costs, which are highly responsive to asset revaluations and additions.

For other expenses the level of recoverable works varies from year to year depending on economic conditions and government initiatives. In 2018 other expenses increased due to write-downs of $55 million as discussed above.

Employee benefits expenses remained steady over the five years to 2018.

Adelaide Desalination Plant (ADP) operation and maintenance contract

The ADP was a major construction undertaking that commenced in 2008-09. The objective of the project was to construct and operate infrastructure that obtains and treats seawater to produce drinking quality water.

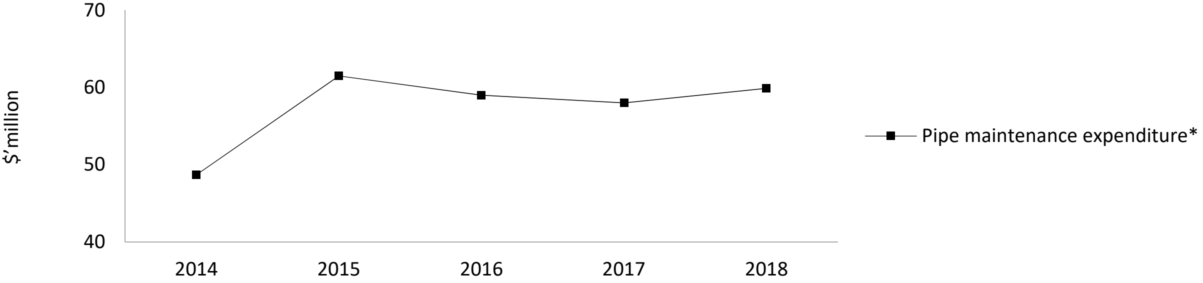
SA Water has major ADP contracts for the:

- operation and maintenance of the desalination plant (O&M contract). The O&M contract is for 20 years from 2012. In 2017-18 expenditure for operating the plant was $20 million ($21 million). There was a minimal increase of water produced by the plant by approximately 0.1 gigalitres to 4.4 gigalitres (4.3 gigalitres) in 2017-18. The slight increase was due to operational requirements
- power to operate the desalination plant. As part of the approval for the ADP, a commitment was made that renewable energy would be used to produce the desalinated water and transfer it to the distribution network. In September 2009 SA Water entered into a 20-year contract for the supply of operational power for the ADP. In 2017-18 expenditure for operational power (including relevant used renewable energy certificates) was $6.7 million.

The total depreciation expense (including intangible assets) for the ADP was $53 million ($55 million) in 2017-18, following a revaluation downwards for the ADP as at 1 July 2017.

SA Water maintenance expenditure

The following chart shows SA Water routine maintenance and repairs expenditure since 2014 on water and sewerage assets.



* Data on specific pipe maintenance expenditure by year provided by SA Water and unaudited.

SA Water's routine maintenance and repairs expenditure, including pipe maintenance, increased from $49 million in 2014 to $60 million in 2018. The pronounced increase in maintenance costs for 2015 was to improve the reliability of pipe infrastructure. There are a number of factors that affect the level of maintenance, including the nature of the pipe being maintained (metropolitan versus country infrastructure), location, age and reason for maintenance. SA Water also has capital expenditure to renew its network, which is described further below.

Pipe bursts data

Maintenance includes the costs of responding to pipe failures, or bursts. The number of bursts over the last four years, with data provided by SA Water and unaudited, is shown in the table below.

	2014-15 Number	2015-16 Number	2016-17 Number	2017-18 Number
Reported pipe bursts:				
Metropolitan	1 805	2 056	1 689	1 693
Country	2 021	1 920	1 968	2 168
Total	3 826	3 976	3 657	3 861

For the time frame shown, the number of water and sewer pipe bursts has remained relatively constant, with country burst rates exceeding those in the metropolitan region and increasing.

The Australian Government Bureau of Meteorology's 'National performance report 2016-17: urban water utilities' reports that SA Water's water main burst rates ranked fifth lowest amongst 14 large urban water utilities.

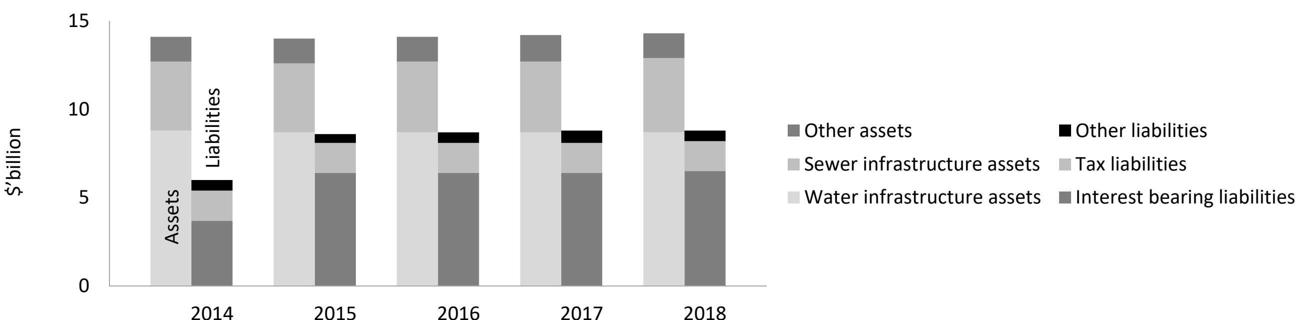
When the data on the number of bursts is considered with the pipe maintenance costs, there has not been a significant increase in maintenance costs due to pipe bursts, which is consistent with SA Water's analysis that the number of bursts is in line with longer-term trends.

Other comprehensive income

Other comprehensive income includes gains and losses on the revaluation of property, plant and infrastructure and available-for-sale financial assets. In 2018 other comprehensive income totalled $73 million ($68 million), principally due to an increase in the value of water and sewer infrastructure assets following their revaluation.

Statement of Financial Position

A structural analysis of assets and liabilities for the five years to 2018 is shown in the following chart.



SA Water's financial position is dominated by non-current water and sewer infrastructure assets and related borrowings and tax liabilities. Since 2014 total assets have increased by $188 million reflecting revaluation increments and additions to water and sewer infrastructure, offset by depreciation.

In 2018 total assets were $14.3 billion, remaining at a similar level to the previous year. Significant movements affecting assets during the year were:

- the acquisition of infrastructure, plant and equipment of $472 million (including water and sewer pipe network renewal). Major capital expenditure includes completed water infrastructure projects of $210 million and sewerage infrastructure projects of $153 million
- a net $100 million revaluation upwards of infrastructure, plant and equipment. This was due mainly to revaluation increments of $32 million for water infrastructure, $56 million for sewer infrastructure and $8 million for land and buildings.

  The increases in value for the water and sewer infrastructure are the result of applying generally increased unit rates for water and sewer mains and connections to SA Water's network. The rates were determined by independent valuers and reflect modern equivalent replacement costs for the existing assets.

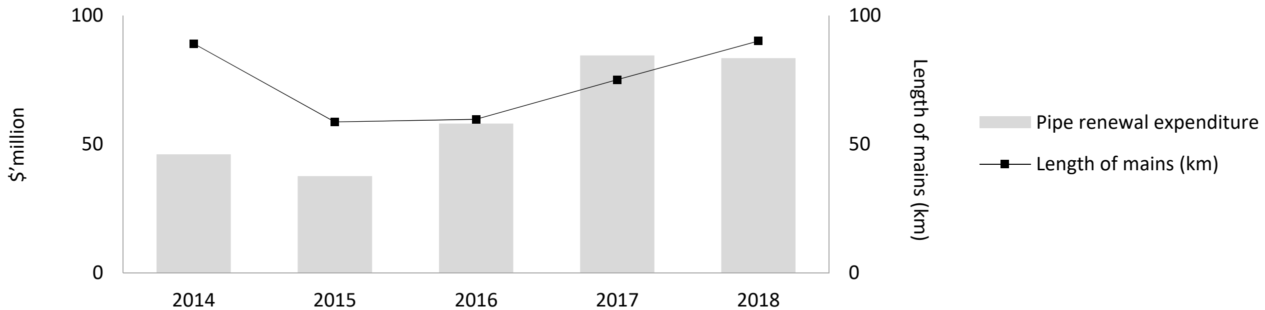
The net upwards revaluation included a decrement to the ADP value of $67 million. The plant was independently revalued for the first time in 2017-18. Since its inception in 2012 the plant has been revalued annually using a producer price index. This has resulted in a total valuation upwards since 2012 of $177 million, or around 2.2% p.a. The 2017-18 independent valuation represented an 8% increase in the construction costs compared to 2012, but below the accumulated value of indexation increases. This resulted in a write-down in the value of the ADP to $1.509 billion

- depreciation and amortisation charges of $357 million
- a $32 million for asset write-downs of water and sewer infrastructure.

In 2018 liabilities increased by $34 million due mainly to increased borrowings of $56 million to fund capital expenditure, partially offset by a decrease in unearned customer contribution of $17 million following the recognition of deferred augmentation revenue in 2017-18. This revenue relates to amounts payed by SA Water customers for future enhancements to pipe infrastructure which are required to be recognised on receipt. SA Water had previously recognised this revenue when works were complete.

Renewal of the water and sewer pipe networks

The following chart shows SA Water's pipe network renewal (based on data provided by SA Water) for both water and sewer pipes, which includes major projects for each year and the length, in kilometres of mains replaced, of water reticulation pipes only.



The chart shows that expenditure for renewal has increased since 2015, after reducing from 2014 levels. The total length of water pipes renewed has also increased since 2015. This follows an initiative to accelerate the replacement of ageing pipe infrastructure from 2016.

Current assets and liabilities

At 30 June 2018 current liabilities amounted to $293 million, exceeding current assets of $237 million by $56 million. While such a deficiency in working capital can be of concern, SA Water has a strong cash flow position from operating activities and access to sufficient borrowing facilities with the South Australian Government Financing Authority (SAFA), which would enable all of its current liabilities to be met. A large component of current liabilities is payables, comprising 72% (70%) of the balance, which includes obligations for capital purchases.

Statement of Cash Flows

While cash increased marginally to $4 million, SA Water's cash position is subject to significant inflows and outflows associated with its operating, investing and financing activities. Factors affecting

cash flows include:

- receipts from customers of $1.4 billion, largely reflecting water and sewerage charges
- investment in the construction and purchase of infrastructure, plant and equipment and intangible assets. In 2018 investing payments for assets amounted to $438 million ($300 million) representing a number of large infrastructure projects
- payment of a cash dividend to the SA Government of $139 million ($193 million) in 2018
- increased net borrowings. In 2018 cash inflows from net borrowings were $66 million ($95 million).

Further commentary on operations

Financial ownership framework, charter and performance statement

SA Water operates under a financial ownership framework, charter and performance statement, all approved by the Treasurer and Minister.

The performance statement defines the contribution to the SA Government in terms of dividends, repayment of capital, income tax equivalents and other rates and taxes. The key financial performance measures agreed to in the performance statement are set out in the following table.

Performance measure	Target 2017-18	Actual results 2017-18
Profit ($'million)	208.7	201.6
Tax expense ($'million)	62.6	58.4
Dividend ($'million)	138.8	139.4
Total contribution ($'million)	201.4	197.8
Gearing ratio (%)*	45	45

* Total interest bearing debt (including borrowings and lease liabilities) divided by total assets.

SA Water's total contribution was $3.6 million below the performance statement target of $201.4 million.

The performance statement and financial ownership framework feature a dividend payout ratio of 95% based on after tax profit, CSO payments from the SA Government to support non-commercial services and the maintenance of a gearing ratio of 45%.

The following table summarises movements in the major items influencing borrowings.

	2014 $'million	2015 $'million	2016 $'million	2017 $'million	2018 $'million
Net cash inflows from operating activities	469	454	504	395	487
Net cash outflows from investing activities	(286)	(246)	(295)	(290)	(413)
Surplus (Shortfall in) cash from operations after investing activities	183	208	209	105	74
Dividend payments to owners	(196)	(184)	(205)	(193)	(139)
Surplus (Shortfall in) funds to pay for dividends and investing activities	(13)	24	4	(88)	(65)
Net increase in borrowings	19	(17)	6	95	66

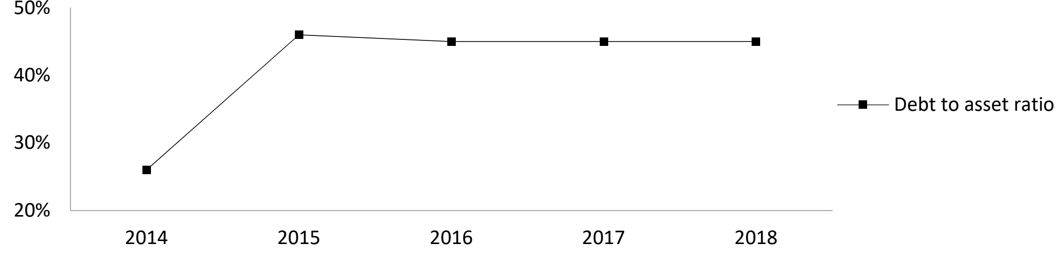
There were small changes in net borrowings between 2014 and 2016. The $95 million increase in net borrowings in 2017 followed a direction from the Treasurer under section 30(5) of the *Public Corporations Act 1993* for an interim dividend of $71 million.

In 2015 the Treasurer recommended to the SA Water Board that an interim dividend of $2.7 billion be paid to the Consolidated Account, funded by the transfer of debt. This increase in SA Water's total debt was designed to bring its debt to asset gearing ratio to 45%, a value consistent with interstate statutory water corporations. The table above does not show the impact of the $2.7 billion increase in borrowings because it relates to a non-cash transfer.

Net borrowings increased by $66 million to $6.4 billion in 2018, representing additional borrowings for capital expenditure and working capital requirements.

In 2015 the Treasurer also approved an increase in SA Water's core debt facility limit with SAFA to $6.43 billion, reflecting the change required from the debt transfer. The Treasurer also approved amendments to SA Water's interest rate risk management policy and liquidity risk management policy and an increase in SA Water's working capital facility limit with SAFA to $150 million, up from $100 million, to be reviewed every two years. In 2018 the Treasurer approved an increase of the core debt facility limit with SAFA by $608 million to $7.04 billion for future requirements.

The following chart shows movements in the debt to asset ratio for the five years to 2018 and demonstrates the impact of the decision to increase SA Water's asset gearing ratio to 45% in 2015.

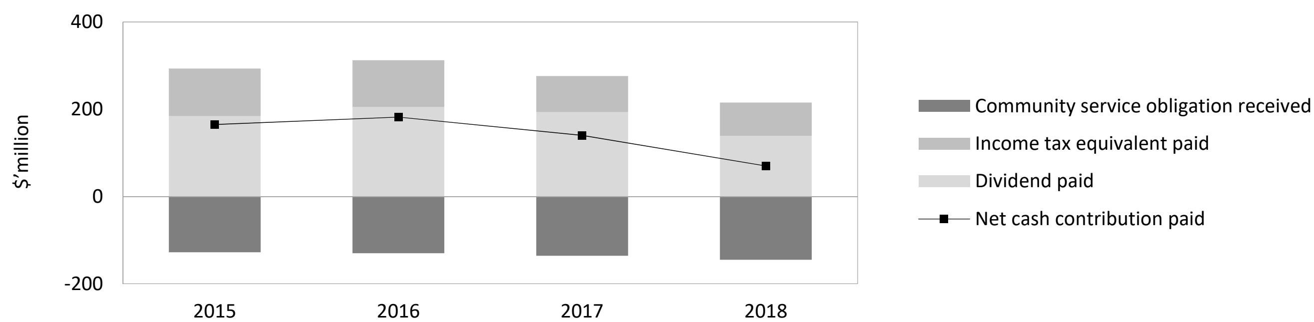


The 2017-18 State Budget included a decision to maintain SA Water's debt to asset ratio at 45%.

SA Water returned a dividend of $139 million ($193 million) calculated at 95% of profit in line with the financial ownership framework.

Income tax equivalent amounts of $76 million ($83 million) were also paid in 2017-18.

A structural analysis of SA Water's cash contributions (dividends, income tax equivalent) to the SA Government and CSO funding provided by the SA Government for the four years to 2018 is shown in the following chart. As the $2.7 billion debt transfer in 2015 was not a cash transaction, it is not included in the chart.



The chart shows the amount of money returned to the SA Government through income tax equivalent and dividend payments reducing since 2016.

The decrease in 2018 recognises the $54 million decrease in dividends paid.

Comparison with other water utilities

As discussed above, when announcing the initial $2.7 billion dividend the SA Government noted that the revised arrangements would bring, or maintain, SA Water's debt arrangements into line with other interstate water utilities. SA Water's debt to asset ratio at 30 June 2018, in line with the policy, is 45%.

The table below details the gearing ratio for four major water utilities from around Australia as at 30 June 2017.

	SA Water	Sydney Water	Water Corporation of Western Australia	Yarra Valley Water	Unitywater
Total debt ($'billion)	6.445	7.659	5.885	2.263	1.558
Total assets ($'billion)	14.195	18.078	17.153	4.731	3.620
Gearing ratio (%)	45	42	34	48	43

SA Water's revised gearing ratio is similar to those of Yarra Valley Water in Victoria, Sydney Water and Unitywater in Queensland.

Water and sewer rates and charges

Essential Services Commission of South Australia

Under the *Water Industry Act 2012* (the WI Act) ESCOSA is appointed as the independent economic regulator for the South Australian water industry. ESCOSA commenced its role as regulator on 1 January 2013. SA Water operates within the requirements of the WI Act by holding a licence, and continuing to provide water supply and sewerage services.

Under the WI Act, ESCOSA is responsible for making price determinations. In making them, the WI Act requires ESCOSA to comply with the requirements of any pricing order issued by the Treasurer under the WI Act.

Pricing orders

Under the WI Act, the Treasurer has issued a number of pricing orders since September 2012. They have specified that ESCOSA is to determine the revenue (not price) that may be derived from the provision of drinking water and sewerage retail services (separately).

Both the first regulatory period (1 July 2013 to 30 June 2016) and the second regulatory period (1 July 2016 to 30 June 2020) included the requirement that ESCOSA adopt specified values for SA Water's retail water and sewerage regulatory asset bases (RAB), at $7.77 billion and $3.58 billion respectively as at 1 July 2013 (in December 2012 dollars).

The first regulatory period (1 July 2013 to 30 June 2016) had a 190 gigalitre drinking water demand forecast for each year. For the second regulatory period (1 July 2016 to 30 June 2020), the demand forecast was set each year ranging from 190.1 gigalitres for 2016-17 to 194.5 gigalitres for 2019-20. As discussed earlier, actual water demand in 2017-18 was 195 gigalitres (176.2 gigalitres).

SA Water sets annual water and sewerage charges to achieve the revenue limits determined by ESCOSA, with ESCOSA then monitoring SA Water's performance.

ESCOSA determinations

In June 2016 ESCOSA issued a final determination establishing the maximum revenue that can be recovered by SA Water for the provision of drinking water and sewerage retail services for the four years commencing 1 July 2016.

The determination set SA Water's maximum allowable revenue for drinking water retail services at $3.12 billion over the four years (averaging $780 million p.a.) and $1.3 billion for sewerage retail services (averaging $326 million p.a.). These amounts are based on December 2014 dollars.

SA Water pricing

SA Water is responsible for setting the prices charged to consumers during the regulatory period based on maximum allowable revenues. Those prices must comply with ESCOSA's revenue determination.

ESCOSA's 2016-2020 revenue determination set four-year total revenue caps for water and sewerage services. Both caps are subject to a demand adjustment mechanism if actual water sales or sewerage connections are materially different to forecasts. Compliance with these caps, including any demand adjustments required, will be assessed at the end of the regulatory period that ends on 30 June 2020. SA Water prices vary according to customer type. The charges for water for residential customers for the five years to 2018-19 are detailed below.

Residential water charges	2014-15 $	2015-16 $	2016-17 $	2017-18 $	2018-19 $
First tier: first 0.3288 kL per day	2.32/kL	2.35/kL	2.27/kL	2.32/kL	2.36/kl
Second tier: from 0.3288 kL to 1.4247 kL per day	3.32/kL	3.36/kL	3.24/kL	3.31/kL	3.37/kl
Third tier: over 1.4247 kL per day	3.59/kL	3.63/kL	3.51/kL	3.58/kL	3.65/kl
Annual residential water supply charge per year	282.80	286.40	286.40	292.40	297.80

As discussed above, 2016-17 was the first year of the second regulatory period. ESCOSA has set maximum levels of revenue for drinking water and sewerage services across the regulatory period (1 July 2016 to 30 June 2020) of $3.12 billion and $1.3 billion respectively. This resulted in a reduction in residential water charges of approximately 3.5% in 2016-17 (apart from the annual residential water supply charge per year). In 2017-18 the residential water charges increased by 2.1% and in 2018-19 charges will increase by 1.9%.

Asset value accounting matters – RAB differs from financial report

When determining the prices for water and sewerage services ESCOSA considers the appropriate RAB. As detailed above, the opening RAB value at the beginning of regulation was determined by the Treasurer in the second pricing order. Each year the RAB is then rolled forward based on regulatory principles to adjust for net capital additions, disposals and depreciation.

The RAB differs from the value of assets reported in SA Water's financial report. The total RAB assets as at 1 July 2013 as specified in the pricing order were $11.35 billion in December 2012 dollars (comprising $7.77 billion for water services and $3.58 billion for sewerage services). This compared to SA Water's total assets at 30 June 2013 of $13.8 billion.

Under the current regulatory parameters the RAB, as initially determined by the Treasurer, is the value of assets on which regulatory revenues are determined.

Regulatory accounting statements

SA Water is required to submit regulatory accounting statements to ESCOSA. Under Water Industry Guideline 2 'Water regulatory information requirements for major retailers', issued under section 8 of the *Essential Services Commission Act 2002*, ESCOSA has specified requirements for major retailers for the collection, allocation, recording and reporting to ESCOSA of regulated business data in line with Guideline 2. Under Guideline 2, SA Water is required to submit special purpose financial statements.

Department of State Development (DSD)

Financial statistics

Net cost of providing services:	$670 million
Revenues from SA Government:	$675 million
Fees and charges:	$66 million
Grants and subsidies:	$557 million
Supplies and services:	$102 million
Employee benefits:	$76 million
Number of FTEs:	627

Significant events and transactions

- DSD provided total funding to TAFE SA of $246 million, which covered the provision of vocational education and training and other grant funding.
- On 1 July 2018, following the State election:
  - DSD's name changed to the Department for Industry and Skills
  - a new department, the Department for Trade, Tourism and Investment (DTTI), was established
  - International Engagement and Health Industries South Australia transferred from DSD to DTTI
  - Investment Attraction South Australia was abolished and the functions transferred to DTTI
  - Arts South Australia and Aboriginal Affairs and Reconciliation transferred from DSD to the Department of the Premier and Cabinet.

Financial report opinion

Unmodified

Financial controls opinion

Modified

Key issues:

- Funding arrangements with some statutory authorities were not correctly approved
- Grant payments were made to recipients before an agreement was in place
- Improvement required in the grant acquittal process
- Key payroll reports were not always reviewed promptly
- WorkReady compliance processes could be improved
- Contractual arrangements entered into without appropriate support

Structure of DSD

The Chief Executive of DSD is responsible to the Premier and the:

- Minister for Industry and Skills
- Minister for Trade, Tourism and Investment.

Functional responsibility

DSD is an administrative unit established under the *Public Sector Act 2009*.

The main function of DSD is to drive economic growth and create jobs while supporting South Australia's economic transformation.

Full details of DSD's objectives are contained in note 2 of its financial report.

Scope of the audit

The audit program covered major financial systems to obtain sufficient evidence to form an opinion on the financial report and internal controls.

Specific areas of audit attention in 2017-18 included:

- expenditure, including funding to TAFE SA and private service providers, grants and accounts payable
- employee benefits and payroll processing
- revenue from fees and charges
- property, plant and equipment
- cash management, including bank reconciliations
- general ledger.

The audit took into account the controls and procedures performed by service providers including Shared Services SA (SSSA).

The work of DSD's internal auditors was also considered in planning and conducting the audit.

Audit findings and comments

Assessment of controls

In my opinion, the controls exercised by the Department of State Development in relation to the receipt, expenditure and investment of money, the acquisition and disposal of property and the incurring of liabilities, except for all matters outlined under 'Communication of audit matters', are sufficient to provide reasonable assurance that the financial transactions of the Department of State Development have been conducted properly and in accordance with law.

Communication of audit matters

Grant payments – Arts South Australia

Arts South Australia oversaw grant payments of $145 million in 2017-18. They are provided to a range of artistic and cultural institutions, including government statutory bodies.

Funding arrangements with some statutory bodies were not correctly approved

Arts South Australia enters into annual funding agreements with a number of statutory bodies. The Treasurer's Instructions capture arrangements like these and require Cabinet approval for arrangements over $15 million.

The Executive Director of Arts South Australia, who approved the funding arrangements for the Libraries Board of South Australia for a total of $34.1 million, did not have the authority to sign a memorandum of administrative arrangements (MoAA) of this value.

We acknowledge these arrangements are reflected in the State Budget and are longstanding, however the approval was not consistent with Treasurer's Instruction requirements.

We raised this issue in 2016-17 and Arts South Australia sought a variation to Treasurer's Instruction 8 'Financial Authorisations' (TI 8) from the Treasurer, which was approved in March 2018. Particularly given this background, the funding for 2017-18 should have been approved by the Minister or Cabinet, as they were the only parties with authority to approve an arrangement for this amount.

DSD responded that shortly after we raised the issue in 2017, Arts South Australia sought a variation to TI 8. The Treasurer approved a variation for the Chief Executive, DSD and the Executive Director, Arts South Australia to approve funding arrangements with arts statutory authorities within government up to $40 million (GST inclusive). Arts South Australia was notified of the variation in March 2018.

The response also noted that Arts South Australia would ensure all contracts were signed by an officer with the appropriate authority.

Grant payments were made to recipients before an agreement was in place

We identified two instances where operating grant payments were made before a signed agreement was in place.

In 2017-18, Arts South Australia provided operating grants to the Adelaide Festival Centre Trust (AFCT) without a signed MoAA. As at January 2018, Arts South Australia had paid $17.7 million to the AFCT. We acknowledge that the funding to the AFCT is consistent with the State Budget.

In the second instance, Arts South Australia paid an operating grant to Carclew Youth Arts Incorporated under a one-year funding agreement. The payment, a one-off lump sum of $2.6 million, was made on 11 July 2017, before the agreement was executed on 11 September 2017.

Paying funds before the terms and conditions of the funding agreement have been agreed increases the risk of mismanaging allocated funds, and Arts South Australia and the grant recipient may be unclear of their obligations in the event of a dispute.

DSD responded that in the absence of an executed grant agreement, terms and conditions will be agreed in an exchange of letters.

Improvement required in the grant acquittal process

A condition for organisations who receive grant funding from Arts South Australia is that they provide an acquittal report within three months of the project end date.

During our review of the list of overdue acquittal reports for the Contemporary Music program (generated as at February 2018), we noted that a number of applications were approved for future grants despite having acquittal reports that were long overdue from previous projects.

We found one instance where a grant recipient received funding totalling $40 000 for four different projects dating back to 2015. However as at February 2018 they had overdue acquittals for all four projects.

There is a risk that applicants who have not submitted an acquittal report may receive further funding.

DSD responded that this issue was addressed by its new grants management system, as there is a system control that does not allow a new application if there are outstanding acquittals.

DSD also advised it would hand over all audit findings relating to Arts South Australia to the Department of the Premier and Cabinet (DPC) as part of the machinery of government changes that take effect from 1 July 2018.

Payroll

Key payroll reports not always reviewed promptly

DSD had total employee benefits expenses of $76 million in 2017-18 and employee benefits liabilities at 30 June 2018 were $23 million.

We found DSD did not have a monitoring control to ensure bona fide certificates were reviewed promptly. In addition, only two of the eight bona fide certificates we sampled were reviewed in the time frames established by DSD policy. A further two of the sample were not provided at all, despite our repeated requests.

These findings are consistent with the results of our audits in previous years.

Delayed review of these key payroll reports increases the risk of financial loss to DSD from inaccurate processing of payroll and leave payments through the payroll system.

DSD responded that it would implement an automated bona fide and leave report solution as part of a series of payroll system enhancements.

DSD also advised it would work with the business units that did not provide the sampled reports to obtain them, although we note they remain outstanding at the time of this Report.

Payments to WorkReady service providers

Total payments to private service providers under WorkReady vocational education and training (VET) programs for 2017-18 were $36 million. In addition to those payments, we reviewed payments under the $6 million Jobs First Employment Programs (JFEP) scheme, a non-VET program also funded through WorkReady.

Compliance audits could be improved to ensure the existence of accredited training participants

The Commonwealth Government is responsible for overall regulation of the VET sector, while DSD has its own regulation functions for its funded programs, including WorkReady. One Commonwealth Government requirement is that each training participant is assigned a unique student identifier (USI). Recognised forms of Australian identification must accompany any application for a USI.

DSD's regulation unit requires service providers to confirm that the Commonwealth requirements have been met for training participants as part of its compliance program, but does not obtain the supporting data for USIs to verify their validity.

Confirming the USI data would help to reduce the risk of paying private service providers for fictitious participants.

DSD responded that the system capability to verify participant information using a connection to the USI Registry Systems provided by the USI Registry Office was implemented in January 2018.

DSD advised that the requirement for students to register for a USI to obtain a qualification had been in place since 2015. The ability to verify participant information commenced in 2017. DSD also noted that not all participant students will require a USI as they can undertake individual training units without it.

DSD's Quality and Compliance team checks that participants have USIs on the providers' paperwork when compliance audits are performed on providers.

Compliance audits could be expanded

DSD's Skills and Employment division has a compliance framework that is designed to ensure consistency in quality and compliance activities for WorkReady programs.

We noted that the compliance framework was not applied to non-accredited training activities such as JFEP in 2017-18, while it was applied to accredited (VET) services.

As a result, there was a greater risk of non-accredited service providers not complying with their contractual obligations, as there was less focused compliance activity from DSD for those areas.

DSD responded that JFEP would no longer be offered from 1 July 2018, but otherwise interim controls had been implemented to minimise risk. DSD advised it would apply the quality and compliance monitoring framework to any future funding programs.

Memorandum of administrative arrangements with TAFE SA not appropriately approved

For the past two years, we have reported that the MoAA for non-commercial services between DSD and TAFE SA did not comply with TI 8.

In February 2017, DSD received approval from the Treasurer for a variation to the requirements of TI 8 for 10 years commencing from 2012. This enabled the responsible Ministers for DSD and TAFE SA, instead of Cabinet, to enter into an MoAA for the WorkReady program where the associated expenditure authority had been approved by Cabinet up to a total value of $200 million p.a.

The 2017-18 MoAA, valued at $225.4 million, was once again entered into by the Chief Executive of DSD in February 2018, although we were not provided with any evidence that the Minister delegated that authority to the Chief Executive.

In addition, the variation from the Treasurer only provides for payments to TAFE SA up to $200 million each year. Therefore, the 2017-18 MoAA provides for expenditure that is $25.4 million more than the varied limit.

To comply with TI 8, the 2017-18 MoAA would need to be approved by Cabinet.

DSD responded that in November 2012, the SA Government approved the former Department of Further Education, Employment and Science Technology executing an MoAA with TAFE SA for the provision of VET services up to $1.5 billion over a five-year contract term.

In February 2017, the Chief Executive of DSD sent a minute to the Chief Executive of DTF seeking approval from the Treasurer to extend the variation to TI 8 for a further five years and recommended an upper limit of around $200 million each year, consistent with budget settings at that time.

In recognition of updated budget settings (relating primarily to the sale and leaseback of VET infrastructure), the Chief Executive of the Department for Industry and Skills (DIS) (formerly DSD) wrote to the Chief Executive of DTF seeking approval from the Treasurer for an amount of up to $300 million each year for five years from November 2017. Once approved, DIS will seek Ministerial approval to formally delegate to the Chief Executive of DIS the authority to execute the MoAA with TAFE SA.

Contractual arrangements entered into without appropriate support

DSD had contractor expenses of $6 million in 2017-18 and paid $40 million in grants to industry, innovation, science and small business recipients in 2017-18.

The engagement of one contractor and awarding of one grant that we examined in 2017-18 were not supported by appropriate documentation.

DSD entered into a contractual arrangement for strategic advice to be provided to DSD and the SA Government and, under the contract, had paid $400 000 since 2017 to the contractor. DSD advised us that it was responsible for finalising the arrangement following initial negotiations with DPC.

DSD also advised that DPC did not provide any documentation to support a direct negotiation approach.

Similarly, DSD made a grant payment to Australian Defence Accelerator Limited to operate accelerator programs for start-up companies seeking to bring new technologies to market. We understand that Australian Defence Accelerator Limited approached the SA Government but DSD could not provide any evidence that the unsolicited proposals process established by Premier and Cabinet Circular PC038 ‘Unsolicited Proposals’ was followed.

In both these arrangements there is a risk that DSD did not follow the appropriate steps to ensure value for money would be obtained from the proposals. In the case of the grant payment, there was no business case prepared that assessed the proposal against a broader market approach, as opposed to direct negotiation.

DSD responded that, in both instances, it was not given the opportunity to follow its policies due to directions provided to it and it had reminded its staff of their responsibilities for procurement.

Shared Services SA – financial systems and transaction processing environments

SSSA processes financial transactions on behalf of DSD under service level determinations. The main systems and control environments include accounts payable, payroll and general ledger financial functions.

Our review and evaluation of controls for these systems concluded that controls were effective for 2017-18.

SSSA is discussed further in the commentary under 'Department of the Premier and Cabinet' in this Report.

Interpretation and analysis of the financial report

Highlights of the financial report

	2018 $'million	2017 $'million
Expenses		
Grants and subsidies	557	524
Employee benefits expenses	76	103
Net loss from disposal of non-current assets	-	116
Supplies, services and other expenses	117	121
Total expenses	750	864
Income		
Revenues from fees and charges	66	71
Commonwealth revenues	-	39
Other revenues	14	14
Total income	80	124
Net cost of providing services	670	740
Revenues from (Payments to) SA Government		
Revenues from SA Government	675	588
Payments to SA Government	-	(612)
Net result	5	(764)
Net cash provided by (used in) operating activities	1	(681)
Assets		
Current assets	113	138
Non-current assets	229	187
Total assets	342	325
Liabilities		
Current liabilities	36	47
Non-current liabilities	18	19
Total liabilities	54	66
Total equity	288	259

Transfer of some DSD functions to the Department of the Premier and Cabinet in 2016-17

A number of DSD business units transferred to DPC effective from 1 April 2017. DSD's financial statements include the transactions for these activities for the nine months from 1 July 2016 to 31 March 2017. The last three months of the year and the full-year financial results for these activities were shown in DPC's financial report in 2016-17.

Sale of property leased to TAFE SA to the Urban Renewal Authority in 2016-17

The 2016-17 State Budget announced the SA Government's intention to transfer ownership of TAFE SA sites from DSD to the Urban Renewal Authority (URA). The transfer of land and buildings that DSD was holding (with a fair value, being the written down replacement cost, of $708 million) occurred on 1 March 2017.

DSD received $595 million in proceeds from the URA, based on an independent valuation using future rental income estimates to determine fair value. The difference between the valuation undertaken by the URA and DSD's carrying value reflects that DSD valued the sites on the basis of depreciated replacement cost while the URA, as a for-profit entity, values the properties based on their income generating potential.

DSD recognised a loss on sale of $113 million, representing the difference between its carrying amount and the amount paid by the URA. The proceeds were then transferred to the Consolidated Account and are reflected as payments to the SA Government in DSD's Statement of Comprehensive Income.

DSD has entered into a lease back arrangement for the sites with the URA. Rental fees of around $52 million p.a. will be incurred by DSD from 1 March 2017. The commencement of this lease arrangement increased DSD's accommodation and service costs by $17 million in 2016-17.

DSD will continue to lease these assets to TAFE SA, recovering the full lease costs payable to the URA from TAFE SA. Under this arrangement DSD controls the use of VET infrastructure facilities in line with its responsibility for VET policy.

DSD's accommodation and service charges increased by $33 million in 2017-18 mainly due to full-year lease payments to the URA (increase of $36 million) offset by a reduction in accommodation costs for the business units transferred to DPC in 2016-17.

In addition, infrastructure recharge revenue from TAFE SA increased by $22 million due to the full-year impact of the leasing arrangements with the URA. These were offset by an equivalent increase in grants and subsidy payments to TAFE SA.

Statement of Comprehensive Income

Expenses

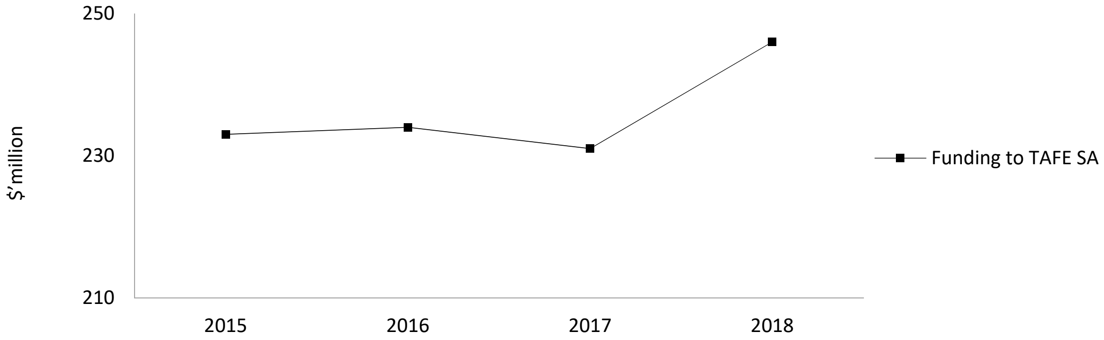
Total expenses for 2017-18 decreased by $114 million to $750 million. The main expenses were grants and subsidies of $557 million ($524 million), supplies and services of $102 million ($87 million) and employee benefits of $76 million ($103 million), which collectively account for 98% (83%) of total expenses.

As noted above, in 2016-17 expenditure included a loss on sale from the disposal of assets transferred to the URA of $113 million.

Grants and subsidies

Funding to TAFE SA

Grants and subsidies to TAFE SA totalled $246 million ($231 million) for 2017-18. The following chart shows that total funding provided to TAFE SA was steady from 2015 to 2017 but increased (by $15 million) in 2017-18.



The amounts shown in the chart include a number of elements, primarily VET subsidies, structural support, capital grant funding and targeted voluntary separation package support.

An MoAA for non-commercial services between DSD and TAFE SA provided for TAFE SA to receive $226 million for various activities, including delivering VET courses, payments for community services that TAFE SA performs and other grant amounts.

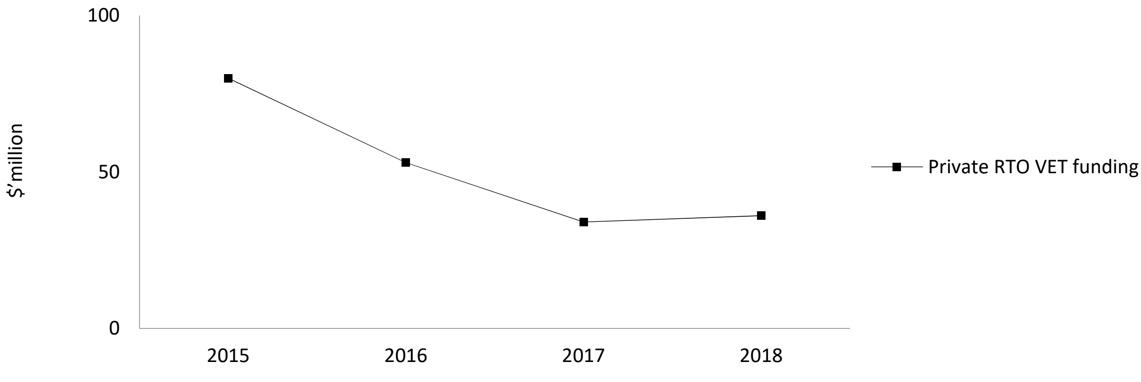
The MoAA clearly identifies that the funding arrangement is an interim arrangement for 2017-18 only, and recognises the timing of the MoAA execution and significant events that have occurred leading to reviews of TAFE SA's operations.

In addition, TAFE SA received funding of $5 million, subject to a separate agreement, for excess staff costs. These amounts are paid to TAFE SA to meet excess employee costs while TAFE SA transitions its business to a more competitive structure.

Most of the remaining $15 million in funding to TAFE SA was for capital grants ($4 million) and targeted voluntary separation package reimbursements ($9 million), which are subject to separate arrangements.

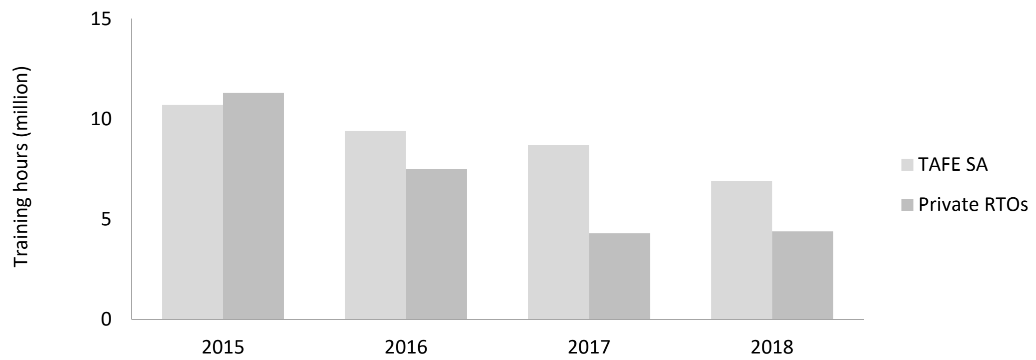
Other VET funding

DSD also provides VET funding to private registered training organisations (RTOs). The chart below shows the total private RTO VET funding for the last four years.



Funding to private RTOs decreased from 2015 to 2017 and remained steady in 2018. The overall reduction in funding to private RTOs reflects the smaller number of subsidised courses under the WorkReady subsidised training list and the focus on supporting TAFE SA to transition its business.

The following chart illustrates the number of training hours funded by DSD through Skills for All and WorkReady over the past four years, split between TAFE SA and private RTOs.



Source: Data on the number of funded training hours has been provided by DSD and is unaudited.

The chart shows that total funded training hours have decreased over the last four years, reflecting decreased WorkReady funding. The chart also illustrates that the level of funded training hours for private RTOs reduced at a greater rate than funded training hours for TAFE SA between 2015 and 2017. This reduction reflects the smaller number of subsidised courses under the WorkReady subsidised training list, and the focus on supporting TAFE SA to transition its business to a more competitive structure.

Arts and cultural grants

Arts and cultural grants increased by $13 million to $145 million in 2017-18. A substantial portion of these grants is paid to SA Government statutory authorities. Payments to the Libraries Board of South Australia, AFCT, Art Gallery Board and Museum Board account for 59% of the total expenditure.

The major movements in arts and cultural grants in 2017-18 included an increase in funding to the AFCT of $6.5 million as revenue supplementation for the Adelaide Festival Centre and car park due to closures while the precinct was being redeveloped.

Other grants

Other major categories of grants include skills and employment grants of $51 million ($47 million) and industry, innovation, science and small business grants of $40 million ($42 million). These grants generally include specific milestones or deliverables that are monitored by DSD.

Further, DSD provided funding to Investment Attraction South Australia (IASA) of $25 million ($22 million).

Resources and energy grants of $6 million were paid in 2016-17. These transferred from DSD to DPC from 1 April 2017.

Skills and employment grants and subsidies include funding of the Tertiary Students Transport Concession Scheme, JFEP and grants to the Tauondi College for workforce development program funding.

Industry, innovation, science and small business grants include payments for the Our Jobs Plan program totalling $8 million, of which $2 million was a payment for the Next Generation Manufacturing Investment Programme. This payment was the SA Government's contribution to the Commonwealth Government's $90 million Next Generation Manufacturing Investment Programme, which is designed to help accelerate manufacturing investment in South Australia and Victoria.

$3 million was spent on programs under the Automotive Transformation Taskforce initiative in 2017-18. This initiative, which commenced in 2013-14, has two components.

The Automotive Supplier Diversification program administered by DSD assists automotive supply chain manufacturers impacted by Holden ceasing manufacturing in Australia. The program started in 2013-14 and $5 million in grants had been provided to 30 June 2018, to help automotive supplier firms to diversify and secure alternate revenue streams.

The Automotive Workers in Transition program provided funding for workers from automotive component supply chain companies affected by the Holden closure to access professional career advice and training for a new job. This program started in 2014-15 and $1 million in grants had been provided to 30 June 2018.

Other payments for industry and innovation include grants of $11 million to TechInSA, $4 million for business expansion grants from the Small Business Development Fund in selected northern areas and $3 million to the Premier's Research and Industry Fund. The Premier's Research and Industry Fund encouraged investment in key science and research areas through grant funding for significant research collaborations, small to medium enterprise research projects and cooperative research centres.

The 2018-19 State Budget announced that a number of these programs would end, including the Automotive Supplier Diversification program and the Premier's Research and Industry Fund.

Income

DSD is predominantly funded by appropriation. Revenues from the SA Government were $675 million ($588 million), 89% (83%) of its total income. The increase in SA Government funding mainly reflects an increase in funding for the Adelaide Festival Centre precinct upgrade of $36 million and an increase in funding for grants and subsidies to TAFE SA of $15 million.

DSD's other significant income streams were revenues from fees and charges which decreased by $5 million to $66 million ($71 million).

Revenues from fees and charges mainly relate to infrastructure recharges from TAFE SA of $54 million ($32 million), paid to reflect TAFE SA's use of assets previously owned by DSD and transferred to the URA on 1 March 2017 to deliver training. The increase in these fees reflects the first full year of these arrangements following the sale to, and leaseback of assets from, the URA. DSD pays the URA commercial rates for the use of these assets and in turn leases the assets to TAFE SA.

The increase in infrastructure recharges was offset by a decrease in mining and petroleum application fees, rentals and licences of $16 million due to the transfer of these functions to DPC as at 1 April 2017.

Commonwealth revenue decreased by $38 million due to the National Partnership Agreement on Skills Reform Agreement ending on 30 June 2017.

Statement of Financial Position

The most significant items in the Statement of Financial Position are shown in the following table.

	2017 $'million	2018 $'million
Assets		
Cash and cash equivalents	115	99
Property, plant and equipment	167	209
Liabilities		
Payables	40	29
Employee benefits	24	23

Property, plant and equipment represents 61% (51%) of total assets, with cash and cash equivalents representing a further 29%.

The increase in property, plant and equipment is mainly due to expenditure on the Adelaide Festival Centre precinct redevelopment.

The decrease in payables is mainly due to a decrease in capital accruals.

Statement of Cash Flows

Cash and cash equivalents at 30 June 2018 total $99 million ($115 million). Of this amount, $55 million ($108 million) is held in DSD's operating account and $45 million ($7 million) is held in the Accrual Appropriations Excess Funds Account, which is not available for general expenditure.

Cash and cash equivalents mainly decreased due to capital expenditure for works associated with the Adelaide Festival Centre precinct redevelopment.

Administered items

Until 1 April 2017, DSD administered the collection of $148 million in royalties levied on mineral and petroleum production on behalf of the SA Government. This function was then transferred to DPC.

Further commentary on operations

Investment Attraction South Australia

The Public Sector (Investment Attraction South Australia) Proclamation 2016 (dated 10 March 2016) established IASA as an attached office of DSD effective from 1 April 2016.

IASA was the lead SA Government body for all major investment attraction activity from both overseas and interstate companies. Its main focus was to attract foreign direct investment to increase economic development and create jobs in South Australia.

In 2017-18 IASA provided $14 million ($6 million) in grants. This included expenditure for 10 new grant recipients.

Payments included:

- $3.7 million to VeroGuard Systems to relocate operations to South Australia, construct an advanced manufacturing centre and global network operations in northern Adelaide
- $2.4 million to Datacom to establish a Datacom customer contact centre in Adelaide.

Effective from 1 July 2018, IASA was abolished and its remaining functions transferred to the Department for Trade, Tourism and Investment.

Superannuation sector overview

South Australian public sector superannuation

The SA Government and its controlled entities contribute to defined benefit and defined contribution superannuation schemes for their employees.

Defined benefit schemes provide post-employment benefits to members as defined by the relevant scheme rules. The main defined benefit schemes are now closed to new members.

Defined contribution schemes are post-employment benefit schemes under which the employer pays fixed contributions into a fund. The amount of benefits payable to members depends on a number of factors such as the amount of member and employer contributions, investment earnings and fees charged to the member's account.

The Auditor-General audits the following South Australian public sector superannuation schemes.

Scheme	Type	Membership/Beneficiaries
South Australian Superannuation Scheme (SASS)	Hybrid (defined benefit and defined contribution)	***Pension Scheme*** SA Government employees who elected to contribute to SASS before 30 May 1986 ***Lump Sum Scheme*** SA Government employees who elected to contribute to SASS after 1 July 1988 and before 3 May 1994
Police Superannuation Scheme (Police Super)	Defined benefit	South Australian police officers who commenced employment with South Australia Police on or before 31 May 1990
Southern State Superannuation Scheme (Triple S)	Defined contribution	SA Government employees from 1 July 1995
SA Metropolitan Fire Service Superannuation Scheme (SAMFSSS)	Hybrid (defined benefit and defined contribution)	Employees of the South Australian Metropolitan Fire Service
South Australian Ambulance Service Superannuation Scheme (Ambulance Super)	Hybrid (defined benefit and defined contribution)	Employees of the SA Ambulance Service Inc
Super SA Retirement Investment Fund (SSARIF)	Hybrid (income stream and defined contribution)	SA Government employees who have retired, or are nearing retirement age, or have ceased employment with the SA Government
Parliamentary Superannuation Scheme (Parliamentary Super)	Hybrid (defined benefit and defined contribution)	Members of Parliament
Super SA Select (Select)	Defined contribution	SA Government employees earning income of up to $37 000 p.a.
Judges' Pensions Scheme (JPS)	Defined benefit	South Australian judges
Governors' Pensions Scheme (GPS)	Defined benefit	Former Governors of the State

With the exception of Select, JPS and GPS, all schemes offer insurance services to their members, which may include income protection, death, and total and permanent disability.

All public sector superannuation schemes are exempt public sector superannuation schemes, which are superannuation schemes that are not regulated by the Australian Prudential Regulatory Authority (APRA) under Schedule 1AA of the Superannuation Industry (Supervision) Regulations 1994. Exempt public sector superannuation schemes have unique attributes that include, but are not limited to, the following:

- concessional contributions (ie contributions before tax) plus earnings may be released from the age of 55 (or 50 for Police Super members), upon termination of South Australian public sector employment. It does not require permanent retirement
- non-concessional contributions plus earnings may be released irrespective of age on terminating South Australian public sector employment
- a member's preservation age will generally remain at age 55 (or 50 for Police Super members) and not increase to age 60
- due to their exempt status, the schemes are not regulated by APRA. However, for statutory purposes, the schemes report to APRA under an agreement between the Commonwealth and State Governments.

A number of South Australian public sector superannuation schemes are also constitutionally protected (ie Triple S, SASS, Parliamentary Super, JPS, GPS, Police Super). As a result, these schemes have the following unique attributes:

- concessional contributions are not taxed on receipt into the scheme, and therefore there is no requirement to deduct the 15% contributions tax
- there is no tax payable on contributions or earnings until the member leaves the scheme. This includes tax on fund income
- there are no annual concessional contribution caps, but a lifetime concessional contribution cap is in place
- annual non-concessional caps do apply to members of the constitutionally protected fund, however any tax payable levied by the ATO is against the member and cannot be deducted from the scheme.

Administration and funds management

The following table outlines the entities responsible for administering (ie receipting contributions and paying benefits) each of the public sector superannuation schemes.

Scheme	Entity responsible for administration
SASS, Triple S, SSARIF, Ambulance Super	South Australian Superannuation Board
Parliamentary Super	South Australian Parliamentary Superannuation Board
JPS, GPS	Legislation is committed to the Treasurer
SAMFSSS	SA Metropolitan Fire Service Superannuation Pty Ltd
Select	Southern Select Super Corporation
Police Super	Police Superannuation Board

Except for Police Super and the SAMFSSS, the Department of Treasury and Finance – State Superannuation Office (Super SA) provides outsourced administration services to the schemes. The Police Super Office, an administrative unit of South Australia Police, provides administration services to Police Super. Mercer Outsourcing (Australia) Pty Ltd provides administration services to the SAMFSSS.

The Superannuation Funds Management Corporation of South Australia (Funds SA) is responsible for investing and managing the superannuation schemes' funds in line with the *Superannuation Funds Management Corporation of South Australia Act 1995*.

Investments and related performance

As at 30 June 2018, the superannuation schemes had $29.8 billion ($27 billion) in investments. In 2017-18 these assets increased in fair value by $2.8 billion ($2.8 billion).

Total investment assets have steadily increased, reflecting growth in membership as well as additional contributions. In 2017-18 the continued strong net investment revenues contributed to this growth.

In 2017-18, net investment income decreased marginally by $21 million (1%). Actual investment returns, while remaining strong, were slightly lower than in 2016-17. In particular, Australian equities and diversified strategy growth recorded returns of approximately 13% to 15% (15% to 20%).

Investment expenses increased in 2017-18 reflecting an increase in funds under management with Funds SA, as costs (including performance fees) are applied on a percentage basis of funds under management.

The following table summarises the rates of return advised by Funds SA for the balanced and growth options for tax exempt (ie constitutionally protected) schemes.

	2016	2017	2018
	%	%	%
Balanced	3.9	11.0	9.5
Growth	3.8	12.4	10.6

Further details are included in the commentary under 'Superannuation Funds Management Corporation of South Australia' in this Report.

Surplus (Deficit) of net assets to member benefits liabilities

The SA Government controls and funds a number of defined benefit superannuation schemes designed to provide employees with pensions or defined lump sum benefits on retirement. Except for JPS and GPS, these schemes are now closed to new members. The SAMFSSS, while still open to new members, is not controlled and funded by the SA Government.

As at 30 June 2018, the total deficit of net assets to member benefits liabilities amounted to $4.9 billion ($5.3 billion). This is represented as follows.

	Net assets available for member benefits		Member benefits liabilities		Total equity over (under) funded	
	2017	2018	2017	2018	2017	2018
	$'million	$'million	$'million	$'million	$'million	$'million
SASS	4 984	5 113	9 861	9 711	(4 877)	(4 598)
Police Super	1 676	1 852	2 153	2 209	(477)	(358)
Parliamentary Super(1)	233	246	200	192	33	53
Ambulance Super(1)	191	202	178	183	13	19
JPS	251	273	224	239	27	35
GPS	-	-	2	2	(2)	(2)
Total(2)	7 335	7 686	12 618	12 536	(5 283)	(4 851)

(1) Amounts included relate only to the defined benefit portion of the schemes.
(2) Table excludes the SAMFSSS as defined benefits are funded by its members.

The total unfunded member benefits liabilities (deficit of net assets to member benefits liabilities) were calculated in line with AASB 1056 'Superannuation Entities'.

Different liability balances are reported under separate accounting standards

The terms of these defined benefit schemes create an obligation for the SA Government to pay future benefits to scheme members. The SA Government estimates an $11.2 billion liability at 30 June 2018 for unfunded superannuation benefits in the 2018-19 State Budget (refer 2018-19 Budget Paper 3 'Budget Statement', page 65). This figure is significantly larger than the accumulated deficit of net assets to accrued benefits of $4.9 billion identified above.

This variance is due mainly to the different discount rates used to calculate accrued member benefits liabilities under AASB 1056, and the rate required under AASB 119 'Employee Benefits'. While both standards require measurement of the present value of expected future benefit payments, superannuation schemes are required to use a market-determined, risk-adjusted discount rate appropriate to the scheme. The schemes apply discount rates ranging from 7% to 8% p.a.

For the purposes of the State Budget and whole-of-government financial reporting, the SA Government's unfunded superannuation liability is measured in line with AASB 119, which requires the use of a risk free discount rate reflecting the market yields on Commonwealth Government bonds. The discount rate at the time of the 2018-19 State Budget was 2.9% p.a. (refer 2018-19 Budget Paper 3 'Budget Statement', page 67). The lower discount rate results in a higher present value liability calculation.

Catch-up funding cash payments continue

A program began in 1994-95 to fully fund all employer superannuation liabilities. The 2018-19 State Budget states that the SA Government is on target to meet its commitment to have the defined benefit schemes fully funded by 2034 (refer 2018-19 Budget Paper 3 'Budget Statement', page 10).

The past service liability contributions for 2017-18 were $431 million ($462 million). The purpose of this contribution is to catch up the shortage of funding for employment in years prior to the full funding policy. The past service contributions are affected by a number of factors including the long-term earnings rate on superannuation assets. Where investment performance exceeds the assumed rate, it is possible to reduce the level of past service payments required to fully fund superannuation liabilities by 2034. Additional contributions are needed to compensate for reduced earnings to remain on target.

South Australian Superannuation Board (SASB)

Financial statistics	Administration expense:	$28.4 million
	Net cost of services:	$791 000
	General reserve:	$981 000

Significant events and transactions

- SASB has spent $18.5 million to 30 June 2018 on implementing the Bluedoor superannuation administration system, including costs for software and internal project management.
- Bluedoor was implemented in May 2018 for three schemes: Triple S, SSARIF and Super SA Select.
- A date for the second phase of Bluedoor implementation was not yet determined, awaiting resolution of outstanding issues and further testing of functionality.

Financial report opinion

Unmodified

Financial controls opinion

Modified

Key issues:

- Some member transaction documents could not be located
- Some member contributions were not allocated promptly
- Delays in month end close processes
- A full reconciliation of financial data transferred to Bluedoor was not performed as part of data migration
- A former bank account signatory was not removed promptly

Functional responsibility

SASB was established by the *Superannuation Act 1988* (the Super Act).

SASB is responsible to the Treasurer for administering the following superannuation schemes:

- South Australian Superannuation Scheme (SASS) under the Super Act
- Southern State Superannuation Scheme (Triple S) under the *Southern State Superannuation Act 2009*
- Super SA Retirement Investment Fund (SSARIF) under the Southern State Superannuation Regulations 2009
- South Australian Ambulance Service Superannuation Scheme (Ambulance Super) under the Super Act.

SASB's administration of these schemes involves maintaining:

- accounts in the names of all members
- employer contribution accounts
- proper accounts for each financial year on receiving contributions and paying benefits.

The Department of Treasury and Finance (DTF) – State Superannuation Office (Super SA) provides services to administer the schemes.

The Superannuation Funds Management Corporation of South Australia is responsible for investing and managing the schemes' funds under the above legislation and the *Superannuation Funds Management Corporation of South Australia Act 1995*.

Bluedoor system implementation

Status of implementation

In 2015-16 the SA Government contracted DST Bluedoor to provide a new superannuation management system on behalf of all the superannuation schemes administered by SASB.

Bluedoor, when fully implemented, is expected to provide SASB with an integrated administration system with a range of complementary capabilities including workflow management, document management and enhanced reporting systems. Bluedoor will replace all existing superannuation administration systems used by SASB.

SASB's budgeted costs from project commencement to full implementation are estimated at $30 million. The budgeted costs have increased since 2017 to reflect known change requests and additional support costs for legacy platforms (initially projected to be decommissioned prior to 2017-18).

Bluedoor was originally expected to be implemented in 2016-17, in two phases. Planned go-live dates were revised due to delays in the implementation of the project which included:

- changes to scope relating to design, coding, testing and data migration due to changes in legislation
- the need to work through the configuration of the system with a number of external parties
- the complexity of data migration from existing systems
- internal resourcing constraints in SASB to support the implementation program.

The first phase of Bluedoor's implementation went live on 7 May 2018, with Bluedoor used for Triple S, SSARIF and Super SA Select.

The table below summarises the original and actual go-live dates for Bluedoor implementation and the schemes covered by each phase.

	Schemes affected	**Original go-live date**	**Actual go-live date**
Phase 1	Triple S, Super SA Select and SSARIF	April 2017	7 May 2018
Phase 2	SASS, Ambulance Super, Parliamentary Superannuation Scheme, Judges' Pensions Scheme, Governors' Pensions Scheme	November 2017	To be determined

The date for Phase 2 implementation will be determined once a number of issues arising from Phase 1 implementation are addressed to SASB's satisfaction and successful testing is carried out for the different functionality required for the Phase 2 schemes.

SASB has conducted a number of internal audits of Bluedoor processes throughout the design and testing process, with the reviews identifying some matters that need to be addressed.

Outstanding issues that had not been resolved at the time of this Report include:

- weaknesses in review processes to verify changes to member details or member bank account information
- weaknesses in processes to ensure member transfers from other schemes using SuperStream are correctly allocated where manual intervention is required
- user profile security settings needed to be reviewed
- some procedures needed to be developed and insurance processes needed to be streamlined.

Financial costs of the project

An internal audit completed in June 2018 found that the actual total spend on the project as at 31 March 2018 was $16.5 million. We were further advised that as at 30 June 2018, the total spend on Bluedoor had increased to $18.5 million out of the estimated total budget until full implementation of $30 million. The software is included in DTF's financial statements as intangible assets – work in progress with a current value of $15.7 million as at 30 June 2018.

Scope of the audit

The audit program covered major financial systems to obtain sufficient evidence to form an opinion on the financial report and internal controls.

Specific areas of audit attention in 2017-18 included:

- administration expenses
- fees and charges revenue (recovery of administration fees from superannuation schemes)
- general ledger
- progress of ICT projects.

Internal audit activities were reviewed to assess the risks of material misstatement in the financial report and to design and perform audit procedures.

Audit findings and comments

Assessment of controls

In my opinion, the controls exercised by the South Australian Superannuation Board in relation to the receipt, expenditure and investment of money, the acquisition and disposal of property and the incurring of liabilities, except for all matters outlined under 'Communication of audit matters', are sufficient to provide reasonable assurance that the financial transactions of the South Australian Superannuation Board have been conducted properly and in accordance with law.

Communication of audit matters

A number of matters identified by the audit were detailed in a management letter to the Chief Executive of SASB and those charged with governance. The main issues and SASB's responses are detailed below.

SASB is responsible for managing more than $27 billion in superannuation funds, with more than 217 000 individual members of the various schemes that SASB supports.

Some member transaction documents could not be located

SASB was unable to locate some of the member transaction documents we sought as part of the audit. SASB advised that documents could not be located due to a combination of issues. In particular:

- resources were extremely stretched following the implementation of Phase 1 of Bluedoor and changes to team structures within SASB
- the way that data is filed by SASB changed following the implementation of Phase 1 of Bluedoor.

SASB advised that it did not expect these issues to occur in future, with structures now clearly understood.

Some member contributions were not allocated promptly

We identified delays in allocating around $800 000 of member contributions to member accounts within Triple S. SASB advised that the implementation of Bluedoor had assisted with allocations generally but that a system defect continued to affect some allocations, with resolution to the defect expected in mid-September 2018.

Delays in month end close processes

Month end close processes for the schemes included in Phase 1 of the Bluedoor implementation were delayed for June 2018. SASB responded that the delays were a result of the time consuming nature of the general ledger upload process following Bluedoor go-live, with system defects and processing difficulties experienced by SASB staff. SASB also noted staff resourcing levels impacted the timing of month end close processes for June 2018.

SASB advised it expected month end close processes to improve in 2018-19.

A full reconciliation of financial data transferred to Bluedoor was not performed as part of data migration

A full financial reconciliation was not completed during the Bluedoor data migration, with financial data not fully reconciled between the general ledger, Bluedoor registry system and fund manager at an investment level. We also noted some member accounts had been adjusted after data migration to correct migration issues.

SASB responded that it was not possible to undertake a full financial reconciliation due to the timing of Phase 1 go-live on 7 May 2018, with full investment data only provided at month or quarter end. A full reconciliation was undertaken at 30 June 2018 and would continue in 2018-19.

A former bank account signatory was not removed promptly

We noted a former SASB employee remained listed as a bank account signatory following their departure in May 2018. SASB advised they would ensure processes were in place to amend bank account signatories following staff changes.

Superannuation on paid parental leave

In previous Reports I have advised that the Southern State Superannuation (Parental Leave) Amendment Bill 2016 was before the Parliament to amend the *Southern State Superannuation Act 2009.* The Bill sought to remove the exclusion of paid parental leave from the definition of salary with effect from 19 November 2012. The Bill was assented to on 10 October 2017 with retrospective effect from 19 November 2012.

Interpretation and analysis of the financial report

SASB's financial report reflects its administration role in that:

- expenses relate mainly to fees paid to DTF to administer the superannuation schemes
- revenues are mainly to reimburse DTF fees from the superannuation schemes.

Highlights of the financial report

	2018 $'million	2017 $'million
Expenses and income		
Total expenses	28.4	27.3
Total income	27.6	18.7
Total comprehensive result	(0.8)	(8.6)
Net cash provided by (used in) operating activities	1.1	(14.1)
Assets		
Cash and cash equivalents	1.8	0.7
Receivables	0.6	1.6
Total assets	2.4	2.3
Total liabilities	0.9	-
Total equity	1.5	2.3

Statement of Comprehensive Income

The total comprehensive result for the year was a loss of $791 000 ($8.6 million). This result mainly reflects:

- revenue from recoveries of administration fees of $27.6 million ($18.5 million). This amount represents the administration fees charged to the superannuation schemes administered by SASB. These fees are set by SASB to recover the costs of SASB's operations from the schemes and are paid to DTF as a reimbursement of actual costs incurred in operating SASB
- administration expenses of $28.4 million ($27.3 million). This amount is paid to DTF for administrative services, which also includes the reimbursement of $5.4 million in estimated ICT project costs for the Bluedoor system.

The increase in administration fees in 2017-18 reflects additional costs associated with running both Bluedoor and legacy systems and costs associated with other SASB initiatives, including revisions to superannuation insurance arrangements.

Multiple system costs are projected to reduce in future years when Bluedoor is implemented for further schemes.

Statement of Financial Position

The increase in the cash balance as at 30 June 2018 was mainly due to more cash being receipted during the year, with a corresponding decrease in receivables. The increased cash on hand was to pay for future payables which increased by $804 000.

The increase in liabilities of $804 000 was due to the increase in the administration fee payable to DTF at the end of the year. The increased administration fee payable resulted mainly from ICT costs incurred for the Bluedoor system.

General reserve

SASB has established a general reserve to:

- account for under and over spend in office expenditure
- provide for future project expenditure
- provide funding for the triennial SASB election.

In 2017-18, $798 000 was released from general reserves to retained earnings to fund the over spend in overall expenditure mainly incurred for the Bluedoor system implementation.

South Australian Superannuation Scheme (SASS)

Financial statistics

Member benefit liabilities:	$9.7 billion
Net assets available for member benefits:	$5.1 billion
Defined benefits underfunded:	$4.6 billion
Past service liability funding:	$372 million
Benefits paid and payable:	
Pension Scheme	$643 million
Lump Sum Scheme	$222 million
Number of members:	
Pension Scheme	15 513
Lump Sum Scheme	3 559
Total	19 072

Significant events and transactions

— There was a change in the fair value of investments of $583 million.

Financial report opinion

Unmodified

Functional responsibility

SASS was established by the *Superannuation Act 1988*.

SASS provides superannuation benefits for people employed by the SA Government and other prescribed people and makes provisions for their families.

SASS is divided into two segments – the Pension Scheme and the Lump Sum Scheme.

The Pension Scheme is the superannuation scheme for SA Government employees who elected to contribute to SASS before 30 May 1986. Contributors to the Pension Scheme are entitled to a pension based benefit.

The Lump Sum Scheme is the superannuation scheme for SA Government employees who elected to contribute to SASS after 1 July 1988 and before 3 May 1994. Contributors to the Lump Sum Scheme are entitled to a lump sum based benefit.

Scope of the audit

The audit program covered major financial systems to obtain sufficient evidence to form an opinion on the financial report and internal controls.

Specific areas of audit attention in 2017-18 included:

- receipting and banking of contributions
- benefit payments
- member benefits liabilities
- maintenance of members accounts
- investments.

The investment and management of SASS's assets is reviewed as part of the Superannuation Funds Management Corporation of South Australia (Funds SA) audit.

Internal audit activities were reviewed to assess the risks of material misstatement in the financial report and to design and perform audit procedures.

Audit findings and comments

Communication of audit matters

We did not communicate any issues to the Chief Executive of Super SA relating specifically to SASS. Other matters communicated to the Chief Executive of Super SA and those charged with governance are discussed under the South Australian Superannuation Board commentary.

Interpretation and analysis of the financial report

Highlights of the financial report

	2018 $'million	2017 $'million
Assets		
Investments	5 116	4 991
Other assets	16	10
Total assets	5 132	5 001
Liabilities		
Benefits payable and other current liabilities	18	17
Total liabilities	18	17
Net asset available to pay benefits	5 113	4 984
Member benefits		
Defined benefit member liabilities	9 058	9 205
Defined contribution member liabilities	653	656
Total member liabilities	9 711	9 861
Equity		
Defined benefits that are over (under) funded	(4 598)	(4 877)
Total equity	(4 598)	(4 877)

	2018 $'million	2017 $'million
Revenue		
Changes in investments measured at fair value	583	604
Total revenue	583	604
Expenses		
Investment expenses	44	39
Higher education expense	9	9
Administration expenses	3	3
Total expenses	56	51
Result from superannuation activities	527	553
Net change in defined member benefits liabilities	(45)	61
Allocation to defined contribution member accounts	(203)	(202)
Operating result	279	412
Changes in member benefits		
Net contributions	466	497
Benefits to members (paid and payable)	(865)	(840)
Net cash flows from operating activities	(12)	(12)
Net cash flows from investing activities	415	356
Net cash flows from financing activities	(400)	(343)

Statement of Financial Position

Investments

Total investments increased by $125 million to $5.1 billion due to marginally increased investment returns. The increase in investments is from investment returns.

Member benefits liabilities

SASS is a defined benefit superannuation scheme. It is comprised of the old scheme whose members are entitled to a pension benefit payment and the new scheme whose members are entitled to a lump sum benefit payment.

Summarised below are the net assets available for member benefits, member benefits liabilities and the resulting excess of liabilities over net assets.

	2017 $'million	2018 $'million
Net assets available for member benefits	4 984	5 113
Member benefits liabilities	9 861	9 711
Over (under) funded member benefits liabilities	(4 877)	(4 598)

The $9.7 billion member benefits liabilities comprise $9 billion (93%) for the old scheme (defined benefit pension scheme) liability and $653 million (7%) for the new scheme (defined contribution lump sum) liability.

The total of unfunded member benefits liabilities decreased by $279 million to $4.6 billion. This decrease is largely due to:

- the $583 million income from changes in investments measured at fair value resulting from the continued strong growth in the market during 2017-18
- the overall decline in member numbers, which is consistent with the ageing membership demographic and SASS's closure to new members since May 1986 (old scheme) and May 1994 (new scheme)
- the actuarial calculation of the liability and the effect of the past service liability funding of $372 million.

As mentioned in the 'Superannuation sector overview section of this Report, the SA Government has committed to fully fund the defined benefit superannuation schemes by 30 June 2034.

The demographic assumptions of the 2016 triennial actuarial review were applied to the calculation of the member benefits liabilities. The following assumptions, which are consistent with the 2016 valuation, were used in calculating the 2018 member benefits liabilities:

- discount rate 7%
- long-term salary inflation 4%
- long-term CPI factor 2.5%.

Vested benefits

Vested benefits are the benefits members are entitled to had their membership been terminated at reporting date. The vested benefits as at 30 June 2018 were $9.8 billion ($10 billion) as disclosed in note 4 of SASS's financial report.

Income Statement

Investment revenue

Total revenue decreased by $21 million (3.5%) to $583 million due to the changes in investments measured at fair value as a result of lower rates of returns on property, Australian equities, diversified strategy growth and inflation linked securities, which outperformed their benchmarks. In particular Australian equities and diversified strategy growth recorded returns of approximately 13% to 15% (15% to 20%).

Further details on investment returns are included in the commentary under 'Superannuation Funds Management Corporation of South Australia' in this Report.

Expenses

Investment expenses increased by $5 million to $44 million. The increased investment expenses were due to higher transactional and operational costs to Funds SA as a result of increased funds under management and strong investment returns.

Statement of Changes in Member Benefits

Contribution revenue

Details of contribution revenue and membership statistics are presented in the following table.

	2017 $'million	2018 $'million
Contributions for past service liability	392	372
Contributions by employers	49	42
Public authority employer contributions	37	36
Contributions by members	18	15
Transfers from other super entities	1	1
Total	497	466

	2016 Number	2017 Number	2018 Number
Pension Scheme	16 327	15 902	15 513
Lump Sum	4 375	3 951	3 559
Total	20 702	19 853	19 072

Net contributions decreased by $31 million (6%) to $466 million, mainly because:

- contributions for past service liabilities decreased by $20 million (5%)
- contributions by employers decreased by $7 million (14%).

Past service liability contributions represent funding from both the SA Government (since 1994) and public sector employers to meet accrued superannuation liabilities. The SA Government expects to fully fund its liabilities by 30 June 2034. During the year the SA Government transferred a total of $367 million ($388 million) into the South Australian Superannuation Scheme Contribution Account for past service liability funding. Public sector employers contributed $5 million ($4 million).

The reduction in employer contributions is indicative of a closed scheme where the number of members is decreasing due to retirements.

Benefits to members

Benefits to members expense comprises the benefits paid and the change in the liability for accrued benefits. Benefits expense can fluctuate significantly due to changing assumptions in the calculation of the estimated liability for accrued benefits. In 2017-18 the assumptions used remained consistent, which is supported by the small increase in benefits to members of $25 million (3%) to $865 million this year. This increase is represented across both defined benefit and defined contribution members and reflects a decrease in member numbers, consistent with last year, offset by the indexation of pensions based on CPI.

An annual actuarial assessment of the defined benefit members liabilities is required by AASB 1056 'Superannuation Entities'. Further details of the liability are provided under 'Statement of Financial Position' above.

Further commentary on operations

Funding of benefit payments

Benefit payments are funded from a number of sources that have remained relatively consistent. Over half of the benefit payments are funded from the SA Government Employer Account.

The South Australian Superannuation Fund (the Fund) portion of a benefit is fully funded. Member contributions are deposited into the Fund and, on payment of a benefit, a proportion of the amount is charged against the Fund. The amount charged is determined by legislation and regulation.

There are numerous arrangements covering the funding of the employer liability for accrued superannuation benefits. Depending on the employer's arrangement with the South Australian Superannuation Board they may either:

- make provisions for superannuation liabilities in their own accounts and pay for benefits as they emerge
- contribute fortnightly to employer contribution accounts managed by Funds SA, in this way funding their accruing liability
- make cash contributions to the Treasurer, which are invested with Funds SA.

Note 1(d) of SASS's financial report provides details of the various funding arrangements.

Although a portion of the total superannuation liability is currently unfunded, members' entitlements to benefits must be paid out of the Consolidated Account, or a special deposit account established for that purpose.

Membership statistics for the last three years are provided in the following table.

Pension Scheme	2016 Number	2017 Number	2018 Number
Contributory	691	532	400
Preserved	392	339	296
Superannuants	15 244	15 031	14 817
Total	16 327	15 902	15 513

Lump Sum Scheme	2016 Number	2017 Number	2018 Number
Contributory	3 080	2 762	2 447
Preserved	1 295	1 189	1 112
Total	4 375	3 951	3 559

Total number of members	2016 Number	2017 Number	2018 Number
Contributory	3 771	3 294	2 847
Preserved	1 687	1 528	1 408
Superannuants	15 244	15 031	14 817
Total	20 702	19 853	19 072

Southern State Superannuation Scheme (Triple S)

Financial statistics	Contribution revenue:	$1.6 billion
	Member benefits liabilities:	$17 billion
	Net assets available for member benefits:	$17.2 billion
	Benefits paid and payable:	$1.3 billion
	Number of members:	181 524

Significant events and transactions

— The Bluedoor superannuation administration system has been used to administer Triple S since May 2018, following its first phase implementation.

— Changes in investments measured at fair value for 2017-18 were $1.6 billion.

Financial report opinion **Unmodified**

Functional responsibility

Triple S was established on 1 July 1995 by the *Southern State Superannuation Act 1994* and is continued under the *Southern State Superannuation Act 2009*.

Triple S is a defined contribution scheme that provides superannuation and other products and services for the benefit of people employed, or who have ceased employment, with the SA Government.

Scope of the audit

The audit program covered major financial systems to obtain sufficient evidence to form an opinion on the financial report and internal controls.

Specific areas of audit attention in 2017-18 included:

- receipting and banking of contributions
- benefit payments
- member benefits liabilities

- maintenance of members accounts
- investments
- reconciling superannuation data transferred to Bluedoor.

The investment and management of Triple S's assets is reviewed as part of the Superannuation Funds Management Corporation of South Australia (Funds SA) audit.

Internal audit activities were reviewed to assess the risks of material misstatement in the financial report and to design and perform audit procedures.

Audit findings and comments

Communication of audit matters

We did not communicate any issues to the Chief Executive of Super SA relating specifically to Triple S. Other matters communicated to the Chief Executive of Super SA and those charged with governance are discussed under the South Australian Superannuation Board commentary.

Interpretation and analysis of the financial report

Highlights of the financial report

	2018 $'million	2017 $'million
Assets		
Investments	17 242	15 406
Other assets	63	41
Total assets	17 305	15 447
Liabilities		
Benefits payable	87	56
Insurance liabilities	24	22
Other liabilities	1	1
Total liabilities	112	79
Net assets available for member benefits	17 193	15 368
Member benefits		
Member benefit liabilities	16 992	15 187
Total net assets	201	181
Total equity	201	181
Revenue		
Changes in investments measured at fair value	1 594	1 595
Total revenue	1 594	1 595
Expenses		
Investment expenses	111	101
Other expenses	17	11
Total expenses	128	112
Result from superannuation activities	1 466	1 483

	2018 $'million	2017 $'million
Insurance expenses	7	6
Net benefits allocated to members accounts	1 438	1 469
Operating result	21	8
Changes in member benefits		
Net contributions	1 639	1 563
Benefits to members (paid and payable)	(1 273)	(1 194)
Net cash flows from operating activities	(22)	(14)
Net cash flows from investing activities	(354)	(389)
Net cash flows from financing activities	381	393

Statement of Financial Position

The accumulative nature of Triple S (a defined contribution scheme) means that member benefits liabilities are fully funded.

Benefits payable

Benefits payable increased by $31 million, mainly due to delays in processing and approving benefit payments, as a result of delays caused by the implementation of Bluedoor.

Net assets available for member benefits

Net assets available to pay member benefits liabilities increased by $1.8 billion (12%) to $17.2 billion. This increase is indicative of the accumulative nature of Triple S, where the increases reflect the total of contributions received and net investment income less benefits paid and other expenses. In 2017-18, while the total dollar value of changes in investments measured at fair value was higher, the actual return on investments was lower than in the previous year.

Income Statement

Revenue

Total revenue decreased marginally by $1.8 million (0.1%) due to the changes in investments measured at fair value as a result of returns on property, Australian equities, diversified strategy growth and inflation linked securities, which outperformed their benchmarks. In particular Australian equities and diversified strategy growth recorded returns of approximately 13% to 15% (15% to 20%).

Further details on investment returns are included in the commentary under 'Superannuation Funds Management Corporation of South Australia' in this Report.

Expenses

The increase in total expenses of $16 million was mainly due to increases in:

- investment expenses of $10 million as a result of higher performance fees paid to Funds SA due to increased funds under management and strong investment returns
- administration fees of $5 million reflecting higher costs for administering the scheme, including costs associated with implementing Bluedoor.

Statement of Changes in Member Benefits

Contribution revenue

Total contributions increased by $76 million (5%) to $1.6 billion. This increase occurred in employer contributions and transfers from other super entities, with a fall in voluntary member contributions. The overall increase reflects the growth in member numbers and the impact of wage increases, which also flow through to higher superannuation contributions.

Details of contribution revenue and membership statistics are presented in the following table.

	2017 $'million	2018 $'million
Contributions by employers	1 099	1 157
Contributions by members	141	109
Transfers from other super entities	322	372
Government co-contributions	1	1
Total	1 563	1 639

	2016 Number	2017 Number	2018 Number
Contributory members	29 595	29 474	29 707
Non-contributory members	85 184	87 645	92 725
Preserved members	60 954	59 887	58 431
Spouses	578	601	661
Total	176 311	177 607	181 524

Active members of Triple S (contributory and spouse members) can elect to make contributions.

Employers are required to make contributions for contributory members of Triple S.

Benefits paid and payable

Benefits paid and payable to members increased by $79 million (7%) to $1.3 billion mainly due to increased transfers to other schemes.

The increase in benefits paid and payable over recent years is shown in the following table.

	2015 $'billion	2016 $'billion	2017 $'billion	2018 $'billion
Benefits paid and payable	1.2	1.2	1.2	1.3

Statement of Cash Flows

The analysis of cash flows shows that Triple S maintains a relatively small balance of funds on hand. Amounts not used to pay benefits and other expenses are transferred to Funds SA for investment, which is reflected in the cash flows from investing and financing activities.

Super SA Retirement Investment Fund (SSARIF)

Financial statistics	Contribution revenue:	$1.1 billion
	Member benefits liabilities:	$4.3 billion
	Net assets available for member benefits:	$4.4 billion
	Benefits paid and payable:	$824 million
	Number of members:	15 105

Significant events and transactions

- The Bluedoor superannuation administration system has been used to administer SSARIF since May 2018, following its first phase implementation.
- Changes in investments measured at fair value for 2017-18 were $331 million.

Financial report opinion **Unmodified**

Functional responsibility

SSARIF continues in existence under the *Southern State Superannuation Act 2009*.

SSARIF provides investment services and other products and services for the benefit of people who have retired, are reaching retirement age or have ceased employment with the SA Government. For details of SSARIF's functions refer note 1 of its financial report.

Scope of the audit

The audit program covered major financial systems to obtain sufficient evidence to form an opinion on the financial report and internal controls.

Specific areas of audit attention in 2017-18 included:

- receipting and banking of contributions

- benefit payments
- investments
- reconciling superannuation data transferred to Bluedoor, the new superannuation administration system.

The investment and management of SSARIF's assets is reviewed as part of the Superannuation Funds Management Corporation of South Australia (Funds SA) audit.

Internal audit activities were reviewed to assess the risks of material misstatement in the financial report and to design and perform audit procedures.

Audit findings and comments

Communication of audit matters

We did not communicate any issues to the Chief Executive of Super SA relating specifically to SSARIF. Other matters communicated to the Chief Executive of Super SA and those charged with governance are discussed under the South Australian Superannuation Board commentary.

Interpretation and analysis of the financial report

SSARIF comprises transactions for the Super SA Income Stream Product (Income Stream) and the Flexible Rollover product.

Highlights of the financial report

	2018 $'million	2017 $'million
Assets		
Investments	4 363	3 758
Other assets	27	19
Total assets	4 390	3 777
Liabilities		
Benefits payable	15	11
Other liabilities	23	15
Total liabilities	38	26
Net assets available for member benefits	4 352	3 751
Member benefits		
Income Stream member liabilities	3 179	2 755
Flexible Rollover product member liabilities	1 154	985
Total member liabilities	4 333	3 740
Total equity	19	11

	2018 $'million	2017 $'million
Revenue		
Changes in investments measured at fair value	331	311
Other revenue	6	5
Total revenue	337	316
Expenses		
Investment expenses	25	20
Other expenses	3	2
Total expenses	28	22
Result from superannuation activities	309	294
Net benefits allocated to members accounts	300	298
Income tax expenses	(1)	1
Operating result	8	(3)
Changes in member benefits		
Net contributions	1 118	1 142
Benefits to members (paid and payable)	(824)	(868)
Net cash flows from operating activities	(11)	(21)
Net cash flows from investing activities	(294)	(274)
Net cash flows from financing activities	313	289

Statement of Financial Position

Net assets available to pay member benefits increased by $601 million (16%) to $4.4 billion. This is the result of investment revenue earned, together with additional funds invested. It is indicative of the accumulative nature of SSARIF, where the increases reflect the total of contributions received and net investment income less benefits paid and other expenses. The accumulative nature of SSARIF also means that it is fully funded.

Income Statement

Revenue

Total revenue increased by $21 million (7%) due to the changes in investments measured at fair value as a result of increased returns on property, Australian equities, diversified strategy growth and inflation linked securities, which outperformed their benchmarks. In particular Australian equities and diversified strategy growth investments recorded returns of approximately 13% to 15% (15% to 20%).

Further details on investment returns are included in the commentary under 'Superannuation Funds Management Corporation of South Australia' in this Report.

Expenses

The increase in total expenses to $28 million ($22 million) was due to increased investment expenses as a result of higher performance fees paid to Funds SA. This fee increase was due to increased funds under management and strong investment returns.

Statement of Changes in Member Benefits

Total contributions decreased by $24 million (2%) to $1.1 billion due to:

- a decline of $42 million in contributions to the Flexible Rollover product mainly from decreases in member and spouse contributions
- offset by an increase of $20 million in rollovers from other schemes.

Contributions to SSARIF are all voluntary and are therefore open to fluctuation.

Benefits paid or payable to members decreased by $44 million (5%) to $824 million mainly due to delays in processing and approving benefits to be paid. These delays were associated with difficulties initially experienced with the introduction of Bluedoor.

Total benefits available to members ultimately depend on the investment strategy and investment performance, with no guarantee of return provided by the SA Government.

Statement of Cash Flows

The increase in cash provided by operating activities of $10 million was due mainly to the decrease in income tax paid in 2018 when compared to 2017. This reduction reflects that the 2017 year included payments related to tax for 2016, as well as 2017.

The net flows from investing activities decreased mainly due to increased payments to Funds SA for the purchase of investments. The net flows from financing activities increased mainly due to higher transfers from other superannuation entities in 2017-18, resulting in more funds available to invest.

Further commentary on operations

Membership statistics and total investments for the last four years are provided in the following table.

	2015 Number	2016 Number	2017 Number	2018 Number
Flexible Rollover product	4 043	4 351	4 733	5 291
Income Stream	6 678	7 965	8 898	9 814
Total	10 721	12 316	13 631	15 105

	2015 $’000	2016 $’000	2017 $’000	2018 $’000
Total investments	2 657 000	3 185 000	3 758 000	4 363 000

Superannuation Funds Management Corporation of South Australia (Funds SA)

Financial statistics	Net surplus:	$1.9 million
	Number of FTEs:	40
	Funds under management:	$32 billion
	Net income of assets under management:	$2.8 billion
Significant events and transactions	Funds under management grew by $3.1 billion to over $32 billion.	
Financial report opinion	**Unmodified**	
Financial controls opinion	**Unmodified**	

Functional responsibility

Funds SA is a statutory authority established by the *Superannuation Funds Management Corporation of South Australia Act 1995* (the SFMCSA Act).

Funds SA's main function is to invest and manage the public sector superannuation funds, nominated funds of approved authorities and other funds (funds under management) under strategies formulated by Funds SA. For details of Funds SA's objectives and functions refer note 2 of its financial report.

Restrictions on operations

Under section 21(1) of the SFMCSA Act, Funds SA is subject to the direction and control of the Minister. However, a ministerial direction must not be given for an investment decision, dealing with property or the exercise of a voting right.

Funds SA has broad powers over the investment of funds under management. It cannot, however, borrow money or obtain any other form of financial accommodation unless authorised to do so by the Regulations under the SFMCSA Act or by the Minister. In addition, the Regulations impose restrictions so that Funds SA cannot invest in real property outside the State or enter into derivative transactions (eg futures contracts, forward contracts and swaps) without the Minister's authority.

Structure

Funds SA operates with a small staff comprising investment managers, operations, corporate engagement and business services staff. This structure is complemented by extensive use of external fund management firms. Fund managers are used for all investment types, and there is a single custodian entity (which is responsible for holding, valuing and accounting for the assets) for the assets managed by most of those fund managers. Each fund manager and the custodian is appointed under an agreement that dictates the scope for investment, fees and reporting requirements.

Scope of the audit

The audit program covered major financial systems to obtain sufficient evidence to form an opinion on the financial report and internal controls.

Specific areas of audit attention in 2017-18 included:

- investment policy and strategy approval and compliance
- investment allocation and redemption
- investment expenditure, income and valuation
- custodial and fund management activities
- administration expenses.

Audit findings and comments

Communication of audit matters

Our review of auditable areas (including financial report verification) found that Funds SA financial controls were satisfactory. Nothing arose during the audit that required management letter communication to the Chief Executive Officer.

Interpretation and analysis of the financial report

Highlights of the financial report

Funds SA	2018 $'million	2017 $'million
Total income	10.2	8.1
Total expenses	8.3	6.9
Net surplus (deficit) and total comprehensive result	1.9	1.2
Net cash provided by (used in) operating activities	0.5	1.5
Total assets	10.0	7.6
Total liabilities	2.5	2.0
Total equity	7.5	5.6

Funds under management	2018 $'billion	2017 $'billion
Net income	2.8	2.9
Net assets	32.3	29.2

Statement of Comprehensive Income

Funds SA's operating result for the year was a net surplus of $1.9 million ($1.2 million).

Revenues from fees and charges increased by $2.1 million as a result of higher fees charged for services provided to Funds SA clients. This was due in part to a higher rate charged for average funds under management of 0.035% (0.03%), and also a higher volume of funds under management. Funds SA aims to only recover its costs and from time to time will rebate amounts charged for its services if excessive amounts are recovered. No rebate was made in 2017-18.

Expenses increased by $1.5 million mainly as a result of an increase in employee benefits costs, up $1 million, and supplies and services, up $428 000.

The increase in employee benefits costs was due mainly to increased salaries and wages, up $832 000, as a result of increased average staff levels and hiring an additional two executive level employees. This is in line with Funds SA's strategic plan to strengthen its capabilities to prepare for the challenges of the future.

The increase in supplies and services was mainly due to increased human resource expenses for the recruitment of additional staff, $178 000, travel and accommodation due to increased international travel, $96 000, and staff development, $57 000.

Further commentary on operations

Funds under management

Funds SA responsibilities

As mentioned, Funds SA exists to invest and manage the public sector superannuation funds, funds of eligible superannuation schemes and nominated funds of approved authorities.

To do this, Funds SA has established a range of different investment options and tailored multi-sector strategies it offers to its clients. These investment options and strategies comprise a mix of differing strategic asset allocations to meet its clients investment objectives, differing time horizons and levels of acceptable risks.

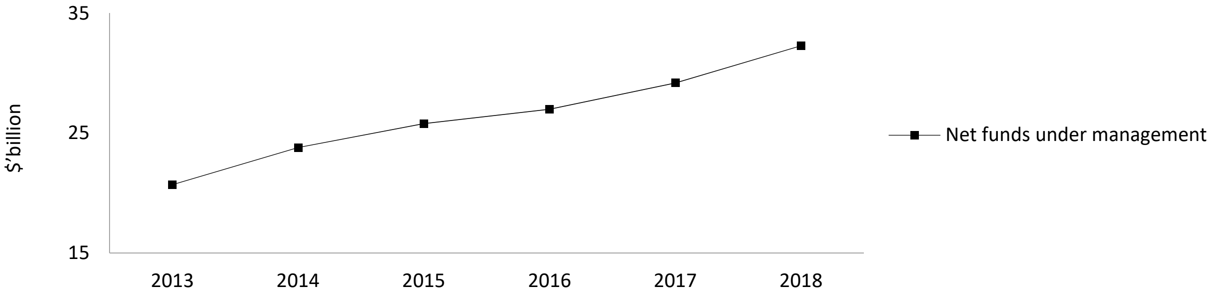
Funds SA is responsible for managing the investment portfolios it has established in line with asset allocations and investment performance reporting agreed with its clients.

Investor responsibilities

The public sector superannuation funds, eligible superannuation schemes and approved authorities decide which of Funds SA's options meets their investment needs. They deposit funds with Funds SA throughout the financial year to acquire units in an investment option, which in turn holds units in each of the asset classes that make up the investment option. They receive investment performance reporting as they require to meet their responsibilities for their invested funds.

Funds under management continue to grow

The following chart illustrates the net funds under management as at 30 June over the past six years.



Entities investing with Funds SA at 30 June 2018

The following table sets out the entities investing with Funds SA, the investment options used and funds under management at 30 June 2018.

Investor/Fund	Investment option	Funds under management $'million
Superannuation funds		
South Australian Superannuation Board:		
South Australian Superannuation Scheme:		
South Australian Superannuation Scheme – Employer Contribution Accounts	Defined benefit strategy	2 887
South Australian Superannuation Fund – Old Scheme Division	Defined benefit strategy	1 581
South Australian Superannuation Fund – New Scheme Division	Various	647
Southern State Superannuation Scheme:		
Southern State Superannuation Fund	Various	17 242
Super SA Retirement Investment Fund	Various	4 363
South Australian Ambulance Service Superannuation Scheme	Balanced B	267
Police Superannuation Board:		
Police Superannuation Scheme	Defined benefit strategy	1 852
South Australian Parliamentary Superannuation Board:		
Parliamentary Superannuation Scheme	Various	273
Trustee of the SA Metropolitan Fire Service Superannuation Scheme:		
SA Metropolitan Fire Service Superannuation Scheme	Various	398
Other superannuation schemes	Various	280
Approved authorities for the purpose of investing funds with Funds SA		
South Australian Government Financing Authority	Various	619
Motor Accident Commission	Motor Accident Commission A	1 012
Lifetime Support Authority of South Australia	Lifetime Support Authority Strategy	598
Other authorities	Various	293

Asset allocation

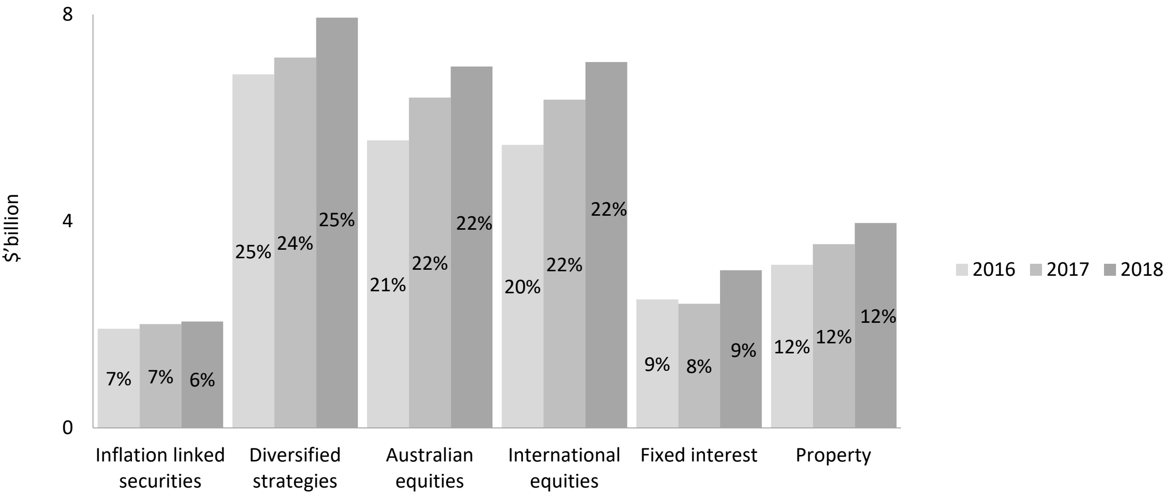
An investment policy drives decisions about how funds will be invested. Section 7 of the SFMCSA Act provides that the objective of Funds SA in performing its functions is to achieve the highest return possible on investment of the funds while having proper regard for:

- the need to maintain the risks relating to investment at an acceptable level
- the need for liquidity in the funds
- such other matters as are prescribed by regulation.

Underpinning the investment policy and decision-making is an understanding of the financial risks facing Funds SA. One of the key strategies Funds SA uses in managing its financial risk is to diversify its funds under management into 17 asset classes.

Funds SA continually monitors investment performance during the year and makes adjustments to investment subclass holdings as required.

The value of each asset class (excluding the cash and socially responsible investment classes, which in total only represent 4% (5%) of the total funds under management) and the holding of each asset class as a percentage of total funds under management at 30 June for the last three financial years is illustrated in the following chart. The asset classes include both taxed and untaxed funds where applicable.



The chart shows the increased value of funds under management across all asset classes over the year. The increases were due to investment returns and net investor cash inflows.

Australian and international equities, and diversified strategies growth were the strongest performing asset classes for the year, recording returns of approximately 13.5%, 15.3% and 14.5% respectively. Australian and international equities increased in value but remained steady as a percentage of holdings.

Diversified strategies (including both growth and income) asset classes increased in value from the prior year, with an increase in its percentage of holdings. The diversified strategies growth asset class

recorded returns of 14.5% as a result of strong returns from private equity markets, while diversified strategies income recorded a return of 1.2% due to the underperformance of the absolute return strategies component of this asset class.

Property assets increased in value and percentage holdings remained steady as a result of strong returns from commercial office markets in Australia. Fixed interest increased in both value and in percentage holdings as a result of strong performance in the Australian bond market, however this was offset by low returns from the performance of long-term fixed interest. Inflation linked securities experienced positive returns resulting in a slight increase in its value with a decrease in its percentage holdings.

The primarily long-term nature of investment strategies means funds under management are exposed to periodic falls in financial markets as well as gains.

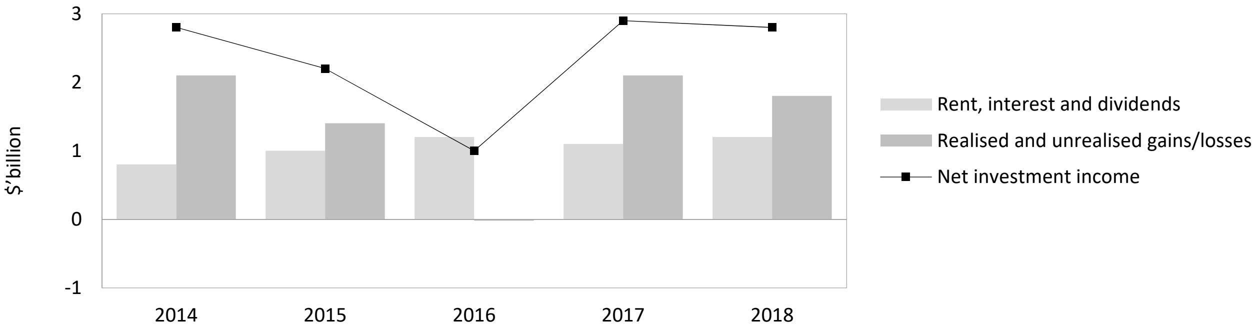
Income from investments

Net income from investment activities comprises income from rent, interest and dividends, and realised and unrealised gains and losses from investment valuations less expenses incurred in the investment activity.

Net income from investment activities was a surplus of $2.8 billion ($2.9 billion). Income comprised rent, interest and dividends of $1.2 billion ($1.1 billion), realised gains of $364 million ($400 million) and unrealised gains of $1.5 billion ($1.6 billion), offset by investment expenses of $222.9 million ($208.7 million).

Schedule 1 of Funds SA's financial report provides full details of income earned from investment activities for each asset class.

An analysis of the investment result for funds under management for the five years to 2018 is shown in the following chart.



As can be seen from this chart, positive realised and unrealised gains in 2014, 2015, 2017 and 2018 contributed significantly to the net investment income result. In 2016 there were negative realised and unrealised gains but these were offset by rent, interest and dividend income to still provide a positive net investment income result.

The following table shows a structural analysis of net income earned for the five years to 2018, highlighting the varying performance of the major investment asset classes. It should be noted that

the magnitude of net income earned from investment activities in each year is a function of not only the performance of financial markets, especially equities, but also the size of total assets invested in the markets.

	2014 $'million	2015 $'million	2016 $'million	2017 $'million	2018 $'million
Inflation linked funds	162	103	28	57	81
Property	209	289	425	313	439
Australian equities	753	315	27	835	849
International equities	1 039	1 007	(125)	1 073	933
Fixed interest	95	109	162	4	72
Diversified strategies	519	320	403	566	417
Cash/Socially responsible/Other	62	52	50	50	34
Total net income	2 839	2 195	970	2 898	2 825
Total value of assets invested as at 30 June	23 835	25 797	26 986	29 246	32 321

The earlier chart showing asset class holdings indicated that Funds SA's investment strategy is weighted towards Australian and international equity holdings. The table above shows an increase in income for the Australian equities class in 2018, and a decrease in income from international equities, reflecting their respective market performance during the year. The volatile nature of these investments will cause their returns to fluctuate from year to year consistent with prevailing economic conditions. Income from diversified strategies decreased due to the underperformance of income assets. Income from property increased in 2018 which reflects the strong performance of the Australian property market. Income from fixed interest increased due to positive returns in both the short and long-term fixed interest portfolio. Income from inflation linked funds increased as a result of the strong performance of the internally managed investments.

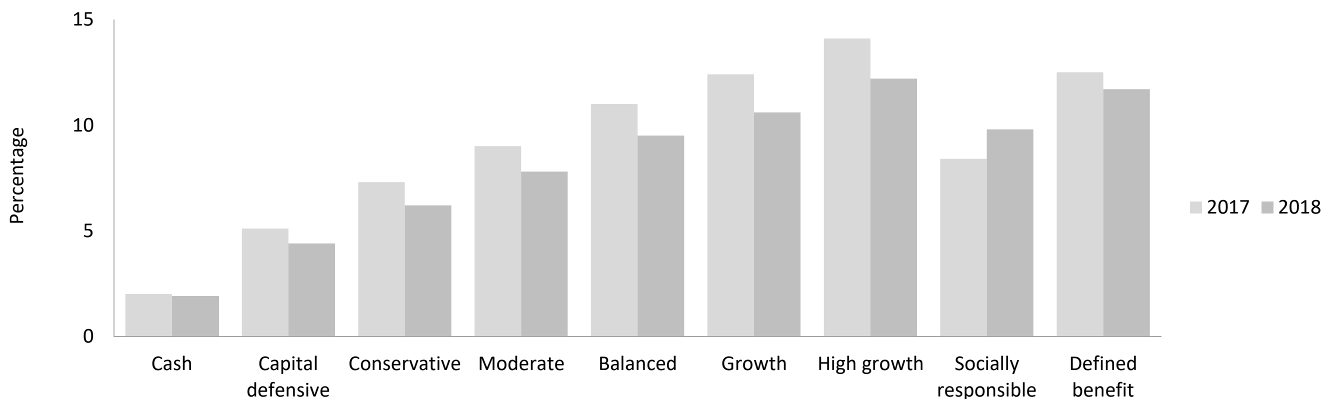
Investment expenses

In 2018 investment expenses amounted to $223 million, an increase of $14 million from the previous year. The increase is primarily the result of a higher value of funds under management during the year, and an increase in performance fees. This is especially evident in the diversified strategies asset classes. Investment expenses are 0.7% (0.7%) of average funds under management.

Year	Investment expenses $'million	Average funds under management $'billion
2014	131.8	22.7
2015	153.4	25.1
2016	162.5	26.4
2017	208.7	28.5
2018	222.9	31.3

Investment option performance

The chart below shows the returns for Funds SA's tax exempt investment options and multi-sector strategies as at 30 June for the past two years.



The chart shows that all investment options and multi-sector strategies, other than socially responsible, achieved lower returns in 2017-18 than the previous year. The returns of each investment option and multi-sector strategy reflect the performance of the underlying asset classes.

The strong performance of equities (Australian and international) and unlisted assets during the 12 months to 30 June 2018 and the more modest performance of defensive assets resulted in the returns of Funds SA's tax exempt investment options and multi-sector strategies ranging from 1.9% for cash through to over 12% for high growth.

The table below shows Funds SA's percentage return for each of the past 10 years for both the balanced and growth (tax exempt) funds, which together account for 50% of total funds under management. These figures were provided by Funds SA and are unaudited.

	10 years	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
	% p.a.	%	%	%	%	%	%	%	%	%	%
Balanced	7.0	(15.3)	12.6	10.9	3.1	14.7	13.8	9.4	3.9	11.0	9.5
Growth	10.6	(17.5)	12.3	11.4	2.0	16.4	14.9	10.0	3.8	12.4	10.6

The performance of the balanced and growth funds for 2018 was ahead of the growth median return of 9.2% as surveyed by Chant West.

Asset class performance against benchmark

The performance against target benchmarks for certain asset classes for 2017-18 and for the three years ended 2017-18 is shown in the following table. These figures were provided by Funds SA and are unaudited.

	1 year Actual %	1 year Benchmark %	3 years Actual %	3 years Benchmark %
Cash	1.9	1.8	2.0	1.9
Short-term fixed interest	2.5	2.3	2.5	2.4
Long-term fixed interest	2.6	3.0	3.7	4.2
Inflation linked securities A	4.2	3.7	2.9	2.9
Diversified strategies income	1.2	2.1	3.8	4.8
Property A	12.5	12.3	12.5	12.1
Australian equities A	13.5	13.2	9.4	9.1

	1 year Actual %	1 year Benchmark %	3 years Actual %	3 years Benchmark %
International equities A	15.3	15.7	10.6	10.4
Diversified strategies growth A	14.5	5.9	13.1	6.0
Inflation linked securities B	3.8	3.4	2.7	2.8
Property B	12.3	12.3	12.3	12.1
Australian equities B	13.2	13.2	9.5	9.1
International equities B	14.4	15.6	10.1	10.3
Diversified strategies growth B	14.0	5.9	12.7	6.0

The performance of asset classes against benchmark for 2017-18 was generally positive, with the diversified strategies growth asset class significantly outperforming the benchmark. Australian equities, cash, short term fixed interest, property and inflation linked securities asset classes outperformed their benchmarks, while the remaining asset classes performed below their benchmark.

TAFE SA

Financial statistics

Total expenses:	$359 million
Net cost of providing services:	$16 million
Total income from the Department of State Development (DSD):	$246 million
Number of FTEs (excluding casuals):*	1973
Number of training hours funded by DSD:*	6.8 million
Total training hours:*	15.5 million

* Data provided by TAFE SA and unaudited.

Significant events and transactions

— Total funding from DSD was $246 million, with $114 million received by TAFE SA to provide 6.8 million training hours.

— A 2017 audit of the quality of certain qualifications undertaken by the Australian Skills Quality Authority resulted in the suspension of 10 qualifications in December 2017, although the suspension was not enforced. The suspension was subsequently lifted in April 2018 after TAFE SA undertook remediation work in these qualifications.

— An audit of TAFE SA's Aircraft Maintenance program In March 2017 by the Civil Aviation Safety Authority resulted in the suspension of TAFE SA's Maintenance Training Organisation certificate and TAFE SA ceased training students in the program. The certificate was reinstated in November 2017 after TAFE SA satisfied the Civil Aviation Safety Authority of action taken.

— Nous Group was appointed in December 2017 by the SA Government to review the quality, sustainability and reputation of the State's public Vocational Education and Training. Moran/Bannikoff were also appointed at this time to review the role of the Public Provider.

— The TAFE SA Chair and Chief Executive left in December 2017.

— 112 TAFE SA staff took voluntary separation packages in 2017-18 bringing the total over the last five years to 634.

Financial report opinion

Unmodified

Financial controls opinion	**Modified**
	Key issues: — Controls around the hiring of, and payments to, hourly paid instructors could be improved — Review or approval of key payroll documents was not prompt — No formal independent reviews were undertaken of altered grades — A charter and a performance statement, required by the *Public Corporations Act 1993,* were not formally approved for 2017-18

Functional responsibility

TAFE SA is established under the *TAFE SA Act 2012* and is a statutory corporation to which the provisions of the *Public Corporations Act 1993* (other than section 35) apply.

The TAFE SA Board is responsible to the Minister for Education.

TAFE SA's main function is to provide technical and further education.

External reviews of TAFE SA

Civil Aviation Safety Authority (CASA)

TAFE SA is an approved CASA Maintenance Training Organisation (MTO) allowing it to deliver training and examinations leading to CASA licensing.

In March 2017 TAFE SA's Aircraft Maintenance program was audited by CASA. Adverse audit findings resulted in the suspension of TAFE SA's MTO certificate and training of students in the program ceased.

TAFE SA's MTO status was reinstated in November 2017 after it satisfied CASA of action taken.

87 students were affected. To date TAFE SA has paid approximately $803 000 to:

- pay expenses to retrain the students with another provider, including accommodation and travel costs ($671 000)
- reimburse course fees and ancillary expenses to students ($84 000)
- retrain the students at TAFE SA, including accommodation and travel costs ($48 000).

TAFE SA has included a $1 million contingent liability in the notes to its financial report in recognition of estimated costs to settle current claims and for any potential further claims.

TAFE SA expects to recover most of the rectification costs from its insurer, SAicorp.

Australian Skills Quality Authority (ASQA)

In May 2017, ASQA undertook an audit of the quality of the training and assessment of certain qualifications taught by TAFE SA. In December 2017, ASQA reported its intention to suspend TAFE SA's registration in 10 qualifications due to non-compliance with the requirements of the Vocational Education and Training (VET) Quality Framework due to the findings of the audit. TAFE SA's Chair and Chief Executive left TAFE SA in December 2017.

The suspension, which had not been enforced by ASQA, was subsequently lifted in April 2018 after TAFE SA undertook extensive remediation in these qualifications. In addition TAFE SA established a Quality, Teaching and Learning Directorate and is developing a Quality System Implementation project to review assessment materials for all units of competency delivered. It is also developing a Quality Teaching and Learning Framework.

ASQA has indicated it will undertake another audit of TAFE SA's training and assessment later in 2018.

Nous and Moran/Bannikoff reviews

A management consulting firm, Nous Group, was appointed in December 2017 by the previous SA Government to consider the recent regulatory findings on TAFE SA from ASQA and make recommendations to ensure the quality, sustainability and reputation of the State's public VET provider. The Nous review is referred to as the Quality Review of TAFE SA.

At the same time as the Nous review, Terry Moran AC and Kim Bannikoff were appointed to conduct a separate review to establish the role of the Public Provider in meeting the skills needs of students and industry and ensuring quality training outcomes across the State, including those associated with thin markets, regional and remote areas and the SA Government's social policies. This review is referred to as the TAFE SA Strategic Capability Review.

Reports from both of these reviews were tabled in Parliament in September 2018.

The new SA Government has indicated that it has accepted some of the findings and is considering others, which will impact the future operations of TAFE SA.

Scope of the audit

The audit program covered major financial systems to obtain sufficient evidence to form an opinion on the financial report and internal controls.

Specific areas of audit attention in 2017-18 included:

- expenditure and accounts payable
- payroll processing
- revenue including funding from DSD, student revenue and accounts receivable
- cash management including bank reconciliations
- general ledger.

The audit took into account the controls and procedures performed by service providers including Shared Services SA (SSSA).

We also considered the work of TAFE SA's internal auditors in planning and conducting the audit.

Audit findings and comments

Assessment of controls

In my opinion, the controls exercised by TAFE SA in relation to the receipt, expenditure and investment of money, the acquisition and disposal of property and the incurring of liabilities, except for all matters outlined under 'Communication of audit matters', are sufficient to provide reasonable assurance that the financial transactions of TAFE SA have been conducted properly and in accordance with law.

Communication of audit matters

Matters identified by the audit, including a number that were raised in prior years, were detailed in management letters to the Chair of the TAFE SA Board. The main matters raised and related responses are detailed below.

Payroll

Total salaries and wages expenses for TAFE SA employees were $181 million (including annual leave), of which $12 million was paid to hourly paid instructors (HPIs).

Controls around the hiring of, and payments to, hourly paid instructors could be improved

A number of hourly paid instructors commenced work without a signed contract

We have reported for a number of years that contracts for HPIs were being signed after the HPI started working with TAFE SA. In 2017-18 we identified that for 1675 HPI contracts, which was 36% of total HPIs, work commenced before signing an employment agreement.

TAFE SA's policies require a contract to be in place before an HPI commences, in part to ensure there is a clear agreement on contract arrangements.

The absence of a signed employment contract increases the risk of HPIs not understanding their responsibilities as TAFE SA employees and TAFE SA not complying with its Educational Staff Enterprise Agreement 2016 (the enterprise agreement).

New and ongoing HPIs are sent a letter containing employment terms and conditions each academic year. However, this letter does not contain sufficient details to be considered a formal letter of offer of employment.

TAFE SA responded that the HR Systems team had created an audit process that does not permit HPI claims to be paid without a signed employment contract. This tool will be expanded to ensure scheduled hours are not worked until the employment contract is signed.

Lack of segregation and no independent checks of new HPI contracts and processed claims

The previous system through which HPI claims were processed was decommissioned in February 2018 and there was no replacement application at that time, resulting in a manual process for HPI claim approvals.

TAFE SA engaged Deloitte to review the controls in place in the interim manual process used for HPI contracting and claims processing. Deloitte's report in March 2018 identified that it was not possible to segregate duties adequately as there was a heavy reliance on the two people in the HR Systems team.

At the time of our audit in May 2018, there was still a heavy reliance on the HR Systems team for HPI contract creation and claims processing functions and a system solution was not yet in place. The process relied on a manual unsecured file and there were no checks to ensure the claims were processed accurately.

The lack of segregation increases the risk that HPI contracts are created and submitted to payroll inappropriately.

TAFE SA responded that it would ensure there was clear segregation of duties, including a reconciliation between a report on HPI payments from the payroll system and HPI claims provided for processing.

HPIs have worked more than 400 hours (the maximum allowed under the enterprise agreement)

The enterprise agreement requires HPIs to be engaged for a maximum of 400 hours between 1 February and 31 January in the following year (the TAFE SA year).

The enterprise agreement states that where the hours of instruction and assessment are regular and can reasonably be predicted to be more than 400 hours in this time, the arrangement must be treated as part-time employment, whether on a temporary or permanent basis.

We identified 26 HPIs who had claimed more than 400 hours during the period, with the highest claiming 528 hours.

There did not appear to be any active monitoring controls in place to identify HPIs who were approaching the 400-hour limit and allow appropriate time for alternative arrangements to be put in place for the associated teaching needs.

This increases the risk of potential staff dissatisfaction or potential legal disputes and claims in future from HPI staff who have been engaged beyond the 400-hour limit.

TAFE SA responded that HR Business Partners would receive monthly reports of all HPI's that had worked between 200 and 300 hours. In addition, the Human Resource Business Partners would initiate workforce planning discussions, stressing the industrial requirements not to employ HPIs for more than 400 hours.

Review or approval of key payroll documents was not prompt

Return of bona fide certificates (BFCs) and leave return reports (LRRs)

TAFE SA's payroll processing moved from Empower to Chris21 from the pay period ending 16 November 2017. Chris21 sends emails to managers each pay run reminding them to review online BFCs. It is the managers' responsibility to notify TAFE SA Human Resources if there are any errors to address within five working days of the pay period end date.

We found that BFCs and LRRs were not effectively reviewed as a number of BFCs and LRRs we sampled were either not reviewed at all (22%), or not within five working days (37%).

The ineffective review of BFCs and LRRs increases the risk of financial loss to TAFE SA due to inaccurate payroll processing or leave recording within the payroll system. This could also lead to inaccuracies in payroll related balances in the financial statements.

TAFE SA responded that it would continue a quarterly communication process reminding managers of their responsibilities to review BFCs and LRRs. Human Resources would audit the BFC register fortnightly and table monthly non-compliance reports to Executive.

Monthly statistics on LRRs would also be tabled at Executive meetings.

Further, non-compliance with the BFC and LRR process would be escalated to the Interim Chief Executive for action.

Employees not assigned to BFCs and LRRs

When the payroll system migrated from Empower to Chris21, 41 employees, who would have impacted 216 reports, were not assigned to a BFC or LRR.

Therefore the details for these employees were not reviewed to ensure their hours worked and leave taken records were accurate.

TAFE SA advised that Human Resources would continue to monitor this issue by reviewing a fortnightly audit report which lists employees who are not assigned to a manager. Any missing details would be updated within 24 hours.

TAFE SA also advised it had no employees who were not assigned to a manager at the time of its response in August 2018.

Delays in processing forms to change work hours

An employee was overpaid $17 500 as they continued to be paid as a full-time employee when they had decreased their hours to work four days a week between February 2017 and December 2017. TAFE SA was in the process of recovering this amount at the time of our audit.

The form that varied this employee's hours was approved and signed by the employee's manager on 20 November 2016, but was not forwarded to SSSA payroll for processing until 5 December 2017.

If the employee's BFC was regularly and appropriately reviewed by their manager, this error should have been identified.

TAFE SA responded that increased accountability was being placed on managers throughout TAFE SA, including increased attention on bona fide completions. It advised this focus should reduce these issues.

Student fees and other revenue

No formal independent review was undertaken of altered grades

The total number of students commencing in 2017-18 with a pass result was 47 000 in 2017-18.

TAFE SA engaged an external firm to review the entry and changing of grades for student results. The external firm's report from February 2018 identified that 434 staff had access to change results and there was a lack of monitoring or review of changes to results.

From March 2018 access to the Student Information System to alter grades was restricted to the seven staff in the Data Services team. However, there was no evidence that grade changes were being independently reviewed to confirm the changes were appropriate.

This increases the risk that incorrect grades are entered in student results.

Further, TAFE SA had no policies or procedures requiring independent reviews of altered student grades.

TAFE SA responded that it would develop a policy or procedure outlining a grade change process. This would involve an automated grade change report to cross check grade changes in the Student Information System against those approved.

A charter and a performance statement were not formally approved for 2017-18

The *Public Corporations Act 1993* (the PC Act) requires the Minister responsible for TAFE SA and the Treasurer to prepare a charter which must be reviewed at the end of the financial year after consultation with TAFE SA. The charter can be amended by TAFE SA's Minister and the Treasurer after such consultation.

In addition, the PC Act requires the Minister and the Treasurer, after consultation with TAFE SA, to prepare a performance statement setting the various performance targets that TAFE SA is to pursue in the coming financial year and dealing with such other matters as the Minister considers appropriate.

We were advised that a draft charter and performance statement were prepared by TAFE SA for 2017-18, however they had not been signed by the Minister.

In the absence of an endorsed charter and performance statement, TAFE SA may not be operating within the expectations of the Minister.

TAFE SA responded that final carriage of the charter and performance statement was primarily through DSD. From 1 July 2018 this responsibility rests with the Department for Education, the Minister for Education and the Treasurer. An interim charter for 2018-19 was being considered at the time of TAFE SA's response to our audit.

Shared Services SA – financial systems and transaction processing environments

SSSA processes financial transactions on behalf of TAFE SA under service level determinations. The main systems and control environments include accounts payable, payroll and general ledger financial functions.

Our review and evaluation of controls for these systems concluded that controls were effective for 2017-18.

SSSA is discussed further in the commentary under 'Department of the Premier and Cabinet' in this Report.

Interpretation and analysis of the financial report

Highlights of the financial report

	2018 $'million	2017 $'million
Expenses		
Employee benefits	226	214
Supplies and services	127	102
Other expenses	6	6
Total expenses	359	322
Income		
Grants and subsidies from DSD	246	231
Student and other fees and charges	89	92
Other income	8	5
Total income	343	328
Total comprehensive result	(16)	6
Assets		
Current assets	76	91
Non-current assets	27	26
Total assets	103	117
Liabilities		
Current liabilities	41	37
Non-current liabilities	48	50
Total liabilities	89	87
Total equity	14	30

Statement of Comprehensive Income

Expenses

Employee benefits

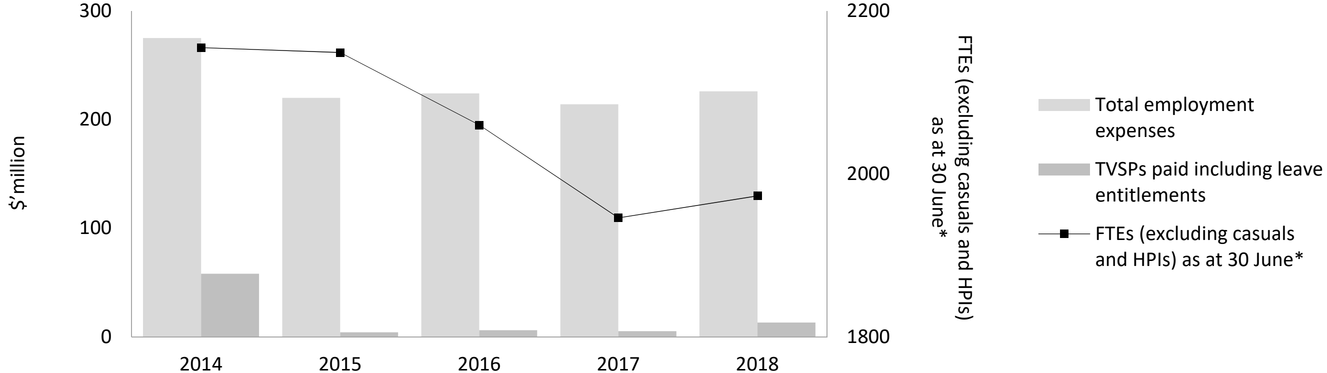
Employee benefits are TAFE SA's main expense, accounting for 63% (66%) of total expenses.

Employee benefits expenses increased by $12 million to $226 million in 2017-18. This was mainly due to an increase in targeted voluntary separation packages (TVSPs) of $5 million and an increase in long service leave expenses of $4 million.

Long service leave expenses mainly increased relative to 2017 as the 2017 figure was low, reflecting the impact of a discount rate reduction which reduced the long service leave liability and expense for that year. The same discount rate as 2017 was used to calculate the long service leave liability in 2018.

Employee benefits expenses included payments of TVSPs and related leave of $13 million ($5 million) to 112 staff and payments totalling $5 million ($10 million) to staff identified as excess, for which TAFE SA receives specific funding from DSD.

The following chart shows total employment expenses, total TVSP payments and total FTE staff (excluding casuals and HPIs) for the last five years.



* FTE data sourced from TAFE SA and unaudited.

When the impact of TVSPs is excluded, the employee benefits expenses in each of the last three years have been relatively consistent.

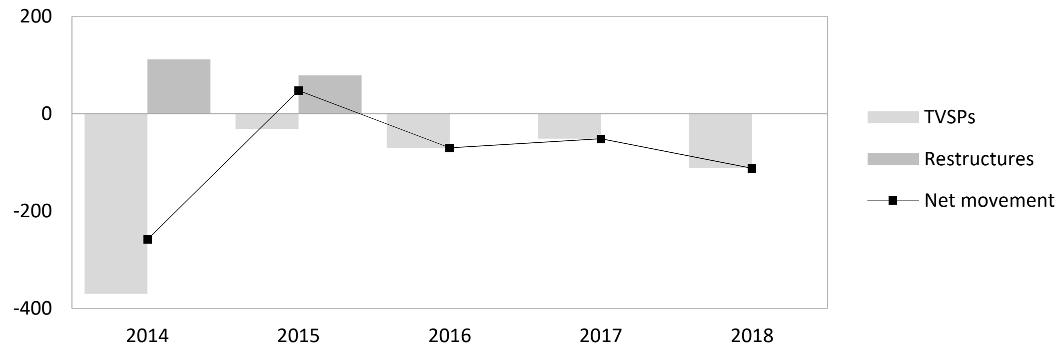
This analysis highlights that decreases in overall staff numbers in prior years have largely been absorbed by increases in payments to remaining staff through enterprise bargaining agreement wage rises, and a slight increase in FTEs as at 30 June 2018, when compared to 30 June 2017.

Salaried FTEs increased from 1946 as at 30 June 2017 to 1973 this year. FTEs as at 30 June 2018 consist of:

TAFE SA Act	1037
Public Sector Act	925
Excess staff	11

The number of FTEs increased by 27 in 2017-18 even though 112 (98 FTEs) staff were paid TVSPs. This increase in staff was mainly due to TAFE SA needing extra staff to deliver Commonwealth funded training following a successful bid for additional work. Some extra resources were also required for remediation work arising from the adverse findings of the ASQA audit.

The chart below further analyses TVSPs and other movements in TAFE SA staff numbers as a result of restructures for the last five years.



634 TVSPs have been paid to TAFE SA staff over the last five years. In that time 191 new staff joined as a result of restructures in the relationship between TAFE SA and the former Department of Further Education, Employment, Science and Technology or DSD. These restructures involved the transfer of staff from these departments, specifically:

- 112 staff from 1 July 2013 to establish autonomous corporate services within TAFE SA
- 79 staff from 8 September 2014 to establish autonomous IT services within TAFE SA.

Reduced payroll system functionality for HPIs

In 2017-18, $12 million ($11 million) was paid to HPIs. As previously mentioned, TAFE SA's payroll migrated from Empower to Chris21 in November 2017. A decision was made to implement the payroll functionality of Chris21 with a manual interim solution for HPIs, as Chris21 could not provide full functionality for HPIs to meet TAFE SA's needs.

Negotiations commenced with SSSA and Frontier with the aim to have a permanent system solution in place for HPIs in February 2018. The previous HPI time and attendance application was decommissioned on 16 February 2018 in anticipation of this functionality becoming available.

TAFE SA was advised by SSSA that a system solution was not available in February 2018. As a result, TAFE SA's manual processes remain in place at the time of this Report. As highlighted in our control findings, the manual nature of the interim processes result in risks to TAFE SA's control environment, as well as impacting on the efficiency of TAFE SA processes.

TAFE SA plans to directly undertake further work to procure a system solution.

Supplies and services

Overall supplies and services expenses were $127 million, an increase of $25 million from 2016-17.

The main change in supplies and services was an increase in infrastructure recharges paid to DSD of $22 million. This increase reflects the application of market rental rates from March 2017 when the ownership of campus land and buildings, leased by TAFE SA, was transferred from DSD to the Urban Renewal Authority (URA). DSD leases the land and buildings from the URA and then leases them to TAFE SA. TAFE SA's funding from DSD increased to compensate for the increased rental charges.

Income

Funding from DSD

TAFE SA's main income source is DSD. Total funding from DSD was $246 million ($231 million).

This funding constitutes 72% (70%) of TAFE SA's total income and is made up of the following components.

	2017 $'million	2018 $'million
VET subsidies (for specific units of competency delivered)	138	114
Other grant funding	57	100
Community services	12	12
Excess staff funding	12	5
Capital funding	5	4
TVSP reimbursement	4	9
Other specific funding	3	2
Total income	231	246

Total funding of $226 million was agreed in a memorandum of administrative arrangement (MoAA) for non-commercial services between TAFE SA and DSD for 2017-18. This total was separated between funding classified as VET subsidies, based on the number of hours of training delivered, community services amounts, funding for infrastructure charges and other grants.

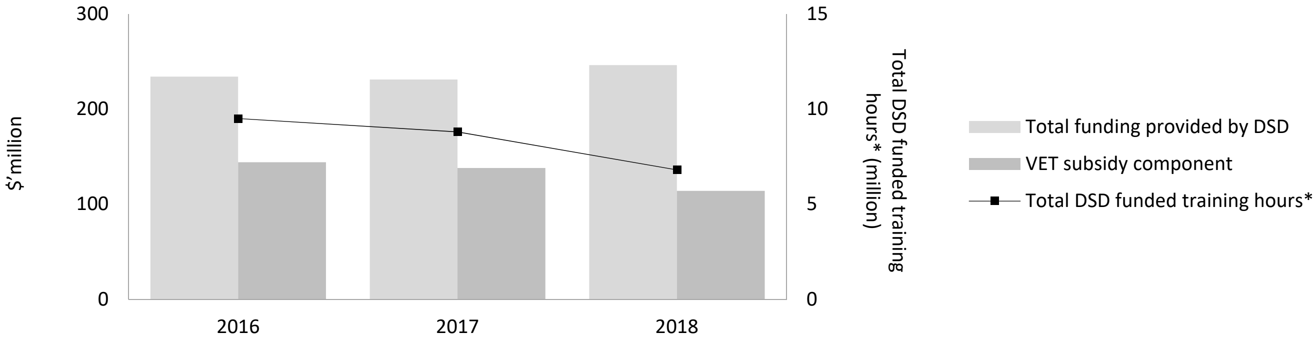
TAFE SA also received funding of $5 million for excess staff under a separate MoAA for TAFE SA structural adjustment. This was paid by DSD to meet the costs of excess employees incurred as a result of transitioning its business to a more competitive structure.

The balance of $15 million is subject to separate arrangements.

The MoAA clearly identifies that the funding arrangement is an interim arrangement for 2017-18 only and recognises the timing of the MoAA's execution and the significant events that resulted in the reviews of TAFE SA's operations.

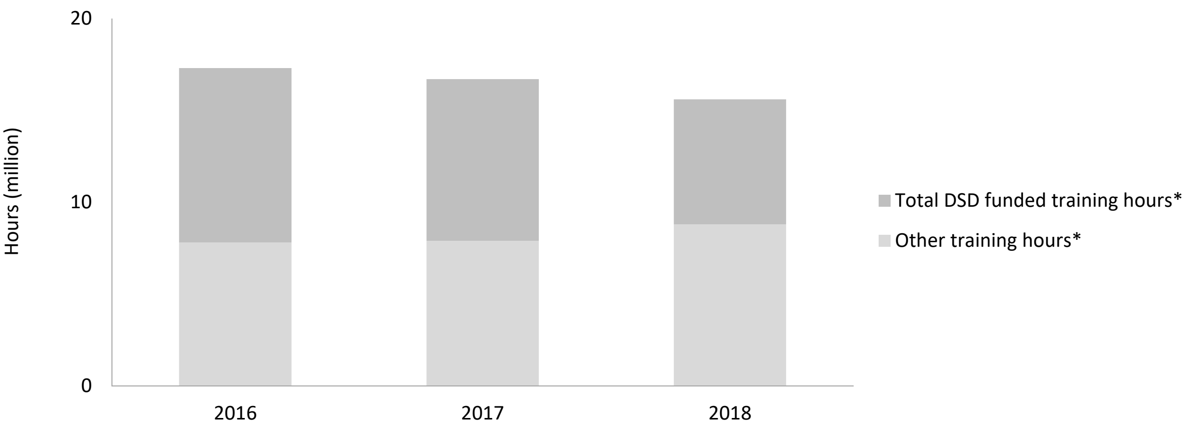
The VET subsidies component of the funding decreased by $24 million reflecting a decrease in training hours delivered, mainly due to reduced enrolments.

The following chart analyses the proportion of VET subsidies as part of overall DSD funding for the past three years, along with the total number of funded training hours delivered.



* Training hours provided by TAFE SA and unaudited.

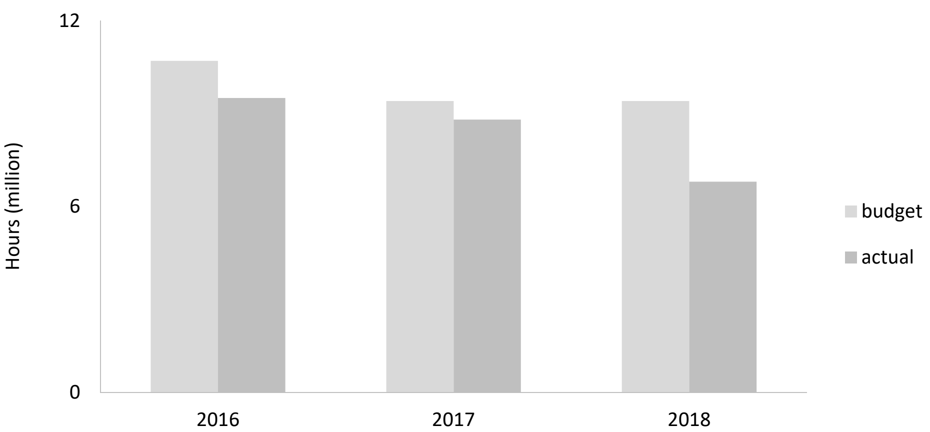
TAFE SA's overall training hours decreased further in 2017-18. The following chart shows the total training hours delivered by TAFE SA over the last three years, and the proportion funded by DSD.



* Training hours provided by TAFE SA and unaudited.

The chart highlights the overall reduction in the number of training hours delivered over the last three years. There has been a 10% overall reduction in this time, with 1.8 million less training hours delivered in 2017-18, compared to 2015-16. This overall reduction is broken down between a 28% reduction in DSD-funded training hours over the three years, partially offset by a 12% increase in other training hours.

The following chart analyses the actual training hours undertaken by TAFE SA for subsidised training compared to the budgeted training hours reflected in the MoAA for the last three years.



This shows that TAFE SA has consistently delivered less training hours than the agreed number in the MoAA, with 28% less hours delivered compared to budget for 2017-18.

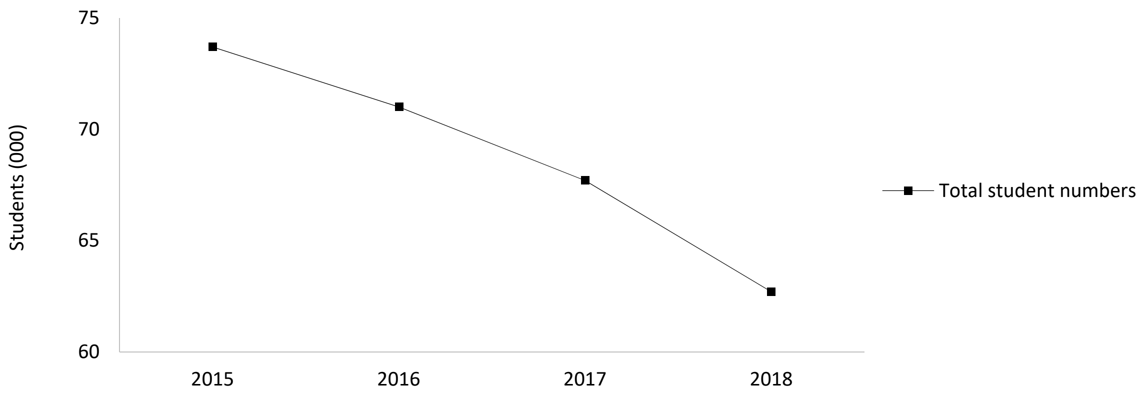
Student and other fees and charges

Student and other fees and charges totalled $89 million ($92 million) and make up 26% (28%) of TAFE SA's total income.

The main components of student and other fees and charges for the past three years are shown in the following chart.

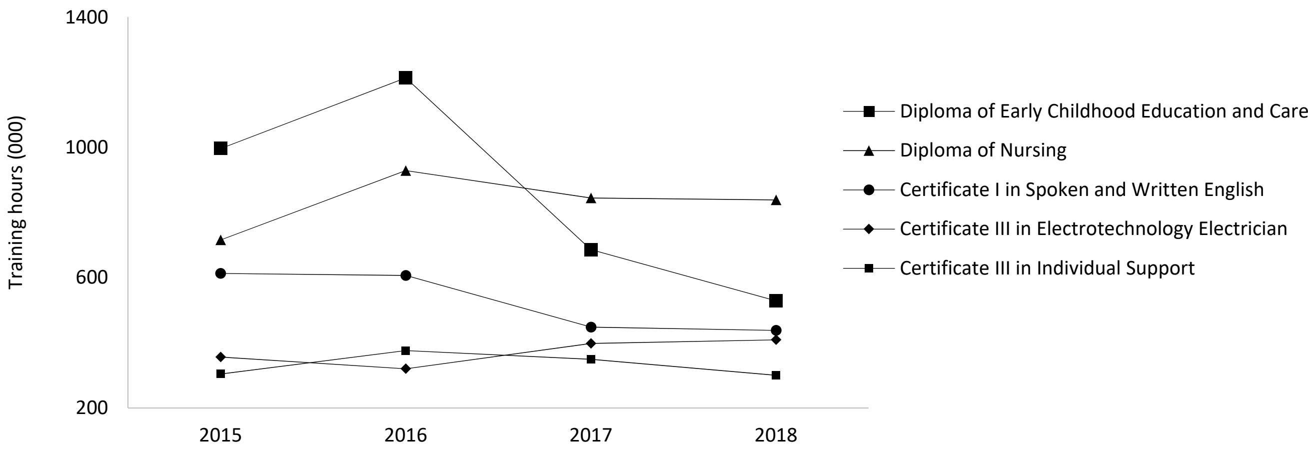
The chart illustrates that sales/fee-for-service income has remained steady over this period while student enrolment fees and charges have decreased by $5 million.

Total student numbers have decreased over the last four years as shown in the following chart.

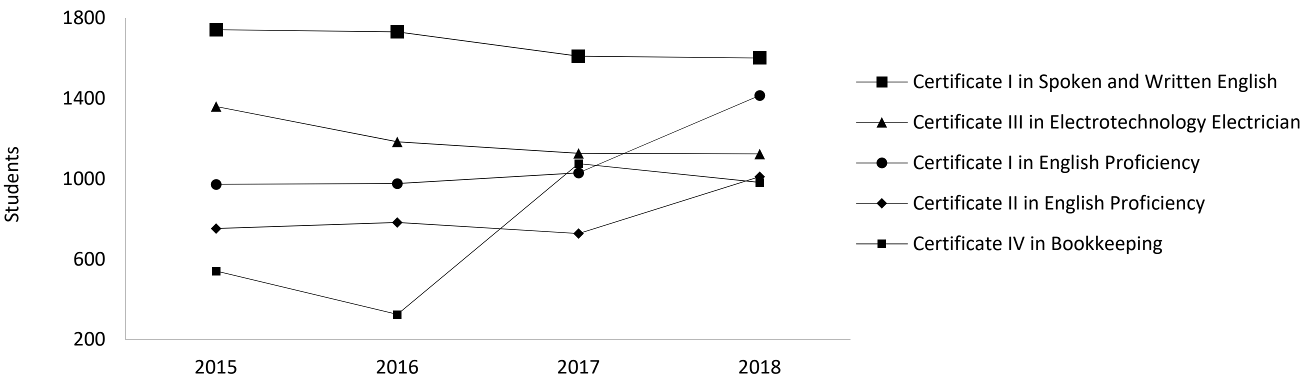


Source: Number of students data provided by TAFE SA and unaudited.

The chart below shows the number of training hours delivered in each of TAFE SA's top five courses (by revenue in 2017-18) over the last four years, showing the change in relative popularity of these courses over that time.



The chart below shows the relative popularity of TAFE SA's top courses when measured by the number of students over the same four year period, with a clear increase in the number of students studying English proficiency courses.



Statement of Financial Position

The most significant items in TAFE SA's Statement of Financial Position are shown in the following table.

	2017 $'million	2018 $'million
Assets		
Cash and cash equivalents	70	55
Receivables	19	20
Property and equipment and intangibles	26	27
Liabilities		
Payables	21	21
Employee benefits	59	61

Receivables as at 30 June 2018 include amounts owing from the Commonwealth Government of $5 million under the VET FEE-HELP and VET Student Loans schemes and amounts owed under the Skills for Education and Employment program. VET Student Loans commenced on 1 January 2017, replacing the VET FEE-HELP scheme. In addition, $4 million is GST recoverable from the ATO.

Employee benefits increased by $2 million. This was mainly due to an increase in accrued salaries and wages of $4 million due to the timing of the last pay date in June. This was partially offset by a decrease in the liability for long service leave of $2 million due to the number of TVSPs in recent years and other staff departures.

TAFE SA does not own its campus infrastructure, which is leased from DSD. Consequently, land and buildings are not a feature of TAFE SA's assets. TAFE SA recognises items of plant and equipment, leasehold improvements and intangible assets (software). Land and buildings used by TAFE SA are recognised as part of the URA's (previously DSD's) non-current assets.

Department of Treasury and Finance (DTF)

Financial statistics	Net cost of providing services:	$110 million
	Total revenues from SA Government:	$128 million
	Employee benefits expenses:	$77 million
	Revenues from fees and charges:	$73 million
	Administered taxation revenue:	$4.094 billion
	Administered Commonwealth revenues:	$9.118 billion
	Number of FTEs (including the South Australian Government Financing Authority, South Australian Superannuation Board, CTP Insurance Regulator, Office of the Valuer-General and the Office of the Registrar-General):	738

Significant events and transactions

- $1.525 billion received from Land Services SA (LSSA), a private sector operator, for the right to be the State's exclusive provider of land services, the right to exploit the State's land information assets and the right to use the State's software (the SAILIS system) for 40 years.
- $80 million received from LSSA for the right to negotiate to become the service provider for other State registries. The $80 million must be repaid, with interest, if the State does not give LSSA an exclusive right to negotiate for other State registries or extend the term of LSSA's 40-year contract.
- $56 million paid to LSSA for providing services to the State in 2018.
- The Office of the Valuer-General transferred from the Department of Planning, Transport and Infrastructure (DPTI) to DTF on 1 July 2017 followed by the Office of the Registrar-General on 1 February 2018. Both Offices transferred back to DPTI on 1 July 2018.
- The Valuer-General commenced a five-year project to ensure valuations of identified areas and property classifications remain sufficiently accurate and relative.

Financial report opinion — **Unmodified**

Financial controls opinion — **Unmodified**

Functional responsibility

DTF is an administrative unit established under the *Public Sector Act 2009*, and is responsible to the Treasurer.

DTF has a number of functions, including:

- setting economic and fiscal policy at the whole-of-government level
- managing whole-of-government financial management processes
- providing a range of direct whole-of-government services including funding and debt management, collection of state taxes and administration of insurance and superannuation
- administering the receipt of Commonwealth Government revenues and passing them on to relevant SA Government agencies.

Land services commercialisation

Appointment of Land Services SA as the exclusive provider of land services

The SA Government commercialised the State's land services operations in 2017-18.

On 10 August 2017, LSSA, a private sector operator, entered into a 40-year contract with the State to provide land services to customers on behalf of the SA Government under a fee-for-service arrangement. Services to be provided include land titling, registration and valuation services.

LSSA started providing land services to customers on 13 October 2017.

Under the contract, LSSA also received the exclusive right to commercialise land services data and introduce new products into the market subject to SA Government approval. If this occurs, LSSA must pay royalties to the State, which owns the underlying data.

The State received a $1.605 billion up-front payment from LSSA

On entering the contract, LSSA paid $1.605 billion to the State comprising:

- $1.525 billion principally for the right to be the exclusive provider of land services, the right to exploit the State's land information assets and the right to use the State's software (the SAILIS system)
- $80 million for the exclusive right to negotiate for a six-month period to become the service provider for other State registries that the State decides to commercialise. Under the contract this amount is to be repaid with interest if the State does not progress with the commercialisation of the motor vehicle registry within three years or does not extend the existing land services contract by seven years.

Benefits of the land services commercialisation to the State

Benefits to the State expected from the land services commercialisation include:

- reduced operating costs to the State and increased innovation for customers

- greater investment in systems and reduced risks to the State from future ICT upgrades
- improved State financial position.

Impact of land services commercialisation on the Registrar-General and the Valuer-General

Under the LSSA arrangements the statutory roles of the Registrar-General and the Valuer-General have continued with legal, policy and regulatory functions remaining with the Lands Titles Office (LTO) and the State Valuation Office (SVO). The Valuer-General also continues to oversee the objection and grievance process and valuations of SA Government owned land.

Fee rates for land titling, property valuations and other land services are still set by the SA Government under various legislation and the fees collected by LSSA are paid into the Consolidated Account.

The SA Government transferred the Office of the Valuer-General from DPTI to DTF on 1 July 2017 followed by the Office of the Registrar-General on 1 February 2018. The financial transactions of these Offices from these dates to 30 June 2018 are recognised in DTF's financial report as either controlled or administered items, including the land services transactions processed by LSSA on behalf of the SA Government.

Both Offices transferred back to DPTI on 1 July 2018.

DTF pays service fees to LSSA

In return for providing land services on behalf of the SA Government, DTF pays LSSA a land titling fee based on the types and volumes of transactions processed, less performance rebates applied for not achieving service level targets, and a valuation fee for providing valuations for use by SA Government agencies. Land services fees paid by DTF to LSSA were $43 million in 2018 and the valuation fee was $13 million, including $5 million for assisting the Valuer-General conduct a Revaluation Initiative.

DTF was appropriated funding for the LSSA fees, as the fees charged by LSSA to customers are paid into the Consolidated Account.

LSSA pays transitional service fees to DTF

Under a Transitional Services Agreement the State is helping LSSA transition into its role as exclusive provider of land services in the State by providing it with seconded LTO and SVO staff, IT support and other support services. DTF charges fees to LSSA for these services, with $6 million charged in 2017-18. At the end of the transition period, LSSA must resource its operations without State assistance. The transition period lasts two years but can be extended. LSSA has employed some of the seconded LTO and SVO staff while others remain DTF employees.

Accounting for the $1.605 billion up-front payment from LSSA

Background to the accounting approach

Accounting for the LSSA transaction required careful consideration.

The 2018-19 State Budget included commentary that the final accounting treatment was not resolved at the time the State Budget was tabled on 4 September 2018. This was a result of delays in receiving a fully developed position on the proposed accounting for the transaction from DTF. The accounting treatment of the LSSA transaction was finalised in the week after the State Budget was tabled.

Due to the complexity of the accounting considerations in this transaction, we started discussions with DTF about the accounting treatment in early 2018. DTF engaged a professional services firm to inform its accounting approach and worked to finalise its position on the accounting for this transaction between late July and early September 2018.

Accounting approach adopted

There is no current accounting standard or SA Government accounting policy applicable to this type of arrangement and transaction. In determining the accounting policy to be applied, DTF concluded that applying the concepts in AASB 1059 'Service Concession Arrangements: Grantors' provided the most relevant and reliable information to users. This was consistent with industry practice for this type of transaction. AASB 1059 was issued by the Australian Accounting Standards Board in July 2017, but will not be mandatory until 30 June 2020 financial reports.

Accordingly, DTF recognised a liability to reflect most of the amount received as unearned revenue. Revenue will be recognised on a straight-line basis over the 40-year term of the arrangement.

In applying the principles of AASB 1059 and industry practice, DTF also reclassified the SAILIS system and associated infrastructure as a service concession asset and revalued it on the basis of current replacement cost.

On transition to AASB 1059 in July 2020, a further asset – the data in the land title registries – will also need to be considered. These assets must be measured at current replacement cost under AASB 1059. A valuation determined with reference to market prices or income modelling is not permitted by AASB 1059. There is no standard industry practice of accounting for the value of such intangible assets as land title data in this manner.

Equivalent interstate accounting policies and international public sector accounting standards do not require recognition of internally generated intangible assets as is required on transition to AASB 1059. Some data included in the titles registry originated in the 1800s and estimating a replacement cost may present significant measurement difficulties. The State is seeking further clarification on the application of AASB 1059 principles to this aspect of the transaction.

DTF will continue to assess the impact of AASB 1059 on this transaction over the coming year.

Accounting impact in DTF's financial report

The accounting treatment applied to the transaction in October 2017 was:

- cash, $1.605 billion
- unearned revenue, $1.525 billion
- financial liability, $80 million (for the right to negotiate for the other registers).

Details of the accounting approach in DTF's financial report includes:

- the SAILIS system as a service concession asset in the controlled financial statements with a value of $17.1 million, following a revaluation of the system to its current replacement cost
- a liability for unearned revenue of $1.498 billion as at 30 June 2018 in the administered financial statements, representing the portion of the $1.525 billion received for the land services commercialisation which will be progressively recognised over the next 39 years
- a non-current payable of $80 million in the administered financial statements representing the upfront payment from LSSA for the exclusive right to negotiate on other State registries
- $27.2 million recognised in other revenue in the administered financial statements, being the portion of the $1.525 billion received for the transaction recognised as relating to the period between when LSSA commenced providing services in October 2017 and 30 June 2018.

Scope of the audit

The audit program covered major financial systems to obtain sufficient evidence to form an opinion on the financial report and internal controls. The audit program also considered the review work of DTF's internal audit section.

Specific areas of audit attention in 2017-18 included:

- accounting for the land services commercialisation
- taxation revenue
- payroll
- expenditure
- general ledger maintenance and reconciliations
- receipting and banking
- debtors follow-up
- system user access.

Financing and insurance services

Commentary on these activities is included under 'South Australian Government Financing Authority' in this Report.

Superannuation services

Commentary on these activities is included under 'South Australian Superannuation Board' in this Report.

Public finances

We review various aspects of the public finances. The results will be reported in a separate Report for the year ended 30 June 2018 on the State finances. The Treasurer's statements for the year ended 30 June 2018 will be published on the Auditor-General's Department website after this Report is tabled in Parliament.

Audit findings and comments

Communication of audit matters

A small number of matters identified by the audit were detailed in management letters to the Chief Executive. The main matters raised and related responses are detailed below.

Weaknesses in the IT controls of the RIO taxation system

The RevenueSA Information Online (RIO) taxation revenue management system is used to calculate and process payroll and land taxes as well as Emergency Services levies.

In our Supplementary Report for the year ended 30 June 2016 'RevenueSA Information Online system: October 2016' we detailed a number of weaknesses in the IT controls of the RIO system requiring remediation. In 2017 we followed up and confirmed that DTF had addressed many issues. There were, however, some unresolved issues including:

- segregation of duties conflicts
- excessive access to sensitive functions
- lack of periodic review of privileged user access and duty segregations
- increased restrictions required for access security.

We were advised by DTF that most of the remaining issues would be addressed by November 2017, and the rest by 30 June 2018.

We will confirm in 2019 that these remaining issues are properly addressed.

DCSI not promptly notifying DTF of clients no longer eligible for Emergency Services levy concessions

We reported in 2017 that the then Department for Communities and Social Inclusion (DCSI), now the Department of Human Services, was not promptly notifying DTF of clients who were no longer eligible for Emergency Services levy concessions and remissions. We also reported that concessions and remissions with an estimated value of $660 000 were applied to 3862 clients without sufficient evidence of ongoing eligibility. Our follow-up of this matter in 2018 indicated that DTF and the Department of Human Services had begun implementing agreements and processes to address this issue, but this remained work in progress.

We will confirm in 2019 that this issue is properly addressed.

Rectifying historical differences in the Treasurer's statements

We have previously reported that DTF had identified $57 million in historical differences between the balances recorded in the Treasurer's central general ledger and agency general ledgers. In 2017, DTF separately identified the $57 million in Treasurer's Statement C. It continued to recognise this amount separately in Treasurer's Statement C in 2018.

DTF is interrogating past transactions to isolate the cause of the historical differences so that appropriate corrections can be made to the central general ledger, with a view to finalising this matter in 2019.

Shared Services SA – financial systems and transaction processing environments

Shared Services SA processes financial transactions on behalf of DTF under service level determinations. The main systems and control environments include accounts payable, payroll and general ledger financial functions.

Our review and evaluation of controls for these systems concluded that controls were effective for 2017-18.

Shared Services SA is discussed further in the commentary under 'Department of the Premier and Cabinet' in this Report.

Interpretation and analysis of the financial report

Highlights of the financial report – controlled items*

	2018 $'million	2017 $'million
Expenses		
Employee benefits expenses	77	67
Supplies and services	108	50
Other expenses	7	5
Total expenses	192	122
Income		
Fees and charges	73	57
Other income	9	4
Total income	82	61
Net cost of providing services	110	61
Revenues from SA Government	128	73
Net result	17	12
Increase in intangible asset revaluation surplus	4	-
Net result and total comprehensive result	22	12
Assets		
Current assets	49	24
Non-current assets	76	51
Total assets	124	75
Liabilities		
Current liabilities	23	16
Non-current liabilities	22	18
Total liabilities	46	33
Total equity	79	41

* Table may not add due to rounding.

Statement of Comprehensive Income (controlled items)

Expenses

Expenses increased by $70 million to $192 million in 2018 mainly due to:

- employee benefits expenses increasing by $10 million mostly due to FTEs increasing when the Office of the Valuer-General and the Office of the Registrar-General transferred to DTF, and changes to the method used by the actuary to calculate the provision for workers compensation.

  Employee expenses also include salaries and wages for staff provided by DTF to support the South Australian Government Financing Authority (SAFA), the South Australian Superannuation Board and the CTP Insurance Regulator. DTF recovers employee costs from these agencies under service level arrangements

- a $58 million increase in supplies and services expenses mainly due to:
  - a new type of payment consisting of service fees paid to LSSA of $43 million for providing land titling, registration and valuation services to customers on behalf of DTF and the State
  - an $8 million increase in valuation fees mainly due to payments to LSSA of $13 million for providing valuations for use by SA Government agencies and for assisting the Valuer-General to perform a Revaluation Initiative (see 'Revaluation Initiative' below for more details). An expense of $5 million in 2017 represented payments to DPTI for these services for RevenueSA previously, with this fee now an internal elimination between DTF divisions
  - a $2 million increase in accommodation costs mostly due to the use of more office space resulting from the transfer of the Office of the Valuer-General and the Office of the Registrar-General to DTF
  - a $2 million increase in contractors expense mainly due to IT contractors developing new software for RevenueSA and Super SA
  - a $4 million increase in other supplies and services expense mostly due to payments to DPTI for providing support services to LSSA. DTF then bills LSSA for these services.

Income

Income increased by $20 million to $82 million in 2018 mainly due to:

- $16 million more in fees and charges mainly due to:
  - $10 million of land titling, registration and valuation fees collected by LSSA on behalf of DTF
  - $5 million more in other fees and charges mostly due to DTF billing LSSA for support services provided by DPTI to LSSA
- a $5 million increase in other income mainly due to DTF charging fees to SA Government agencies for providing them with valuations.

Revenues from SA Government

Revenues from the SA Government increased by $55 million to $128 million mainly due to an extra $50 million received from the Governor's Appropriation Fund to pay LSSA fees.

Statement of Financial Position (controlled items)

Assets

Total assets increased by $50 million to $124 million in 2018 due mainly to:

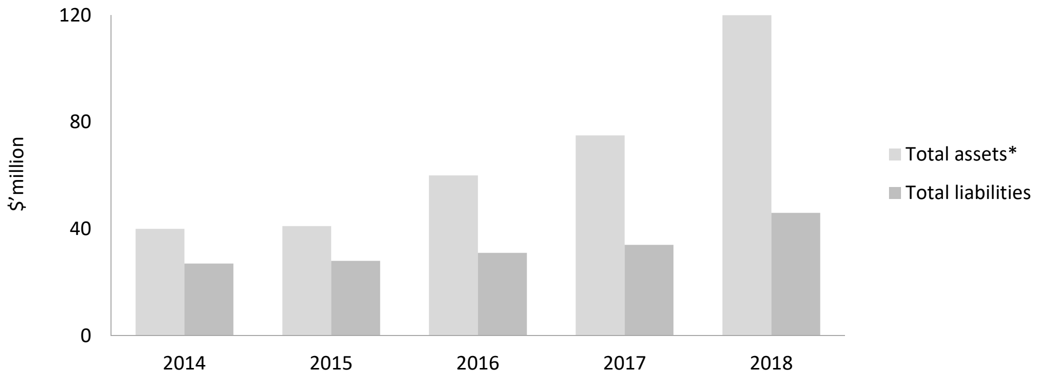
- a $14 million increase in receivables from DPTI, mostly representing assets held by DPTI on behalf of the Office of the Valuer-General and the Office of the Registrar-General that were not transferred to DTF in the 2017-18 administrative restructures as they will be transferred back to DPTI in 2018-19 restructures
- a $23 million increase in intangible assets, including $10 million for new software being developed for RevenueSA and Super SA and $13 million relating to the SAILIS system transferred to DTF from DPTI and used by the Office of the Registrar-General, offset by $4 million in amortisation expense. As a result of the LSSA transaction, SAILIS was revalued upwards by $4 million and reclassified as a service concession asset, as discussed under ' Accounting approach adopted' above
- a $7 million increase in cash due to receipts and equity contributions from the SA Government of $131 million being $7 million higher than the amounts used in operating and investing activities.

Liabilities

Total liabilities increased by $13 million to $46 million in 2018 mainly due to:

- a $6 million increase in payables mostly due to accrued fees owed to LSSA
- a $2 million increase in employee benefit liabilities mainly due to FTEs increasing when the Office of the Valuer-General and the Office of the Registrar-General transferred to DTF
- a $3 million increase in provisions resulting from changes to the method used by the actuary to calculate the provision for workers compensation and one newly deemed seriously injured claimant.

The following chart shows the movements in DTF's assets and liabilities since 2014.



* Total assets for 2016 and 2017 include $10 million for the construction of the ANZAC Centenary Memorial Garden Walk.

Total assets and liabilities remained relatively stable in 2014 and 2015. The significant increase in total assets in 2016 and 2017 is due to construction of the ANZAC Centenary Memorial Garden Walk and new software being developed for RevenueSA and Super SA. The significant increase in assets and liabilities in 2018 reflects the impact of the transfer of the Office of the Valuer-General and the Office of the Registrar-General to DTF.

Statement of Cash Flows

Significant changes in the cash flow amounts between 2017 and 2018 are largely attributable to the transfer of the Office of the Valuer-General and the Office of the Registrar-General to DTF. Notably, there was a $58 million increase in receipts from the SA Government that was partially offset by a $54 million increase in supplies and services payments, mostly due to service fees paid to LSSA.

Highlights of the financial report – administered items

The administered financial statements mainly reflect DTF's transactions on behalf of the SA Government for the Consolidated Account. The Consolidated Account result for 2018 is reported in the Treasurer's statements (published on the Auditor-General's Department website).

	*2018 $'million	*2017 $'million
Expenses		
Payments to SA Government	13 507	11 006
Grants, subsidies and transfers	3 356	2 873
Other expenses	819	1 216
Total expenses	17 682	15 095
Income		
Taxation	4 094	4 083
Commonwealth revenues	9 118	8 312
Revenues from SA Government	1 796	1 490
Other revenues	1 193	1 213
Total income	16 201	15 098
Net result	(1 482)	3
Assets		
Current assets	1 261	1 043
Non-current assets	13	12
Total assets	1 273	1 055
Liabilities		
Current liabilities	920	742
Non-current liabilities	1 573	34
Total liabilities	2 493	776
Total equity	(1 220)	279

* Table may not add due to rounding.

Administered expenses

Payments to the SA Government increased by $2.5 billion to $13.5 billion in 2018 due to a $1.525 billion up-front payment received from LSSA for the right to provide land titling, registration and valuation services on behalf of the State for 40 years on a fee-for-service basis and for the right to

exploit the State's land information assets. The up-front payment was paid into the Consolidated Account and is recognised as unearned revenue.

The remainder of the increase in payments to the SA Government represent increased revenue received by DTF on behalf of the Consolidated Account including:

- an $806 million increase in Commonwealth revenue comprising mainly a $499 million increase in GST revenue grants and a $273 million increase in funding received under the Inter-Governmental Agreement on Federal Financial Relations (IGAFFR)
- a $38 million increase in dividends from SA Government agencies due mostly to increases of $18 million from the South Australian Water Corporation, $12 million from HomeStart Finance and $7 million from the Urban Renewal Authority. Dividends received in 2018 were $207 million ($169 million)
- $27 million reflecting the straight-line apportionment of the $1.525 billion of unearned revenue received from LSSA
- an $11 million increase in taxation revenue due mostly to:
  - increases of $82 million in payroll tax, $79 million in income tax equivalents paid by SA Government agencies and $32 million from the new betting operations tax applied from 1 July 2017 on wagering revenue of betting companies offering services in the State
  - $159 million less land tax due mainly to SA Government agencies, including the South Australian Housing Trust, not being invoiced in 2016 and having to pay two years' worth of land tax in 2017
  - $43 million less stamp duties on property sale conveyances.

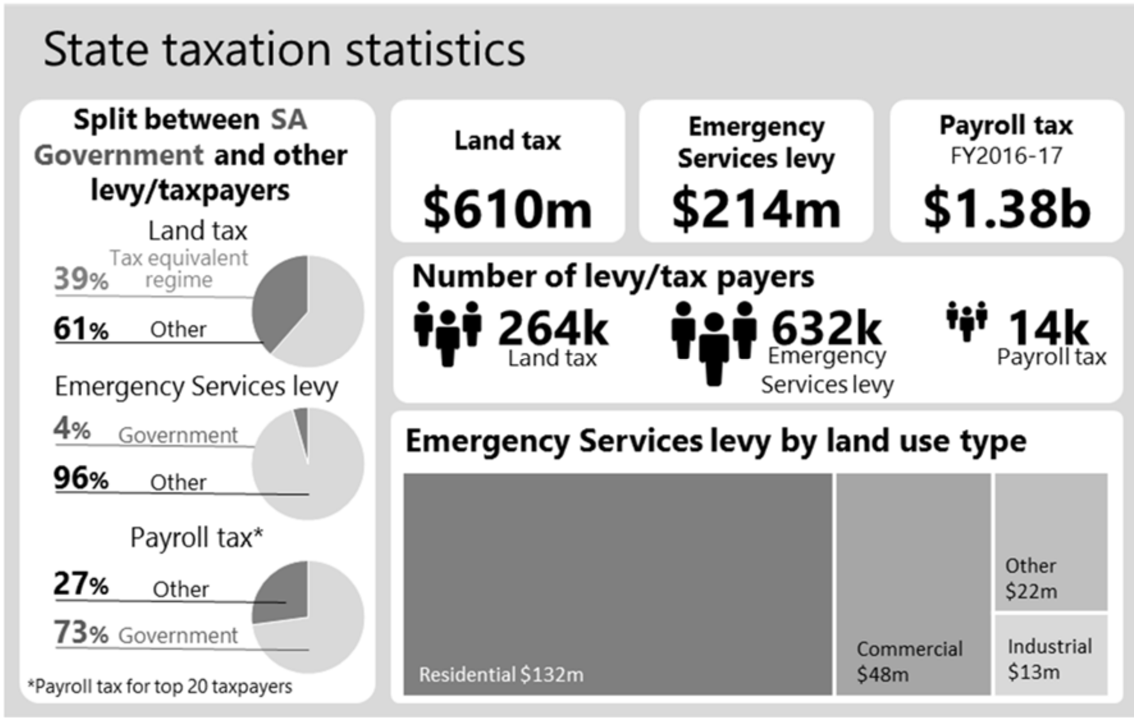
Grants, subsidies and transfers increased by $483 million to $3.4 billion in 2018, mainly due to the transfer of increased funding from the Commonwealth under the IGAFFR to relevant SA Government agencies and more payments for purposes approved by the Treasurer using appropriations from the Treasury and Finance administered items account. These payments included $170 million to DPTI for the Goodwood and Torrens rail junctions, $86 million to the Department of the Premier and Cabinet for the Our Energy Plan and $63 million to the Department for Health and Wellbeing to meet increased service demands in the public health system.

Other expenses fell by $397 million to $819 million in 2018 due mainly to once-off payments of $381 million in 2017 comprising: $259 million received from four private insurers for initial market shares under the compulsory third party (CTP) insurance market reforms which DTF paid into the DPTI Highways Fund; and $121 million in transitional CTP premiums paid to the private insurers for taking the insurance risk of insurance policies novated to them.

Administered revenue

The following table of State taxation statistics shows that SA Government agencies paid:

- 39% of land tax but only 4% of the Emergency Services levy in 2017-18
- 73% of payroll tax collected by RevenueSA from the top 20 taxpayers in 2016-17. We have not included in our statistics the payroll tax paid in 2017-18 as the amount payable by employers will not be finalised until their tax assessments are determined in 2018-19.



Administered net assets

Net assets changed from $279 million in 2017 to negative $1220 million in 2018. This was due to administered liabilities increasing by $1716 million mostly due to unearned revenues from the land services commercialisation and revenues collected but not yet paid into the Treasurer's account, while administered assets increased by $218 million due to a $218 million increase in cash.

Further commentary on operations

Revaluation Initiative

A key function of the Valuer-General under the V*aluation of Land Act 1971* is to undertake general valuations of South Australian properties. The valuations are the basis for calculating various State and Local Government taxes, rates and levies.

The general valuations are determined using mass appraisal techniques and manual valuation approaches. An indexation approach is the primary mass appraisal technique used since the mid-1980s. The indexation approach means that any error in the existing valuation is carried over to the next valuation. The Valuer-General decided that a review of the valuation roll was required to ensure the valuations remain sufficiently accurate and relative. To achieve this, the Valuer-General is undertaking a five-year project (Revaluation Initiative) to review site values and capital values across identified areas and property classifications. DTF pays LSSA a fee for assisting the Valuer-General to perform the Revaluation Initiative.

Commonwealth Government funding arrangements

The IGAFFR is the framework for the Commonwealth's financial relations with the states and territories.

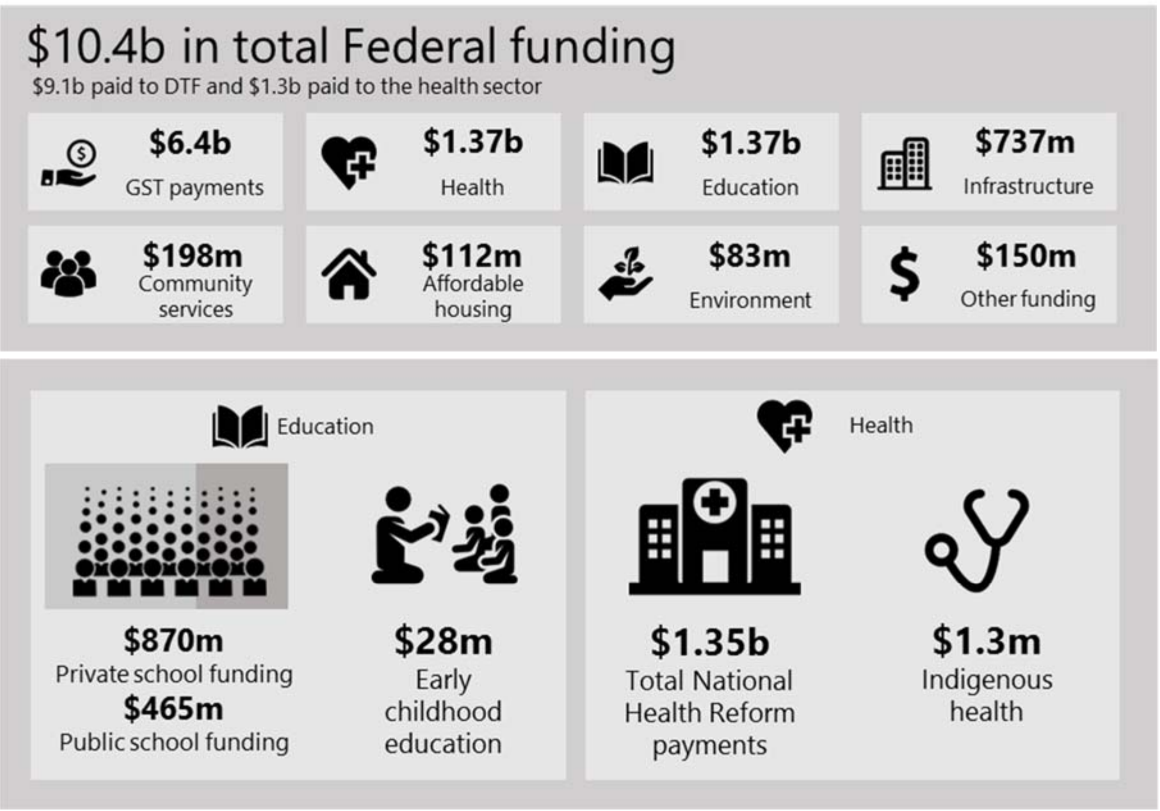
The IGAFFR provides for the following types of Commonwealth payments:

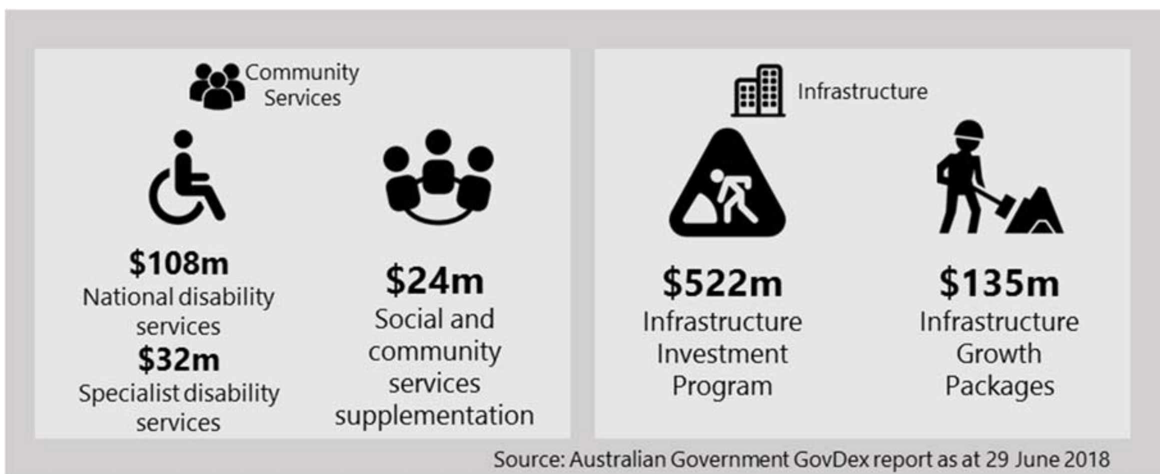
- general revenue assistance, including the ongoing provision of GST payments, to be used by the states and territories for any purpose
- national specific purpose payments (SPPs) to be spent in the key service delivery sectors agreed to between the Commonwealth and the states. Each national SPP is linked to a national agreement that contains objectives, outcomes, outputs and performance indicators, and clarifies the roles and responsibilities of each jurisdiction
- national partnership payments to support the delivery of specified outputs or projects, to facilitate reforms or to reward those jurisdictions that deliver on nationally significant reforms.

Under the IGAFFR all Commonwealth funding, with the exception of funding under the National Health Reform Agreement and the National Education Reform Agreement, is provided to DTF, which distributes funds to agencies. The Treasurer has established a special deposit account to receive and disburse money paid to the State for the national SPP purposes listed in Schedule F of the IGAFFR and the national partnership payments purposes listed in Schedule G.

The balance of the IGAFFR account at 30 June 2018 was $26 million ($11 million). This represents funds that DTF is yet to transfer to other agencies.

Commonwealth funding was provided in 2018 for the purposes shown in the following table. The Commonwealth provided $9.1 billion to DTF and $1.3 billion directly to the health sector. Of the Commonwealth funding, 61% related to GST revenue grants of $6.4 billion which can be used for any purpose, whereas most of the remaining Commonwealth funding is for specific purposes.





Future Jobs Fund

The former SA Government created a $200 million future jobs fund in 2017 to attract new businesses to South Australia, support local industries to grow, build new industries, support sectors already competing successfully and create incentives to encourage businesses to invest.

$120 million of the fund was apportioned to DTF, $60 million to the Department of State Development and $20 million to the South Australian Tourism Commission.

The $120 million apportioned to DTF was available to businesses for job creation, including $70 million available as low interest loans and $50 million available as grants. Applications from businesses for loans and grants closed on 29 September 2017.

As at 30 June 2018 approved loan applications were $44.4 million with $286 000 drawn down, leaving an undrawn loan balance of $44.1 million. The loans drawn from the Consolidated Account are recognised as Treasurer's loans in the Treasurer's statements and as recurrent transfers to the DTF loans administration account, which is administered by SAFA, in DTF's administered financial statements.

As at 30 June 2018 approved grant applications were $41.3 million with $11.3 million drawn down, leaving an undrawn grant balance of $30 million. The grants drawn down are recognised as recurrent grants in DTF's administered financial statements.

The 2018-19 State Budget announced that the Future Jobs Fund would be closed.

Economic Investment Fund (EIF)

The SA Government announced that funding for the EIF managed by Investment Attraction South Australia (IASA) would cease in 2019. IASA provided loans and grants from the EIF for projects that deliver significant economic benefits to the State by attracting large interstate and overseas companies to relocate to or expand their operation in South Australia.

As at 30 June 2018, loan applications approved totalled $21.2 million of which $5.5 million was drawn down, leaving an undrawn loan balance of $15.7 million. The loans drawn from the Consolidated Account are recognised as Treasurer's loans in the Treasurer's statements and as recurrent transfers to the DTF loans administration account, which is administered by SAFA, in DTF's administered financial statements.

Grants provided from the EIF are recognised in the financial statements of IASA.

University sector overview

Overview

The Auditor-General audits the following South Australian universities:

- Flinders University
- University of Adelaide
- University of South Australia.

They are the State's three public universities. They advance learning and knowledge in South Australia by providing university education and conducting research activities.

Sector summary

Financial statistics

The following table shows key financial statistics for the three universities.

	2017 $'million	2016 $'million
Australian Government financial assistance	1 220	1 233
Fees and charges revenue	483	454
Employee related expenses	1 196	1 169
Assets	4 650	4 543
Liabilities	1 105	1 101

	2017 Number	2016 Number
FTEs	8 386	8 334
Students (EFTSLs)	60 572	60 863

Financial report opinions

We issued audit opinions for each university's financial report. Flinders University and the University of Adelaide received unmodified opinions.

Consistent with prior years, we modified the financial report opinion for the University of South Australia. In our opinion, its accounting for grant revenue does not comply with Australian Accounting Standards. This is further discussed in the University of South Australia's commentary under 'Auditor's report on the financial report'.

Financial control opinions

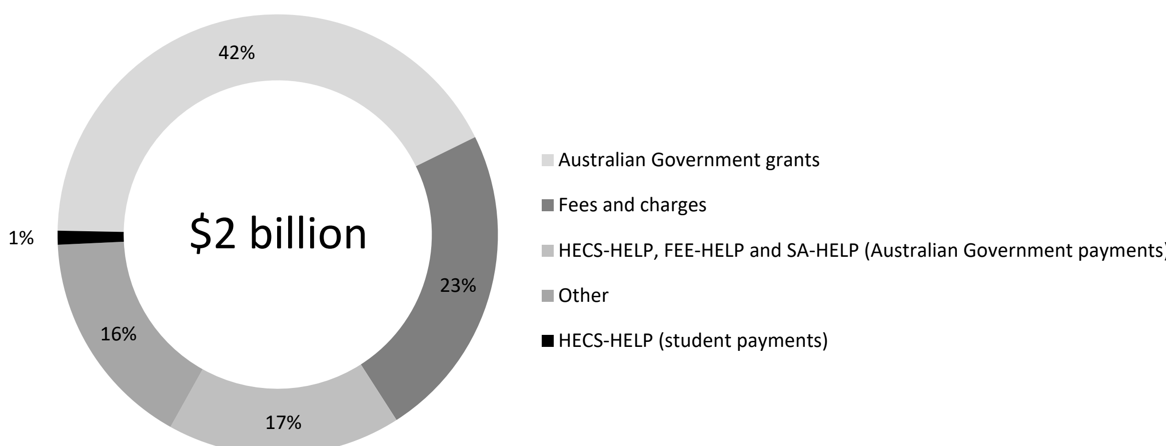
All three universities received modified control opinions. The individual matters resulting in these modifications are disclosed in each university's commentary under 'Communication of audit matters'.

We noted some commonality in the areas we identified across the universities. In particular, there were opportunities to improve controls over the management of payments to staff and staff leave entitlements.

Key financial statistics

Income

Total income for the three universities was $2 billion in 2017. The sources of income are presented in the following chart.



Australian Government grants and payments

The universities are highly dependent on Australian Government financial assistance. This constituted 60% of their total income in 2017. It comprises the Commonwealth Grants Scheme, Higher Education Loan Program (HELP) income, research grants and other funding.

Further information is included in each university's commentary under 'Statement of Comprehensive Income'.

Fees and charges

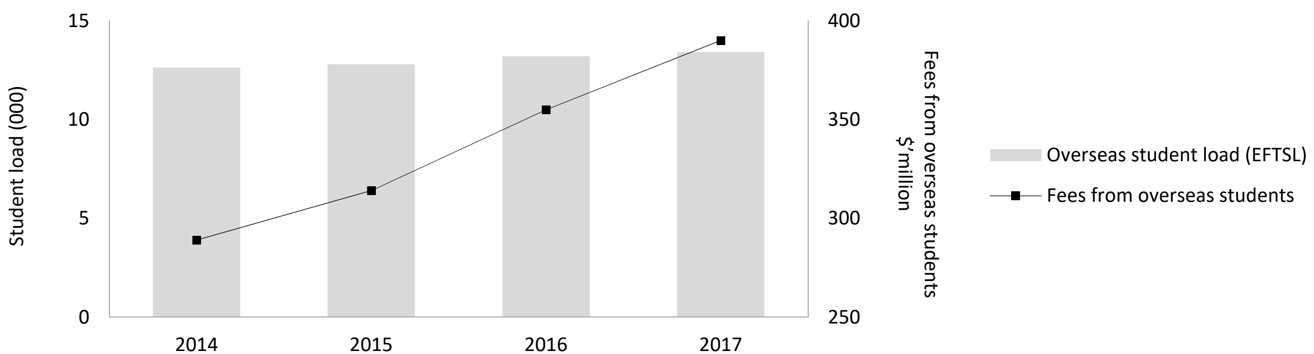
In the last four years, fees and charges across the universities have increased by 27%, from $381 million in 2014 to $483 million in 2017. The main driver of this increase has been fees and charges generated from overseas students.

The following table shows that total student loads have marginally increased over the last four years, with the sources of students remaining relatively stable at 78% domestic and 22% overseas in 2017.

	2014 Number	2015 Number	2016 Number	2017 Number
Domestic students	47 427	47 466	47 666	47 161
Overseas students	12 629	12 790	13 197	13 411
Total students	60 056	60 256	60 683	60 572

Source: Student numbers, which are based on equivalent full-time student load (EFTSL), were obtained from data published by the three universities and are unaudited.

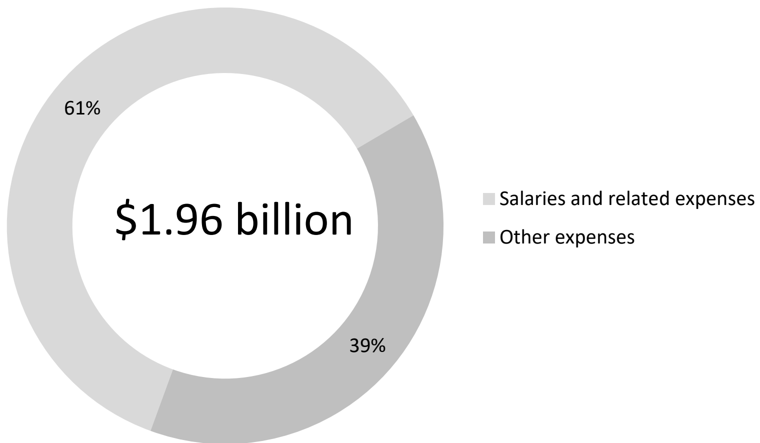
Revenue from fees and charges from overseas students increased by 35% across the last four years to $390 million in 2017. The number of overseas students increased by only 6% over this time.



Source: Student numbers, which are based on EFTSL, were obtained from data published by the three universities and are unaudited.

Expenditure

Total expenditure for the three universities was $1.96 billion in 2017. The sources of expenditure are presented in the following chart.



Employee related expenses

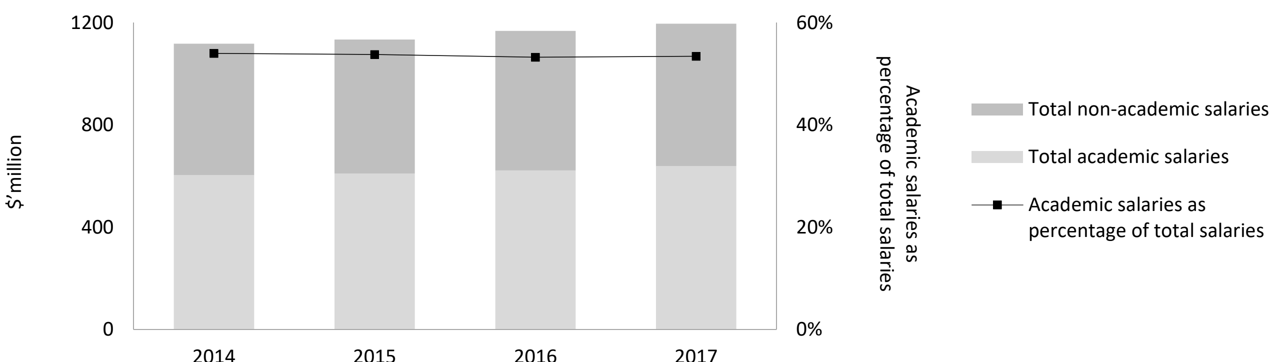
In the last four years, employee related expenses across the universities increased by 7% from $1.12 billion in 2014 to $1.19 billion in 2017.

The following table shows total staff numbers for all three universities, based on FTEs.

	2014 FTEs	2015 FTEs	2016 FTEs	2017 FTEs
Academic	3 785	3 781	3 634	3 681
Non-academic	4 804	4 761	4 700	4 705
Total FTEs	8 589	8 542	8 334	8 386
Percentage of academic staff	44%	44%	44%	44%

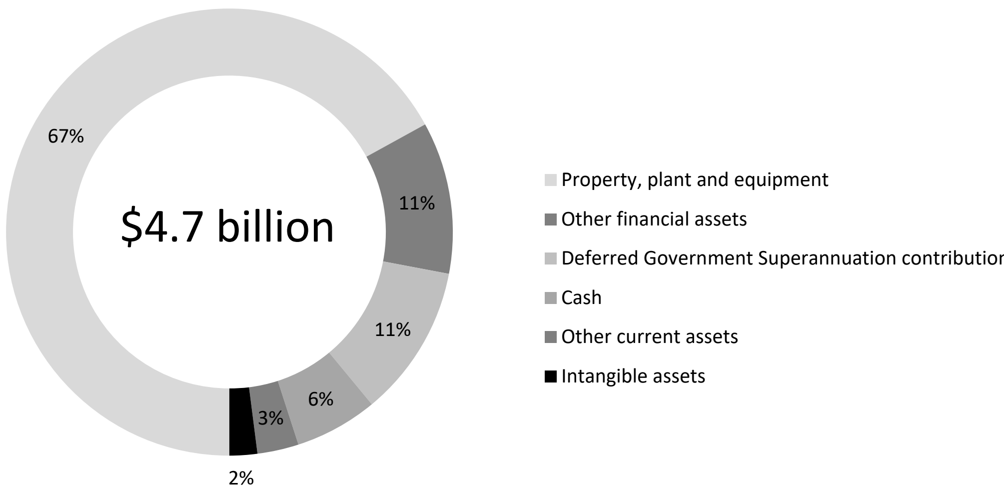
Source: Staff numbers, which are based on FTEs, were obtained from data published by the three universities and are unaudited.

The following chart shows academic salaries as a percentage of total salaries. The percentage remained consistent at 54% for 2014 and 2015, with a slight decrease to 53% in 2016 and 2017.



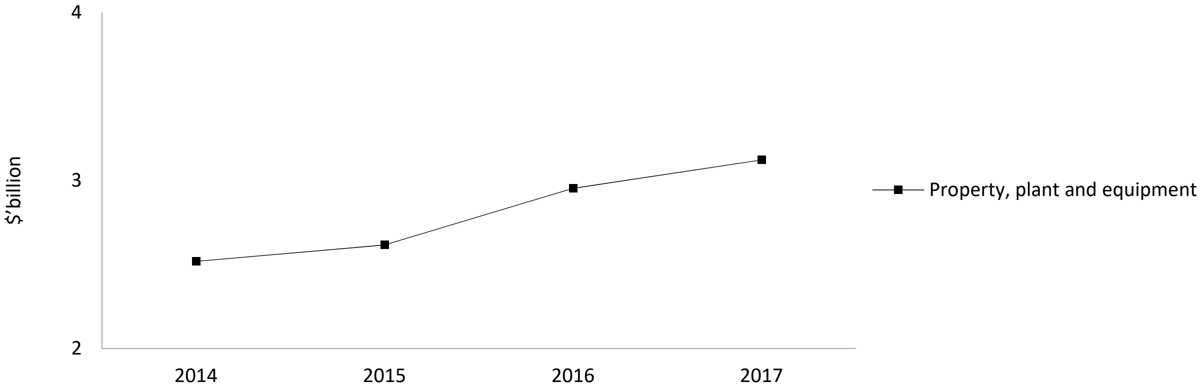
Assets

Total assets for the three universities were $4.7 billion in 2017. The categories of assets are presented in the following chart.



Property, plant and equipment

Property, plant and equipment totals $3.1 billion, which is 67% of the total value of assets held by the three universities. It primarily consists of $2.17 billion of buildings and infrastructure (70%) and land of $419 million (13%). The following chart shows the value of property, plant and equipment over the last four years.



In 2016 all three universities revalued their land, buildings and infrastructure. This resulted in a collective net revaluation gain across the universities of $110 million.

Capital work in progress totalled $292 million ($362 million) as at 31 December 2017 for the three universities. The decline is attributable to the completion of major capital works projects for the University of Adelaide and the University of South Australia in particular. Further information on individual large capital works is provided in the commentary for each university under 'Statement of Financial Position'.

Deferred Government Superannuation contribution

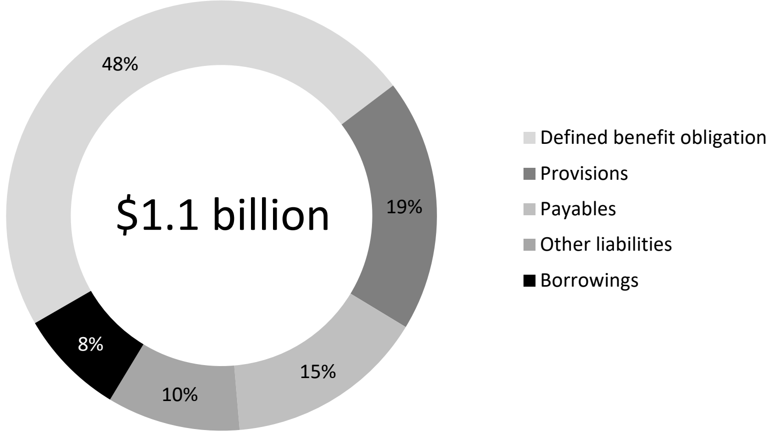
A number of present and former employees of the three universities, and their predecessor institutions, are members of state managed superannuation schemes. Under current arrangements the Commonwealth Government funds the universities on an emerging cost basis.

The defined benefit obligations of all three universities totalled $532 million, with a corresponding receivable of the same value being recognised from the Commonwealth Government. The receivables represent 11% of total assets held by the three universities.

For information on the individual schemes refer to the 2017 financial report for each university.

Liabilities

Total liabilities for the three universities were $1.1 billion in 2017. The categories of liabilities are presented in the following chart.



Defined benefit obligation

Defined benefit obligations total $532 million, 48% of the liabilities held by the three universities, and are offset by deferred government contributions as explained under 'Deferred Government Superannuation contribution' above.

Provisions

Provisions total $210 million, 19% of the liabilities held by the three universities.

Provisions primarily comprise $129 million in long service leave liabilities and $68 million in annual leave liabilities.

Emerging issues

The University of Adelaide and University of South Australia agree to explore the merits of a potential merger

In June 2018 the Chancellors of the University of Adelaide and the University of South Australia announced that the two universities would explore the merits of a potential merger to create a new, leading Australian university. They agreed to explore whether a merged university would generate a stronger institution that has the potential to deliver greater outcomes for South Australia and the relevant student bodies.

Both University Councils have endorsed a six-month period of collaboration to discuss a potential merger, with the two Vice-Chancellors, Professor David Lloyd (University of South Australia) and Professor Peter Rathjen (University of Adelaide), to oversee a joint report to be delivered by the end of 2018. The Councils will consider the report and determine the merits and viability of progressing with a merger.

Changes to Commonwealth funding arrangements

As noted above, the university sector in South Australia receives 60% of its funding from the Commonwealth Government, meaning changes to those funding arrangements will impact the sector.

The Commonwealth Government announced a freeze on increases for Commonwealth Grant Scheme funding payable for bachelor degree courses in December 2017.

This funding was previously demand driven, increasing in line with student numbers. However, funding in 2018 and 2019 will be capped at 2017 levels, regardless of any growth in student numbers. The number of Commonwealth supported places is not capped under this scheme. Universities will still receive the normal Commonwealth Grant Scheme payments for each place up to the cap limit on the same basis as previously used for funding Commonwealth supported places in designated courses.

The Commonwealth Government has announced that from 2020 onwards, increases in funding will be possible, based on meeting certain performance based requirements – which have not yet been determined.

The Commonwealth Department of Education and Training's four-year funding projections forecast the following revenue declines as a consequence of the freeze.

	%	Impact over four years $'million
Flinders University	9.8	115
University of South Australia	5.7	83
University of Adelaide	4.2	53

Source: Data obtained from published media reports based on Department of Education and Training documents obtained through Freedom of Information applications and unaudited.

Total base funding will continue to grow over this period, but at a slower rate.

The total amount of assistance a student can access under the HELP scheme will also be capped from 1 January 2019.

Flinders University (Flinders)

Financial statistics	Net result:	$26 million
	Australian Government financial assistance:	$330 million
	Number of FTEs:	1 918
	Number of students (EFTSLs):	17 289

Significant events and transactions

- Flinders implemented the first elements of a significant organisation structure change to move from four faculties and 14 schools to six colleges.
- Accompanying the organisation structure change, Flinders also implemented a Professional Services Project to align professional services to the new college structure.

Financial report opinion

Unmodified

Financial controls opinion

Modified

Key issues:

- Supervisor review of payroll payments not performed with sufficient frequency
- Finance systems segregation of duties could be strengthened

Functional responsibility

Flinders is established by the *Flinders University Act 1966*.

The functions of Flinders include establishing and providing educational facilities and courses of study at a university standard, and generally disseminating knowledge and promoting scholarship.

Scope of the audit

The audit program covered major financial systems to obtain sufficient evidence to form an opinion on the financial report and internal controls.

Specific areas of audit attention in 2017 included:

- payroll
- property, plant and equipment
- Commonwealth financial assistance
- student revenue
- research grant revenue
- cash and investments
- general ledger and reporting
- expenditure.

Internal audit activities were reviewed to assess the risks of material misstatement in the financial report and to design and perform audit procedures.

The audits of Flinders' controlled entities for the year ended 31 December 2017 were carried out by private accounting firms.

Audit findings and comments

Assessment of controls

In my opinion, the controls exercised by Flinders University in relation to the receipt, expenditure and investment of money, the acquisition and disposal of property and the incurring of liabilities, except for all matters outlined under 'Communication of audit matters', are sufficient to provide reasonable assurance that the financial transactions of Flinders University have been conducted properly and in accordance with law.

Communication of audit matters

Matters identified by the audit were detailed in a management letter to the Vice-Chancellor. The main matters raised are detailed below. The matter relating to payroll has been raised in prior years.

Payroll

Supervisor review of payroll payments not performed with sufficient frequency

Consistent with prior years, we identified that supervisor review of payroll bona fide reports was not regular enough to identify invalid, inaccurate or incomplete processing of payments, with the review only undertaken bi-annually. While Flinders performs a number of other processes for employees and has project reporting tools for managers, the reporting of these items is only on an exception basis.

Flinders indicated that it considers its current bona fide process satisfactory, making reference to preventative and detective controls, budget reviews and additional scrutiny coming from the Professional Services Project.

Finance systems segregation of duties could be strengthened

There was significant structural change at Flinders as it transitioned to providing centralised financial services to support the new college structure. We noted instances where segregation of duties could be improved in a number of functions across its finance systems. We considered this was an increased risk due to staff performing higher duties and additional roles while the new structure was implemented. While we identified this risk, we found no material breakdown of internal controls in our testing.

In response Flinders noted that it had undergone a major organisation change through the Professional Services Project and had invested significant time to design and improve organisational structures and internal controls. During the change, Flinders advised that all conflicting accesses had compensating controls implemented to mitigate the residual risk. Flinders also noted it would continue to perform an annual segregation of duties review and actively monitor any conflicts.

Interpretation and analysis of the financial report

Highlights of the financial report

	2017 $'million	2016 $'million
Income		
Australian Government grants	228	234
HECS-HELP, FEE-HELP and SA-HELP (Australian Government payments)	102	98
HECS-HELP (student payments)	7	8
Fees and charges	103	94
Other	57	56
Total income	497	490
Expenses		
Employee related expenses	310	314
Other expenses	161	148
Total expenses	471	462
Operating result	26	28
Net cash provided by (used in) operating activities	77	63
Net cash provided by (used in) investing activities	(87)	(53)

	2017 $'million	2016 $'million
Assets		
Current assets	119	104
Non-current assets	770	743
Total assets	889	847
Liabilities		
Current liabilities	86	72
Non-current liabilities	72	77
Total liabilities	158	149
Total equity	731	698

Income Statement

Income

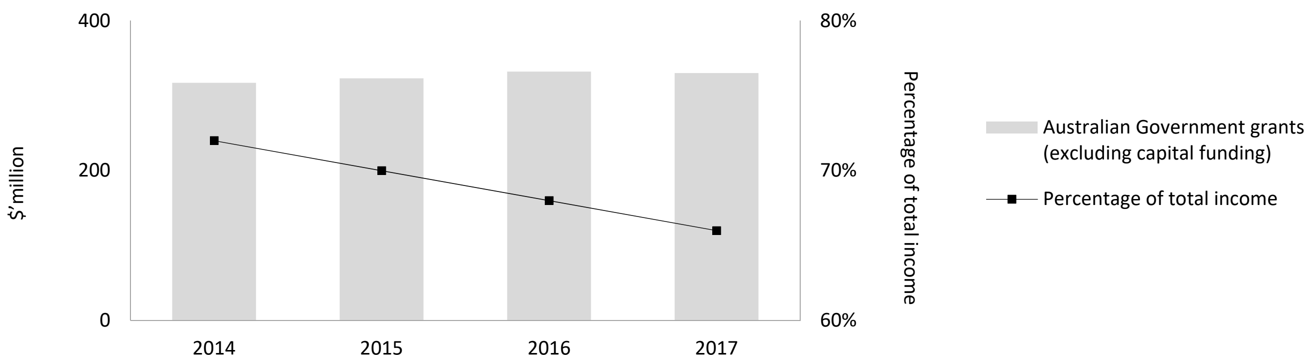
Flinders' income remained steady with an increase of 1% in 2017, with decreases in Australian Government grants offset by increases in fees and charges as explained below.

Australian Government grants and payments

The total Australian Government financial assistance received by Flinders in 2017 decreased by $3 million to $330 million.

The chart below shows Australian Government grants and payments, excluding capital funding as this is not necessarily comparable from year to year. It shows that the proportion of non-capital Australian Government grants and payments to total income was highest in 2014 and has trended progressively lower in more recent years.

The continuing decrease in 2017 reflects the continued growth in fees and charges for the year.



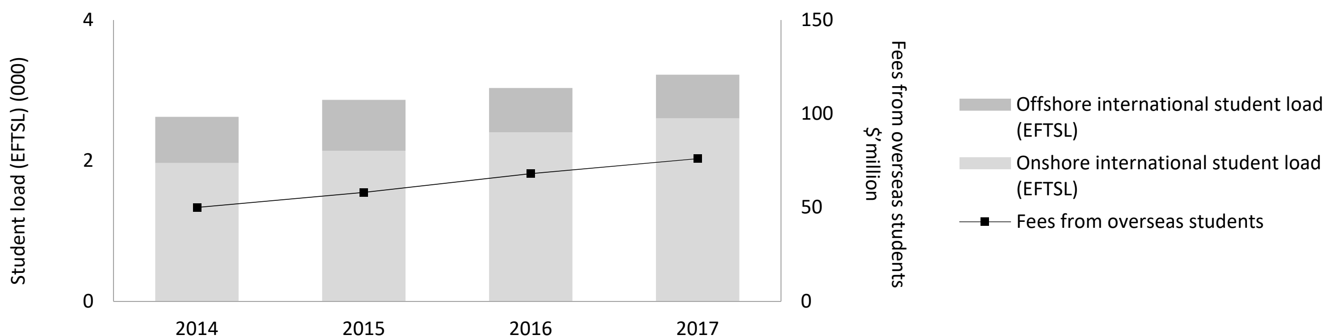
Australian Government grants and payments include the following major items:

- $102 million Higher Education Loan Program (HELP) funding including HECS-HELP. In 2017 HECS-HELP funding increased by $3 million (3%) to $90 million, primarily due to growth in Commonwealth supported places (3%), price indexation and growth in the proportion of students opting to defer their contribution through the HELP program
- $50 million Australian Government funding for research activities including competitive research grant programs and research infrastructure grants, which was a $4 million decrease in funding for 2017

- $149 million Commonwealth Grants Scheme funding for Commonwealth supported student places. Commonwealth Grants Scheme funding increased by $4 million (3%) primarily due to a 2% increase in the number of Commonwealth supported students.

Fees and charges

The following chart shows fees from overseas students together with international student numbers.



Source: Student numbers, which are based on equivalent full-time student load (EFTSL), were obtained from Flinders' published statistics and are unaudited figures.

Fees from overseas students increased by $8 million (12%) to $76 million primarily due to a 6% growth in international student numbers together with price increases per course of between 2.5% and 9%.

The following table shows that total student loads increased by 5% over the last four years, with a 1% increase in domestic students and a 24% increase in overseas students.

	2014 Number	2015 Number	2016 Number	2017 Number
Domestic students	13 849	13 802	14 071	14 050
Overseas students	2 614	2 952	3 070	3 239
Total students (EFTSL)	16 463	16 754	17 141	17 289

Source: Student load data sourced from Flinders Statistical Summary and is unaudited.

Investment revenue and income

Investment revenue and income (net of losses) increased by $2 million to $11 million due to gains in the value of investments.

Expenses

Total expenses increased by $9 million (2%). This was primarily due to a $9 million (9%) increase in other expenses related to additional spending on software, non-capitalised equipment and student related expenditure.

Employee related expenses

Employee related expenses totalled $310 million in 2017. Employee expenses decreased by $4 million (1%) in 2017 mainly due to the completion of the voluntary early retirement scheme (VERS) for

academics in 2016 of $6 million, offset by a $2 million increase in payments due to enterprise agreements.

	2014 $'million	2015 $'million	2016 $'million	2017 $'million
Employee related expenses	290	298	314	310

The following table shows total staff numbers for Flinders based on FTEs. The numbers have remained relatively constant over the last four years, with a fall in 2016 due to the VERS. The table also shows the percentage of academic staff over the last four years.

	2014 FTEs	2015 FTEs	2016 FTEs	2017 FTEs
Academic	873	874	844	827
Non-academic	1 198	1 207	1 114	1 091
Total FTEs	2 071	2 081	1 958	1 918
Percentage of academic staff	42%	42%	43%	43%

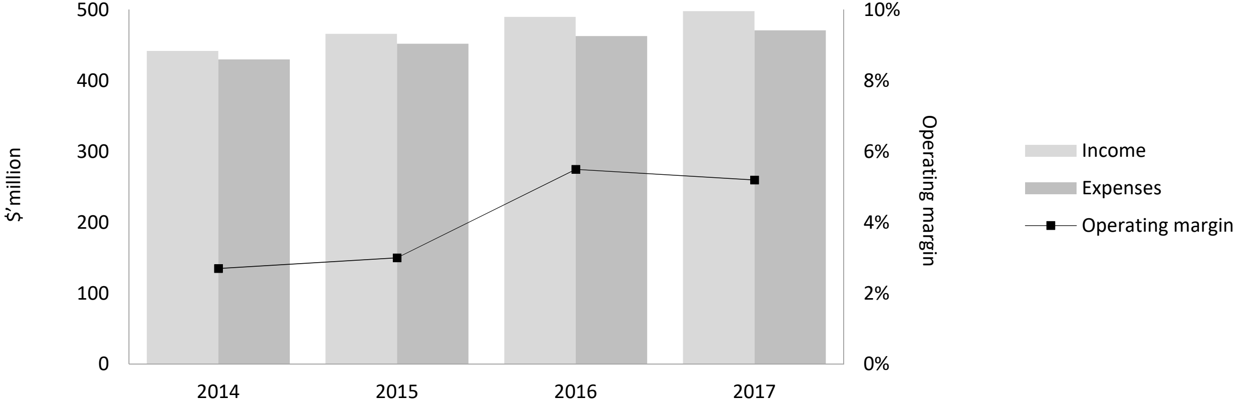
Source: Staff numbers, which are based on FTEs, were obtained from Flinders' published statistics and are unaudited figures.

Operating result

The operating surplus was $26 million, marginally lower than 2016. Contributing to the surplus were:

- a $9 million increase in fees and charges as a result of an increase in course fees and charges, mainly in fees from overseas students
- a $6 million increase in consultancy and contract income, mainly as a result of an increase in contract research income
- a $4 million decrease in employee related expenses, mainly due to the expense relating to the VERS in 2016.

The following chart shows the operating income, operating expenses and operating margin for the four years to 2017.



Flinders' operating margin (the operating result for the year divided by total income) decreased slightly in 2017, reflecting a consistent operating result with an increase in expenditure.

Statement of Financial Position

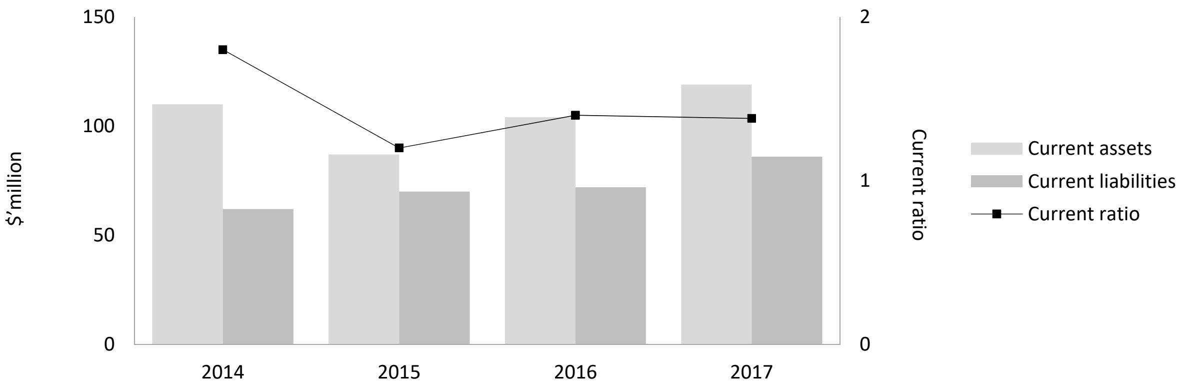
Flinders' consolidated net assets as at 31 December 2017 totalled $731 million ($698 million), an increase of $33 million.

Assets

Current assets

Flinders' cash and current financial assets (term deposits) increased by $22 million to $98 million, primarily due to the reduced spending on infrastructure following the completion of major projects and increased overseas student numbers and fees.

The following chart shows Flinders' current assets and liabilities. The current ratio remains positive, with Flinders' current assets exceeding current liabilities by $33 million, which is consistent with 2016. The chart shows a decline in its current ratio reflecting significant self-funded investments in infrastructure projects in 2014 and 2015.



Property, plant and equipment

The main item of Flinders' Statement of Financial Position is property, plant and equipment, representing 68% of total assets. The carrying value of property, plant and equipment decreased by $2 million to $600 million mainly due to:

- asset additions of $29 million
- offset by $31 million in depreciation charges.

Liabilities

Flinders' liabilities increased by $9 million to $158 million. The major items contributing to this were a $10 million increase in trade payables and a $5 million increase in other liabilities, offset by a $4 million decrease in employee provisions.

Statement of Cash Flows

Cash flows from operating activities increased by $14 million to $77 million. Cash outflows for property, plant and equipment decreased by $6 million due to the completion of major projects, offset by an increase of $40 million in payments for financial assets. Total cash and cash equivalents decreased by $13 million to $43 million.

University of Adelaide (Uni Adelaide)

Financial statistics	Net operating result:	$56 million
	Australian Government financial assistance:	$494 million
	Number of FTEs:	3 873
	Number of students (EFTSLs):	21 141

Significant events and transactions

— The Adelaide Health and Medical Sciences building opened for use in 2017. The building, the largest capital project in Uni Adelaide's history, is included in Uni Adelaide's financial statements at 31 December 2017 as a $228 million building, with a further $15 million recognised for Adelaide Health and Medical Sciences specific plant and equipment.

— In June 2018 Uni Adelaide and the University of South Australia announced a six-month process to explore the merits of a potential merger.

Financial report opinion

Unmodified

Financial controls opinion

Modified

Key issues:

— Ineffective review of payroll bona fide reports

— Ineffective controls to monitor leave recorded

Functional responsibility

Uni Adelaide is established by the *University of Adelaide Act 1971*.

Uni Adelaide has the objective of advancing learning and knowledge, which it achieves by providing university education and conducting research activities.

Scope of audit

The audit program covered major financial systems to obtain sufficient evidence to form an opinion on the financial report and internal controls.

Specific areas of audit attention in 2017 included:

- corporate governance
- ICT
- Commonwealth financial assistance
- research grants, student fees and other revenue
- cash, investments and borrowings
- property, plant and equipment
- payroll
- accounts payable
- general ledger and financial accounting.

Internal audit activities and reports were reviewed to assess the risks of material misstatement in the financial report and to design and perform audit procedures.

The audits of Uni Adelaide's controlled entities for the year ending 31 December 2017 were carried out by private accounting firms.

Audit findings and comments

Assessment of controls

In my opinion, the controls exercised by the University of Adelaide in relation to the receipt, expenditure and investment of money, the acquisition and disposal of property and the incurring of liabilities, except for all matters outlined under 'Communication of audit matters', are sufficient to provide reasonable assurance that the financial transactions of the University of Adelaide have been conducted properly and in accordance with law.

Communication of audit matters

Matters identified by the audit were detailed in a management letter to the Vice-Chancellor and President. Uni Adelaide's responses to the letter indicated that appropriate action would be taken to address the matters raised. The main matters raised and the related responses are detailed below.

Payroll

Ineffective review of payroll bona fide reports

Uni Adelaide made payments for salaries and related expenses of more than $500 million in 2017.

Uni Adelaide relies on the review of bona fide reports by faculties and divisions to ensure that accurate payroll related information is recorded for its staff in the payroll system. If this control is not effective there is a risk that errors in payroll information may not be detected and corrected.

Our audit identified that:

- the reviews performed by officers over bona fide reports varied significantly between cost centres. The reviews would not identify invalid employees or incorrect pay grades or steps but may identify ad hoc variations in these areas for further follow up
- there were delays in returning quarterly bona fide reports to Human Resources. In quarters one and three, more than half of the reports were returned later than the due date, with quarter two recording only 7% being returned late.

Uni Adelaide responded that it would remind key leaders and bona fide recipients of their obligations under its procedures.

Ineffective controls to monitor leave recorded

Uni Adelaide had employee leave provisions of more than $86 million at 31 December 2017.

Consistent with 2016, we found that Uni Adelaide's control to ensure all leave taken is deducted from employee leave entitlement balances in the payroll system was ineffective. We found that leave taken data recorded on bona fide reports was not being used to confirm that all leave taken was recorded.

Uni Adelaide did not identify another control to mitigate the risk that leave being recorded was incomplete and inaccurate. As a result, a risk exists that leave taken is not recorded in the payroll system, resulting in the potential overstatement of leave liabilities.

Uni Adelaide responded that it would develop policies and procedures to support the implementation of the new leave management arrangements when the new enterprise agreement comes into effect.

Interpretation and analysis of the financial report

Highlights of the financial report

	2017 $'million	2016 $'million
Revenue		
Australian Government grants	377	387
HECS-HELP, FEE-HELP and SA-HELP (Australian Government payments)	118	119
HECS-HELP (student payments)	10	13
Fees and charges (course and non-course)	247	227
Other	195	201
Total revenue	947	947

	2017 $'million	2016 $'million
Expenses		
Salaries and related expenses	509	498
Other expenses	382	388
Total expenses	891	886
Operating result from continuing operations	56	61
Other comprehensive income	-	52
Total comprehensive income	56	113
Net cash provided by (used in) operating activities	77	84
Net cash provided by (used in) investing activities	(94)	(107)
Net cash provided by (used in) financing activities	10	11
Assets		
Current assets	98	106
Non-current assets	1 877	1 819
Total assets	1 975	1 925
Liabilities		
Current liabilities	119	141
Non-current liabilities	231	215
Total liabilities	350	356
Total equity	1 625	1 569

Statement of Comprehensive Income

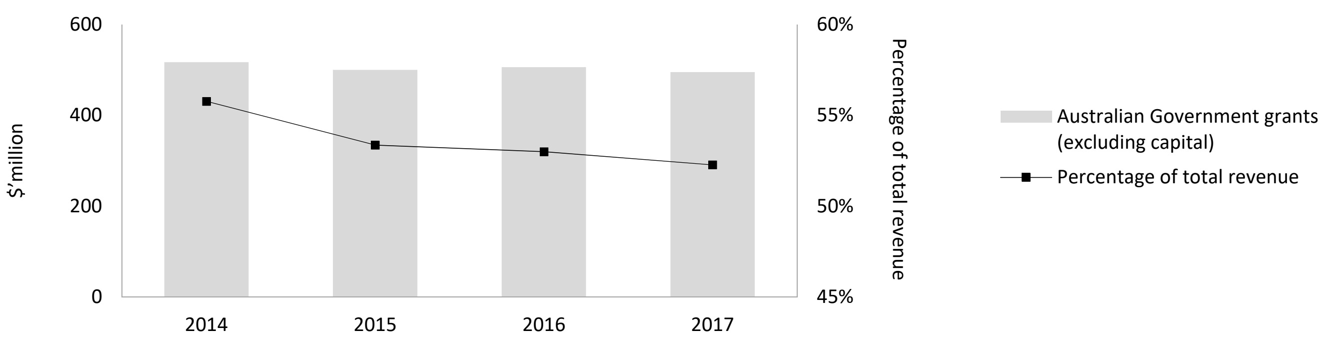
Revenue

Revenue in 2017 totalled $947 million which was consistent with 2016. Rises in fees and charges (course and non-course) were offset against lower Australian Government grants and lower HECS-HELP (student payments).

Australian Government grants and payments

Total Australian Government financial assistance received by the University in 2017 decreased by $11 million to $495 million.

The following chart shows Australian Government grants and payments, excluding capital funding as this is not necessarily comparable from year to year. It shows that there was a slight fall in the proportion of non-capital Australian Government grants and payments to total income in 2017, to 52%, from the steady level of 53% in 2015 and 2016. The higher proportion in 2014 primarily relates to the reduced contribution of investment income in that year.



In 2017 Australian Government grants and payments include the following major items:

- $166 million in Commonwealth Grants Scheme funding for Commonwealth supported student places. Commonwealth Grants Scheme funding decreased by $9 million (5%) in 2017, reflecting the impact of additional funding received in 2016 for efficiency dividend payments, which had previously been withheld by the Commonwealth, and a 462 EFTSL decrease in Commonwealth supported places in 2017
- $118 million in Higher Education Loan Program (HELP) funding which included funding for HECS-HELP. In 2017 HECS-HELP funding remained steady at $104 million.

Fees and charges

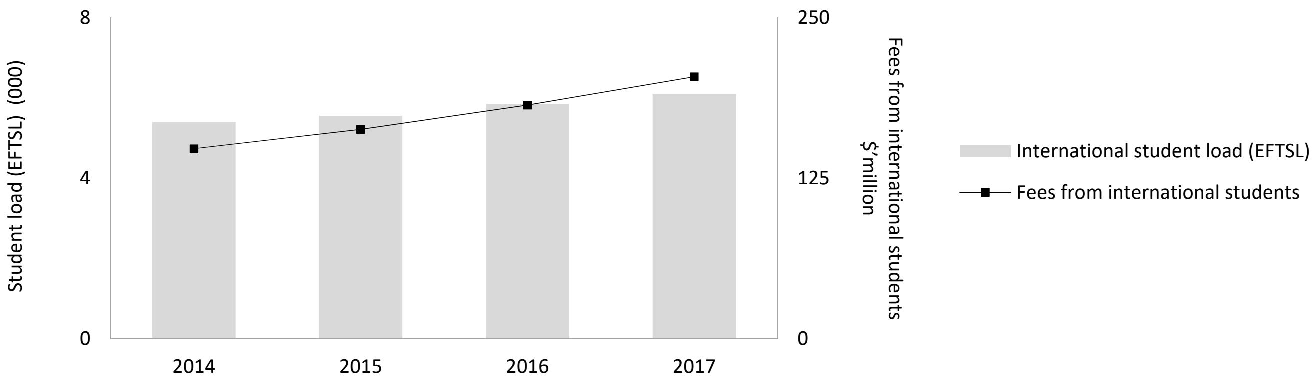
Fees and charges (course and non-course) increased by $20 million to $247 million in 2017. This increase is attributable to a $22 million rise in revenue from international fee paying students, which was mainly offset by lower rental and accommodation fees.

The following table shows that total student loads steadily increased between 2014 and 2016, before a slight fall in 2017.

	2014 Number	2015 Number	2016 Number	2017 Number
Domestic students	15 707	15 688	15 618	15 050
International students	5 397	5 550	5 843	6 091
Total students (EFTSL)	21 104	21 238	21 461	21 141

Source: Student numbers, which are based on equivalent full-time student load (EFTSL), were obtained from Uni Adelaide's annual report and are unaudited.

The following chart highlights the upward trend in revenue received from international fee paying students.



Source: Student numbers, which are based on EFTSL, were obtained from Uni Adelaide's annual report and are unaudited.

Fees from international students increased by $22 million (11%) to $204 million in 2017, due primarily to a 4.3% increase in total international fee paying student numbers and an average 6.1% price increase in fees equating to a $9 million increase in revenue.

Other revenue

Other revenue decreased by $6 million (3%) to $195 million. The major items causing this change were:

- a decrease of $17 million in the contract research revenue earned by the Adelaide Research and Innovation Investment Trust. In 2017 the wind-down of the Trust continued, with many of its contract research agreements either being novated to Uni Adelaide or not renewed as at 31 December 2017, resulting in a decline in consolidated contract research income
- offset by a $14.6 million increase in investment income, mostly reflecting $10 million in unrealised gains on the value of endowment fund investments.

Expenses

Expenses in 2017 totalled $891 million, an increase of $5 million compared to 2016. The increase reflects an $11 million (2%) rise in employee related expenses, offset by a $6 million (2%) decrease in combined other expenses.

Employee related expenses

The $11 million increase in salaries and related expenses reflects the effect of enterprise bargaining wage percentage increases of 3%.

The following table shows total staff numbers, based on FTEs. The numbers have remained relatively steady over the last four years.

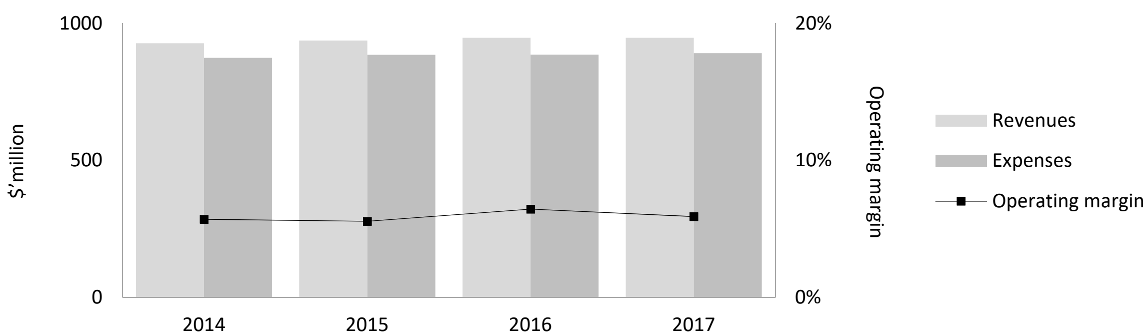
	2014 FTEs	2015 FTEs	2016 FTEs	2017 FTEs
Academic	1 785	1 781	1 729	1 732
Non-academic	2 091	2 084	2 155	2 141
Total FTEs	3 876	3 865	3 884	3 873
Percentage of academic staff	46%	46%	45%	45%

Source: Staff numbers, which are based on FTEs, were obtained from Uni Adelaide's annual report and are unaudited.

Operating result

The consolidated operating result for 2017 was a surplus of $56 million compared to $61 million in 2016.

The following chart shows the operating revenues, operating expenses and operating margin (the operating result for the year divided by total income) for the four years to 2017.



Uni Adelaide's operating margin has been stable over the past four years. This is because there were none of the large one-off transactions, mostly associated with capital funding receipts for significant projects, that occurred in earlier years.

Statement of Financial Position

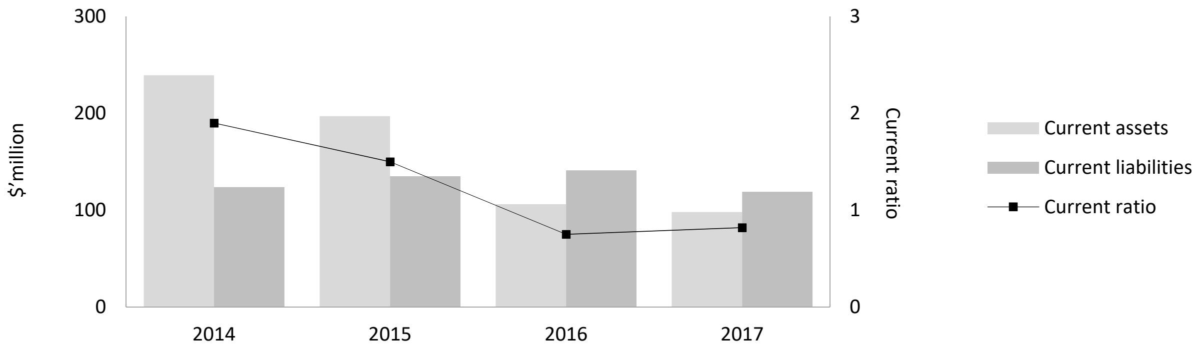
Uni Adelaide's consolidated net assets at 31 December 2017 were $1625 million ($1569 million), an increase of $56 million.

Assets

The value of Uni Adelaide's assets increased by $50 million (3%) in 2017. The major items driving this change were:

- an increase of $12 million in property, plant and equipment mainly resulting from additions of $69 million, mostly related to buildings, offset by $47 million in depreciation and amortisation charges and $5 million in disposals
- an increase of $35 million in other financial assets mainly attributable to endowment fund investment gains of $27 million.

As at 31 December 2017, current assets of $98 million were less than current liabilities of $119 million. The following chart shows Uni Adelaide's current assets, current liabilities and current ratio for the four years to 2017.



Uni Adelaide's current ratio increased slightly in 2017. This is primarily attributable to a $24 million reduction in current payables reducing total current liabilities by a greater amount than the decrease in total current assets.

Major capital works projects

In May 2014, Uni Adelaide's Council approved the construction of a new Adelaide Health and Medical Sciences (AHMS) building in the South Australian Health and Biomedical Precinct located in Adelaide's West End.

The AHMS building has 12 floors and had a total budgeted cost of $246 million. Construction commenced in August 2014 with completion achieved in 2017.

Final capital expenditure on the building was $243 million (including $15 million for AHMS specific plant and equipment). The building project was funded in part by a $60 million capital grant received from the Australian Government in June 2013. The balance was funded by Uni Adelaide through a reduction in assets, including the disposal of non-current assets held for sale, and an increase in borrowings.

Liabilities

The value of Uni Adelaide's liabilities decreased by $6 million (2%). The major items causing this change were:

- a reduction in payables of $25 million compared to 2016, with significant payments associated with the AHMS building paid by balance date in 2017
- a drawdown in borrowings of $15 million to fund a range of innovation and strategic initiatives, including additional scholarships and fellowships
- an increase in employee benefit liabilities of $2 million (1%).

Statement of Cash Flows

Total cash and cash equivalents at 31 December 2017 were $36 million ($42 million).

Net cash flows from operating activities decreased by $7 million, due mainly to reductions in Australian Government financial assistance of $11 million and a reduction in consultancy and contract research of $19 million, offset by fee paying student revenue increases of $25 million.

Cash outflows for investing activities declined by $62 million mainly due to reductions in payments associated with the construction of the AHMS building.

University of South Australia (UniSA)

Financial statistics	Operating result before income tax:	$13 million
	Australian Government financial assistance:	$396 million
	Number of FTEs:	2 595
	Number of students (EFTSLs):	22 142

Significant events and transactions

- Construction of the Health Innovation Building (now named the UniSA Cancer Research Institute) continued with $220 million spent in total at 31 December 2017.
- Construction of Pridham Hall also continued with $45 million spent in total at 31 December 2017.
- Additional building refurbishments and fitouts, with $22 million spent in total, were completed by 31 December 2017.
- In June 2018 the University of Adelaide and UniSA announced a six-month process to explore the merits of a potential merger.

Financial report opinion

Modified

UniSA recognised $30.5 million of unspent funding as a liability for the year ended 31 December 2017. These funds represent contributions and meet the recognition criteria of income under Australian Accounting Standard AASB 1004 'Contributions' and Accounting Policy Framework V 'Income Framework'. UniSA controls these funds upon receipt and it is highly unlikely that they will be repaid.

Financial controls opinion

Modified

Key issues:

- Improvements required to contract management processes
- No independent review over changes made to the Vice-Chancellor's authorisations master list
- Management of excessive annual leave balances could be improved
- No review of casual employee payments for pre-filled timesheets

Functional responsibility

UniSA is established under the *University of South Australia Act 1990*.

The main functions of UniSA are to provide tertiary education programs, preserve, extend and disseminate knowledge through teaching, research, scholarship and consultancy and to provide educational programs for the benefit of the wider community or the enhancement of its cultural life.

Scope of the audit

The audit program covered major financial systems to obtain sufficient evidence to form an opinion on the financial report and internal controls.

Specific areas of audit attention in 2017 included:

- corporate governance
- Commonwealth financial assistance
- consultancy and research income
- student fees and other revenue
- receipting and banking
- cash, investments and borrowings
- payroll
- expenditure
- general ledger and financial accounting
- property, plant and equipment
- major capital works.

Internal audit activities were reviewed to assess the risk of material misstatement in the financial report and to inform the design of audit procedures.

The audits of UniSA's controlled entities for the year ended 31 December 2017 were carried out by a private accounting firm.

Audit findings and comments

Auditor's report on the financial report

The following is an extract from the 2017 Independent Auditor's Report that outlines the qualification of UniSA's financial report.

> ***Qualified opinion***
>
> *In my opinion, except for the effects of the matter described in the Basis for qualified opinion section of my report, the financial report has been prepared in accordance with the Treasurer's Instructions promulgated under the provisions of the* Public Finance and Audit Act 1987*, Division 60 of the* Australian Charities and Not-for-profits Commission Act 2012*, the* Higher Education Support Act 2003 *and Australian Accounting Standards …*

Basis for qualified opinion

The University and its controlled entities has recognised $30.5 million of unspent funding as a liability for the year ended 31 December 2017. These amounts have been accounted for as income received in advance and included in 'Other Liabilities - Commonwealth and State Government Grants', 'Other Liabilities - Income in advance on incomplete projects' and 'Other Liabilities - Other' in note 21 to the financial report. The University has disclosed its accounting treatment of these funds in note 21 to the financial report.

The funds represent contributions and meet the recognition criteria of income in accordance with Accounting Standard AASB 1004 Contributions and Accounting Policy Framework V Income Framework. The University controls these funds upon receipt and it is highly probable that any unspent funds will be spent in accordance with stipulated conditions. It is highly unlikely that unspent funds will need to be repaid to the granting bodies and as such funds should be recognised as income at the time of receipt.

As a result, the following has been misstated in the 2017 financial report:

- *Revenue recognised as Australian Government grants is understated by $1.3 million ($3.7 million overstated in 2016)*
- *Revenue recognised as State and Local Government financial assistance is understated by $2.6 million ($2.6 million understated in 2016)*
- *Revenue recognised as Consultancy and contract research is understated by $1.6 million ($202 000 understated in 2016)*
- *Operating result attributable to members of University of South Australia is understated by $5.6 million ($893 000 overstated in 2016)*
- *Other liabilities is overstated by $30.5 million ($25 million overstated in 2016)*
- *Closing retained earnings is understated by $30.5 million ($25 million understated in 2016).*

Assessment of controls

In my opinion, the controls exercised by the University of South Australia in relation to the receipt, expenditure and investment of money, the acquisition and disposal of property and the incurring of liabilities, except for all matters outlined under 'Communication of audit matters', are sufficient to provide reasonable assurance that the financial transactions of the University of South Australia have been conducted properly and in accordance with law.

Communication of audit matters

Matters identified by the audit were detailed in a management letter to the Vice-Chancellor and President and those charged with governance. The main matters raised and the related responses are detailed below.

Grant funding

Consistent with prior years UniSA has recognised a liability for unspent grant funding as at 31 December 2017. As mentioned in the 'Auditor's report on the financial report' under the 'Basis for qualified opinion', under AASB 1004 'Contributions' these grants should be recognised as revenue in the year of receipt.

Contract management

Improvements required to contract management processes

We previously identified gaps in UniSA's approach to contract management and the lack of central procedures governing its contract management system.

In 2017 we found that implementation of UniSA's established framework and guidelines for contract management was still a work in progress and:

- there were still no procedures for monitoring, reporting and updating contract registers
- there was still no process to ensure all contracts meeting the established thresholds were recorded
- key performance indicators detailed in the framework were still not monitored or reported in the system
- duplicate registers were still in use as the main system was unable to track milestones or monitor contracted spend.

UniSA responded that it would investigate the contract management system's capabilities, noting the recent upgrade of the finance system. A solution would be implemented once the functionality could be confirmed.

Expenditure

No independent review over changes to the Vice-Chancellor's authorisations master list

We previously identified a risk of incorrect changes being made to the Vice-Chancellor's authorisations master list. This information is the basis of system delegations used to approve invoices. We noted there remained no independent review of changes in 2017. While the monthly reconciliation and annual review processes that are in place may identify these errors, there was still an opportunity for errors to exist in the system.

UniSA's response indicated that work was progressing to develop the Vice-Chancellor Authorisations Management System for implementation across UniSA.

Payroll

Management of excessive annual leave balances could be improved

For a number of years, we have noted a high number of staff with excessive annual leave balances. This was still the case in 2017 with over $4.7 million in excessive annual leave, despite the processes implemented by UniSA to reduce leave balances. Our analysis found that while the number of employees with excessive leave balances decreased from 252 in 2016 to 206 in September 2017, there remains the risk that not all leave taken is being recorded. We also noted a potential increased risk of workers compensation claims where individual staff have not taken recreation leave and had a sufficient break from their workplace.

UniSA's response indicated that it was committed to reducing excessive leave liabilities and:

- would discuss a report reviewing the effectiveness of current policy and procedures and make recommendations to more pro-actively address excess leave balances through its Senior Staff Collective Agreement and Enterprise Agreement
- would continue to meet regularly with senior managers to encourage the completion of leave plans and active management of excess balances
- had implemented a summary report for senior managers to track the total leave liability accrued across their business units.

No review of casual employee payments for pre-filled timesheets

UniSA pays more than $25 million a year for casual staff. A proportion of these staff have pre-filled timesheets. We previously identified that timesheets for casual employees, which are pre-filled with information about work hours already recorded in the Casual Administration System, were not reviewed prior to payment. In 2017 UniSA reviewed the new Casual Administration System to identify whether changes to processes were needed, including any need to reinstate the use of the 'acknowledgement of casual payments' report.

As the review was still in progress, we found that no changes had been made to the existing process, meaning pre-filled timesheets for casual employees were still not reviewed prior to payment. As a result there remained a risk of unauthorised rates and payments for casual staff.

UniSA responded that the review was completed after the audit and it would work through the recommendations and establish an implementation plan for the agreed actions. The recommendations included up-front approvals and exception reporting on variances to provide assurance for the pre-filled timesheets.

Interpretation and analysis of the financial report

Highlights of the financial report

	2017 $'million	2016 $'million
Income		
Australian Government grants	261	265
HECS-HELP, FEE-HELP and SA-HELP (Australian Government payments)	135	130
HECS-HELP (student payments)	10	11
Fees and charges	133	133
Other	72	70
Total income	611	609
Expenses		
Employee related expenses	377	357
Other expenses	221	212
Total expenses	598	569
Operating result before income tax	13	40
Net cash provided by (used in) operating activities	64	75
Net cash provided by (used in) investing activities	(194)	(100)

	2017 $'million	2016 $'million
Assets		
Current assets	266	400
Non-current assets	1 520	1 370
Total assets	1 786	1 770
Liabilities		
Current liabilities	198	182
Non-current liabilities	399	414
Total liabilities	597	596
Total equity	1 189	1 174

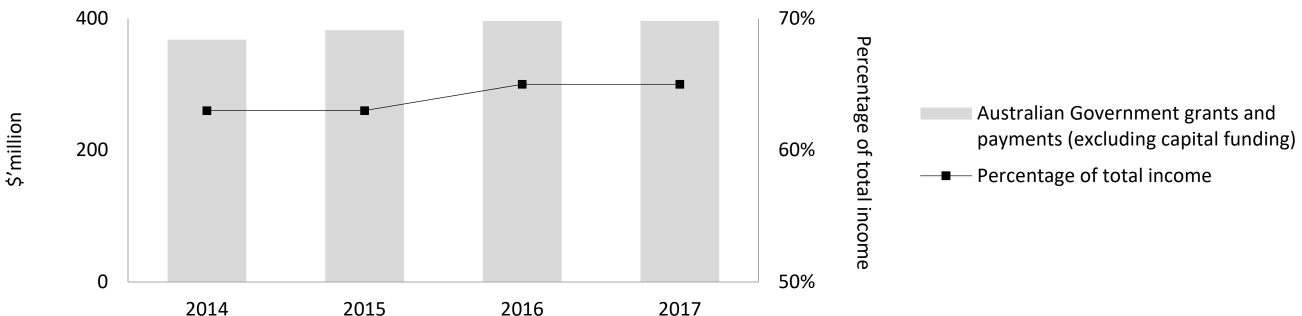
Statement of Comprehensive Income

Income

UniSA's total income increased marginally in 2017.

Australian Government grants and payments

Total Australian Government financial assistance provided to UniSA (excluding capital funding as this is not necessarily comparable from year to year) is shown in the chart below. This highlights that UniSA's reliance on Australian Government financial assistance, excluding capital funding, has remained relatively consistent over the four years. This year's overall funding is consistent with that received in 2016.



Australian Government grants decreased by $4 million in 2017 to $261 million, as a result of:

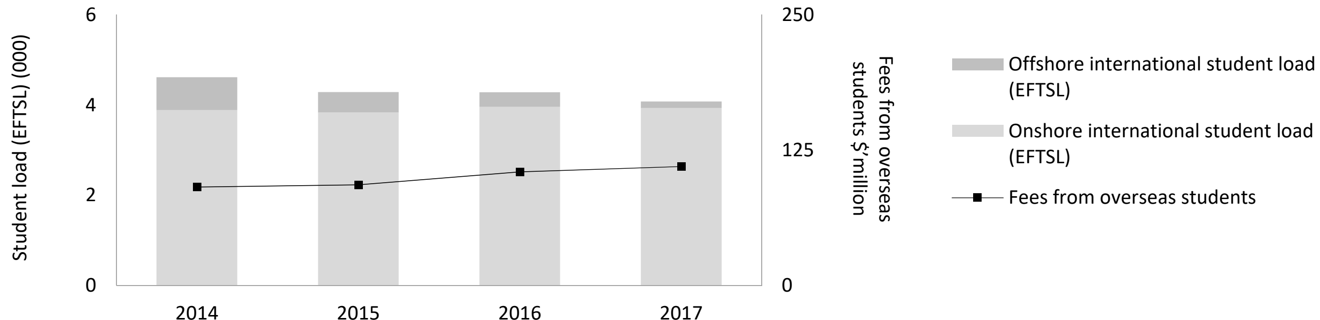
- a decrease in Commonwealth Grants Scheme and other grants of $5 million, reflecting the one-off nature of an efficiency dividend payment received in 2016. While there was a decrease in this funding overall, it was indexed by 1.5% in 2017 and included an increase in Commonwealth supported students
- HECS-HELP, FEE-HELP and SA-HELP income increasing by $4 million (3%) to $135 million in 2017. This was mainly the result of indexation of 1.5% and increased domestic student load (EFTSL) in 2017.

Fees and charges

Fees and charges remained constant at $133 million in 2017, despite an increase of $5 million for fee-paying overseas students in 2017 as a result of fee increases. The increase was offset by a decrease of $5 million in non-course fees and charges.

The main component of fees and charges is fee-paying overseas students (83%), which represents 18% of total revenue.

The following chart shows that the fee-paying overseas student load decreased by 5% in 2017. Fee revenue from international students increased by $5 million in 2017 from price increases to these fees and indexation for overseas student fees.



Source: Student numbers, which are based on equivalent full-time student load (EFTSL), were obtained from UniSA's annual reports and are unaudited figures.

The table below illustrates a marginal decrease in student load in 2017.

	2014 Number	2015 Number	2016 Number	2017 Number
Domestic students	17 877	17 976	17 984	18 061
Overseas students	4 618	4 288	4 284	4 081
Total students (EFTSL)	22 495	22 264	22 268	22 142

Source: Student numbers, which are based on EFTSL, were obtained from UniSA's annual reports and are unaudited figures.

Other revenue

Other revenue increased by $2 million to $72 million in 2017 largely from:

- an increase in State and Local Government financial assistance of $2 million, mainly as a result of a $1.5 million grant from the SA Government for new projects
- an increase in consultancy and contract research revenue of $3 million as a result of receiving $1.6 million for international collaboration research and $1.1 million for new Co-operative Research Centre projects
- a decrease in investment revenue of $3 million due to a reduction in dividends, distributions and interest revenue.

Expenses

Total expenses increased by $29 million (5%) to $598 million in 2017.

The split between employee expenses (63%) and other expenses (37%) remained stable in 2017.

Employee expenses

UniSA's main expense is employee related expenses which increased by $20 million (6%) to $377 million in 2017. The increase was mainly a result of enterprise agreement increases of $11 million and an increase in payments to casual employees of $7 million.

The following table shows a breakdown of staff FTE numbers between academic and non-academic staff, along with the percentage of total staff classified as academic since 2014. There was an increase in overall staff numbers in 2017.

	2014 FTEs	2015 FTEs	2016 FTEs	2017 FTEs
Academic	1 127	1 126	1 061	1 122
Non-academic	1 515	1 470	1 431	1 473
Total FTEs	2 642	2 596	2 492	2 595
Percentage of academic staff	43%	43%	43%	43%

Source: Staff numbers, which are based on FTEs, were obtained from UniSA's annual report and are unaudited figures.

Other expenses

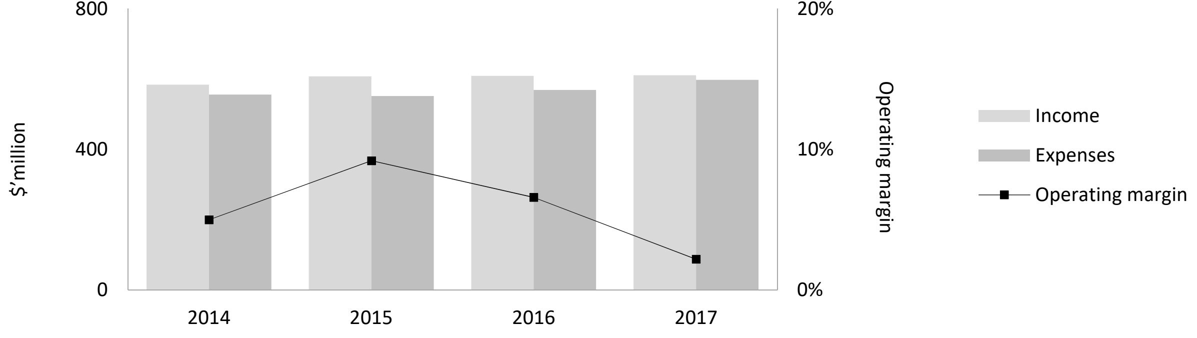
Other expenses increased by $9 million to $221 million in 2017. The main components of this change were:

- an increase of $1.9 million in advertising, marketing and promotion expenses
- an increase of $2.3 million in IT hardware and software expenses
- an increase of $1.4 million in utilities expenses
- an increase of $1.4 million in travel, staff development and entertainment expenses
- an overall increase of $2 million in other expenses mainly from library subscriptions, printing costs, loss on investments and net foreign exchange losses.

Operating result

The consolidated operating result before income tax for the year was a surplus of $13 million ($40 million). As mentioned in the analysis above, the decrease is mainly due to marginal increases in revenue offset by an increase in total expenditure of $29 million.

The following chart shows the movement in income, expenses and the operating margin for the last four years. The high operating margin in 2015 is a result of one-off receipts in that year. The decline in the operating margin this year reflects the decreased operating result as a result of the increase in expenses for 2017.

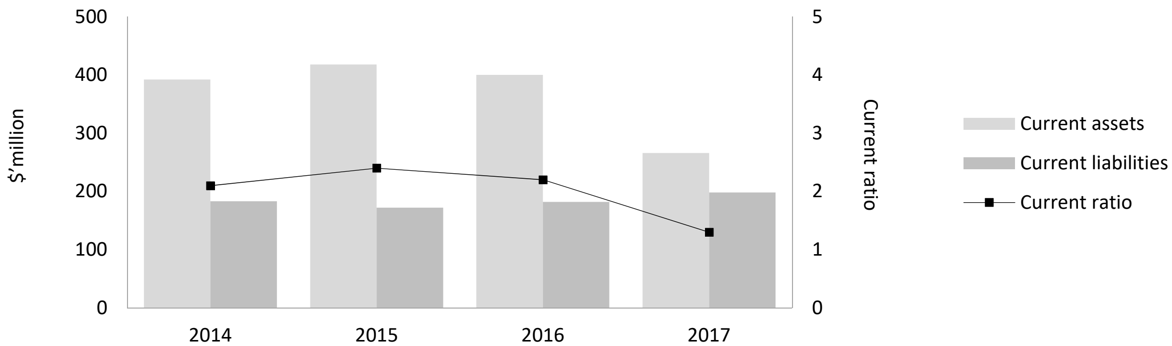


UniSA's operating margin (the operating result as a percentage of total income) decreased to 2.2% in 2017 as a result of the $29 million increase in expenses.

Statement of Financial Position

UniSA's net assets at 31 December 2017 were $1189 million ($1174 million).

The following chart shows that UniSA's current ratio has reduced since 2015 as a result of reduced cash holdings, reflecting spending on property, plant and equipment. As at 31 December 2017, current assets exceeded current liabilities by $68 million.



Assets

Cash and cash equivalents

As at 31 December 2017 UniSA's cash and cash equivalents totalled $188 million compared to $318 million in 2016. The reduction in cash holdings is largely attributable to investments in the construction of major new buildings in 2017. These buildings will be completed in 2018.

Property, plant and equipment

The main component of UniSA's Statement of Financial Position is property, plant and equipment, representing 61% of total assets. The carrying value of property, plant and equipment increased by $157 million to $1087 million due mainly to:

- asset additions of $194 million, predominantly for construction in progress for major buildings
- revaluation decreases of $4 million, mainly for buildings
- offset by depreciation charges of $33 million.

Capital program

UniSA has a significant ongoing capital investment program. The major active capital projects in 2017 were the continued construction of:

- the UniSA Cancer Research Institute, with $220 million of the total budget of $254 million spent as at 31 December 2017
- Pridham Hall, with $45 million of the total budget of $50 million spent as at 31 December 2017.

Liabilities

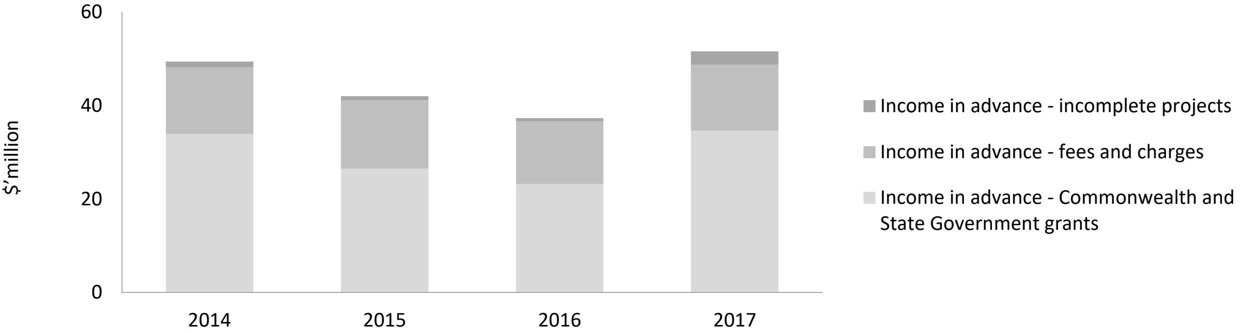
UniSA's liabilities increased by $1 million to $597 million in 2017. The significant components contributing to total liabilities were:

- defined benefit superannuation obligations, which decreased by $15 million to $416 million as a result of increased investment returns and a decrease in the discount rate of 0.3%
- provisions for employee liabilities, which remained unchanged at $72 million in 2017. The provisions are predominantly for annual and long service leave liabilities (97%)
- trade and other payables of $54 million in 2017, which was a $3 million (6%) increase from last year
- other liabilities, which increased by $13 million to $56 million in 2017, predominantly for income received in advance which is explained below.

Income in advance

The chart below shows the breakdown of income received in advance recorded in other liabilities. These liabilities represent the deferral of the income into future reporting periods based on UniSA's income recognition policies (refer to the qualification of other liabilities for the revenue deferral as outlined in the 'Auditor's report on the financial report' and note 21 of UniSA's financial report).

In 2017, income in advance increased by $14 million to $52 million, reversing the former trend of decreases in these amounts, with the main increase in Commonwealth and State Government income due to more research grants received and deferred by UniSA.



Statement of Cash Flows

The net cash flows provided by operating activities decreased by $11 million due mainly to increases in payments to suppliers and employees, partly offset by increases in Australian Government grants received and receipts from student fees and other customers.

Net cash used in investing activities increased by $94 million as a result of increased payments for major capital works projects for the UniSA Cancer Research Institute and Pridham Hall.

Further commentary on operations

Pridham Hall was officially launched on 7 May 2018. The building was designed to deliver a comprehensive sporting hub to UniSA's City West campus and provide an on-campus venue for graduations.

The UniSA Cancer Research Institute officially opened on 10 May 2018. It is home to UniSA's School of Pharmacy and Medical Sciences, the Centre for Cancer Biology (an alliance between UniSA and SA Health), UniSA's technology-based business incubation hub (in collaboration with DXC Technology and the State Government), the Innovation Collaboration Centre, and a new future-focused public museum, the MOD.

In July 2018, it was announced that UniSA's Chancellor, Jim McDowell, had been appointed as the Chief Executive Officer of the Department of the Premier and Cabinet. On 17 August 2018, UniSA announced Pauline Carr as its new Chancellor. She will commence in her new role from September 2018.

Urban Renewal Authority (URA)

Financial statistics	Sales:	$87 million
	Cost of sales:	$49 million
	Rental income:	$70 million
	Profit before income tax equivalent:	$29 million
	Inventories and investment properties:	$1.03 billion
	Borrowings:	$894 million
	Number of FTEs:	293
	Hectares of land inventory:	3691

Significant events and transactions

- In March 2018, the former Royal Adelaide Hospital site (now known as Lot Fourteen) was transferred from the Department for Health and Wellbeing to the URA for $0 consideration.
- Demolition of some buildings at Lot Fourteen has commenced together with refitting of heritage buildings.
- On 1 July 2018, as part of machinery of government changes, 166 URA employees were transferred to the employment of the Chief Executive, South Australian Housing Trust.
- The 2018-19 State Budget announced the planned closure of several TAFE SA campuses, three of which are owned by the URA. The URA is working with the SA Government to determine the impact of these closures on the URA.

Financial report opinion — **Unmodified**

Financial controls opinion — **Unmodified**

Functional responsibility

The URA is established by the *Urban Renewal Act 1995* (URA Act).

The URA is responsible for leading and coordinating urban renewal activity to ensure future housing needs are met through better planned, affordable and vibrant mixed use (residential and commercial) urban developments located near transport, employment, education and other services.

The URA's functions contained in the URA Act include:

- the development of residential, commercial and industrial land in the public interest, particularly for urban renewal purposes
- facilitation of public and private investment, undertaking development activities which are attractive to potential investors and participating in the development of the State
- managing the orderly development of areas through the management and release of land
- holding land and other property to be made available as appropriate for commercial, industrial, residential or other purposes.

The URA's trading name is Renewal SA. It is a for-profit entity under Accounting Policy Framework II 'General Purpose Financial Statements Framework'.

Urban renewal program

The URA conducts its urban renewal program through a series of development projects. Its major development projects are currently Lot Fourteen, Playford Alive, Tonsley Park, Woodville West and Bowden. A separate business plan is prepared for each major development project and progress against the plan monitored. Refer to 'Major development projects' below for further commentary on these projects.

Scope of the audit

The audit program covered major financial systems to obtain sufficient evidence to form an opinion on the financial report and internal controls.

Specific areas of audit attention in 2017-18 included:

- corporate governance
- project, procurement and contract management
- land sales
- property income
- expenditure
- payroll
- inventory.

Internal audit activities were reviewed to assess the risks of material misstatement in the financial report and to design and perform audit procedures.

Audit findings and comments

Communication of audit matters

No significant matters were identified by the audit.

We noted that the URA had addressed our past recommendations with:

- the Minister and the Treasurer approving the URA's ownership framework in 2018. The URA operated for six years without an approved ownership framework

- the URA Board using a single consolidated business plan from 2018-19 to direct and monitor its progress. Last year, we reported that the URA Board received individual plans on specific activities but not a consolidated business plan.

Shared Services SA – financial systems and transaction processing environments

Shared Services SA processes payroll transactions on behalf of the URA under service level determinations. Our review and evaluation of the payroll system controls concluded they were effective for 2018.

Shared Services SA is discussed further in the commentary under 'Department of the Premier and Cabinet' in this Report.

Interpretation and analysis of the financial report

Highlights of the financial report*

	2018 $'million	2017 $'million
Income		
Sales	87	70
Cost of sales	(49)	(37)
Revenues from government	9	7
Property income	80	43
Other revenues	23	24
Gain resulting from changes in value of non-current assets	2	-
Total income	152	107
Expenses		
Employee benefits expenses	32	31
Operating expenditure, depreciation and amortisation	51	46
Borrowing costs	40	28
Loss resulting from changes in value of non-current assets	-	21
Total expense	123	126
Profit (Loss) before income tax equivalent	29	(19)
Income tax equivalent	9	-
Total comprehensive result	21	(19)
Net cash provided by (used in) operating activities	54	31
Net cash provided by (used in) investing activities	3	(642)
Net cash provided by (used in) financing activities	(26)	504
Assets		
Current assets	123	93
Non-current assets	966	976
Total assets	1 089	1 069

	2018 $'million	2017 $'million
Liabilities		
Current liabilities	212	193
Non-current liabilities	750	761
Total liabilities	962	954
Total equity	126	115

* Table may not add due to rounding.

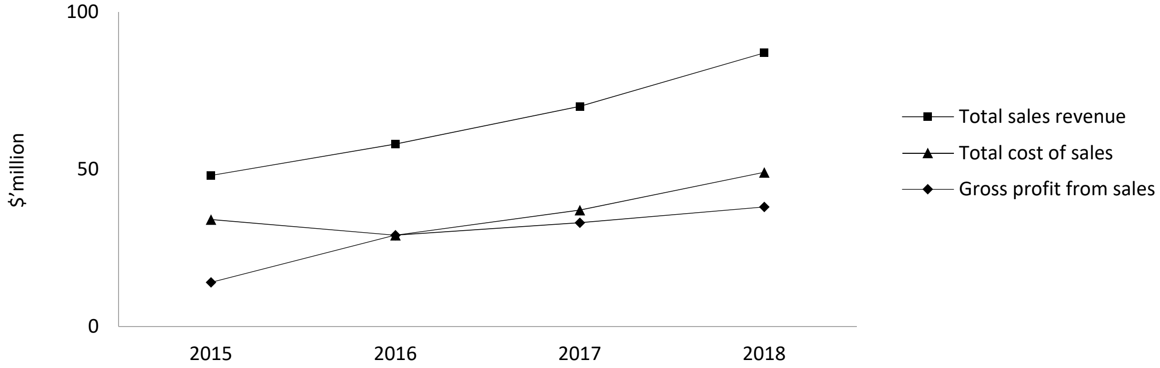
Statement of Comprehensive Income

Income

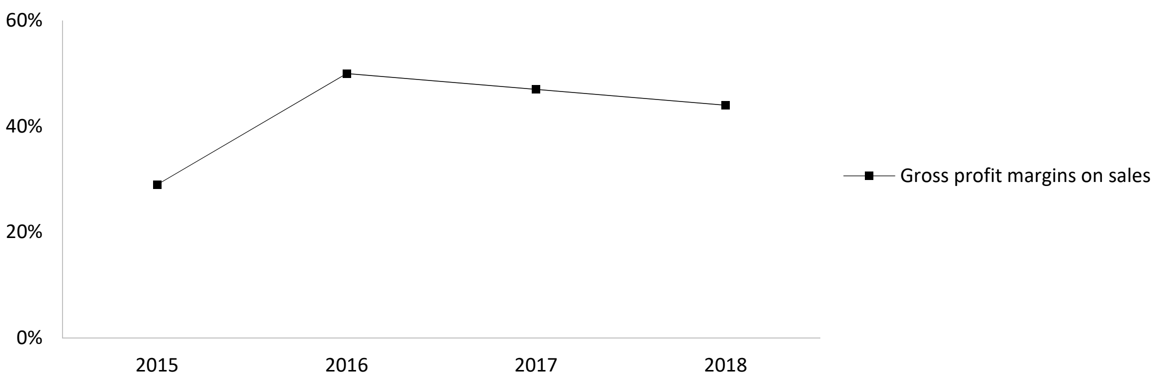
Income increased by $45 million to $152 million due mainly to:

- property income increasing by $37 million to $80 million due mainly to rental income from TAFE SA properties purchased from the Department of State Development (DSD) on 1 March 2017
- gross profit from land sales increasing by $5 million to $38 million, reflecting a $17 million increase in sales offset by a $12 million increase in the cost of sales. Increases in the sale of residential and mixed use land were partially offset by reduced sales of industrial land. There were large increases in land sales in Gillman, Seaford Residential, Woodville West, Tonsley, Elizabeth West, Bowden and Bowering Hill.

The following chart shows total land sales and cost of sales for the four years to 2018.



The gross profit margin on sales is an important driver of URA's profitability and is influenced by market prices for land and the historic costs of acquisition and development. The following chart shows the gross profit margin on sales for the four years to 2018.



Sales are trending upwards while the gross profit margin since 30 June 2016 has remained relatively constant resulting in higher gross profits. The increase in gross profit margin since 2016 reflects the sale of lower cost industrial properties or properties previously written down to their net realisable value. Before these write-downs the land sold was carried at higher values resulting in smaller profit margins.

Expenses

Expenses decreased by $3 million to $123 million due mostly to:

- the absence of losses from decreases in the value of non-current assets – a $21 million loss was experienced in 2017
- borrowing costs increasing by $12 million to $40 million principally due to the full-year impact of borrowings to partly fund the purchase of TAFE SA properties on 1 March 2017
- a $5 million increase in operating expenditure largely resulting from changes in the timing of capitalisation of land tax.

Dividend

Under section 26 of the URA Act, the URA is required to recommend to the Minister whether a dividend will be paid each financial year. The Minister approved an annual dividend payment of $7.6 million for 2018.

The URA is also required to declare a dividend of 100% of the profit relating to the Adelaide Station and Environs Redevelopment (ASER) site under the requirements of the Cabinet decision to transfer the site from the Department of Planning, Transport and Infrastructure to the URA effective 30 June 2013. The Minister approved an ASER dividend payment of $1.6 million for 2018.

Statement of Financial Position

Assets

Total assets increased by $20 million to $1089 million, reflecting a $31 million increase in cash, offset by reductions of $9 million in receivables and $3 million in investment properties.

Investment properties

The URA holds significant investment properties valued at $716 million, including TAFE SA properties purchased from DSD on 1 March 2017 for $619 million. The fair value of investment properties was reduced by $1 million due mainly to the normal expiration of leases and is supported by independent valuations performed as at 30 June 2018.

Inventories

The URA's primary activities involve holding and developing land inventory for sale. The value of this inventory increased by $1 million to $315 million and reflected:

- inventory additions:
  - $55 million ($53 million) in capitalised development costs including direct materials, salaries, land tax and borrowing costs where those costs are directly attributable to land currently under development. These costs are then recognised as part of cost of sales when inventories are sold

  - $9 million ($1 million) of land acquisition costs due mainly to the recognition of future land payments to the Commonwealth Department of Defence for land in Edinburgh Parks acquired by the URA in 2004 and 2005. The URA is contractually obliged to make these payments if the land is not on-sold within specified time frames
  - $9 million ($15 million) reversal of past write-downs of inventory to net realisable value
- inventory reductions:
  - $19 million ($7 million) of community service obligations. These obligations, which are funded by the SA Government, are non-commercial in nature and do not increase the likely sales value of inventory. Community service obligations increased by $12 million due mainly to $13 million provided by the SA Government to fund the capital costs of Lot Fourteen
  - $49 million ($37 million) of inventory was sold and included in cost of sales
  - $5 million ($18 million) of write-downs of inventory to net realisable value.

Inventory valuations and write-downs

In line with AASB 102 'Inventories' the URA recognises inventory at the lower of its cost and net realisable value. The measurement of the net realisable value of inventories depends on the URA's intended use of the inventories. The URA has grouped its inventories into the following two classes:

- land held for sale requiring low capital investment. The URA intends to release this land for sale based on market conditions. As at 30 June 2018 the value of land in this class was $208 million ($209 million)
- development projects requiring significant capital investment over extended periods of time before the land can be sold. These projects may be initiated by the SA Government, which provides community service obligation payments to partly fund the projects. As at 30 June 2018 the development projects were valued at $107 million ($105 million).

In 2016, the URA wrote its inventory down by $137 million. The significant write-down related mostly to changes in the URA's cash flow models used to determine the net realisable value of development projects. Importantly, these changes included reductions in revenue forecasts that occurred when the URA reassessed the likely outcomes of its business strategies for these projects. The revised revenue forecasts took into account the prevailing challenging market conditions and the extent to which the conditions were expected to continue into the future. In response, the URA modified its business strategies for some development projects to lower future costs. However, the URA considered its revised strategies would be insufficient to fully recover the past costs of some projects, and subsequently wrote them down.

In 2017, the URA wrote its inventory down by a further $2 million. This comprised an $18 million write-down due mainly to $11 million in higher remediation requirements for the Port Adelaide Waterfront, partially offset by past write-downs of $15 million that were reversed, including a $4 million reversal for Osborne North and a $3 million reversal for Bowden.

In 2018, the combination of write-downs and reversals of prior write-downs resulted in a net reversal of $4 million. This comprised a $5 million reversal arising from a change in the Woodville West business strategy and reversals of prior write-downs for Tonsley and Bowden, all partially offset by net write-downs of $3 million on other projects – including a $3 million write-down for Edinburgh Parks.

The following table shows the inventory and investment property write-downs and reversals that have occurred over the last three years.

Inventory	Write-downs (reversals) 2016 $'million	2017 $'million	2018 $'million	Carrying amount 30.06.18 $'million	Land area 30.06.18 Hectares
Development projects:					
Tonsley	54	(2)	(1)	69	46
Playford Alive	52	-	-	3	314
Bowden	17	(3)	(1)	25	11
Woodville West	5	0.5	(5)	10	4
Lot Fourteen	-	-	-	1	6
Land held for sale	9	7	3	208	3 081
Total inventory	137	2	(4)	315	3 462
Investment property	6	18	1	716	229
Total inventory and investment property	143	21	(2)	1 031	3 691

Note: Table may not add due to rounding.

The table highlights the impact of the URA's sales forecasts and capitalisation policy on the carrying amount of long-term development projects and their net realisable value. Significant land tax and other holding costs are included in the determination of their net realisable value. Longer development periods result in higher holding costs and lower net realisable value. This is particularly evident for Playford Alive where the project is expected to end in 2025-26. After the $52 million write-down in 2016, the project, which has a land area of 314 hectares, has a carrying amount of $3 million, due to the level of investment required and the extended period over which revenue is expected to be realised.

Measuring net realisable value involves estimating

Measuring the net realisable value of land held for sale is determined by the URA using independent valuations of current market value less selling costs. Measuring the net realisable value of large development projects is more complex. For these projects the URA determines net realisable value by estimating the future net cash flows of the projects (before interest) and discounting the cash flows back to present values. The URA applied a discount rate that reflects its financing costs and was adjusted for risk. The estimated cash flows were based on the amount and timing of sales and development costs, which for some projects extend many years into the future. The URA estimated when the development of each land parcel under current strategies will be completed and its market price once developed, and also estimated the development costs taking into account inflation.

Inventory is valued at lower of cost and net realisable value

AASB 102 requires that inventory be measured at the lower of cost and net realisable value. Net realisable value refers to the net amount that an entity expects to realise from the sale of inventory in the ordinary course of business. For the URA the ordinary course of business reflects the SA Government's approved plans for major development projects. Fair value reflects the price an orderly transaction to sell the same inventory, in the principal (or most advantageous) market for that inventory, would realise between market participants. The former is an entity-specific value, the latter is not. Net realisable value may not equal fair value less costs to sell.

If net realisable value is lower than cost, the URA is obliged to write down the value to net realisable value.

The URA does not, and is not required by AASB 102 to, disclose the fair value of its inventory. The URA's inventories have a carrying amount of $315 million, which may be less than their fair value.

Liabilities

Total liabilities increased by $8 million to $962 million and reflected:

- liability increases:
  - a $6 million increase in provisions due mainly to an increase of $6 million for income tax equivalent payable to the SA Government. The income tax liability is based on the Treasurer's accounting profit method, which requires that the corporate income tax rate (presently 30%) be applied to the profit for the reporting period
  - an $8 million increase in payables due mainly to the recognition of future land payments to the Commonwealth Department of Defence for land in Edinburgh Parks acquired by the URA in 2004 and 2005. The URA is contractually obliged to make these payments if the land is not on-sold within specified time frames
  - an $11 million increase in unearned income due mainly to receiving a lease premium from SkyCity for granting a lease over additional land area to facilitate the expansion of the Adelaide Casino. The premium will be recognised as revenue over the lease term
- liability decreases:
  - a $17 million reduction in borrowings resulting from positive cash flows from operations. Borrowings of $894 million ($911 million) comprise 93% (95%) of total liabilities. Borrowings are primarily required to fund property purchases, capital development costs for inventories and operating expenditure. Refer to 'Borrowings, liquidity and review of asset holdings' below for further commentary on debt management.

Statement of Cash Flows

Net cash provided by operating activities increased by $23 million to $54 million due mainly to:

- cash increases:
  - increases of $52 million in receipts from tenants (due mostly to rent from TAFE SA properties purchased in 2017), $17 million in sales and $14 million in receipts from the SA Government
  - a $26 million decrease in payments for land purchases and development
- cash decreases:
  - a $56 million decrease in GST recovered from the ATO (due mostly to GST on the purchase of TAFE SA properties in 2017)
  - a $13 million increase in interest paid on borrowings.

Net cash provided by investing activities was $3 million whereas in 2017 the net cash used in investing activities was $642 million. The change was due mainly to the purchase of TAFE SA properties in 2017 for $619 million plus GST of $59 million.

Net cash used in financing activities was $26 million whereas in 2017 the net cash provided by financing activities was $504 million. The change was due mainly to new borrowings of $400 million in 2017 to partly fund the purchase of TAFE SA properties.

Further commentary on operations

Provision of services to South Australian Housing Trust (SAHT)

On 8 December 2014, the SA Government approved a strategy to progressively replace ageing SAHT owned housing with new social housing dwellings that better meet contemporary social housing needs. The SAHT and the URA have entered into a service level administrative arrangement to reflect the financial, asset management and not-for-profit community housing sector services provided by the URA.

To enable the URA to manage the services it provides to the SAHT under the service level administrative arrangement, a number of employees were transferred from the then Department for Communities and Social Inclusion to the URA on 5 February 2015. The salary costs and leave entitlements of the transferred employees and corresponding recharges of these costs back to the SAHT are reflected in the URA's financial report. All costs associated with the SAHT capital program, including the construction of new social housing dwellings, continue to be reflected in the SAHT's financial report.

On 1 July 2018, as part of machinery of government changes, 166 employees of the URA were transferred to the employment of the Chief Executive of the SAHT on the same basis of engagement as applied before the transfer.

Provision of administrative support to the Riverbank Authority

The Riverbank Authority was established by the Housing and Urban Development (Administrative Arrangements) (Riverbank Authority) Regulations 2014 on 13 February 2014. It has a Board of Management but does not have any employees. All the administrative support functions for the Board are provided by employees of the URA under a service level administrative arrangement.

On 19 July 2018, the dissolution of the Riverbank Authority was gazetted, with its assets, rights and liabilities transferred to the URA.

Borrowings and liquidity

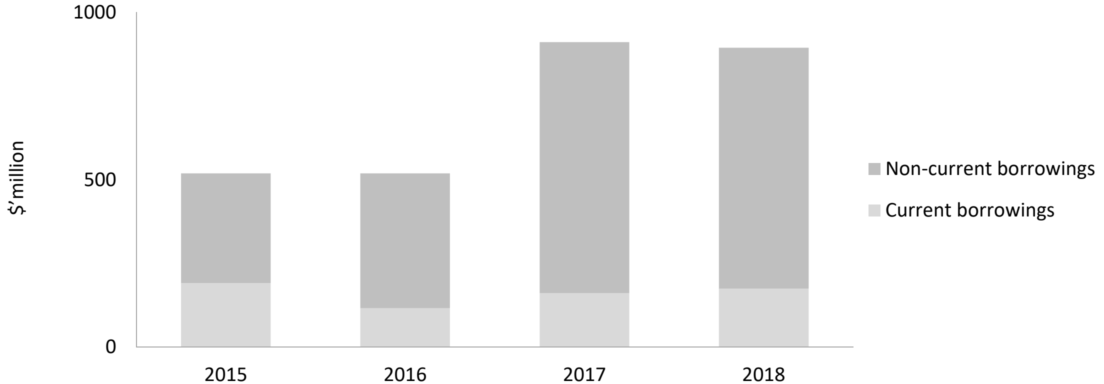
The URA's borrowings from the South Australian Government Financing Authority at 30 June 2018 reduced by $17 million to $894 million due mostly to positive cash flows from operations.

The URA's borrowings include:

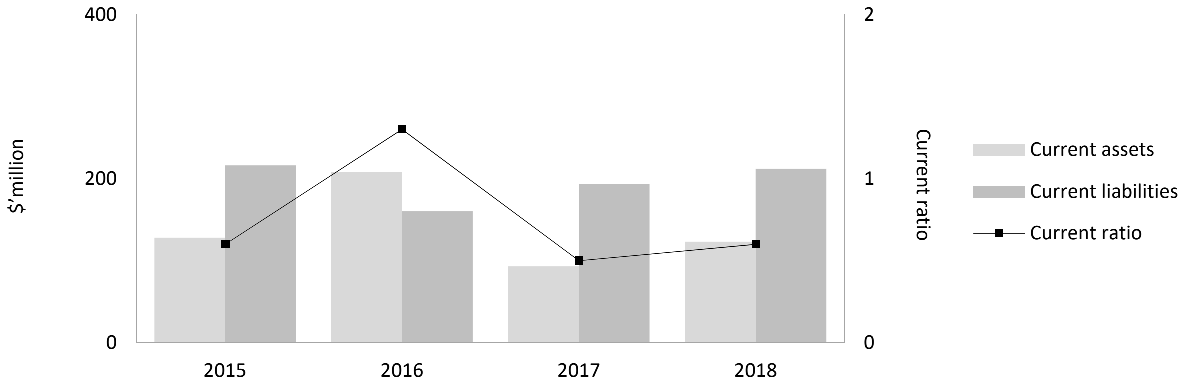
- $400 million of borrowings in 2017 to partly fund the purchase of TAFE SA properties from DSD
- debt incurred by the former Land Management Corporation

- borrowings incurred on the establishment of the URA to fund asset transfers from Defence SA and the SAHT
- borrowings to fund land developments and operating expenditure. The URA's current business model requires a level of up-front investment in projects that result in an accumulation of borrowings, until such time as sufficient revenues are realised to progressively retire the loans.

The chart below shows the impact of the new borrowings in 2017.



The chart below shows the trend in the URA's liquidity measured by the ratio of current assets to current liabilities.



Current liabilities exceeded current assets in all years except 2016, when the SA Government provided the URA with a $135 million equity contribution. This increased the cash held by the URA at 30 June 2016 and its liquidity. The $135 million was used in 2017 to partly fund the purchase of TAFE SA properties. The improved liquidity was therefore temporary. In future years, the rental income from TAFE SA properties should gradually improve the URA's liquidity position and is evident in 2018.

Debt management, financial sustainability and purchase of TAFE SA properties

The Department of Treasury and Finance requires the URA to adopt a core debt management facility approach, consistent with other public non-financial corporations. This requires approval by the Minister and Treasurer of an annual debt ceiling. In June 2016, the Minister and Treasurer approved that the core debt facility be increased by $390 million to $930 million with the continuation of a $50 million working capital facility. The additional borrowings, together with equity contributions from the SA Government of $219 million, were used to buy TAFE SA properties. The Minister and Treasurer anticipate that the TAFE SA properties will provide a longer term commercial revenue stream for the URA and enable the debt to asset ratio to remain at prudent levels. The URA's core debt facility was increased by $194 million in June 2018 to accommodate investment by the URA in the Lot Fourteen redevelopment.

The 2018-19 State Budget was tabled in the South Australian Parliament on 4 September 2018. It announced the planned closure of several TAFE SA campuses, including the Tea Tree Gully, Port Adelaide and Cooper Pedy campuses which are owned by the URA and leased to DSD, and then sub-leased to TAFE SA. The URA is working with the SA Government to determine the future strategy for the three properties and the impact of their closure on the URA.

Status of major development projects

Lot Fourteen

In March 2018, the former Royal Adelaide Hospital site (renamed Lot Fourteen) was transferred to the URA from the then Department for Health and Ageing for $0 consideration. Some Lot Fourteen buildings will be demolished while heritage buildings will be re-fitted and retained. In 2018, the SA Government provided community service obligation funding of $16 million for the project, which included $13 million for capital costs. Capital funding received was offset against the capital expenditure incurred in 2018 of $14 million, resulting in the project having a carrying value of $1 million.

The 2018-19 State Budget announced the redevelopment of Lot Fourteen at an estimated cost of $476 million over five years. This will include the establishment of an Innovation and Commercialisation Precinct, a new International School of Culinary Excellence, Hospitality and Tourism and a National Aboriginal Art and Cultures Gallery.

Playford Alive

The Playford Alive project was approved by Cabinet in February 2006. The project involves renewing the suburbs of Davoren Park and Smithfield Plains and developing land at Munno Para, Munno Para Downs, Andrews Farm and Penfield. The URA delivers the renewal areas of the project for the SAHT and develops the greenfield component of the project in its own right. The project is expected to be completed in 2026.

Playford Alive inventory is valued at $3 million ($5 million). In 2016 the inventory was written down by $52 million but has required no further write-downs. Income from inventory sales was $10 million in 2018 while capital expenditure was $6 million.

Tonsley

In December 2009, Cabinet approved the purchase of the former Mitsubishi Motors Tonsley Park manufacturing site at Clovelly Park. The URA is developing the site into a precinct that supports knowledge-intensive industries helping the economic growth of southern Adelaide. Land is also being developed and sold from the site. The project is expected to be completed in 2028.

Tonsley inventory is valued at $69 million ($53 million) after reversing $1 million of previous write-downs. Income from inventory sales was $6 million in 2018 while capital expenditure was $23 million.

Woodville West

The Woodville West medium density residential development commenced in 2009 following Cabinet approval for the then Department for Communities and Social Inclusion to demolish outdated SAHT owned dwellings and create new dwellings. The project was transferred to the URA in April 2012. The project is expected to be completed in 2021.

Woodville West inventory is valued at $10 million ($19 million) after reversing $5 million of write-downs incurred in 2017 and 2016. Income from inventory sales was $22 million in 2018 while capital expenditure was $4 million.

Bowden

Bowden is a higher density urban infill project expected to house approximately 3500 residents in over 2400 dwellings, and has a substantial commercial and retail component. The URA manages land development, remediation, infrastructure works, community engagement and marketing, with the private sector purchasing vacant developed land for building construction. The project is expected to be completed in 2026.

Bowden inventory is valued at $25 million ($28 million) after reversing $1 million of previous write-downs. Income from inventory sales was $8 million in 2018 while capital expenditure was $3 million.

Part B – General index

A

Acronyms
- AFCT *see* Adelaide Festival Centre Trust, 3
- AGD *see* Attorney-General's Department, 19
- AOSMA *see* Adelaide Oval SMA Limited, 9
- AVMC *see* Adelaide Venue Management Corporation, 15
- CAA *see* Courts Administration Authority, 73
- CALHN *see* Central Adelaide Local Health Network Incorporated, 142
- CHSALHN *see* Country Health SA Local Health Network Incorporated, 163
- DCP *see* Child Protection, Department for, 53
- DCS *see* Correctional Services, Department for, 63
- DEW *see* Environment and Water, Department for, 98
- DHS *see* Human Services, Department of, 224
- DHW *see* Health and Wellbeing, Department for, 121
- DPC *see* Premier and Cabinet, Department of the, 282
- DPTI *see* Planning, Transport and Infrastructure, Department of, 261
- DSD *see* State Development, Department of, 399
- DTF *see* Treasury and Finance, Department of, 460
- EPA *see* Environment Protection Authority, 92
- Flinders *see* Flinders University, 481
- HomeStart *see* HomeStart Finance, 212
- ICAC *see* Independent Commissioner Against Corruption, 238
- LSA *see* Lifetime Support Authority of South Australia, 242
- MAC *see* Motor Accident Commission, 250
- NALHN *see* Northern Adelaide Local Health Network Incorporated, 171
- OPI *see* Office for Public Integrity, 238
- PIRSA *see* Primary Industries and Regions, Department of, 296
- RTWSA *see* Return to Work Corporation of South Australia, 308
- SA Water *see* South Australian Water Corporation, 383
- SAAS *see* SA Ambulance Service Inc, 182
- SAFA *see* South Australian Government Financing Authority, 345
- SAFECOM *see* South Australian Fire and Emergency Services Commission, 330
- SAHT *see* South Australian Housing Trust, 357
- SALHN *see* Southern Adelaide Local Health Network Incorporated, 190
- SAPOL *see* South Australia Police, 320
- SASB *see* South Australian Superannuation Board, 416
- SASS *see* South Australian Superannuation Scheme, 423
- SATC *see* South Australian Tourism Commission, 378
- SSARIF *see* Super SA Retirement Investment Fund, 433
- Triple S *see* Southern State Superannuation Scheme, 429
- Uni Adelaide *see* University of Adelaide, 488
- UniSA *see* University of South Australia, 496
- URA *see* Urban Renewal Authority, 507
- WCHN *see* Women's and Children's Health Network Incorporated, 205

Adelaide 500
- Naming rights sponsor, 382
- South Australian Tourism Commission, 380

Adelaide Convention Centre
- Adelaide Venue Management Corporation, 16

Adelaide Desalination Plant
- South Australian Water Corporation, 390

Adelaide Entertainment Centre
- Adelaide Venue Management Corporation, 16

Adelaide Fashion Festival
- South Australian Tourism Commission, 380

Adelaide Festival Centre and Plaza
- Adelaide Festival Centre Trust, 8

Adelaide Festival Centre Trust, 3
- Financial controls opinion, 3
- Financial report opinion, 3
- Financial statistics, 3
- Redevelopment of Her Majesty's Theatre, 7
- Redevelopment of the Adelaide Festival Centre and Plaza, 8
- Significant events and transactions, 3

Adelaide Oval redevelopment
- Planning, Transport and Infrastructure, Department of, 273

Adelaide Oval SMA Limited, 9
- Commercial Operations Trust, 14
- Financial controls opinion, 9
- Financial report opinion, 9
- Financial statistics, 9
- Insurance, 14
- Leasing and licensing arrangements, 14
- Significant events and transactions, 9
- Sinking fund, 14
- South Australian Cricket Association, 9
- South Australian National Football League, 9
- Stakeholder contributions, 12
- State legislative requirements, 13
- Trading activities, 11

Adelaide Venue Management Corporation, 15
- Adelaide Convention Centre, 16
- Adelaide Entertainment Centre, 16
- Coopers Stadium, 16
- Financial controls opinion, 15

Financial report opinion, 15
Financial statistics, 15
Loss on property management activities, 18
Profit from trading activities, 17
Significant events and transactions, 15

Attorney-General's Department, 19
Consumer and Business Services, 24
Crown Solicitor's Office, 23
Financial controls opinion, 20
Financial management, 22
Financial report opinion, 19
Financial statistics, 19
Fines Enforcement and Recovery Unit, 26, 34
Gaming machine administration, 37
Independent Gaming Corporation Limited, 38
Murray-Darling Basin Royal Commission, 38
National Redress Scheme for Institutional Child Sexual Abuse, 36
Payroll, 21
Public Trustee, 39
Qualified opinion – Financial controls
Assessment of controls, 21
Residential Tenancies Fund, 25, 38
SafeWork SA, 23
Shared Services SA – financial systems and transaction processing environments, 27
Significant events and transactions, 19
South Australian Government Radio Network, 22
Taxation, 37
Victims of Crime Fund, 35

Auditor-General's Department, 52
Financial controls opinion, 52
Financial report opinion, 52
Financial statistics, 52

B

Bluedoor system implementation
South Australian Superannuation Board, 417

Bridgestone World Solar Challenge
South Australian Tourism Commission, 380

C

Central Adelaide Local Health Network Incorporated, 142
Enterprise Pathology Laboratory Information System, 146
Expenditure, 151
Financial controls opinion, 143
Financial report opinion, 143
Financial statistics, 142
Governance changes, 148
Health sector, 117, 142
New Royal Adelaide Hospital, 144
Commencement of service delivery, 144
Impact of completion of the new RAH, 144
Legal action in progress, 144
Public private partnership arrangement, 144
Quarterly service payments, 144
Refinancing event, 145
Patient billing, 156
Payroll, 149
Private practice audits, 158
Property, plant and equipment, 161
Qualified opinion – Financial controls
Assessment of controls, 149
SA Pathology, 155
SA Pharmacy, 152
Significant events and transactions, 142

Child Protection, Department for, 53
Commercial care expenditure processes, 56
Expenses, 60
Financial controls opinion, 53
Financial report opinion, 53
Financial statistics, 53
Governance arrangements, 55
Number of children in care, 54
Qualified opinion – Financial controls
Assessment of controls, 55
Review of key payroll reports, 58
Shared Services SA – financial systems and transaction processing environments, 59
Significant events and transactions, 53
Transfer of Families SA from Department for Education, 88
Weaknesses in IT management controls, 58

Community Emergency Services Fund
South Australian Fire and Emergency Services Commission, 341

Consumer and Business Services
Attorney-General's Department, 24

Coopers Stadium
Adelaide Venue Management Corporation, 16

Correctional Services, Department for, 63
Additional compensation provision, 67, 71
Annual cost per prisoner per facility, 68
Capital works in progress, 70
Equity contribution, 69
Expenses, 66
Financial controls opinion, 63
Financial report opinion, 63
Financial statistics, 63
Procurement and contract management processes, 65
Property, plant and equipment, 70
Qualified opinion – Financial controls
Assessment of controls, 64
Shared Services SA – financial systems and transaction processing environments, 65
Significant events and transactions, 63
Supplies and services expenses, 67
Workers compensation, 67, 71

Country Health SA Local Health Network Incorporated, 163
EPAS revenue – Port Augusta, 167
Financial controls opinion, 163
Financial report opinion, 163
Financial statistics, 163
Governance changes, 164
Health sector, 117, 163

New regional local health networks, 164
Barossa Hills Fleurieu Local Health Network Incorporated, 164
Eyre and Far North Local Health Network Incorporated, 164
Flinders and Upper North Local Health Network Incorporated, 164
Riverland Mallee Coorong Local Health Network Incorporated, 164
South East Local Health Network Incorporated, 164
Yorke and Northern Local Health Network Incorporated, 164
Payments to medical practitioners, 166
Qualified opinion – Financial controls
Assessment of controls, 165
Revenue, 167
Shared Services SA – financial systems and transaction processing environments, 168
Significant events and transactions, 163
Supplies and services, 167

Courts Administration Authority, 73
Court facilities planning, 77
Electronic Court Management System project, 77
Financial controls opinion, 73
Financial report opinion, 73
Financial statistics, 73
Payroll, 74
Qualified opinion – Financial controls
Assessment of controls, 74
Significant events and transactions, 73

Credit Union Christmas Pageant
South Australian Tourism Commission, 380

Crown Solicitor's Office
Attorney-General's Department, 23

CTP insurance regulator
Motor Accident Commission, 250

D

Department for Child Protection *see* Child Protection, Department for, 53

Department for Correctional Services *see* Correctional Services, Department for, 63

Department for Education *see* Education, Department for, 80

Department for Environment and Water *see* University of South Australia, 98

Department for Health and Wellbeing *see* Health and Wellbeing, Department for, 121

Department of Human Services *see* Human Services, Department of, 224

Department of Planning, Transport and Infrastructure *see* Planning, Transport and Infrastructure, Department of, 261

Department of Primary Industries and Regions *see* Primary Industries and Regions, Department of, 296

Department of State Development *see* State Development, Department of, 399

Department of the Premier and Cabinet *see* Premier and Cabinet, Department of the, 282

Department of Treasury and Finance *see* Treasury and Finance, Department of, 460

Disability and aged care reform
Human Services, Department of, 235

E

Economic Investment Fund
Treasury and Finance, Department of, 473

Education, Department for, 80
Disaster recovery management, 86
Employees, 82
Financial controls opinion, 80
Financial report opinion, 80
Financial statistics, 80
Funding to schools and preschools, 81
Minor works and maintenance, 84
Payroll, 85
Payroll system IT controls, 86
Property, plant and equipment, 90
Qualified opinion – Financial controls
Assessment of controls, 83
SA Schools Investment Fund, 89
Shared Services SA – financial systems and transaction processing environments, 87
Significant events and transactions, 80
Transfer of Families SA to the Department for Child Protection, 88

Environment and Water, Department for, 98
Accounts payable, 100
Cash, 103
Financial controls opinion, 98
Financial report opinion, 98
Financial statistics, 98
Fixed assets, 104
General ledger, 104
IT general control review – Masterpiece, 106
Murray-Darling Basin Authority, 110
National Landcare Program, 109
Natural Resources Management Boards, 110
Natural Resources Management Fund, 110
Payroll, 101
Qualified opinion – Financial controls
Assessment of controls, 99
Risk management, 105
Shared Services SA – financial systems and transaction processing environments, 106
Significant events and transactions, 98

Environment Protection Authority, 92
Cash and cash equivalents, 96
Financial controls opinion, 92
Financial report opinion, 92
Financial statistics, 92
Green Industries Fund, 96
Payments to SA Government, 95

Shared Services SA – financial systems and transaction processing environments, 93
Significant events and transactions, 92
Waste levies, 97

Essential Services Commission of South Australia
South Australian Water Corporation, 396

F

Fines Enforcement and Recovery Unit
Attorney-General's Department, 26, 34

Flinders Medical Centre
Southern Adelaide Local Health Network Incorporated, 204

Flinders University, 474, 481
Australian Government grants and payments, 484
Fees and charges, 485
Finance systems segregation of duties, 483
Financial controls opinion, 481
Financial report opinion, 481
Financial statistics, 481
Payroll, 483
Property, plant and equipment, 487
Qualified opinion – Financial controls
Assessment of controls, 482
Significant events and transactions, 481
Staff numbers, 486
Student loads, 485
University sector, 481

Funds SA *see* Superannuation Funds Management Corporation of South Australia, 437

Future Jobs Fund
Treasury and Finance, Department of, 473

G

Governors' Pensions Scheme
Superannuation sector, 412

Green Industries Fund
Environment Protection Authority, 96

H

Health and Wellbeing, Department for, 121
Accounts payable, 129
Comparison of actual expenses to original budget, 139
Financial controls opinion, 121
Financial report opinion, 121
Financial statistics, 121
FTEs, 119
Governance and accountability, 130
Governance changes, 122
Health sector, 116, 121
IT general controls, 132
EPAS, 133
Oracle Corporate System, 132
Medical officer professional development, 130
Payroll, 131
Procurement and contract management, 123
Qualified opinion – Financial controls
Assessment of controls, 123
Revenues from the SA Government, 135
Shared Services SA – financial systems and transaction processing environments, 133
Significant events and transactions, 121
Supplies and services expenses, 134, 139

Health sector
Central Adelaide Local Health Network Incorporated, 117, 142
Country Health SA Local Health Network Incorporated, 117, 163
Governance arrangements, 115
Health and Wellbeing, Department for, 116, 121
Health care legislation, 115
Health sector staffing and patient activity, 118
Hospital activity statistics, 119
Staffing statistics, 119
Information technology and system change
Enterprise Pathology Laboratory Information System, 114
Enterprise Patient Administration System, 114
Legacy systems, 114
Local health networks, 116
National Health Reform Agreement, 116
New Royal Adelaide Hospital, 113
Impact on the financial reports, 113
Outstanding matters and operational disputes, 113
Northern Adelaide Local Health Network Incorporated, 117, 171
Oakden Older Persons Mental Health Facility, 114
Overview, 111
Repatriation General Hospital, 113
SA Ambulance Service Inc, 182
SA local health networks, 116
Health Advisory Councils, 117
Significant events and challenges, 111
Financial sustainability and budget, 111
governance and accountability changes, 111
High turnover of senior executive positions, 112
New Royal Adelaide Hospital, 113
Oakden Older Persons Mental Health Facility, 114
Regional country local health networks, 112
Repatriation General Hospital, 113
Southern Adelaide Local Health Network Incorporated, 117, 190
Women's and Children's Health Network Incorporated, 117, 205

Her Majesty's Theatre
Adelaide Festival Centre Trust, 7

Highways Fund
Planning, Transport and Infrastructure, Department of, 278

HomeStart Finance, 212
Bad and impaired loans expense, 215
Breakthrough loans, 216
Customer loans repaid, 222
Distributions to government, 221
Financial controls opinion, 212

Financial report opinion, 212
Financial statistics, 212
General reserve, 218
HomeStart operating parameters, 223
Investments, 220
Liabilities, 220
Loan quality, 218
Loans and advances, 216
Net interest income, 214
Provisions for impairment, 217
Risk management, 219
Shared equity option loans, 216
Significant events and transactions, 212

Human Services, Department of, 224
Brokerage care services, 226
Concessions payments, 226, 234
Disability and aged care reform, 235
Early childhood early intervention, 236
Supported Community Accommodation Services, 236
Transfer of domiciliary care services, 235
Financial controls opinion, 224
Financial report opinion, 224
Financial statistics, 224
Grants, subsidies and client payments, 229
Machinery of government changes, 237
National Disability Insurance Scheme, 234
Qualified opinion – Financial controls
Assessment of controls, 225
Shared Services SA – financial systems and transaction processing environments, 228
Significant events and transactions, 224
South Australian Housing Trust, 358

I

Independent Commissioner Against Corruption, 238
Evaluation of the operations of the Public Trustee, 44
Financial controls opinion, 238
Financial report opinion, 238
Financial statistics, 238
Northern Adelaide Local Health Network Incorporated, 180
Office for Public Integrity, 238
Shared Services SA – financial systems and transaction processing environments, 239
Significant events and transactions, 238

Independent Gaming Corporation Limited
Attorney-General's Department, 38

Investment Attraction South Australia
State Development, Department of, 410

J

Judges' Pensions Scheme
Superannuation sector, 412

L

Land services commercialisation
Treasury and Finance, Department of, 461

Lifetime Support Authority of South Australia, 242
Annual contribution and levy, 249
Auditor's report on the financial report, 243
Significant inherent uncertainty – provision for participants' treatment, care and support services, 244
Financial controls opinion, 242
Financial report opinion, 242
Financial statistics, 242
Independent reviewing actuary, 248
Lifetime Support Scheme Fund, 243
Probability of sufficiency, 248
Provision for participants' treatment, care and support services, 247
Shared Services SA – financial systems and transaction processing environments, 244
Significant events and transactions, 242
Significant inherent uncertainty in the provision, 247
Superannuation Funds Management Corporation of South Australia, 440

M

Motor Accident Commission, 250
CTP regulator, 250
Financial controls opinion, 250
Financial report opinion, 250
Financial statistics, 250
Investment result, 257
Investments, 258
Net claims, 257
Outstanding claims liability, 254
Planning, Transport and Infrastructure, Department of, 277, 278, 280
Return of capital, 253
Further capital returns are projected, 251
Payment to the Highways Fund, 251
Road safety funding, 253
Sale of investment property portfolio, 253
Shared Services SA – financial systems and transaction processing environments, 252
Significant events and transactions, 250
Solvency level is above the target level, 253
Superannuation Funds Management Corporation of South Australia, 440

Murray-Darling Basin Authority
Environment and Water, Department for, 110

Murray-Darling Basin Royal Commission
Attorney-General's Department, 38

N

National Disability Insurance Scheme
Human Services, Department of, 234

National Landcare Program
Environment and Water, Department for, 109

National Redress Scheme for Institutional Child Sexual Abuse
Attorney-General's Department, 36

South Australian Government Financing Authority, 355

Natural Resources Management Boards
Environment and Water, Department for, 110

Natural Resources Management Fund
Environment and Water, Department for, 110

New Royal Adelaide Hospital
Central Adelaide Local Health Network Incorporated, 144
Health sector, 113

Northern Adelaide Local Health Network Incorporated, 171
Accounts payable, 177
Financial controls opinion, 172
Financial report opinion, 171
Financial statistics, 171
Governance changes, 172
Health sector, 117, 171
Independent Commissioner Against Corruption, 180
Oakden facility, 180
Older Persons Mental Health, 180
Patient billing, 176
Payroll, 174
Professional development leave, 177
Qualified opinion – Financial controls
Assessment of controls, 173
Recall allowances, 175
Significant events and transactions, 171

O

Oakden facility
Health sector, 114
Northern Adelaide Local Health Network Incorporated, 180

Office for Public Integrity
Independent Commissioner Against Corruption, 238

Office of Recreation, Sport and Racing
Planning, Transport and Infrastructure, Department of, 272

P

Parliamentary Superannuation Scheme
Superannuation Funds Management Corporation of South Australia, 440
Superannuation sector, 412

Pipe bursts data
South Australian Water Corporation, 391

Planning, Transport and Infrastructure, Department of, 261
Accounts payable, 272
Across government facilities management, 270
Adelaide Oval redevelopment, 273
Administered items, 280
Capital works in progress, 279
City Tramline Extension internal audit, 265, 269
Financial controls opinion, 261
Financial report opinion, 261
Financial statistics, 261
Highways Fund, 278
ICT and control, 273
Land, buildings and facilities, 280
Motor Accident Commission, 277, 278, 280
Network assets, 279
Office of Recreation, Sport and Racing, 272
Operating expenses by activity, 274
Payroll, 271
Plant and equipment, 280
Procurement and contract management, 263
Qualified opinion – Financial controls
Assessment of controls, 262
Revenue sources, 276
Shared Services SA – financial systems and transaction processing environments, 273
Significant events and transactions, 261

Police Superannuation Scheme
Superannuation Funds Management Corporation of South Australia, 440
Superannuation sector, 412

Premier and Cabinet, Department of the, 282
Accounts payable, 284
Financial controls opinion, 282
Financial report opinion, 282
Financial statistics, 282
ICT revenue from government agencies, 284
PACE Gas
Grants, 284, 292
Qualified opinion – Financial controls
Assessment of controls, 283
Renewable Technology Fund, 285
Royalties, 295
Shared Services SA
Accounts payable controls, 286
Financial systems and transaction processing environments, 285
IT general controls, 288
Basware, 289
Chris21, 288
CommBiz, 290
Masterpiece, 289
Payroll controls, 286
Significant events and transactions, 282
Transfer of some Department of State Development functions, 406

Pridham Hall
University of South Australia, 505

Primary Industries and Regions, Department of, 296
Administered items, 307
Concessional loans schemes, 305
Financial controls opinion, 296
Financial report opinion, 296
Financial statistics, 296
Payroll, 299
Qualified opinion – Financial controls
Assessment of controls, 297

Regional Development Fund, 298, 303
Shared Services SA – financial systems and transaction processing environments, 300
Significant events and transactions, 296
South Australian River Murray Sustainability program, 302
System access, 299

Private practice arrangements
Southern Adelaide Local Health Network Incorporated, 199

Public Trustee, 39
Financial controls opinion, 39
Financial report opinion, 39
Financial statistics, 39
Governance arrangements, 40
Independent Commissioner Against Corruption evaluation of operations, 44
Information technology audit, 43
Masterpiece user access, 41
Payroll reconciliations, 42
Qualified opinion – Financial controls
Assessment of controls, 40
Shared Services SA – payroll transaction processing environment, 45
Significant events and transactions, 39
Trust operations, 42
Trusts being Administered, 48
Analysis, 49
Common fund financial reports, 48

Q

Qualified opinion – Financial controls
Assessment of controls
Attorney-General's Department, 21
Central Adelaide Local Health Network Incorporated, 149
Child Protection, Department for, 55
Correctional Services, Department for, 64
Country Health SA Local Health Network Incorporated, 165
Courts Administration Authority, 74
Education, Department for, 83
Environment and Water, Department for, 99
Flinders University, 482
Health and Wellbeing, Department for, 123
Human Services, Department of, 225
Northern Adelaide Local Health Network Incorporated, 173
Planning, Transport and Infrastructure, Department of, 262
Premier and Cabinet, Department of the, 283
Primary Industries and Regions, Department of, 297
Public Trustee, 40
SA Ambulance Service Inc, 184
South Australia Police, 321
South Australian Fire and Emergency Services Commission, 331
South Australian Housing Trust, 359
South Australian Superannuation Board, 419
Southern Adelaide Local Health Network Incorporated, 193
State Development, Department of, 400
TAFE SA, 449
University of Adelaide, 489
University of South Australia, 498
Women's and Children's Health Network Incorporated, 207

Qualified opinion – Financial report
University of South Australia, 497

R

Renewable Technology Fund
Premier and Cabinet, Department of the, 285

Renewing Our Streets and Suburbs initiative
South Australian Housing Trust, 366

Repatriation General Hospital
Health sector, 113
Southern Adelaide Local Health Network Incorporated, 204

Residential Tenancies Fund
Attorney-General's Department, 25, 38

Return to Work Corporation of South Australia, 308
Auditor's report on the financial report, 310
Inherent uncertainty – outstanding claims liability and funding ratio, 311
Claim management fees, 314
Claim payments, 313
Financial controls opinion, 308
Financial report opinion, 308
Financial statistics, 308
Investment profits, 315
Investments, 318
Investments by asset class, 319
Legislative changes, 309
Legislative reform, 317
Legislative review, 310
Market value of investments, 318
Outstanding claims – Compensation Fund, 316
Probability of sufficiency, 318
Return to Work Scheme, 310
Sensitivity to changes in key assumptions, 316
Significant events and transactions, 308
Total comprehensive result, 312
Underwriting result, 313

Riverbank Authority
Service provided by Urban Renewal Authority, 515

Royal Adelaide Hospital *see* New Royal Adelaide Hospital, 144

S

SA Ambulance Service Inc, 182
Financial controls opinion, 182
Financial report opinion, 182
Financial statistics, 182

Health sector, 182
Payroll, 186
Qualified opinion – Financial controls
Assessment of controls, 184
Revenue, 184
Shared Services SA – financial systems and transaction processing environments, 186
Significant events and transactions, 182
Staffing statistics, 119
Supplies and services expenditure, 185

SA Metropolitan Fire Service Superannuation Scheme
Superannuation Funds Management Corporation of South Australia, 440
Superannuation sector, 412

SA Venture Capital Fund
South Australian Government Financing Authority, 355

SafeWork SA
Attorney-General's Department, 23

Santos Tour Down Under
South Australian Tourism Commission, 380

School loans scheme
South Australian Government Financing Authority, 355

Shared Services SA
Accounts payable controls, 286
Financial systems and transaction processing environments
Attorney-General's Department, 27
Child Protection, Department for, 59
Correctional Services, Department for, 65
Country Health SA Local Health Network Incorporated, 168
Education, Department for, 87
Environment and Water, Department for, 106
Environment Protection Authority, 93
Health and Wellbeing, Department for, 133
Human Services, Department of, 228
Independent Commissioner Against Corruption, 239
Lifetime Support Authority of South Australia, 244
Motor Accident Commission, 252
Planning, Transport and Infrastructure, Department of, 273
Premier and Cabinet, Department of the, 285
Primary Industries and Regions, Department of, 300
SA Ambulance Service Inc, 186
South Australia Police, 324
South Australian Fire and Emergency Services Commission, 335
South Australian Housing Trust, 368
South Australian Tourism Commission, 379
State Development, Department of, 405
TAFE SA, 453
Treasury and Finance, Department of, 466
Urban Renewal Authority, 509
Women's and Children's Health Network Incorporated, 209
IT general controls, 288
Basware, 289
Chris21, 288
CommBiz, 290
Masterpiece, 289
Payroll controls, 286
Payroll transaction processing environment
Public Trustee, 45

South Australia Police, 320
Additional compensation provision, 326
Expiation fees, 329
Financial controls opinion, 320
Financial report opinion, 320
Financial statistics, 320
Information and communications technology and control, 323
Payroll – leave recording, 322
Qualified opinion – Financial controls
Assessment of controls, 321
Shared Services SA – financial systems and transaction processing environments, 324
Significant events and transactions, 320
Staffing, 329
Victims of Crime levy, 329
Workers compensation provision, 327

South Australian Ambulance Service Superannuation Scheme
South Australian Superannuation Board, 417
Superannuation Funds Management Corporation of South Australia, 440
Superannuation sector, 412

South Australian Country Fire Service
Leave dispute, 339
South Australian Fire and Emergency Services Commission, 331
Staffing, 343
Volunteers, 344

South Australian Cricket Association
Adelaide Oval SMA Limited, 9

South Australian Fire and Emergency Services Commission, 330
Community Emergency Services Fund, 341
Employee benefits expenses, 336
Financial controls opinion, 330
Financial report opinion, 330
Financial statistics, 330
Governance, 332
Manual payments, 334
Payroll, 333
Property, plant and equipment, 337
Provision for additional compensation, 338
Significant uncertainty with the estimate, 339
Provision for workers compensation, 338
Qualified opinion – Financial controls
Assessment of controls, 331
Shared Services SA – financial systems and transaction processing environments, 335
Significant events and transactions, 330

South Australian Country Fire Service, 331
Leave dispute, 339
South Australian Metropolitan Fire Service, 331
South Australian State Emergency Service, 331
Staffing, 343
Volunteers, 344

South Australian Government Financing Authority, 345
Business risk management, 351
Funding risk, 353
General market risk, 353
Operational risk, 351
Capital and distributions, 350
Catastrophe reinsurance program, 354
Financial controls opinion, 345
Financial report opinion, 345
Financial statistics, 345
Insurance activity, 348
Insurance settlement paid to Mr Henry Keogh, 356
Interest revenue and expense, 347
Leasing and hire revenue, 348
Loans to government agencies, 350
National Redress Scheme for Institutional Child Sexual Abuse, 355
SA Venture Capital Fund, 355
SAFA Advisory Board, 351
School loans scheme, 355
Significant events and transactions, 345
Superannuation Funds Management Corporation of South Australia, 440
Treasury portfolio structure, 352

South Australian Government Radio Network
Attorney-General's Department, 22

South Australian Housing Trust, 357
Amount returned to the State budget, 373
Board policy framework, 360
Business System Transformation, 368
Commonwealth funding agreements, 369
Debt management, 361
Debt policies, 363
Debt write-offs, 376
Financial controls opinion, 357
Financial report opinion, 357
Financial statistics, 357
Governance arrangements, 358, 359
Housing stock, 371
Human Services, Department of, 358
Installation of solar panels and Tesla batteries, 377
Land tax reimbursements, 373
Maintenance, 363
Properties transferred to community housing providers, 364
Qualified opinion – Financial controls
Assessment of controls, 359
Renewing Our Streets and Suburbs initiative, 366
1000 homes in 1000 days, 366
Renewing 4500 older SAHT homes, 366
Transfer of property and tenancy management, 366
Rental operations, 371
Rental properties, 374
Service provided by Urban Renewal Authority, 515
Shared Services SA – financial systems and transaction processing environments, 368
Significant events and transactions, 357
Triennial review, 367
Urban Renewal Authority, 358

South Australian Metropolitan Fire Service
South Australian Fire and Emergency Services Commission, 331
Staffing, 343

South Australian National Football League
Adelaide Oval SMA Limited, 9

South Australian River Murray Sustainability program
Primary Industries and Regions, Department of, 302

South Australian State Emergency Service
South Australian Fire and Emergency Services Commission, 331
Staffing, 343
Volunteers, 344

South Australian Superannuation Board, 416
Bluedoor system implementation, 417
Financial controls opinion, 416
Financial report opinion, 416
Financial statistics, 416
General reserve, 422
Qualified opinion – Financial controls
Assessment of controls, 419
Significant events and transactions, 416
South Australian Ambulance Service Superannuation Scheme, 417
South Australian Superannuation Scheme, 417
Southern State Superannuation Scheme, 417
Super SA Retirement Investment Fund, 417
Superannuation Funds Management Corporation of South Australia, 440
Superannuation on paid parental leave, 420
Superannuation sector, 416

South Australian Superannuation Scheme, 423
Benefits to members, 427
Contribution revenue, 427
Financial report opinion, 423
Financial statistics, 423
Funding of benefit payments, 428
Investment revenue, 426
Investments, 425
Lump Sum Scheme, 423
Member benefits liabilities, 425
Membership statistics, 427, 428
Pension Scheme, 423
Significant events and transactions, 423
South Australian Superannuation Board, 417
Superannuation Funds Management Corporation of South Australia, 440
Superannuation sector, 412, 423

South Australian Tourism Commission, 378
  Adelaide 500, 380
    Naming rights sponsor, 382
  Adelaide Fashion Festival, 380
  Bridgestone World Solar Challenge, 380
  China Brand Ambassador Campaign, 380
  Credit Union Christmas Pageant, 380
  Expenses, 380
  Financial controls opinion, 378
  Financial report opinion, 378
  Financial statistics, 378
  Industry assistance expenses, 380
  Santos Tour Down Under, 380
  Shared Services SA – financial systems and transaction processing environments, 379
  Significant events and transactions, 378
  Tasting Australia, 380

South Australian Water Corporation, 383
  Adelaide Desalination Plant, 390
  Asset value accounting, 397
  Cash and financing, 385
  Charter and performance statement, 394
  Community service obligations, 389
  Comparison with other water utilities, 396
  Ellipse system controls, 384
  Financial controls opinion, 383
  Financial ownership framework, 394
  Financial report opinion, 383
  Financial statistics, 383
  Key financial performance measures, 394
  Main sources of income, 387
  Operating result, 387
  Pipe bursts data, 391
  Renewal of the water and sewer pipe, 393
  SA Water maintenance, 391
  Significant events and transactions, 383
  Water and sewer rates and charges, 396
    ESCOSA, 396
    ESCOSA determinations, 397
    Pricing orders, 396
    Water pricing, 397
  Water usage, 388

Southern Adelaide Local Health Network
  Incorporated, 190
  Accounts payable, 195
  Financial controls opinion, 191
  Financial report opinion, 191
  Financial statistics, 190
  Governance changes, 191
  Health sector, 117, 190
  Hospital billing, 196
  Infrastructure changes, 204
    Flinders Medical Centre, 204
    Repatriation General Hospital, 204
  Payroll, 193
  Private practice arrangements, 199
  Professional development entitlements, 200
  Qualified opinion – Financial controls
    Assessment of controls, 193
  Significant events and transactions, 190

Southern State Superannuation Scheme, 429
  Benefits payable, 431, 432
  Contribution revenue, 432
  Financial report opinion, 429
  Financial statistics, 429
  Membership statistics, 432
  Significant events and transactions, 429
  South Australian Superannuation Board, 417
  Superannuation Funds Management Corporation of South Australia, 440
  Superannuation sector, 412, 429

State Development, Department of
  Funding to TAFE SA, 456

State Development, Department of, 399
  Financial controls opinion, 399
  Financial report opinion, 399
  Financial statistics, 399
  Funding to TAFE SA, 407
  Grant payments – Arts South Australia, 401
  Investment Attraction South Australia, 410
  Payments to WorkReady service providers, 402
  Payroll, 402
  Qualified opinion – Financial controls
    Assessment of controls, 400
  Sale of property leased to TAFE SA to the Urban Renewal Authority, 406
  Shared Services SA – financial systems and transaction processing environments, 405
  Significant events and transactions, 399
  Transfer of some functions to the Department of the Premier and Cabinet, 406

State Development, Department of
  Sale of property leased to TAFE SA to the Urban Renewal Authority, 516

Super SA Retirement Investment Fund, 433
  Benefits payable, 436
  Financial report opinion, 433
  Financial statistics, 433
  Flexible Rollover product, 434
  Member benefits, 436
  Membership statistics, 436
  Significant events and transactions, 433
  South Australian Superannuation Board, 417
  Super SA Income Stream Product, 434
  Superannuation Funds Management Corporation of South Australia, 440
  Superannuation sector, 412, 433

Super SA Select
  Superannuation sector, 412

Superannuation Funds Management Corporation, 437
  Superannuation sector, 437

Superannuation Funds Management Corporation of South Australia
  Asset allocation, 441
  Entities investing with Funds SA, 440
  Financial controls opinion, 437
  Financial report opinion, 437

Financial statistics, 437
Funds under management, 439
Income from investments, 442
Investment expenses, 443
Investment option performance, 443
Lifetime Support Authority of South Australia, 440
Motor Accident Commission, 440
Parliamentary Superannuation Scheme, 440
Police Superannuation Scheme, 440
Restrictions on operations, 437
SA Metropolitan Fire Service Superannuation Scheme, 440
Significant events and transactions, 437
South Australian Ambulance Service Superannuation Scheme, 440
South Australian Government Financing Authority, 440
South Australian Superannuation Board, 440
South Australian Superannuation Scheme, 440
Southern State Superannuation Scheme, 440
Super SA Retirement Investment Fund, 440
Superannuation sector, 414

Superannuation sector, 412
Administration and funds management, 413
Catch-up funding, 415
Governors' Pensions Scheme, 412
Investments and related performance, 414
Judges' Pensions Scheme, 412
Member benefits liabilities, 414
Parliamentary Superannuation Scheme, 412
Police Superannuation Scheme, 412
SA Metropolitan Fire Service Superannuation Scheme, 412
South Australian Ambulance Service Superannuation Scheme, 412
South Australian Superannuation Board, 416
South Australian Superannuation Scheme, 412, 423
Southern State Superannuation Scheme, 412, 429
Super SA Retirement Investment Fund, 412, 433
Super SA Select, 412
Superannuation Funds Management Corporation, 437
Superannuation Funds Management Corporation of South Australia, 414

T

TAFE SA, 446
External reviews of TAFE SA, 447
Australian Skills Quality Authority, 448
Civil Aviation Safety Authority, 447
Nous and Moran/Bannikoff reviews, 448
Financial controls opinion, 447
Financial report opinion, 446
Financial statistics, 446
Funding from Department of State Development, 407, 456
Payroll, 449
Qualified opinion – Financial controls
Assessment of controls, 449
Sale of property leased to TAFE SA to Urban Renewal Authority, 406, 516
Shared Services SA – financial systems and transaction processing environments, 453
Significant events and transactions, 446
Student and other fees and charges, 457
Student fees and other revenue, 452
Training hours delivered, 456, 457, 458
TVSP payments, 454

Tasting Australia
South Australian Tourism Commission, 380

Treasurer's statements
Rectifying historical differences
Treasury and Finance, Department of, 465

Treasury and Finance, Department of, 460
Commonwealth funding, 472
Commonwealth Government funding, 471
Economic Investment Fund, 473
Financial controls opinion, 460
Financial report opinion, 460
Financial statistics, 460
Future Jobs Fund, 473
Land services commercialisation, 461
Accounting for up-front payment, 462
Appointment of Land Services SA, 461
Up-front payment from Land Services SA, 461
Revaluation Initiative, 471
Shared Services SA – financial systems and transaction processing environments, 466
Significant events and transactions, 460
State taxation statistics, 470
Treasurer's statements – Rectifying historical differences, 465
Weaknesses in the IT controls, 465

U

UniSA Cancer Research Institute
University of South Australia, 506

University of Adelaide, 474, 488
Australian Government grants and payments, 491
Controls to monitor leave recorded, 490
Fees and charges, 492
Financial controls opinion, 488
Financial report opinion, 488
Financial statistics, 488
Major capital works projects, 494
Payroll, 489
Potential merger with University of South Australia, 479
Qualified opinion – Financial controls
Assessment of controls, 489
Significant events and transactions, 488
Staff numbers, 493
Student loads, 492
University sector, 488

University of South Australia, 474, 496
- Australian Government grants and payments, 501
- Capital program, 504
- Contract management, 499
- Expenditure, 499
- Fees and charges, 501
- Financial controls opinion, 496
- Financial report opinion, 496
- Financial statistics, 496
- Grant funding, 498
- Income in advance, 505
- Payroll, 499
- Potential merger with University of Adelaide, 479
- Pridham Hall, 505
- Property, plant and equipment, 504
- Qualified opinion – Financial controls
  - Assessment of controls, 498
- Qualified opinion – Financial report, 497
  - Basis for Qualified Opinion, 498
- Significant events and transactions, 496
- Staff numbers, 503
- Student load, 502
- UniSA Cancer Research Institute, 506
- University sector, 496

University sector, 474
- Changes to Commonwealth funding arrangements, 479
- Defined benefit obligation, 479
- Financial control opinions, 475
- Financial report opinions, 474
- Financial statistics, 474
- Flinders University, 481
- FTEs, 474
- Government speranuation contribution, 478
- Key financial statistics, 475
  - Assets, 477
  - Australian Government grants and payments, 475
  - Employee related expenses, 476
  - Expenditure, 476
  - Fees and charges, 475
  - Income, 475
  - Liabilities, 478
  - Property, plant and equipment, 477
- Staff numbers, 477
- Student loads, 476
- Students, 474
- University of Adelaide, 488
- University of Adelaide and University of South Australia potential merger, 479
- University of South Australia, 496

Urban Renewal Authority, 507
- Borrowings and liquidity, 515
- Debt management, 516
- Dividend, 511
- Financial sustainability, 516
- Inventories, 511
- Inventory valuations and write-downs, 512
- Investment properties, 511
- Land sales, 510
- Major development projects, 517
  - Bowden, 518
  - Lot Fourteen, 517
  - Playford Alive, 517
  - Tonsley, 517
  - Woodville West, 517
- Provision of administrative support to the Riverbank Authority, 515
- Provision of services to South Australian Housing Trust, 515
- Sale of property leased by TAFE SA to Urban Renewal Authority, 406, 516
- Shared Services SA – financial systems and transaction processing environments, 509
- South Australian Housing Trust, 358
- Urban renewal program, 508

V

Victims of Crime Fund
- Attorney-General's Department, 35

Victims of Crime levy
- South Australia Police, 329

W

Waste levies
- Environment Protection Authority, 97

Women's and Children's Health Network
- Incorporated, 205
- Financial controls opinion, 205
- Financial report opinion, 205
- Financial statistics, 205
- Governance changes, 206
- Health sector, 117, 205
- Patient billing, 208
- Payroll, 207
- Qualified opinion – Financial controls
  - Assessment of controls, 207
- Shared Services SA – financial systems and transaction processing environments, 209
- Significant events and transactions, 205
- Supplies and services expenditure, 208