

Report of the Auditor-General

Report 11 of 2020

Adelaide Oval redevelopment
for the designated period
1 January 2020 to 30 June 2020

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Auditor-General's Department

www.audit.sa.gov.au

Enquiries about this report should be directed to:

Auditor-General
Auditor-General's Department
Level 9, 200 Victoria Square
Adelaide SA 5000

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Level 9
State Administration Centre
200 Victoria Square
Adelaide SA 5000
Tel +618 8226 9640
Fax +618 8226 9688
ABN 53 327 061 410
audgensa@audit.sa.gov.au
www.audit.sa.gov.au

President
Legislative Council
Parliament House
ADELAIDE SA 5000

Speaker
House of Assembly
Parliament House
ADELAIDE SA 5000

Dear President and Speaker

**Report of the Auditor-General:
Report 11 of 2020 *Adelaide Oval redevelopment for the designated
period 1 January 2020 to 30 June 2020***

Under section 9 of the *Adelaide Oval Redevelopment and Management Act 2011*,
I present to each of you Report 11 of 2020 *Adelaide Oval redevelopment for the designated
period 1 January 2020 to 30 June 2020*.

Acknowledgements

The audit team for this report was Salv Bianco, Philip Rossi and Grace Lum.

I express my appreciation for the cooperation and assistance provided by staff of the South Australian Government Financing Authority, the Department of Treasury and Finance and the Department for Infrastructure and Transport during the audit.

Yours sincerely

A handwritten signature in black ink, appearing to read 'Richardson', with a long horizontal flourish extending to the right.

Andrew Richardson
Auditor-General

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1 Executive summary

1.1 Introduction

This is the eighteenth Report to the Parliament on the Adelaide Oval redevelopment. The report is required by the *Adelaide Oval Redevelopment and Management Act 2011* (the Act) for each six-month period beginning on 1 January and 1 July each year.

This Report addresses my obligation under the Act to report on the Adelaide Oval Hotel development. I am required to report on this development as:

- the Adelaide Oval Hotel is a development for the purposes of the Act
- public money was made available to Adelaide Oval SMA Limited (AOSMA) through a \$42 million loan facility.

We address the Act's requirements as three terms of reference. Terms of reference two and three are explained and discussed in sections 4 and 5.

Term of reference one is no longer applicable as explained in section 2.3.1.

On 7 August 2019 the Treasurer entered into a loan facility to provide funds to AOSMA of up to \$42 million at a fixed interest rate of 4.5% per annum to fund the hotel development. Money was appropriated from the Consolidated Account in the 2019-20 State Budget to meet drawdowns of the loan facility by AOSMA. The loan facility has a repayment period of 10 years with repayments commencing shortly after the date that practical completion of the Adelaide Oval Hotel development is achieved. As at 30 June 2020 the Treasurer had advanced \$28.8 million to AOSMA. Construction of the hotel is in progress and it is expected to reach practical completion and commence operations in September 2020.

For this designated reporting period our review focussed on assessing the public accounts used to make loan funds available to AOSMA for the hotel development. We also reviewed processes established by the South Australian Government Financing Authority (SAFA) to manage the loan arrangement and ensure the obligations of AOSMA and the State are met.

Section 3 provides further background about the hotel development and loan arrangement.

1.2 Conclusion

The audit conclusions on each term of reference for the six-month period to 30 June 2020 are as follows.

1.2.1 Term of reference one

Section 9(1)(a) of the Act requires the Auditor-General to report on:

the extent to which money has been made available or expended within the \$535 million limit specified by this Part during the designated period.

Due to the effect of section 8(2) of the Act our obligation to report on this section ceased on 1 December 2019.

1.2.2 Term of reference two

We found that the state of the public accounts that are relevant to the Adelaide Oval Hotel development was satisfactory.

1.2.3 Term of reference three

On the basis of information obtained and reviewed to date we have not identified anything for the designated period that indicates the public money made available for the purpose of and in connection with the Adelaide Oval Hotel development was not managed and used properly and efficiently. We did identify some areas for improvement and made some other observations and these are detailed in sections 5.3 and 5.4.

1.3 Future challenges

We also identified some future challenges for the State in monitoring AOSMA's ability to meet its loan obligations due to the impact of the COVID-19 pandemic and overseeing the project for defects. These are discussed further in section 5.4.

2 Background

2.1 Introduction

The Act came into operation on 29 September 2011. Section 9 of the Act incorporates requirements for the financial supervision and reporting by the Auditor-General on the redevelopment of the Adelaide Oval envisaged by the Act. This Report discharges those requirements.

This is the eighteenth Report to the Parliament on the Adelaide Oval redevelopment. For the purpose of this designated period the Adelaide Oval redevelopment involves the design and construction of a hotel (the Adelaide Oval Hotel development). Section 2.3 provides the detail of how my reporting obligations under the Act apply to this project.

2.2 Structure of this Report

Section 1 provides an executive summary of the matters arising from the audit for the three reporting terms of reference provided in the Act.

My substantive Report is in sections 4 and 5, which cover the two remaining terms of reference. In addressing them I have provided an overview of my understanding of, and the approach taken to address, each term of reference and the outcome of my audit.

2.3 Requirements of the Act relevant to this Report

Section 9 of the Act provides for financial supervision of the Adelaide Oval Redevelopment project by the Auditor-General. It requires the Auditor-General to report to the Parliament on three terms of reference, for each six-month period beginning on 1 January and 1 July each year:

- Section 9(1)(a) – the extent to which money has been made available or expended within the \$535 million limit specified by the Act during the designated period.
- Section 9(1)(b) – the state of the public accounts that are relevant to the redevelopment of Adelaide Oval envisaged by the Act.
- Section 9(1)(c) – the extent to which it appears that public money made available to any entity, including an entity that is not a public authority, for the purposes of, or in connection with, the redevelopment of Adelaide Oval envisaged by the Act has been properly and efficiently managed and used during the designated period.

I sought advice to clarify my ongoing reporting obligations after 1 December 2019, being the end date specified in the Act that the expenditure limit of \$535 million applies. After receiving this advice I formed the view that:

- reporting on the \$535 million limit ceased on 1 December 2019

- I have an ongoing obligation to monitor and report on future developments for the Adelaide Oval
- the Adelaide Oval Hotel project is a development for the purpose of the Act and I am required to report on it.

This is further discussed below.

2.3.1 Reporting on the \$535 million limit is complete

For the first term of reference, the effect of section 8(2) of the Act is that the \$535 million limit prescribed under section 8(1) ceased on 1 December 2019. Consequently, my obligation to report on the matters under section 9(1)(a) also ceased at the end of the designated period in which that date fell.

2.3.2 Ongoing monitoring and reporting on Adelaide Oval developments

The obligations under sections 9(1)(b) and (c) are not time limited and extend to any future redevelopment that would fall under section 10(3) of the Act, whether it occurred before or after 1 December 2019. This is because of the apparent purpose of section 9 (to supervise expenditure relating to redeveloping the Adelaide Oval) and the ongoing supervision of AOSMA under section 6 of the Act extending beyond the expiry of the \$535 million limit.

This means that I have an ongoing obligation to:

- monitor any future redevelopment activity on the Adelaide Oval that falls under section 10(3) of the Act
- report on this redevelopment activity under sections 9(1)(b) and (c) of the Act if public money is made available to any entity for the purpose of, or in connection with, this activity.

2.3.3 Adelaide Oval Hotel reporting obligations

Based on the ongoing monitoring and reporting obligations described in section 2.3.2, I am required to report on the Adelaide Oval Hotel development as:

- the Adelaide Oval Hotel is a development for the purposes of the Act
- public money was made available to AOSMA in the form of a \$42 million loan from the Treasurer appropriated from the Consolidated Account.

The audit approach I have taken in addressing and reporting on the terms of reference is explained in sections 4 and 5.

2.4 Comment on the terms of reference

The terms of reference for the Auditor-General's supervision and reporting on the financial management of the Adelaide Oval redevelopment incorporate certain unique provisions.

Within the South Australian jurisdiction, public money may only be made available through an appropriation process, which provides Parliamentary authorisation for the application of money from the Consolidated Account. While it is a necessary first step, the appropriation process in itself does not make funds available to agencies. Money will only be available for expenditure by agencies when they draw down appropriation funding from the Consolidated Account. Both agencies and officers of the Department of Treasury and Finance (DTF) exercise some discretion in determining if, and when, appropriation funding is drawn down.

My capacity to respond to the requirements of the Act is supported by the provisions of the *Public Finance and Audit Act 1987* (PFAA) that empower me to require parties to provide information and explanations and obliges the parties to respond to my requests.

2.5 Approach to the review and preparing this Report

In preparing this Report, as required by section 9 of the Act, we sought to identify and review relevant documentation and other information.

Consistent with established audit practice, our review considered a sample of transactions and associated documentation and information. The matters addressed in this Report reflect our understanding of the documentation and other information we considered at the time of preparing it. Subsequent reviews build on the knowledge and understanding gained in preparing these Reports and following up the matters raised.

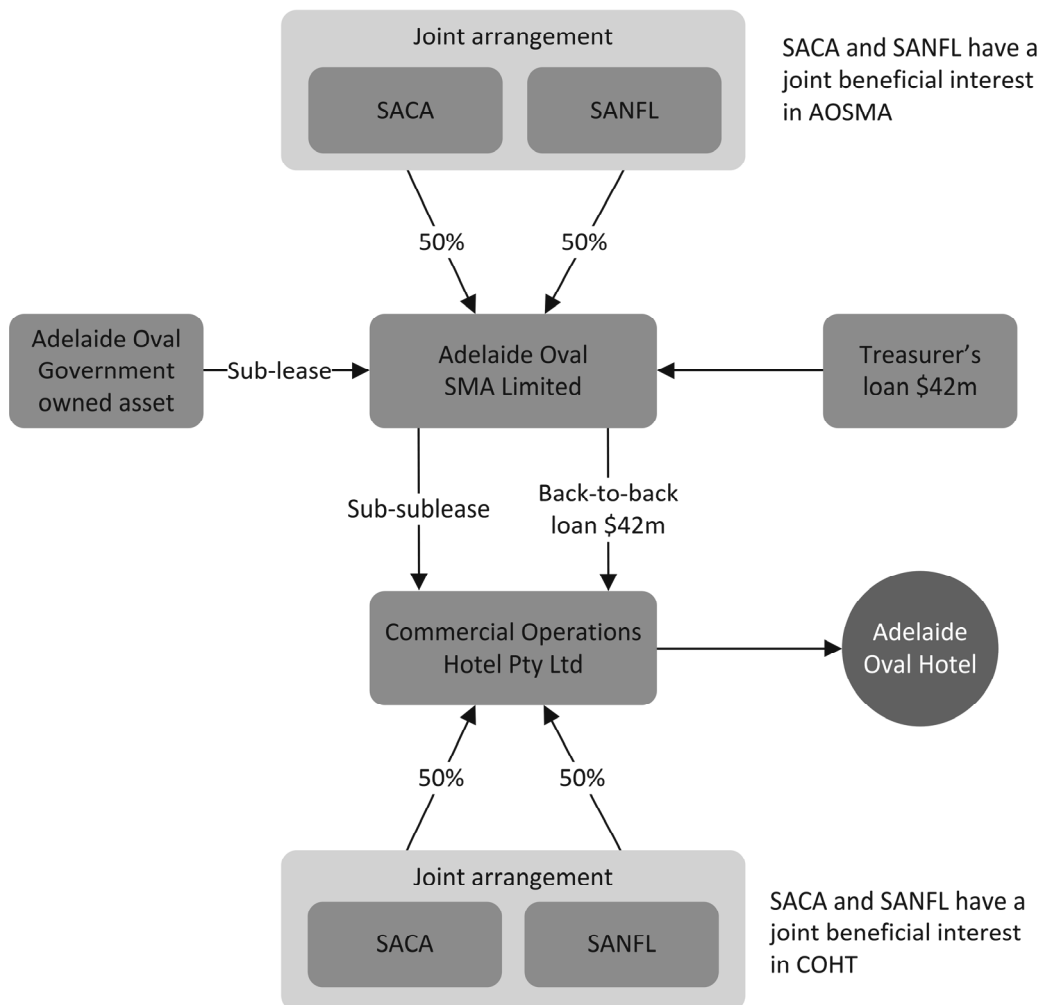
3 Adelaide Oval Hotel development

3.1 Background

In November 2018 AOSMA and the SA Government announced a project to construct a hotel at Adelaide Oval. The hotel is to be integrated into the eastern façade of Adelaide Oval and is being constructed through an arrangement between AOSMA and a separate trust company, the Commercial Operations Hotel Pty Ltd¹ (COHT). Through this arrangement the COHT will ultimately fund the construction of the hotel using funds loaned from AOSMA to COHT, and COHT will contract AOSMA to run the hotel operations.

Figure 3.1 provides an overview of the hotel development arrangements.

Figure 3.1: Adelaide Oval Hotel development arrangements



¹ The Commercial Operations Hotel Pty Ltd is trustee for the Commercial Operations Hotel Trust. (They were renamed the Adelaide Oval Hotel Pty Ltd and the Adelaide Oval Hotel Trust on 13 July 2020 and 1 July 2020 respectively.)

3.2 Loan provided to AOSMA to fund the hotel development

On 22 October 2018 the SA Government approved for the Treasurer to provide a loan to AOSMA to assist with construction of the hotel.

The loan was initiated after AOSMA made a proposal for financial assistance to the SA Government.

As part of the State's due diligence, SAFA assessed and provided advice on the proposal for financial assistance. SAFA advised us that this included reviewing AOSMA's business case, supporting analysis and due diligence, and the financial statements for AOSMA, the South Australian Cricket Association (SACA) and the South Australian National Football League (SANFL).

SAFA's assessment of the loan proposal noted the following:

- AOSMA asserts that the project has a critical timeline due to commitments to host the International Cricket Council T20 World Cup event in the latter half of 2020, which is driving the urgency to resolve financing for the project.
- AOSMA asserts that the project is necessary to remain competitive and support revenue streams into the future and is consistent with similar developments in stadiums internationally.
- According to AOSMA, commercial finance is problematic because it is restricted from offering a registered real property mortgage as security due to the hotel development being built on Crown land. SAFA observed that therefore the only security on the loan was the hotel business cash flows.
- The assets owned by SACA and the SANFL are limited.
- SACA, the SANFL and AOSMA are not proposing to contribute equity, with the full project cost being funded by the State through a loan.
- The project's financial model is based on a 4.5% financing cost.

SAFA's assessment concluded that it was not feasible for AOSMA to obtain commercial finance for the project due to a lack of equity contributions – a bank would typically lend 60% to 70% of the business value, with the remainder funded through equity. SAFA identified the preferred terms and structure of the loan if it was to be supported by the SA Government.

The Minister gave consent in a letter dated 30 June 2019 for AOSMA to undertake the Adelaide Oval Hotel development and grant a sub-sublease to COHT.

The loan agreement between the Treasurer and AOSMA was executed on 7 August 2019 and provides AOSMA with a loan facility of up to \$42 million to fund the hotel development.

Money was appropriated from the Consolidated Account to DTF Administered Items in the 2019-20 State Budget² to meet the loan drawdowns by AOSMA.

3.3 Status of the hotel development as at 30 June 2020

A construction contract was entered into between COHT and Built Environs Pty Ltd on 1 July 2019 for the construction of a 138-room hotel. Offsite construction started in July 2019, with major works construction beginning onsite in October 2019.

Design of the hotel is being overseen by COX Architecture and Mott MacDonald is the project manager for the hotel build. Mott Macdonald were also project managers for the initial redevelopment of the Adelaide Oval.

As at 30 June 2020 construction of the hotel was in progress. Progress reporting provided to SAFA by AOSMA, indicated:

- structural and roofing works were complete
- glazing was largely complete except for the reception pod, which was due to be completed in July
- façade cladding was progressing
- installation of acoustic flooring was generally completed in guest suites and was progressing in the corridors
- guest rooms were at various stages of completion – electrical, plumbing and interior fitout works were underway
- structural works for the reception pod were complete.

The hotel is expected to reach practical completion in September 2020 and commence operations from 25 September 2020.

The total project budget is \$45 million (excluding GST), \$42 million of which is being funded through a loan from the Treasurer and the rest by AOSMA.

3.4 Loan arrangements

3.4.1 Key features of the arrangements

The loan is for an amount up to \$42 million to AOSMA at a fixed interest rate of 4.5% per annum to fund the hotel development. The loan funds may only be used for specific purposes defined in the loan agreement.

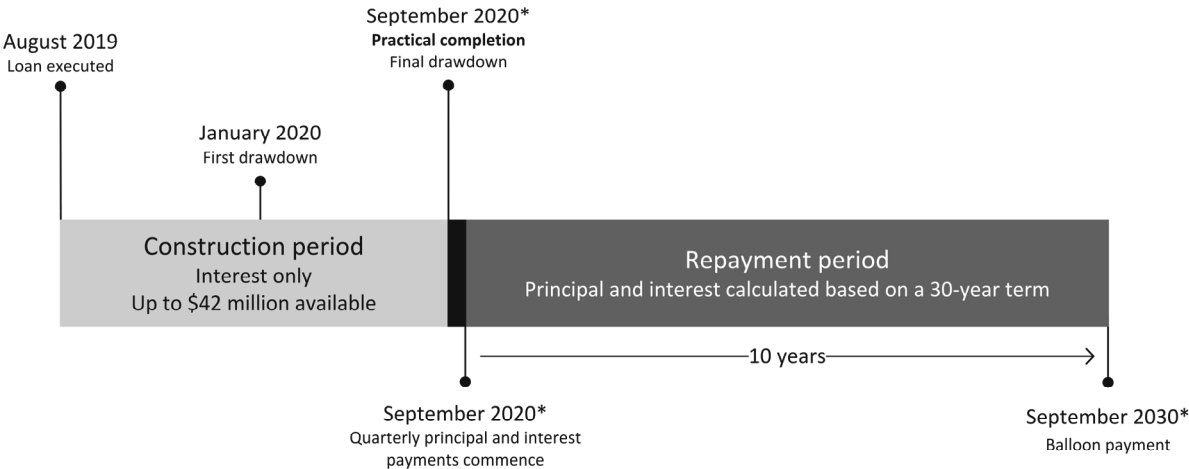
² 2019-20 State Budget Paper 4 *Agency Statements*, Volume 4, page 187.

Interest only repayments are required until construction reaches practical completion (ie for about nine months), after which quarterly principal and interest repayments commence. The loan is repayable in full 10 years from when practical completion is achieved, with a balloon payment at the end of the 10-year term.³

The loan agreement provides for the loan to be drawn down in instalments on the achievement of 11 agreed construction performance milestones. AOSMA is required to provide evidence to the Treasurer’s satisfaction that the performance milestones have been achieved prior to each advance.

Figure 3.2 summarises these arrangements.

Figure 3.2: Loan timeline



* Estimated dates based on hotel construction achieving practical completion in September 2020.

SACA and the SANFL are guarantors, limited to 50% of the loan amount capped at \$21 million each.

The loan is secured with:

- a second registered general security over AOSMA’s assets
- a first registered general security over COHT’s assets
- a first registered general security over SACA’s assets
- a second registered general security over the SANFL’s assets.

Section 5.3.1.2 provides an overview of SAFA’s assessment of the nature and limitations of the security arrangements.

The loan agreement appoints certain SAFA officers as Treasurer’s representatives to exercise certain powers and functions of the Treasurer under the Treasurer’s facility documents. Contract management staff from SAFA are responsible for ensuring that both the State and AOSMA comply with their obligations under the facility agreement.

³ The loan is a principal and interest loan with repayments calculated based on a loan amortising to \$0 over 30 years. A large payment, referred to as a balloon payment, is required at the end of year 10 to repay the loan in full.

3.4.2 Requests to vary the loan agreement

AOSMA wrote to the Treasurer on 20 March 2020 requesting a reduced interest rate due to the impact of the COVID-19 pandemic. This request was not approved by the Treasurer. Instead, the Treasurer approved that interest on the loan that would otherwise be payable during the construction period be deferred to 30 September 2020 and capitalised over the remaining life of the loan.⁴ SAFA advised us that the Treasurer has provided similar financial assistance to other borrowers with government loans experiencing financial difficulties due to COVID-19 and that these arrangements are similar to that being offered by commercial banks to businesses.

On 18 June 2020, AOSMA wrote to the Treasurer again seeking a reduction in the interest rate. This request was not approved by the Treasurer.

3.4.3 Cost of funds

The 2018-19 Mid-Year Budget Review⁵ indicates that there is no cost to the SA Government associated with providing the loan as the cost of interest being charged on the loan to AOSMA (fixed rate of 4.5% per annum) exceeds the SA Government's cost of borrowing those funds. In documentation provided to the Redevelopment of Adelaide Oval Select Committee, the Treasurer stated that the State's cost of funding was 3.2% at the time the loan was approved.

3.4.4 Status of loan

To 30 June 2020, the Treasurer had advanced \$28.8 million to AOSMA for six performance milestones that are linked to construction progress. Figure 3.3 sets out the date and amounts of each advance made.

Figure 3.3: Money advanced to AOSMA for the Adelaide Oval Hotel to 30 June 2020

Performance milestone	Date of advance	Amount advanced \$ million
Performance milestone 1	24 January 2020	7.4
Performance milestone 2	10 March 2020	3.8
Performance milestone 3	27 March 2020	4.1
Performance milestone 4	30 April 2020	4.9
Performance milestone 5	28 May 2020	4.0
Performance milestone 6	26 June 2020	4.6
Total advances to 30 June 2020		28.8

The closing balance of the loan at 30 June 2020 was \$28.8 million, with deferred interest charges of \$257 705 to be capitalised to the loan on 30 September 2020. Figure 3.4 sets out the loan status as at 30 June 2020.

⁴ The loan agreement provides the Treasurer with authority to capitalise interest on the loan.

⁵ 2018-19 Mid-Year Budget Review, Appendix A: Policy measures by agency, page 28.

Figure 3.4: Loan status at 30 June 2020

	\$ '000
Opening balance as at 1 January 2020	-
Money advanced to 30 June 2020	28 801
Interest on money advanced to 30 June 2020	42
Fees and charges on money advanced to 30 June 2020	-
<i>Less payments received to 30 June 2020:</i>	
Principal	-
Interest	42
Fees and charges	-
Total payments received to 30 June 2020	42
Closing balance as at 30 June 2020	28 801
Remaining loan funds available as at 30 June 2020	13 199
Deferred interest charges as at 30 June 2020	258
Amounts overdue as at 30 June 2020	-

As at 30 June 2020 there was \$13.2 million in loan funds available for drawdown. SAFA advised that based on current project reporting it expects the full amount to be drawn down by AOSMA. The final advance is to be made when practical completion is achieved, which according to reporting provided by AOSMA to SAFA is expected to occur in September 2020.

4 Term of reference two

4.1 Background

Section 9(1)(b) of the Act requires the Auditor-General to report on:

the state of the public accounts that are relevant to the redevelopment of Adelaide Oval envisaged by this Act.

This term of reference requires the Auditor-General to evaluate the state of the public accounts that are relevant to the Adelaide Oval redevelopment. The Act defines public accounts in the same terms as the PFAA:

public accounts means the Consolidated Account, special deposit accounts, deposit accounts, accounts of money deposited by the Treasurer with SAFA, imprest accounts and all other accounts shown in the general ledger.

In this context the general ledger is the Treasurer's ledger, which comprises accounts that summarise the financial transactions of the Treasurer.

I have understood the term 'state' to mean both the financial position and condition, circumstances or attributes of the public accounts. Specific matters considered in evaluating the state of the public accounts include whether the public accounts have been operated lawfully in line with the requirements of the PFAA and associated Treasurer's Instructions. I also considered whether the public accounts have been operated in a way that supports my reporting on the extent that money made available to any entity for the purposes of, or in connection with, the redevelopment of Adelaide Oval envisaged by this Act has been properly and efficiently managed and used.

4.2 Approach to evaluating the state of public accounts relevant to the Adelaide Oval redevelopment

We enquired with relevant agency staff to identify the accounts through which public money has been made available.

Having identified the public accounts relevant to redeveloping Adelaide Oval, we identified the financial systems, records and controls used by the agencies to process and control money made available in connection with the redevelopment (ie the design and construction of the Adelaide Oval Hotel). In evaluating the state of the public accounts we have considered whether the:

- purpose of the accounts, established under the PFAA, was consistent with their use to record and control money made available for the redevelopment
- detailed records supported both the agencies' effective management and control of the activity and public accountability required by the Act.

We also considered matters that were identified by ongoing audit of the agencies' financial systems and records and the impact of these matters on the assessment of the state of the public accounts required by the Act.

4.3 Findings for term of reference two

The financial activity associated with the Adelaide Oval redevelopment from 1 January 2020 to 30 June 2020 involved providing a loan to AOSMA to design and construct the hotel.

We confirmed that the public accounts relevant to the designated review period 1 January 2020 to 30 June 2020 were:

- the Consolidated Account
- special deposit account: Treasury and Finance Administered Items Account
- Treasurer's ledger account: Adelaide Oval SMA Treasurer's loans
- Treasurer's ledger account: Adelaide Oval SMA interest recoveries.

The public authorities responsible for operating these accounts are DTF and SAFA.

For term of reference two, on the basis of information obtained and reviewed to date, we found that the state of the public accounts that are relevant to the Adelaide Oval Hotel development was satisfactory.

4.3.1 Maintaining the Treasurer's ledger and SAFA's loans administration system

DTF's Financial Management, Reporting and Policy branch is responsible for the administration of Consolidated Account activities including operating and maintaining the Treasurer's ledger. These activities are performed by SAFA on behalf of the Financial Management, Reporting and Policy branch. We noted that a service level agreement documenting the roles and responsibilities for Consolidated Account services being provided by SAFA had not been finalised at 30 June 2020 due to delays caused by COVID-19. We reported this matter separately to DTF and SAFA who have advised this has now been signed.

SAFA is responsible for administering Adelaide Oval Hotel loan transactions through its loans administration system, which records all financial information associated with the loan including payments made to AOSMA, repayments received and interest charges. Information from the loans administration system is transferred to the Treasurer's ledger. As such SAFA is responsible for maintaining adequate records to support loan transactions.

Our enquiry and testing for the current designated reporting period confirmed that DTF and SAFA procedures ensured the loan provided to AOSMA was correctly established and recorded in the Treasurer's ledger.

5 Term of reference three

5.1 Background

Section 9(1)(c) of the Act requires the Auditor-General to report on:

the extent to which it appears that public money made available to any entity, including an entity that is not a public authority, for the purposes of, or in connection with, the redevelopment of Adelaide Oval envisaged by this Act has been properly and efficiently managed and used during the designated period.

5.1.1 Public money made available

Within the South Australian jurisdiction, public money may only be made available through an appropriation process, which provides Parliamentary authorisation for the application of money from the Consolidated Account. Money was appropriated from the Consolidated Account in the 2019-20 State Budget to meet the loan facility drawdowns by AOSMA. This money was managed through the Treasury and Finance Administered Items Account special deposit account.

5.1.2 Proper and efficient management and use of public money

This term of reference requires the Auditor-General to express an opinion on whether the management and use of public money by an entity for the purposes of, or in connection with, the Adelaide Oval redevelopment was proper and efficient.

In responding to this term of reference the term 'managed' is understood to mean the way money is handled, directed, governed or controlled and the term 'used' is understood to mean the way money is consumed or expended.

Whether money has been 'properly' managed and used requires an assessment of whether that management and use conforms to established standards of financial management practice and behaviour.

In the context of the Act, the established standards of practice and behaviour reflect:

- relevant authoritative documentation that is specific to this project, including SA Government approvals and contractual documentation
- authoritative regulations and guidelines such as the Treasurer's Instructions and Premier and Cabinet Circulars
- the context of the specific arrangements implemented by relevant entities
- generally accepted standards of financial management practice and behaviour.

Assessing whether money has been 'efficiently' managed and used requires an assessment of whether money was used to progress the Adelaide Oval Hotel development, including whether loan funds were:

- necessary to complete the project

- managed to enable the project to progress in line with required time frames and milestones.

5.2 Approach to evaluating whether the management and use of money for the Adelaide Oval redevelopment was proper and efficient

The Adelaide Oval Hotel development involves providing public money to AOSMA through a loan arrangement and the expenditure of the money on the construction activity. The money loaned to AOSMA is required to be repaid to the Treasurer in line with the loan agreement, as explained in section 3.

The parties and their responsibilities for the management and use of the public money are summarised in figure 3.5.

Figure 3.5: Key parties and responsibilities

Entity	Responsibility
DTF	Manage Consolidated Account activities
SAFA	Manage loan
Department for Infrastructure and Transport	Owner of State asset – Adelaide Oval Manage sublease to AOSMA for use of the Adelaide Oval core area
AOSMA	Manage, operate and maintain Adelaide Oval in line with the sublease
Commercial Operations Hotel Pty Ltd	Trustee for the Commercial Operations Hotel Trust Develop and manage the Adelaide Oval Hotel under lease and agreement with AOSMA

In responding to this term of reference, the entities identified and considered by us for review in preparing this report are DTF and SAFA. We looked at the controls these agencies used to address whether money is being used properly and efficiently.

For the designated reporting period that ended on 30 June 2020, our review of the proper and efficient use of money focused on reviewing the processes SAFA established to assess and manage the loan arrangement and ensure the obligations of AOSMA and the State are met. At 30 June 2020 AOSMA had drawn down \$28.8 million in loan funds.

Construction work on the project was still progressing at 30 June 2020. The project is expected to achieve practical completion in September 2020 during the next designated reporting period. We will report on construction activity, including an explanation of our audit coverage and scope, in our report for the designated reporting period ending 31 December 2020, which is due on 28 February 2021.

5.3 Findings for term of reference three

For term of reference three, on the basis of information obtained and reviewed to date, we have not identified anything for the current designated period that indicates the public money made available for the purpose of and in connection with providing loan funds for the Adelaide Oval Hotel development was not managed and used properly and efficiently.

We found that SAFA had established practices to manage the loan including:

- a procedure manual
- a purpose built contract management system to record and manage loan obligations
- a file management system to store records and easily access them.

Notwithstanding this, we noted areas for improvement and made some other observations.

5.3.1 Loan due diligence

5.3.1.1 No documentation maintained for not using the SAFA advised preferred interest rate

SAFA assessed AOSMA's proposal for financial assistance and provided advice on the loan arrangements to the SA Government. SAFA's assessment indicated a preference for the loan to be provided at a rate equivalent to a commercial rate of between 5% and 5.5% per annum if a loan was to be supported by the SA Government. We note that the loan was provided at a lower rate of 4.5% per annum.

We found that agency documentation was not maintained explaining the reasons for not using the commercial rate as advised by SAFA or analysing any potential risks introduced by adopting the lower lending rate.

For future proposal evaluations, we recommend the SA Government document the basis for not following specialist advice provided by agencies.

SAFA response

AOSMA sought loan financing from the State for the hotel on the basis of its project business case, which assumed a financing cost of 4.5% per annum. SAFA was asked to provide advice as to whether the project could be funded commercially. On 16 October 2018, SAFA provided that advice, which included that the hotel construction would be 100% debt financed by the State's loan. SAFA advised at that time that, in its view, it could not be funded commercially at 4.5% without an equity contribution in the order of at least 30%, and that a commercial rate would be more in the order of 5% – 5.5%. SAFA advised a preference for a commercial rate to be consistent with Accounting Standard AASB9 Financial Instruments should a loan be supported. However, SAFA noted that the project may not be commercially viable with a financing cost above 4.5%.

Following consideration of that advice by the Treasurer, SAFA was asked to advise the impact on the State budget, particularly the net operating balance, should the loan be provided at the concessional rate of 4.5%. This was also documented in an email from SAFA dated 16 October 2018.

5.3.1.2 Assessment of securities

SAFA's assessment of AOSMA's proposal observed the following limitations with the securities to be provided:

- the only security for the loan was the hotel business cash flows
- SACA and the SANFL own limited assets, with their only asset of significant value being the right to the Adelaide Oval licence.

SAFA's assessment also highlighted areas where further analysis of SACA's and the SANFL's financial performance was warranted to get a better picture of their ongoing performance.

SAFA provided three minutes to the Treasurer regarding the security for the loan.

We found however:

- documentation was not maintained to support how limitations with the adequacy of securities were to be addressed by the SA Government
- further analysis of SACA's and the SANFL's ongoing performance was not performed.

We recommend that for future loans that are not secured by a charge over real property or other assets, the SA Government should ensure agency documentation is maintained showing how risks associated with the adequacy of securities are addressed.

SAFA response

Following approval for the loan in October 2018, SAFA further considered the financial position of AOSMA, SACA and SANFL in the context of negotiating contractual terms. A significant focus of the negotiations was on the contractual provisions relating to permitted financial indebtedness and security in the context of the existing and forecast debt and equity requirements of these entities. The terms for the loan agreement and associated securities were negotiated over several months between SAFA (on behalf of the Treasurer), AOSMA, SACA and SANFL and their respective advisors, with those negotiations concluding in June 2019.

The contract negotiations are documented in SAFA's files, which record the matters discussed by way of meeting agendas and documented outcomes. Additionally, SAFA advised the Treasurer of material matters relating to permitted financial indebtedness and security in three formal minutes between November 2018 and July 2019, which documented the status of the negotiations, and SAFA's recommendations for best securing and protecting the value of the securities.

5.3.2 Loan administration

The Treasurer agreed to make the loan facility available to AOSMA subject to the terms of the loan agreement and relying on representations and warranties made by AOSMA.

The loan agreement requires AOSMA to provide a project certificate to the Treasurer at each drawdown, which evidences several elements including:

- the nature, stage and value of completed project works
- the completed project works are of a satisfactory standard and meet the requirements of the project documents
- all payments due to the builder and contractors engaged by COHT to complete the project including their subcontractors have been made.

The project certificate is a key document for SAFA to manage the loan advances. SAFA uses it to assess whether the relevant performance milestone was achieved and if certain other conditions precedent were met.

5.3.2.1 Project certificate requirements

Completion of works to a satisfactory standard

The loan agreement requires the borrower to provide a project certificate that evidences works are completed to a satisfactory standard and meet the requirements of the project documents.

The loan agreement also requires the content in the project certificate to be certified by a quantity surveyor. The specific wording in the loan agreement states:

The Treasurer being:

.... provided with a satisfactory Quantity Surveyor's certificate verifying the above matters and any other matters certified by the Borrower in the associated Project Certificate (as applicable).

The loan agreement does not define 'as applicable' and it is therefore unclear what this refers to. One interpretation could be the quantity surveyor needing to verify all matters in the project certificate. We found that the quantity surveyor did not verify all the elements in the project certificate but provided a report for each milestone that:

- certified the value of works complete and incomplete
- included a statement that the costs claimed by COHT were incurred on the project.

The report states the quantity surveyor does not provide expressed or implied warranty that the standard of work executed or quality of materials supplied are in accordance with the contract drawings, specifications, conditions or approvals. The report does include a certificate from:

- the builder's engineer that states works are in accordance with design requirements and contractual requirements

- the builder's architect that states works are in accordance with design requirements and contractual requirements.

We also note the above certificates may not cover all aspects of the standard of works or quality of materials (for example whether the finished works meet relevant building code standards and contain visual imperfections).

Payments made to builder, contractors and subcontractors

The project certificate also requires the borrower to certify that all payments due to the builder, contractors and subcontractors have been made.

We found the project certificate did not include this certification. SAFA advised that it is satisfied that this requirement is met by other representations and warranties provided by AOSMA and making a false representation or warranty will trigger a default event.

While AOSMA is required to make representations and warranties at each drawdown, we consider that the project certificate is an important mechanism that enables the Treasurer to:

- make an evidence-based assessment as to whether AOSMA complies with the loan agreement
- corroborate the accuracy of representations and warranties made before advancing funds to AOSMA.

Without a clearly worded certification that aligns to the loan agreement, there may be lack of clarity on:

- the accountabilities of the various parties providing representations
- what assurance the State is able to obtain from the representations/certifications provided.

AOSMA advised that it considered the certificates provided the necessary assurance via the architect and engineer. Notwithstanding this, AOSMA indicated that to add clarity and address the audit finding the quantity surveyor has adjusted the wording in its certificate for the most recent drawdown to indicate the architect and engineer have provided a Consultant's Certificate verifying the relevant design and contractual requirements.

AOSMA also noted that when the works are completed, further assurances from the architect and engineer will be sought on whether the finished works meet relevant building codes and visual standards. This will be further managed through the ongoing 12-month defect liability period.

We recommend that for future loans involving the construction of assets SAFA should:

- ensure the project certificate requirements are clearly documented in the loan agreement

- ensure the project certificate includes all elements required by the loan agreement and that all certifications are obtained
- review and update the content of the loan agreement to ensure the certification process meets the level of assurance required.

SAFA response

The loan agreement provides that at each drawdown a number of specific conditions are met including but not limited to:

- *the borrower (AOSMA) must provide a project certificate to the Treasurer (acting through his representative) that is to his satisfaction. The agreement is silent on who must prepare the certificate, and*
- *a quantity surveyor must verify matters in the project certificate as applicable.*

To meet its obligation to provide a project certificate for each drawdown, AOSMA submitted a report to SAFA which was prepared by the quantity surveyor (the SAFA Report). Included in the SAFA Report was the required verification from the quantity surveyor with regard to the nature and stage of the project then completed. Under the loan agreement, the quantity surveyor is not required to verify any other elements of the project certificate if they are not within the scope of its role as a quantity surveyor.

As required for the project certificate, the SAFA Report provided from AOSMA to SAFA evidences that the nature and stage of the completed works have been satisfactorily completed in accordance with, and meet the requirements of, the project documents. The certifications were provided by the parties best able to attest to the following matters for each drawdown:

- *the builder that the works the subject of the claim for payment and all prior claims for payment have been completed in accordance with the construction contract, and all subcontractors and workers have been paid all that is due*
- *the engineer who has inspected the project works and is satisfied that the works are in accordance with the design requirements and contractual requirements*
- *the architect who has inspected the project works and is satisfied that the works are in accordance with the design requirements and contractual requirements.*

To date, no material defects have been identified. At project completion, further evidence that the works have been completed to a satisfactory standard will be received through the certificate of practical completion.

SAFA notes that the project certificate prepared by the quantity surveyor did not include a statement that all payments then due to the builder and contractors engaged by COHT to complete the project have been made. SAFA relied on the borrower's representations and warranties repeated at each drawdown that the funds advanced will only be applied to the approved purpose, together with its obligations to comply with the project documents.

In addition, on 14 August 2020, AOSMA expressly certified to SAFA that all payments due to the builder and contractors engaged by AOSMA had been made.

SAFA received an appropriate level of assurance from the Borrower, the builder, its consultants and the quantity surveyor to advance the funds requested by AOSMA and assess that AOSMA was compliant with the loan agreement. Notwithstanding this, SAFA will consult with the Crown Solicitor's Office in relation to relevant clauses when drafting future loan agreements.

5.3.2.2 No regular review of the sufficiency of project funds for the entire project

We found that SAFA does not regularly review the sufficiency of funds to complete the entire project.

The loan agreement requires that prior to making each advance the Treasurer is satisfied that AOSMA has sufficient project funds to complete the project in line with the project documents.

It is important that the State obtains assurance that AOSMA has sufficient funds to not only complete construction of the project, but also to become operational in order to generate revenue and meet its loan repayment obligations.

The total project budget is \$45 million. While most of the project is being funded by the loan provided by the Treasurer, AOSMA is providing \$3 million of its own funds for furniture, fittings and equipment.

Although SAFA regularly reviews the sufficiency of funds to complete the construction component of the project, this review does not consider the sufficiency of funds for the entire project. We do note that SAFA reviewed the sufficiency of funds to complete the entire project in its early stages. This was a once-off review and financial circumstances may have changed, warranting another review.

We recommend that SAFA reviews AOSMA's ability to sufficiently fund the completion of the entire project before making each advance.

AOSMA advised it provided SAFA with evidence of its funding facilities for its operations and the hotel. It also advised that prior to the most recent drawdown it provided verification to SAFA that it had sufficient funds to complete the project in line with the project documents.

SAFA response

SAFA assessed AOSMA had the ability to fund completion of the project through the \$42 million loan facility, which provides 100% funding for the fixed price design and construct contract, as well as access to debt facilities to fund consulting costs associated with the project and furniture, fittings and equipment. SAFA obtained confirmation that the project was on schedule for completion prior to the date required under the loan agreement. When the

operations of AOSMA were impacted by COVID-19, SAFA supported deferring and capitalising interest through the construction period to protect AOSMA's cash available to meet ongoing expenses. AOSMA confirmed to SAFA in July and August 2020 that it has sufficient funding in place to fund the additional costs of the project, which is due to be completed in September 2020.

5.3.3 Governance

5.3.3.1 Oversight of hotel development risks

The loan agreement provides for specific reporting and project certification by AOSMA to the Treasurer to ensure proper management of the loan arrangement. SAFA has been delegated responsibility for administering the loan arrangement.

The hotel development will be integrated into the eastern façade of the Adelaide Oval, which is a government owned asset. Consequently, we consider that broader oversight of the risks and exposure to the State of the hotel development, outside of what is required under the loan arrangement, is warranted.

We noted during our review that oversight of the arrangement was limited to SAFA managing the loan facility obligations.

We recommend that DTF works with relevant SA Government stakeholders, including the Department for Infrastructure and Transport, to establish oversight and governance processes to manage asset ownership and management risks, including processes to:

- independently ensure the facility is built to standard
- maintain oversight over the hotel development
- manage the State's exposure if there are any issues with the hotel development that may impact the State as asset owner.

This should include:

- carrying out a risk assessment of these broader risks and creating the related risk management processes to identify and report on the risks and any proposed mitigating actions and responsibilities
- governance arrangements including key stakeholders (such as the Department for Infrastructure and Transport) and clearly defined responsibilities for ongoing oversight. We acknowledge that these arrangements should not duplicate the oversight arrangements over the loan facility.

SAFA response

SAFA has contacted the Department for Infrastructure and Transport to review how oversight of the Adelaide Oval assets will be managed going forward.

5.4 Future challenges

5.4.1 Ongoing impact of COVID-19 on AOSMA's financial position

The COVID-19 pandemic has impacted AOSMA's ability to hold events and significantly reduced its ability to earn income. The ongoing impact of COVID-19 on AOSMA's operating position is currently unknown due to the highly uncertain economic environment and may present a risk to it being able to fulfil its loan obligations.

AOSMA has written to the Treasurer on two occasions, in March 2020 and June 2020, seeking financial relief from its loan obligations. In this correspondence, AOSMA expressed concerns about its ability to earn income. It also noted that under the contractual arrangements in place for the Adelaide Oval, deficits it incurs are required to be covered by SACA and the SANFL, but given the financial impact of the pandemic their capacity to fund AOSMA's operations may be reduced.

Given the financial challenges facing AOSMA, SAFA should consider performing regular financial health checks on the loan arrangements including an assessment of:

- whether AOSMA is able to service its debt
- whether securities remain adequate to cover the loan amount in the event of default
- any other risk exposures to the State.

This would help to identify any specific issues and develop timely and appropriate responses to them.

5.4.2 Assurance that the asset is fit for purpose and free of major defects

We noted that the loan agreement requires AOSMA to provide quarterly information on major defects arising from the design and construction of the hotel. Up to 30 June 2020, AOSMA advised that no material defects were identified.

As construction nears completion, the State should consider developing processes to get independent assurance that the project is delivered without any major defects and is fit for purpose. In particular, the State should give focus to ensuring all identified defects impacting existing infrastructure owned by the State are satisfactorily rectified.

AOSMA advised that when the works are completed, assurances from the architect and engineer will be sought on whether the finished works meet relevant building code and visuals standards, as well as documenting defects. Further, defects will be managed through the ongoing 12-month defect liability period, with builder's insurance bonds held by the COHT.