

Report 6 of 2019

Annual report

for the year ended 30 June 2019

Part A: Executive summary



Report of the Auditor-General

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Auditor-General's Department

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30 September 2019

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President
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The Hon V A Tarzia MP
Speaker
House of Assembly
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Dear President and Speaker

**Report of the Auditor-General:
Report 6 of 2019 *Annual Report for the year ended 30 June 2019***

As required by the *Public Finance and Audit Act 1987*, I present to you my 2019 Annual Report.

Content of this Report

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

Part A: Executive summary contains this letter of transmittal, which provides the opinions I am required to give under section 36, and identifies any examinations I have made under section 32 of the *Public Finance and Audit Act 1987*. It also summarises the main matters that should, in my opinion, be brought to the attention of the Parliament and the SA Government from our 2018-19 audits of public sector agencies.

This includes significant financial outcomes, events and control matters communicated to agencies and small scale specific reviews.

Part B: Controls opinion now reports our approach to the controls opinion and the outcomes from our work.

Part C: Agency audit reports is a summary of the audit outcomes for each agency included in this Report. It has more detailed commentary on many of the matters in Part A and Part B. It features a snapshot of key agency information covering financial statistics, significant events and transactions, and whether the financial report opinion is unmodified or modified (qualified). If

modified, the key matters causing the modification are noted. The snapshot also lists the controls opinion findings and any other audit findings for each agency. It 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 significant financial transactions.

Agency financial reports not included in this Report

Not every public sector agency I am required to audit is included in this Report. Some audits are continuing at the time of preparation, and some I have used my discretion to exclude. I give priority to areas I assess as important enough to be published in this Report.

To strengthen accountability for the activities of these agencies I now also prepare a report to Parliament annually that provides a summary of the audit outcomes for the agencies not included in my Annual Report, with a particular focus on agencies with:

- a modified Independent Auditor's Report
- 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 expect this report will be completed in early 2020.

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

A list of the agencies not included in my Annual Report is provided in the Annexure to Part A.

Auditor-General's opinions

Section 36(1)(a) of the *Public Finance and Audit Act 1987* sets out three opinions I must state in my Annual Report. I deal with each of them in this section.

In my opinion, the Treasurer's statements reflect the financial transactions of the Treasurer as shown in the accounts and records of the Treasurer for the preceding financial year.

The Treasurer's statements for the year ended 30 June 2019 will be published on the Auditor-General's Department website after this Report is tabled in Parliament.

In my opinion, the financial statements of each public authority reflect the financial position of the authority at the end of the preceding financial year and the results of its operations and cash flows for that financial year.

I give this opinion for each of the public sector agencies included in this Report except the University of South Australia, for which I have issued a modified opinion.

In addition, without modifying my opinion on the financial reports of the Lifetime Support Authority and the Return to Work Corporation of South Australia, I drew attention to the inherent uncertainty in certain liabilities reported for those entities at 30 June 2019.

In all cases where a modified opinion is given, or I draw attention to something like an inherent uncertainty, the Independent Auditor's Report explains my reason(s). This is also explained in the commentary on each of those agencies in Part C of this Report.

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

My controls opinion is not modified. We did however identify several issues from the work we performed this year. These are, in my opinion, areas in need of significant improvement for the public sector agencies we reviewed to meet the standards of financial probity, propriety and process expected of them and, at all times, discharge their responsibilities within the letter and spirit of the law as instrumentalities of government discharging public functions.

Part B reports our approach to the controls opinion and the outcomes from our work. Part C explains any control opinion findings made at individual agencies.

Section 32 examinations

Section 36(1)(ab) of the *Public Finance and Audit Act 1987* requires me to report on any section 32 examinations that were completed during the year and briefly describe the outcome.

On 1 May 2017 the Treasurer requested that I examine the accounts of the District Council of Coober Pedy. The Report on this examination was provided to Parliament in December 2018.

A brief summary of the work we have undertaken in the local government sector is provided in section 7 of Part A.

Acknowledgments

I have great pleasure in recognising and thanking my professional and dedicated staff for their complete commitment and efforts in 2018-19. We introduced a new approach to and reporting for our controls opinion work this year. We are also continuing to change other aspects of how we complete our work for the Parliament. The high standard of their work and commitment to their responsibilities throughout the year, while contributing to our various change projects, is evidenced in the timely production and quality content of this and our other reports. The senior managers of the teams that have contributed to this work are listed in section 8 of Part A.

I am grateful for the professional services provided by contractors who have assisted with this year's audit program, and for the cooperation all public sector agencies gave to my staff.

I also extend my thanks to the Chief Executive of the Department of Treasury and Finance, Government Publishing SA and their staff for their part in producing this Report.

Yours sincerely

A handwritten signature in black ink that reads "Richardson". The signature is written in a cursive style with a long horizontal flourish extending to the right.

Andrew Richardson
Auditor-General

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1 Overview

Part A summarises the main matters that should, in my opinion, be brought to the attention of the Parliament and the SA Government in this Annual Report, except for our work for the controls opinion. Part B now reports our approach and the summary outcomes for our controls opinion work. Agency audit reports are now in Part C.

The Annual Report represents the principal part of our 2018-19 audits. Its content is designed to meet the annual reporting requirement in the *Public Finance and Audit Act 1987* (PFAA). The Annual Report also naturally follows in timing with the end of the financial year and reporting by the Treasurer and public authorities. This Part of the Report includes significant financial outcomes and events and small-scale specific reviews. We also deliver other reports on individual topics or themes throughout the year.

1.1 Introduction

When deciding our annual audit program, we are naturally looking to how we can best discharge our responsibilities to the Parliament. Our planning considers the settled and ongoing activities that make up the largest part of public sector operations, as well as new or changing activities.

We set our audit program at the start of each year to ensure we have the time needed to properly address all the work required to issue opinions. Most audit resources and effort are allocated to completing the financial statement and controls audits we are responsible for annually. While doing that work, we also complete performance audits and local government examinations.

As the first full year of a new government, many changes occurred in 2018-19 or were set to commence in 2019-20. The following sections give a snapshot of some of the significant public sector matters we considered as emerging risks in our audit planning for 2018-19. Most of them influenced our audit plans for the year and, where relevant, the work we performed is described in this Report. Notably some matters in progress, for example settling legal disputes, cannot be audited until an appropriate decision point is reached. Further, an annual report can only be part of our outcomes if we are to be timely and relevant. We will publish other reports, as outlined in section 1.2.

1.1.1 Governance changes

New governance arrangements were implemented in various agencies. Examples are the South Australian Housing Trust, now operating under a new governance structure and trading as the South Australian Housing Authority, and TAFE SA, with a new board and senior management including the chief executive appointed.

In Health, chairs of the new Local Health Network Governing Transition Boards commenced during the year. They worked with Health to prepare for when boards started operating on 1 July 2019.

1.1.2 Health budget risks

We have reported for several years that SA Health has not achieved budgets or saving targets that governments have set or has experienced other service demands, both of which have necessitated additional funding. The SA Government said in its 2018-19 State Budget that the sector does not deliver services as efficiently as is achieved in other States. It requires health networks to address inefficiencies in the health system over the next four years to reduce the cost of public health services to the national average by the end of 2021-22. The new local health network governing boards will be responsible for driving these reforms.

The Central Adelaide Local Health Network Incorporated (CALHN) was identified as having significant financial pressures. In 2018-19, the SA Government appointed KordaMentha to help develop a performance improvement plan.

1.1.3 Information technology and system changes

IT and systems are at the heart of public sector operations, as they are for most of the community directly or indirectly. Daily activities place an enormous reliance on IT and systems working, being secure and being accurate. Achieving these three things involves disciplined work by system owners and administrators and by users who affect the information going into and coming out of these systems. Across government there are multiple major systems in development. These projects have multi-million dollar budgets. Developing and implementing IT systems is well understood to be often complex and risky. Factors such as ever advancing technology, uncertainty, cost and the need to coordinate users and IT staff all contribute to this risk.

In 2018-19 we conducted selected control testing of key agency financial systems (Basware, Masterpiece, CommBiz, Chris21 and Health's Oracle Corporate System) and the controls over State taxation systems (RevenueSA's Revenue Information Online and RevenueSA Online systems) used to collect over \$3.6 billion in taxation revenue each year. In addition, we monitored the status of key IT system implementation projects. This included the end user computing program, the education management system and Health's electronic medical record program (previously known as the Enterprise Patient Administration System or EPAS).

1.1.4 Assets

Infrastructure assets are vital to delivering public services. This year we put concerted effort into reviewing various aspects of asset management, in response to the continuing large investment program and the need to maintain the existing more than \$50 billion asset base.

Key investment areas for new infrastructure include the Department of Planning, Transport and Infrastructure's (DPTI's) capital works in progress totalling \$1.7 billion. Education is also progressing plans to invest over \$1 billion between 2016 and 2020. In 2018-19 this included science, technology, engineering and maths facilities, improving, refurbishing and expanding capacity and moving year 7 students from primary to high school by January 2022.

The South Australian Housing Trust is progressing the Renewing Our Streets and Suburbs initiative to rejuvenate older Housing Trust homes and improve the supply of affordable housing for rent or purchase. This involves redeveloping more than 4500 homes, constructing 1000 new homes including 100 disability houses, and transferring property and tenancy management responsibilities for 5000 houses to community housing providers.

The Urban Renewal Authority (URA) is now developing Lot Fourteen, formerly the old Royal Adelaide Hospital (RAH) site. The SA Government's commitments for the site are specified in the Adelaide City Deal between the SA Government, Commonwealth Government and the Corporation of the City of Adelaide.

Multiple energy related investments are in progress including:

- the SA Water Zero Net Electricity Cost 2020 Project
- the \$100 million Home Battery Scheme to deliver battery system subsidies and loans to 40 000 households
- phase two of the Tesla virtual power plant where 1000 Housing Trust properties will have solar energy systems and batteries installed
- the purchase and leasing of nine temporary emergency generators
- implementation of the \$50 million Grid Scale Storage Fund.

1.1.5 Targeted voluntary separation payments

The 2018-19 State Budget included \$170 million for agencies to meet the cost of targeted voluntary separation packages (TVSPs) and/or separation payments to help them achieve their budget targets. From 1 July 2019, agencies became responsible for managing TVSPs and separation payments costs.

Many agencies settled TVSPs as at 30 June 2019.

1.1.6 Machinery of government changes

Machinery of government changes are a natural part of public sector arrangements. Major machinery of government changes took effect from 1 July 2018. Affected agencies included the Department of Human Services, Department for Industry and Skills, Department of the Premier and Cabinet, Department of Treasury and Finance, Department for Trade, Tourism and Investment, URA, South Australian Housing Trust and DPTI.

Two new activities introduced are the South Australian Productivity Commission and Infrastructure SA.

Changes of the scale seen in 2018-19 make trends in financial activity for individual agencies difficult to follow over the short term. We have explained the most significant changes affecting the agencies included in this Report.

The annual consolidated financial report produced by the Department of Treasury and Finance represents transactions between the South Australian public sector and external parties. It is unaffected by internal changes. It will be available later this year.

1.1.7 Service contracts

The State significantly relies on privately sourced resources to deliver public services. In 2018-19 some significant new arrangements were entered into or were being renegotiated.

Foremost of these were the service arrangements for the RAH. There were ongoing contractual disputes being worked through by SA Health about matters relating to both the build and operational arrangements. The SA Government announced an in principle agreement on 21 August 2019.

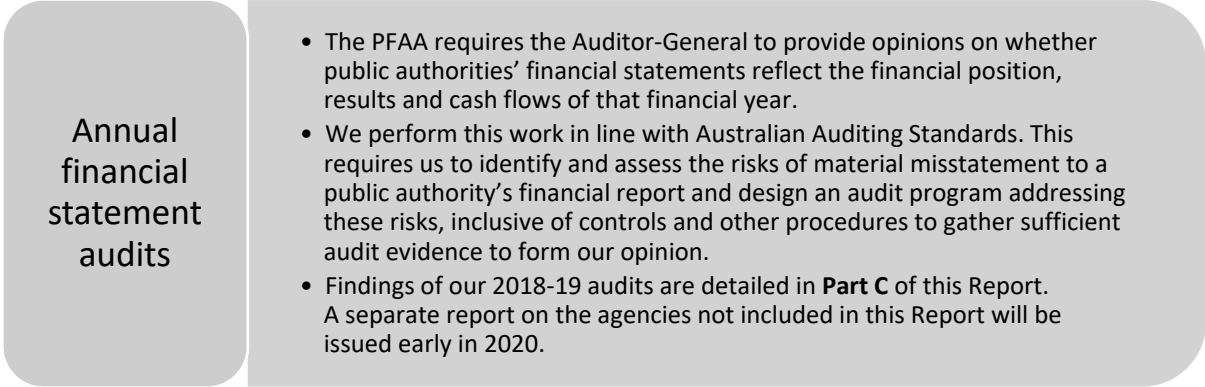
Other major contract arrangements include the contract to operate the Adelaide Remand Centre from August 2019 for seven years and the Motor Accident Commission’s outstanding claims being reinsured with the private sector.

1.2 What we do

Last year I reported changes in how we were going to do control opinion audits. I thought it important this year to give an overview of this audit work. I trust this will help to assure the Parliament of the breadth of our work for the Parliament and will explain why last year I said that our reporting changes would not result in reduced audit commentary.

We perform several types of audits annually to meet our responsibilities under the PFAA. We have summarised these reviews and where the outcomes will generally be reported in figure 1.1.

Figure 1.1: Our audits and how we report on them



Annual controls opinion audit

- The PFAA requires the Auditor-General to provide an opinion on whether the controls exercised by the Treasurer and public authorities 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.
- Annually we use the criteria reported in **Part B** of this Report to identify a program of work that informs the opinion. This criteria is based on quantitative and qualitative considerations across all public authorities we audit.
- Our 2018-19 program and significant outcomes are reported in **Part B** of this Report. Individual agency matters are then further detailed in Part C.

Performance audits

- The PFAA enables the Auditor-General to conduct performance audits which involve examining the efficiency, economy and effectiveness with which a public authority uses its resources.
- These are in-depth reviews performed with the objectives of contributing to public accountability and improvement in public sector governance.
- Each year we identify a range of topics for potential review and prioritise them based on criteria such as the significance and risk, potential benefits and impact, auditability and previous audit findings relating to the topic.
- Our performance audits are reported in individual Reports to Parliament throughout the year.

Local government examinations

- The PFAA enables the Auditor-General to conduct examinations of the accounts and activities of a publicly funded body, project or local government indemnity scheme.
- There is a broad scope and discretionary power of examination by the Auditor-General.
- Each year we identify a range of topics for potential review and prioritise them based on a set criteria such as the significance and risk, potential benefits and impact, auditability and previous audit findings relating to the topic.
- Our local government examinations are reported in individual Reports to Parliament throughout the year.

We also perform examinations at the request of the Treasurer or the Independent Commissioner Against Corruption.

1.2.1 Our new controls approach – how it has impacted our work

Our new controls opinion approach involves planning our program from a whole-of-government perspective. Our 2018-19 audit program and its outcomes are reported in Part B of this Report.

This audit program focuses our attention on controls over areas of importance across the whole of government based on the criteria explained in Part B. This means we can focus our resources on the areas we consider most significant.

Some of our findings in 2018-19 include the following:

- Asset management processes for across government facilities management arrangements (AGFMA) participating agencies need to improve in the areas of policies and plans, asset data collection and monitoring asset condition.
- The AGFMA is not operating as intended, with specific findings involving governance, asset condition monitoring, asset data collection and managing subcontractor qualifications.
- There are opportunities to improve asset management processes at non-AGFMA participating agencies.
- Performance management processes for staff need to be consolidated and improved.
- There were differing levels of workforce planning maturity across the agencies we reviewed.
- Some key payroll processing controls require improvement.
- There were several instances of non-compliance with State Procurement Board or agency policies and procedures for procurement and contract management.
- There are opportunities to improve procurement and contract management processes.
- There are opportunities to strengthen controls over delegations and approvals.

While this is a new approach it does not mean we have stopped looking at controls across all public authorities. We also review them through our financial report audits and performance audits.

1.2.1.1 Financial report audits

The PFAA requires the Auditor-General to provide opinions on whether public authorities' financial statements reflect the financial position, results and cash flows of that financial year.

To meet this mandate and our professional auditing obligations, we identify and assess the risk of material misstatement of a financial report.

To do this, we are interested in controls relevant to identifying and assessing the risks of material misstatement, whether due to fraud or error, in the financial report. Controls may provide a means for us when designing and implementing audit responses to our assessed risks of material misstatement.

As professional auditors, we are required to understand the agency and its environment, including its internal controls. We are also expected to take a controls reliance approach where possible to gathering sufficient and appropriate evidence to form our opinion. This is regarded as the most efficient and effective audit approach.

Auditors are required to understand internal controls relevant to the audit. Not all controls that relate to financial reporting are relevant to the audit. It is a matter of the auditor's professional judgement whether a control, individually or in combination with others, is relevant.

Indeed, we have found that many controls that are vital to whether a transaction is conducted properly and lawfully, may not affect whether or not the transaction is materially misstated in a financial report. This is a reason for revising our controls opinion approach.

Any findings we identify from our review of controls are communicated to the agency through a procedural fairness process which confirms the factual accuracy of the finding. The more significant findings from these audits and agency responses are detailed in Part C of this Report.

For those agencies not included in this Report a separate report will be issued early in 2020.

Common themes from our financial audit findings in 2018-19 include the following:

- Processes used to ensure user access to key systems could be improved.
- Policies and procedures were not always established, needed improvement or were, in some cases, out of date.
- There were opportunities to improve contract management practices.

Some of these are similar to the findings from our controls opinion work, detailed in Part B of this Report.

1.2.1.2 Performance audits

The PFAA enables the Auditor-General to undertake performance audits, which involve examining the efficiency, economy and effectiveness with which a public authority uses its resources.

These are in-depth reviews and may involve reviewing controls as part of a review of the performance of an activity, an IT system or other areas of importance identified at the discretion of the Auditor-General.

Any controls findings we identify from our performance audits are communicated to the agency through a procedural fairness process which confirms the factual accuracy of the finding. Our findings together with the agency's response are detailed in separate reports to Parliament throughout the year.

1.3 Audit outcomes in this Report

This Annual Report focuses on the agencies we assessed as the most significant this year. A further summary report will be tabled to address the remaining agencies so that each year we will account for our work on all agencies.

This section sets out the matters I wish to bring to the attention of Parliament and the SA Government

Section 2 summarises the more significant financial outcomes and events for individual agencies in 2018-19.

Our findings concerning internal controls we audited, are now summarised in a new Part B of this Report. We have again identified many areas where we consider controls should have been better and we report on them with the expectation that future practices will improve.

The details of our audit findings and comments for individual agencies are provided in Part C of this Report.

Section 3 summarises the significant machinery of government restructures that occurred in 2018-19.

Section 4 gives commentary and findings about several specific topics we chose to focus on in 2018-19:

- Health sector budget and performance
- Health governance and accountability changes
- procurement of KordaMentha services by the Department for Health and Wellbeing
- the Adelaide Festival Centre Precinct Upgrade.

Section 5 gives an update on how changes to accounting standards are being implemented. In 2018-19 further work was performed by agencies to prepare for or implement new Australian Accounting Standards. AASB 9 *Financial Instruments* applied for the first time in 2018-19. Standards that will impact the preparation of future financial reports are:

- AASB 16 *Leases*
- AASB 15 *Revenue from Contracts with Customers*
- AASB 1058 *Income of Not-for-Profit Entities*.

These have various implications for agencies across the public sector. We continue to urge all who have responsibilities to prepare financial reports to act early in the next year to resolve any challenges that arise. Historically, many complex accounting issues have presented challenges that have taken well into, or close to the end of, the financial reporting period to resolve. Both my office and agencies are unlikely to be able to manage multiple significant matters left too late in the financial year. We will not issue an audit opinion until material matters are resolved. Early work will mitigate this risk. My office is prepared and willing to assist as far as we can as auditors. It is each agency's responsibility to prepare accounts and decide how it applies accounting requirements.

Beyond this Annual Report, we also have individual performance audits and examinations in progress and will report on those as soon as the work is complete. They are:

- State finances and related matters
- information and communications technology reviews
- Country Health SA Hospital Sites maintenance
- Darlington Upgrade-Flinders Link
- the use of credit cards in local government.

1.4 Access to Cabinet records

The purpose of this section is to inform the Parliament about progress on the matter of accessing Cabinet documents.

The SA Government authorised a new policy on the disclosure of Cabinet documents to investigative agencies in March 2019. The policy provides for the Auditor-General to request access. Requests are subject to the approval of the Premier. The Auditor-General is not permitted access to the Cabinet Office or to costing comments attached to a Cabinet submission.

I subsequently made several requests for Cabinet submissions under the new policy. I received access to all the Cabinet submissions I requested.

I also requested Cabinet decision sets of the previous government for audits we performed this year. I received all the decision sets I requested in line with the previous government's policy.

I appreciate the work of staff of the Cabinet Office to implement processes for the policy to operate. I will continue to work with the Department of the Premier and Cabinet and the Cabinet Office to streamline the new process where possible, to ensure audits progress efficiently and effectively and to minimise costs across the public sector.

1.4.1 Why the Auditor-General seeks to access privileged information

I have been relating with the previous and current governments over the past three years about accessing government documents that are protected under various privileges. This started in September 2016 when the previous government introduced a new policy restricting access to Cabinet documents. Before this policy, confidential access to Cabinet submissions was available to the Auditor-General by request, a practice that had operated for decades. Past Annual Reports go into detail about how this matter progressed.

Parliament has charged the Auditor-General with the annual responsibility to report an opinion about whether the controls exercised by the Treasurer and public authorities over various financial transaction are sufficient to provide reasonable assurance that the financial transactions were conducted properly and in accordance with law. I am professionally bound to ensure I meet specific requirements before issuing an assurance opinion. I must obtain sufficient appropriate audit evidence to provide a basis for an audit opinion. What is sufficient is a matter of judgement and risk for the auditor. In the absence of information that is key to transaction decisions, the potential exists for a scope limitation in an audit because of inaccessibility to required evidence.

Cabinet is, by convention, the pre-eminent executive body of the State. By convention or administrative arrangements, such as Treasurer's Instructions,¹ Cabinet makes decisions authorising financial transactions.

Accordingly, giving an audit opinion on whether a transaction has been conducted properly and in accordance with law occasionally necessitates accessing evidence about what Cabinet has authorised and the information that informed its decision.

¹ An example for administrative arrangements is Treasurer's Instruction 8 *Financial Authorisations*.

1.4.2 New policy for disclosure of Cabinet documents to investigative agencies

After September 2016, we had significant problems accessing documentation from government agencies related to Cabinet submissions. Either we were denied documents because Cabinet records or agency staff were unclear if a document had immunity status or delays occurred while the status was resolved. This caused, at minimum, significant delay in completing audits. I have also reported instances of a scope limitation in an audit because we could not access the required evidence.

Because of this, in August 2018 I wrote to the Premier and to the Cabinet Office proposing a way forward.

In March 2019 the Premier advised me that Cabinet had authorised a new policy on the disclosure of Cabinet documents. The policy is set out in a new Department of the Premier and Cabinet Circular, PC047 *Disclosure of Cabinet documents to investigative agencies*.

PC047 provides for access to Cabinet documents of the current government for the Auditor-General as follows:

- 3.1. *Where the Auditor-General certifies that access to a Cabinet submission (including the attachments to a Cabinet submission) of the current government is required for the proper exercise of the Auditor-General's statutory functions, the Auditor-General may request the submission in writing from the Chief Executive of DPC.*
- 3.2. *Upon receiving a request under section 3.1, the Chief Executive of DPC will provide access to the Cabinet submission, subject to the approval of the Premier.*
- 3.3. *Notwithstanding the provisions of this circular, the Auditor-General is not permitted access to the Cabinet Office or costing comments attached to a Cabinet submission.*
- 3.4. *Access to a Cabinet submission (including any attachments) is provided to the Auditor-General subject to the following conditions:*
 - 3.4.1 *The Auditor-General must ensure that the document is stored securely and is distributed only to members of the Auditor-General's staff who require access to the document in order to assist the Auditor-General in the exercise of the Auditor-General's statutory functions*
 - 3.4.2 *In publishing a public report, the Auditor-General may only make reference in the report to a decision of Cabinet where such a reference is necessary for the proper exercise of the Auditor-General's statutory functions, and*
 - 3.4.3 *A reference to a Cabinet decision in a public report must be made in such a way as to not disclose any other information regarding the deliberations of Cabinet, including quoting from the document.*
- 3.5. *This section also applies to Cabinet documents of a former government of the same political persuasion as the current government.*

We have made several requests for Cabinet submissions and decisions under PC047 and have received all requests. I appreciate the efforts of staff of the Cabinet Office as we worked through clarifying protocols, managing uncertainties and streamlining access where appropriate. This policy and their assistance help to ensure audits can progress efficiently and effectively for the Parliament and to minimise costs across the public sector.

1.5 A protocol to confidentially access legally privileged information

This year we settled a protocol for seeking confidential access to legally privileged information.

The agreed protocol is a practical and efficient way to help me to perform my statutory functions for Parliament and maintain the SA Government's privilege.

We have requested access to advice of counsel under this protocol. We have received some, on the basis that privilege was not waived.

1.5.1 Why access to legally privileged information is an issue

Legal professional privilege protects confidential communications and documents between a lawyer and a client made for specific purposes, such as for the dominant purpose of giving or obtaining legal advice.

The privilege is the client's, not the lawyer's. The client can waive the privilege. Critically, the privilege can be lost or waived if the client does (or authorises) something that is inconsistent with the confidentiality the privilege is intended to protect.

The Auditor-General sometimes seeks access to information provided under legal privilege. The reason for access is again to meet Parliament's requirement for an annual opinion about whether financial transactions are conducted properly and lawfully.

Advice of counsel is a part of many transactions. For the Auditor-General to form an opinion, it is efficient and effective to be able to understand the legal advice received.

The Auditor-General can seek independent advice. I prefer not to do so unless there is sufficient cause. The better way, in my opinion, is to be able to review the counsel received when conducting audits. This immediately has context for the transaction being audited, saves further cost to taxpayers and, where the audit is satisfied, avoids the risk of different outcomes because of different instructions and interpretation.

As with Cabinet privilege, we have been seeking a protocol that both enables smooth performance of audit work and protects the privilege that recipients of counsel advice enjoy.

1.5.2 The protocol to confidentially access legally privileged information

This year we settled a protocol through the Crown Solicitor's Office.

Under the protocol, where the Auditor-General identifies that the SA Government has received legal advice on a matter that is subject to audit and assesses it is necessary to understand that advice for the proper exercise of the Auditor-General's statutory functions, the Auditor-General's authorised officers may request access to the advice directly from the relevant public authority. In seeking access, we will acknowledge that the agency is required to refer our request to the Crown Solicitor's Office to confirm whether the advice can be provided to us.

Any access granted is expressly conditional to ensure that legal privilege is maintained. We are advised that the advice is legally privileged, and the provision of the advice does not waive legal professional privilege. We understand that access will not be granted if the SA Government considers this will prejudice its interests.

Consistent with the position for accessing Cabinet documents under PC047, in publishing a public report I can only make reference in the report to advice from counsel where it is necessary for the proper exercise of my statutory functions, and any such reference must be made in a way that maintains privilege.

If we consider it necessary to publish more details, we will discuss this with the Crown Solicitor's Office in the course of the procedural fairness process.

1.6 The Auditor-General does not have powers to compel production of information that is subject to Cabinet and legal professional privilege

The powers given to the Auditor-General in conducting an audit or examination under the PFAA are a matter for the Parliament. To give the Auditor-General access to all confidential and privileged information relevant to performing audit functions, the PFAA would have to expressly and clearly state Parliament's intent that the Auditor-General has that access power.

Section 34 of the PFAA sets out the Auditor-General's powers to obtain information. Since the previous government's September 2016 policy, I have understood that these are general powers and do not empower me to compel information that is the subject of Cabinet and legal professional privilege. Accordingly, I have sought to establish practical protocols for access to be given on a confidential basis.

PC047 notes that the confidentiality of Cabinet deliberations is a fundamental principle of our system of government. Except where there is a legal power to compel the production of information on Cabinet's deliberations, the only body that may determine whether to disclose such information is Cabinet itself.

The new PC047 is working well. The protocol for accessing legally privileged advice gives a clearer and improved opportunity to gain access for audit purposes.

I do note that under the policy and protocols, access remains at the discretion of the government.

1.6.1 Access powers in some other jurisdictions

Given the responsibilities of the Auditor-General to Parliament, I respectfully offer the following observations about arrangements in the Commonwealth and Victoria. In those jurisdictions, the audit legislation provisions for information gathering powers do specifically provide for accessing information that is subject to either legal professional privilege, any other privilege or Cabinet confidentiality.

The provisions are subject to certain tests and limitations but not a general government discretion about providing access.

The Commonwealth *Auditor-General Act 1997*,² for example, provides that the power to obtain information is not limited by any rule of law relating to legal professional privilege, any other privilege or the public interest in relation to disclosing information or producing documents. It also provides that disclosure or production of, or access to, information or documents under the Act does not affect the operation of a rule of law relating to privilege or the public interest in relation to disclosure of the information or production of the document.

The Commonwealth *Auditor-General Act 1997*³ also specifically provides that sensitive information is not to be included in public reports including if, in the opinion of the Auditor-General, disclosing the information would be contrary to the public interest for prescribed reasons. One of the reasons is it would involve the disclosure of deliberations or decisions of the Cabinet or a Committee of the Cabinet.

Part 7 of the Victorian *Audit Act 1994* sets out the Auditor-General's information gathering powers and duties. The provisions include that a person may only comply with a request by the Auditor-General to provide information or a document that is subject to Cabinet confidentiality if the request is made for any of the prescribed audit purposes.⁴

1.7 Government outsourcing

Most governments have been successfully delivering services through outsourced private service providers for many years. It is a practical reality of providing access to sufficient, reliable and affordable public services. Outsourcing does generally commit governments to long-term contractual arrangements. Accordingly, making the right initial procurement decision and setting satisfactory contractual arrangements are critical to most successful arrangements.

² Part 5—Information-gathering powers and secrecy.

³ S37 Sensitive information not to be included in public reports.

⁴ S40(3) Secrecy and confidentiality

(a) a financial audit under Part 3;

(b) a performance audit under Part 4;

(c) an assurance review under Part 5;

(d) performing the Auditor-General's functions or powers under another Act where the other Act expressly authorises the provision of that information.

In 2018-19, the SA Government has entered into new or renegotiated outsourcing arrangements and announced market testing by releasing tenders to contract for the operation of public transport. It also has some long-standing arrangements.

My responsibility is to audit expenditure of public money and, where possible, to examine the degree of efficiency, economy and effectiveness with which public resources are used. When reporting to Parliament, there is a natural leaning to highlighting the downside risks of government activity. The public sector must always exercise appropriate processes to protect the public interest and meet the public's expectations of good practice. The public and taxpayers typically have a low tolerance for public sector inefficiency or failure.

Government remains responsible for delivering public services no matter how that occurs.

Last year, I reported about the Carillion experience in the United Kingdom. I did that to emphasise the risk inherent in outsourcing where the Executive do not directly control all aspects of how services are provided.

Whether through direct or outsourced arrangements, the public will quickly rely on the provision of public services and expect their availability. No matter how services are delivered, the government will be held responsible for satisfactory performance. An unsatisfied service seeker does not care how services are provided, just who is responsible and whether services will be available. Taxpayers and users of public services who do not have choice, do not expect to be exposed to unnecessary or unmanaged risks and stresses associated with public services.

Outsourcing involves two key activities:

- entering into transactions
- contract management.

I have made some comments on these two activities in the following sections. We have also reported on work we performed in 2018-19 in Part B and in Part C. Before doing so, I would like to emphasise an overriding matter for any outsourcing arrangement.

1.7.1 Responsibility cannot be delegated

Governments have been reminded that responsibility cannot be delegated many times as various contracting arrangement issues have arisen over many years.

The House of Commons Public Administration and Constitutional Affairs Committee Report I referred to last year stated in its conclusions and recommendations:

At different times, private, charitable and public providers have both succeeded and failed to contribute to successful public services. All the witnesses to our inquiry accepted that the public sector should buy in some goods or services from the private sector, and should insist on providing others internally. The public sector should not contract out the final decision making about policy. The public sector always retains responsibility for the entitlement of individuals to benefits or services. Whether ordinary services should be

outsourced though will depend upon the capacity of the public sector, private sector or voluntary sector to deliver them, the comparative cost, and ultimately, the value that each provider can produce.⁵

While entering into contracts will entitle the government to all the rights established by contractual arrangements, when issues arise the government will still be obliged to maintain services, while resolving the issues.

1.7.2 Entering into contracts

In 2018-19 the SA Government announced it was putting public transport services out to tender. Section 39 of the *Passenger Transport Act 1994* provides that if the Minister awards service contracts that are or are reasonably expected to be liable to make payments equal to or exceeding \$4 million over the term of the contract, the Minister must, within 28 days after awarding the contract, forward to the Auditor-General a copy of the contract and a report that describes the processes applied to the awarding of the contract.

The Auditor-General must, within four months of receiving this contract and report, examine the contract and prepare a report on the probity of the processes leading to the awarding of the contract.

Our work on the probity of the processes will start as soon as we receive the relevant information from the Minister.

In addition to the areas we are required to report on for transport contracts, there are areas I consider critical in processes leading up to the awarding of a contract. They reflect our experience and that of the UK with the Carillion experience and are:

- whether it is clear how and why the government decides whether to outsource a service
- that the government has a process to make decisions about how it should deliver services and always follows its own process
- whether evidence used to support these decisions is satisfactory, thin or non-existent
- that the government has developed a deep understanding of its commercial partners' supply chains and of the risks hidden behind their published accounts and public statements
- whether the government has completely analysed and understood risks and is ensuring that risk transfer is realistic and that quality, an appreciation of systemic risk and economic impact, as well as price, drives decision-making
- that the government has had regard to the successes and failures associated with the form of past contracts entered into with providers so as to establish sound, manageable and practical contractual arrangements.

⁵ House of Commons – Public Administration and Constitutional Affairs Committee 2018, *After Carillion: Public sector outsourcing and contracting*, Seventh Report of Session 2017–19, Parliament of the United Kingdom, 9 July 2018, p. 12.

In summary, we expect procurement processes to:

- minimise the likelihood of problems occurring later
- maximise the likelihood of achieving objectives
- improve the management of risk and its consequences.

A good process can mitigate the risks of:

- selecting an inappropriate or suboptimal delivery model (overlooking a model that would better meet project objectives or critical success factors)
- cost underestimation or optimism bias at the outset
- unforeseen risks materialising
- poor project management during delivery.⁶

1.7.3 Managing contracts

We have report on contract management annually through our financial and performance audits. Outcomes from our controls program work are provided in Part B of this Report.

I would like to take this opportunity to reflect on some of the findings we have made in recent years.

One overriding message is that active and timely contract management of outsourced arrangements is critical. With long-term arrangements where delivery of services is outsourced, the government must robustly and independently monitor the contract and the delivery of services. This is because the government outsources the services but not its responsibilities.

The contract management arrangements should ideally be established at the beginning of the contract term. Contract management arrangements need to be more than general oversight and receiving information from the service provider.

Some key elements we believe should be in place at the start of any outsourced arrangements or shortly after are as follows:

Audit clauses

We have found that contracts often provide for self-reporting by the service provider on performance against key performance indicators (KPIs) and service levels and the functioning of systems and controls. For the SA Government to get assurance on these areas it is not enough to rely on self-reporting.

⁶ Department of Infrastructure and Regional Development 2008, *National Public Private Partnership Guidelines, Volume 1: Procurement Options Analysis*, Commonwealth of Australia, Canberra, p 2.

The contracts we reviewed give the SA Government broad rights to access and audit the service provider's records for any aspect of the transaction documents. It is important that it exercises these contractual audit rights regularly and effectively. This means establishing a risk-based audit program that covers elements such as the effectiveness and reliability of:

- service provider systems and controls established to meet the requirements of the contractual arrangements
- service level reporting/performance reporting. This is especially important as it will form the basis of any abatements/performance rebates under the contract.

In setting up the audit program there also needs to be clarity about the scope, coverage and resourcing of audits to be performed under contractual audit provisions.

Compliance management

Formal compliance management frameworks are required to effectively identify and monitor:

- the timely supply of contract deliverables by the service provider
- the State's obligations under the contract.

The frameworks should outline the nature and timing of compliance and monitoring activities for contract deliverables, as well as specifying the officers responsible for the activities, and should be in place from the start of the service delivery contract.

These are often not in place at the beginning of the contract and are not up to date or actively used to monitor the contract.

Risk management

We have found there is often a need to establish up-to-date risk registers reflecting ongoing contract management risks and how they will be managed (often through the compliance program). These registers were often not in place or incomplete at the beginning of a contract for delivery of services.

Risk registers that existed prior to the outsourcing of the activity need to be updated to reflect the new arrangements and different risk profile.

We have also found that contract risks and proposed mitigation strategies were not being reported to governance committees.

Transition planning

Often with outsourced arrangements, the services need to be transitioned from in-house to the service provider. A detailed transition plan clarifies the nature, timing, responsibilities and cost of transition activities and should be in place as close as possible to the start of services being provided by the contractor. This is critical if there is a transition period where government still has some involvement and there are cost sharing arrangements.

Contingency planning in an outsourced environment

In an environment where the provision of services is outsourced over multiple decades (for example, the RAH: 35 years, land services functions: 40 years) it is important to have a formal and comprehensive contingency plan/framework to address continuity of service risks.

Contracts will often have a range of clauses contemplating this scenario (step-in rights, financier responsibilities to cure/step in) but this is not enough in itself to outline the risks the State faces and the strategies for how it will address these risks if they eventuate. Contingency planning should consider the full legal, operational and financial options.

The State is ultimately responsible for delivering public services. As a result, it should have contingency plans that outline the strategies and interim measures it can put into place to ensure the continuation of vital services if the service provider fails to provide the contracted services.

1.8 Retention and access to documentation

We have continued to find agency documentation or recordkeeping that was not to the standard needed for good public administration. Parts B and C of this Report explain where we have made this assessment.

In my opinion, there remains a significant need to improve recordkeeping in government activities. Documentation needs to be appropriate for the matter at hand and need not involve excessive effort. The benefits of improving existing practices include:

- giving clear guidance to public servants about the policies and procedures they are expected to follow
- providing sufficient and reliable records to:
 - support decision-makers and evidence the decisions they make
 - evidence all critical internal and external interactions to support the integrity of procurement processes
 - support procurement management.

Consideration should also be given to whether existing training for staff involved in recordkeeping is adequate and provides enough information about policies and procedures and records management and retention requirements and how they can be satisfied most efficiently and effectively.

Last year I noted that legislation and instructions support this principle in many ways. For example, the *Public Sector Act 2009* requires public sector employees to deal with agency information in line with the law and agency requirements. Treasurer's Instructions state that chief executives of public authorities must maintain documentation that substantiates the existence or occurrence, completeness, valuation or allocation, passing of control, rights

and/or obligations relating to expenditure activities. The PFAA requires a public authority's financial statements to be accompanied by a certificate of compliance with the requirement for the statements to be in line with its accounts and records.

1.9 Productivity Commission inquiry into government procurement

The South Australian Productivity Commission (SAPC) has reported the first stage of a two-stage inquiry into government procurement.

The SA Government has accepted the recommendations in that report.

Our role as auditors is to give annual opinions about whether controls are in place to reasonably assure that transactions are conducted properly and lawfully. We assess the design, implementation and application of controls. We will adapt our future audit processes to the relevant guidelines as they evolve through the work of the SAPC or other changes the government introduces. I briefly describe some of the SAPC's report here to highlight some of the matters we will consider in the future.

We will also have regard to the procurement objectives set out in section 3 of the *State Procurement Act 2004*:

- obtaining value in the expenditure of public money
- providing for ethical and fair treatment of participants
- ensuring probity, accountability and transparency in procurement operations.

In doing so, we are mindful that the procurement approach taken should be commensurate with the risks and benefits inherent in the procurement.

The SAPC was established in October 2018. It provides the SA Government with independent advice on facilitating productivity growth, unlocking new economic opportunities, supporting job creation and removing existing regulatory barriers.

The SA Government issues terms of reference to the SAPC to evaluate the effectiveness and efficiency of its policies and practices for procuring goods and services (not including capital projects) and identify reform options to improve them and to improve the impact of procurement on local industry output and employment.

The SAPC's report on the first stage of its inquiry addresses government procurement for the purchase of goods and services other than by prescribed agencies or for construction. The second stage will complete the examination of the full procurement system and address some system-level matters including the architecture of the system, institutional arrangements and some matters especially pertinent to construction.

The SAPC reported that it considers the SA Government's procurement system is prescriptive, unnecessarily risk averse, and lacks transparency and guidance in key areas.

The SAPC considers that the system has limited capacity to drive whole-of-government procurement with authority, accountability and human resources. In summary it noted that:

- there is insufficient policy clarity in some key areas including value for money, market engagement and probity
- the procurement system can be streamlined and simplified to cut costs for participants while increasing the efficiency and effectiveness of procurement
- better value outcomes seem likely if public authorities generally increase their knowledge of and appropriate engagement with the marketplace, including local suppliers.

The report proposes some improvement foundations including:

- adopting the principle that, in general and unless otherwise determined, procurement decisions should only be authorised once
- reforming system-level procurement reporting and central data collection to enable comparative analysis and identification of improvements
- developing procurement capability.

Procurement practice is the basis for controlling about a third of government recurrent spending. Seeking ways to continually improve it offers considerable benefits, even for small improvements in practice.

1.10 Public sector liabilities are rising partly from falling interest rates

A large proportion of the State's financial liabilities are employment and insurance obligations. They are valued by annual estimation processes for financial reporting. Those processes all involve estimating when and what value of financial payments will be made over the time it takes to fully pay out the liability. Some liabilities, mainly insurance claims, and employee benefits including superannuation and long service leave, involve many payments over many years. The estimated payments are then discounted by prevailing interest rates to take account of the time value of money and produce an estimated value now.

As is well known, interest rates continued to fall in 2018-19. As they fall, the effect on estimating liabilities is that the values rise. Because interest rates are so low, the value of liabilities reported are at very high levels. Critically, there is no change in the underlying liability.

In 2018-19, all financial liabilities estimated in this way rose, in some cases substantially, because of the discounting effect. To illustrate the significance, RTWSA estimated that as at 30 June 2019, a further 1% decrease in the real discount rate would lead to an increase in its net outstanding claims provision of \$431 million. For employee obligations, the 2019-20 State Budget reported a rise for 2018-19 in the unfunded superannuation liability of \$2.1 billion. The long service leave liability, in the Health sector, about one third of the public sector employees, rose by \$143 million, mainly due to the lower discount rate.

Notably, lower interest rates can also mean lower interest expense on borrowings financing the public sector. For example, under the contractual arrangements for the RAH, the State received the benefit of being able to renegotiate its finance commitments. This has resulted in annual savings of many millions of dollars.

1.11 Insurance

The SA Government operates significant insurance activities for workers and accident victims and self-insures some of these activities. The main agencies involved are the Return to Work Corporation of South Australia (RTWSA), Lifetime Support Authority of South Australia and the South Australian Government Financing Authority's (SAFA's) insurance division, SAicorp. Each year, the value of outstanding insurance claims is estimated to provide the basis for deciding fee and investment strategies and to make other decisions. Uncertainty in this estimate continues to affect RTWSA and the Lifetime Support Authority of South Australia because of the relative newness of their insurance arrangements. Despite this uncertainty, the estimation approach is designed to be sufficiently reliable to estimate the value of the liabilities.

1.12 Agencies included in this 2018-19 Annual Report

In this Annual Report I have included agencies that met our criteria for selecting agencies to include in. Unless an agency exceeds specific quantitative and qualitative criteria, I will not include it in my Annual Report. Qualitative guidance includes:

- the significance of an agency's financial and operational activity to the State's public finances
- the significance of issues arising from the annual audit
- significant parliamentary visibility and public profile
- emerging financial risks
- large asset or liability acquisitions or disposals
- the implementation of significant new IT systems.

This is an assessment I make annually.

The financial statements of all agencies will be available on the Auditor-General's Department website (www.audit.sa.gov.au) as soon as audits are completed.

1.13 Public finances

1.13.1 Estimated result for 2018-19 is higher than budgeted

The 2019-20 State Budget estimated result for 2018-19 is a net operating surplus of \$101 million. This compares to a \$48 million surplus in the 2018-19 State Budget and \$40 million surplus in the 2018-19 mid-year budget review.

The \$53 million improvement compared to the original budget is mainly due to Commonwealth national partnership infrastructure grant funding of \$738 million being brought forward to 2018-19, offset by:

- a once-off grant payment of \$602 million to the South Australian Housing Trust to restructure its operations and support its viability
- downward revisions to GST revenue.

Figure 1.2 sets out the key budget information and outcomes for the general government sector for the three years to 2019-20.

Figure 1.2: Key budget information and outcomes for the general government sector

	2017-18 Result \$'million	2018-19 Budget \$'million	2018-19 Estimated result \$'million	2019-20 Budget \$'million
Net operating balance	(313)	48	101	94
Net lending	(977)	(866)	(579)	(1 069)
Net debt	5 447	6 288	6 289	9 468
Net worth	43 085	44 591	42 017	41 675
Revenue and expenses:	%	%	%	%
Revenue real growth	2.3	(0.3)	3.7	(2.5)
Expenses real growth	6.6	(2.5)	1.5	(2.5)
Net debt to revenue ratio	28.2	32.1	30.9	46.9

The net lending estimated result for 2018-19 is a deficit of \$579 million compared to the originally budgeted deficit of \$866 million. The \$287 million improvement in net lending from budget was mainly due to purchases of non-financial assets being \$393 million lower than budgeted and the net operating surplus being \$53 million higher than budgeted, offset partly by sales of non-financial assets being \$158 million lower than budgeted.

Net debt is expected to increase significantly by \$3.179 billion (51%) in 2019-20 to \$9.468 billion, primarily to fund the SA Government's investing program and as a result of accounting standard changes outlined in section 1.13.2.

Auditor-General's Report 8 of 2019 *State finances and related matters* will provide further details on the 2018-19 estimated result and trends in net lending and net debt over the four years of the Budget.

1.13.2 Accounting standards and budget presentation changes

The following new accounting standards issued by the Australian Accounting Standards Board have been applied for the first time in the 2019-20 Budget:

- AASB 15 *Revenue from Contracts with Customers*
- AASB 1058 *Income of Not-for-Profit Entities*
- AASB 16 *Leases*.

These new standards are effective from 1 July 2019 and do not apply to the 2018-19 estimated results.

The new revenue standards aim to align when revenue is recognised more closely with the timing of related expenditure. Under the transition arrangements, \$850 million in grant revenue for certain obligations has been recognised in the 2018-19 estimated result or prior years, as well as in the four years of the Budget.

The new leases standard requires certain leases that were previously classified as operating lease commitments to be recognised on the balance sheet from 2019-20, resulting in a substantial increase in net debt on 1 July 2019 (\$1.2 billion). This increase is a reporting change rather than an actual deterioration in the State's financial position relating to new borrowing activity.

In addition to the new accounting standards, presentation changes were applied from 2019-20 to achieve full compliance with the Uniform Presentation Framework for budget reporting. The impacts largely relate to certain assets no longer being offset by related liabilities (eg Treasurer's deposits and borrowings with/from SAFA), and certain revenues no longer being offset by related expenses (eg interest revenues and expenses). The Budget indicates that these budget presentation changes have no net impact on key budget indicators.

Auditor-General's Report 8 of 2019 *State finances and related matters* will provide further details on the impact of the new accounting standards and budget presentation changes on the four years of the Budget.

1.13.3 Treasurer's statements for 2018-19

The Treasurer's statements reflect the financial transactions of the Treasurer as shown in the accounts and records of the Treasurer. The main public accounts are the Consolidated Account, special deposit accounts and deposit accounts established under the PFAA.

The Consolidated Account is credited with all revenue of the Crown that is not authorised by law to be credited to any other account. Money must not be issued or applied from the Consolidated Account except under the authority of Parliamentary appropriation. There is significant financial activity outside of the Consolidated Account in approved special deposit accounts and deposit accounts.

The Consolidated Account result for 2018-19 was a deficit of \$2 billion, \$216 million higher than the budgeted deficit of \$1.789 billion. The higher deficit was mainly due to higher expenditure, with total payments \$207 million higher than budgeted. Total receipts were also marginally lower than budgeted (by \$9 million).

Total payments from the Consolidated Account of \$14.808 billion were within appropriation authority of \$15.019 billion (refer Statement K of the Treasurer's statements).

The balance of funds on hand in special deposit accounts (\$7.657 billion) and deposit accounts (\$2.057 billion) collectively increased by \$1.921 billion. The largest contributor to

the increased deposit account balances was an increase of \$754 million in the Intergovernmental Agreement on Federal Financial Relations account, reflecting funding related to DPTI projects not yet passed on to and spent by DPTI. The Highways Fund also increased by \$294 million in 2018-19, partly due to the receipt of \$143 million from the Motor Accident Commission surplus assets.

The SA Government's indebtedness to SAFA increased to \$13 billion in 2018-19 from \$11 billion. This was mainly due to the \$2 billion Consolidated Account deficit for 2018-19.

The Treasurer's statements are available on the Auditor-General's Department website (www.audit.sa.gov.au) and a summary of key items is provided in section 8 of this Report.

2 Significant financial outcomes and events in 2018-19

2.1 Key findings

The key findings in this section are as follows:

- Return to Work Corporation of South Australia (RTWSA) – outstanding claims liability was \$3.2 billion and inherent uncertainty associated with the Return to Work Scheme remains high.
- Motor Accident Commission (MAC) – made a payment of \$143 million to the Highways Fund.
- Lifetime Support Authority of South Australia (LSA) – Lifetime Support Scheme participants and liabilities continued to increase and inherent uncertainty associated with the Scheme remains high.
- South Australian Water Corporation (SA Water) – profit increased due to higher water sales. The 2019-20 Budget noted that SA Water would maintain a debt to asset ratio of at least 45% over the forward estimates.
- Urban Renewal Authority (URA) – recorded a loss before income tax equivalent in 2018-19 of \$206 million.
- South Australian Housing Trust (SAHT) – was re-established with a new governance structure.
- Actual Health expenses were more than the original 2018-19 budget by \$478 million while total actual income exceeded budget by \$73 million, leading to an overall deterioration of \$405 million against the original budget.

Commentary is also provided on several other matters.

2.2 Insurance agencies

2.2.1 Return to Work Corporation of South Australia liabilities increased

The *Return to Work Act 2014* came into full operation on 1 July 2015. The legislative changes to entitlements, coupled with RTWSA's initiatives to get claimants back to work more promptly, have had a significant impact on the Return to Work Scheme (RTW Scheme).

The outstanding claims liability increased to \$3.2 billion

The liability for outstanding claims as at 30 June 2019 was \$3.2 billion, an increase of \$486 million from the previous year. The RTW Scheme actuary's projections are reviewed by an independent professional actuary engaged by the Auditor-General. Our audit did not identify any issues or variations from expected practice that required the estimate for 30 June 2019 to be adjusted in any material way.

Risk margin reduced

The estimate of outstanding claims liability for the Compensation Fund is determined by reference to a 75% probability that the provision for outstanding claims will be adequate. The risk margin included in the provision decreased to 14% (15%) which added an additional \$389 million to the provision as at 30 June 2019.

Inherent uncertainty associated with the new RTW Scheme remains high

There is still inherent uncertainty associated with the new RTW Scheme arrangements, which may impact the liability for outstanding claims. In particular, the independent actuary noted the uncertainty regarding serious injury claims and the importance of maintaining the robustness of the Whole Person Impairment assessments that are the gateway to lifetime benefits for serious injury claims. The outcome of any legal challenges was also noted as potentially impacting the RTW Scheme. I included an emphasis of matter in RTWSA's unmodified financial report opinion, drawing attention to the uncertainty associated with the outstanding claims liability reported as at 30 June 2019.

The actuarial estimation is primarily based on the anticipated impact of the new legislation. If the RTW Scheme does not operate as intended, the cost implications may be significant.

The RTW Scheme continues to be fully funded

RTWSA had a net asset position as at 30 June 2019 of \$374 million and a funding ratio of 111.5%, which means that the RTW Scheme continues to be fully funded. The average premium rate in 2018-19 was 1.7%, a 0.1% decrease from the 2017-18 rate of 1.8%. The average premium rate for 2019-20 has been set at 1.65%.

The total comprehensive result for 2017-18 was a loss of \$153 million

In 2018-19 the underwriting result was a loss of \$378 million, after the net liability for outstanding claims increased by \$486 million and premium income decreased by \$11 million. Net investment profit increased by \$52 million to \$284 million. Other operating expenses remained steady at \$59 million.

2.2.2 Motor Accident Commission reinsured its remaining outstanding claims and distributed \$143 million

MAC reinsured its remaining outstanding claims

In December 2018 MAC entered into a reinsurance arrangement with the National Indemnity Corporation (NICO), a subsidiary of Berkshire Hathaway. Under the contract, NICO assumed responsibility for settling and managing MAC's remaining outstanding claims liability at 1 January 2019, which had a value of \$756 million. MAC will compensate NICO for assuming this responsibility with payments of \$718 million consisting of:

- a \$418 million initial payment
- a \$200 million balance that will be held by MAC and used to pay NICO for claims as they settle. It is currently expected that the remainder of the \$200 million will be paid in 2019-20

- a \$100 million final payment, initially retained by MAC for five years and used to support local fund managers.

In addition, MAC will pay NICO \$13 million in interest as a result of retaining the \$100 million for five years.

On 1 January 2019 the payment from MAC to NICO represented a gain of \$38 million, being the difference between the estimated value of outstanding claims, \$756 million, and the amounts MAC will pay NICO, \$718 million. The \$38 million gain will be recognised as income over the life of the arrangement at a rate consistent with the reduction in the outstanding claims liability.

This reinsurance arrangement reduces the State's risk as the cost of settling claims now lies with NICO. The reinsurance arrangement is designed to provide certainty to the State, subject only to satisfactory contract performance by NICO. Under the arrangement, if claims settle for more than the amount estimated at 1 January 2019 the additional cost will be borne by NICO. In the same way, should NICO be able to settle claims more favourably than expected in the January 2019 valuation, it will benefit from the reduced cost.

As the contract with NICO is a reinsurance arrangement, meaning that claims are still in MAC's name, the outstanding claims will remain on MAC's statement of financial position until they are extinguished, with an offsetting reinsurance receivable. Therefore MAC will need to maintain oversight over the outstanding claims liability to ensure claims are being managed and settled appropriately by NICO.

MAC paid \$143 million to the Highways Fund in 2018-19

In June 2019 MAC paid \$143 million to the Highways Fund. This payment was made out of net assets in excess of the level required for sufficient solvency of the MAC Fund. The Treasurer directed that, consistent with section 26(2) of the *Motor Accident Commission Act 1992*, the payment be made to the Highways Fund, which is administered by DPTI.

The \$143 million payment brings the total capital returned by MAC to \$2.5 billion over the last five years.

2.2.3 Lifetime Support Scheme is growing and liabilities are sensitive to change

The LSA administers the Lifetime Support Scheme and Fund for people who suffer very serious injuries in motor vehicle accidents. The Lifetime Support Scheme commenced operation on 1 July 2014 and 2018-19 is its fifth full year of operation. It is mainly funded by a levy on South Australian motor vehicle registrations.

Lifetime Support Scheme is growing

The Lifetime Support Scheme is growing, with the total number of participants increasing from 166 in 2017-18 to 209 in 2018-19. The related estimated future cost of caring for current participants increased by \$104 million to \$502 million.

LSA made an operating surplus of \$58 million

The LSA's operating surplus for 2018-19 was \$58 million. The levy raised during the year of \$156 million was sufficient to cover operating expenses. Expenses included \$18 million in direct expenses for participant care and a \$104.2 million increase in the provision for the estimated future costs of caring for current participants.

Lifetime Support Scheme is fully funded

The LSA had net assets of \$257 million, which means the Lifetime Support Scheme is fully funded as at 30 June 2019.

Significant uncertainty around provision for future treatment, care and support costs

The value of the provision for participant treatment, care and support is pivotal to the financial position and operating outcome of the LSA. The Board of the LSA determined the value of the provision after considering a report from an independent actuary. The role of the actuary is critical to estimating the provision liability, and the LSA engaged a reviewing actuary to provide additional comfort about the sufficiency of the amount provided.

The Lifetime Support Scheme is not an insurance scheme. Consistent with similar interstate schemes, the LSA determined the provision in line with relevant accounting requirements and did not apply a risk margin to its central estimate of liabilities.

The liability estimate is measured as the present value of the expected future payments for claims incurred up to 30 June 2019, including claims incurred but not yet reported. Sensitivity analysis illustrates that relatively small changes to key assumptions in the estimate can result in changes in the order of millions of dollars.

Given the limited participants' experience to date and the long-term nature of the claims, there is still significant uncertainty surrounding the estimate of the provision for participant treatment, care and support services. An emphasis of matter was included in LSA's financial report opinion drawing attention to this uncertainty.

2.3 Other statutory corporations

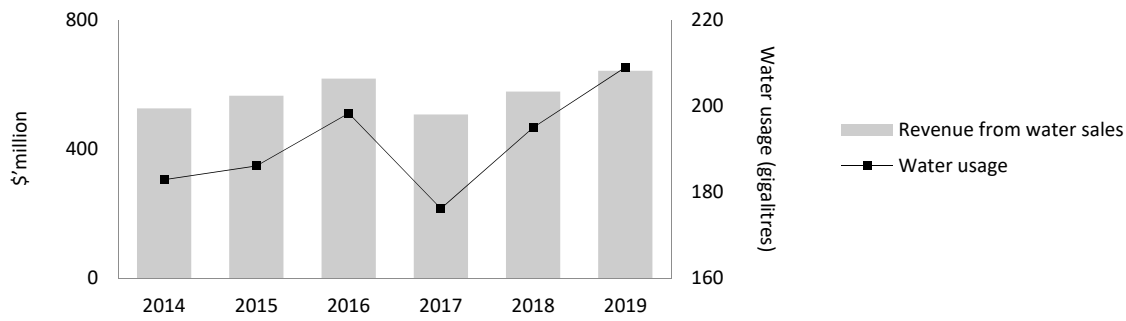
2.3.1 South Australian Water Corporation's profit increased following higher water sales

SA Water recorded a profit before income tax of \$272 million

SA Water's profit before income tax of \$272 million represents a \$70 million (35%) increase from the prior year. This increase was mainly driven by a 14 gigalitre increase in the volume of water sold and a 1.9% increase in rates charged for residential use.

Figure 2.1 shows water usage and revenue from water sales over the last six years.

Figure 2.1: Water usage and revenue from water sales



There was a further \$11 million increase in revenue from higher water pricing this year, reflecting the impact of the regulatory pricing decision.

SA Water’s debt to asset ratio increased to 45.9%

The 2019-20 State Budget noted that SA Water would maintain a debt to asset ratio of at least 45% over the forward estimates, in line with its interstate peers. Figure 2.2 highlights the relative debt to asset gearing ratios of a sample of water corporations from around Australia, as at 30 June 2018.

Figure 2.2: Debt to asset gearing ratios around Australia

	SA Water	Sydney Water	Water Corporation of Western Australia	Yarra Valley Water	Unitywater
Total debt (\$'billion)	6.708	8.189	6.141	2.414	1.558
Total assets (\$'billion)	14.666	19.093	17.490	4.966	3.778
Gearing ratio (%)	46	43	35	49	41

Figure 2.2 shows that SA Water’s revised gearing ratio is similar to those of Sydney Water, Yarra Valley Water in Victoria and Unitywater in Queensland.

SA Water’s cash contributions to the State Budget remain strong

In May 2019 the SA Government determined that all government business are required to pay a dividend ratio of 100% of after tax profit each year from 2018-19 onwards.

In 2018-19 SA Water paid dividends totalling \$179 million and income tax equivalents totalling \$100 million. It received \$140 million in community service obligation funding, leading to a net contribution for 2018-19 of \$139 million. Figure 2.3 shows SA Water’s net cash contributions to the SA Government over the last five years.

Figure 2.3: Net cash contributions to the SA Government

	2014-15 \$'million	2015-16 \$'million	2016-17 \$'million	2017-18 \$'million	2018-19 \$'million
Net cash contributions	165	182	140	71	139

Under the *Water Industry Act 2012* the Treasurer has issued a number of pricing orders since September 2012. They have specified that the Essential Services Commission of South Australia (ESCOSA) is to determine the revenue (not price) that may be derived from the provision of drinking water and sewerage retail services (separately). The next regulatory period (SAW RD20) begins on 1 July 2020. ESCOSA has started its process to inform SAW RD20.

In the 2018 State Election the government announced that it would establish an independent inquiry into water pricing in South Australia. The inquiry's *Abridged Advice – Final Report of the SA Inquiry into Water Prices* was released in July 2019. It covers a range of issues including the valuation of SA Water's Regulatory Asset Base, which ESCOSA considers when making its revenue determinations. The SA Government is currently considering the report and is yet to announce any changes to the Regulatory Asset Base. Any change will likely impact on the level of revenue SA Water can recover.

2.3.2 Urban Renewal Authority's financial performance deteriorates following a change in funding method

URA records a loss before income tax of \$206 million

The URA recorded a loss before income tax equivalent in 2018-19 of \$206 million, a \$227 million deterioration from its 2017-18 result. The loss was driven by a \$220 million net decrease in the value of inventory and investment properties. This amount includes the recognition of a \$100 million provision for future development expenditure (liability) to estimate the URA's obligations arising from the SA Government's commitments to develop the Lot Fourteen site.

The decrease in inventory asset values was due mainly to the removal of SA Government funding from the discounted cash flow models used by the URA to measure its development projects (inventory), following the Treasurer's decision to provide SA Government capital project funding as an equity contribution.

The value of land inventory is measured using cash flow models that estimate the net realisable value of development projects. This modelling estimates the likely outcomes of the URA's business strategies for these projects based on forecast market conditions. Accounting standards do not allow equity contributions to be included in these cash flow models.

Any future changes to market conditions, SA Government or URA policy or business strategies can also impact future inventory values.

TAFE SA properties to be transferred back to the general government sector

The URA holds significant investment properties valued at \$707 million, including TAFE SA properties purchased from the former Department of State Development in March 2017. In the 2019-20 State Budget, the SA Government announced the transfer of a number of TAFE SA properties back to the general government sector in 2019-20 for \$601 million.

URA employees transfer to South Australian Housing Trust

As a result of the SA Government's new governance arrangements for the SAHT, 165 URA employees transferred to the SAHT.

2.3.3 The South Australian Housing Trust was re-established with a new governance structure

The Board appoints a Chief Executive and staff are transferred from DHS and URA

The Minister for Human Services established a new governance structure for the SAHT. Previously it had no Chief Executive and no employees and depended on the Department of Human Service (DHS) and the URA to deliver services on its behalf.

In 2018-19 a new SAHT Board and Chief Executive were appointed, and a total of 1038 staff transferred from DHS and the URA.

Responsibility for paying grants to specialist homelessness service providers transferred on 1 July 2018 from DHS.

SAHT received funding of \$949 million

The SA Government provided the SAHT with recurrent funding of \$825 million and an equity contribution of \$124 million. Recurrent funding included additional once-off funding to restructure its operations, which now include homelessness, and support its viability.

According to the 2019-20 State Budget the SAHT will receive further equity contributions totalling \$778 million between 2019-20 and 2022-23, but will receive minimal recurrent grants over this period, meaning large annual operating deficits are expected.

Net cost of services increased to \$382 million

The SAHT recorded a net cost of providing services of \$382 million, a \$104 million increase from 2017-18. The increase mainly reflects a \$71 million increase in grant expenses, largely from grant payments to specialist homelessness service providers, and a \$64 million decrease in Commonwealth funding. Commonwealth base funding provided under the National Affordable Housing Agreement is now transferred to the SAHT by the SA Government as an equity contribution, whereas in 2017-18 funding of this nature was transferred as a grant.

These movements were partially offset by a \$31 million increase in the net gain from the disposal of assets, reflecting the volume of activity within the SAHT's financial viability strategy and housing renewal program.

2.3.4 Adelaide Festival Centre Trust major capital works

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 2018-19. The construction work resulted in the closure of the car park and restricted access to the Dunstan Playhouse, Space Theatre and footbridge. Redevelopment work on the Festival Plaza is to be carried out from 2020 to 2022.

The SA Government provided supplementation funding of \$1.1 million during the year to replace the loss of car park revenue.

Redevelopment of Her Majesty’s Theatre

The redevelopment of Her Majesty’s Theatre commenced in April 2018 when the theatre closed. The redevelopment will expand the existing auditorium as well as improve front-of-house amenities and technical facilities. The estimated total capital cost of the project is \$66 million and construction is expected to be completed in early 2020.

The project will primarily be funded by a \$62 million loan from SAFA and \$3 million from fundraising by the Adelaide Festival Centre Trust Foundation. During the year \$20.5 million of loan funding was drawn down.

2.3.5 Environment Protection Authority waste levy income increased

Solid waste levies increased

Income from fees and charges (controlled and administered) totalled \$88 million for 2019, an increase of \$3.6 million from the previous year. This increase is largely driven by an increase in waste levies, which totalled \$70.5 million (\$67.2 million).

Waste levies include solid waste levies from waste depots. Solid waste levy rates increased by 15% from 1 July 2018.

Increase in waste levy rates offsetting a decrease in the volume of solid waste collected

Figure 2.4 shows the amounts collected from waste levies over the past five years. It is based on data provided by the Environment Protection Authority.

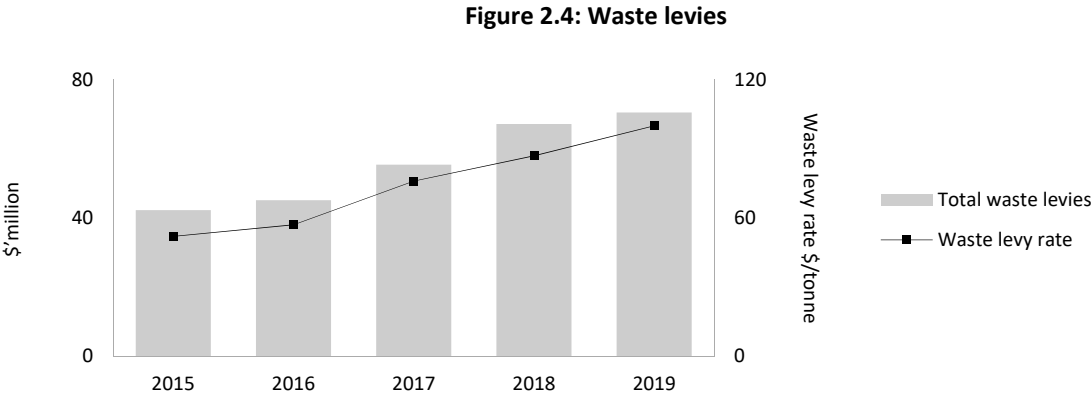
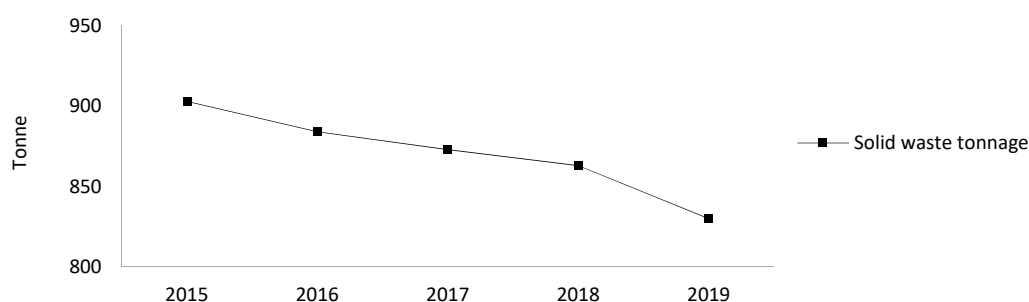


Figure 2.5 shows the downward trend in solid waste tonnage over the same period.

Figure 2.5: Solid waste tonnage



The figures demonstrate how increases in waste levy rates have offset decreases in the volume of solid waste collected over the period.

The balance of the Green Industries Fund continued to increase

The balance of the Green Industries Fund at 30 June 2019 was \$131.8 million (\$120.3 million).

The Environment Protection Authority transfers 50% of solid waste levies collected from waste depot licence holders to the Green Industries Fund.

The Green Industries Fund is controlled by Green Industries SA, a statutory authority established under the *Green Industries Act 2004*. Green Industries SA must apply the Fund in line with an annual business plan approved by the Minister for Sustainability, Environment and Conservation, or in any other manner authorised by the Minister for the purposes of the *Green Industries Act 2004*.

Under changes to the *Green Industries Act 2004* assented to in 2016-17, the Minister may also apply the Green Industries Fund towards the costs of climate change initiatives, or the costs of managing waste or debris or harm to the environment following an identified major incident, major emergency or disaster declared under the *Emergency Management Act 2004*.

In June 2019 the Minister approved the expenditure of \$155.6 million across the four years to 2021-22 from the Green Industries Fund. Most of this expenditure (96%) will fund the Home Battery Scheme and Grid Scale Storage Fund initiatives being delivered by the Department of Energy and Mining.

Green Industries SA advised that the Fund will have an estimated balance of \$21.3 million by 30 June 2022.

2.3.6 HomeStart Finance's graduate loans continue to increase

Graduate loans have increased by \$330 million since 2015-16

HomeStart Finance's total gross loans and advances increased by \$142 million to \$2.2 billion in 2018-19. This was due mainly to a \$155 million increase in graduate loans, partially offset by a decrease in variable loans of \$13 million.

Graduate loans have increased by \$330 million since 2015-16 reflecting changes in HomeStart Finance's lending criteria for these loans in 2015. The changes allowed students with a TAFE SA certificate III qualification to be eligible for a graduate loan.

Overall coverage for loan impairment remains consistent

HomeStart Finance's specific and collective provisions for impairment totalled \$18.6 million at 30 June 2019. It also has a general reserve for credit losses, which decreased by \$800 000 this year. In total, coverage for loan impairment increased slightly from \$25.6 million in 2017-18 to \$25.9 million in 2018-19, representing about 1.22% of gross loans and advances.

Loan portfolio is concentrated in some geographic areas

Due to the nature of HomeStart Finance's customer base, it has a greater concentration of loans in some geographic areas. 33% of loans by value are within the City of Playford and City of Salisbury, while a further 22% of loans by value are located outside of metropolitan Adelaide.

2.3.7 South Australian Government Financing Authority

Loan assets increased by \$2.4 billion

SAFA is the central borrowing authority for the State, and is responsible for managing most of the State's debt and for implementing debt policy as determined by the Treasurer. As at 30 June 2019 SAFA had loan assets of \$24.3 billion predominantly made up of:

- loans to the Treasurer – \$13.7 billion
- loans to public non-financial corporations – \$8.6 billion
- loans to public financial corporations – \$1.9 billion.

South Australia's participation in the National Redress Scheme for Institutional Child Sexual Abuse commenced in February 2019

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 SAFA's insurance division, SAicorp, to administer all payments associated with this. On 6 June 2018 the Premier signed an Intergovernmental Agreement confirming South Australia's participation.

The start date for the Scheme was 1 February 2019 and it will accept applications until 30 June 2027.

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. Any funds not paid under the Scheme will be returned to the Victims of Crime Fund following closure of the Scheme.

The Scheme is administered by SAFA through a separate insurance fund. As at 30 June 2019 the outstanding claims liability for this fund was \$136.7 million. The liability was calculated by an external actuary.

While the current estimate of claims is below the level of funding provided, the estimate is subject to change because the Scheme is open until 2027.

There were 95 Scheme applications as at 30 June 2019.

As at 30 June 2019 no redress payments had been made.

2.3.8 South Australian Superannuation Board (SASB)

SASB completed the first phase of implementing its new superannuation management system for three major superannuation schemes and decided not to proceed with the second phase

SASB implemented a new superannuation management system for three of the main superannuation schemes it administers in May 2018. The three schemes were the Southern State Superannuation Scheme, the Super SA Retirement Investment Fund and Super SA Select.

SASB formally closed the first phase of the project in December 2018 following additional work to address software functionality issues and a conclusion that the core functionality of the system had been delivered by the vendor.

As a result of delays in implementing the first phase, and the software functionality issues encountered, SASB decided not to proceed with the second phase of the project. The remaining schemes – the South Australian Superannuation Scheme, South Australian Ambulance Service Superannuation Scheme, Parliamentary Superannuation Scheme, Judges' Pensions Scheme and Governors' Pensions Scheme – will continue to be administered on the existing legacy platforms.

The total implementation cost of the project as at 31 December 2018 was \$23.5 million, including capitalised software costs and project implementation costs.

2.4 Health

2.4.1 Department for Health and Wellbeing

Consolidated net deficit result exceeded the original budget

The consolidated net result for the Department for Health and Wellbeing (DHW), the local health networks (LHNs) and SA Ambulance Service Inc (SAAS), collectively SA Health, exceeded the original 2018-19 budget by \$297 million. Actual expenses were more than the original 2018-19 budget by \$478 million, while total actual income exceeded budget by \$73 million, leading to an overall deterioration of \$405 million against the original budget. The SA Government also contributed \$107 million more than the original budget.

Provision for insurance increases to \$131 million

DHW's provision for insurance, which estimates the liability for professional indemnity including medical malpractice and general public liability, increased by \$12 million to

\$131 million. This provision is impacted by a range of factors considered by an actuarial assessment including prudential margins, inflation, taxes and claim numbers.

Governance changes from 1 July 2019

From 1 July 2019 amendments to the *Health Care Act 2008* provide for LHNs to be governed by boards. The amendments also change the role of the Chief Executive, DHW from 1 July 2019 to remove direct responsibility for administering LHNs.

Governing boards were established on and commenced from 1 July 2019. The board chairs and members were appointed by the Minister for Health and Wellbeing. The chairs and members were initially appointed in an advisory capacity during the transition in 2018-19 under the *Constitution Act 1934* to enable and support their induction and familiarisation.

Governing boards of LHNs are responsible for addressing the local need, providing strategic direction and monitoring their LHN's operating and financial performance. The boards must comply with any direction of the Minister for Health and Wellbeing or Chief Executive, DHW.

Under these changes DHW remains responsible for setting State-wide policy and the Minister for Health and Wellbeing remains responsible for setting reform agendas and priorities.

To support devolving governance and responsibility for delivering public health services to new LHN governing boards, the SA Government and DHW are making significant changes to SA Health's governance and accountability frameworks. The details of these changed arrangements are discussed in section 4.2.

Associated with the revised arrangements SA Health made changes to its organisation structure, including transferring some staff and responsibilities to Shared Services SA from 1 July 2019. DHW is also considering which functions should be devolved from DHW to LHNs. The process for realigning employees is ongoing, with some expected to occur in 2019-20 and others deferred until later years.

At the time of this Report a second round of legislative amendments, the Health Care (Governance) (No 2) Amendment Bill 2019, was being debated in Parliament. It proposes provisions relating to the service agreements for LHNs as a key element of the performance framework, as well as provisions relating to the function and role of the Chief Executive, DHW.

2.4.2 Central Adelaide Local Health Network Incorporated (CALHN)

KordaMentha appointed to assist in a financial recovery for CALHN

SA Health appointed KordaMentha to help oversee a financial recovery program for CALHN. The program aims to improve:

- clinical performance – reducing emergency department and elective wait times, length of stay and clinical complications
- financial performance – removing a \$264 million deficit over three years and meeting national efficient price targets for service provision.

In 2018-19, KordaMentha conducted work across a range of areas at CALHN. This included working with CALHN management to understand current operational issues in these areas and develop plans for improvement. KordaMentha staff have also been involved in reviewing procurement across CALHN, with financial delegations reduced for most procurement and purchase requests reviewed.

SA Health is in the process of assessing outcomes from this process and have not formally decided whether to extend KordaMentha's contract beyond the initial 25 November 2019 end date.

In-principle agreement reached between the SA Government, Spotless and Celsus in relation to the delivery of services at the RAH

The State's public private partnership arrangement for the RAH is with Celsus. Celsus, in turn, contracted Spotless to deliver a range of operational services under the arrangement.

On 5 June 2018, Spotless issued Celsus with three Notices of Dispute under the contractual arrangements relating to operational matters. On the same day, Celsus issued corresponding Notices of Dispute to the State.

On 21 August 2019, Spotless, Celsus and the SA Government announced they had reached in-principle agreement in relation to the delivery of services by Spotless at the RAH. The agreement, outlined in a terms sheet, remains subject to various approvals by all parties. It addresses:

- settling historical abatement claims
- a revised KPI and abatement regime designed to better reflect the services provided by Spotless
- an increase to Spotless' monthly service fee
- commitments by the parties to work collaboratively on initiatives to further reduce costs and improve patient outcomes.

Details of the agreement are commercially confidential.

It is expected that a finalised settlement agreement will take financial effect from 1 July 2019.

2.4.3 Southern Adelaide Local Health Network Incorporated (SALHN)

The SA Government announced a concept master plan reactivate the Repat Health Precinct (RHP)

The SA Government announced a concept master plan to reactivate the RHP, previously the Repatriation General Hospital, in February 2019.

The State and Commonwealth Governments have announced joint funding commitments for the RHP which include:

- funding from the Commonwealth Government:

- \$30 million for a new State-wide brain injury and spinal cord injury rehabilitation unit, including a new 53-bed inpatient facility
- more than \$1.3 million to fund the operation of an eight-bed specialised Dementia Care Unit, in addition to the 18-bed unit in Ward 18
- \$5 million for a Veteran’s Wellbeing Centre
- \$5 million for a new State-wide Eating Disorder Service facility
- funding from the SA Government:
 - \$14.5 million towards an 18-bed specialised facility to care for South Australians suffering extreme Behavioural and Psychological Symptoms of Dementia and site preparation works for the development of a dementia village
 - \$24.6 million for a state-of-the-art gymnasium for brain injury and spinal cord injury patients and athletes, as well as a ‘town square’ in the heart of the RHP to create a community hub and outdoor space.

SA Health is working with proponents for the development of a dementia village facility and assessing responses to a request for information from interested developers and private health service providers about how they could collaborate with SA Health and LHNs to provide facilities and services relating to surgical and procedural services at the site.

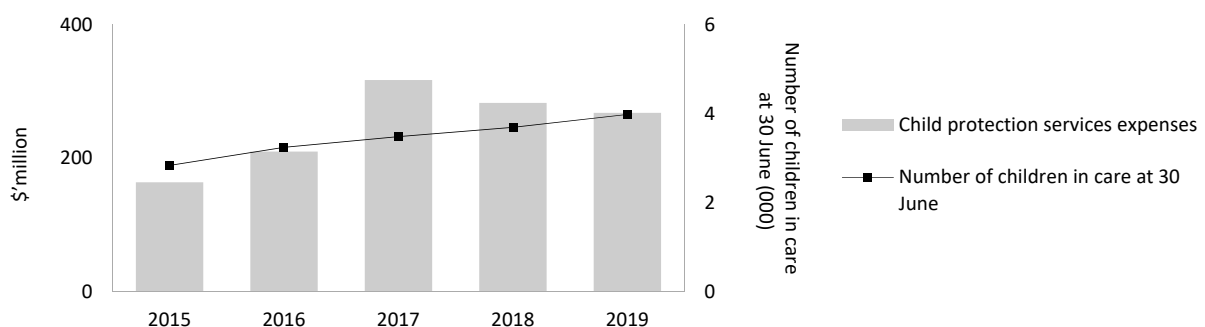
2.5 Other agencies

2.5.1 Department for Child Protection

The number of children in State care continued to increase, but the cost of care per child decreased

The number of children in care rose by 293 or 8% as at 30 June 2019, but the average cost of care per year was \$67 130 per child, down from \$76 470 per child in 2018. Figure 2.6 shows the number of children in care at 30 June and the total care related expenditure for the past five years.

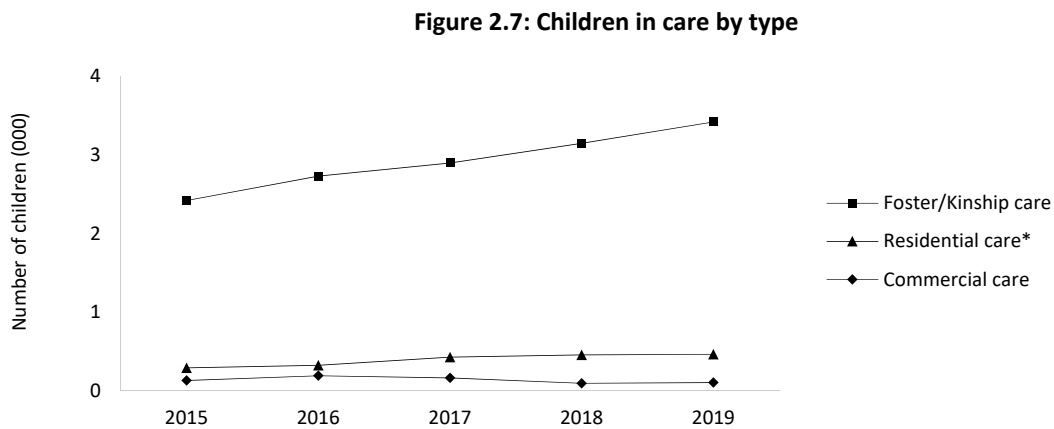
Figure 2.6: Children in care and care related expenditure



Source: Number of children at 30 June was sourced from the Department for Child Protection’s website and is unaudited.

The type of care children are in remains stable in 2018-19

Figure 2.7 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 Department for Child Protection's website and is unaudited.

* Residential care includes 50 children in independent living.

The proportion of children in commercial care remained steady at 2% in 2018-19 and the proportion in foster or kinship care increased slightly to 86% from 85%.

2.5.2 Department for Innovation and Skills (DIS)

Funding to TAFE SA increased in 2018-19

Funding from DIS to TAFE SA increased in 2018-19 by \$13 million to a total of \$259 million.

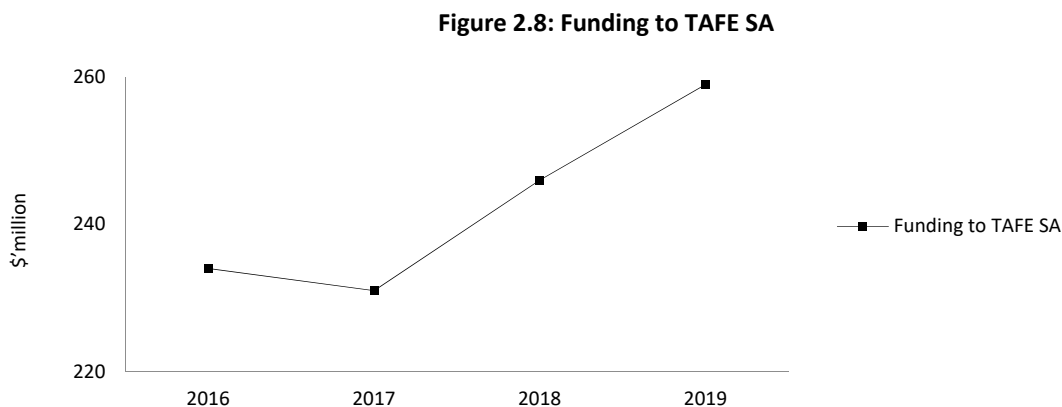


Figure 2.8 shows that total funding has increased since 2017. Funding increased in 2017-18 partly to fund additional rental charges TAFE SA pays to DIS to reimburse DIS for costs it incurs in leasing TAFE SA sites from the URA (following the sale of TAFE SA sites to the URA in 2016-17). Further increases in 2018-19 were mainly due to an increase in vocational education and training subsidy funding, which included \$13 million from the Skilling Australia Fund in South Australia.

The 2019-20 State Budget announced the SA Government's intention to transfer ownership of TAFE SA campuses from the URA to TAFE SA in 2019-20.

These properties are currently leased to DIS, which in turn subleases them to TAFE SA. The existing lease cost funding and lease recharge income of \$54 million that DIS pays and receives will no longer be required under this revised ownership structure.

DIS restructured in 2018-19

The former Department of State Development was renamed the Department for Industry and Skills from 1 July 2018. Several functions, including Arts South Australia and Aboriginal Affairs and Reconciliation transferred out of the Department for Industry and Skills on 1 July 2018.

DIS was created in April 2019 when the Department for Industry and Skills was renamed and further transfers of responsibility occurred between DIS and the Department for Trade, Tourism and Investment.

2.5.3 Attorney-General's Department

Fines Enforcement and Recovery Unit

The Fines Enforcement and Recovery Unit collects outstanding court fines, expiation fees (including overdue local government amounts referred) and other outstanding amounts, including Victims of Crime levies and third party suitor amounts.

Total outstanding debts and related payments as at 30 June 2019 were \$445 million (\$404 million). Of this amount, \$378 million (\$303 million) is under active management, with \$98 million (\$121 million) subject to payment arrangements and \$38 million (\$50 million) having been referred to external debt collection agencies.

During the year the Fines Enforcement and Recovery Unit collected \$104 million in fines and related fees (including Victims of Crime amounts), a decrease of \$14 million from the previous year. A further \$30 million, which is not yet overdue, is subject to payment arrangements.

Victims of Crime Fund

The Attorney-General's Department administers the Victims of Crime Fund. The maximum amount that can be awarded under the *Victims of Crime Act 2001* is \$106 000. The balance of the Fund at 30 June 2019 was \$153 million (\$153 million).

In 2018-19, total payments from the Victims of Crime Fund were \$36 million (\$173 million), including \$25 million (\$19 million) in victim compensation and legal payments. In 2017-18, \$146 million was paid to SAicorp for the National Redress Scheme for people who have experienced institutional sexual abuse.

Total Victims of Crime income for 2018-19 was \$37 million (\$55 million) and included Victims of Crime levies totalling \$23 million (\$39 million) and revenues from the SA Government of \$9 million (\$9 million).

Amounts recovered directly from offenders totalled \$992 000 (\$1.2 million), with a further

\$2.8 million (\$2.8 million) recovered from offenders under the *Criminal Assets Confiscation Act 2005*.

2.5.4 Department for Correctional Services

Operation of the Adelaide Remand Centre was outsourced

The Department for Correctional Services entered into a contract with Serco Australia to operate the Adelaide Remand Centre from August 2019 for seven years. The SA Government retains an option to extend the contract for a further five years, for a total value of \$127 million.

Prisoner bed numbers continue to increase

Prisoner numbers as at 30 June 2019 totalled 2872, a marginal decrease in numbers from 30 June 2018. Over the same period prisoner beds increased by 160 to 3291, with capital works in progress to increase prison capacity by a further 290 beds.

As at 30 June 2019 capital work in progress was \$39 million and included \$27 million for a further:

- 20 beds at the Adelaide Women's Prison
- 270 beds at the Yatala Labour Prison.

2.5.5 Department for Education

Significant capital works program over the next six years

The Department for Education is spending \$894 million on capital works over the next six years on sustainable enrolment growth projects. The projects include spending \$692 million to improve, refurbish and expand capacity at 91 government schools. In addition, a further \$185 million will be spent to provide facilities to move year 7 students from primary to high school, in line with government policy.

New Education Management System

During the year the Department for Education signed a contract for \$76 million with Civica for the right to use their education management system software for 10 years, with a 10-year right of renewal. The system will encompass finance, student records, timetables, administration and other school management tools. It will be rolled out to all sites over three years starting in 2020.

2.5.6 Department of Treasury and Finance (DTF)

Significant functions transferred to DTF in 2018-19

Shared Services SA, Strategic Procurement, ICT Transformation, Return to Work Services, Industrial Relations and a number of other units transferred from Department of the Premier and Cabinet (DPC) to DTF from 1 July 2018.

SafeWork SA transferred to DTF from the Attorney-General’s Department on 1 July 2018, and the South Australian Employment Tribunal also transferred from the Attorney-General’s Department with effect from 1 October 2018.

DTF transferred responsibility for the Office of the Registrar-General and Office of the Valuer-General to DPTI on 1 July 2018.

As a result of these transfers, and some further smaller transfers that occurred in 2018-19, DTF is now a larger department. DTF’s total FTEs increased by 648 to a total of 1386 between 30 June 2018 and 30 June 2019.

2.5.7 Department for Environment and Water (DEW)

Property, plant and equipment controlled or administered by DEW exceeds \$2 billion

DEW manages significant asset holdings on behalf of the State. As at 30 June 2019 the fair value of property, plant and equipment it managed exceeded \$2 billion.

Property, plant and equipment recognised by DEW at 30 June 2019 includes that shown in figure 2.9.

Figure 2.9: Property, plant and equipment recognised by DEW

	\$’million
State’s interest in the property, plant and equipment of the joint operation, Murray-Darling Basin Authority*	727
Crown land (administered on behalf of the State)	548
Land controlled by DEW	330
Park infrastructure, buildings and improvements, roads, tracks and trails, and other infrastructure and equipment (controlled)	437

* Mainly comprises infrastructure assets of \$701 million.

Responsibility for the *Pastoral Land Management and Conservation Act 1989* transferred to the Minister for Primary Industries and Regional Development

This transfer of responsibility, which occurred on 1 January 2019, resulted in the transfer of \$54 million in net assets (mainly pastoral land) to the Department of Primary Industries and Regions.

2.5.8 Department of Planning, Transport and Infrastructure

Capital works in progress total \$1.7 billion

Reflecting its infrastructure responsibilities, DPTI has significant capital works in progress. As at 30 June 2019 capital works in progress of \$1.7 billion included \$677 million for the Northern Connector project, \$509 million for the North-South Corridor Darlington Upgrade and \$99 million for the Gawler Line Electrification and Modernisation project. DPTI relies on significant volumes of Commonwealth funding to deliver its infrastructure projects.

Highways Fund received a further \$143 million from MAC

In 2018-19 MAC paid \$143 million into the Highways Fund. The Treasurer directed MAC to make the payment under section 26(2) of the *Motor Accident Commission Act 1992*. Since 2015 a total of \$2.5 billion has been received into the Highways Fund from MAC.

Further contributions from MAC are subject to the direction of the Treasurer.

DPTI assumed responsibility for an administered liability of \$1.5 billion

The SA Government commercialised the State's land services operations in 2017-18. 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 provided include land titling, registration and valuation services. LSSA started providing land services to customers on 13 October 2017.

On entering the contract LSSA paid \$1.605 billion to the State, including \$1.525 billion principally for the right to be the exclusive provider of land services, the right to use the State's land information assets and the right to use the State's software.

In line with Australian Accounting Standards, DTF, on behalf of the State, recognised a liability for unearned revenue. Following the transfer of the Office of the Registrar-General and Office of the Valuer-General from DTF to DPTI on 1 July 2018, DPTI assumed responsibility for administering this liability.

Over the term of the agreement with LSSA this liability will be progressively reduced, with DPTI recognising administered revenue of \$38 million in 2018-19.

2.5.9 Department of Primary Industries and Regions (PIRSA)

South Australian River Murray Sustainability (SARMS) program

PIRSA received \$31.5 million from the Commonwealth in 2018-19 for the SARMS program. This is a \$265 million program delivered over six years through a National Partnership Agreement.

PIRSA paid \$23 million in SARMS grants, with the payments being made over time as approved projects are delivered.

Regional Growth Fund

The former Regional Development Fund has been repurposed as the Regional Growth Fund. It includes \$150 million available over 10 years to support regional South Australia. Its purpose is to unlock new economic activity in regional South Australia, deliver critical economic infrastructure to create direct benefit across regional industries and strengthen regional communities

PIRSA has entered into \$24 million of funding agreements for 16 projects. Amounts paid in 2018-19 were \$440 000 as funds are not paid on approval, but over time as project milestones are achieved.

Funding of \$7.3 million was also paid from the former Regional Development Fund for previously approved projects.

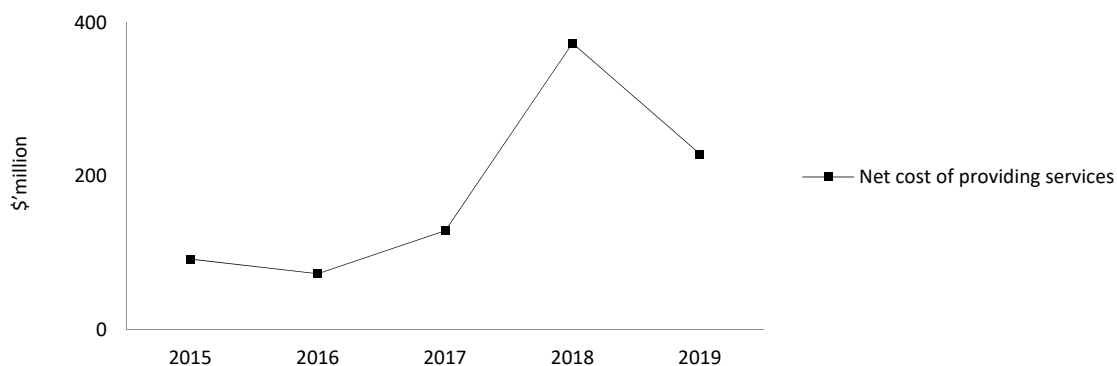
2.5.10 Department of the Premier and Cabinet

DPC became smaller through restructures, reducing its net cost of services to \$228 million

DPC became a smaller agency as a result of restructures in 2018-19. Shared Services SA, Mineral and Energy Resources and a number of other functions transferred to other agencies on 1 July 2018. Aboriginal Affairs and Reconciliation and Arts South Australia came into DPC on the same date. Further detail about restructures is provided in section 3.

DPC has been impacted by several restructures over recent years, as reflected in the following chart which shows DPC's net cost of providing services over the last five years and the significant variation over that time.

Figure 2.10: DPC's net cost of providing services



2.5.11 Department of Human Services (DHS)

National Disability Insurance Scheme (NDIS) transition complete

All eligible State funded disability clients transferred to the NDIS by 30 June 2019. In 2018-19 NDIS expenditure totalled \$183.1 million, including the fixed State contribution under the full scheme bilateral agreement, offset by cash ceiling adjustments and in-kind provision of services (such as the supported accommodation DHS continues to provide to disability clients). It is expected that these payments will increase significantly in future years.

Grants for disability services and payments for brokerage services fall significantly

Grants for disability services decreased by \$130.1 million to \$132.7 million. These grants are primarily to non-government organisations that provide services to individual clients based on their needs.

Payments for brokerage services decreased by \$80 million to \$115.1 million. These payments are to care service providers who were engaged through brokerage arrangements.

The decreases in both grants and payments for brokerage services reflect the impact of clients transitioning to the NDIS and it is expected that these costs will continue to reduce in future years.

Disability and aged care reform

Work continued in 2018-19 on implementing 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 reforms. These changes, along with the full transition to the NDIS, will have a significant impact on DHS's operations, structure and finances in future years.

During the year Adult Therapy Services and Child and Youth Services (through an employee-led mutual) transitioned to the non-government sector. 179 DHS staff transitioned with these two services.

Other planned reforms include the transfer of domiciliary equipment services to the non-government sector. A market tender process was conducted during the year, however DHS did not identify a suitable provider to meet the objectives of the transfer.

DHS employees transfer to South Australian Housing Trust

As a result of two machinery of government changes, 872 DHS employees transferred to the SAHT.

DHS also made a once-off grant payment of \$602 million to the SAHT to enable it to reprioritise its operations and to support its viability. DHS received \$470.2 million in additional appropriation towards funding the grant payment.

Significant changes to DHS operations in 2018-19

As a result of the reforms in the disability and aged care sectors and the transfer of staff to the SAHT, DHS staff numbers reduced by 1307.7 FTEs (33%). A number of staff took TVSPs, which is further discussed below.

From 1 July 2019, Child and Family Support Services transferred from the Department for Education and Department for Child Protection to DHS. These services will form part of a Child and Family Support System being established by DHS.

To accommodate the changing nature of its business, DHS underwent an organisational restructure in June 2019.

TVSPs paid totalling \$26.8 million

In 2018-19 DHS paid TVSPs totalling \$26.8 million to 345 employees. DHS received \$27.5 million of additional funding from DTF to cover this cost.

Most employees were from the NDIS Reform and Services division, with other major affected areas including Accommodation Services and corporate divisions.

2.5.12 Department for Energy and Mining (DEM)

DEM was established on 1 July 2018 when the Resources, Energy and Energy Implementation Groups transferred from DPC.

DEM purchased nine emergency generators in December 2018 and they were used in January 2019

In December 2018 DEM purchased nine generators from APR Energy Holdings Limited, under a commitment made by the previous SA Government in its 'Our Energy Plan'. The generators were purchased for \$227 million and are reported as property, plant and equipment assets.

In response to a shortage of generation capacity, DEM operated the generators on 24 January 2019 providing recoveries of \$2 million, reported under other income, under the Australian Energy Market Operator's Reliability and Emergency Reserve Trader Scheme.

As the generators are operated by the SA Government for emergency generation capacity, this was the only time in 2018-19 that they operated and generated income.

The SA Government has announced the emergency generators will be leased for 25 years

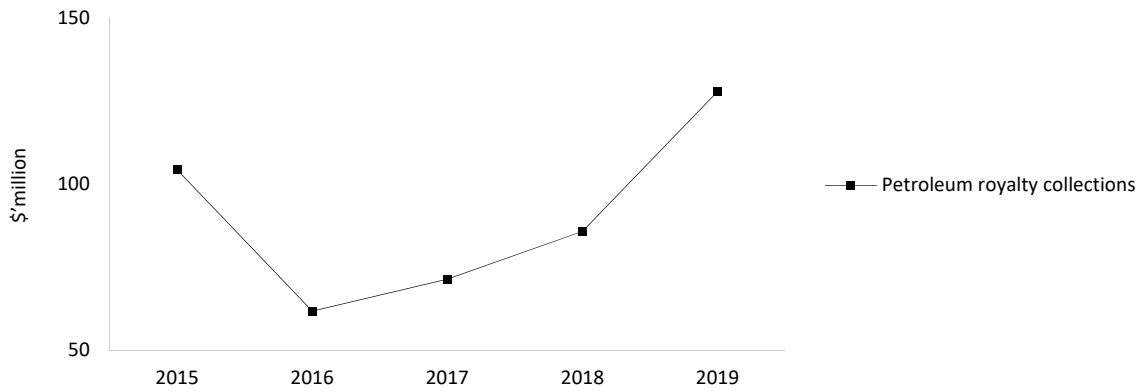
On 26 August 2019, the SA Government announced it had approved two 25-year lease agreements for two entities to operate the nine emergency generators owned by DEM. The lease arrangements will take effect in 2020.

DEM collected \$299 million in mining and petroleum royalty revenue in 2018-19

DEM is responsible for administering the collection of royalties levied on mineral and petroleum production on behalf of the SA Government. In 2018-19 DEM administered the collection of \$299 million, which it advised was the highest amount collected in a year, and paid it to the Consolidated Account.

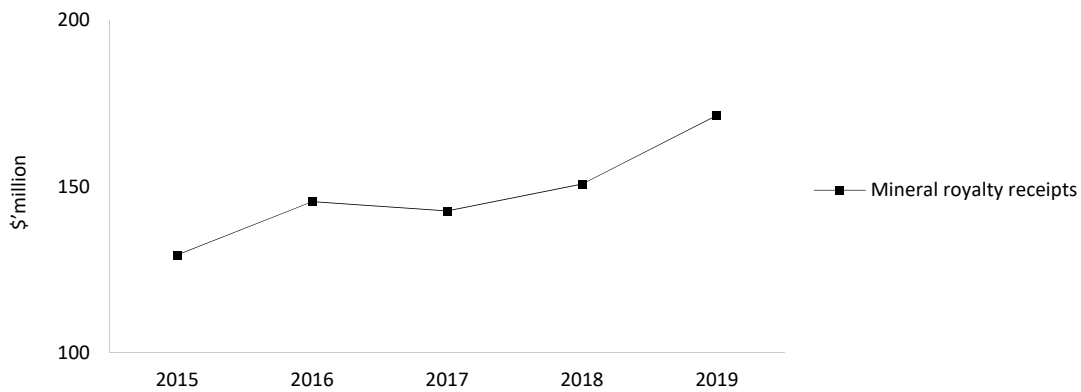
Figures 2.11 and 2.12 show royalty receipts over the last five years. During this period responsibility for collecting royalties shifted between the former Department of State Development, DPC and DEM.

Figure 2.11: Petroleum royalty collections



From 2016-17 royalties have steadily increased up to 2018-19, when a significant increase occurred due to increases in petroleum production and pricing.

Figure 2.12: Mineral royalty receipts



Mineral royalty receipts have remained relatively consistent over the five years shown in figure 2.12, with an increase in 2018-19 due to an improvement in commodity prices and increased production, particularly relating to copper and gold.

2.6 Summary of selected financial disclosures

A summary of selected financial statement items is provided in section 7. It is taken from information disclosed in the financial reports of the agencies listed in section A.1 of the Annexure to this Report. The data does not encompass all public sector agencies.

3 Significant restructures occurred in 2018-19

A number of departments were impacted by significant restructuring in 2018-19. The following major transfers occurred:

- the transfer of Aboriginal Affairs and Reconciliation and Arts South Australia, along with associated corporate functions, from DIS to DPC on 1 July 2018
- the transfer of Mineral Resources, Energy Resources, Energy and Technical Regulator, the Energy Plan Implementation Taskforce and other functions from DPC to DEM on 1 July 2018
- the transfer of Shared Services SA, Electorate Services, Fleet Services (ministerial chauffeurs), ICT transformation, Return to Work Services and Industrial Relations and other functions from DPC to DTF on 1 July 2018
- the transfer of Health Industries South Australia, International Engagement, Trade and corporate functions from DIS to the Department for Trade, Tourism and Investment on 1 July 2018
- SafeWork SA transferred from the Attorney-General's Department to DTF on 1 July 2018
- the Office of the Registrar-General and Office of the Valuer-General transferred from DTF to DPTI on 1 July 2018
- responsibility for the South Australian Employment Tribunal transferred from the Attorney-General's Department to DTF on 1 October 2018
- the Simpler Regulation Unit transferred from DTF to the newly established Office of the South Australian Productivity Commission on 27 October 2018
- 872 DHS employees and 165 URA employees transferred to the SAHT.

Some of these transfers involved the creation of new departments, with the Department for Energy and Mining and Department for Trade, Tourism and Investment created.

The SA Government also created a number of other new agencies in 2018-19, including:

- the Office of the South Australian Productivity Commission
- the Office for Recreation, Sport and Racing
- Infrastructure SA
- the Office of the Commissioner for Public Sector Employment.

4 Other reviews in 2018-19

Areas we gave specific attention to this year for small-scale focused audits were:

- Health sector budget and performance
- Health sector governance and accountability changes
- procurement of KordaMentha services by the Department of Health and Wellbeing
- the Adelaide Festival Centre precinct upgrade.

4.1 Health sector budget and performance

For the last two years we have reported on SA Health's budget management and financial performance.

These and other reports⁷ highlighted continued hospital expenditure growth, failure to achieve set savings targets and ongoing risks associated with the financial sustainability of the public health system.

In 2018-19 we performed a limited review of reported outcomes for the LHNs and SAAS against budget targets. We reviewed to see if the 2018-19 LHN and SAAS budgets were achieved and what factors influenced budget outcomes.

The main observations from our review are:

- in 2018-19, the LHNs and SAAS collectively were expected to exceed their target budgets by \$297 million, based on end of year DHW projections in June 2019
- although the LHNs and SAAS failed to meet their allocated budget targets, DHW projected a balanced net operating result for the total portfolio using centrally retained DHW reserves and approved budget amendments in the 2019-20 State Budget
- CALHN was the largest contributor to the budget outcome and was estimated to fail to meet its budget by \$217 million. About half of this was due to activity volume pressures
- the most significant contribution to overspending by the LHNs and SAAS came from salaries and wages
- LHN and SAAS salaries and wages in 2018-19 grew by 4.95%, in line with recent annual trends
- total actual expenditure by the LHNs, excluding CALHN, has exceeded budget for each of the last four years.

The new governance arrangements, discussed in section 4.2, are partly designed to improve the past budget outcomes, together with other SA Government budget initiatives.

⁷ For example, our annual reports on the State finances and related matters.

4.1.1 Health expenditure remains the largest component of the State budget and exceeded the original budget by \$405 million in 2018-19

The 2019-20 State Budget estimates that more than \$6.5 billion of public money will be spent annually in South Australia's public health system for the next four years. As hospital expenditure is a significant component of the Budget (32%), growth can have a substantial impact on the State's budget.

The 2019-20 State Budget indicated that SA Health would not meet its financial targets in 2018-19, estimating that it would overspend by \$95 million. It indicated a significant savings task remains, and that SA Health and the LHNs will need to continue to drive efficiencies and service improvements across the sector. The \$95 million overspend estimate was after additional funding provided in the mid-year budget review and other budget adjustments and was based on 2018-19 estimated results at that time. DHW reported an unfavourable variance in actual net cost of services against original budget of \$405 million (refer note 35 of DHW's financial report).

In the last two State budgets, the SA Government has allocated significant additional funding over the forward estimates to the health system:

- The 2018-19 State Budget provided an extra \$730 million over the four years to 2021-22, in addition to \$70 million for 2017-18 to ensure that the public health system continued to provide the necessary services required by the community.
- The 2018-19 mid-year budget review in December 2018 provided an additional \$83 million (\$59 million for 2018-19, \$24 million for 2019-20) to meet the increased cost of providing hospital services.
- The 2019-20 State Budget provided an additional \$451 million (including \$95 million for 2018-19) towards establishing a sustainable, efficient health system.

4.1.2 SA Government's strategies to meet efficiency targets

The SA Government, in its 2019-20 State Budget, confirmed its commitment to achieving national average efficiency for the hospital system by 2021-22. It is implementing a number of strategies with the intention of delivering quality health outcomes efficiently, including:

- a new governance and accountability framework for the public health system
- devolving governance and responsibility for the delivery of public health services to new LHN governing boards, which took effect on 1 July 2019. The governing boards have full responsibility for providing health services in line with the *Health Care Act 2008* (HC Act) and performance agreements
- commencing financial and organisational recovery plans in LHNs including CALHN, and in SA Pathology.

4.1.3 Total health portfolio budget result for 2018-19 was balanced

DHW monitors the budget performance of individual LHNs and SAAS throughout the year using an established system and reporting in the DHW Portfolio Performance Report (PPR). This report also contains a whole-of-portfolio financial performance summary.

In 2018-19, the LHNs and SAAS collectively were expected to exceed their target budgets by \$297 million based on end of year projections in the June 2019 interim PPR (the most recent available report at the time of this Report). This was in part due to activity volume pressure as shown later. We have not audited the composition of budgets or the PPRs.

Although the LHNs and SAAS failed to meet their allocated budget targets, DHW’s June 2019 interim PPR projected a balanced net operating result for the total portfolio. This was because of centrally retained DHW reserves and approved budget amendments, including \$95 million for 2018-19 in the 2019-20 State Budget.

Notably, this balanced net operating result is also after substantial increases in the total Health budget in the past three State Budgets.

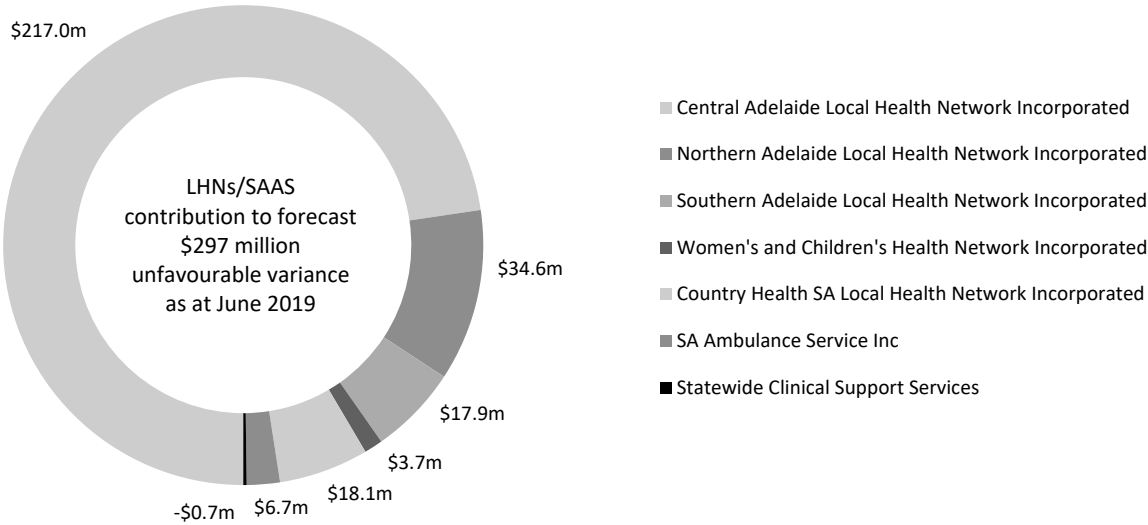
Summary of 2018-19 budget and expenditure

This section provides brief analysis of the composition of the estimated budget outcomes for the LHNs and SAAS based on the June 2019 interim PPR.

CALHN continued to be the largest contributor to the budget outcome and was estimated to fail to meet its budget by \$217 million.

Figure 4.1 shows the estimated contribution of each LHN and SAAS to the projected unfavourable budget variance at June 2019 (interim).

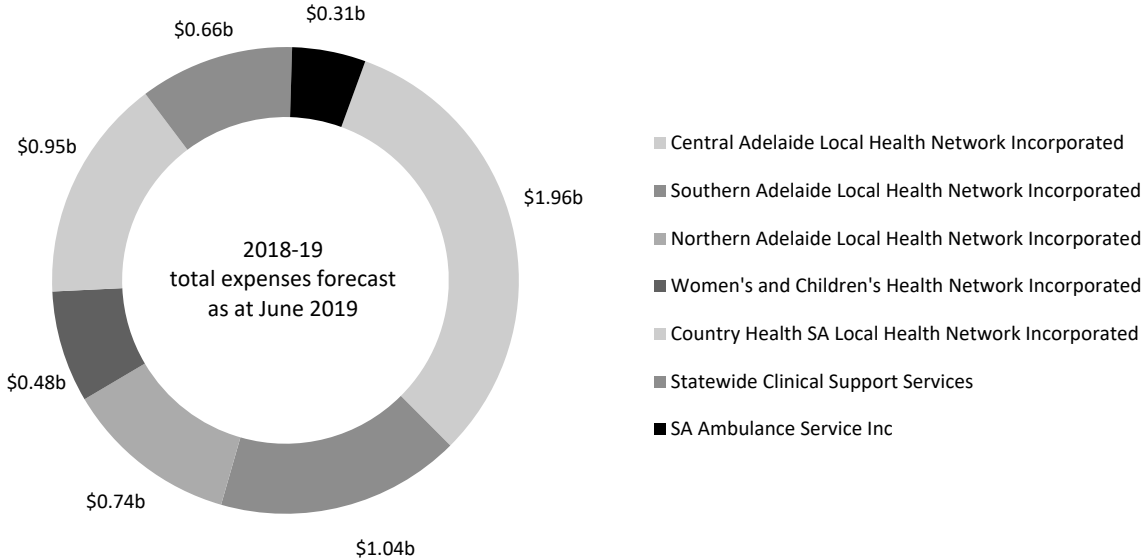
Figure 4.1: Contribution of LHNs and SAAS to the unfavourable budget variance



Source: DHW’s June 2019 interim PPR.

Figure 4.2 shows the June 2019 interim forecast total expenditure of each LHN and SAAS. Comparing the two charts shows that CALHN is the largest contributor to the budget overspend, and its proportion of overspend to total expenditure is considerably higher than the other LHNs and SAAS.

Figure 4.2: Forecast total expenditure of LHNs and SAAS



Source: DHW's June 2019 interim PPR.

4.1.4 Reported reasons for the CALHN net result

The June 2019 interim PPR reported the following reasons for CALHN's forecast unfavourable variance of \$217 million:

- activity volume pressures – \$97.5 million
- CALHN inefficiency to be achieved in years two and three of its recovery plan – \$116.7 million
- other various inefficiencies – \$56.1 million
- less budget overrun funding received – \$37.8 million
- less other revenue in excess of budget – \$15.5 million.

In 2018-19, DHW appointed KordaMentha in a role as implementation partner for CALHN's organisational and financial recovery plan. KordaMentha conducted work across a range of areas at CALHN, including developing plans for improvement and reviewing procurement and financial delegations.

The recovery program is expected to take three years. The KordaMentha contract ends on 25 November 2019. The contract management plan lists required financial milestones and KPIs, which include the following reductions in forecast variance to budget:

- \$41 million by 30 June 2019
- a further \$30 million in the period July to November 2019.

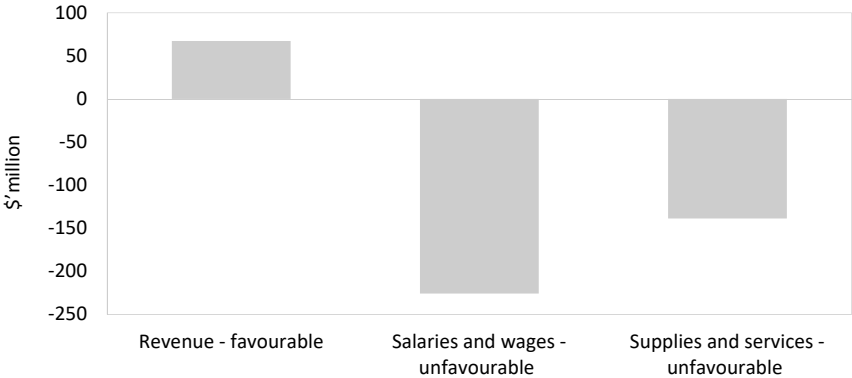
CALHN engaged accounting firm PKF on 12 July 2019 to review the overall performance of KordaMentha against the contract, including assessing for value for money, compliance, achievement of target dates and quality of work. At the time of this Report, PKF had completed its analysis and the results were being reviewed by DHW and CALHN.

4.1.5 Salaries and wages is the largest part of the LHN and SAAS overspend

The June 2019 interim PPR shows the nature of the expenditure and revenue contributing to the \$297 million budget overspend. The most significant contribution to the overspend came from salaries and wages. Unfavourable expenditure forecasts were partly offset by overachieved revenue, which is described in the June 2019 interim PPR as predominately once-off patient and ongoing transport revenue.

Figure 4.3 shows the June 2019 interim forecast.

Figure 4.3: June 2019 interim forecast

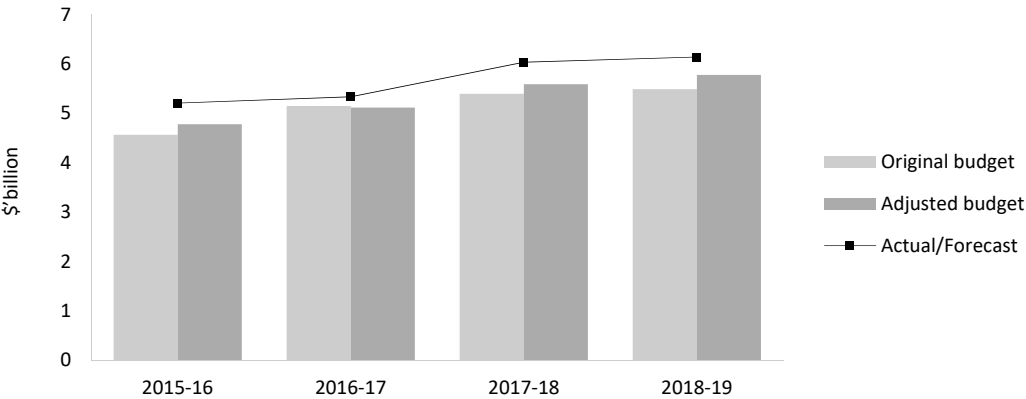


Source: DHW’s June 2019 interim PPR.

4.1.6 Total LHN and SAAS expenses

Figure 4.4 shows that LHN and SAAS expenditure grew in 2017-18, coinciding with the opening of the RAH. Expenditure growth is relatively consistent over the other years.

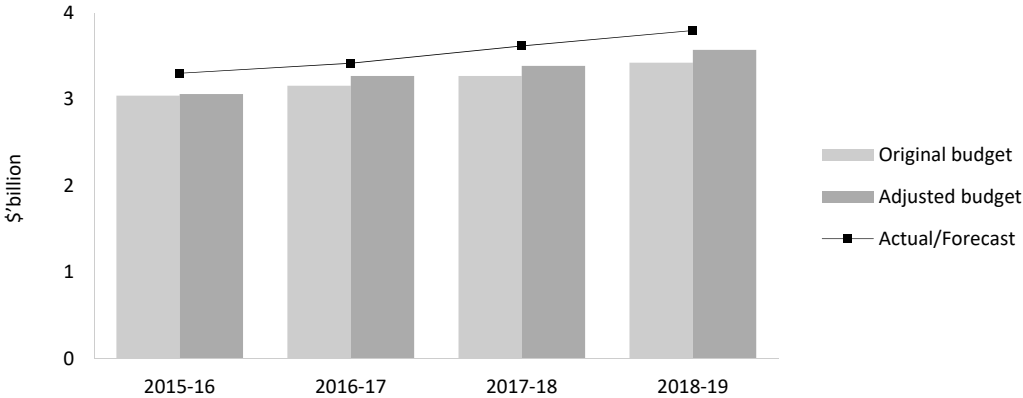
Figure 4.4: LHN and SAAS expenditure growth



Source: DHW’s June 2019 interim PPR.

Salaries and wages make up 62% of LHN and SAAS total expenditure in 2018-19. Figure 4.5 shows that salary and wage expenditure has grown relatively consistently over the last four years at around 5%. Forecast salaries and wages in 2018-19 grew 4.95%, in line with the recent trend. Figure 4.5 also shows that forecast/actual salaries and wages consistently and significantly exceed original and adjusted budgets.

Figure 4.5: LHN and SAAS salaries and wages expenditure

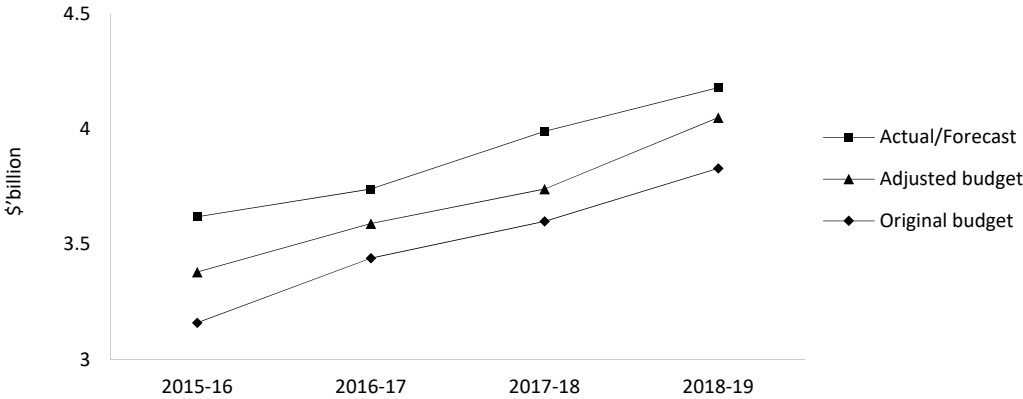


Source: DHW’s June 2019 interim PPR.

4.1.7 LHN and SAAS expenditure growth (excluding CALHN)

Figure 4.6 shows the LHNs and SAAS (excluding CALHN) total budget and actual expenditure for the four years to 2018-19. We have excluded CALHN as the impact of the RAH in 2016-17 and 2017-18 is significant and detracts from showing trends over the years. Figure 4.6 shows that each year actual expenditure exceeds budget and that expenditure growth is relatively consistent. It shows improvements in the variance between actual expenditure to adjusted budget in 2018-19, reflecting an increase in the adjusted budget.

Figure 4.6: Budget and actual expenditure for LHNs and SAAS (excluding CALHN)



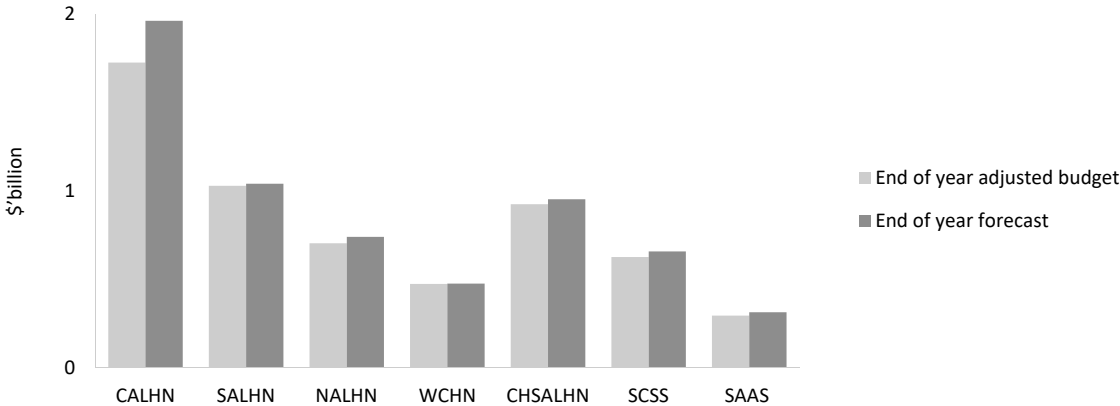
Source: DHW’s June 2019 interim PPR.

Figure 4.6 also shows that in each year budgets were set below the previous year’s actuals. Consequently, under these circumstances, to achieve budgets provided by DHW the LHNs

would not only have to reverse the health expenditure trend but spend at levels lower than previous years. The budgets reflected targets for each year including various savings targets. These were subsequently adjusted each year.

Figure 4.7 shows LHNs and SAAS budget and forecast expenditure for 2018-19 (interim forecast at June 2019).

Figure 4.7: 2018-19 budget and actual expenditure



Source: DHW’s June 2019 interim PPR.

Figure 4.7 shows CALHN having the significantly largest variance from budget.

4.2 Health sector governance and accountability changes

The financial sustainability of the State’s public health system is managed through the HC Act and related structural and governance arrangements. These arrangements are undergoing significant change. The HC Act, initially amended in 2018 to start these changes, sets out the role and functions of the Minister and the Chief Executive, DHW, as well as the functions and powers of LHNs (referred to as incorporated hospitals). Further legislative amendments to the HC Act are being debated in Parliament. Changed governance and accountability structures at DHW and LHNs are commencing.

In 2018, recognising the SA Government’s proposed new governance and accountability framework, we made some observations and recommendations for DHW to consider when developing the framework. They are contained in our 2017-18 Health budget performance report.⁸

We concluded that a clear challenge for this framework, in our view, will be to effectively align the collective and overarching responsibilities for providing an integrated public health system with individual accountabilities. We suggested the success of the SA Government’s changes will be highly dependent on how well they support the roles of the Minister, DHW, the new LHN boards and LHN operational and clinical decision-makers, and create accountabilities throughout the sector.

⁸ Auditor-General’s Report 8 of 2018 *Health budget performance 2017-18*.

Key success factors we identified in our 2017-18 review included:

- gaining commitment and a shared understanding of goals and responsibilities
- providing for clear authority and accountability of decision makers
- improved information for decision-makers
- increasing the capacity of decision-makers
- improving strategic and other management plans.

In 2018-19 we followed up SA Health's progress and the status of structures supporting the governance and accountability changes. Our review was limited to considering the progress of the proposed frameworks, as the changes are progressing and were not applicable until 1 July 2019.

DHW's advice shows that the transition of governance arrangements is well progressed. We observed that:

- LHN governing boards have commenced for 10 LHNs from 1 July 2019
- from 1 July 2019 the Chief Executive, DHW no longer had direct responsibility for administering incorporated hospitals
- DHW has made significant changes to SA Health's governance and accountability frameworks to support devolving governance and responsibility
- DHW is developing a Charter of Responsibility to establish a shared commitment to system mindedness, a culture of respect and clarity of roles and responsibilities
- the 2019-20 SA Health performance framework is published. It includes a shared governance model to promote transparency and shared accountability for performance improvement across the system
- DHW is developing a corporate governance, performance and accountability framework to outline governance requirements that apply across SA Health
- DHW has updated its commissioning principles and priorities by which health and care services are planned, purchased and monitored, and has distributed them to LHNs as a part of the 2019-20 budget process
- service agreements between the Chief Executive, DHW and each LHN and SAAS are being significantly updated for format, structure and content in 2019-20. They were not complete at the time of this Report
- SA Health undertook a capability preparedness and transition process to support preparations for changes to roles and responsibilities in a devolved governance model
- two initiatives to improve information for decision-makers are developing an internal performance information dashboard and supporting LHNs with their continued education on the coding of medical records to relevant standards
- work to establish Wellbeing SA and the Commission on Excellence and Innovation in Health is underway
- a restructure of DHW was implemented in May 2019
- devolution of staff to LHNs and Shared Services SA commenced and 81 FTEs transferred from DHW to Shared Services SA effective 1 July 2019.

A brief description of these activities follows.

4.2.1 Legislative changes

In August 2018 the *Health Care (Governance) Amendment Act 2018* was proclaimed and came into effect within the HC Act on 1 July 2019. The amendments changed the role of the Chief Executive, DHW to remove direct responsibility for administering of incorporated hospitals. The amendments also provide for each LHN to have a governing board.

At the time of this Report a second round of legislative amendments, the Health Care (Governance) (No 2) Amendment Bill 2019 was being debated in Parliament. It proposes provisions relating to the service agreements for LHNs as a key element of the performance framework, as well as provisions relating to the function and role of the Chief Executive, DHW.

DHW advised us that while these amendments relate to governance reforms, they are not critical to implementing the revised governance arrangements and do not impede the operation of LHN governing boards from 1 July 2019. This is because service agreement arrangements have been in place for a number of years administratively and are continuing (refer section 4.2.5.5).

4.2.2 New regional local health networks for country South Australia

A proclamation under the HC Act coming into effect on 1 July 2019 dissolved the Country Health SA Local Health Network Incorporated and transferred its assets, rights and liabilities to six new regional incorporated hospitals (LHNs). These new regional LHNs, listed below, were established by proclamation in August 2018:

- 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
- Limestone Coast Local Health Network Incorporated
- Yorke and Northern Local Health Network Incorporated.

4.2.3 Changes in the Department for Health and Wellbeing's role from 1 July 2019

Under the amendments to the HC Act, from 1 July 2019 the Chief Executive, DHW does not have direct responsibility for administering incorporated hospitals. DHW's role includes a system leadership function and supporting the Minister for Health and Wellbeing and the Chief Executive, DHW in discharging their functions.

4.2.4 Governing boards

The governing boards of 10 LHNs were established on and commenced from 1 July 2019. The governing board chairs and members were appointed by the Minister for Health and Wellbeing. The HC Act requires that governing boards comprise people who between them have knowledge, experience and expertise in specific professional fields. At least two members of each governing board are health professionals and one member has expertise in Aboriginal health.

DHW advised that chairs and members were initially appointed in an advisory capacity during the transition in 2018-19 under the *Constitution Act 1934* to enable and support their induction. The transitional advisory appointments of the 10 chairs (and one deputy chairperson for CALHN) occurred in August and September 2018. Five transitional members were appointed for CALHN on 22 November 2018. Transitional appointments for members across the nine remaining LHNs occurred in 2018-19.

The governing boards' role includes the following financial accountability functions prescribed by the HC Act:

- ensure effective, efficient and economical operations of the incorporated hospital
- manage its budget so that performance targets are met
- provide strategic oversight of and monitor the incorporated hospital's financial and operational performance
- manage performance against the performance measures in the service agreement between the incorporated hospital and the Chief Executive, DHW.

4.2.5 Frameworks supporting the governance and accountability changes

DHW has made significant changes to SA Health's governance and accountability frameworks to support devolving governance and responsibility for the delivery of public health services to the new LHN governing boards. DHW recognises there is still work being done to embed the reforms, build new partnerships across the system and complete the full transition of some of the agreed functions and roles to the LHNs.

The following sections update the progress of the proposed frameworks and other supporting policies and documents, as advised to us by DHW in September 2019.

4.2.5.1 Draft Charter of Responsibility

DHW is developing a Charter of Responsibility to support the effective functioning of the State's public health system. DHW advised us that the Charter will establish a shared commitment to system mindedness, a culture of respect and clarity of roles and responsibilities.

The draft Charter received in principle endorsement from the former Governance Reform Oversight Committee.⁹ It is expected to be finalised and released after the Health Care (Governance) (No 2) Amendment Bill 2019 is passed through Parliament.

The draft Charter sets out the guiding philosophy and key legislative responsibilities of the HC Act and other legislation under which DHW, the LHNs and SAAS interact and deliver outcomes for South Australians.

⁹ The Governance Reform Oversight Committee was established by SA Health to provide executive governance and oversight of its governance reform program.

We are advised the Charter will not be binding. It will rely on a shared commitment by each entity within the public health system to operate under the principles and intent of the Charter. This will include a commitment to progress key areas of health system priority and common interest.

Once implemented, DHW intends to review the Charter as functions and responsibilities are devolved and the public health system moves to its future state.

4.2.5.2 SA Health performance framework

DHW advised that it has developed, after consultation, and published a new SA Health performance framework. It is a public document.¹⁰ DHW advised that the new framework aligns to *The Australian Health Performance Framework 2017* and includes a shared governance model to promote transparency and shared accountability for performance improvement across the public health system.

SA Health's performance framework sets out how DHW, as the leader and steward of the public health system, monitors and assesses the performance of public health services and resources within South Australia. The systems and processes in place to achieve this include, but are not limited to, assessing and monitoring LHN performance, reporting on LHN performance and, as required, intervening to manage identified performance issues.

The performance assessment section of the framework details how performance levels are assessed, including the scoring methodology used to calculate indicative performance levels. The framework also introduces a new simplified performance escalation process for each performance level, underpinned by a range of intervention strategies which will be used to manage under performance.

4.2.5.3 Draft corporate governance, performance and accountability framework

DHW is developing a corporate governance, performance and accountability framework to outline governance requirements that apply across SA Health. The draft framework aims to help staff across SA Health, including within LHNs, to understand the reporting structures and their accountabilities.

DHW considers that establishing and complying with principles of sound corporate governance is essential in a diverse multi-agency like the SA Health public health system.

Information in the draft framework is sourced from legislation, whole-of-government directives issued by DPC and DTF, SA Health policy directives or guidelines, and best practice resources.

4.2.5.4 Draft Commissioning Principles

Commissioning is the process by which health and care services are planned, purchased and monitored. DHW uses a commissioning approach to procure medical and health care services including from LHNs and SAAS.

¹⁰ SA Health Performance Framework 2019-20, was published on DHW's website, viewed September 2019.

DHW has updated its Commissioning Principles and Priorities and has distributed them to LHNs as a part of the 2019-20 budget process.

The updated principles and priorities recognise key changes to the commissioning process in 2019-20 including:

- LHNs to be funded at 100% of the National Efficient Price (with the exception of regional LHNs)
- removal of all peer adjustment loadings in emergency departments and outpatients
- rebalancing the system through home hospital and priority care centre initiatives
- detail of election commitments and new initiatives funded in 2019-20
- pricing adjustments including for hospital acquired conditions, elective surgery and emergency department breaches
- signals from the Independent Hospital Pricing Authority regarding efforts to introduce a hospital readmissions pricing position.

4.2.5.5 Updated service agreements (draft not finalised for 2019-20)

Service agreements between the Chief Executive, DHW and each LHN and SAAS set out a mutual understanding of their respective statutory and other legal functions and obligations through a statement of expectations and performance deliverables for each financial year.

Service agreements are required by the National Health Reform Agreement with the Commonwealth Government, through which the Commonwealth's funding contribution is received. DHW has used them for many years. They are publicly published annually when complete.

DHW advised us that it had significantly updated the format, structure and content of the draft service agreements for 2019-20. It advised that this followed extensive consultation between DHW and the LHNs (including the governing board chairs, chief executive officers and executives), including two formal rounds for feedback and amendments.

While the service agreements relate to the 2019-20 financial year, at the time of our review in September 2019, DHW had not finalised its service agreements with the LHNs or SAAS.

Examples of updates to the service agreements include:

- the language and intent of the agreement will support and reflect a partnership approach between DHW and the LHNs
- greater emphasis has been placed on strategic priorities (national, State and local)
- the description of roles and responsibilities for DHW and the LHNs has been expanded and delineated to reflect the new governance structure
- the performance monitoring schedule has been updated to align to the new SA Health performance framework. This includes updates to the suite of KPIs.

As discussed in section 4.2.1, at the time of this Report the Health Care (Governance) (No 2) Amendment Bill 2019 was progressing through Parliament. Among other things the Bill sets out provisions relating to the service agreements for LHNs as a key element of the performance framework.

4.2.5.6 Capability assessments

SA Health undertook a capability preparedness and transition process to support preparations for changes to roles and responsibilities in a devolved governance model and the transition to LHN governing boards from 1 July 2019. This work largely occurred in the six months from January to June 2019. The primary focus of the work related to LHN preparedness to work under governing boards and preparing information and briefings for boards on their commencement.

DHW advised that some LHNs undertook wellness checks, seeking discussion and advice from external experts. Other LHNs held internal discussions about capability and preparedness and sought external advice for some areas.

DHW advised that the work undertaken had significant benefits in supporting preparations to implement the new governance model.

4.2.5.7 Information for decision-makers

Performance dashboard

DHW is developing an internal performance information dashboard, which is nearing completion and was in test mode in September 2019.

DHW considers the dashboard will be a valuable resource that will enable quick assessment of complex information, including recent performance related data. The data on the dashboard can be viewed at a whole-of-system level and can also be drilled down to hospital level across a range of performance indicators.

Coding reviews

DHW advised that it had supported LHNs with their continued education of staff on the coding of medical records to relevant standards. This has included the technical advice provided by DHW's Medical Records Advisory Unit in response to specific issues raised by LHNs.

Further, DHW has worked with the LHNs to support coding reviews that are conducted with LHN input with the aim of promoting complete and accurate coding of medical records to relevant standards.

4.2.5.8 Wellbeing SA and the Commission on Excellence and Innovation in Health

The SA Government priorities include establishing Wellbeing SA and the Commission on Excellence and Innovation in Health.

Wellbeing SA

DHW advised that work is underway to establish Wellbeing SA as an attached office,¹¹ indicating that it had initially commenced as a division of DHW. It advised that it would develop a model for Wellbeing SA over the next six months, which will include information about its vision, goals, approaches, functions and outcomes.

DHW expects that over the next 12 to 18 months, Wellbeing SA will progressively become responsible for:

- system leadership in prevention, the collection and use of data and evidence to inform practice and out of hospital strategies and services
- funding approaches and services for prevention, health promotion and hospital avoidance
- working collaboratively with community and stakeholders to impact physical, mental and social wellbeing and coordination of care
- supporting the implementation of evidence-based approaches for health promotion and integrated community-based health care
- focusing on priority settings and priority population groups who experience poorer health outcomes and are at higher risk of preventable hospital admissions.

The Commission on Excellence and Innovation in Health

DHW advised that as an interim arrangement the Commission on Excellence and Innovation in Health (the Commission) had commenced as part of DHW. DHW indicated that the operational model and design for the Commission would be developed over the next six months and it will be formally established as an attached office to DHW in early 2020.

DHW advised that the Commission will provide leadership and advice on clinical best practice. It will focus on maximising health outcomes for patients, improving care and safety, championing evidence-based practice and clinical innovation, and supporting clinical collaboration. In doing this, DHW advised the Commission will:

- bring together expertise from clinicians, consumers, health partners and other relevant stakeholders to maximise health outcomes for patients
- be recognised as a centre for excellence, a strong partner for clinical improvement and innovation and will have recognised expertise
- support the provision of safer, more innovative and efficient healthcare by empowering clinicians and consumers.

It is expected that the following three divisions of the Commission will become operational over the next 12 months:

- Clinical Partnerships
- Clinical Improvement and Innovation

¹¹ Attached offices are established under Part 6 of the *Public Sector Act 2009*. The chief executive of an office that is an attached office to a department or departments can have responsibilities to the Premier and the office's Minister and to the chief executive of the department.

- Clinical Informatics.

4.2.5.9 Restructure of DHW and devolution of staff to LHNs and Shared Services SA

As part of the governance reform processes, DHW restructured to best meet its new role as system leader, as well as to support the LHNs. The new DHW structure was implemented in May 2019.

DHW also considered which functions should be devolved from DHW to LHNs or Shared Services SA. This process is ongoing, with some transfers of employees expected to occur in 2019-20 and others deferred until later years.

DHW transferred its centralised Financial Accounting functions (81 FTEs) to Shared Services SA, effective 1 July 2019. This centralised function currently provides various financial services to all LHNs and SAAS. This includes preparing financial statements, journal processing, financial reconciliations, asset accounting and taxation services.

4.3 Procurement of KordaMentha services by the Department for Health and Wellbeing

4.3.1 Introduction and background

CALHN has for many years experienced difficulties reigning in its expenditure to meet its budget and savings targets.

In 2018 a team comprising senior executives of CALHN, DHW and DTF, together with independent health experts, met to create a focused sustainability plan (turnaround plan) to address CALHN's financial performance and to improve the quality of its services over three years in three phases:

- Phase 1 – Diagnostic review
- Phase 2 – Planning
- Phase 3 – Implementation.

In 2018-19 CALHN and DHW engaged KordaMentha through several contracts to help CALHN with its plans. Our 2018-19 audit included a review of the various procurement activities associated with this initiative. We reviewed this procurement because it was a high value, multi-year service arrangement. It is also foundational to CALHN's critical goals to improve its clinical and financial performance. We did not review contract performance.

A background to the various contracted arrangements with KordaMentha is as follows.

August 2018 – KordaMentha was engaged to undertake diagnostic review and develop and document an implementation plan (Phase 1 and 2)

CALHN planned to address a very significant and recurring financial deficit and improve the quality of its services over three years. As it considered that it did not have the skillset to support the necessary programs, it aimed to implement its plan with the support of a range of experts.

CALHN sought to procure this expertise to introduce the required skillsets and, to an extent, transfer skills and knowledge to CALHN employees from the consultants, with a view to making the consultants redundant over a short period of time (three to six months). The procurement's acquisition plan did, however, recognise that depending on the level of skills transfer from experts to CALHN employees in the initial stages, and the complexity of the solutions suggested, another phase of outsourced services may be required.

The overall procurement objective of CALHN turnaround services included improving:

- clinical performance (reducing emergency department and elective wait times, length of stay and clinical complications)
- financial performance by removing a \$264 million deficit over three years and meeting National Efficient Price targets (this target was later changed to \$274 million in the implementation plan).

CALHN engaged KordaMentha in August 2018 as a consultancy to undertake diagnostics (phase 1) and develop and document an implementation plan (phase 2). The estimated cost of the 12-week consultancy was \$880 000. CALHN's Chief Executive Officer sought approval from the Chief Executive, DHW to undertake a single source (direct negotiation) procurement process.

September 2018 – Contract varied and an additional contract executed

In September 2018 the Minister approved a \$1.1 million contract variation, extending KordaMentha services by an additional seven weeks. The purpose was to initiate works under KordaMentha's expedited implementation proposal. The variation changed the scope of the previous appointment, extending it to include aspects of implementation. The procurement of these extended services also occurred through a single source (direct negotiation) procurement process, which was approved by the Chief Executive, DHW.

In addition, CALHN executed a separate contract with KordaMentha for consultancy services valued at about \$300 000 including GST. Under that contract, KordaMentha provided two FTE employees for a period of 10 weeks commencing 24 September 2018 for two business operations positions. This was also a single source (direct negotiation) procurement process approved by the Chief Executive, DHW.

October 2018 to November 2018 – procuring KordaMentha as implementation partner (Phase 3 – CALHN restructuring and financial turnaround implementation services)

The acquisition plan for the procurement of the diagnostic review and planning phases anticipated that the third phase, implementation, may have been performed in-house or using an implementation partner. It anticipated this may occur through a variation to the initial contract. The approach to vary the contract did not eventuate and CALHN developed a separate acquisition plan which sought to engage a supplier through a two-stage process, an expression of interest (EOI), followed by direct negotiation or a select market procurement process. The acquisition plan envisaged the contract would be for a period of 36 months, including two one-year extension options.

The State Procurement Board's (SPB's) Procurement Approvals Committee considered DHW's proposed acquisition plan for the phase 3 procurement. On 18 October 2018 the Committee approved the release of an EOI from SA Health.

Resulting from the EOI process, the evaluation team recommended direct negotiation with KordaMentha for the stage two procurement process when its consensus scoring of EOI responses established a clear gap between KordaMentha and other respondents. On 12 November 2018 the SPB noted the outcomes of the EOI process, approved the stage two acquisition strategy and delegated purchase recommendation approval to SA Health's Procurement Approvals Committee.

The acquisition plan estimated the cost of the engagement as \$45 million, being \$15 million for the base contract term and \$15 million for each of the one-year options.

4.3.2 Audit scope

Our review predominantly focused on the procurement processes for phase 3 (CALHN restructuring and financial turnaround implementation services). We also considered evidence of the rationale and approval for a single source (direct negotiation) approach to the other contracts with KordaMentha.

We note the SPB's role in considering and approving aspects of DHW's phase 3 acquisition plan. We sought to independently evaluate procurement documentation, including reviewing how well the documentation demonstrated the rationale for important decisions made in the procurement process.

Our review of procurement processes was limited to reviewing the key procurement documents and discussion with key DHW staff, including those in DHW's Procurement and Supply Chain Management division.

4.3.3 Conclusion

We found that DHW complied with most of the mandated requirements of the SPB and SA Health directives and requirements. Procurement activities and expenditure were approved by authorised officers and, for phase 3, the SPB. We did note some authorisations occurred after the processes had begun.

The phase 1 and 2 acquisition plan showed a significant level of confidence within CALHN and DHW that a direct negotiation approach was appropriate. The documentation did note that a formal market assessment was not conducted. We consider SA Health should have undertaken and documented a comprehensive market research and evidence-based analysis to support its documented views that no other company had the capability, experience and suitability to meet its complex needs and help CALHN with its turnaround strategy. We also consider DHW should have evidence-based analysis to support its view that it was responding to an urgent government policy decision and the services could not be obtained in time by means of an open market approach.

What started as a 12-week, \$880 000 urgent consultancy procured through direct negotiation, grew to arrangements in excess of \$20 million over 15 months. CALHN

envisaged a three-year turn around. Depending on future decision-making, there is a potential for these arrangements to significantly increase given there is another two years of the implementation process remaining after the existing contracts expire.

In our view, the procurement processes for phases 1 and 2 did not adequately consider potential procurement risks associated with engaging a consultant for a relatively short initial period when there was reasonable likelihood of significant additional work.

We consider CALHN and DHW's procurement approach to phase 3 should have better managed KordaMentha's inherent advantage as the incumbent consultant for the previous phases. This was not identified as a specific risk in phases 1 and 2. Further, potential phase 3 suppliers did not have access to an implementation plan and the time to respond to the EOI was restricted to 10 days.

We also consider CALHN and DHW could have better documented management's independent assessment of the consultant's plans and assessment of internal capability gaps before proceeding with the plan. This is particularly important where consultants have a significant role in advising on strategy for successful long-term operations.

4.3.4 Summary of areas for improvement, our recommendations and SA Health's responses

Our audit identified areas where SA Health could improve its procurement processes. The main findings, recommendations and SA Health's responses are set out here.

Phase 1 and 2 – Support for the decision to appoint KordaMentha through a direct negotiation approach should have been evidence based

We consider SA Health should have undertaken and documented a comprehensive market research and evidence-based analysis to support its documented views that no other company had the capability, experience and suitability to meet its complex needs and assist the organisation in their turnaround strategy. We also consider DHW should have evidence-based analysis to support its view that it was responding to an urgent government policy decision and the services could not be obtained in time by means of an open market approach.

We recommended SA Health only approve direct negotiations when comprehensive and documented evidence-based analysis clearly demonstrates that the reasons for limiting the number of suppliers under the SPB's *Acquisition Planning Policy*, are satisfied.

SA Health responded that the direct negotiation for phases 1 and 2 was an appropriate procurement strategy and complied with the SPB's guidelines.

The response indicated the acquisition plan for phases 1 and 2 stated that CALHN had already used a number of the other large consulting companies to address its budgetary shortfall in the past, indicating that none of them had been able to achieve any significant and lasting change to its financial performance.

The response also discussed the urgency caused by the significance of CALHN's budget deficit, indicating that for every week delayed the financial loss amounted to approximately \$5 million, and the benefit of starting the financial recovery work at the beginning of the 2018-19 financial year.

Phase 1 and 2 acquisition planning and approval processes did not contain some important information

The acquisition plan and support for direct negotiation of phases 1 and 2 described the procurement as short term. It held out that KordaMentha had proposed a model based on a short-term consultancy but failed to detail that KordaMentha's proposal also envisaged a longer role across the three-year improvement period.

We acknowledge that DHW and CALHN must act independently from any proposal provided by a consultant. However, in our view, specific detail of the terms of KordaMentha's proposal was important to those approving the procurement approach and should have been discussed in the acquisition plan and the direct negotiation approval. This is important because it would allow approvers to consider and manage the likelihood of future work and associated procurements. The SPB's *Acquisition Planning Policy* discusses factors to consider when setting contract periods, including switching costs from the incumbent to another supplier.

We recommended SA Health ensure acquisition plans and other supporting documentation adequately describe proposals put forward by recommended suppliers, particularly where there are likely implications of proposed significant additional work.

SA Health responded that it would amend its acquisition plan template to include guidance notes requiring acquisition plans to outline any known potential phases associated with an engagement, whether they are included in the current procurement approach (including justification) and a preliminary discussion on how any inherent advantages would be managed.

It also indicated it would consider this matter in a post-sourcing review and would communicate the concerns with its staff.

Phase 1 and 2 acquisition planning and approval processes did not adequately consider future procurement risks

At the time of the phase 1 and 2 procurement, based on KordaMentha's proposal, there was a reasonable possibility that KordaMentha could have been contracted for further work. We found the acquisition plan did not address procurement risks associated with engaging a consultant for a relatively short initial period when there was reasonable likelihood of significant additional work.

We consider the procurement's risk management process should have identified and managed the risk to future procurements, including:

- the costs of switching to another provider, which may act as a disincentive from moving away from the incumbent

- any inherent advantage of the incumbent potentially compromising any future procurement activities
- risk of potential conflicting interest, where the party providing advice could stand to benefit significantly from the advice given through continuing engagements.

We recommended that when engaging a consultant for a relatively short initial period where there is reasonable likelihood of significant additional work, SA Health should ensure procurement processes adequately identify and address any risk to future procurement processes.

SA Health responded that it would amend its acquisition plan template to include clear guidance requiring appropriate consideration of risks associated with engaging consultants for short-term engagements with the reasonable likelihood of additional work beyond the original contract.

It also indicated it would consider this matter in a post-sourcing review and would communicate the concerns with its staff.

Improvements necessary to demonstrate management's independent assessment of consultant's advice

There were several important processes or evaluations to be made once the implementation plan was provided by KordaMentha at the conclusion of phase 2 and prior to moving on to phase 3. These included evaluating, accepting or recommending the plan and evaluating the alternative methods for implementing the plan. We found these evaluations and decision-making processes were not documented. Documented management evaluation and decision-making on plans provided by an outsourced consultant is important to demonstrate that SA Health maintained responsibility and accountability over the strategies followed.

We recommended management demonstrate that they have independently assessed plans and approaches at critical points of a consultancy, including determining whether to proceed or abandon a plan. This is particularly important where consultants have a significant role in advising on strategy.

SA Health responded that it would update its fact sheet on managing contractors to specify the need to undertake critical assessments of plans and approaches at critical points of a consultancy and that the assessments are to be approved by an appropriate officer.

Importance of managing any inherent advantage of the incumbent contractor during the phase 3 procurement

Given the potential for inherent advantage to the incumbent, KordaMentha, we expected the phase 3 procurement process to pay particular attention to ensuring:

- sufficient information was given to all responders to ensure an even playing field
- responders had adequate time to review the information, ask questions and prepare their tenders.

Our review of these areas found the following:

- The implementation plan was not provided to the market.

The implementation plan developed by KordaMentha was mentioned in the EOI but was not available to other respondents to the EOI call. Respondents were required to indicate what methodology and approach they would follow to achieve the deliverables and outcomes and implement the plan.

The SPB recommended that DHW remove any reference to the implementation plan in the EOI specifications. We note that while DHW did make some amendments to the EOI specifications, references to the implementation plan remained.

The implementation plan may be an advantage to suppliers in responding to these specifications. We note that management advised us that the rationale for not providing the implementation plan to the market was that the criteria for evaluating the respondents to select or shortlist did not depend on the plan.

We recommended that SA Health ensure all respondents have equal access to information discussed in EOI specifications.

SA Health indicated that, after reviewing the draft acquisition plan, the SPB requested that SA Health develop a revised EOI specification that did not refer to the implementation plan and amend the evaluation criteria to focus on experience, capability, capacity and the approach to implementing financial turnaround plans.

SA Health indicated that the EOI specifications were then structured to identify potential respondents with sufficient inherent capabilities and prior experience of financial turnaround plans. It indicated that the provision of an implementation plan to all respondents would not have detracted or contributed to the inherent capabilities or prior experience of any potential respondent.

- There was a short time frame for EOIs.

The response period of 10 days (seven business days) for the EOI was less than the default minimum period of 30 days for free trade agreements. The default minimum period may be reduced to no less than 10 days if specific conditions exist, including where procuring entities are able to demonstrate the conditions exist and where the time limit is sufficiently long to enable suppliers to prepare and submit responsive tenders. The acquisition plan discussed urgency as a reason for the short time frames but did not demonstrate how SA Health's market approach complied with the State's international obligations.

We recommended that the period between advertising a tender and the closing date should only be reduced below the default 30-day minimum when documented evidence-based analysis shows that the reduced period gives suppliers enough time to prepare and submit responsive tenders, taking into account the nature and complexity of the procurement. A state of urgency should only be used as a rationale to reduce time frames below 30 days where documented evidence-based analysis supports that a 30-day time frame is impractical.

SA Health responded with its view that the tender open period complied with the SA Government's obligations under free trade agreements and was in line with an SPB directive to publish the EOI with a response period not less than 10 days. SA Health indicated that free trade agreements allow the tender period to be reduced to no less than 10 days when procuring commercial goods and services. It provided a view that the consultancy and financial turnaround services sought were commercial services that are customarily purchased by non-governmental buyers for non-governmental purposes, thus enabling a reduction in the tender open period to 10 days.

SA Health also indicated that despite the short time frame, the open tender process received nine responses.

Probity planning not adequate for the phase 3 contract

SPB guidelines require higher value and risk procurements to have a probity plan. We consider the procurement was high value and risky because of the complexity of the services being procured and the fact that there was an incumbent supplier who had a role in the prior phases. SA Health did not prepare a probity plan at the planning stage of phase 3 because its acquisition plan rated the procurement risk as moderate.

We recommended SA Health develop probity plans for higher value and risk procurements to ensure probity issues are considered throughout the procurement process.

SA Health responded with its view that a formal probity plan was not required for the KordaMentha procurement as the risk rating in the risk register attached to the acquisition plan was 'moderate'.

SA Health appointed a probity advisor on 26 October 2018, about a week after the EOI market document was released. The advisor's report only concluded on procurement activities undertaken between 26 October 2018 and 6 November 2018. The probity advisory scope was limited to probity aspects of the evaluation processes and included assessing compliance against approved acquisition and evaluation plans. The probity advisor's limited engagement period meant that they did not cover some important procurement processes including establishing the procurement approach, providing uniform information and direct negotiations.

We recommended SA Health ensure a probity advisor's engagement period covers all important procurement processes and decisions.

SA Health responded with its view that probity advisors are not generally used during the acquisition planning stage or business case approval processes. They are used to focus on specifications, evaluation criteria and advising evaluation teams, steering committees or governance committees/boards during the evaluation, approval or endorsement stage.

SA Health's response also indicated that although the independent probity advisor was appointed after the EOI documents were released to the market, the advisor reviewed the EOI documents.

Management of potential conflicts of interest not documented or declared

Section 7 of the EOI invitation required respondents to declare any actual or potential conflict of interest and not employ or engage the services of any person who has a duty to the agency as an adviser, consultant or employee (or former adviser, consultant or employee).

We found that KordaMentha's submission did not disclose its existing advisory arrangements with SA Health. At the time of the submissions, KordaMentha had contractual relationships as consultants and as employees. We acknowledge that these arrangements were well known by DHW and CALHN staff.

We found that the evaluation report did not discuss how these matters were considered and managed throughout the evaluation process. We consider it was important for the evaluation report to demonstrate how the evaluation team considered and managed any conflict of interest risk.

We recommended that evaluation teams ensure EOI submissions include declarations of any actual or perceived conflicts and any existing and past contracts or relationships involving a duty to the agency as an adviser, consultant or employee.

SA Health's response provided its view that it is up to tender respondents to decide what information they provide, and that the evaluation team can only evaluate the veracity and quality of the information provided in a response.

SA Health indicated that the SPB was aware of previous KordaMentha engagements and directed SA Health to address the potential inherent KordaMentha advantage through an expanded risk assessment. SA Health indicated that it updated its risk register along with other amendments requested and resubmitted the acquisition plan, which was approved by the SPB.

DHW did not assess whether deviation from phase 3 acquisition plan was significant enough to require consideration by the SPB

The phase 3 contract with KordaMentha did not match the acquisition plan for the term of the contract, scope of works and value. SPB guidelines require that where an acquisition plan can only be approved by the SPB due to its value, the public authority is to assess whether the deviation is significant enough to require consideration by the SPB. The purchase recommendation did not assess the materiality of the departure from the acquisition plan and the details of the deviation were not provided to the SPB for its consideration.

We recommended SA Health ensure departures from an approved procurement acquisition plan are assessed for significance and, where appropriate, approved by the original approving authority.

SA Health indicated that the deviation was assessed as not having any impact on the procurement process or outcome and therefore was insignificant and, under its policy directives, only need to be documented in the purchase recommendation.

KordaMentha commenced before contracts were signed

We found that for two of the contractual arrangements, KordaMentha commenced underlying services before contracts were finalised. Any period without a formal instrument of agreement potentially impacts on SA Health's ability to manage contractual obligations and conditions, including price. We raised similar concerns in our review of contracting for the Transforming Health implementation partner.

We recommended that SA Health ensure contracts are executed by both parties prior to the contract commencement date. SA Health responded that it would remind staff to ensure contracts are executed appropriately.

4.4 Adelaide Festival Centre (AFC) precinct upgrade

4.4.1 Background

The AFC precinct upgrade is comprised of multiple projects being delivered in stages, including:

- an integrated carpark, office tower and retail area development delivered by the Walker Corporation
- a new hotel and expanded Casino delivered by SkyCity
- upgrades to the AFC
- the redevelopment of the Festival Plaza public realm
- precinct integration works.

Annexure 2 shows the components of the precinct upgrade and the current estimated completion dates.

The Minister for the Arts and the Walker Corporation entered into a development agreement (DA) in May 2016 for the redevelopment of the AFC carpark and integrated development above the carpark comprising a public realm, retail area and office building.

The AFC car park, retail area and office building works are to be funded by the Walker Corporation under the DA. The Walker Corporation is also committed to providing a \$40 million in-kind contribution to developing the Adelaide Festival Plaza public realm.

The State is committed to funding any costs of the Festival Plaza public realm works that exceed \$40 million and the precinct integration works. Further details on the precinct upgrade and DA financial arrangements are provided in section 4.4.6.4.

The SA Government and SkyCity entered into an agreement in July 2017 for the SkyCity development, including a hotel, new gaming facilities, bars and restaurants. The new hotel and casino expansion works are funded entirely by SkyCity with no contributions from the SA Government.

The AFC upgrades, including northern promenade works, internal works and technical, structural and façade upgrades, were funded by the SA Government through Arts South Australia in DPC. DPTI has managed the delivery of the works through a number of construction contractors, including Badge and Schiavello.

An externally appointed contractor (Mott MacDonald) provides project management and project controller services for the AFC works, redevelopment of the Festival Plaza public realm and precinct integration works.

4.4.2 Previous audit review of AFC precinct upgrade

Our past reviews of the AFC precinct upgrade covered:

- the procurement arrangements used to select the Walker Corporation as the preferred tenderer for the Festival Plaza redevelopment and execute the DA¹²
- the procurement and contract management arrangements for two contracts awarded to Mott MacDonald to project manage the State works for the project.¹³

Our review of the procurement process used to select the Walker Corporation identified fundamental shortcomings in key areas, including the basis for key decisions, governance, planning, risk and probity management. Further, there was an absence of analysis and documentation for decisions made. We concluded that the controls over the procurement process were not sufficient to provide reasonable assurance that the process was conducted properly and in line with accepted standards for procurement management.

We also found there were significant deficiencies in the procurement process used to engage Mott MacDonald.

4.4.3 Follow-up review of AFC precinct upgrade

Our review in 2018-19 focused on understanding:

- AFC precinct upgrade governance arrangements
- the status of DA conditions precedent and outstanding actions
- the status of the AFC precinct upgrade including latest developments.

Given the delays to the AFC precinct upgrade noted in sections 4.4.5.1 and 4.4.6.2, we will consider performing a further review at an appropriate time. The review scope and objectives will be determined based on the status of the upgrade projects and our assessment of relevant risks.

¹² Refer to Auditor-General's Report 13 of 2017 *Adelaide Riverbank (Festival Plaza) Development*.

¹³ Refer to section 4.6 in Part A of the Auditor-General's Annual Report for the year ended 30 June 2017.

4.4.4 AFC precinct upgrade governance arrangements

4.4.4.1 Governance committees

The governance committees established to oversee the upgrade of the precinct include:

- Festival Plaza Delivery steering committee
- Festival Plaza and Walker Projects project control group
- Adelaide Festival Centre Redevelopment project control group
- Interface Management Group.

The Riverbank Entertainment Precinct Advisory Committee (REPAC) was also established in November 2018 to advise the Minister for Transport, Infrastructure and Local Government on the development and activation of the Core Entertainment Precinct within the Adelaide Riverbank. This precinct is defined as the area bounded by King William Road, North Terrace, Montefiore Road and Pennington Terrace. REPAC includes representatives from:

- the URA
- the AFC
- the Adelaide Convention Centre
- Adelaide Oval SMA Limited
- the Corporation of the City of Adelaide
- the InterContinental Hotel
- SkyCity.

The current AFC precinct upgrade delivery governance structure is provided in Annexure 3.

Festival Plaza Delivery (Steering Committee)

The Steering Committee was established as the peak State governance body for the AFC precinct upgrade. It was formed and held its first meeting in May 2019. The membership of the Steering Committee includes the following senior representatives from agencies and advisory bodies involved with the delivery of the upgrade projects:

- Chief Executive, DPTI (Committee Chair and Project Sponsor)
- Chair, REPAC
- Chief Executive, URA
- Chief Executive, AFC
- Project Director, DPTI
- Government Architect, DPTI
- Executive Director Corporate Services, DPC.

The purpose of the Steering Committee is to provide oversight, governance and direction on the design, delivery and construction of the Festival Plaza precinct upgrade to ensure it is delivered on time and on budget. The Steering Committee also endorses or escalates project design changes, key procurement decisions and other key project decisions as required to the Project Sponsor, who can then escalate to the Minister for Transport, Infrastructure and Local Government, Ministerial Reference Group or Cabinet as required.

The Steering Committee was established due to proposed changes to the design concept plan that required coordination across government to ensure issues were administered in line with the DA. Further detail on proposed changes to the design concept is provided in section 4.4.6.1.

Festival Plaza and Walker Projects project control group (Walker PCG)

The Walker PCG was established under the DA. It has five members, with two appointed by the State (currently the DPTI Project Director and URA Chief Executive), two appointed by the Walker Corporation and one from the project controller (Mott MacDonald). The role of the Walker PCG is to prioritise, guide and monitor the planning and completion of the integrated development. This includes considering and recommending changes in scope and design from the concept plans to the Project Sponsor and Minister for Transport, Infrastructure and Local Government, as well as ensuring completion of the integrated development in line with the final plans and program.

Adelaide Festival Centre Redevelopment project control group (Festival Centre PCG)

The Festival Centre PCG was established with the following roles and objectives:

- safely delivering the AFC redevelopment works to the agreed program, budget and quality parameters
- providing project oversight governance and direction
- reviewing and considering regular project status reports prepared by the delivery teams and providing responses and direction.

The Festival Centre PCG has representatives from DPTI, Arts South Australia, the Adelaide Festival Centre Trust and Mott MacDonald as project controller.

Interface Management Group

The Interface Management Group has representatives from DPTI, URA, Arts South Australia/ DPC, Walker Corporation and SkyCity. It was established under the Interface Agreement to discuss the progress of projects, compliance with the interface program and any issues or concerns related to the interface between the projects or the Interface Agreement, including the coordination of staging plans and programs.

4.4.4.2 Governance structure and plan

The original AFC precinct upgrade governance structure and plan were endorsed in May 2016, with a subsequent revision made in May 2017.

A new governance structure for delivering the precinct upgrade was endorsed by the Steering Committee in August 2019. The updated governance structure reflects several recent changes impacting the AFC precinct upgrade. This includes the abolition of the Riverbank Authority in July 2018, the establishment of REPAC in November 2018 and the establishment of the Steering Committee in May 2019.

The revised AFC precinct upgrade governance structure is provided in Annexure 3.

The delivery governance plan has not yet been updated to reflect recent changes impacting the AFC precinct upgrade. It is a key document outlining the roles and responsibilities of agencies, governance committees and key project personnel. The prompt update of the governance plan will help to ensure current SA Government expectations and arrangements for the precinct upgrade are captured and clarified. Clarity of roles and responsibilities is a vital element for the success of the AFC precinct upgrade.

4.4.4.3 Agency roles and responsibilities for managing the development agreement with the Walker Corporation

The DA set out the roles and responsibilities of SA Government agencies in administering the agreement at the time it was signed in May 2016:

- the Riverbank Authority was nominated as the agency of the State responsible for administering the DA, including the design, use, enjoyment or any other matter affecting or relating to the public realm
- DPTI was nominated as the agency of the State responsible for administering the DA in relation to the development and construction of the integrated development.

Responsibility for administering the DA in relation to the design of the public realm during construction was transferred from the Riverbank Authority to DPTI in October 2017. DPTI continued to be responsible for delivering the contracted works.

The Riverbank Authority was dissolved in July 2018 and its assets, rights and obligations were transferred to the URA. This included taking on the Riverbank Authority's roles and obligations under the DA, specifically administering the DA in relation to the use, enjoyment and any other matter affecting the public realm.

The URA, through its service level agreement with the Riverbank Authority, played a lead role in developing the concept design for the public realm and the integration of the components of the overall redevelopment. It now plays a supporting role to DPTI in managing the DA in relation to developing the design of the public realm.

The URA also advised us that it has taken a lead role in administering the following components of the DA:

- negotiating and granting the leases for the car park, office building and retail area
- consolidating the integrated development land
- administering the soil banking agreement
- exercising the State's rights of first refusal to sublease portions of the office tower and retail area
- negotiating the public realm management agreement
- negotiating and granting the retail curtilage licence.

4.4.5 Development agreement

4.4.5.1 Status of DA conditions precedent and outstanding actions

The DA outlines the obligations of the State and the Walker Corporation in relation to conditions precedent to be met and required actions with corresponding timelines.

Project status reporting for July 2019 highlighted the following actions outlined in the DA that were outstanding and required closure:

- agreeing design responsibility, final plaza design, construction program and payment schedule between the SA Government and the Walker Corporation
- submitting final plans for the public realm, office tower and retail area by the Walker Corporation and approval by the SA Government
- the Walker Corporation proving financial capacity and achieving binding pre-commitment agreements with tenants for the office tower
- the Walker Corporation obtaining development approval, proving financial capacity and achieving binding pre-commitment agreements with tenants for the retail area
- granting leases for the retail area by the SA Government to the Walker Corporation
- finalising the public realm management agreement by the SA Government.

DPTI advised that no condition precedent under the DA has been waived.

The URA advised that the Walker Corporation is currently preparing its final plans for the office building and retail area and is seeking tenants. This is expected to be closed out in 2020 prior to the Walker Corporation constructing the office building and retail area. The retail area lease is expected to be granted in 2020 after the Walker Corporation has obtained development approvals for the retail area.

The URA also advised that finalising the public realm management agreement is outstanding, pending final designs and resolution of State ownership and management arrangements for the public realm. It is expected that this agreement will be finalised in 2020-21, prior to the completion of the first stage of the Festival Plaza public realm.

To minimise project delays, the SA Government should continue to implement strategies to ensure the prompt resolution of outstanding DA actions with the Walker Corporation.

Promptly finalising the public realm management agreement will also clarify and confirm ongoing ownership and maintenance arrangements for the precinct.

4.4.5.2 Managing compliance with the DA

The URA and DPTI advised that they obtain comfort that the Walker Corporation and the State are complying with their obligations under the DA primarily through:

- Walker PCG meetings which they participate in with the Walker Corporation
- monthly reports to the PCG prepared by DPTI and Mott MacDonald.

DPTI also reviewed the DA in 2018 to identify outstanding actions and conditions precedent. DPTI formally wrote to the Walker Corporation in November 2018 to initiate follow-up action as needed.

The URA indicated that it does not currently have a separate contract management plan for the project. It is currently establishing a comprehensive matrix of the State's obligations and responsibilities under the DA. This will form the basis of an ongoing project management plan.

It is sound practice to establish a contract obligations register and contract management plan for the DA to ensure all contract deliverables are systematically identified and regularly monitored by a specific officer or governance committee.

4.4.6 Current status of AFC precinct upgrade

4.4.6.1 Proposed changes to public realm design

The URA advised that a number of changes were proposed to the original design concept plans in the DA for the Festival Plaza public realm in 2019. These changes were driven by a combination of:

- the Walker Corporation's proposed changes to the office building and retail area, with consequential impacts to the interface with the adjacent public realm
- proposed changes to the public realm to accommodate input and feedback from the AFC and other members of REPAC
- proposed changes by DPTI to achieve a better value for money outcome from the State's investment in the precinct redevelopment through value management opportunities.

The Walker Corporation and the SA Government (led by DPTI and the State's lead architect, ARM Architects) have engaged in a series of integrated design workshops to assess the Walker Corporation's proposals and develop a revised integrated design reflecting the combined impact of the potentially acceptable changes.

The URA is also conducting a parallel exercise on behalf of the Steering Committee to discuss the potential commercial implications of the Walker Corporation's proposed changes.

The URA advised that the revised designs for all elements of the Walker Corporation's development will also require final development approvals from the State Commission Assessment Panel (SCAP).

The URA also advised that, at this point in time, no changes to the original design concept plans in the DA have been formally accepted by the State and no revisions to the DA or project time frames have been agreed by the State.

It is important that the SA Government gives ongoing focus to ensuring any changes to the original design concept plans in the DA are reviewed and approved in line with DA requirements.

4.4.6.2 Progress against program schedule

Figure 4.8 summarises the status of key project milestones compared to originally scheduled dates in the DA as advised by DPTI.

Figure 4.8: Progress against key milestones in the DA

Milestone	Date in DA final program	Current forecast completion date
Carpark design – submission of final carpark plans	15 May 2017	September 2019
Carpark construction completion	25 November 2019	Late 2020
Festival Plaza public realm design – submission of final documentation	22 January 2018	Subject to resolution of program in consideration of the proposed design changes
Festival Plaza public realm construction completion	14 April 2021	2022
Completion of office building and retail area	23 June 2021	2022

There are significant delays in the current forecast completion dates compared to the final program dates in the DA.

If the SA Government intends to keep to the original milestones or to otherwise minimise project timelines, it is important that it continues to implement strategies to ensure the Festival Plaza public realm design plans are promptly finalised.

DPTI advised that the final program in the DA is subject to design changes and extension of time claims. Programs dates were impacted by:

- stakeholder feedback
- proposed changes to the Walker Corporation office tower and retail building
- the resolution of a grade separation extension of time claim
- value management opportunities.

The proposed changes in design are also subject to the SCAP planning process and the time frames for this will also impact on program dates.

DPTI indicated that the impacts of the above factors on the program dates are yet to be resolved. Further details on design changes, extension of time claims and value management opportunities are provided in sections 4.4.6.1, 4.4.6.3 and 4.4.6.6 respectively.

DPTI indicated the forecast completion date for the SkyCity hotel and casino works is currently October 2020. The remaining AFC upgrade works are expected to be completed in late 2020, conditional on the Walker Corporation completing the car park.

4.4.6.3 Extension of time claims

Lendlease was contracted by the State to complete grade separation works in the precinct, including works to lower Festival Drive and separate vehicle and pedestrian traffic.

The Walker Corporation submitted an extension of time claim under the DA for delays to the grade separation works. The grade separation works were completed around five months later than anticipated due to latent conditions discovered during construction including old piles, walls and heritage arches.

DPTI advised that the Walker Corporation has not specified any financial impact amounts as part of their extension of time claim, as the DA does not contemplate any rights to claim for financial compensation as a result of delays to completing the grade separation works.

DPTI also advised that the SA Government and the Walker Corporation have agreed the duration and basis of the delay. They have been unable to agree on how the delay will be taken into account in the final program. The extension of time claim is still subject to negotiation between the SA Government and the Walker Corporation, and the outcome of the claim is not yet resolved.

Additional extension of time claims have also been made by other contractors for other aspects of the precinct upgrade, including AFC upgrade works. The estimated total cost of these claims to 30 June 2019 is \$2.1 million.

4.4.6.4 AFC precinct upgrade financial position

DPTI is responsible for managing the budget to deliver the State's components of the Festival Plaza public realm. The URA manages a small budget component related to signage, communications and legal advice.

The SA Government committed \$182 million to the project. Figure 4.9 details the key costs to the SA Government of the upgrade.

Figure 4.9: AFC precinct upgrade – key costs to the SA Government

Cost	\$' million
Lease of 400 car parks in Festival Centre carpark	30.0
Festival Plaza public realm works	48.3
Precinct integration works	61.4
<i>Less: Consideration from the Walker Corporation for development rights</i>	<i>(40)</i>
Total – car park, festival plaza and precinct works	99.7
AFC consequential impacts and complementary works	82.7
Total net cost to SA Government	182.4

The DA requires the Walker Corporation to pay \$40 million to the SA Government by incurring construction costs for the public realm as consideration for the State agreeing to grant the leases for the integrated development.

The current State funded total budget for the precinct upgrade managed by DPTI, excluding the Walker Corporation's contribution of \$40 million, is \$222.4 million.

DPTI advised there are cost pressures for the AFC precinct upgrade budget associated with:

- the upgrade of the area between the AFC and Dunstan Playhouse shells, which was not originally budgeted
- escalation costs
- use of South Australian/Australian products for the public realm (particularly paving)
- works to the existing Parliament House retaining wall not originally budgeted
- additional professional fees and variation costs to the design.

DPTI indicated that the cost impacts for these areas and corresponding value management strategies are being worked through.

4.4.6.5 Status of key financial obligations under the DA

The URA advised that under the DA, the \$30 million upfront payment of the carpark sublease to the Walker Corporation must occur within 30 days of practical completion of the carpark. This payment is therefore expected to be made in 2020-21, with the carpark forecast for completion in late 2020.

The URA advised that the scope of the public realm works and framework for the \$40 million contribution from the Walker Corporation was agreed and is detailed in the DA as amended by the Deed of Acknowledgement, Further Agreement and Amendment (DoAFAA) dated 3 May 2017. The DoAFAA sets out the process by which the Walker Corporation and the State will finalise the public realm scope of works.

The Walker Corporation submitted the preliminary design documentation and cost estimate for the Festival Square public realm redevelopment plaza landscaping works to DPTI in June 2019. DPTI advised that:

- this cost plan was reviewed, with advice and input from the State's Cost Manager, Rider Levett Bucknall
- following this review, Rider Levett Bucknall reviewed and updated the State's own cost estimate and they continue to provide updates in their monthly cost report.

4.4.6.6 Value management

The SA Government has started to review the precinct design to identify value management opportunities to address the cost pressures referred to in section 4.4.6.4. Value management savings opportunities identified by DPTI and the URA, with the assistance of ARM Architects, were endorsed for implementation by the Steering Committee. DPTI advised that a minute to the Minister will be prepared to note:

- the changes identified as part of the value management review
- that the modifications to the design will be referred to SCAP.

5 Financial reporting

5.1 Financial reporting obligations of agencies and matters requiring attention

All public authorities are required to prepare financial statements that present a true and fair view and comply with Australian Accounting Standards and Treasurer's Instructions.

Preparing financial statements that present a true and fair view is not achieved through strict application of all accounting standards, or solely through the use of a model. Significant judgement must be applied to determine what information is of value to users of financial reports and what is required to achieve compliance.

In particular, preparing useful disclosures requires analysis and thought and should not only be about compliance. While DTF produces model financial statements that are a useful reference, they must not be blindly followed.

The disclosures contained in agency draft financial statements received by my office demonstrate a lack of review to ensure they provide useful insights and meaningful information.

A number of draft financial statements submitted contained boilerplate disclosures including:

- disclosures about balances and transactions the agency does not have
- disclosures about irrelevant accounting policies or policies the agency has chosen not to apply
- no information about balances and transactions not contained in the model financial statements
- no specifics about accounting policies chosen and applied by the agency.

Significant accounting policies included in the model financial statements may include some that are not relevant to an agency. Including them (and any related disclosures) in the agency's financial statements contributes to financial statement clutter and obscures the key messages. Not only is meaningful information obscured by this approach, but it is a missed opportunity to explain how specific policies have been applied.

Further, accounting standards require many disclosures that need entity-specific consideration, including key estimates and judgements. Model financial statements cannot address all the possible permutations or cater for all transactions and events that may occur. Responsibility for compliance rests with preparers and chief finance officers and needs increased focus in future years.

5.2 Impact of new accounting standards on 2018-19 financial reports

5.2.1 AASB 9 Financial Instruments

31 December 2018 and 30 June 2019 financial statements were required to comply with AASB 9 for the first time. It replaces AASB 139 *Financial Instruments: Recognition and Measurement* and changes the way certain types of financial assets and liabilities are accounted for. It also changes the way impairment of financial assets is calculated.

Implementing AASB 9 has not had a material impact on most agency financial statements. While the new model for impairment generally resulted in an earlier recognition of impairment losses and a reduction in receivables, this was not significant. However, the level of disclosure required from consequential amendments to AASB 7 *Financial Instruments: Disclosures*, together with transitional disclosure requirements, has had a sizable impact on some financial statements.

Last year I expressed concerns about agencies' lack of preparation for implementing AASB 9. I also highlighted that agencies should reflect on recent experiences in implementing new accounting standards to learn from prior approaches. This reflected our past observations about the implementation of new standards being left until late in the financial year, putting further pressure on already tight deadlines.

It appears that there was a similar approach to implementing AASB 9. We found that:

- some new impairment calculations were not considered until late in the financial year and were not adequately supported
- initial disclosures contained errors that needed correction
- changes to policies and processes were still required.

Outstanding matters that still need to be addressed for AASB 9 will impact agencies' ability to meet the requirements of the new revenue and leases standards in 30 June 2020 financial reports.

Further, agencies must learn from this experience and implement better and more timely processes, preparing disclosures and developing calculation models well before year end, particularly given the significance of the changes required to 2019-20 financial statements. Sound quality assurance processes must also be developed and adequately resourced, with quality reviews being undertaken before statements are submitted for audit.

5.3 Upcoming changes to accounting standards

New accounting standards applicable from 1 July 2019 and 2021 will significantly change aspects of financial reporting, including:

- when income is recognised
- the recognition of new assets and related liabilities for all leases and certain arrangements with the private sector

- service concession arrangements.

The new standards and their application dates are shown in figure 5.1.

Figure 5.1: Application dates for new accounting standards

Accounting standard	Application date for 30 June financial reports
AASB 16 <i>Leases</i>	30 June 2020
AASB 15 <i>Revenue from Contracts with Customers</i>	Not-for-profit entities: 30 June 2020
AASB 1058 <i>Income of Not-for-Profit Entities</i>	30 June 2020
AASB 1059 <i>Service Concession Arrangements: Grantors</i>	30 June 2021

Last year I expressed concerns about the SA Government’s ability to successfully implement the accounting treatments required under these new standards. While progress has been made, there is still a substantial amount of work required and my concerns remain.

Progress has been partly facilitated by DTF requiring agencies to prepare 2019-20 budget figures in line with the new revenue standards. Agencies were also required to provide information for external leases, while internal lease information was excluded.

Where a new accounting standard has been issued but is not yet effective, agencies are required to disclose known or reasonably estimable information on the possible impact that applying the standard will have on their financial statements.

Due to the significance this year, I asked agencies to submit their draft disclosures for the impact of these standards prior to the statutory deadline. While agencies met this request, it was clear that they are at different stages of their implementation plans. Further, most disclosures were boilerplate and provided little to no context about the estimated numbers.

It was clear that while estimated impacts could be provided, they were very much preliminary, and there is still work required to resolve outstanding issues and calculate the required adjustments for 1 July 2019. In particular, during our 2018-19 audit it became evident that DPTI had not completed all the work required to provide agencies with the information needed to adopt the leasing standard. Further information about this is provided in section 5.4.

Given the significance of the changes, there is a real risk that there may be material errors in financial statements that could result in qualification if agencies do not have enough support or do not allocate sufficient resources to resolve these issues before the next reporting date.

Further, there will be limited time to perform our work if issues are not resolved early. DPTI has outlined some options for calculating non-lease components. For one option, DPTI has estimated it will take between six and nine months to review its leases and develop a reliable model for separating non-lease components. This will impact most agencies and their ability to prepare compliant financial statements.

5.4 Fundamental changes to lease accounting

The most significant impact of AASB 16 is the creation of new right-of-use (ROU) assets and lease liabilities and the related impacts on solvency and liquidity ratios. The impact to the balance sheet (assets and liabilities) will be significant for agencies with a large number of leases. This will eventually include concessional leases for which agencies will have to determine the fair value of the leased asset – the Australian Accounting Standards Board has temporarily deferred this treatment until further notice.

The largest volume of contracts in SA Government relates to accommodation and motor vehicles. A number of public private partnerships will also be captured by AASB 16. The changed accounting does not reflect a change in the substance of the SA Government's contractual arrangements for leases or resulting cash flows. It is not anticipated that credit rating agencies will vary credit ratings as a result of the new lease accounting requirements, as rating agencies and investors have long adjusted leverage ratios to incorporate the hidden leverage of operating leases.

5.4.1 Impact on the balance sheet

Total assets will increase significantly by the creation of the ROU assets, which will equal the lease liability at inception but not over time. The ROU asset will amortise over time independent of the lease liability, likely amortising on a straight-line basis. The ROU asset will not equal the lease liability over time because of the difference in amortisation of the assets and the liability. The ROU asset will likely be lower than the lease liability.

Total debt (liabilities) will increase on adoption of AASB 16 by the amount of the present value of future lease payments discounted at the incremental borrowing rate. On transition, there will be no impact on equity other than adjustments for existing deferred lease assets or liabilities. Over time, equity (retained earnings) will be reduced by interest expense and ROU amortisation. In the early years of the lease term, these amounts will be higher than the level of operating lease expenses. This will reverse in the later years of the lease term.

The ROU asset will not be split into a current and non-current portion; rather it will all be classified as non-current. However, the lease liability must be split. The impact on current assets and current liabilities will not be consistent.

5.4.2 Impact on profit and loss and cash flows

Currently accounting sees the operating lease expense generally being recognised in supplies and services expense on a straight-line basis. Under AASB 16, the expense is recognised as two distinct components:

- amortisation of the ROU asset on a straight-line basis
- financing expense using effective interest method.

The only impact on the cash flow statement will be that the principal repayment portion of the lease payments will be included in financing cash flows rather than operating.

5.4.3 The SA Government's response to AASB 16 *Leases*

Opportunities to reduce the cost of compliance by agencies

The development of AASB 16 has been forthcoming for more than a decade, with initial discussion papers issued in 2009 and the final standard issued in early 2016.

Commentators and accounting experts have long advised entities to consider the impacts early, allowing necessary information to be obtained and/or change leasing arrangements. It was anticipated that entities would either alter leasing arrangements in advance of adopting the new standard, or in the future to manage the accounting complexities and/or perception of leverage.

While most external government accommodation leases sit with DPTI, Memorandums of Administrative Arrangements with agencies generally pass on the terms, conditions and costs contained in the contract. These are considered to be enforceable arrangements under AASB 16 and meet the definition of leases due to the specificity of the accommodation being leased.

In anticipating the complexities, at least one other State has amended its internal lease contracts to include substantive substitution criteria, meaning they no longer meet the definition of a lease. In my view, this would be a good outcome for the public sector in light of the costs and complexities involved in accounting for subleases, the impact on consolidation and the resulting impact on multiple sets of financial statements.

Framework for compliance set by DTF

AASB 16 contains ongoing and transitional options and practical expedients. To provide consistent information for whole-of-government reporting, and after considering and weighting the budget implications and costs of compliance, DTF has finalised the options that must be applied by agencies in their financial reporting.

DTF has mandated adoption of all application expedients available in AASB 16. As a result, agencies need not recognise lease assets or liabilities for leases:

- with terms of 12 months or less, together with that which may have had longer terms but have less than 12 months remaining on transition
- where the value of the underlying asset is less than \$15 000 when new.

By taking these options, lease expenses will be recognised on a straight-line basis over the term of these leases. In addition, no analysis is required for contracts that have previously been assessed under the former leases accounting standard (AASB 117 *Leases*) as not containing a lease.

There is no change to existing finance leases, which will be transitioned at the amounts currently recognised.

Agencies are required to adopt the modified retrospective approach on transition. Under this approach, prior periods are not restated and lease cash flows and discount rates reflect those remaining/in effect on the adoption of AASB 16 (1 January or 1 July 2019).

This will mean that the figures presented, in particular assets and liabilities, will not be comparable to their prior periods and trend analysis will be difficult. Specific disclosures are required on transition, which will go some way to alleviating this.

Given that many of the SA Government's leases sit with DPTI (for accommodation leases) and SAFA (for motor vehicle leases), DTF directed these agencies to provide information for compliance with AASB 16 to their lessees through the Treasurer's Instructions (Accounting Policy Statements).

Given the most significant impact comes from accommodation leases, the rest of my comments will focus on these.

Significant judgement required

Often organisations only truly appreciate the complexity and difficulty of implementing new standards as they progress through the implementation project. There are a wide range of challenges involved in implementing AASB 16.

Lease contracts for accommodation are generally not standardised. Due to the sheer volume of contracts, AASB 16 requires a significant investment in individuals who can effectively assess lease contracts. Significant time is required to analyse contracts. It is important for responsible agencies to determine an appropriate framework for exercising judgement to be applied throughout the organisation.

While DPTI has developed systems to record information and perform the necessary calculations, the consideration of facts and circumstances and judgements required about key inputs cannot be performed by a system. These judgements are critical to the lease calculations resulting in numbers that materially comply with the standard to be used in agencies' financial statements. They are subject to a high degree of estimation uncertainty.

Conclusions made about these key inputs will impact not only at inception of the new standard, but over time as the assumptions and methods of transition unwind over the lease term.

Lease term

Given most accommodation leases include options to extend, the conclusion on lease term is one of the most significant judgement areas impacting on the lease liability and ROU asset brought to account. For example, a lease that has an initial non-cancellable period of five years, with an option to extend for a further five years, will almost double if the preparer makes a judgement that the option to extend is reasonably certain, compared to the alternative. To the extent that such assumptions change over time, the financial statement effects will also change.

In measuring assets and liabilities, lessees (and lessors) must include payments to be made in optional renewal periods only if the lessee will be:

- reasonably certain to exercise an option to extend the lease, or
- reasonably certain not to exercise an option to terminate the lease.

Reasonably certain is a fairly high threshold. However, where assets being leased are specialised in nature, or have had significant investments in leasehold improvements with lives that will extend beyond the non-cancellable term of lease, the options would generally be considered reasonably certain to be exercised. Further, the shorter the initial term of the lease, the more likely it is that an extension option will be exercised. DPTI has used known accommodation strategies when concluding whether the exercise of options is reasonably certain.

Renewals that are reasonably certain to occur may not have been included in the previous disclosures.

Separating non-lease components

AASB 16 requires lessors to separate non-lease components and account for them under other standards. While it provides a practical expedient to allow both lease and non-lease components to be included in lease liability for lessees, DTF has mandated agencies to separate. While some non-lease components may already be separately billed (ie net leases), for gross leases application of this requirement requires identification and estimation of the value of the components included in the rental charge. This is causing significant application issues for preparers of lease information.

DPTI has not yet developed a calculation model for separating non-lease components, meaning that impacts disclosed in notes to the 2018-19 financial statements may be overstated.

Discount rate

The discount rate is determined at the inception of the lease and generally not updated unless certain remeasurement events are triggered.

Because of the transition method chosen, for leases in place at 1 July 2019 the discount rate will be tied to the date of transition rather than the discount rate in effect when the leases were negotiated. Because of the set and forget approach taken in AASB 16, the rate at transition will have a significant impact on both the determination of the lease liability and the resulting interest expense derived by that rate and amortisation of ROU assets until the date the last lease existing at transition of the standard is completed. Over time, the lease obligation will include a mix of discount rates.

On the basis that most SA Government agencies cannot borrow funds in their own right, DTF mandated that agencies use incremental borrowing rates provided by SAFA. These rates reflect the SA Government's cost of borrowing. Rates have been provided for terms varying from one to 30 years, ranging from 1.37% to 2.64%. The weighted average interest rate applied to agencies' leases on transition will be disclosed in 2019-20 financial statements.

Ongoing work required as part of this standard

The complexity and resources required for the ongoing accounting requirements under AASB 16 must not be underestimated. Seemingly innocuous changes to an agreement could be a lease modification, affecting ROU assets and lease liabilities at unexpected times, with major balance sheet consequences.

To appropriately account for leases, constant monitoring and updating is required in the following areas:

- changes in facts and circumstances which trigger reassessment of conclusions about extension options being taken
- remeasurement requirements when a lease is modified, or payments change (eg CPI)
- lease modifications (ie when the scope of consideration for a lease changes from the original terms and conditions).

Systems and processes must be in place to identify the occurrence of such events and determine the appropriate accounting treatment to be applied. Applying the appropriate treatment will require detailed analysis of all the facts and circumstances and significant judgement to be applied. Based on the current accounting policies mandated by DTF, ROU assets will also be required to be subsequently measured at fair value, which will require reassessment at regular intervals.

5.4.4 Disclosures are critical

While quantitative information has been provided about the expected impact in 2018-19 financial statements, a number of issues still need to be resolved by agencies, and until disclosures are provided that support the estimation uncertainty and judgements made, it will be difficult for users to obtain meaningful insights.

Further, the impact assessment will need to be reperformed as DPTI and agencies establish more in-depth accounting policy guidance, and IT and internal control specifications may need to be revisited once assessment has been finalised.

The recognition of lease obligations in the financial statements does not reduce the importance of lease disclosures. To provide meaningful information, financial statements will need to provide information about the nature of the underlying lease arrangements and how management's assumptions and judgements were incorporated – or not incorporated – into the lease liability measurement and the resulting ROU asset. Further, readers need to understand how lease liabilities may be impacted by variable lease payments, and how they will not fluctuate to reflect current economic conditions because of the impact of certain frozen assumptions.

AASB 16 requires qualitative and quantitative disclosures about the future cash outflows to which the lessee is potentially exposed that are not reflected in the measurement of lease liabilities. This information will be helpful to users in estimating the committed future cash flows that have not been included in the measurement of the lease liability. New disclosures will also be required to indicate the extent of concessionary leases in which an agency is lessee.

The transitional and ongoing disclosure requirements are essential for a user's understanding and the time and effort involved should be commensurate. Agencies must not underestimate the resources required or place insufficient emphasis on these disclosures.

5.5 Timing of revenue recognition will change for capital funding or specific purpose funding received from the Commonwealth

The new revenue standards, AASB 15 and AASB 1058, will impact the timing of revenue recognition where grants are received for the purposes of acquiring or constructing assets for use by the entity, or where they include sufficiently specific performance obligations that will only be met over a period of time. Under previous accounting standards these were generally recognised on receipt, however under the new standards revenue will be recognised as the entity acquires or constructs the asset or performance obligations are met. A liability will be recognised until this occurs. The extent of the impact will be dependent on when the Commonwealth makes payments, which is often subject to change.

A number of agencies receive specific purpose funding from the Commonwealth, including National Partnership payments. The funding is often transferred by the Commonwealth to a central fund or entity, primarily DTF or SA Health, before it is transferred to the agency/LHN.

5.5.1 Who is the party to these Commonwealth funding agreements?

Given application of the new revenue standards is likely to result in recognising contract assets or liabilities for these types of arrangements, DTF considered:

- who was responsible for meeting the obligations in the agreement with the Commonwealth
- whether the transfer from the central fund or entity to the agency who will ultimately provide the goods and services (including acquisition or construction of own use assets) is a separate transaction.

In considering the application of the new principal and agent requirements, DTF determined that the Crown is ultimately responsible for meeting the obligations contained in Commonwealth funding agreements, and accordingly is the principal in the arrangement. This means that the Crown, primarily through DTF administered items, will recognise any outstanding contract assets or liabilities in the financial report.

When the money is transferred from the central fund or entity to the agency, it is considered to be a separate transaction which generally falls under AASB 1058. Accordingly, there will be no impact on agencies' financial statements unless they receive funding directly from the Commonwealth or there is a separate agreement with the Crown that contains performance obligations to be met over time.

The agency ultimately receiving the funding will be required to provide the central entity or fund with the information needed for reporting contract assets or liabilities in its financial statements. The central agencies will need to work closely with the agencies affected to develop processes for timely collection of accurate and reliable data.

Further consideration will be given to the application of this position through assessment of each Commonwealth funding arrangement individually to ensure the application of the concept is appropriate in each circumstance.

5.5.2 Impact of the transition method and practical expedients adopted

DTF has finalised the accounting policy choices that must be adopted by agencies in applying AASB 15 and AASB 1058 on transition, including adoption of the modified retrospective approach. Under this approach, prior periods will not be restated and instead adjustments will be made to the opening balance of retained earnings at the date of initial application.

Under this transition method, the standards allow entities to apply them retrospectively only to those contracts that were not completed at the date of transition. DTF has mandated that agencies must not apply this approach, as this would not faithfully represent revenue in the years following initial application.

This means agencies are required to assess all revenue contracts in place on transition, to determine whether there are obligations the entity still needs to satisfy under AASB 15 or AASB 1058 for acquisition or construction of own-use assets. This requires judgement and estimation by agencies which, depending on the agency's circumstances, may be a resource intensive process.

Where performance obligations still need to be met, the agency will adjust the revenue recognised in prior periods through retained earnings and recognise a contract liability at 1 July 2019 for the performance obligations that remain unsatisfied, where funds have been received.

This combination of approaches will result in a perceived double counting of revenue for those performance obligations outstanding on transition. Agencies will need to ensure this is clearly explained in financial reports to avoid misinterpretation of what might otherwise be considered favourable results.

The standards require disclosures to explain the impact, which go some way to addressing the lack of comparability between reporting periods.

5.5.3 The SA Government's response to these standards

Framework for compliance set by DTF

Both revenue standards include options and practical expedients. For the purposes of providing consistent information for whole-of-government reporting, and after considering and weighting the budget implications and costs of compliance, DTF has finalised the options that must be applied by agencies in their financial reporting.

DTF has mandated adoption of all application expedients available in the standards. As a result, agencies must not apply the standards to:

- licences that have a term of 12 months or less
- licences for which the transaction price is less than \$15 000.

The effect of adopting these expedients is that public sector licensors will, in most circumstances, recognise revenue on the same basis as they currently do.

While there has been no change to the accounting requirements for recognising volunteer services by the public sector, the new standards brought new focus to this issue. AASB 1058 allows, as a policy choice, recognition of volunteer services at fair value where they can be measured reliably, regardless of whether or not the services would have been purchased had they not been donated.

DTF has mandated that agencies must not recognise volunteer services if they would not have been otherwise purchased. In the public sector, volunteer services are prominent in emergency services, education and health. While some agencies were able to reliably measure the value of the services provided by volunteers, they could not reliably determine what proportion of those services would have been purchased had they not been donated. Accordingly, volunteer services have not been recognised in financial statements.

Improvements needed in documentation and analysis

At the time of this Report, there are agencies that have not finalised their analysis or conclusions for significant revenue streams received from the Commonwealth Government. These must be prioritised, and expert advice obtained if necessary.

Where conclusions have been reached by agencies, we often found the analysis and documentation lacking. Where this occurred, my auditors could not perform an efficient audit and higher engagement than necessary was required to obtain the evidence we needed. This is an area for improvement and agencies should prioritise developing processes to ensure sufficient documentation is maintained.

Where agencies outsource some of the analysis required, including to Shared Services SA, they must ensure that those experts have all the requisite information. Similarly, those undertaking this type of work must ensure they have clearly advised the client what information is required. We noted that in many cases, conclusions were drawn without considering all the relevant documents, facts and circumstances. For example, applications for funding often form a critical part of the agreement and can significantly affect the conclusions drawn about how the revenue should be accounted for.

While agencies are encouraged to liaise with their auditors, it is essential that agencies have put in the requisite time and effort to understand the requirements, make their own judgements and form conclusions prior, to maintain my independence as required by both legislation and professional standards. Improvement is required in this area.

There is no doubt that the determination of whether there are sufficiently specific performance obligations in an agreement is highly complex and judgemental and, in many cases, will not be evident without a detailed understanding and analysis of agreements together with other relevant facts and circumstances. Agencies must not underestimate the complexity, resources and expertise required to resolve these matters.

Further, although most agencies have indicated that the impact of the new standards will not be material, the disclosure requirements are still extensive. Agencies must not be complacent.

Systems, policies and processes

Government revenue arrangements are generally not standardised. Due to the significant amount of judgement required by the new standards, investment in individuals who can effectively analyse and interpret new or modified contract arrangements will be necessary, together with systems and processes for capturing the necessary information.

The impact and effort required under the new revenue standards will differ from agency to agency, depending on circumstances.

Accountants will need:

- access to all relevant documentation, including the data needed to comply with the disclosure requirements of the standards
- to effectively communicate with business unit staff to acquire further information needed to determine which standard applies to each arrangement and, where applicable, when performance obligations have been met prompting revenue recognition
- to be made aware when there are contract modifications so reassessment can be performed.

Similar to the leasing standard, the revenue standards are not set and forget. Agencies must have systems and processes in place to identify and respond to contract modifications to ensure they are appropriately accounted for. Given modifications can be approved in writing, by oral agreement or implied by customary business practices, this will require understanding not only by those in finance roles.

Accountants will also need to be advised when performance obligations are met so revenue can be recognised, and be provided with sufficient information for any new contracts or funding agreements. While ideally these systems and processes would already be in place given the implementation date has passed, where this is not the case these issues must be prioritised.

These processes will become more difficult where an agency has more complex arrangements and the further removed accountants are from relevant business operations, for example in large agencies and where Shared Services SA is responsible for the agency's accounting function. These difficulties should be anticipated and effective solutions implemented as soon as possible to avoid delays in financial statement preparation.

5.5.4 Significant increase in disclosures required

Because comparatives will not be restated, agencies are required to disclose in a note, what revenue would have been reported in the 2019-20 Statement of Comprehensive Income had the new standards not been applied. This provides comparability with the figures reported in the financial statements for the comparative year. Explanations for differences between those and the actual numbers reported must also be included. This will effectively require agencies to maintain two sets of systems and accounting records in 2019-20.

For this to be done effectively and efficiently, processes should already be in place to capture this information.

While most agencies have indicated the adoption of the new revenue standards will not have a material impact on the measurement and timing of revenue, the disclosure requirements of the standards will be extensive. They may require agencies to change the way they present items in the statements and will almost certainly enhance the volume of disclosures needed to meet the disclosure objectives, particularly given the amount of judgement and estimation that is likely to be required.

This will include disclosure of both qualitative and quantitative information about:

- its contracts with customers
- any practical expedients applied
- when performance obligations are typically satisfied
- significant payment terms, for example when payment is typically due
- the nature of the goods or services that have been promised, including whether the agency is acting as an agent
- categories of revenue that depict how the nature, amount, timing and uncertainty of revenue and cash flows are affected by economic factors
- contract assets and contract liabilities
- the significant judgements, and changes in the judgements, made in applying the standard.

Agencies will need to use judgement to determine the level of detail that is required to meet the above objectives. This cannot be achieved through the use of a model.

5.6 Valuations required for service concession assets as a matter of priority

AASB 1059 does not treat public private partnership arrangements as leases. It requires the assets and liabilities to be recognised in the balance sheet and valued at current replacement cost when the SA Government gains control of them, generally taken to be when the project becomes operational. Any intangible assets, such as intellectual property rights, must be included in the aggregate of project assets.

Service concession arrangements captured by AASB 1059 are contracts where a party external to government is compensated for providing public services either through the assets it provides, or that are already held by the government. This standard applies where there is government control or third-party regulation of what services are provided, who services are provided to and at what price. The operator must be responsible for managing at least some of the public services provided.

While application of this standard has been deferred to 30 June 2021, valuation of any service concession assets is still required at 1 July 2019 using a cost approach. To date, the only arrangement where DTF has confirmed application of AASB 1059 relates to the Land Services Group, which transferred from DTF to DPTI in 2018-19.

DTF is monitoring several other SA Government arrangements and future projects but is yet to reach conclusions. Major arrangements under consideration include the arrangements with community housing providers and public private partnerships linked to hospitals and schools.

DTF needs to consider valuation issues for service concession assets as a priority. In 2017, Treasurer's Instructions were varied so that the RAH could be carried at cost, rather than fair value. This was necessary because of the complexity of the arrangement and the need to have a government policy about which costs should be included when considering how the market would value such an asset.

Some of these issues are under consideration by standard setters. Accordingly, DTF has yet to set policy because a lack of settled application guidance from standard setters means that any government policy could introduce changes that may not align with forthcoming guidance.

In June 2018 and again in 2019 the Treasurer approved further variations so the RAH could continue to be held at cost, as government policy is still to be finalised.

It has not yet been determined whether a number of arrangements will be within the scope of AASB 1059. However, it is essential that this and all other arrangements being considered are resolved urgently, as valuation instructions will need to be drafted for community housing assets (should they be determined to be service concession arrangements) and the land services databases. There is a real risk that valuations will not be obtained for the associated assets in these arrangements in time to support application at 1 July 2019 (without the use of hindsight).

There are also potential increases in liabilities that relate to these arrangements depending on how they have been accounted for in the past. At the time of this Report, the complexities of accounting for grants of rights to operator (GORTO) liabilities on transition is still being discussed with the Australian Accounting Standards Board to ensure that anomalous outcomes do not result from applying the transitional requirements.

6 Local government – Examination update

6.1 Background

Section 32(1) of the PFAA gives the Auditor-General the discretion to examine the:

- accounts of a publicly funded body and the efficiency, economy and effectiveness of its activities
- accounts relating to a public funded project and the efficiency, economy and effectiveness of the project
- accounts relating to a local government indemnity scheme and the efficiency, economy and effectiveness of the scheme.

Section 32 of the PFAA also enables the Treasurer or the Independent Commissioner Against Corruption to request the Auditor-General to conduct an examination under section 32(1).

A publicly funded body includes a council constituted under the *Local Government Act 1999*, including a subsidiary and a regional subsidiary of a council. In effect, the statutory remit of the Auditor-General extends to the local government sector.

Section 32 provides a broad scope and discretionary power of examination by the Auditor-General. The examination of the accounts and activities of a publicly funded body, project or local government indemnity scheme may relate to a review of a diverse range of matters.

Under the PFAA, the Auditor-General is not the auditor of any council. I therefore do not provide an audit opinion on the financial reports of the councils and the schemes, or on the controls exercised by each council. These audit opinions are provided by the auditors appointed by each council and for each scheme.

The PFAA requires a report to be prepared after making an examination under section 32 and delivered to the Parliament. All completed examinations for the local government sector will therefore be separately reported.

6.2 Summary of section 32 examination – Examination of the District Council of Coober Pedy

In 2018-19 we completed and reported on an examination of the District Council of Coober Pedy (the Council). This examination was conducted from a request from the then Treasurer, the Hon Tom Koutsantonis MP, dated 1 May 2017, to examine the accounts of the Council under section 32(1)(a) of the PFAA.

Our examination of the Council was based on its accounts for the years from 2011-12 to 2016-17. I concluded the following:

- The Council's financial position, and particularly its current level of indebtedness, was unsustainable. The Council could not meet its operational cash flows and had no realistic prospect of repaying its indebtedness from its own resources.

The Council's financial performance was inadequate. It reported losses in 2011-12, 2013-14, 2014-15 and 2015-16 that were not budgeted for. There was no evidence the Council considered the impact of these losses until it was in financial crisis. The Council had from time to time developed planned responses that were, in my opinion, reasonable, but it had not demonstrated an ability to implement the required actions.

- The Council's accounting systems and records were significantly deficient and unable to support effective financial management of the Council's operations.

I further concluded the Council failed to comply with key aspects of the strategic and financial management requirements of the *Local Government Act 1999* during the period 1 July 2014 to 30 June 2017.

In my opinion, the Council would only successfully respond to its current financial position if it was able to recruit and retain a chief executive and finance manager who are appropriately qualified and experienced.

After our Report was tabled, in January 2019 the Minister for Transport, Infrastructure and Local Government, Stephan Knoll, announced that an administrator had been appointed for the Council after it was declared to have defaulted. The Minister made this recommendation based on an extensive Ombudsman's Report finalised in July 2018, which demonstrated serious failings and irregularities at the Council.

7 Summary of selected financial disclosures

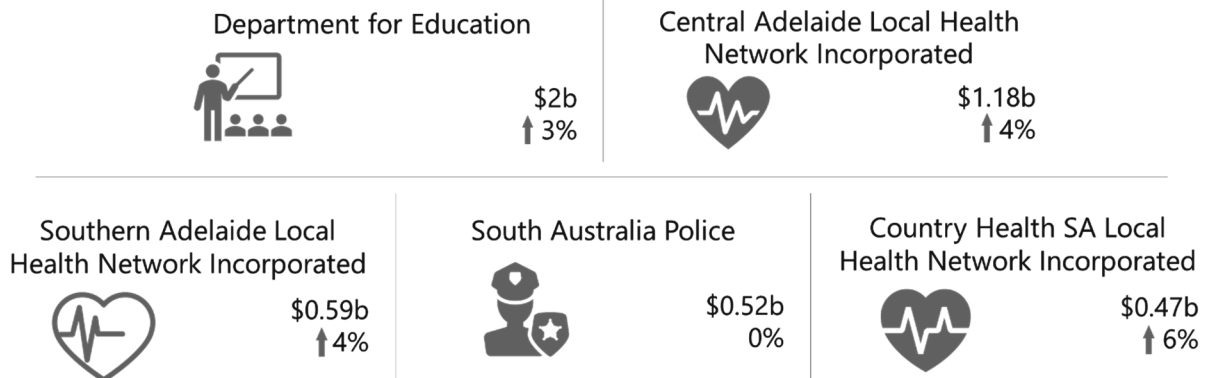
The following selected financial disclosures are taken from the published financial reports of the agencies listed in section A.1 of Annexure 1. The data does not include all public sector agencies. More details on these disclosures are in the individual published financial reports.

This information is provided to give an overview of the level of financial activity for each area. It represents the more material balances in financial reports or items that are typically of public interest. While audited, audits of financial reports provide assurance that there is not material error. An audit does not ensure complete consistency in the transactions that agencies include in these items.

7.1 Salaries and wages expense



Top 5 agencies



7.2 Remuneration of employees disclosures

The Treasurers Instructions (Accounting Policy Statements), Schedule 1, APS 119.D requires public authorities to disclose an explanatory note about employees whose normal remuneration is equal to or greater than the base executive remuneration level for the year (\$151 001 in 2018-19).

Disclosure includes the number of employees whose total remuneration paid or payable exceeds the benchmark, within \$20 000 bands, and the aggregate of the remuneration paid or payable for those employees.



\$1.3b


Total remuneration of employees disclosure in 2018-19



5.6%


Top 5 agencies

Central Adelaide Local Health Network Incorporated




\$357m ↑6%
1,226 employees

Southern Adelaide Local Health Network Incorporated



\$178m ↑9%
632 employees

Northern Adelaide Local Health Network Incorporated



\$119m ↑10%
420 employees

South Australia Police



\$100m ↓10%
563 employees

Department for Education



\$81m ↑14%
453 employees

7.3 Targeted voluntary separation packages

The Treasurer's Instructions (Accounting Policy Statements), Schedule 1, APS 119.C requires public authorities to disclose an explanatory note with information about TVSPs.

Disclosure includes the number of employees paid a TVSP and the amount of those TVSPs paid.



\$126m

Total targeted voluntary separation packages in 2018-19



\$126m (\$38m)
1,544 employees (499)

Top 5 agencies

Department of Human Services



\$27m (\$2m)
345 employees (28)

Department for Education



\$13m (\$1m)
145 employees (12)

Department for Environment and Water



\$10m (\$0.5m)
119 employees (5)

Department for Correctional Services



\$9m (\$0m)
126 employees (0)

South Australian Housing Trust



\$8m (\$0m)
94 employees (0)

7.4 Employee benefits liabilities

Employee benefits liabilities comprise annual and long service leave entitlements accrued by employees.

The annual leave liability is mainly a short-term employee benefit measured at nominal value. Long service leave is a long-term employee benefit estimate measured as the present value of expected future payments for services provided by employees up to the end of the reporting period. The present value will change from year to year if market yields or other significant assumptions change. This year there was a decrease in the discount rate used, resulting in an increase in reported employee benefits liabilities.




\$3.1b


Total employee benefits liabilities in 2018-19



9%


Top 5 agencies


Department for Education

 \$682m
 ↑6%

Central Adelaide Local Health Network Incorporated

 \$508m
 ↑17%

South Australia Police

 \$292m
 ↑7%

Southern Adelaide Local Health Network Incorporated

 \$266m
 ↑19%

Country Health SA Local Health Network Incorporated

 \$182m
 ↑13%






7.5 Workers compensation and additional compensation

The workers compensation provision is an actuarial estimate of the outstanding liability as at 30 June 2019 provided by a consulting actuary engaged through the Office for the Public Sector. The provision is the estimated cost of ongoing payments to employees as required under current legislation.

As at 30 June 2018, following changes to relevant public sector enterprise agreements, most agencies recognised an additional compensation provision for continuing benefits to workers who have suffered eligible work-related injuries and whose entitlements have ceased under the *Return to Work Act 2014*. 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.



Top 5 agencies

<p>South Australia Police</p>  <p>\$121m 0%</p>	<p>SA Fire and Emergency Services Commission</p>  <p>\$102m ↑ 35%</p>	
<p>Department for Education</p>  <p>\$81m ↑ 39%</p>	<p>Southern Adelaide Local Health Network Incorporated</p>  <p>\$43m ↑ 10%</p>	<p>Department for Correctional Services</p>  <p>\$30m ↑ 7%</p>

7.6 Outsourced/Service contracts

Examples of outsourced contracts include: bus service contracts; major infrastructure service contracts; claims management (claim agents); investment and insurance fees; plant operations and maintenance; and internal payments to Shared Services SA.



\$1.9b

Total outsourced/service contracts in 2018-19



2%

Top 5 agencies



Department of Planning, Transport and Infrastructure

\$471m
↑ 18%

Department for Education



\$263m
↓ 2%

South Australian Water Corporation



\$219m
↑ 18%

Department for Child Protection



\$200m
↓ 9%

South Australian Housing Trust



\$123m
↓ 7%

7.7 Contractors and temporary staff

Contractors and temporary staff expenses include agency nursing, IT and private legal practitioners.



\$317m

Total contractors and temporary staff in 2018-19



0%

Top 5 agencies

Central Adelaide Local Health Network Incorporated



\$66m
↓ 2%

Department for Education



\$35m
↑ 12%

Department for Health and Wellbeing



\$27m
↓ 2%

TAFE SA



\$24m
↑ 10%

Northern Adelaide Local Health Network Incorporated



\$19m
↑ 7%

7.8 Consultants

The Treasurer’s Instructions (Accounting Policy Statements), Schedule 1, APS 101.J requires public authorities to disclose in the notes the expenses incurred as a result of engaging consultants (as reported in the Statement of Comprehensive Income).



\$28.9m

Total consultants in 2018-19



13.5%

Top 5 agencies

Central Adelaide Local Health Network Incorporated



\$4m
↑ 218%

Department for Health and Wellbeing



\$3m
↓ 26%

Department for Energy and Mining



\$2m

Motor Accident Commission



\$2m
↓ 33%

Department for Education



\$2m
↓ 32%

8 Summary of key items in the Treasurer's statements

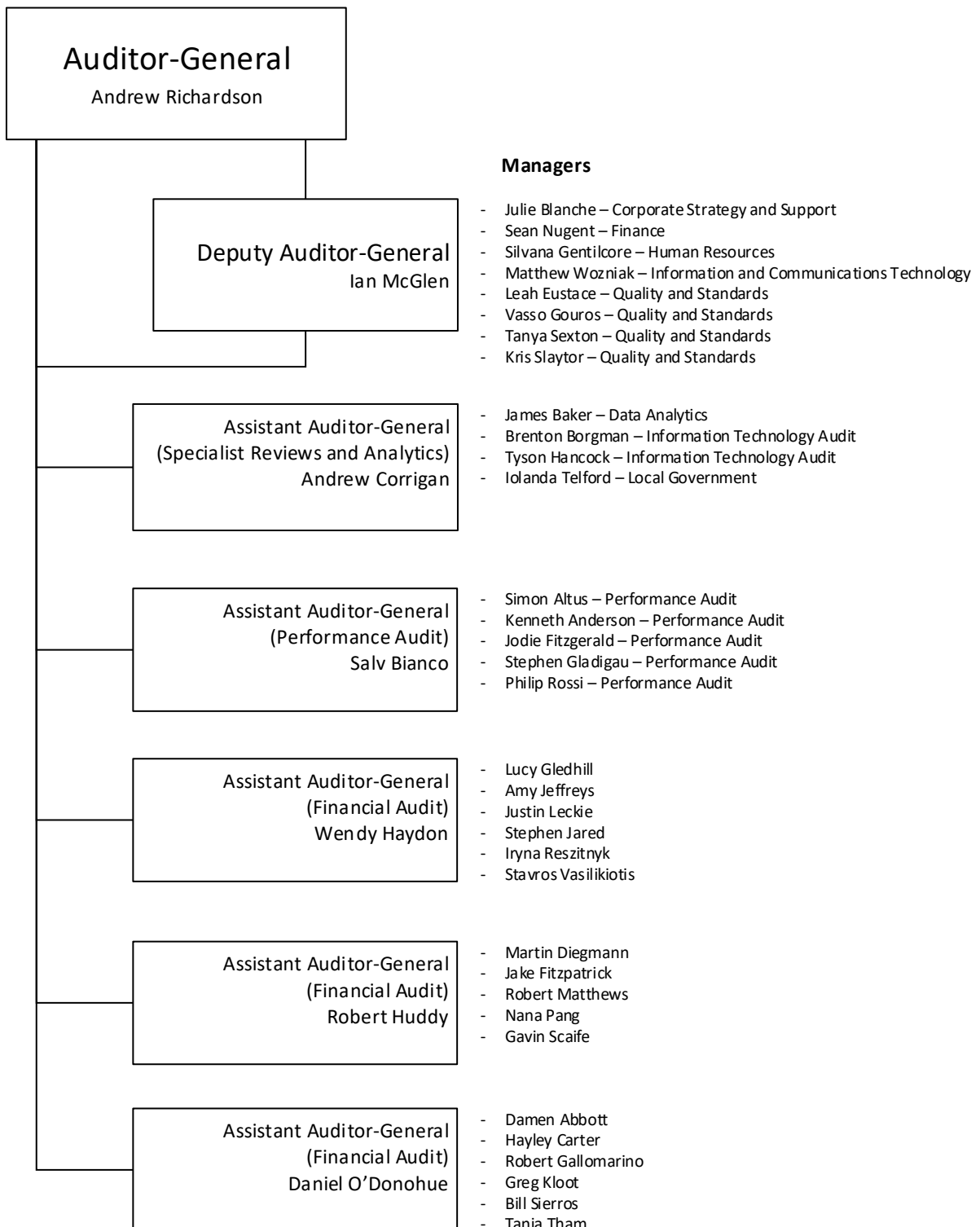
Under section 36(1)(4) of the PFAA I will publish the Treasurer's statements on the Auditor-General's Department website (www.audit.sa.gov.au).

The following summarises the Consolidated Account outcome.

8.1 Summary of the Consolidated Account for the year ended 30 June 2019

	Budget \$	Actual \$
Receipts		
Taxation	4 010 691 000	3 921 302 812
Commonwealth general purpose grants	6 887 200 000	6 684 426 789
Commonwealth specific purpose grants	212 995 000	212 526 557
Commonwealth National Partnership payments	262 992 000	293 336 539
Contributions from state undertakings	345 606 000	410 905 722
Fees and charges	495 045 000	534 566 415
Recoveries	142 745 000	283 870 568
Royalties	265 544 000	299 418 345
Other receipts	188 699 000	162 326 354
Total receipts	12 811 517 000	12 802 680 101
Payments		
Appropriation Act	14 486 285 000	14 687 599 080
Specific appropriation authorised in various Acts	114 062 000	120 279 869
Total payments	14 600 347 000	14 807 878 949
Consolidated Account deficit	1 788 830 000	2 005 198 848

9 Management structure of the Auditor-General's Department



Annexure 1 – Agencies audited whose financial statements will be published on the Auditor-General’s Department website

The PFAA requires me to publish on a website the audited financial statements of all public authorities. This is a significant accountability measure that ensures they will all be available centrally.

In addition, the PFAA allows me to publish other documents on that website. Other documents would include the financial statements of agencies that are not public authorities.

Under section 36(1)(4) of the PFAA I will publish the financial statements of all agencies audited by me on the Auditor-General’s Department website (www.audit.sa.gov.au).

A.1 Agency financial statements to be published immediately after the Annual Report is tabled

The following agencies are included in Part C and their financial statements will be published on our website immediately after the Annual Report is tabled.

Adelaide Festival Centre Trust
Adelaide Oval SMA Limited
Adelaide Venue Management Corporation
Attorney-General’s Department
Auditor-General’s Department
Central Adelaide Local Health Network Incorporated
Child Protection – Department for
Correctional Services – Department for
Country Health SA Local Health Network Incorporated
Courts Administration Authority
Education – Department for
Energy and Mining – Department for
Environment Protection Authority
Environment and Water – Department for
Flinders University
Health and Wellbeing – Department for
HomeStart Finance
Human Services – Department of
Independent Commissioner Against Corruption
Innovation and Skills – Department for
Lifetime Support Authority of South Australia
Motor Accident Commission
Northern Adelaide Local Health Network Incorporated
Planning, Transport and Infrastructure – Department of
Premier and Cabinet – Department of the
Primary Industries and Regions – Department of
Public Trustee

Return to Work Corporation of South Australia
SA Ambulance Service Inc
South Australia Police
South Australian Fire and Emergency Services Commission
South Australian Government Financing Authority
South Australian Housing Trust
South Australian Superannuation Board
South Australian Superannuation Scheme
South Australian Tourism Commission
South Australian Water Corporation
Southern Adelaide Local Health Network Incorporated
Southern State Superannuation Scheme
Super SA Retirement Investment Fund
Superannuation Funds Management Corporation of South Australia
TAFE SA
Treasury and Finance – Department of
Treasurer’s statements
University of Adelaide
University of South Australia
Urban Renewal Authority
Women’s and Children’s Health Network Incorporated

A.2 Agency financial statements to be published after the audit is completed

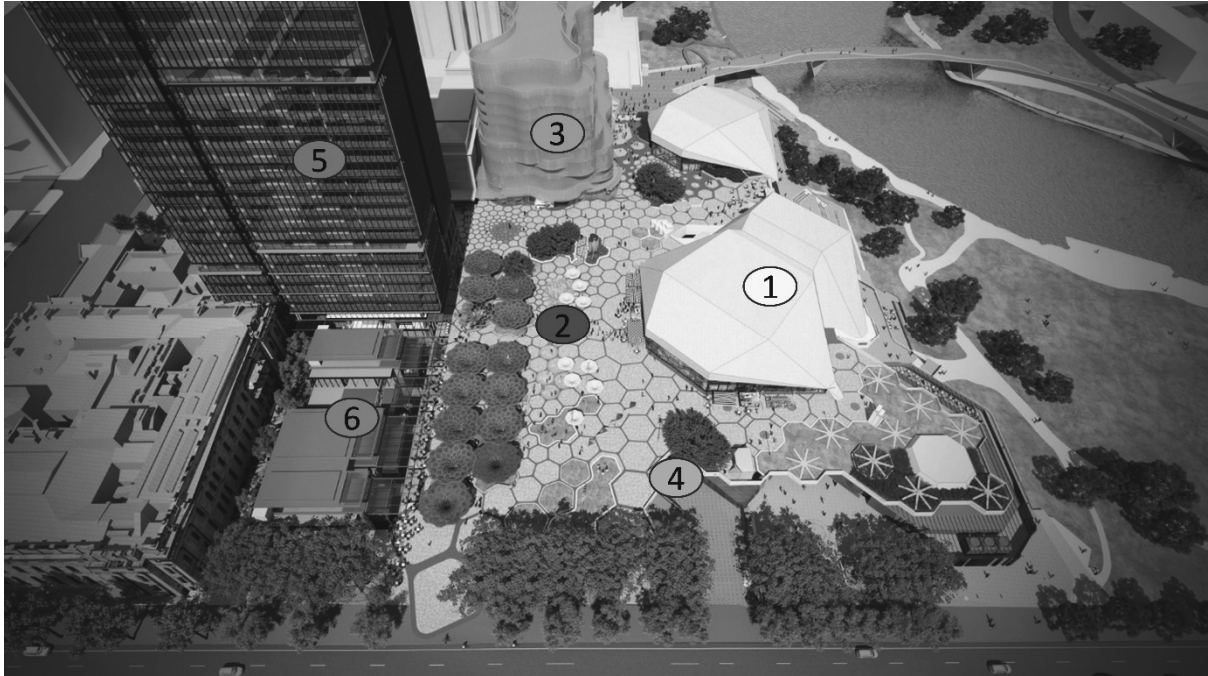
The financial statements of the following agencies that are not reported in Part C of my Annual Report will be published as soon as reasonably practicable on our website after their audit is completed.

Aboriginal Lands Trust
Adelaide and Mount Lofty Ranges Natural Resources Management Board
Adelaide Cemeteries Authority
Adelaide Festival Corporation
Adelaide Film Festival
Agents Indemnity Fund
Alinytjara Wilurara Natural Resources Management Board
Art Gallery Board
Australian Children’s Performing Arts Company
Australian Energy Market Commission
Board of the Botanic Gardens and State Herbarium
Carrick Hill Trust
Coast Protection Board
Construction Industry Training Board
CTP Regulator
Dairy Authority of South Australia
Defence SA
Distribution Lessor Corporation
Dog and Cat Management Board
Dog Fence Board
Electoral Commission of South Australia

Electricity Industry Superannuation Scheme
Essential Services Commission of South Australia
Eyre Peninsula Natural Resources Management Board
Generation Lessor Corporation
Governors' Pensions Scheme
Green Industries SA
Health Services Charitable Gifts Board
History Trust of South Australia
House of Assembly
Independent Gambling Authority
Independent Gaming Corporation Ltd
Infrastructure SA
Investment Attraction South Australia
Joint Parliamentary Service
Judges' Pensions Scheme
Judicial Conduct Commissioner
Kangaroo Island Natural Resources Management Board
Legal Services Commission
Legislative Council
Libraries Board
Local Government Finance Authority of South Australia
Lotteries Commission of South Australia
Maralinga Lands Unnamed Conservation Park Board
Minister for Primary Industries and Regional Development – Adelaide Hills Wine Industry Fund
Minister for Primary Industries and Regional Development – Barossa Wine Industry Fund
Minister for Primary Industries and Regional Development – Citrus Growers Fund
Minister for Primary Industries and Regional Development – Clare Valley Wine Industry Fund
Minister for Primary Industries and Regional Development – Eyre Peninsula Grain Growers Rail Fund
Minister for Primary Industries and Regional Development – Grain Industry Fund
Minister for Primary Industries and Regional Development – Grain Industry Research and
Development Fund
Minister for Primary Industries and Regional Development – Langhorne Creek Wine Industry Fund
Minister for Primary Industries and Regional Development – McLaren Vale Wine Industry Fund
Minister for Primary Industries and Regional Development – Riverland Wine Industry Fund
Minister for Primary Industries and Regional Development – South Australian Apiary Industry Fund
Minister for Primary Industries and Regional Development – South Australian Cattle Industry Fund
Minister for Primary Industries and Regional Development – South Australian Grape Growers
Industry Fund
Minister for Primary Industries and Regional Development – South Australian Pig Industry Fund
Minister for Primary Industries and Regional Development – South Australian Sheep Industry Fund
Museum Board
Native Vegetation Fund
Northern and Yorke Natural Resources Management Board
Office for Recreation, Sport and Racing
Office of the Commissioner for Public Sector Employment
Office of the Industry Advocate
Office of the National Rail Safety Regulator
Office of the South Australian Productivity Commission
Outback Communities Authority
Parliamentary Superannuation Scheme
Planning and Development Fund
Police Superannuation Scheme

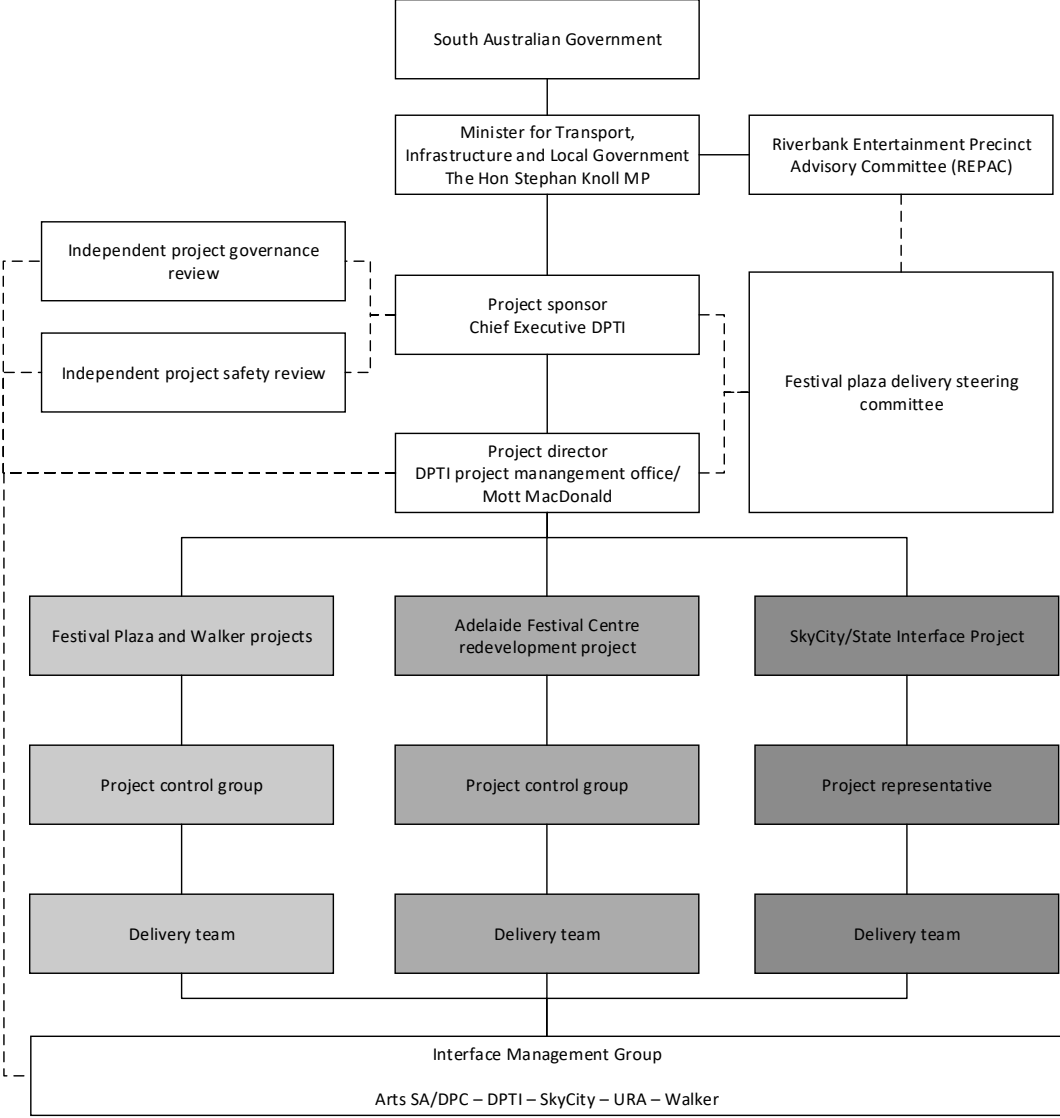
Professional Standards Council
Rail Commissioner
Residential Tenancies Fund
Retail Shop Leases Fund
Riverbank Authority
Rural Industry Adjustment and Development Fund
SA Metropolitan Fire Service Superannuation Scheme
SACE Board of South Australia
Second-hand Vehicles Compensation Fund
Small Business Commissioner
South Australian Ambulance Service Superannuation Scheme
South Australian Arid Lands Natural Resources Management Board
South Australian Country Arts Trust
South Australian Country Fire Service
South Australian Film Corporation
South Australian Forestry Corporation
South Australian Local Government Grants Commission
South Australian Mental Health Commission
South Australian Metropolitan Fire Service
South Australian Murray-Darling Basin Natural Resources Management Board
South Australian State Emergency Service
South East Natural Resources Management Board
South Eastern Water Conservation and Drainage Board
State Opera of South Australia
State Planning Commission
State Procurement Board
State Theatre Company of South Australia
Stormwater Management Authority
StudyAdelaide
Super SA Select Fund
Teachers Registration Board of South Australia
TechInSA
Trade, Tourism and Infrastructure – Department for
Transmission Lessor Corporation
West Beach Trust

Annexure 2 – Adelaide Festival Centre precinct upgrade: design overview and forecast project completion dates



1. Redevelopment of Festival Centre Foyers and Northern Walkway (Completed 2018).
2. Upgraded public realm and event space (Forecast completion: late 2022).
3. Expansion of SkyCity Casino including hotel (Forecast completion: October 2020).
4. Festival Centre car park developed by the Walker Corporation (Forecast completion: late 2020).
5. Office tower developed by the Walker Corporation (Forecast completion: 2022).
6. Retail/Restaurant area developed by the Walker Corporation (Forecast completion: 2022).

Annexure 3 – Adelaide Festival Centre precinct upgrade governance structure: August 2019



Annexure 4 – Acronyms and abbreviations

A number of acronyms and abbreviations are used throughout this Report. Most are summarised here.

AFC	Adelaide Festival Centre
AGFMA	Across government facilities management arrangements
CALHN	Central Adelaide Local Health Network Incorporated
CHSALHN	Country Health SA Local Health Network Incorporated
CPI	Consumer price index
DA	Development agreement
DEM	Department for Energy and Mining
DEW	Department for Environment and Water
DHS	Department of Human Service
DHW	Department for Health and Wellbeing
DIS	Department for Innovation and Skills
DoAFAA	Deed of Acknowledgement, Further Agreement and Amendment
DPC	Department of the Premier and Cabinet
DPTI	Department of Planning, Transport and Infrastructure
DTF	Department of Treasury and Finance
EOI	Expression of interest
ESCOSA	Essential Services Commission of South Australia
Festival Centre PCG	Adelaide Festival Centre Redevelopment project control group
FTE	Full-time equivalent
HC Act	<i>Health Care Act 2008</i>
KPIs	Key performance indicators
LHNs	Local health networks
LSA	Lifetime Support Authority of South Australia
LSSA	Land Services SA
MAC	Motor Accident Commission
NALHN	Northern Adelaide Local Health Network Incorporated
NDIS	National Disability Insurance Scheme
NICO	National Indemnity Corporation
PCG	Project control group
PFAA	<i>Public Finance and Audit Act 1987</i>
PIRSA	Department of Primary Industries and Regions
PPR	Portfolio Performance Report
RAH	Royal Adelaide Hospital
REPAC	Riverbank Entertainment Precinct Advisory Committee
RHP	Repat Health Precinct
ROU	Right-of-use
RTWSA	Return to Work Corporation of South Australia

RTW Scheme	Return to Work Scheme
SA Water	South Australian Water Corporation
SAAS	SA Ambulance Service Inc
SAFA	South Australian Government Financing Authority
SAHT	South Australian Housing Trust
SALHN	Southern Adelaide Local Health Network Incorporated
SAPC	South Australian Productivity Commission
SARMS	South Australian River Murray Sustainability
SASB	South Australian Superannuation Board
SCAP	State Commission Assessment Panel
SCSS	Statewide Clinical Support Services
SPB	State Procurement Board
TVSP	Targeted voluntary separation package
URA	Urban Renewal Authority
Walker PCG	Walker Projects project control group
WCHN	Women's and Children's Health Network Incorporated

