

# Key Audit Themes

2015–16



**VAGO**

Victorian Auditor-General's Office



**Helping you to use the key audit themes**

We regularly give tailored presentations on the key audit themes to specific sectors or interests. If you want us to present to your organisation, email us at [ag@audit.vic.gov.au](mailto:ag@audit.vic.gov.au).

## Introduction

Audits are designed to help agencies understand risks and challenges and help them to improve performance, governance and accountability.

All of our audit reports are publicly available. Despite this, agencies do not always take the opportunity to learn from the experience of others.

To help agencies benefit from insights from our wider audit program, each year we look through our reports to see whether similar findings appear across different reports. If a matter comes up in several audits, it is likely to be a widespread theme of interest to a range of agencies.

## Key audit themes for 2015–16

Seven themes arise from our 2015–16 audit reports, each drawing on a number of common findings:

- governance and oversight
- effective leadership
- managing information
- implementation and delivery
- measuring and reporting performance
- monitoring and managing risks to financial sustainability
- stakeholder engagement.

This year, about 20 per cent of findings in our audit reports were positive—higher than usual. Where appropriate, we have reflected this in the themes. However, as our audit program is designed to address areas of risk for the public sector, audit findings more often cover areas to improve than affirm positive practice.

## How to use the themes

Each theme includes a high-level summary and detail on what we have seen and why it is problematic. We include excerpts from audit reports published between July 2015 and June 2016 to illustrate our findings and help you to identify reports that you may want to read in more detail. We present specific instances of good management, where available. It is important to remember that practices may have improved since our reports were tabled.

The self-assessment questions for each theme give a practical starting point for assessing how your agency fares in relation to that theme. People use the themes in different ways:

- Boards and audit committees can ask managers to tell them how their organisations are addressing the risks identified in the themes.
- Risk managers can use the themes to help identify potential risks to address in their organisation's risk management plans.
- Managers can consider the themes when designing new programs.
- Internal auditors can use the themes to help them to choose what operational areas to audit each year.
- Human resources teams can use the themes to identify areas where further training for staff may be useful.

# Governance and oversight



Governance arrangements include the structures, processes and practices that an agency uses to achieve its objectives. Poor governance arrangements make it more difficult for an agency to operate effectively and blur accountability for actions and outcomes. A long-running challenge in the public sector, the past year's audits found some areas of positive performance, as well as persistent shortcomings.

## Governance frameworks

There were encouraging improvements in relation to governance frameworks. We found that several agencies have worked to more clearly and formally define their governance arrangements.

*'Over the past six months the Department of Economic Development Jobs Transport & Resources (DEDJTR) has put a governance framework in place to ensure that there are consistent assumptions underpinning the transport modelling and economic appraisal of projects, and that these have been properly applied.'*

— *Applying the High Value High Risk Process to Unsolicited Proposals* (August 2015).

However, many aspects remain to be improved. We found that several governance frameworks were unclear or inadequate. The task of appropriately governing collaborative operations continues to be challenging, particularly for information-sharing.

*'[The Department of Education and Training's (DET)] governance framework is deficient and consequently undermines the application of its planning framework ... DET's reliance on committees makes it difficult to identify responsible executive officers and diminishes their accountability. It is impossible to know whether these committees are operating effectively as it is often unclear who oversees their performance, how decisions are made, who is attending and how often they meet.'*

— *Department of Education and Training: Strategic Planning* (October 2015).

## Oversight of delegated or contracted activity

In 2015–16, we continued to find significant shortcomings in how senior managers and agencies oversee and monitor, especially in outsourced or 'arm's length' arrangements.

*'In some cases, DET relies on system authorities to administer and oversee grants made to schools. In effect, this means that the system authorities oversee themselves ... DET does not oversee or monitor system authorities to assure itself that grants are used for their intended purpose or achieving the intended outcomes.'*

— *Grants to Non-Government Schools* (March 2016)

*'While there have been overall improvements during the year in how outsourced IT environments are managed, additional improvements are still required. There is a need to increase awareness of ownership and obligations relating to these outsourced environments, including assessing the reliability and quality of audits conducted over an entity's outsourced environment and assessing the impact of any control weaknesses on the entities' control environment.'*

— *Financial Systems Controls Report: Information Technology 2014–15* (October 2015)

## Responding to recommendations and reviews

A key aspect of governance is having systems in place to ensure that actions take place in response to audits and other reviews. We found positive signs of responsiveness to our recommendations.

*'The majority of agencies, 82 per cent, reported assigning recommendations to responsible individuals. Nearly half of the individuals assigned to monitor and report on specific recommendations held executive management positions. This greater accountability for the timely completion of recommendations is reflected in the completion rates for agencies that took this approach.'*

—*Responses to Performance Audit Recommendations 2012–13 and 2013–14* (December 2015)

*'The department has initiated adequate action to address all of the recommendations in our 2014 report. In most instances, this has meant addressing systemic issues that require a long time to overcome.'*

—*Follow up of Residential Care Services for Children* (June 2016)

However, we found several examples where the effort was not enough to address identified problems. Some agencies were particularly slow to address recommendations or did not address all recommendations. In other instances, the action taken did not lead to effective change. Audit committees did not always fulfil their role in seeking assurance that recommendations were being addressed.

*'The department's audit committee has processes in place to assess progress in implementing recommendations from other external reports. However, it is not assessing the impact these actions are having. As a consequence, neither the department nor the audit committee can be assured that the effort being put into addressing the issues underlying the recommendations is effective.'*

—*Follow up of Managing Major Projects* (August 2015)

## Complying with regulatory frameworks

Some agencies did not comply with mandatory requirements, mainly in relation to financial management and accountability. We found several instances where agencies did not comply with the *Financial Management Act 1994*—the public sector's framework for financial administration, accountability and

reporting—and the Standing Directions and standards that sit under this Act. More broadly, some agencies did not comply with mandated processes and policies, or fulfil reporting obligations.

*'2014–15 was the first financial year public hospitals were required by Standing Direction 4.5.6 Treasury Risk Management of the Financial Management Act 1994, to invest non-operational funds of greater than \$2 million with the state's treasury bodies, rather than investing in deposit institutions with a lower than AAA credit rating. Seventeen public hospitals did not comply with this requirement.'*

—*Public Hospitals: 2014–15 Audit Snapshot* (November 2015)

*'Agencies also fall well short of fully complying with their obligations under Part II of the Freedom of Information Act 1982, to publish registers of the information they hold.'*

—*Access to Public Sector Information* (December 2015)

## Self-assessment questions

- 1 What assurance does my agency have that its governance arrangements are appropriate, clear and well understood?
- 2 How does my agency monitor activity that it is responsible for or that it has delegated or contracted to others?
- 3 How does my agency know whether it is identifying, managing and monitoring all relevant risks?
- 4 Does my agency have a system in place to monitor action on recommendations and reviews in a way that ensures that action is timely and meaningful and addresses the core problem?
- 5 Have we done enough to address the problems we already know about?
- 6 Does my agency have assurance over how it complies with relevant legislation and regulations?

# Effective leadership



Leadership is a critical element of an organisation. The approach of public sector leaders to decision-making and culture has a major influence on their organisations. Although audits rarely set out to consider the effectiveness of leadership, several reports highlighted the significant role of leadership within the programs and activity they assessed.

## Guidance and direction

There were instances of leadership showing the way and being the source of improvement, as well as instances where agencies failed to effectively set direction and drive change.

*'Systemic failures by [the Department of Health & Human Services] DHHS—some of which were identified over a decade ago in our 2005 audit—collectively indicate that DHHS is not effectively providing leadership or oversight of patient safety.'*

**—Patient Safety in Victorian Public Hospitals (March 2016)**

Operational guidance from the centre on key activities or processes was often unclear, inadequate or absent, although we found some examples of good guidance material.

## Creating a positive and ethical culture

Leaders are role models for an organisation's behaviour and actions. Leaders who model appropriate conduct and behaviour will contribute to a positive culture. We found problems with culture—how members of an organisation approach their work and interact with each other—that were concerning. Leaders have opportunities to make a difference to these matters, by driving cultural change.

*'There is widespread fear among staff and a reluctance to raise issues or make formal complaints because of the perceived repercussions of doing so.'*

**—Bullying and Harassment in the Health Sector (March 2016)**

*'There needs to be cultural change across Victoria Police, supported by strong leadership for this initiative to succeed.'*

**—Follow up of Asset Confiscation Scheme (June 2016)**

## Frank and fearless advice

For leaders to fulfil their roles and make informed decisions, they need frank, impartial and timely advice from the public sector. This is enshrined in the values and principles that guide the public sector, with ‘providing frank, impartial and timely advice to government’ listed as a key value in the *Public Administration Act 2004*. We found some positive examples where decision-makers were supported well with advice.

*‘Advice provided to government to support decisions on the establishment and rollout of the [Protective Services Officer (PSO)] ... program was comprehensive. The report back to government following the first 18 months of the program was focused on the government’s priorities at the time, but it also advocated for changes to the PSO program in order to improve efficiency and effectiveness and to reduce costs. While government chose not to follow this advice, the options presented were comprehensive and soundly based.’*

—*Public Safety on Victoria’s Train System* (February 2016)

However, we found several instances where this principle was not fulfilled across aspects of public sector administration including for major policies and infrastructure decisions. Similarly, we found shortcomings in advice or information provided to oversight bodies such as audit committees.

*‘Over the life of this costly and complex project, advice to government did not always meet the expected standard of being frank and fearless. This highlights a risk to the integrity of public administration that needs to be addressed.’*

—*East West Link Project* (December 2015)

*‘The application of the [High Value High Risk] ... process to CityLink Tulla had significant gaps which [the Department of Treasury and Finance] ... needs to address for similar proposals in the future. The lack of sufficient information on the project’s benefits, the absence of a full funding analysis and weaknesses in the approach to stakeholder engagement are fundamental gaps which compromise the quality of advice government is entitled to receive.’*

—*Applying the High Value High Risk Process to Unsolicited Proposals* (August 2015)

*‘Public sector leadership needs to be focussed on creating a sense of public trust for government’s stewardship role. This public trust needs to be a network of trust: Citizens must be able to trust public institutions to defend their interests. Politicians and ministers must be able to trust that the public service will give them objective, high quality and fearless advice.’*

—Chris Eccles, Secretary, Department of Premier & Cabinet, in his ‘Leadership from the centre’ address, Melbourne 23 June 2016

## Self-assessment questions

- 1 How does my agency get assurance and feedback about whether the guidance and support we give other agencies or staff meets their needs?
- 2 Does my agency’s leadership group use indicators to benchmark positive culture to strengthen integrity and monitor the risk of inappropriate behaviour?
- 3 Do I have assurance that my agency provides frank and fearless advice to government? Do I offer advice both for and against options in briefings to support decision-making?

# Managing information



The right information can completely change the way you look at a problem. Having relevant, complete and accurate information helps to improve decision-making. Sharing information can have a huge impact. Taking time to focus on the technical side of managing information can provide your agency with more reliable reporting.

## Quality of data and information

We continued to find widespread shortcomings in data and information throughout the public sector. Some agencies failed to record important decisions or activity. Others did not effectively analyse, use or disseminate the information they held. Some agencies did not model or forecast options and plans effectively. Nonetheless there were positive examples where agencies had good quality data and information.

*'[The Department of Environment, Land, Water and Planning's] spatial data has long been recognised for its high quality, and efforts to ensure that it is supported by mature and robust governance and management processes have made it one of Victoria's most valuable and highly used data sources.'*  
—Access to Public Sector Information (December 2015)

## Systems and controls

Today, the public sector does much of its work using information systems. We found examples of out-of-date systems, including those used for financial management and reporting, that undermined efficiency and effectiveness. We found that, although financial reporting systems and controls throughout the public sector are generally sound, many weaknesses remained, including in security controls.

*'IT security controls need improvement—IT security control weaknesses account for 68 per cent of all IT audit findings. There is poor management of IT security, particularly relating to user access and alignment with Victorian Government IT security standards.'*  
—Financial Systems Controls Report: Information Technology 2014–15 (October 2015)

## Record-keeping

Often, agencies could not show why or how they had spent funds, made decisions or managed risks. However, record-keeping is not just about creating an audit trail. It is a fundamental governance matter because it is about retaining corporate knowledge and improving how the public sector works. Addressing this shortcoming is a straightforward way of improving the public sector's efficiency, economy and effectiveness. We found pervasive inadequacies in record-keeping.

*'The absence of documentation for three of the 15 selected projects is a significant issue, as it is impeding effective project governance by agencies and means we have been unable to assess if these projects addressed key elements in the investment lifecycle guidance.'*  
—Managing and Reporting on the Performance and Cost of Capital Projects (May 2016)

## Self-assessment questions

- 1 What information does my agency collect and how does it use it? Is this enough? Could this be improved?
- 2 Are my agency's information and monitoring systems in place, up to date, secure, and meeting users' needs?
- 3 Is my agency committed to record-keeping, including training our staff and allocating enough time and resources to record-keeping? Is it easy to trace decisions and demonstrate activities? Are key processes documented properly?



# Implementation and delivery

The public sector is responsible for delivering big-budget projects and programs to bring about the outcomes and objectives that government sets. The community expects government to deliver the services and outcomes it says it will. In keeping with legislation, performance audits examine whether it has done so effectively, efficiently and economically.

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## Achieving results

Public sector goals are hard to achieve. Agencies do not face an easy task to achieve their targets in a complex environment with limited resources and constant change. We found that the public sector's performance was mixed. We found examples of the public sector achieving good results:

*'[State schools are] now performing better than non-government schools and the Victorian workers' compensation scheme in returning injured employees back to work earlier.'*

—*Follow up of Management of Staff Occupational Health and Safety in Schools* (August 2015)

*'[The Parole System Reform Program] has improved the operations of the APB [Adult Parole Board]. Board members now have sufficient time to consider each case, and improved ICT systems allow easier access to information and the improved recording of decisions made.'*

—*Administration of Parole* (February 2016)

We found several instances where the public sector did not achieve intended results, or fully implement projects and programs.

*'I also found a real risk that the expected benefits will not be achieved. Current forecasts predict consumers will only receive approximately 80 per cent of the benefits identified in the most recent 2011 cost-benefit analysis—provided that all issues and risks are effectively mitigated—and as costs increase over the life of the program, the final net cost to consumers is likely to rise above \$319 million.'*

—*Realising the Benefits of Smart Meters* (September 2015)

## Project management

Several audits found that projects and programs were delivered late and over budget. Infrastructure and services were not available as soon as intended, and the state paid millions of dollars more than planned, particularly in relation to ICT and capital projects.

*'None of the ICT Projects considered in this audit were completed or will be completed as initially budgeted. One of the six projects examined finished on schedule. One project was terminated prior to system delivery, six years after the planned completion date and having cost twice the intended budget. Most of the six projects examined in this audit faced significant challenges at various points during implementation.'*

—*Digital Dashboard: Status Review of ICT Projects and Initiatives – Phase 2* (March 2016)

## Self-assessment questions

- 1 Is my agency achieving its objectives?
- 2 How informative are the explanations given for any target shortfalls?
- 3 How is my agency monitoring project timeliness and spending?
- 4 How does my agency respond when projects are in danger of going over budget or schedule?

# Measuring and reporting performance



Reporting financial and non-financial performance demonstrates whether government has delivered on its commitments and used funds provided by Parliament efficiently, effectively and for the purposes that were intended. Public sector agencies are required to publish financial reports that comply with legislation and standards and that fairly present their financial position. If performance measurement and reporting systems are designed poorly or reports are difficult to understand or unreliable, then the public sector cannot be held to account for its performance.

## Financial reporting

We continued to find that public sector financial reporting can be largely relied on, with most financial statements of Victorian public sector agencies receiving a clear audit opinion.

*'Clear financial audit opinions were issued for the 79 local councils for the year ended 30 June 2015. This means that Parliament and the public can have confidence in the financial statements of these local councils.'*

—*Local Government: 2014–15 Audit Snapshot* (November 2015)

However, we found that more financial reports could not be completely relied on. Twenty-six audit opinions were either a qualified or disclaimer opinion or the opinion identified an emphasis of matter. Of particular concern, the Annual Financial Report of the State of Victoria (AFR) and the financial reports of two of the seven government departments had problems that led to the Auditor-General issuing qualified opinions.

*'The AFR received a modified audit opinion, consisting of two audit qualifications: the AFR did not record an expense, and associated liability, recognising the state's obligation to return to the Commonwealth Government \$1.5 billion of funding relating to the [East West Link] ... project; the property, plant and equipment balances of DET, which are included in the AFR, were not supported by proper accounts and records.'*

—*Auditor-General's Report on the Annual Financial Report of the State of Victoria, 2014–15* (November 2015)

We observed that the overall timeliness of financial reporting is slipping. This reduces the accountability and transparency of the public sector's finances. The AFR was late, because most of the agencies that contribute to this report were late in providing their draft financial statements to the Department of Treasury & Finance.

## Designing performance measurement frameworks

If the framework for measuring performance is not designed well in the first place, it undermines the entire performance measurement regime. This has been a longstanding theme in our audits. We found that some programs or agencies did not have performance measurement frameworks at all. For those that did, key performance indicators were not always relevant, or agencies did not set targets for performance. In several instances, evaluations should have been carried out but were not, meaning that agencies had no strong evidence to demonstrate performance or inform future activities.

*'The long-term water quality monitoring programs in the Port Phillip and Western Port region are not clearly linked to these objectives and they have not been evaluated against them.'*

—*Monitoring Victoria's Water Resources* (May 2016)

We found some positive examples, especially in our financial audits.

*'The 2014–15 reporting period was the first year local councils were required to prepare information on a prescribed set of performance indicators in accordance with the Local Government Performance Reporting Framework. The new regime requires extensive financial and non-financial information to be disclosed.'*

—*Local Government: 2014–15 Audit Snapshot* (November 2015)

### Demonstrating and reporting performance

This year, we found that some agencies had improved their performance reports.

*'We have observed better-quality performance statements in 2015, as TAFEs included more information describing indicators and the method of calculation, and more detailed explanations of variances.'*

—*Technical and Further Education Institutes: 2015 Audit Snapshot* (May 2016)

However, more commonly, agencies' performance reports could not demonstrate what they had done or show the benefits and results of their programs. We sometimes found a lack of transparency, where agencies held information but did not report it, either internally to management or externally to the public.

*'Public reporting lacks transparency and has been inadequate over the past decade ... The absence of sufficient information on the changing scope and components of these initiatives make the content and impacts of these programs impenetrable to citizens.'*

—*Reducing the Burden of Red Tape* (May 2016)

### Self-assessment questions

- 1 Does our performance measurement framework cover our key activities? Does it have relevant and appropriate key performance indicators and targets set in advance to help us measure our progress?
- 2 Do we evaluate key projects and programs to determine whether they are meeting their objectives?
- 3 Are we reporting all the information we are required to, internally and externally?
- 4 How do we monitor the timeliness of our financial reporting? How do we ensure that it receives a clear audit opinion?

# Monitoring and managing risks to financial sustainability



Agencies must be able to generate enough funds from operations to meet financial obligations, fund asset replacement and renewal, and absorb foreseeable changes. Management must monitor and manage its agency's ability to do this. Our audits found improvements in most indicators of risks to financial sustainability, although a range of challenges remain.

## Impact of funding models on financial sustainability

The funding or pricing models that some agencies are required to operate within can challenge the capacity of management to make long-term financial plans, or to grow income beyond a fixed ceiling. Agencies that rely on earned income from operations, including arts, sports and tourism organisations, can be particularly vulnerable to financial sustainability risks.

*'These [self-funded] entities face significant financial challenges, that if not addressed, may lead to a reduction in the services they provide to the community. If they are to be financially sustainable over the long term, the underlying pricing model used to generate revenue may need amendment, another funding source may need to be identified, cost structure may need review, or additional government support may be required.'*

—*Portfolio Departments and Associated Entities: 2014–15 Audit Snapshot*  
(December 2015)

## Maintaining and renewing assets

A key aspect of financial sustainability is being able to replace and repair assets. Assets include buildings such as schools, hospitals, and universities and other infrastructure such as community swimming pools. Assets have to be maintained and eventually replaced. Managing this process is a significant part of the work of many agencies. We found that some agencies were not funding new assets or maintaining assets at the same rate as assets were depreciating. If assets are not maintained or replaced, the quality of services the community receives can decrease and, as time goes by, it can become more expensive to address problems.

*'The continuing deficits are not allowing public hospitals to build up reserves from operations to replace or renew their fixed assets. Funds for replacement and new assets are provided mostly through specific purpose government grants, which are awarded based on the assessment of business cases. In addition, public hospitals also undertake specific fund raising. Current revenue levels create longer-term financial sustainability risks, and could, ultimately, impact the quality and variety of services offered to the public.'*

—*Public Hospitals: 2014–15 Audit Snapshot*  
(November 2015)

## Self-assessment questions

- 1 Has my agency assessed the impact of our funding or pricing models on our financial sustainability?
- 2 Does my agency monitor key indicators of risk to financial sustainability, including debt and cash flow?
- 3 Does my organisation have an appropriate risk management regime in place to assess financial sustainability risks?
- 4 What actions does my agency take in response to significant and emerging risks to its financial sustainability?
- 5 Is my organisation maintaining, replacing and renewing assets as required?

# Stakeholder engagement

This year, several of our audits assessed how well agencies engage with stakeholders, including the public. This engagement has become more frequent, reflecting the impact it has on effective public sector administration. One of the Victorian Special Minister of State's six directions for reforming the public sector includes considering how citizens and communities co-create public value.



## Getting input from stakeholders

We found good examples of stakeholders being consulted to collect information, opinions and advice.

*'The department is working to improve its complaints processes and assess the feasibility of an independent advocacy role for children and young people in residential care, which will contribute further to meeting their needs. This has involved engaging with children and young people in residential care to include their voice in identifying the issues and the possible actions to address these.'*

—*Follow Up of Residential Care Services for Children* (June 2016)

However, we did see shortcomings. Sometimes, agencies did not consult key stakeholders, or did not consult in a well-planned way.

*'DEDJTR engages extensively with non-government stakeholders on livestock biosecurity matters. However, this engagement has not occurred in line with an overarching strategic approach. The needs of, and risks to, non-government stakeholder groups—including livestock industries and private veterinary practitioners—have not been systematically assessed.'*

—*Biosecurity: Livestock* (August 2015)

## Communicating to stakeholders

Communications activities can often be overlooked. Failing to communicate can significantly affect outcomes, effective implementation, the uptake of a service and stakeholders' perceptions. Although some agencies' communications and awareness activities were effective, others' were not.

*'The lack of a PSO public awareness strategy means that agencies are not capitalising on the presence of PSOs to improve perceptions of safety and increase patronage on trains after 6 pm.'*

—*Public Safety on Victoria's Train System* (February 2016)

## Self-assessment questions

- 1 Do we have a stakeholder engagement plan for the whole organisation?
- 2 Is stakeholder engagement given adequate consideration in planning key projects, programs and activities?
- 3 Do we carry out adequate communications and awareness activities for stakeholders?
- 4 Do we review how effectively we engage stakeholders?

Key Audit Themes 2015–16 was first published as an appendix to our 2015–16 Annual Report.

To read the full report, please visit [www.audit.vic.gov.au](http://www.audit.vic.gov.au)

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