

# VAGO

Victorian Auditor-General's Office



## Managing the Municipal and Industrial Landfill Levy

July 2018





# Managing the Municipal and Industrial Landfill Levy

**Independent assurance report to Parliament**

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Victorian Auditor-General's Office

The Hon Bruce Atkinson MLC  
President  
Legislative Council  
Parliament House  
Melbourne

The Hon Colin Brooks MP  
Speaker  
Legislative Assembly  
Parliament House  
Melbourne

Dear Presiding Officers

Under the provisions of section 16AB of the *Audit Act 1994*, I transmit my report  
*Managing the Municipal and Industrial Landfill Levy*.

Yours faithfully



Andrew Greaves  
*Auditor-General*

25 July 2018



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## Acronyms and abbreviations

CES	Commissioner for Environmental Sustainability
committee	Sustainability Fund Committee
CPI	Consumer Price Index
DELWP	Department of Environment, Land, Water and Planning
DHHS	Department of Health and Human Services
DPC	Department of Premier and Cabinet
DTF	Department of Treasury and Finance
EPA	Environment Protection Authority
ERSC	Expenditure Review Sub-Committee
FMA	<i>Financial Management Act 1994</i>
FPSC	Finance and Performance Sub-Committee
fund	Sustainability Fund
GEMS	Global Engagement Management System
Guidelines	Sustainability Fund Guidelines
GWRRG	Gippsland Waste and Resource Recovery Group
MAC	Ministerial Advisory Committee
MILL	Municipal and Industrial Landfill Levy
minister	Minister for Energy, Environment and Climate Change
MoU	memorandum of understanding
MWRRG	Metropolitan Waste and Resource Recovery Group
PV	Parks Victoria
RFP	request for payment
SET	senior executive team
SFIP	Sustainability Fund Investment Policy
SV	Sustainability Victoria
SWRRIP	Statewide Waste and Resource Recovery Infrastructure Plan
TCV	Treasury Corporation of Victoria
team	Sustainability Fund team
VAGO	Victorian Auditor-General's Office
VFMC	Victorian Funds Management Corporation
VGSO	Victorian Government Solicitor's Office
WRRG	waste and resource recovery group
WS PIDC	Water Sector Productivity Inter-Departmental Committee



# Audit overview

Since 1992, Victorians have been paying the Municipal and Industrial Landfill Levy (MILL) when they dispose of waste to landfill. The levy aims to encourage recycling by putting a price on every tonne of waste that goes to landfill.

Since 2005, approximately \$1.7 billion has been collected through the levy. These proceeds are used first to fund core activities of environmental agencies, with the balance being transferred to the Sustainability Fund (the fund) that was established in 2005.

The fund was established under section 70 of the *Environment Protection Act 1970* (the Act). It is a hypothecated trust account and as such under the Act, payments from the fund can be made only for the purposes of fostering:

- environmentally sustainable uses of resources and best practices in waste management
- community action or innovation in relation to the reduction of greenhouse gas substance emissions, or adaptation or adjustment to climate change in Victoria.

Good financial management and transparency is particularly important for trust account expenditure.

The Department of Environment, Land, Water and Planning (DELWP) administers the fund and provides support to the Sustainability Fund Committee (the committee) set up by the Minister for Energy, Environment and Climate Change (the minister) to support the strategic and accountable management of these trust monies. The Sustainability Fund team (the team)—established within the Finance and Planning division of DELWP—provides secretariat support to the committee, along with finance and administration support for the MILL and the fund.

The committee's role is to provide impartial, strategic advice to the minister regarding allocations from the fund. Consent from both the Premier and the minister is required before money is committed to a project designed to pursue one of the fund's legislative purposes.

Fund recipients are responsible for the delivery of projects.

We audited five agencies that are involved with the collection of the MILL, administration of the fund and/or are recipients of its funding:

- DELWP
- Environment Protection Authority (EPA)
- Sustainability Victoria (SV)
- Metropolitan Waste and Resource Recovery Group (MWRRG)
- Gippsland Waste and Resource Recovery Group (GWRRG).

A hypothecated trust account holds money collected from a specific levy for a particular purpose.

Such accounts form part of the Trust Fund under section 19 of the *Financial Management Act 1994*.

Throughout the report we refer to 'proposals' to describe what the committee provides advice on, 'programs' to describe what the minister and Premier ultimately approve and then 'projects' to refer to project management after their approval and once funding agreements have been established.

We focused on the financial management of the MILL and the fund, processes for prioritising and selecting programs funded from the fund, project management and outcomes of funding.

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## Conclusion

While we found that MILL distributions to environmental agencies and the transfer of the remaining balance to the fund accord with the Act, there is a potential risk that the MILL, and the fund, are not always used for their intended purposes, and that activities that receive fund monies are not achieving the legislative objectives of better waste management, reduced greenhouse gases or effective adaptations to climate change. This is because:

- there is no process to ensure that agencies that receive MILL funding under section 70E(3)(d) of the Act spend this money in line with legislative objectives
- committee advice to government on the eligibility and merit of proposals to fund is incomplete and inconsistent, limiting the ability of the minister to make informed decisions that allow full comparison between competing proposals
- the construct of the committee, which includes senior staff of DELWP—the main funding beneficiary—creates an inherent conflict of interest
- the lack of a formal process to ensure the committee considers proposals by departments other than DELWP, or that change significantly after feedback from the Expenditure Review Sub-Committee (ERSC), means proposals can bypass the requirement for committee assessment, as occurred in 2017–18
- there is a significant lack of evaluation of funded activities and public reporting on fund outcomes.

DELWP recognises these design and implementation issues and has taken steps to resolve them, such as ensuring all 2018–19 proposals to the fund received committee appraisal; establishing an evaluation framework; and releasing an activity report in May 2018 and committing to its annual publication. The minister has also recently approved changing the membership of the committee to make it fully independent.

These developments if sustained will help foster greater public trust and confidence in the rationale for the fund and the ability of DELWP to administer it effectively.

However, a significant proportion of funds have remained unspent over many years, representing an opportunity cost. The 2016–17 and 2017–18 State Budget (Budget) commitments will only reduce the balance of the fund in the short term. If the situation persists, where significant fund balances remain unspent over extended periods, the public may by extension, reasonably question the quantum of the charge on every tonne of waste that goes to landfill.

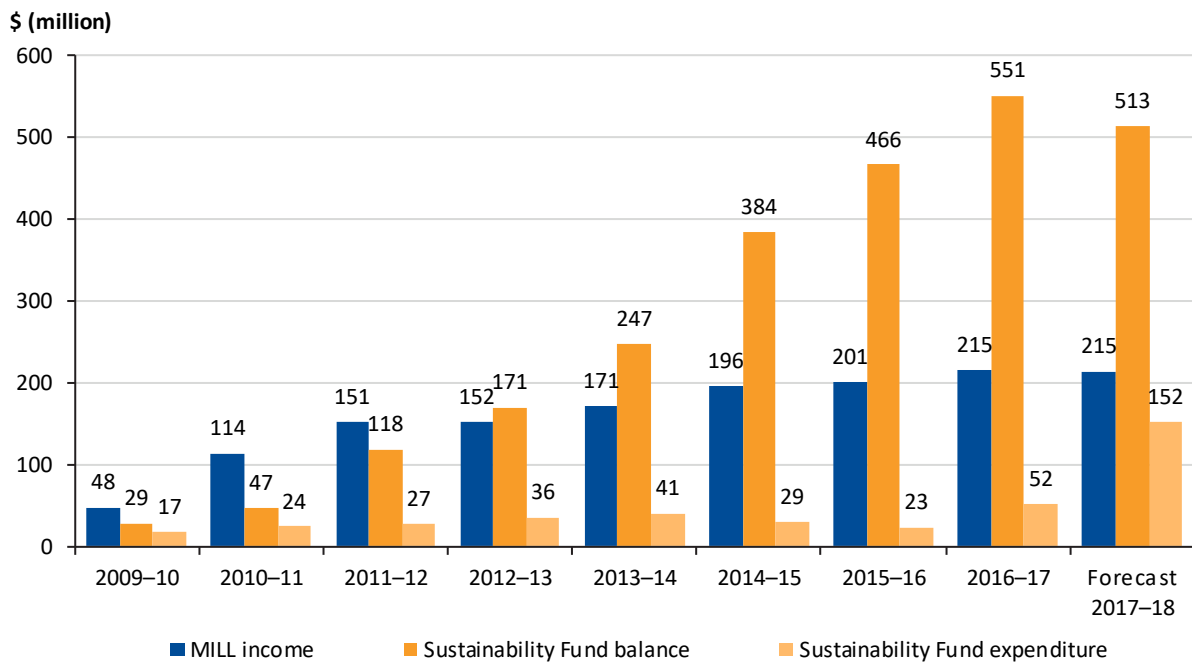
## Findings

### Fund balances

As at 31 December 2017, the balance of the fund was \$562 million. DELWP expects this to be \$513 million by 30 June 2018. The balance of the fund was \$29 million in 2009–10. As noted below, actual and budgeted expenditure has significantly increased over the past two years, however, the balance of the fund is predicted to remain high. To date, government has made no public commitment, nor outlined a strategy or target to reduce this balance.

Since 2009, \$401 million has been distributed from the fund—48 per cent of the \$829 million that has been transferred into it over this period. Figure A shows the growth of the fund since 2009 compared to the total of MILL income raised.

**Figure A**  
**MILL income compared with fund growth**



Source: VAGO.

### MILL distributions

Over the past three years, MILL payments to environmental agencies have increased by 71 per cent—from \$76.1 million in 2015–16 to a forecasted \$130.5 million in 2017–18. This increase is primarily due to EPA reform funding. Over the next four years, the MILL is expected to collect approximately \$215 million a year.

The minister determines the amount to be paid, the timing of payments and period over which they apply. Increasing direct payments from the MILL reduces the amount transferred into the fund.

In 2014, the Act was changed to include section 70E(3)(d). This allows public entities, in addition to those identified in section 70E(3), to be funded from the MILL for 'environment assessment, protection, restoration or improvement purposes'. Funding under this section of the Act increased from \$5.9 million in 2015–16 to \$24 million in 2017–18, with Parks Victoria (PV) being the primary recipient.

Currently DELWP policy areas suggest to the minister possible programs to be funded under this provision. There are currently no guidelines or governance processes to inform or evaluate the use of this funding from the MILL and to ensure it meets the conditions of section 70E(3)(d). Although the 22 committees of management that receive funding under section 70E(3)(d) provide financial acquittals to DELWP, PV and the Commissioner for Environmental Sustainability (CES) do not—despite accounting for over 95 per cent of the expenditure under this provision. Where the team has concerns about the alignment of a distribution it has sought legal advice. However, it has no formal responsibility to oversee these distributions. Monies paid from the MILL under this provision are not consistently subject to a financial acquittal, meaning most agencies are not required to demonstrate whether they use these funds for the specific purpose provided.

### Fund program expenditure

Fund distributions have varied over time depending on government policy and priorities. Over the past two years, budget commitments from the fund have been at their highest levels since the fund was established.

Government distributed \$52 million from the fund in 2016–17 and committed to spend \$152 million in 2017–18. The 2017–18 Budget provides for fund expenditure of \$439 million in new funding over five years between 2016–17 and 2020–21. However, the government has recently announced an allocation of only \$32.7 million from the fund in its 2018–19 Budget.

The government established the MILL to incentivise waste resource recovery and reprocessing and put a price on every tonne of waste that goes into landfill. At that time the fund was designed to fund programs that foster best practices in waste management. China's recent restriction on recycling material highlights the need for the government to consider how best to address this issue. In February 2018, the Victorian Government announced a \$13 million support package for councils and industry affected by this issue. The government intends to resource this from the fund.

### Investment and administration

DELWP has minimised administrative overheads and maximised returns on the cash balance of the fund.

DELWP investment of the cash balance of the fund is consistent with government legislation and policies. DELWP uses the Sustainability Fund Investment Policy (SFIP) to guide its investment decisions. Investment returns are consistent with expectations and interest earnings are retained within the fund.

The cost of administering the scheme has remained constant despite a significant increase in the work associated with this role. The activity of the team and committee has increased as the value and number of programs approved for funding from the fund has gone up. The administrative budget has not significantly changed for several years—it has remained at \$0.8 million.

## Role of the committee

The committee plays an important role assessing proposals seeking monies from the fund. It provides advice to the minister to assist in the selection and approval of proposals, including advice about their eligibility and merit.

Since its establishment in 2016 the committee has identified issues with, and made changes to improve its engagement with potential funding recipients, project establishment and oversight, assessment methodology and processes, and program evaluation.

However, more needs to be done. There is an opportunity to further strengthen the committee's advice by:

- providing them with access to all proposals seeking funding from the fund prior to ministerial consideration
- removing conflicts of interest
- clarifying guidance
- more clearly and completely documenting how each proposal performs against the evaluation criteria in the advice to the minister.

## Regular and alternative approval pathways

In 2017–18 the committee did not provide advice on all proposals that were funded. This was a breach of the statutory *Sustainability Fund Guidelines* (the Guidelines) which require the minister and Premier to seek advice from the Sustainability Fund Manager or committee prior to approving the use of fund money. The committee did, however, provide advice for all 2018–19 Budget proposals recommended to be approved from the fund.

There is no process to ensure the committee has access to all proposals prior to their consideration by government. In the 2017–18 Budget process only eight of the approved programs (representing 53 per cent of the value of those approved) went through the 'regular' pathway, which includes committee assessment. The remaining six programs went through one of three other possible approval pathways. This prevented the committee from reviewing, rating and providing advice to the minister on proposals prior to ERSC, which considers proposed expenditure as part of the Budget process.

Of the eight programs that followed the regular pathway, the committee rated one program and a component of another as needing 'more information'. This rating, at the time, was used interchangeably to refer to bids that required more information to enable assessment as well as those the committee assessed as not aligned with the legislation, as there was no 'do not support' advice option in 2017–18. Further, the committee did not give any rating to one component of another proposal. This means that the committee only assessed against evaluation criteria, rated and provided advice to the minister on four out of the 14 programs approved for funding in 2017–18.

The two highest value bids announced in the 2017–18 Budget, to receive funding from the fund, were Timber Plantation Establishment and Protecting Victoria's Environment—Biodiversity 2037. The committee did not review the Timber Plantation Establishment program before ERSC endorsement and it rated the Protecting Victoria's Environment—Biodiversity 2037 program as needing 'more information'. Expenditure for these programs has been committed in the 2017–18 Budget and the minister and Premier have approved funding for the biodiversity program. Further information regarding the alignment of the Timber Plantation Establishment program's legislative objectives needs to be provided before the minister and Premier approve expenditure from the fund.

For the 2018–19 Budget, the committee rated the Port Phillip Bay Beach Renourishment program 'not currently supported' because it did not align with the legislative objectives of the fund. The 2018–19 Budget announced funding for this program from the fund, but at that time the minister and Premier had not yet provided final approval for release of the funds. DELWP has advised that these proposals are now not being put forward for approval from the fund.

Due to the nature of the budget process, the committee does not always assess the final version of proposals as they may continue to change right up until the time departments submit them to ERSC for consideration. DELWP is aware of the risk this situation creates to the integrity of the approval process and advised it is seeking endorsement from the minister and Premier for a formalised system to ensure the committee reviews and provides advice on all future bids before the minister and Premier approve them.

### Conflict of interest

One outcome from the 2013 *Report of the Ministerial Advisory Committee on Waste and Resource Recovery Governance Reform* was the transfer of fund management from SV to DELWP. The report found a perceived conflict of interest in SV's role as the administrator of the fund and being one of its primary funding recipients.

DELWP is now the primary recipient of funding from the fund, receiving \$354.13 million or 79 per cent of active program funding, though a proportion of this funding is passed on through grant programs. Two of the five Sustainability Fund Committee members are DELWP employees responsible for policy areas that benefit from funding. As committee members they are also involved in assessing and providing advice on their own budget proposals.

The committee has attempted to address these conflicts through a conflict of interest policy and procedures that require members to disclose conflicts and decisions made on how they should manage them. These controls are not sufficient to address the inherent conflict of interest created by the current membership of the committee. DELWP recognises this is an issue that needs to be resolved. The minister has recently approved an update of the Guidelines, as part of DELWP's response to the audit, to change the membership of the committee to make it fully independent.

### Clarifying guidance

According to the Guidelines, proposals that seek funding for their core administrative costs are not eligible for funding from the fund. We reviewed all funding proposals the committee assessed in 2017–18 and found seven examples where, due to definitional ambiguities, there is a risk that the committee recommended proposals that may contain core administrative costs and may therefore be ineligible.

DELWP advised that these examples related to proposals that expand service provision into new areas and therefore do not represent core administrative costs. Our discussions with DELWP staff revealed that there is no documented definition of what constitutes core administrative costs. This highlights the need for an agreed definition of 'core administrative cost' and for the committee to apply this consistently in the assessment and recommendations for funding.

The Guidelines do not specify how to deal with proposals seeking ongoing funding or programs that are looking to shift their funding from output appropriations to the fund. Funding proposals may seek a fixed amount of funding for a period of the program, usually three to five years, plus ongoing annual funding beyond this period. DELWP advised that \$20 million in ongoing funding was approved in 2017–18 and it requested over \$80 million in ongoing funding as part of its proposals in the 2018–19 Budget process. The committee recognises that committing fund monies to projects on an ongoing basis could be an issue if, for example the demand, as demonstrated by the number and size of 2018–19 proposals, led to a significant decline in the fund balance. The committee noted in its advice to the minister that ongoing funding may limit innovation and the ability of government to ensure effective alignment of funded programs. It also noted funding for ongoing components could be made subject to a four-yearly evaluation to confirm alignment with the fund.

### Committee assessments and advice

This year, for the first time, the value of proposals requesting funding exceeded the fund balance. The growing demand on the fund underlines the importance of providing clear and complete advice to the minister about each proposal's alignment with legislative objectives, and performance against all other evaluation criteria.

The committee rates each proposal as highly recommended, recommended, recommended subject to additional consideration, more information or not currently supported.

Five evaluation criteria (impact, quality, policy alignment, value for money and outstanding issues) inform the overall rating. However, the committee's assessment against each criterion is not included in their advice to the minister making it difficult for the minister to distinguish between the merits of each proposal.

The committee's assessments also do not consistently document consideration of alternative funding sources—a requirement in the Guidelines. In addition, the value for money assessment currently performed by the committee does not include enough information to enable the minister to determine which programs will most cost-effectively deliver on the fund's objectives. The value for money assessment included in a program's business case does not specifically consider the objectives of the fund and it is not clear how the committee uses this information in the assessment of proposals.

Committee advice also lacked sufficient detail to enable the merit of one proposal to be weighed against another; and also lacked clear and complete documentation about what proposals or proposal components may be ineligible for funding. The advice provided by the committee to the minister for different bids is inconsistent, which limits the minister's ability to fully compare and contrast bids when making funding decisions.

In addition, the committee requested more information on a number of proposals in 2017–18 which was not forthcoming prior to approval, meaning it could not make a complete assessment and fully advise the minister on particular projects to confirm alignment. These proposals were approved creating the potential risk that they may not be aligned with the fund's legislative objectives or represent the best application of fund resources.

The minister recently approved an update of the Guidelines to change the membership of the committee to make it fully independent, and to provide better clarity about the advisory function of the committee and the definition of core administrative costs.

## Project delivery

Project delivery is hampered by delays in establishing project plans and funding agreements. Opportunities exist to better align the number of milestones attached to reporting and funds release with the complexity and value of funded programs. There is an opportunity for DELWP to clarify roles and responsibilities for escalation of underperforming projects.



## Role of the team

DELWP directs the majority of the team's resources to managing funding agreements. The team has six staff, the Sustainability Fund manager, one financial analyst, one to support the committee and provide advice on proposals and three responsible for managing funding agreements.

The team's role during the various stages of project development and delivery is not clear, creating the potential for duplication of effort. Recognition should be given, where warranted, to the processes and mechanisms some recipients have in place to oversee the delivery of projects such as project control or independent boards who are appointed by and accountable to a minister.

## Funding agreements

Following approval by the minister and Premier, funding recipients develop a project plan. The team assists as required with the development of project plans and funding agreements are developed once sufficient information is available for their completion. Recipients do not receive any money until the funding agreement is established.

We reviewed the time frames for establishing funding agreements for 16 projects from 2015 to 2018. DELWP took 213 days on average to develop a funding agreement from the point of program approval. One project took a year to establish a funding agreement after the minister and Premier approved its funding. Agencies stated that significant resources are required to develop the project plan and they absorb development costs until receipt of the first payment. Delayed establishment of project plans continues to be an issue that results in fund underspending. DELWP has advised that it aims to have project plans established by 30 June 2018 for programs approved in 2018–19 and have engaged consultants to assist with their development.

Funded projects are paid against achievement of project milestones. Our analysis of 49 funding agreements found that the average number of project milestones was 15, with the highest number for a single project being 71, and the lowest being three. There is no relationship between the number of milestones and the project cost or length. The rationale for some projects having significantly more milestones than others is not clear. Funding recipients raised concerns about the administrative burden of putting through requests for payments tied to each milestone. This illustrates the need for the team to be aware of this issue when developing funding agreements.

## Monitoring

Funding agreements specify the monitoring, reporting and acquittal requirements for each initiative over the approved funding period. The team monitors and ensures recipients, with some exceptions, comply with these requirements. For example, recipients do not always provide their quarterly reports, however, where this occurs we saw evidence that the team follows this up.

## Reporting

The fund's quarterly report provides the committee with the opportunity to review key aspects of project and financial management. Recipients are required to submit a quarterly progress report to the team but not all consistently comply with this requirement. According to the November 2017 quarterly report to the committee, 16 of the 56 project managers (29 per cent) had not submitted their most recent quarterly progress report. The team therefore could not accurately assess and report on the status of these projects.

DELWP recently aligned its internal management report and the committee's quarterly reporting. DELWP's report to its senior executive team now includes the status of funded programs delivered by DELWP, its portfolio agencies and DHHS. However, this report does not contain the progress of a project delivered by the Department of Treasury and Finance (DTF).

## Escalation of project risks

DELWP should document a clear process for the management of underperformance or project risks for funded programs. Currently, the team raises project issues with the committee as part of its quarterly exception reporting. The exception report reviews and flags projects that may need attention or support. It raises any issues for escalation to the committee and identifies suggested committee actions. However, actions identified in these exception reports need to be clearer to ensure that the issues are being addressed. Committee meeting minutes from 14 November 2017 do not show that the committee discussed issues raised in the quarterly report or endorsed suggested actions to address the issues identified.

## Financial acquittal

The team relies on the approval of the funding recipient's financial officer as evidence of financial acquittal. The team received a financial acquittal for all 17 projects that we tested. All include an expenditure report designed to include information on how funding was accounted for, what recipients spent funds on and what financial year they spent the funds in. The expenditure reports vary in the level of detail provided and may not always enable the team to confirm that recipients use the funds for their intended purpose.

## Funding outcomes

### Evaluation

DELWP has not been able to demonstrate the extent to which funded initiatives achieve their intended outcomes. As part of the audit, we reviewed the 18 projects that have closed in the past two years and found that all of them completed a project evaluation. The team completes a closure report that assesses the evaluation, where available, to determine whether closed projects have met their objectives.

Of the 18 projects we reviewed, only seven (39 per cent) reportedly met their objectives. Only two of the other 11 projects relate to programs that commenced during DELWP's administration of the fund. One of these programs was terminated early. The other was designed to achieve long-term behaviour change, and its outcomes have not yet been able to be assessed.

DELWP has worked to make project outcomes clearer in funding agreements with the aim of improving project evaluations on completion. DELWP has recently developed an evaluation framework to support a whole of fund evaluation and advises that this will be detailed in a 2017–18 activity report due to be released alongside the DELWP annual report.

### Lessons learned

DELWP currently does not have a formal process to capture and share lessons learned from completed projects. It intends to embed these lessons into the recently developed evaluation framework. The team captures lessons learned as part of the Final Evaluation Report but these are not stored in a central location. This means they are not easily accessible to the committee when new but similar proposals come up for assessment. The current process relies on the knowledge of the team or the committee members. The team does not currently share this information with funding recipients to allow this to inform future program development.

### Overall fund outcomes

DELWP does not measure overall fund outcomes. The legislation and *2016 Sustainability Fund Priority Statement* (Priority Statement) provide broad objectives for the fund but DELWP does not use these to evaluate the success of the use of fund monies. The committee advised that a recently developed evaluation framework will support a whole of fund evaluation, which it intends to complete every four years. However, DELWP has not applied the framework to any projects to date, and it is not clear how this will work in practice.

### Public reporting

DELWP has not publicly reported on the overall fund outcomes since it took over administration of the fund.

It is unclear how funded programs have contributed to the achievement of the fund's legislative purposes and the extent to which, if any, they have addressed the challenges posed by waste and climate change.

Until May 2018, public reporting about the activities of the MILL and the fund was limited to appendices to DELWP's annual report and general information on their website.

DELWP has recently published an activity report for 2015–17, *Investing in a more sustainable future*. The report was released in May 2018. It is similar to the report produced by SV. It is unclear why it has taken DELWP nearly two years to produce it. The delay in its publication affects its relevance and usefulness as a tool to improve the transparency of the fund and its management. DELWP advised it intends to publish an annual activity report each September after the close of the financial year. This process will be aligned to the annual reporting process. There has been no reporting of the fund’s governance arrangements.

It is important for the public to understand not just how this money is being spent, but also the extent to which it has been used to achieve its intended outcomes. There is a lack of transparency about the activities and outcomes of the fund. This undermines public trust in the collection of the levy.

There has been improved financial transparency about the fund in Budget Papers since 2016–17. They now more clearly identify programs that receive monies from the fund.

## Recommendations

We recommend that the Department of Environment, Land, Water and Planning:

1. assess alignment with the legislative purpose and establish a financial acquittal process for distributions made under section 70E(3)(d) of the *Environment Protection Act 1970* (see Section 2.3)
2. establish an independent committee to manage inherent conflicts of interest while maintaining access to subject-matter expertise (see Section 3.5)
3. review the role of the Sustainability Fund Committee and Sustainability Fund team:
  - revise and update the committee’s terms of reference (role and responsibilities, memberships, managing conflicts of interest, +/- KPIs, rules for decision-making)
  - clarify the role of the team and the committee in the oversight of project delivery (see Sections 3.5 and 4.2)
4. develop clear guidance regarding the treatment of the following:
  - applications seeking core administrative costs
  - eligibility of applications seeking ongoing funding (see Section 3.3)
5. establish processes to ensure all proposals seeking funding from the Sustainability Fund are assessed by the Sustainability Fund Committee before approval by the Minister for Energy, Environment and Climate Change and the Premier (see Section 3.4)
6. review the evaluation criteria applied to assessing proposals to clearly reflect the requirements specified in the legislation, *2016 Sustainability Fund Priority Statement* and *Sustainability Fund Guidelines* (see Section 3.2)

7. improve the quality of advice provided to the Minister for Energy, Environment and Climate Change by providing the assessment against each evaluation criteria (see Section 3.5)
8. relate the number of funding agreement milestones to the value and/or complexity of funded programs and link payment milestones to reporting requirements to minimise administrative burden (see Section 4.2)
9. examine mechanisms to encourage the earlier development of project plans for approved programs (see Section 4.2)
10. require funding recipients to provide key categories of expenditure in support of the financial acquittal of funding agreements to enable the Sustainability Fund team to review whether the funds have been used for the purpose intended (see Section 4.2)
11. implement the evaluation framework to evaluate outcomes of funded programs to clearly demonstrate the extent to which programs have contributed to the specified legislative objective (see Section 4.6)
12. identify overall Sustainability Fund outcomes to measure the extent to which expenditure has successfully delivered legislative objectives (see Section 4.6)
13. develop a formal process to consistently apply lessons learned including:
  - capturing and storing them centrally to enable them to be considered by the Sustainability Fund Committee when assessing proposals
  - sharing them with agencies to enable them to be considered when developing new program proposals (see Section 4.7)
14. publish an annual public report for 2018–19 and future years detailing the activities of the Sustainability Fund and outcomes achieved (see Section 4.8).

## Responses to recommendations

We have consulted with DELWP, EPA, SV, MWRRG and GWRRG and we considered their views when reaching our audit conclusions. As required by section 16(3) of the *Audit Act 1994*, we gave a draft copy of this report to those agencies and asked for their submissions or comments. We also provided a copy of the report to the Department of Premier and Cabinet (DPC).

The following is a summary of those responses. The full responses are included in Appendix A.

DELWP accepted all 14 recommendations and provided an action plan to address them. SV welcomed the audit and looks forward to supporting DELWP to address the recommendations. The two waste and resource recovery groups (WRRG) noted that the audit was consistent with their past experience as Sustainability Fund recipients and were supportive of the recommendations.



# 1

## Audit context

Victoria's MILL was established in 1992 to create a disincentive to putting waste into landfill and to encourage resource recovery and recycling. Income generated by the MILL supports Victoria's environmental agencies, with the remainder transferred to the fund to be used only for initiatives that aim to address environmental challenges for the benefit of all Victorians.

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### 1.1 Municipal and Industrial Landfill Levy

#### Legislation

The Act requires the MILL to be charged on each tonne of waste deposited at licensed landfills. The EPA collects the levy from landfill operators and councils.

#### Changes to the levy

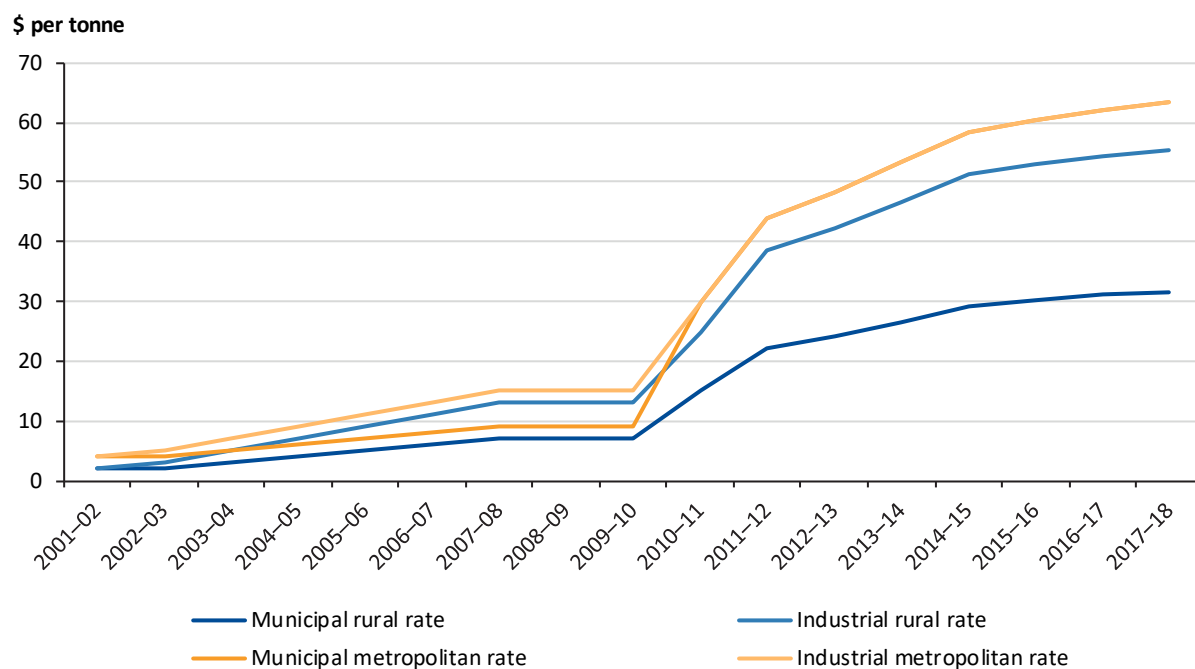
The landfill levy system has changed significantly over the past 25 years. The metropolitan waste levy has increased from \$2 per tonne in 1992 to its current rate of \$63.28 per tonne. DELWP forecasts MILL income for 2017–18 to be \$215 million.

In 2010, the government considered the metropolitan municipal waste levy of \$9 and the regional municipal waste levy of \$7 too low to drive behavioural changes. It increased the levy substantially to make recycling economically competitive compared to depositing valuable materials to landfill. Figure 1A shows the change in the Victorian levy since 2001.

The objective was to increase recycling rates and stimulate the recycling industry by making new recycling ventures more viable and create new jobs. The expected impact of the rate increase was a fall in annual volumes of waste to landfill of 34 per cent between 2009–10 and 2013–14.

Environmental groups and the waste industry supported the 2010 rate increase, which brought Victorian landfill levy rates in line with those of New South Wales. Since then, New South Wales's 2017–18 rates have increased to \$138.20 per tonne for the metropolitan rate and \$79.60 per tonne for the regional levy, more than double Victoria's rates.

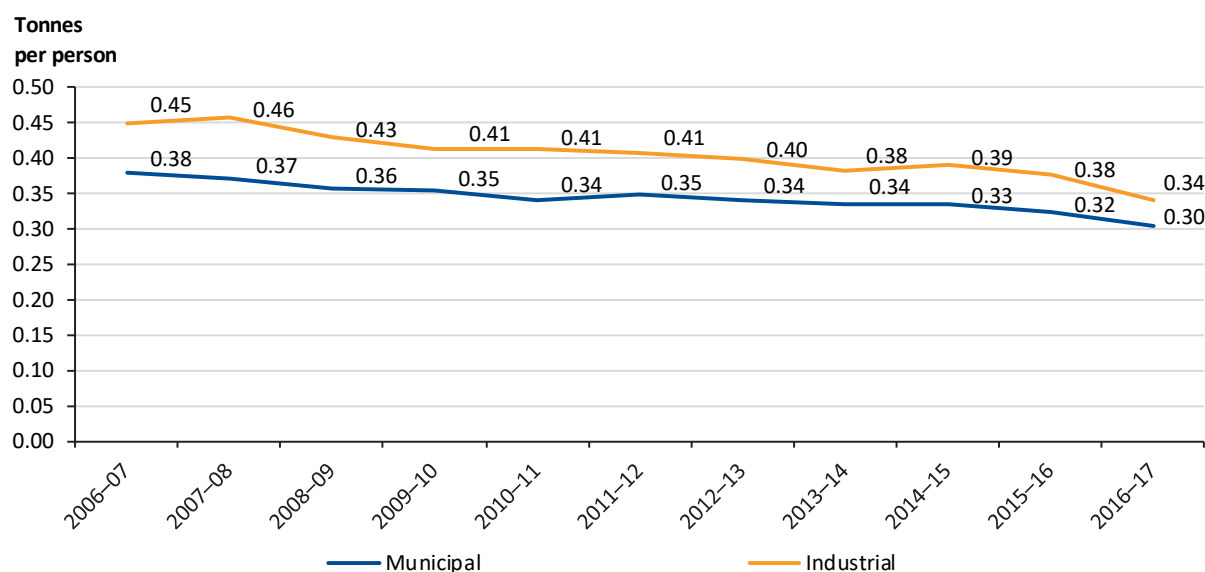
**Figure 1A**  
**Changes in the Victorian Municipal and Industrial Landfill Levy rates**



Note: Annual rate increases started in 2010-11. At that time, the industrial and municipal metropolitan rates became the same rate.  
 Source: VAGO based on EPA data.

Figure 1B shows the changes in the volume of waste to landfill between 2006-07 and 2016-17. While this shows a decline, there may be other contributing factors, such as community education.

**Figure 1B**  
**Volume of municipal and industrial waste to landfill (tonnes per person)**



Source: VAGO based on EPA and Australian Bureau of Statistics data.

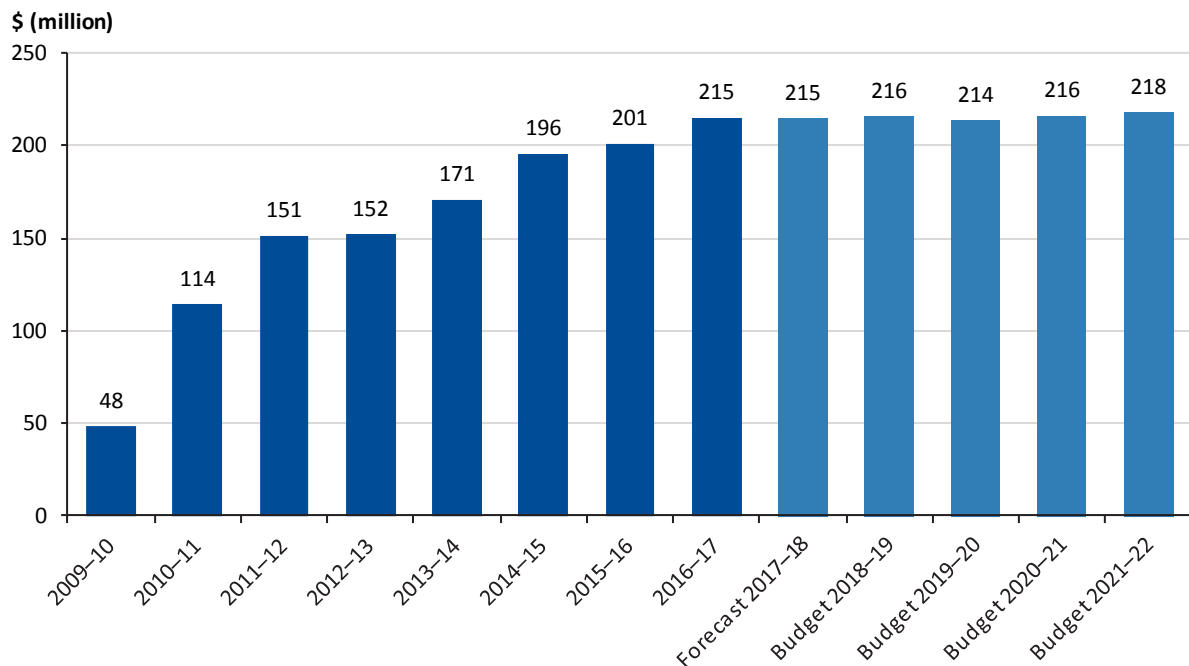


## MILL collection and distribution

EPA is responsible for collecting and distributing the MILL under the Act. EPA collects the MILL from licensed landfill operators, managed by councils or commercial operators, and transfers the income to the MILL Trust Account, managed by DELWP.

Figure 1C shows MILL income since 2009.

**Figure 1C**  
**MILL income**



*Note:* The amounts above are on an accrual accounting basis. Income is accounted for in the period it is earned, not received.

*Source:* VAGO.

MILL income is used first to fund the core operating activities of environmental agencies in accordance with section 70E(3) of the Act. These are the EPA, SV and Victoria's seven WRRGs under subsections 70E(3)(a)–(c).

Subsection 70E(3)(d) of the Act was inserted in 2014 and enables the MILL to fund 'a public entity or other body established for public purposes to be used for environment assessment, protection, restoration or improvement purposes'. Distributions under this provision have, to date, been made to PV, the CES and 22 committees of management.

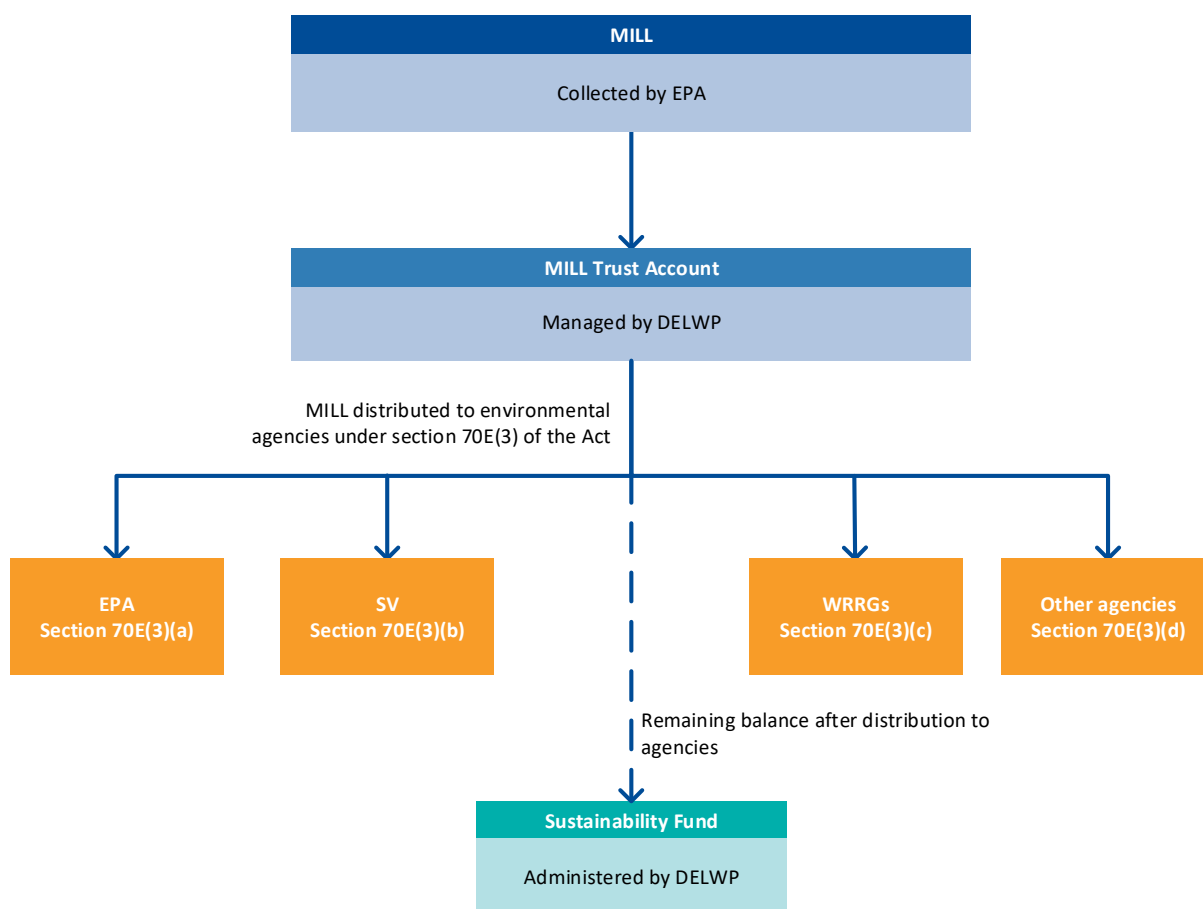
The minister determines, on advice from DELWP policy areas, the funding levels, period and timing of payments for environmental agencies and organisations under section 70E(3). However, this determination occurs after the budget process whereby ERSC first reviews the funding for these agencies for the four-year budget period.

## 1.2 Sustainability Fund

### Establishment

In 2004, the government amended the Act to create the fund and directed a portion of the MILL towards it. The MILL is the sole source of revenue for the fund. Figure 1D details the flow of MILL monies to the fund under today's legislative arrangements.

**Figure 1D**  
**Flows from the MILL into the Sustainability Fund**



Source: VAGO.

### Purpose

The fund is a hypothecated trust account created under section 70F of the Act for the specific purpose of fostering:

- environmentally sustainable uses of resources and best practices in waste management
- community action or innovation in relation to the reduction of greenhouse gas substance emissions, or adaptation or adjustment to climate change in Victoria.

The second clause—enabling the fund to be used for greenhouse gas reduction or climate change adaptation—was introduced in 2010.

## Priorities and guidance

Before any money can be distributed from the fund, the minister must issue a Priority Statement and Guidelines, under section 70A of the Act. These documents are designed to maximise the effectiveness of the fund and to ensure that a strategic approach is taken to the application of its monies.

Section 70F also requires the consent of both the Premier and the minister before fund monies can be applied to one of the fund's legislative purposes.

### Priority Statement

Section 70A(1)(a) of the Act requires that the Priority Statement set out, in order of priority, how the minister and Premier intend to use the money. The Priority Statement is refreshed at intervals consistent with changes to government policy directions. The minister and Premier approved the current version in 2016.

The current Priority Statement does not order the strategic priorities for the fund but notes preference for initiatives that foster employment, new technology and innovation, resource efficiency or ongoing behaviour change. It states that the following climate change and waste policies and strategies should inform the choice of potential investments from the fund:

- climate change policies
- *Victoria's Climate Change Adaptation Plan 2017–2020*
- *Victoria's Energy Efficiency and Productivity Statement*
- *Renewable Energy Action Plan*
- *Protecting Victoria's Environment – Biodiversity 2037* and other relevant strategies
- the *Statewide Waste and Resource Recovery Infrastructure Plan (SWRRIP)*
- the Regional Waste and Resource Recovery Implementation Plans and other relevant strategies.

### Guidelines

The Act requires guidelines be in force that explain how the minister and Premier will exercise their powers in relation to the application of money from the fund.

The Guidelines state that the minister and Premier will seek advice from the Sustainability Fund Manager (a DELWP staff member who manages the team) directly or via the committee, before allocating fund money to a project so they are informed about:

- compliance of the proposal with legislated obligations
- its consistency with the Priority Statement
- other considerations such as value for money.

Under the Guidelines funding should be directed to support projects, programs, services or technologies that will benefit Victoria environmentally, socially and economically.

The Guidelines also identify the types of projects that the fund should not be used for, including:

- projects that seek retrospective funding, or that duplicate environmental programs already operating
- the core administrative costs of an existing organisation.

## Administration

SV was initially responsible for managing the fund.

In 2013 the MAC review found issues with the administration of the fund:

- governance arrangements remained overly complicated
- perceptions of conflicts of interest and a lack of transparency, as SV was both the administrator and a recipient of funding
- that reporting of fund activity was unclear.

In 2015, in response to stakeholder concerns and the findings of the MAC review, government amended the Act and transferred responsibility for the fund from SV to DELWP. DELWP has administered the fund since 1 July 2015.

The team sits within DELWP's Finance and Planning unit and is responsible for administering the MILL Trust Account and the fund. This includes financial management, providing secretariat support to the committee, assessment of funding proposals and the establishment and management of funding agreements.

## Sustainability Fund Committee

When SV administered the fund, the Sustainability Fund Advisory Panel—an independent statutory committee—was established to review and recommend projects for funding to the minister. The legislative changes that transferred fund administration to DELWP in July 2015 removed the requirement for a statutory committee.

In its place, the minister established an advisory committee to provide advice to the minister on funding proposals before fund monies are allocated to a program.

The committee has no delegated decision-making authority. Authority to apply money from the fund rests with the minister and Premier.

The Guidelines require that the committee's advice to the minister and Premier be based on:

- alignment of the proposal's objectives with the fund's legislative objectives
- alignment of the expected outcomes of the proposal against the defined priorities of the fund as stated in the Priority Statement
- achieving value for money given the immediate and long-term environmental benefits expected to be achieved by the proposal
- the availability of funding to the applicant from other sources.

The committee has five members: an independent Chair, a finance expert (currently an independent member who is also the Deputy Chair), two DELWP subject matter experts and a governance expert.

The governance position was vacant from July 2017 until March 2018. DELWP's subject matter experts are the Executive Director, Energy Policy and Programs and the Executive Director, Climate Change.

The committee held its first meeting in May 2016 but did not have its full complement of members until December 2016. The interim arrangements are explained in more detail in Section 3.4.

### 1.3 Sustainability Fund distributions

Open grant rounds refer to the ability of potential recipients, including community groups, councils, government departments, statutory entities, non-government organisations and businesses, to apply directly for a grant from the fund.

#### Access to funds

The Guidelines state that funding recipients may be direct grant recipients or government departments or agencies. When SV administered the fund, open grant rounds were available. However, there have been no open grant rounds announced since 2009.

All distributions now occur through the budget process with departments and agencies as recipients. A proportion of these funded initiatives involve grant programs that provide subsequent opportunities for councils and non-government organisations to access monies from the fund.

The team handles public enquiries seeking direct funding from the fund. It attempts to refer people to currently available grant programs, funded from the fund, or to direct them to alternative government grant programs. The team shares details of enquiries with relevant DELWP policy areas and portfolio agencies. Details of public enquiries are included in the team's quarterly report to the committee and the committee's annual report to DELWP's Secretary.

## Developing funding proposals

Department policy areas or agencies develop funding proposals as part of the government's annual budget cycle. To request funding from the fund applicants nominate it as the source of funding on the State Budget Bid Template. In some cases, the government or central agencies recommend the fund as the funding source.

## Assessing funding proposals

### Role of the team

The Sustainability Fund Manager and the team receive a copy of DELWP's funding proposals prior to its minister's presentation of initiatives to ERSC for endorsement. It prepares an assessment of each funding proposal against the legislative objectives for the committee's review. The team liaises with DELWP policy areas and its portfolio agencies if more information is required.

### Role of the committee

The committee reviews funding proposals submitted by DELWP and its portfolio agencies prior to submission to ERSC and any other department proposals provided to them. All bid information is provided to the independent members. The independent members have an established practice of reading and forming their own initial views on the merit of funding proposals prior to reviewing the team's proposed recommendations. The two independent members of the committee meet with the team to consider and test draft positions before they are put to the committee. The whole committee then reviews each proposal based on documentation collated by the team and reaches a recommendation.

The committee chair subsequently provides written advice to the minister with the committee's recommendations on which proposals it supports for funding.

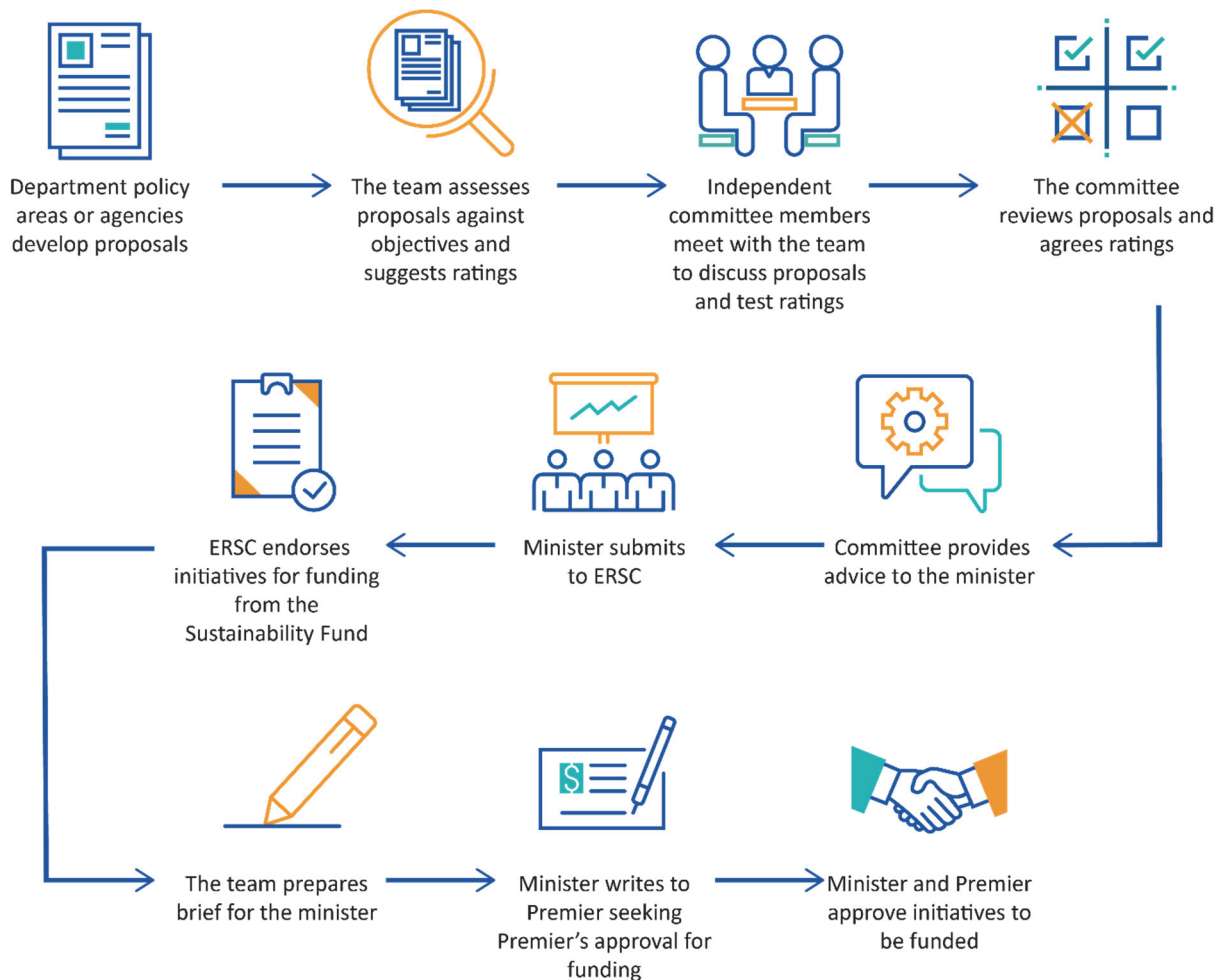
The committee's review occurs as part of the budget cycle. The timing of its meetings is coordinated so that they occur after the policy areas develop funding proposals and prior to ERSC's consideration of funding proposals.

The nature of the budget process means that the time frame for development, assessment and recommendation can be tight and proposals may continue to change up to the point that departments lodge proposals with the Cabinet office for consideration by ERSC.

## Expenditure Review Sub-Committee

ERSC considers and endorses all funding proposals from all sources as part of the budget process. The minister and Premier then approve the endorsed proposals for release from the fund. Figure 1E shows the standard approval process for proposals seeking funding from the fund.

**Figure 1E**  
**Funding approval process**

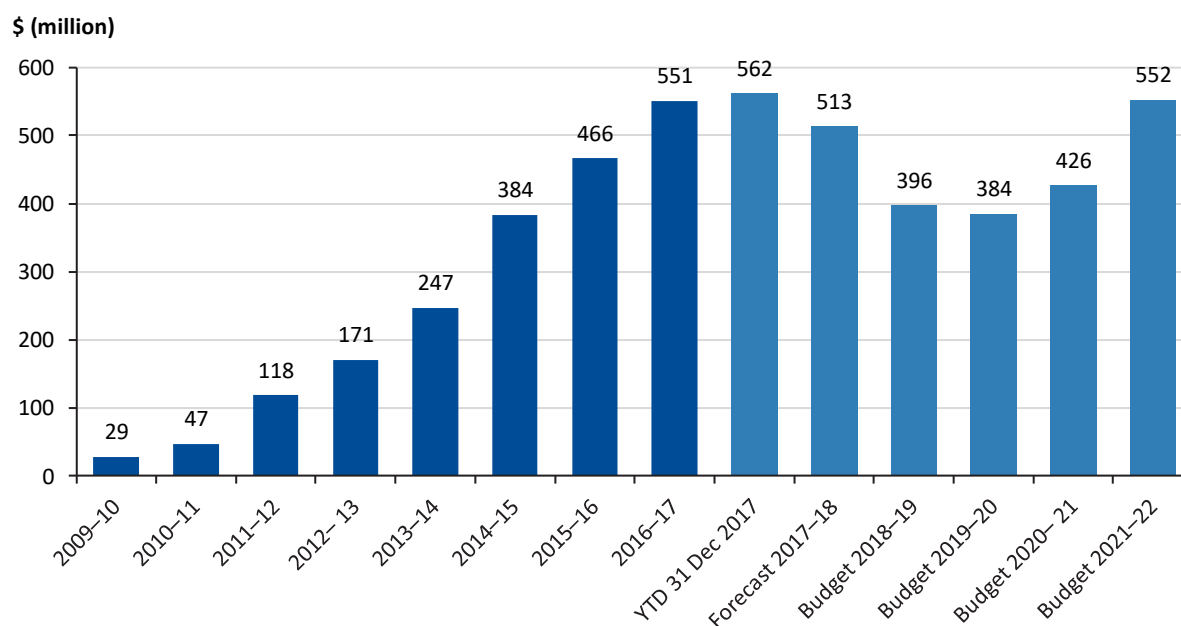


Source: VAGO.

## 1.4 Sustainability Fund balances

The fund balance had grown to \$562 million as at 31 December 2017. Figure 1F shows the growth of the fund balance since 2009–10. The forecast closing balance of the fund at 30 June 2018 is \$513 million. By the end of the forward estimates, 2021–22, the balance is expected to be \$552 million. This balance assumes no new funding from the fund is announced between now and 2021–22.

**Figure 1F**  
**Sustainability Fund balance**



Note: Balances are at 30 June each year.

Source: VAGO based on EPA and DELWP data.

## Rate of future expenditure

The rate of expenditure from the fund against income has been low when compared to other trust funds such as the Community Support Fund and the New South Wales Environment Trust Fund that typically distribute over 90 per cent of their annual income.

Reducing the balance of the fund can be achieved by:

- reducing the income to the fund by distributing more money from the MILL Trust Account
- increasing distributions from the fund.

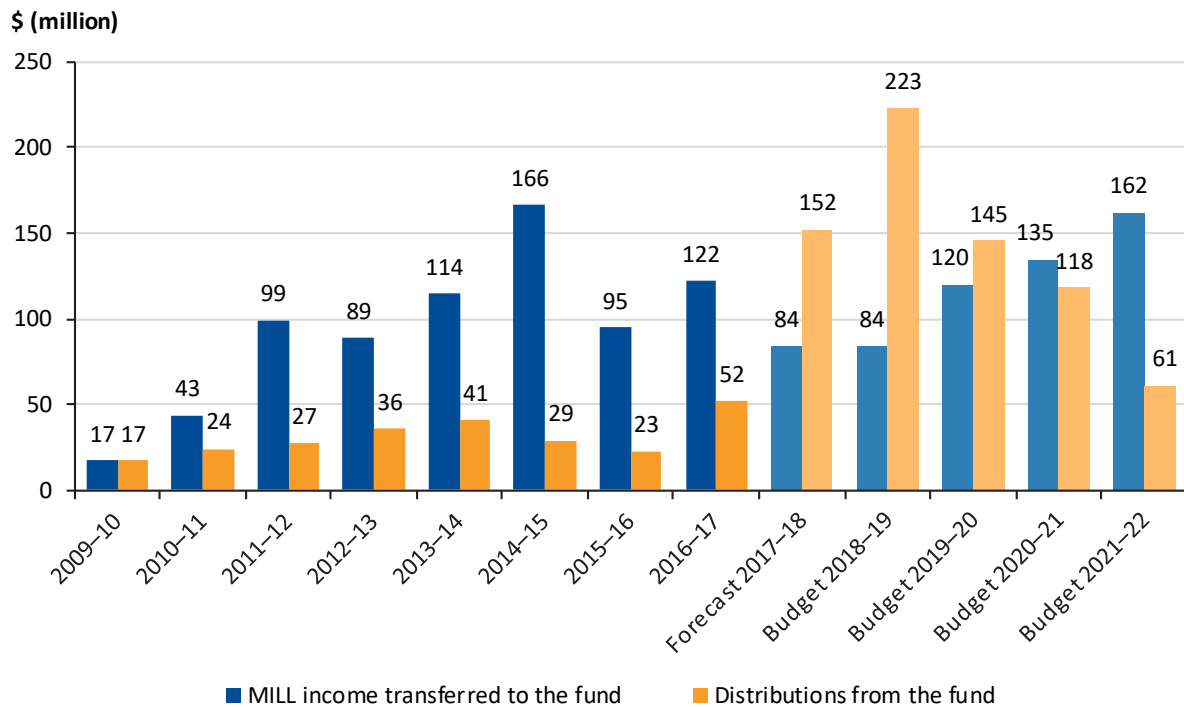
The government has increased funding to environmental agencies, from \$76.1 million to \$130.5 million in the past two years, a 71 per cent increase. This has resulted in less MILL income transferred to the fund.



Figure 1G shows MILL income transferred to the fund and distributions from the fund from 2009–10 to 2016–17 and budgeted income and expenditure for the period 2017–18 to 2021–22.

The 2017–18 Budget provides for fund expenditure of \$439 million in new funding approved over five years between 2016–17 and 2020–21. The forecast amounts included in Figure 1G are more than this as they include future distributions for existing programs.

**Figure 1G**  
**Fund income and distributions**



*Note:* Fund distributions for 2015–16 and 2016–17 are on a cash accounting basis. Forecast and Budget figures for 2017–18 onwards are on an accrual basis and exclude administration costs.

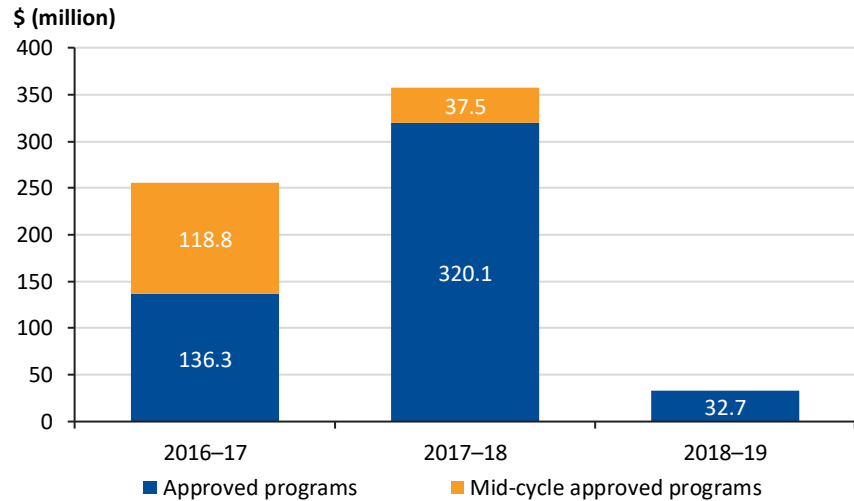
*Note:* The total cash transferred into the fund may not equal the sum of the accrual revenue less distributions in Figure 2A due to timing differences.

*Source:* VAGO based on DELWP and SV annual reports and DELWP forecast data.

Figure 1G shows that the government distributed \$52 million in 2016–17 and expects to spend \$152 million in the 2017–18 financial year. Despite the government’s commitment to spend, actual program expenditure is falling behind budget, resulting in lower than expected expenditure from the fund.

From 2016–17 to 2017–18, budget commitments from the fund have been at their highest levels since the fund was established. However, Figure 1H shows also that commitments from the fund in the 2018–19 Budget drop significantly from \$320.1 million in 2017–18 to \$32.7 million 2018–19.

**Figure 1H**  
State Budget commitments from the fund in 2016–17 to 2018–19



Source: VAGO.

Figure 1I shows the income and expenditure from the fund over the past three years and the impact on the balance of the fund.

**Figure 1I**  
Sustainability Fund Trust Account

	Fund opening balance	Transfer of fund from EPA to DELWP	Return of unspent distribution	Transfers from MILL Trust account	Investment income	Distributions to fund programs	Fund closing balance
2015–16 Actual	\$0.0m	\$383.8m		\$94.6m	\$11.1m		\$466.3m
2016–17 Actual	\$466.3m		\$0.6m	\$121.6m	\$15.3m	–\$23.2m	\$551.1m
2017–18 Forecast	\$551.1m			\$98.7m	\$15.3m	–\$52.7m	\$513.1m
						–\$152.0m	

Note: The amounts above are on a cash accounting basis. The total cash transferred into the fund may not equal the sum of the accrual revenue less distributions in Figure 2A due to timing differences. The amount in distributions to fund programs includes administrative costs.

Note: Prior to the establishment of the Sustainability Fund Trust Account, the money was held in the Environment Protection Fund. As a result, its balance was \$0 in 2015 when it was established.

Source: VAGO based on DELWP data and annual reports.

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## 1.5 Stakeholder interest

There has been substantial interest in the MILL and the fund in recent years. The waste industry and local councils supported the introduction of the levy and the subsequent increases to the levy on the basis that it would fund environmental agencies and the remainder would support innovative waste and resource recovery initiatives.

Waste industry groups, councils and environmentalists have expressed concern over the growth of the fund and the low level of expenditure from the fund on waste and resource recovery initiatives. A recent decision by China to restrict the importation of some recyclable material has further highlighted concerns about the future of the recycling industry. Waste industry advocates, councils and environmental organisations are lobbying the Victorian Government to access the fund to invest in future solutions for recycling.

In February 2018, the Victorian Government announced a \$13 million support package for councils and industry affected by the recent Chinese restriction on recycling imports. This has been approved to be funded from the fund.

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## 1.6 Why this audit is important

The MILL and its distribution is designed to play an important role in minimising the environmental impacts of waste and in promoting investment in alternatives to landfills.

The SWRRIP states that based on the current rate of population growth total waste generation is likely to increase by 57 per cent from 12.7 million tonnes in 2015–16 to 20 million by 2046.

There is significant community concern about how the government and its agencies spend funds generated through the MILL. Some stakeholders are concerned that government may not direct enough funds towards waste management activities.

This audit provides an independent assessment of, and insights into, whether the landfill levy system is being managed transparently and is meeting its intended legislative objectives.

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## 1.7 What this audit examined and how

This performance audit examined DELWP's management of MILL income, including its distribution and expenditure. It assessed how the money is spent and whether and to what extent it aligns with the legislative objectives of the MILL Trust Account and the fund.

The audit examined the management of the MILL Trust Account and the fund since responsibility transferred to DELWP on 1 July 2015. We examined the administrative practices of DELWP since this transfer, considered the impact of legislative changes and compared the structure of funding agreements established prior to the transfer.

We conducted our audit in accordance with section 15 of the *Audit Act 1994* and ASAE 3500 *Performance Engagements*. We complied with the independence and other relevant ethical requirements related to assurance engagements. The cost of this audit was \$520 000.

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## 1.8 Report structure

We have structured the remainder of the report as follows:

- Part 2 examines the distribution and management of the MILL
- Part 3 examines the administration of the fund
- Part 4 examines program outcomes of the fund.

# 2

## Financial management of trust funds

Public monies are set aside in trust accounts for specific purposes, and as such are quarantined from the rest of a department's operations. This places an added premium on good financial management and control, and transparency.

In this part of the report, we consider how well the monies in the two trusts are controlled. We place emphasis on making sure the systems of financial control that support their operation are sound, and operate so that:

- funds are distributed only for approved purposes
- unused cash balances are managed and invested to maximise return
- administration costs are relevant and not excessive.

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### 2.1 Conclusion

DELWP is exercising appropriate financial control over, and management of, trust balances, transfers and disbursements. Administration costs are reasonable and investment performance is meeting the objectives of the investment policy.

However, there are significant control weaknesses in distributions made under section 70E(3)(d) of the Act from the MILL Trust Account—namely ensuring that money is being used for the purpose provided. Money distributed under this provision is not subject to assessment against the legislative objectives. In addition, only 5 per cent of these distributions are subject to financial acquittals to ensure they are used for their intended purpose. This creates a risk that programs may be funded that are not in line with the legislative purpose.

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## 2.2 Transfers

### EPA—MILL collection and transfer

EPA is responsible for the collection of the MILL from licensed landfills and for the transfer of the income to DELWP's MILL Trust Account. Section 70E(2) requires EPA to credit funds to the MILL Trust Account by 15th day of the following quarter. We are satisfied that EPA transfers MILL income to DELWP in a timely manner, consistent with legislative requirements.

### DELWP—MILL Trust Account and Sustainability Fund

When DELWP took over responsibility for distribution of the MILL and administration of the fund on 1 July 2015, the minister approved the establishment of the MILL Trust Account and the Sustainability Fund Trust Account, as required by the Act.

#### MILL Trust Account

DELWP has established appropriate internal controls around transfers to and from the MILL Trust Account. However, not all agencies that receive distributions made under section 70E(3)(d) are required by DELWP to demonstrate that funds provided were used for their intended purpose.

Section 70F(2) of the Act requires the remaining balance of the MILL Trust Account to be transferred to the fund by the end of each quarter.

#### Sustainability Fund Trust Account

We independently confirmed the balance of fund investments as at 30 June 2017.

Payments are subject to DELWP's standard internal controls, financial delegations and supported by evidence of approval by the minister and the Premier.

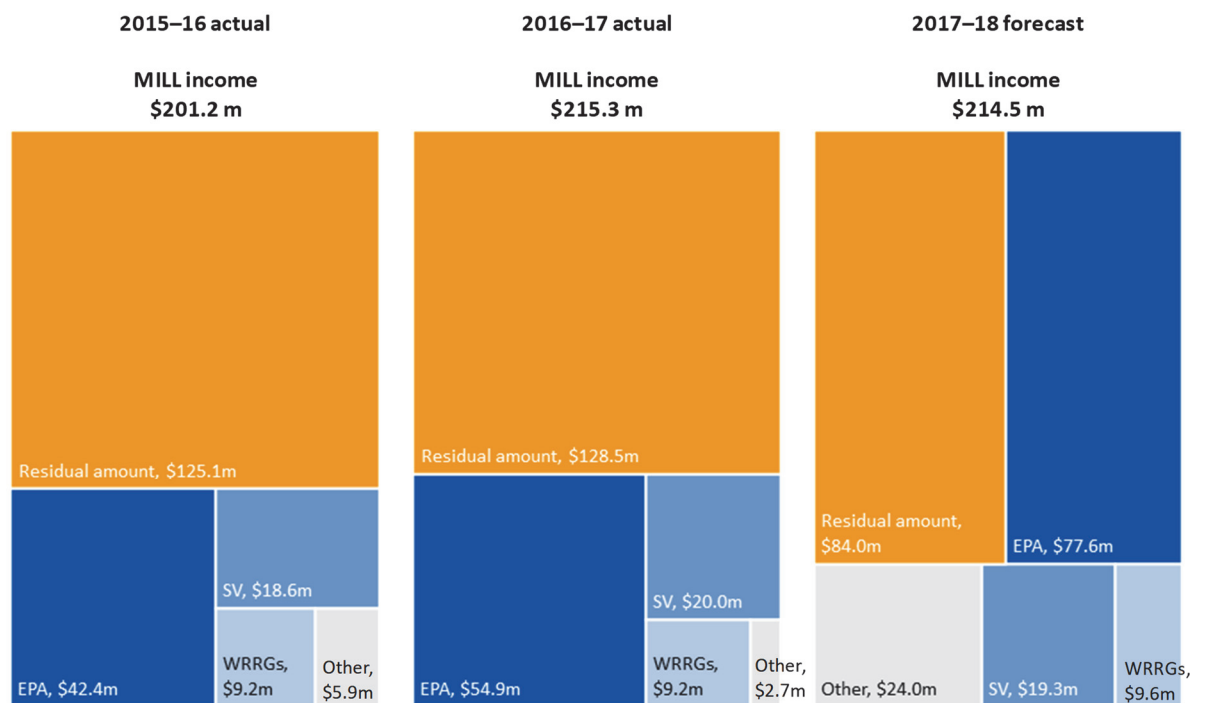
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## 2.3 Distributions

### Distributions from the MILL Trust Account

Distributions from the MILL Trust Account primarily support the core operating activities of specified environmental agencies and from 2014 can also be used to fund a broad range of agencies provided that these monies are 'used for environment assessment, protection, restoration or improvement purposes'. Figure 2A shows MILL income distribution over the past three years.

**Figure 2A**  
**MILL Trust Account distribution**



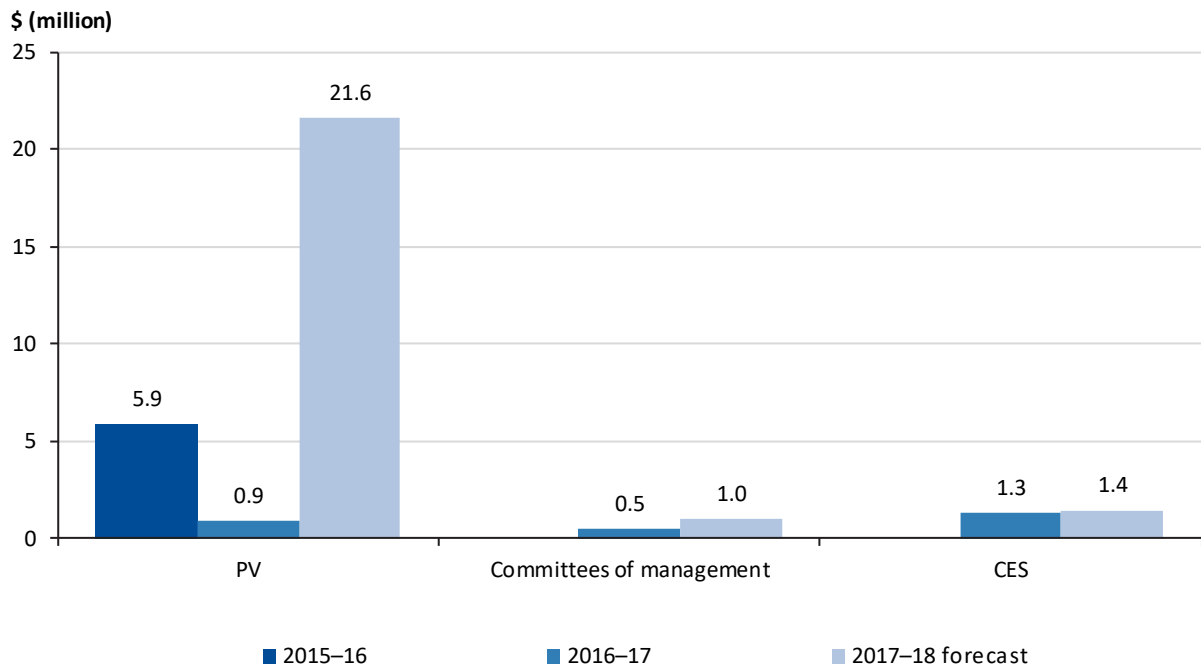
*Note:* The increase in EPA’s distribution from 2016–17 to 2017–18 was a direct result of EPA reform funding initiatives. The amounts above are shown on an accruals basis. Amounts shown in Figures 1G and 1I differ as they are shown on a cash accounting basis.  
*Source:* VAGO based on DELWP data.

Expenditure from the MILL Trust Account is not subject to the same governance framework as the fund. In line with the legislation, the minister determines the amount to be paid from the MILL Trust Account, the timing of payments and period over which they are to be applied.

DELWP’s Energy, Environment and Climate Change policy team brief the minister seeking an approved determination based on DTF-approved estimates of available funding in the MILL Trust Account. These briefings are made collaboratively with the team to ensure there is sufficient funding available for any existing and new commitments made from the fund. The team is responsible for processing agency distributions made under ministerial determination. The team maintains contact with DELWP policy areas to monitor the cash flow impacts of distributions from the MILL Trust Account on the fund.

Over the past two years, funding distributed under section 70E(3)(d) has increased from \$5.9 million in 2015–16 to \$24 million in 2017–18. PV, CES and committees of management have received funding under this provision. Figure 2B shows funding received by each agency under section 70E(3)(d).

**Figure 2B**  
**Agencies funded under section 70E(3)(d)**



Source: VAGO based on DELWP data.

There are currently no guidelines or governance processes to inform or evaluate the use of this funding from the MILL Trust Account and ensure it meets the conditions of section 70E(3)(d). In addition, only committees of management are required to provide financial acquittals to demonstrate that they have used these funds for the purpose provided. These control weaknesses need to be resolved to address the risk that this money is spent on programs that do not align with its legislative purpose. The current arrangement means that it is difficult to identify any unspent funds to ensure they are transferred back to the fund.

DELWP should consistently assess and provide advice on the alignment of any distributions made under this provision and require recipients to provide financial acquittals for this expenditure.



DELWP recognised the importance of ensuring these funds are used as intended by the legislation and has made an effort to assess alignment for the distributions to PV and CES. It obtained legal advice on whether proposed funding for PV and the CES met the intended purpose of the legislation: that is, whether the allocations were consistent with the legislative purpose of 'environment assessment, protection, restoration or improvement purposes'. The advice received stated that funding for the CES met the purpose for environmental assessment and the funding for PV broadly met the legislative purpose of section 70E(3)(d).

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## 2.4 Sustainability Fund investment performance

### Investing unused funds

DELWP has developed an investment policy compliant with legislative requirements that aims to maximise returns and minimise risk.

DELWP's SFIP sets out the general principles that govern the investment of monies held in the fund. The minister delegated the power to approve investments with the Victorian Funds Management Corporation's (VFMC) Capital Stable Fund to DELWP's Executive Director, Finance and Planning in February 2016. The minister did so on the condition that the agency provide a six-monthly report on the fund's cash balance and investments.

DELWP designed the SFIP to operate within the *Financial Management Act 1994* (FMA) and Victorian Government and DELWP investment policies.

The FMA governs DELWP's cash reserve investment, administration and management. The Treasurer's centralised treasury and investment policy, which applies to all Victorian public sector agencies, requires agencies to undertake all investments and financial arrangements with the Treasury Corporation of Victoria (TCV) and/or VFMC. DELWP's Trust Fund Policy requires all trust accounts to maintain a positive balance and be in interest-bearing deposits approved by the Minister for Finance. Agencies investing with VFMC are required to have an investment strategy.

The SFIP is reviewed annually and DELWP's Risk and Audit Committee note revisions. DELWP obtained independent advice on the SFIP as part of the revision that occurred in 2016–17. The advice found that the fund complied with legislation and government policy. It examined how the fund could preserve its balance, minimise risk and maximise return, and recommended the appropriate mix of investments to achieve this outcome. DELWP incorporated all of the recommendations in their policy update in 2017–18.

Funds 'at call' are available for access quickly when needed to make contract payments to fund recipients.

## Investment objectives

DELWP's investment objectives for the fund are to maximise returns on the available cash balance, to ensure that funds are available at call to meet funding distributions, and to comply with legislative requirements.

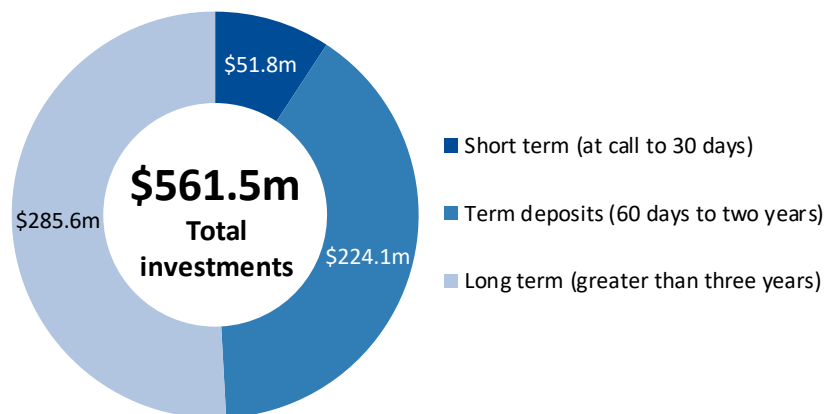
To guide the strategic allocation of long-term investments, the SFIP specifies the following risk and return investment objectives:

- return—Consumer Price Index (CPI) plus 1.5 per cent on a rolling three-year basis for long-term investments
- risk—experience an annual investment loss no more than once every 10 years, and experience a loss greater than 1 per cent no more than once every 20 years.

## Investment profile

DELWP has established investments with TCV and VFMC, consistent with the SFIP. DELWP's short-term investments are with TCV and its long-term investments are in VFMC's Capital Stable Fund, the most conservative investment option offered by VFMC. Figure 2C shows the investment profile of the fund as at 31 December 2017.

**Figure 2C**  
**Fund investment profile as at 31 December 2017**

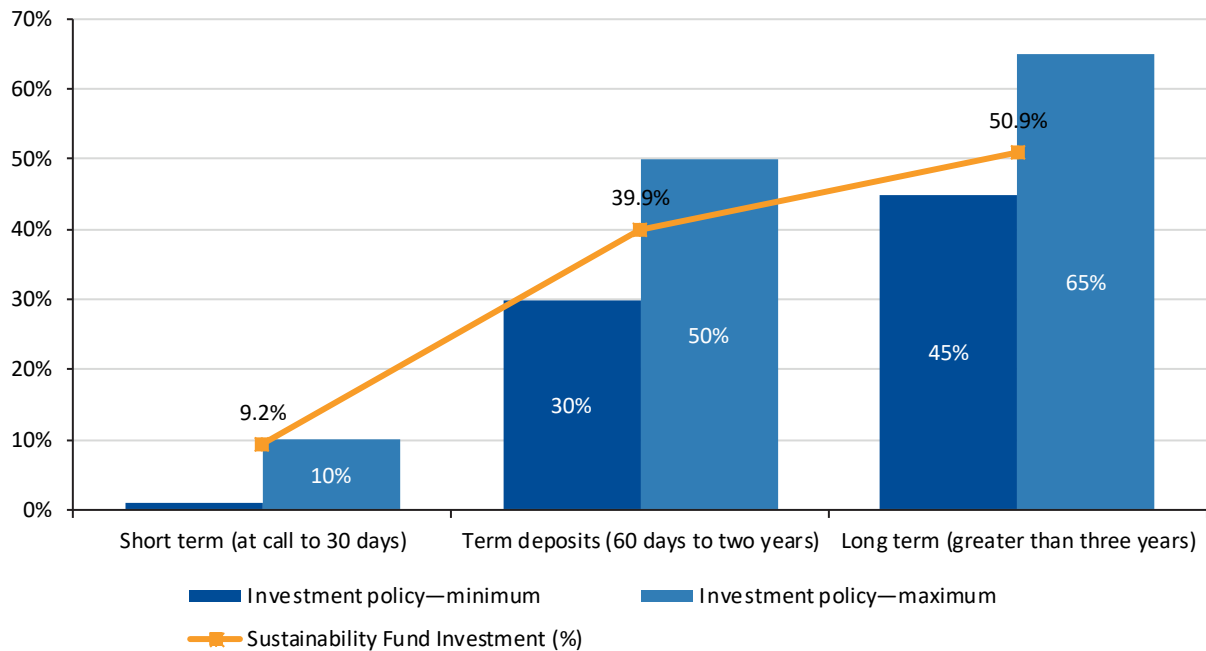


Source: VAGO based on DELWP Quarterly Compliance Report, 31 December 2017.

Our review of DELWP's quarterly compliance reports for the current financial year indicates that the fund mix of investments complies with the SFIP. Figure 2D shows the current fund investment profile compared with the SFIP investment parameters.

**Figure 2D**

**Actual fund investment profile against the SFIP as at 31 December 2017**



Source: VAGO based on DELWP data.

## Investment performance

The fund is achieving SFIP targets and maximising returns. The SFIP target return for long-term investments of 1.5 per cent greater than the CPI, on a rolling three-year basis, equated to 3.2 per cent as at 31 December 2017. VFMC reported that the fund achieved a three-year return of 3.89 per cent to 31 December 2017, 0.69 per cent ahead of the target, and 0.16 per cent ahead of VFMC's performance benchmark. TCV short-term deposits currently return 1.45 per cent to 1.77 per cent.

## Interest

The Minister for Finance granted approval, under section 20 of the FMA, for interest to be earned and retained by the fund when administrative responsibility was transferred to DELWP in 2015.

Prior to its transfer to DELWP, EPA was responsible for the financial management of the fund and retained the interest earned (consistent with the Act) on the fund as a revenue stream to support its operations.

The transfer of the fund to DELWP resulted in a revenue shortfall for EPA. To address this shortfall, the Treasurer approved up to \$15 million in additional funding to EPA for both 2015–16 and 2016–17. EPA received these payments in addition to its distribution from the MILL Trust Account, equivalent to the value of actual investment returns on the fund balance: \$13.80 million in 2015–16 and \$14.65 million in 2016–17.

Interest earnings since the fund transferred to DELWP, total \$36.5 million to 31 December 2017. The interest earned for the year to 31 December 2017 was \$10.5 million. Forecast interest for 2017–18 is \$15.3 million.

### Cash flow forecasting

DELWP invests surplus cash in accordance with the SFIP.

The team monitors cash flows by updating a rolling cash flow forecast monthly. Estimates of MILL income from EPA, distributions to portfolio agencies, investment income and expected milestone payments to funding recipients are progressively replaced with actuals as they become known.

DELWP bases investment decisions on the SFIP and monthly cash requirements of the fund. DELWP uses a milestone payment report from its grant management system, Global Engagement Management System (GEMS), to determine the expected timing of distributions.

DELWP reports indicate that budgeted funding distributions have been underspent since it has administered the fund. This is mainly due to project management issues which are discussed further in Section 4.5 of this report.

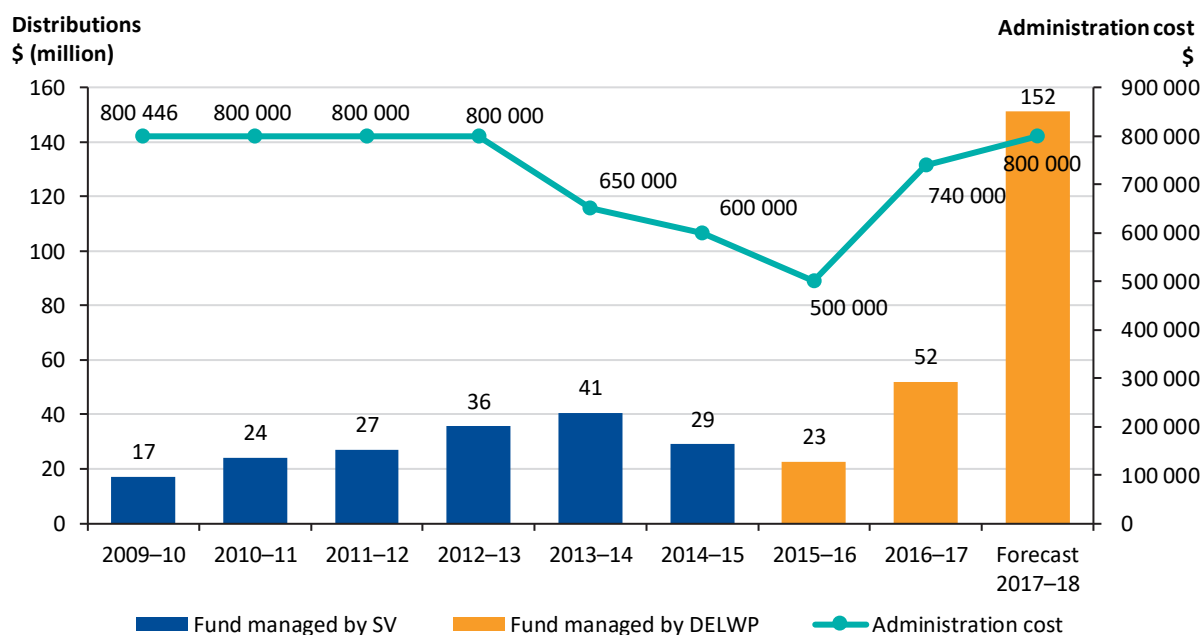
As at 30 September 2017, GEMS shows that actual payments were \$18.2 million compared with an expected \$36.7 million for the quarter—a 50 per cent underspend. As at 31 December 2017, performance had improved, with year-to-date payments of \$52.6 million, in line with the forecast of \$52.1 million. DELWP advised that budgeted cash flows had undergone significant reworking as part of the mid-year State Budget update in December 2017 to align them with contracted milestones and to include the impact of contract variations. We discuss the challenges with project management further in Section 4.5.

Overestimating expected expenditure results in DELWP holding more liquidity than required. However, the variance in return for amounts held at call, in short-term investments and investments for a fixed 12-month period is minimal.

## 2.5 Sustainability Fund administration costs

Administration costs have remained constant despite a significant increase in the activity of the fund. Figure 2E shows administration costs compared to fund distributions over time. The current cost of fund administration compared with distributions is very low. While fund distributions provide an indication of the level of activity, the amount distributed does not reflect the effort involved in other administrative activities such as establishing memorandums of understanding (MoU) for new projects.

**Figure 2E**  
**Administration costs compared to fund distributions**



Note: Administrative cost for 2017-18 is the budgeted amount.

Source: VAGO based on DELWP and SV data.

The activity of the team and committee has increased as the value and number of programs approved for funding from the fund has gone up. However, the administrative budget has remained at \$0.8 million for 2016-17 and 2017-18.



# 3

## Sustainability Fund management

The public's trust in government depends on transparency and accountability. The fund's governance and transparency issues identified by the 2013 MAC report eroded this trust and undermined public and industry confidence. It is important therefore, that the current operating arrangements address past governance issues. The committee, which replaced the independent statutory committee, has a significant role to play in this regard as, under the Guidelines it should:

- oversee fund management to support fund transparency and accountability
- provide impartial, strategic advice regarding allocations from the fund.

The committee's advice to the minister is important to ensure proposals meet legislative and eligibility requirements and that sufficient information is provided to ensure proposals with the greatest merit are prioritised.

In this part of the report, we examine how proposals seeking money from the fund are selected and the role of the committee and the team in supporting the minister prior to, and after, government deliberations about the merits of these proposals.

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### 3.1 Conclusion

The committee has identified and made attempts to address a range of procedural, structural and governance issues. However, more needs to be done to enable it to effectively fulfil its role:

- The committee should support its advice to the minister with clearer, and more definitive, comprehensive information. This information should provide sufficient detail to enable merit based decisions that prioritise proposals seeking funding and clearly describe the degree to which proposals comply with the legislation.
- The committee should improve its record keeping to ensure it has complete and reliable records of its deliberations, to improve transparency and accountability.
- DELWP should put in place a formal process for the committee to review and comment on the final version of all proposals considered by the Premier and minister before their approval to stop proposals being approved that bypass the committee, in contravention of the Guidelines.
- The inherent conflicts of interest that result from the administrator also being a major beneficiary of funding must be addressed.

The Guidelines are unclear on how to deal with requests that seek a component of ongoing funding, or move programs from annual appropriations. There is also lack of clarity about what constitutes 'core administrative costs', which are ineligible for funding. These ambiguities are particularly sensitive in the context of a hypothecated fund, where a levy is collected for a particular purpose with the public therefore reasonably expecting that fund expenditure should meet that purpose.

While there is no evidence that any program that received funding from the fund does not align with its legislative objectives, there is a potential risk this may be the case. This is because the committee has not considered and provided advice on all approved programs. In addition, some of those that it has considered were approved despite concerns about legislative alignment.

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### 3.2 Evaluation criteria

The Guidelines state that the committee will provide impartial strategic advice to the minister and Premier regarding allocations from the fund, based in the first instance on:

- alignment of the objectives with the legal objectives under the Act
- alignment of the expected outcomes of the proposal against the defined priorities of the fund as included in the Priority Statement
- the value for money and funding requirements of the project in light of the immediate and long-term environmental benefits that will be achieved
- the availability of funding to the applicant from other funding sources.



## Ineligibility criteria

The Guidelines include six ineligibility criteria:

- proposals that seek retrospective funding for projects or programs that have already started or that have been completed
- applications for funding to supplement the core administrative costs of an existing organisation
- projects that duplicate programs already operating with respect to a specific environmental priority
- projects that are considered inconsistent with government policy objectives
- projects not meeting state and national legislative requirements, and other relevant statutory approvals and permits
- applications not made in accordance with the guidelines.

DELWP advised that the team considers the eligibility of a proposal prior to providing advice to the committee. They only bring eligible proposals to the committee for consideration. However, the team does not document its eligibility assessment. This diminishes accountability and is inconsistent with the record keeping requirements that apply to decision-making.

## Application of evaluation criteria

The team and the committee assess proposals according to their:

- Impact—does the proposal address the problem it aims to fix and deliver social outcomes?
- Quality—does it have clearly stated objectives, outcomes and deliverables, a well-developed budget and plans to complete a project evaluation?
- Policy alignment—is there alignment with legislative objectives and priorities?
- Value for money (new for 2018–19, previously included in the Impact criterion)—what is the potential return on investment? Is the proposal ‘shovel-ready’? Is it scalable? Is there potential for the project to leverage additional or new investment?
- Outstanding issues—this deals with any concerns that the committee might have about the project. It includes questions raised that the policy area has not responded to or concerns about the project based on the experience of similar projects or proposals.

When we compared the evaluation criteria in the Priority Statement and Guidelines with the criteria the team and the committee use to assess funding proposals we found that the committee’s assessment process is not fully aligned with these two overarching foundation documents. The team and the committee use the evaluation criteria identified in the Guidelines to determine their recommendations and advice to the minister. However, the application of the value for money assessment lacks sufficient depth and the documentation of any analysis of options for alternative funding sought is inconsistent.

Figure 3A shows our analysis of the alignment of the criteria used by the team and committee in their 2017–18 and 2018–19 assessments.

**Figure 3A**  
**Evaluation criteria**

Evaluation criteria included in the Guidelines	Team or committee criteria	Alignment of criteria
Compliance with legislative objectives	Assessment table clearly notes alignment with climate change, waste or both	Yes
Merit relative to the Priority Statement	Assessment table clearly notes alignment with Priority Statement	Yes
Proposed value for money in light of the immediate and long-term environmental benefits that will be achieved	Included as criteria but not well assessed	Yes
Options to fund from alternative funding sources	Alternative funding sources are documented inconsistently in committee advice	Partly

Source: VAGO.

As shown in Figure 3A, the team and the committee only fully use three of the four evaluation criteria referenced in the Guidelines to assess proposals. In 2017–18 and 2018–19 the committee provided advice that five proposals should seek funding from appropriations. However, it does not consistently document its assessment against this criteria for each proposal. To be consistent with the Guidelines the committee should clearly document its assessment of options to fund from alternative funding sources for each proposal. Without this assessment and subsequent advice, the minister will not be fully informed about the most appropriate funding source for each proposal.

### Value for money assessment

Value for money is the achievement of a desired outcome at the best possible price, not necessarily the lowest price, based on a balanced judgement of financial and non-financial factors relevant to the procurement. In the context of the fund it is expected that the committee considers these factors in light of the immediate and long-term environmental benefits that a program will achieve.

In 2017–18, the team and committee included value for money in their impact evaluation criteria but did not separately document and provide advice on these. For 2018–19, the committee established a value for money criterion and separately listed it in the evaluation documentation.

We reviewed all assessments for 2017–18 and 2018–19 and found that they did not include a clear analysis of value for money. There was also no indication of which projects provided the best value for money considering the immediate and long-term environmental benefits that will be achieved. The committee does not consider factors such as costs and resources, fitness for purpose, time lines and risk. DELWP advised that the committee discusses these as part of its deliberations but does not document this assessment.

Although the nature of some funding proposals evaluated present challenges for value for money assessments, there is a need for greater rigour in how this criterion is applied. The extent of this assessment should reflect, at a minimum, program risk and value. The committee has reviewed proposals ranging in value from \$5 million to \$196 million with no substantive variation in the approach used.

DELWP advised that each funding proposal includes an analysis of value for money in its business case. However, the committee does not consistently complete a value for money assessment that contains sufficient evidence to enable the minister to determine which proposals are most cost-effective. In addition, a clear evaluation of how each proposal performs against this criterion is not included in the advice provided to the minister in 2017–18 and 2018–19.

### Other considerations

The committee should document its consideration of other relevant factors included in the Priority Statement and Guidelines as part of their assessment of proposals.

The Priority Statement includes that preference should be given to initiatives that foster employment, new technology and innovation, resource efficiency or ongoing behaviour change.

Of the 24 proposals assessed by the committee between 2017–18 and 2018–19, 15 (63 per cent) considered these issues. In the remaining nine there is no evidence the committee assessed how well proposals demonstrated they address these criteria. Twelve of these cases (80 per cent) noted that the project fosters innovation and the remaining three noted resource efficiency and ongoing behaviour change. However, without definitions to inform the assessment of these impacts, it is difficult to determine whether and to what extent the committee has or should consider these matters.

The Guidelines also state 'The purpose of the Fund is to support projects, programs, services or technologies that will benefit Victoria environmentally, socially and economically'. While the committee's 'impact' criteria requires an assessment of the extent to which proposals address or deliver social outcomes it does not consider other impacts. The committee should consider expanding this assessment to include an assessment of environmental and economic impacts of proposals. There is a risk that eligible programs that have a strong economic or environmental impact may be overlooked for funding.

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### 3.3 Application of the Guidelines

#### Core administrative costs

As noted above, the Guidelines specify that applications for funding to supplement core administrative costs are ineligible. Our discussions with DELWP staff revealed that there is no common understanding or consistently applied definition of what constitutes core administrative costs. We found seven examples where the committee recommended proposals that may conflict with this guidance. Due to definitional ambiguities, there is a risk that the committee recommended proposals that may contain core administrative costs and were therefore ineligible.

We identified one instance in 2017–18 where the committee highly recommended funding for ongoing staff for a component of a proposal that appeared to be administrative in nature. DELWP advised that the ongoing component of this bid was removed before it was submitted to ERSC.

The January 2018 committee meeting papers noted a number of funding requests for core government work and departmental staffing. The 2018–19 submissions seek funding for ongoing staff, which may be an example of core administration costs, equating to 16 per cent of the value of the submission total. The committee recommended or highly recommended all but one of these proposals, which may be in contravention of the above ineligibility criterion.

DELWP has advised that these examples related to proposals based on expanding service provision into new areas and therefore did not cover core administrative costs. However, in the committee's December 2017 letter to the minister, it noted the above costs were for a 'high level of core government work and departmental staffing'. This highlights the need for an agreed definition of what constitutes 'core administrative cost' and which component(s) of staffing costs are and are not eligible for funding.

The minister has recently approved an update of the Guidelines, as part of DELWP's response to the audit, to provide better clarity about the advisory function of the committee and definition of core administrative costs.

#### Ongoing funding

The Guidelines do not specify how to deal with proposals seeking ongoing funding. The committee recognises that this is an emerging issue for 2018–19 proposals due to the cumulative size of requests for 2018–19. It has raised this issue in advice provided to the minister.

DELWP advised that \$20 million in ongoing funding that was not part of the original bid was approved in 2017–18. Funding agreements for these projects have been established for a four-year period. This gives the team and committee the opportunity to reassess and provide advice to the minister on programs that have received ongoing funding and the appropriateness of using the fund for this purpose.

DELWP then requested a total of over \$80 million in ongoing funding as part of eight of its proposals in the 2018–19 Budget process. However, no ongoing funding was approved in the 2018–19 Budget.

The committee discussed this issue in a number of the meetings we attended. We observed that there was robust discussion about the merit and risk to government of using the fund for ongoing funding.

The committee’s advice to the minister for 2018–19 recommended the ongoing funding but noted its use may curtail innovation and the ability of government to ensure effective alignment between funded work, statutory objectives and government’s priorities for the fund.

It advised ‘If proposals continue to seek ongoing funding at the current quantum, the committee may need to consider reviewing its alignment criteria and recommend caps be applied for ongoing commitments to maintain capacity to fund new programs.’

To ensure that the committee can reassess these funding streams, it advised the minister that the team should build a requirement for a four-yearly evaluation in the funding agreements to ensure continuing alignment with the objectives and priorities of the fund. On the review of each evaluation, the committee would provide advice to the minister if alignment concerns arise. The committee’s letter to the minister reflects the risks of using the fund for ongoing funding.

Despite this, there is currently no documented or formal requirement for this to occur for the program that received ongoing funding in 2017–18.

### Programs previously funded from appropriations

The Guidelines also do not specify how to deal with programs that are looking to shift their funding from appropriations to the fund. An increasing number of proposals attempt to transfer funding of existing DELWP programs to the fund, where there is alignment with the fund’s legislative objectives.

For example, DELWP’s biodiversity, threatened species, land remediation and beach renourishment programs, previously funded through appropriations, are now funded from the fund. Figure 3B is an example of a program that was previously funded through appropriations.

#### **Figure 3B Biodiversity**

During the 2017–18 budget cycle, DELWP sought funding for a biodiversity program from the fund rather than through appropriations.

The committee felt that the proposal should continue to be funded from appropriations rather than the fund. In their advice to the minister, the program was marked as needing ‘More Information’, showing the committee had insufficient information to assess the proposal’s alignment with the fund’s legislative objectives.

In the end a decision was made to fund the \$86.3 million program Protecting Victoria’s Environment—Biodiversity 2037 from the fund.

Source: VAGO.

The committee's terms of reference state that it should provide input into the revision of the fund's Priority Statement and Guidelines. It should drive the revision of the Guidelines so that there is clarity about the appropriate short- and long-term application of monies from the fund and what should be taken into consideration when programs look to shift their funding from appropriations.

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### 3.4 Alternative approval pathways

DELWP took responsibility for fund management on 1 July 2015. Until it had finalised the formal governance structures for its new role, it was not able to provide recommendations to the minister about which proposals to support in the 2016–17 budget process. During this time, the team did, however, conduct preliminary assessments of funding proposals for that year and shared these with DTF and DPC to inform their budget deliberations.

DELWP established the committee in May 2016 but not all members were appointed until December 2016. As a result, the committee was also not able to provide any advice directly to the minister on proposals for funding from the fund during the 2016–17 mid-cycle budget review. The team did not provide advice in the committee's absence. DELWP advised that this was due to significant time constraints associated with the preparation of the mid-year submission.

The total value of the proposals approved for funding from the fund in the 2016–17 mid-year budget was significant. ERSC endorsed five proposals for approval, at a total value of \$118.8 million without advice from the committee.

For the 2017–18 budget cycle, the committee advised it assessed and provided advice to the minister on all DELWP proposals seeking funding from the fund. However, there is no documented assessment by the team or the committee of two DELWP programs approved. They also did not provide advice to the minister on proposals from other departments. This makes it difficult to assess if they completed their work transparently or if it is merit-based.

In the 2018–19 budget process, the team assessed and documented all DELWP funding proposals against the evaluation criteria and provided this to the committee for discussion. The committee then advised the minister on the funding proposals. ERSC endorsed four proposals for funding from the fund and these were announced in the 2018–19 Budget. One of these proposals was not supported by the committee. The committee reassessed the proposal but did not change its position. It is now not included in the proposed programs to be funded from the fund, and the committee has provided advice on the remaining proposals. DELWP will refer them back to the minister and Premier for approval. These proposals followed the regular pathway.

However, all programs proposed for funding in 2018–19 are DELWP programs. Funding proposals from other agencies in 2017–18 bypassed a significant part of the assessment process. The committee only became aware of these proposals once ERSC considered them. As a result, it did not formally assess these proposals against the evaluation criteria before ERSC considered them.

In 2018–19, DELWP sought advice directly from other departments on potential funding proposals they submitted. Despite this, the team was aware of two potential proposals from other departments that it was not able to assess or provide advice on before ERSC consideration. This is a risk because it means the committee was not able to inform the minister about the alignment and merit of these bids to the objectives of the fund before ERSC discussed them. Ultimately these proposals were not funded from the fund.

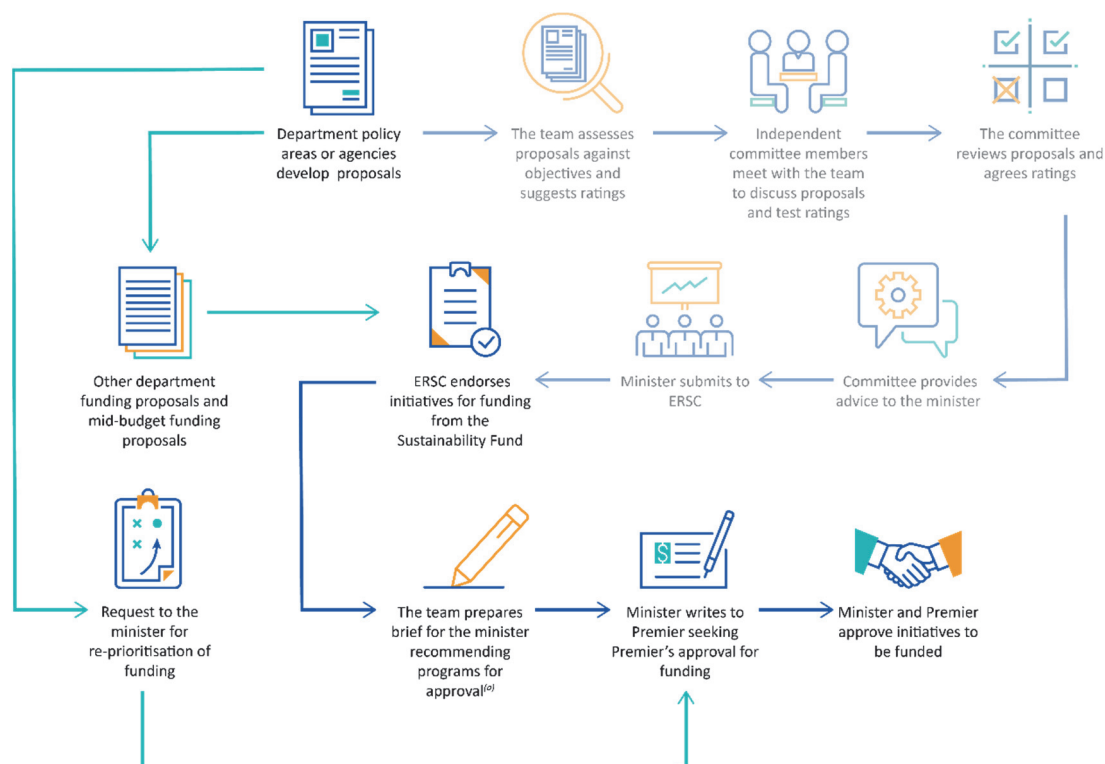
DELWP took action to identify proposals from other departments seeking funding from the fund prior to their submission to ERSC. This included working with DTF to amend the 2018–19 State Budget Bid Template to include a nominated source of funding category and directly approaching departments prior to their submission to ERSC.

However, the nature of the budget process and its time constraints makes it challenging for the committee to get access to all other departmental funding proposals.

To address this issue DELWP advised it is seeking approval from the minister and Premier for a process to ensure the committee provides advice on any proposals that bypass the regular pathway before they are approved by the minister and Premier.

Figure 3C shows the alternative approval pathways that proposals can take.

**Figure 3C**  
**Alternative approval pathways**



(a) The ministerial briefing for the Timber Plantation Establishment program noted that the program will be subject to an assessment by the committee against legislative objectives.

Source: VAGO.

Section 70A(1) of the Act requires that the Premier and minister must not consent to the application of any money from the fund unless there are **in force** [emphasis added] guidelines as to how they will exercise their powers.

The Guidelines state:

Projects may be funded based on direct recommendation of the Committee. For any other proposals, the Premier and the Minister will seek advice from the Sustainability Fund Manager directly or via the committee before allocating Fund monies to a project, so that they are informed about compliance of the proposal with legislated obligations, its consistency with the priority statement and other considerations such as value for money.

In 2017–18, five funding proposals did not comply with this requirement. The minister and Premier did not always seek advice from the committee before allocating fund monies to a project and the Sustainability Fund Manager did not act as an alternative advice source from the committee. It is unclear therefore how they were informed about compliance and consistency with legislated obligations. In 2018–19 the committee provided advice on all programs proposed for approval.

The committee advised that it is aware of the need to have a stronger process to test proposals that other agencies put forward. Its ability to fulfil its role varies depending on the point along this alternative process at which it becomes aware of the proposal. As Figure 3C illustrates, the committee is sometimes not aware of them until after ERSC considers them, as a result there is a risk that some requests receive more scrutiny than others. As noted above, plans are in progress to establish new processes to address this issue.

Figure 3D describes the one case where the committee has successfully challenged a proposal that ERSC endorsed.

**Figure 3D**  
**Water efficiency program**

As part of the 2015–16 Budget, the government announced the creation of the Water Sector Productivity Inter-Departmental Committee (WS PIDC) as a mechanism to drive water sector efficiency and productivity. The WS PIDC was to be funded from the fund, at a cost of \$250 000.

When DELWP assumed responsibility for fund management, the team identified that the WS PIDC may not align with the legislative objectives of the fund. The team discussed the project with staff within the Water Division to see whether they could reshape the funding proposal to provide better alignment.

The team formed the view that, rather than being a catalyst for improvements in waste management, the proposal's focus was on industry productivity. Cost reduction rather than investment in wastewater innovation and development was the clear aim of the project.

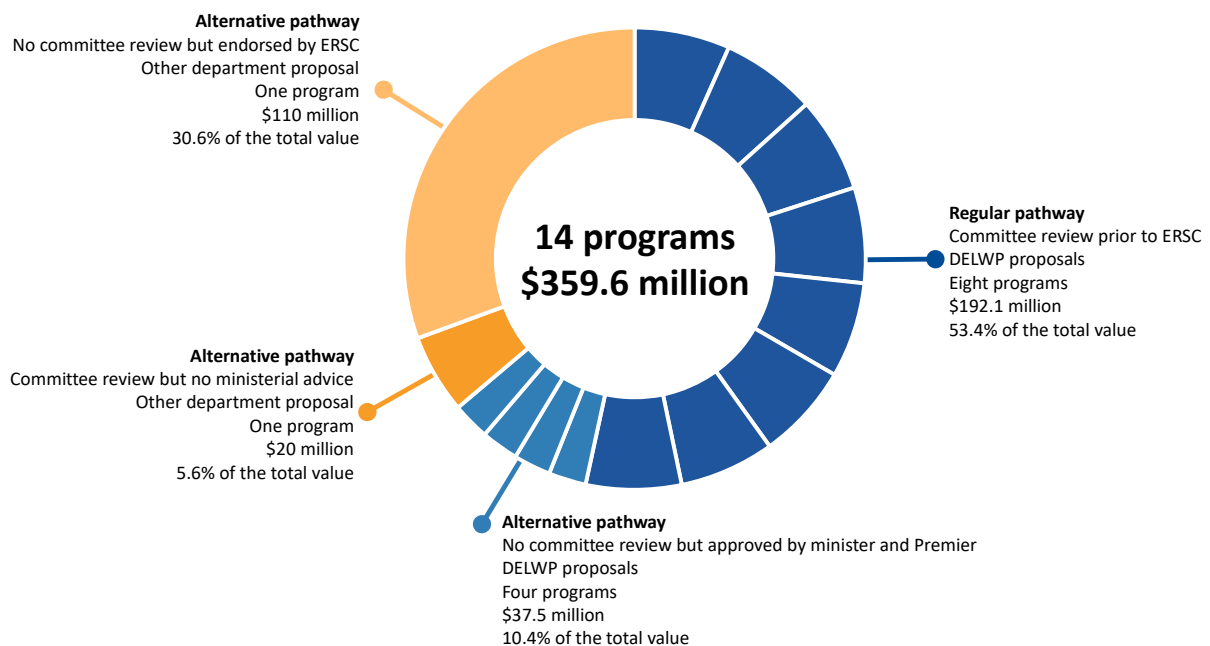
As a result, DELWP's executive team agreed that it would be more appropriate to fund the program from internal reprioritisation rather than from the fund.

Source: VAGO.



Figure 3E provides an overview of the approval pathways for programs approved in 2017–18. It shows whether the committee assessed funding proposals and provided advice on the programs that were approved.

**Figure 3E**  
**Approval processes 2017–18**



*Note:* The total in this figure includes \$320.1 million approved budget plus \$37.5 million in mid-budget approvals consistent with the information provided in Figure 1H. This figure includes an additional \$2 million of reprioritised funding.

*Source:* VAGO based on program values from the Victorian Government's *Budget Paper No. 3, Service Delivery 2017–18* and DELWP information.

Only eight programs or 53 per cent of the value of approved programs went through the 'regular' pathway, which means the committee reviewed and provided advice to the minister prior to consideration by ERSC. Within this category the advice provided was at varying levels of completeness with the committee not assessing at least one program against evaluation criteria or giving it a rating. The remaining six programs went through one of three possible alternative approval pathways.

The committee assessed nine of the 14 programs that received funding for 2017–18, provided advice on eight of these, but did not include a rating against evaluation criteria for one approved program and one component of another approved program.

Of the eight programs that went through the regular process the committee rated one whole program and a component of one program as needing 'more information' and did not rate one program. It did not rate but provided advice to the minister on one part of another program which lacked links to the legislative objectives and recommended that it should be funded from appropriations. This means the committee only assessed against evaluation criteria, rated and provided advice to the minister on four out of the 14 programs approved for funding in 2017–18.

DELWP advised that in 2017–18 the committee informally assessed the alignment of any bids it had not already seen before the minister and Premier approved them. However, we have not seen documented evidence to support this. The 2017–18 ministerial briefing does not contain information about the alignment of the additional proposals before requesting the minister's sign off. The 2017–18 process exposed the minister and Premier to the risk that proposals may have been approved that did not align with the fund's legislative objectives.

During 2017–18, a DPC bid bypassed the committee. ERSC endorsed it without the committee considering its alignment with the fund's legislative obligations or Priority Statement. Furthermore, it was the highest value bid approved from the fund that year, and represents the highest value bid ever approved from the fund. Figure 3F summarises this bid.

**Figure 3F**  
**Timber plantation establishment**

In the 2017–18 Budget, government announced a \$110 million project to establish a timber plantation using money from the fund. This was a DPC initiative.

DPC advised that the bid was in line with the fund's objectives and Priority Statement owing to its links to biodiversity. The project aims to provide funding to establish a timber plantation in the Latrobe Valley, to support the long-term sustainability of Victoria's timber-harvesting industry. The description of this project does not include any biodiversity benefits. DPC advised that there was not a formal business case considered by ERSC, however, it used a consultant's report to inform its budget decision. There is no documented assessment of how the project meets the fund's objectives or Priority Statement and provides the best value for money to achieve these objectives.

Funding for this project is being held in contingency until DPC meets milestones set by the Treasurer. On their achievement, the Treasurer will release the funding for the minister and Premier to approve. DELWP advised that it will not make payments for this project until an agreement is in place. DELWP has advised that during the development of the funding agreements consideration will be given to the alignment of this proposal with the legislated objectives.

The committee requested documentation to enable it to conduct an assessment of the project's alignment with the fund's legislative objectives and Priority Statement. Almost a year later, DPC has not provided the committee with this documentation.

In the absence of a clearly documented rationale informing its selection, it is not possible to determine whether the project is consistent with the purposes of the fund.

Source: VAGO.

In 2017–18, there was not a process to ensure the committee assessed all funding proposals prior to submission to ERSC or following ERSC endorsement. This meant its advice was incomplete to the extent that not all submissions were assessed. Consequently, it does not fully inform the minister and Premier about the merit, risks and value for money of funding proposals before they make funding decisions.

For 2018–19, the committee provided advice on all four programs that have been proposed to receive \$32.7 million of fund money. These proposals went through the regular pathway and the committee assessed and provided advice on them before they went to ERSC. However, it did not document its assessment of one proposal against the evaluation criteria as required by the Guidelines.

### Reprioritisation of funding

Reprioritisation occurs when departments cancel programs or have unspent funds that they earmark for redirection to other initiatives. Only one reprioritisation has occurred since the committee was established. This request went directly to the minister and the Premier for assessment and approval, bypassing the committee.

In 2016–17, unspent funds of \$325 941 from the Advance Organics program were requested to be redirected to another program—‘Waste to Energy’. The minister approved this. While we recognise that the latter program had already been through the approval processes, there was no assessment of whether this was the best use of this money. Without committee assessment against the objectives, the minister does not have complete advice to determine whether this, or for example a previously unsuccessful proposal, is more worthy of funding.

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## 3.5 Effectiveness of the committee

### Committee advice

The committee uses a rating system to assess funding proposals based on alignment with legislative objectives, quality, value for money and outstanding issues. However, within each rating category, there is not sufficient detail to enable the merits of each proposal to be ranked.

In the 2017–18 budget process, the committee recommended each proposal to the minister using one of the following ratings:

- Highly Recommended—strong legislative and priority alignment, quality, value for money and no outstanding issues
- Recommended—moderate legislative and priority alignment, quality, value for money and no significant outstanding issues
- More Information—more information or improvements required to achieve a recommended rating.

The committee did not use a 'do not recommend' rating during that year. This decreases the value and clarity of the advice provided to the minister. The committee's recommendations are equivocal and open to interpretation. Greater detail would provide the minister with better information on which to base decisions on the best use of fund monies.

Figure 3G shows the committee identified four of the 2017–18 funding proposals as requiring more information or as not rated. The minister and Premier approved all for funding.

**Figure 3G**  
**Committee advice on 2017–18 funding proposals**

Committee rating	Number of proposals committee rated	Number of programs approved
More Information	2	2
No rating	2 <sup>(a)(b)</sup>	2
<b>Total</b>	<b>4</b>	<b>4</b>

(a) The committee advised that one program not rated in 2017–18 should seek funding from appropriations.

(b) Committee advice to the minister on the other program states there is alignment with legislative objectives but provides no rating.

Source: VAGO.

The committee determined that it needed more information before it could provide a recommendation on one proposal and for one part of another proposal. However, it is not clear whether it actually required more information or whether the proposal did not adequately align with the legislative objectives of the fund. This is because for that year there was no 'do not recommend' option in the assessment process.

The committee's letter to the minister states that one of the funding proposals that was not rated by the committee 'lacks links to Sustainability Fund and should seek appropriation'. The minister approved the program.

Although the minister and Premier approve programs at their discretion the committee needs to provide the most clear, comprehensive and definitive advice possible to fully inform them when they make this decision.

The committee addressed this, in part, in the 2018–19 budget process when it included a new rating—Not Currently Supported (NCS).

The committee 'Recommended' or 'Highly recommended' 91 per cent of DELWP's proposals or their parts. It did not support part of one proposal and 'Recommended with comment for additional consideration' for two others. It is not clear how the latter rating differs from the 'More Information' rating as there is no documented definition.

There was only one instance where the committee felt more information was required. Where proposals do not align with objectives or priorities, the committee advises agencies how to fix these, before finalising its assessment of how well proposals meet the legislative objectives of the fund.

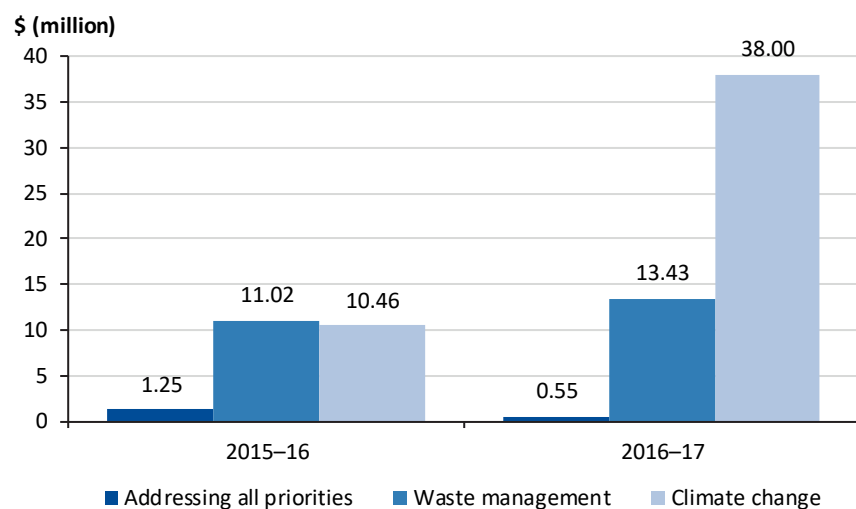
In the 2018–19 Budget it was announced that the Protecting Port Phillip Bay and its Beaches program will be funded from the fund. This program is made up of two components. The committee rated the Beach Renourishment component of this program ‘NCS’ because it did not align with the legislative objectives of the fund. The committee discussed this program at its meeting in May 2018 following ERSC endorsement of this proposal and its announcement in the Budget. There was no change to the proposal or additional evidence provided and as a result the committee did not change its position on this program. As a result, DELWP does not intend to include this program in its list of those proposed to receive fund money.

This year, for the first time, the value of proposals seeking funding totalled more than the amount of money in the fund. To provide better advice to the minister on the best use of the fund the committee should consider how it can further improve its ratings system and the advice it provides. The committee should increase the level of detail included in its advice, to allow the minister to differentiate the merits of one proposal compared with another.

### Alignment to legislative objectives

The committee assesses funding proposals for alignment of their objectives with the fund’s legislative objectives. Figure 3H shows the distributions from the fund by legislative objective. Following revision of the Priority Statement in 2016, there was a considerable increase in funds allocated to climate change initiatives.

**Figure 3H**  
**Fund distributions by legislative objective**



Source: VAGO based on DELWP data.

## Challenging poor alignment

Where the committee has questions about alignment with the fund's legislative objectives, the team works with the policy areas within the relevant department to, where possible, more clearly align the project with the objectives. If this is not possible, or doubts remain, the committee seeks legal advice on the matter.

DELWP sought legal advice on four occasions to provide guidance in relation to expenditure from the fund. This advice was relevant to seven initiatives endorsed for funding by ERSC.

Figure 31 provides three examples of where it used legal advice to help it assess whether endorsed initiatives align with the fund's legislative objectives.

**Figure 31**  
**Legal advice on fund programs**

### **Threatened Species Protection Initiative**

In 2015, the government approved funding the \$6 million Threatened Species Protection Initiative from the fund. It included several programs designed to assist in the protection of Victoria's most threatened flora and fauna. In 2015, during program development, DELWP sought advice from the Victorian Government Solicitor's Office (VGSO). The advice concluded that the initiative was consistent with one of the legislative objectives of the fund. To more clearly align with the fund's legislative objectives, the advice suggested that DELWP make this clearer by editing the associated program plan to better describe elements of adaptation, efforts to address climate change and fostering innovation. DELWP explained that it did not provide the committee with this advice when it was considering other related proposals because it obtained the advice before the committee was established.

### **Critical Coastal Protection Assets**

DELWP also sought advice on projects related to coastal risk management and general coastal management. VGSO formed the view that these were unlikely to satisfy fund criteria. Only those projects that had a purpose linked to climate change adaptation in Victoria would be likely to qualify for funding. The 2016–17 Budget allocated \$15 million to the Critical Coastal Protection Assets project from the fund. Although this was not one of the projects assessed by VGSO, there is no evidence that the committee considered whether previous advice on this issue was applicable despite its similarities to other coastal management projects.

### **Greener Government Buildings**

The Greener Government Buildings program aims to provide energy-efficient lighting, solar energy and battery storage to government buildings in Victoria. In November 2015, VGSO advised the committee that this program did not align with the legislated objectives of the fund. DELWP was concerned that VGSO based its advice on a particularly narrow view of the legislation. As a result, it sought independent legal advice in December 2015. This advice took a broader view of the legislation and concluded that the program did align with fund objectives. The committee decided that more information was required but did not provide this advice to the minister. Its assessment made reference to the VGSO advice obtained but not the independent advice. In 2017–18, \$20 million was allocated from the fund for the program.

Source: VAGO.

These examples show that DELWP and the committee have used legal advice to help interpret and understand the extent to which the fund can be used to support various government programs and initiatives. However, DELWP has not consistently shared this advice with the committee to inform its deliberations, rather it decides when it is relevant to do so. Therefore, the committee has not been able to consider whether it was relevant and adequately acquitted before providing advice to the minister about the alignment of proposals with the fund's legislative purposes. This means the minister does not necessarily have all the relevant information when deciding which programs to invest in from the fund.

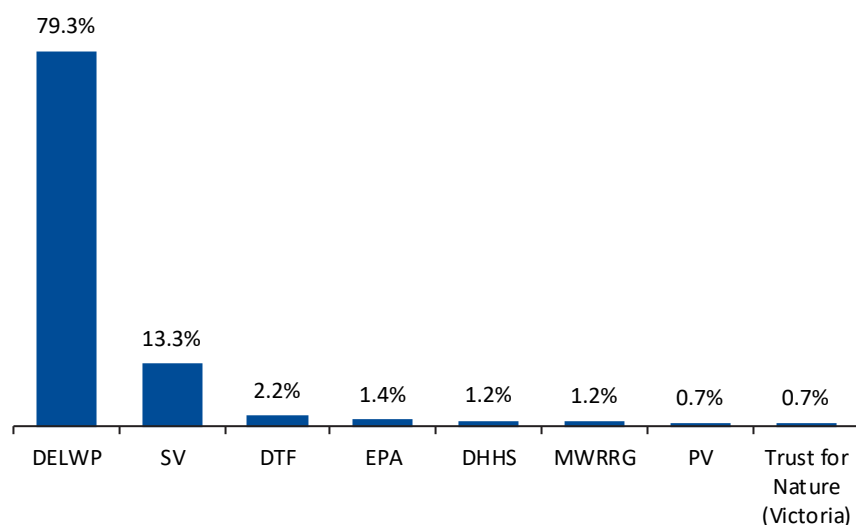
### Conflict of interest

The 2013 MAC report on Waste and Resource Recovery Governance Reform found there was a perceived conflict of interest because SV was both the administrator of the fund and one of the primary recipients. It recommended that the government transfer responsibility for fund management to DELWP.

The Act was changed and the requirement for an Independent Advisory Panel to exist was also removed from the Act. To assist it with its new role, DELWP, in May 2016, established its own fund committee.

Since taking over administration of the fund, DELWP has become the primary recipient of program funding. Consequently, this creates a mix of actual and perceived conflicts of interest for the committee to manage as it has to assess and provide advice on funding proposals that are put forward by DELWP. Figure 3J shows the breakdown of fund recipients for programs active at December 2017, which refers to those with established funding agreements.

**Figure 3J**  
**Funding recipients—percentage of total amount contracted December 2017**



*Note:* DELWP advised that a proportion of the money it receives passes through to other agencies or organisations but was unable to quantify this amount.

*Source:* VAGO based on DELWP's GEMS data.

Active program funding reflects approved program allocations that have established funding agreements and are currently drawing down on the fund.

DELWP receives \$354.13 million or 79 per cent of active program funding from the fund. The next highest recipient is SV, which receives \$59.22 million or 13 per cent.

A further issue exists with the membership of the committee. Of the five members, two are subject matter experts from DELWP—the Executive Director, Energy Policy and Programs and the Executive Director, Climate Change. This creates an inherent conflict of interest within the committee particularly when proposals considered by the committee come from one of their policy areas within DELWP.

The committee has attempted to address this with its conflict of interest policy and standing agenda item. This gives members the opportunity to raise any conflicts of interest and the committee the opportunity to agree on how it will manage these. The committee’s meeting minutes clearly note potential conflicts of interest.

DELWP advised that there are instances where a conflicted committee member will step outside the room while it is discussing a bid. However, in the three meetings we observed involving assessment of the 2018–19 funding proposals and from our review of committee minutes since May 2016, we did not observe this occurring. As a result, these members were involved in the deliberations of their own funding proposals.

DELWP considers these subject matter experts make valuable contributions to discussions and deliberations of the committee. This could be achieved by getting independent and DELWP subject matter experts to share their knowledge and expertise as attendees instead of being members of the committee. This would resolve the inherent conflicts of interest created by the current arrangements.

The vacancy of one committee position from July 2017 to March 2018 further complicated this, requiring all four members to be present for a quorum. The DELWP Secretary has recently appointed an independent governance member, resolving this issue. In addition, the minister has recently approved an update of the Guidelines as part of DELWP’s response to the audit to change the membership of the committee to make it fully independent.

## Decision-making process

The committee’s terms of reference do not include rules for decision-making. There is a risk that it may not be clear how committee decisions are finalised. DELWP should review the terms of reference to provide clear guidance on the committee decision-making processes.



# 4

## Program outcomes

Trust in government is important for the success of many policies, programs and regulations that depend on the cooperation and compliance of citizens. Transparent public reporting on government performance is an important way to build and maintain public trust. This is particularly relevant where money is collected from the public for a particular purpose as is the case with the MILL. It is important to explain to the public not just how this money is being spent, but also the extent to which it is achieving intended outcomes.

In this part of the report, we examine how the team manages the establishment of funding agreements, the delivery of funded initiatives, reporting and evaluation of outcomes. We also look at how DELWP measures and publicly reports on the outcomes of individual projects and how it uses these reports to understand how individual project outcomes contribute to the overall fund outcomes.

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### 4.1 Conclusion

The MILL has been collected from the public and set aside to address two important environmental issues. Despite the fund being established in 2005, DELWP has not been able to demonstrate the extent to which the allocation of fund money has contributed to achieving the objectives of the fund. Without demonstrable and publicly reported outcomes the public may reasonably question the rationale for paying the MILL.

While DELWP's annual reports document expenditure from the MILL Trust Account and the fund they do not demonstrate to the community how this has contributed to the achievement of the fund's legislative purposes, explain the fund's governance arrangements, or the extent to which funded programs have met their expected outcomes.

Without established performance measures for the fund it is not possible to evaluate its success. DELWP cannot fully capitalise on its success or failures because it does not measure overall fund outcomes or utilise lessons learned from individual funded initiatives. Further, individual funded initiatives do not always achieve their intended outcomes or realise their expected benefits.

The team and the committee have focused on establishing the governance framework and administrative processes for the fund. However, the lack of clarity about what role they have in setting up and overseeing projects once approved has led to potential duplication in effort.

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## 4.2 Project delivery

Funded initiatives may consist of more than one program and some have many projects under each program. The team establishes separate funding agreements between DELWP and the funding recipient for each project.

A range of agencies are responsible for delivery of programs funded from the fund. DELWP is responsible for those that involve policy development or have statewide application. Other delivery partners include DTF, the Department of Health and Human Services (DHHS), PV, EPA and Trust for Nature.

### Project plan development

Following approval by the minister and Premier, the relevant department policy area or agency develops a project plan. The team uses the project plan to develop the funding agreement. The recipient does not receive any money until the team establishes a funding agreement.

### Funding agreements

Funding agreements for other departments or for initiatives managed by other agencies are set out in an MoU. DELWP-managed projects use an Internal Funding Memorandum.

The team uses the project plan to populate the funding agreement milestones and deliverables. The Funding Agreement Team operating procedures state that the team should use the project plan to populate the Agreement Schedules template ensuring that the project aligns to at least one of the fund objectives and that the deliverables are clear. It checks to ensure that:

- ‘the payment schedule reflects the amount of budget approved through ERSC
- the proposed milestones and payments can be processed through DELWP’s GEMS and finance system as required
- the milestones and payments are connected and realistic.’

It is important that there is clarity about each party’s role so that the team can construct the funding agreements to ensure that risks are appropriately apportioned to those best placed to manage them.

We examined a selection of funding agreements and assessed whether:

- they established appropriate requirements with agencies
- the team effectively monitored agency compliance with the funding agreement or MoU.

We found all funding agreements we assessed are appropriate and include key elements such as:

- funding objectives
- milestones and a requirement for payment to be made in accordance with agreed performance milestones
- a requirement to submit a funding variation if milestones are not achieved in the financial year
- a requirement for performance measures
- reporting requirements, including quarterly progress reporting and a Final Evaluation Report
- acquittal processes, including certification of financial expenditure.

### Role of the team

The team's role in the oversight of approved projects should be clarified to prevent potential duplication of effort and address any questions about the effectiveness and efficiency of the allocation of the team's resources. Funding recipients advised that the team can overstep its role when it comes to its involvement and influence in the development of the project plan.

There is also a question as to the amount of oversight needed from the team for initiatives once they have commenced. For example, SV is an independent statutory authority established by legislation, with an independent board appointed by the minister who is accountable to Parliament. Accordingly, SV has existing statutory obligations to deliver on behalf of the Victorian Government and the minister, therefore additional oversight by the team may be inefficient.

### Monitoring

Funding agreements specify the monitoring, reporting and acquittal requirements for each initiative over the approved funding period. Funding agreements are stored in GEMS, which assists with performance monitoring and reporting. The team uses funding agreements to:

- demonstrate the alignment of funded projects with the legislation and priorities
- facilitate and reconcile payments
- monitor and evaluate the extent to which projects meet the legislated objectives.

The team monitors and ensures recipients, with some exceptions, comply with requirements included in funding agreements. Recipients do not always provide their quarterly reports, however, where this occurs we saw evidence that the team follows this up.

## Performance measures

We reviewed 33 funding agreements established between 2015 and 2017 and found that six did not include performance measures. SV established all of these agreements before DELWP took over administration of the fund. SV advised that performance measures for these projects are included in their project plans.

## Milestones and requests for payment

### Requesting milestone payments

Recipients can request payments when a specified milestone is completed or when lodging a quarterly progress report. Recipients must provide evidence of completion of the payment milestone and a completed request for payment (RFP).

The team runs a monthly due payments report using GEMS to identify projects that have missed RFP due dates. It follows up with project managers to encourage them to submit their RFPs.

Our analysis of a selection of 49 funding agreements found that the average number of milestones was 15, with the highest number of milestones for a single project being 71 and the lowest being three. There is no relationship between the number of milestones and the project cost or length. The rationale for some projects having significantly more milestones than others is not clear. DELWP advised that the recipient's level of activity determines the number of milestones. The administrative issue raised by funding recipients illustrates the need for the team to avoid the creation of unnecessary milestones during the development of project plans.

The team establishes funding agreements prior to the first payment. However, 14 recipients stated that this is an issue because it often takes them significant resources to develop the project plan, which is a prerequisite to the establishment of a funding agreement.

We reviewed the time frames for establishing funding agreements for 16 projects from 2015 to 2018. DELWP took 213 days on average to develop a funding agreement from the point of approval. One project took a year to establish a funding agreement after the minister and Premier approved its funding. DELWP should examine mechanisms to encourage the earlier development of project plans for approved programs or review the requirements for, and format of, funding agreements.

DELWP aims to have projects plans in place by 1 July 2018 for initiatives approved in the 2018–19 Budget and has engaged a consultant to assist with this.

## Financial acquittal

The team relies on the approval of the funding recipient's financial officer as evidence of financial acquittal. The team received a financial acquittal for all 17 projects that we tested. All included an expenditure report designed to include information detailing how funding was accounted for, what recipients spent funds on and what financial year they spent the funds in. The expenditure reports vary in the level of detail provided and may not always enable the team to confirm that recipients use the funds for their intended purpose.

### 4.3 Project reporting

#### Recipient reporting

Recipients do not always comply with their reporting obligations.

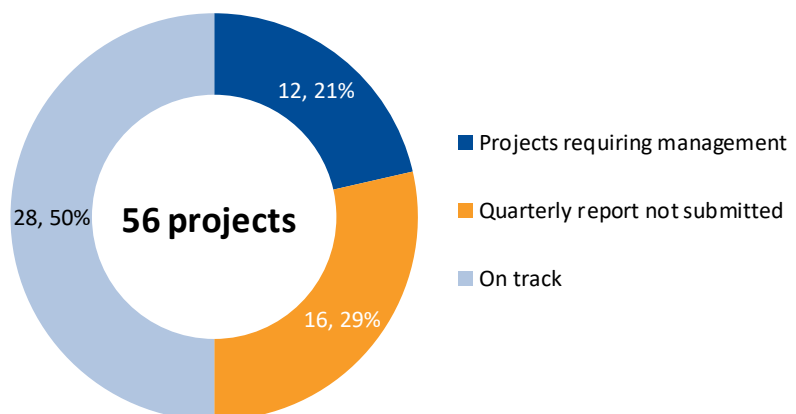
Recipients are required to submit a quarterly progress report to the team 10 working days after the end of each financial quarter.

These reports provide sufficient information to the team to allow them to raise any project issues to the committee. However, the committee does not have a clear process to manage these issues. This is discussed further in Section 4.4.

According to the November 2017 quarterly report to the committee, 16 of the 56 project managers (29 per cent) had not submitted their most recent quarterly progress report. The team could not accurately assess and report on the status of these projects. DELWP manages 11 of the 16 projects (69 per cent) that did not submit their report. Figure 4A shows the reporting rates of funding recipients for the September 2017 quarterly progress reports.

DELWP advised that for both the December and March quarters there were a total of three projects where quarterly reports were not provided by the deadline.

**Figure 4A**  
**Quarter ending September 2017 progress reporting from funding recipients**



Source: VAGO.

As part of their quarterly progress reporting, recipients self-report their project status based on whether or not they are meeting milestones. The team reviews this information and provides its own assessment of the project status. The committee receives the recipients' and the team's assessments side-by-side so that it can see any difference in assessment, as part of the fund quarterly report. We compared these in the November 2017 report and found the ratings varied for only one project.

The fund quarterly report provides the committee with the opportunity to review key aspects of project and financial management. This report includes:

- progress of the development of funding agreements
- details of issues that may be delaying payment and appear as an underspend in the fund budget
- a traffic light report showing progress of active projects
- an exception report providing more detail on projects that may need attention or support
- details of any project closures
- a snapshot of the current financial position based on the known information
- a summary of the range of public enquiries that the team receives.

## DELWP reporting

DELWP has its own internal reporting requirements. Program managers must report progress monthly by providing status updates in Sytle, DELWP's performance management system. This informs the monthly Senior Executive Team (SET) performance dashboard and SET performance reporting.

The performance reporting includes a traffic light report for each program, however, this rating is for each program overall rather than each individual project. For example, 21 individual projects make up the overall program Protecting Victoria's Environment—Biodiversity 2037. DELWP has clear criteria for how to determine the overall status of a program.

## Alignment of reporting

DELWP ensures consistency between its internal management report and the committee's quarterly reporting. Its internal management reports now contain reports of the status of funded programs being delivered by DELWP, its portfolio agencies and DHHS as in the committee's February 2018 quarterly report. However, this report does not include reporting on the progress of projects delivered by DTF.

The traffic light rating used for DELWP executive reporting differs in that it details the status of overall programs whereas the team's traffic light report provided to the committee reports on the status of the overall program and at an individual project level.

The detail and content of quarterly progress reports are adequate and DELWP and SV advised us that they were easy to use and did not provide a significant administrative burden.

#### 4.4 Escalation of project risks

There is no clear process to manage underperformance or risks of all projects that receive fund money. Despite this, there is evidence that the team withholds payments where recipients are not meeting their milestones. The team may recommend program termination to the minister, under the terms of the funding agreement, where:

- there has been a substantial breach of the funding agreement
- the team has issued a notice giving 14 days to rectify a breach and the program manager has failed to do so
- progress is suspended for a period of more than six months without written consent of the team
- there is any other reason that the team thinks is appropriate.

There is no evidence this has ever occurred despite the team raising project issues with the committee as part of its quarterly reports.

DELWP advise that senior management is currently reviewing roles and responsibilities for escalation of projects not achieving milestones or objectives.

#### Exception reporting

The team produces an exception report before every quarterly meeting that reviews and flags projects that may need attention or support and raises any issues for escalation to the committee.

Examples of issues identified for consideration by the committee include:

- grant programs that are undersubscribed
- lack of evaluation of failed programs or the use of this to inform new programs
- broader issues of how DELWP and SV work together to develop concept and project planning
- funding or prioritisation of funding to projects that are the same as previously failed projects without clear evidence of application of lessons learned or of mitigation actions for new programs
- lack of clear mitigation actions or strategies to deal with significant time line extensions, under delivery and missing documentation.

The exception reports we reviewed also include suggested committee actions such as:

- seeking clarification of project status and delivery issues from SV
- considering how to best encourage quality and transparent reporting.

The actions identified in these exception reports need to be clearer to ensure that project performance issues are being addressed. DELWP should document a clear process to manage underperformance or program risks of all recipients of fund distributions.

The team identifies and escalates project issues but the committee's role and powers to address these are unclear. There are potential issues with conflicts of interest as DELWP committee members who manage DELWP-funded programs also advise on program termination and are responsible for performance issues.

Committee meeting minutes from 20 March 2017 do not clearly record the Committee's discussion of the performance issues raised in the quarterly report or show that the committee endorsed suggested actions to address the issues identified.

DELWP advised that it manages program issues through its internal reporting process but this does not include reporting on funded programs that DTF delivers. We expect the escalation process for management of funded project risks to incorporate all relevant programs while making use of existing processes to minimise duplication.

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## 4.5 Program management

In response to concerns across DELWP about under-expenditure and fund governance processes, DELWP's Finance and Performance Sub-Committee (FPSC) requested that it receive a 'deep dive' report into the fund.

FPSC requested that DELWP's Finance and Planning Division report on the following issues:

- Are the governance mechanisms and processes, such as project plans and funding agreements, appropriate?
- Do the relevant areas of DELWP and other agencies have the capabilities required to deliver under these mechanisms and processes?

DELWP's Finance and Planning Division presented the report to the FPSC in October 2017. It found:

- issues with the quality of project plans and the time it takes to establish funding agreements
- various delays and issues in projects, leading to significant issues with budget phasing, milestones not aligning with actual expenditure and projects failing to deliver expected outcomes
- gaps in staff capability
- lack of an evaluation process for the fund.

Review of committee quarterly reports shows that various projects are experiencing delays, with only 50 per cent of projects reported as being on track in the November 2017 report. The team's November 2017 exception report notes that delays in implementation have resulted in an increase in requests for contract variations. Most delays linked to deliverables resulting in re-phasing of payments to future years.



The 'deep dive' report concludes that the root cause of the issue was project design and delivery issues within DELWP more broadly.

It proposed 11 recommendations to address issues affecting the timely delivery of projects within budget, including to:

- undertake an immediate assessment of gaps in project management skills
- facilitate engagement with the team at the start of project planning to maximise alignment of the project plan and funding agreement
- finalise the evaluation framework as a matter of urgency.

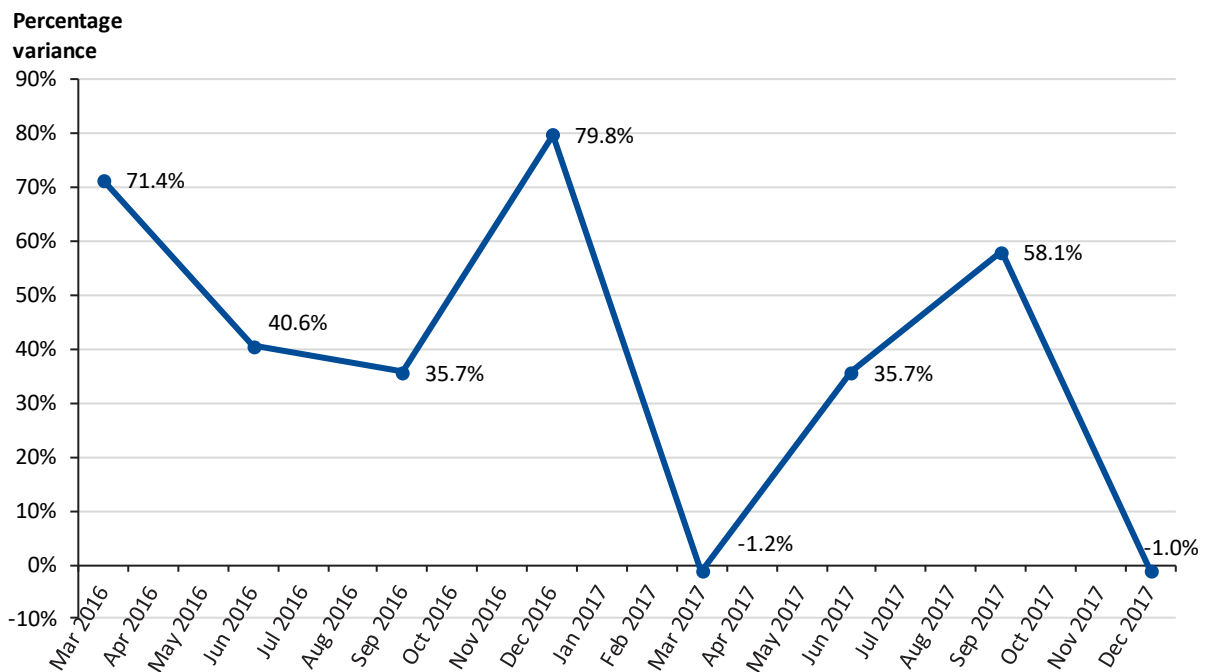
As a result of DELWP's subsequent skills gap analysis, it developed a Project Management Strategic Framework and rolled out project management training modules across the department. The team, where possible, engages early with policy and recipient areas in the development of business cases and project plans respectively.

The committee approved the evaluation framework in its December 2017 meeting.

## Underspend

Figure 4B shows the quarterly program underspend against the combined budget of the approved programs.

**Figure 4B**  
**Quarterly program underspend**



Source: VAGO based on DELWP's quarterly compliance reports.

The highest quarterly underspend was in December 2016, at 79.8 per cent. DELWP advised that underspend occurs as a result of factors such as:

- using preliminary financials from programs as they are announced in the Budget to track performance instead of updated figures from the final budget in the project plan
- delays in establishment of funding agreements due to the time it takes agencies to develop project plans
- increased government targets and commitments to spend the money but its capacity to ramp up delivery is limited.

DELWP advised that it reviews alignment of funding agreements and approved budgets on a regular basis. DELWP significantly reworked budgeted cash flows as part of the mid-cycle budget in December 2017 to align them to contracted milestones and reflect contract variations. As at 31 December 2017, year to date program expense was \$52.6 million, in line with forecast expenditure of \$52.1 million. However, GEMS indicated that \$60.2 million was expected to be paid in milestone payments for this period. This underspend is due to delays from program delivery areas seeking milestone payments. The improvement in underspend therefore does not necessarily reflect an improvement in the timeliness of program delivery.

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## 4.6 Evaluation

The funding agreement requires each recipient to submit a Final Evaluation Report to the team within six weeks of project completion. The report must include as a minimum:

- a detailed breakdown of expenditure certified by the recipient's chief financial officer (or delegated equivalent)
- a description of the quantifiable outcomes of the project and an assessment of the effectiveness of the project in meeting its objectives
- an assessment of the project's achievement of key performance indicators
- an assessment of why targets were not met or exceeded
- a summary of any consultation or communication that the recipient has undertaken with the community and any stakeholders during the duration of this MoU and an assessment of the effectiveness of these activities and the community's and stakeholders' responses to the project
- an assessment of the performance of the project in terms of time, cost and quality (planned versus actual)
- a discussion of the recipient's key lessons learned from the project in terms of planning and implementation
- a discussion of what would/could be done differently to achieve a better outcome if the process were to begin again.

We reviewed all 18 projects that have closed in the past two years and found that all of them completed a project evaluation. The team completes a Closure Report that assesses the evaluation, where available, to determine whether closed projects have met their objectives. Of the 18 projects we reviewed, only seven (39 per cent) clearly met their objectives. Of the remaining projects, four did not meet objectives, four partly met objectives and three were not clearly assessed against objectives as part of their evaluation. Only two of these projects commenced during DELWP's administration of the fund. One of these was terminated early and the other was designed to achieve long-term behaviour change and its outcomes have not yet been able to be assessed. DELWP has worked to enhance the clarity of project outcomes in funding agreements with the aim of improving project evaluations on completion.

### Evaluation framework

At its December 2017 meeting, the committee endorsed an evaluation framework for the fund. The committee noted that, currently, the fund receives project evaluations and the content and quality of them vary greatly depending on the experience of the program manager. The framework aims to improve this by requiring clear articulation of project objectives and the demonstration of how they link to the legislated objectives of the fund. This is required at the outset of the project to ensure recipients report this in Final Evaluation Reports.

A key new addition to the evaluation framework is the introduction of a Priority Statement benefits table that will support budget submission authors and program managers to understand and articulate the line of sight between their project's benefits/objectives and the legislated objectives and priorities of the fund.

The Priority Statement notes that Victorian Government policies and other relevant strategies, all of which include their own objectives, will guide investment. However, DELWP does not use these to evaluate the success of the use of fund monies. DELWP advised that policy guides program development and recipients identify the measures that will be used to show alignment and performance.

DELWP advised the evaluation framework is in the process of being implemented and will be detailed in the 2017–18 Activity Report due to be released alongside the DELWP annual report. The committee advised that the evaluation framework will support a whole-of-fund evaluation, which it intends to complete every four years. However, DELWP has not applied the framework to any programs and it is not clear how this will work in practice.

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## 4.7 Lessons learned

Recipients are required to include a section on lessons learned in the Final Evaluation Report.

DELWP does not have a formal process to consistently apply lessons learned from previous projects during the development or selection of new projects funded from the fund. Lessons learned are not stored in a central location to enable them to be considered easily by the committee when new but similar programs come up for assessment. This process relies on the team to raise these issues in its summary assessment of proposals or on the organisational knowledge of the committee members.

There is no debrief held between the team and recipients at project close. Funding recipients provided feedback to us that the team does not share lessons learned from projects to inform the development of future initiatives seeking funding. Recipients advised that feedback about past programs is dependent solely on organisational knowledge. This represents a lost opportunity as there is a risk that corporate knowledge will be lost.

DELWP advised that the committee and the team have identified this as an issue and it intends to address it across the department.

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## 4.8 Public reporting

### Annual report

The MAC report recommended that there be greater transparency of the collection and distribution of the MILL and the fund. Previously, SV and EPA reported information about expenditure and balances separately in their annual reports. MAC recommended consolidating this information in DELWP's annual report. DELWP now publishes this information in appendices 7 and 8 of its annual report.

DELWP's annual report includes the fund movements and a brief description as an appendix to the financial statements. DELWP provides a brief summary of the purpose of each fund and fund movements. Details of payments made during the year to funding recipients by program are also included. This information is insufficient to inform the public about the governance, activities of the fund, programs funded and how program outcomes deliver against the legislative purposes.

### Budget Papers

The 2016–17 Budget Papers were the first to clearly identify the fund as the source of funding of budget initiatives. This shows an improvement in the transparency of reporting programs that receive funding from the fund.

## Website and media releases

DELWP's website includes background information on the fund, details of budget commitments funded from the fund and links to the Priority Statement and Guidelines. The website lacks detail about the composition of the committee, the role of the committee and outcomes of funded activities. Media releases inconsistently refer to the fund as the source of funding. The government did not announce that the Stepping In To Support Industry And Councils With Recycling program was funded by the fund in a media release in February 2018.

## Activity report

SV produced an annual sustainability fund activity report. This report provided details of the fund's governance arrangements, financial performance and funding provided during the period. It included case studies of programs funded by the fund and the program outcomes. This activity report was not a statutory requirement, but SV published it to improve the transparency of fund management.

Since the administration of the fund moved to DELWP, there has been limited public reporting about the activities of the fund. There has been no reporting of the fund's governance arrangements or information about the nature and outcomes of funded programs.

DELWP published an activity report for 2015–17 in May 2018, *Investing in a more sustainable future*. DELWP intends to provide such an activity report annually in the future. The report details the fund governance arrangements, including the role and membership of the committee.

The report provides a good description of the MILL and the MILL Trust Account and the flow of money to the fund. It details the legislative purpose of the fund and Priority Statement. Analysis of funding recipients is included with a list of programs that received funding. Detailed project case studies outline the purpose of projects funded and the outcomes delivered.

There are clear similarities between DELWP's activity report and SV's annual activity reports. It is unclear why it has taken DELWP nearly two years to produce it. The delay in its publication affects its relevance and usefulness as a tool to improve the transparency of the fund and its management.



# Appendix A

## *Audit Act 1994* section 16— submissions and comments

We have consulted with DELWP, EPA, SV, MWRRG and GWRRG, and we considered their views when reaching our audit conclusions. As required by section 16(3) of the *Audit Act 1994*, we gave a draft copy of this report, or relevant extracts, to those agencies and asked for their submissions and comments. We also provided a copy of the report to DPC.

Responsibility for the accuracy, fairness and balance of those comments rests solely with the agency head.

Responses were received as follows:

DELWP .....	78
SV .....	82
MWRRG .....	83
GWRRG .....	84

**RESPONSE provided by the Acting Secretary, DELWP**



**Department of Environment,  
Land, Water and Planning**

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Mr Andrew Greaves  
Auditor-General  
Victorian Auditor-General's Office  
Level 31 / 35 Collins Street  
MELBOURNE VIC 3000

Ref: SEC013659



Dear Mr Greaves

**PROPOSED PERFORMANCE AUDIT REPORT, MANAGING THE MUNICIPAL AND INDUSTRIAL  
LANDFILL LEVY**

Thank you for your letter dated 2 July 2018 providing the Department of Environment, Land, Water and Planning (DELWP) with the proposed performance audit report *Managing the Municipal and Industrial Landfill Levy* (MILL).


It is critical that Victorians have confidence in government to administer the MILL and Sustainability Fund with transparency, rigorous financial management and a focus on outcomes.

I note that DELWP has responsibility for achieving all fourteen recommendations. Please find attached the action DELWP proposes to acquit these. I welcome your staff following up periodically with DELWP to monitor our progress in implementing these.

Please contact Stephen Creaney, Chief Operating Officer, Energy, Environment and Climate Change on (03) 9637 8818 or [stephen.creaney@delwp.vic.gov.au](mailto:stephen.creaney@delwp.vic.gov.au).

Finally, I would like to extend my thanks to your office, in particular, Jenny Koong and Zoe Parer-Cook, for the support and flexibility they have provided DELWP throughout the audit process.

Yours sincerely



**Terry Garwood**  
Acting Secretary

13/7/2018

Encl.

Any personal information about you or a third party in your correspondence will be protected under the provisions of the *Privacy and Data Protection Act 2014*. It will only be used or disclosed to appropriate Ministerial, Statutory Authority, or departmental staff in regard to the purpose for which it was provided, unless required or authorized by law. Enquiries about access to information about you held by the Department should be directed to [foi.unit@delwp.vic.gov.au](mailto:foi.unit@delwp.vic.gov.au) or FOI Unit, Department of Environment, Land, Water and Planning, PO Box 500, East Melbourne, Victoria 8002.





## Managing the Municipal and Industrial Landfill Levy

### DELWP's Management Action Plan

Recommendations	Agreed Action	Completion Date
<b>Recommendation 1</b> Assess alignment with the legislative purpose and establish a financial acquittal process for distributions made under section 70E(3)(d) (See Section 2.3)	<b>DELWP accepts this recommendation</b> DELWP will extend the financial acquittal process in place for crown land managers to all funding recipients of distributions made under section 70E(3)(d).	September 2018
<b>Recommendation 2</b> Establish an independent committee to manage inherent conflicts of interest while maintaining access to subject-matter expertise (See Section 3.6)	<b>DELWP accepts this recommendation</b> DELWP supports the replacement of the two DELWP Committee members with independent members and to make available relevant senior executives for advice on funding proposals.	September 2018
<b>Recommendation 3</b> Review the role of the Sustainability Fund Committee and Sustainability Fund Team <ul style="list-style-type: none"> <li>revise and update the committee's terms of reference (role and responsibilities, memberships, managing conflicts of interest, +/- KPIs, rules for decision-making)</li> <li>clarify the role of the team and the committee in the oversight of project delivery (See Sections 3.6 and 4.2)</li> </ul>	<b>DELWP accepts this recommendation</b> DELWP will review the Terms of Reference for the Committee and clearly document the role of the team and the funding recipient in relation to project delivery.	September 2018
<b>Recommendation 4</b> Develop clear guidance regarding the treatment of the following: <ul style="list-style-type: none"> <li>applications seeking core administrative costs</li> <li>eligibility of applications seeking on-going funding (See Section 3.3)</li> </ul>	<b>DELWP accepts this recommendation</b> DELWP will develop guidance on the treatment of core administrative costs and ongoing funding.	September 2018
<b>Recommendation 5</b> Establish processes to ensure all proposals seeking funding from the Sustainability Fund are assessed by the Sustainability Fund Committee before approval by the minister and Premier (See Section 3.4)	<b>DELWP accepts this recommendation</b> DELWP implemented a process for the 2018-19 Budget to ensure proposals were considered by the Committee before the Minister and Premier. This process has also been embedded in broader government decision-making processes and steps are being taken to strengthen this process for 2019-20.	September 2018
<b>Recommendation 6</b> Review the evaluation criteria applied to assessing proposals to clearly reflect the requirements specified in the legislation, Priority Statement and Guidelines (See Section 3.2)	<b>DELWP accepts this recommendation</b> DELWP considers that all requirements are being consistently assessed. To avoid any doubt, the assessment process (template) has been updated to demonstrate clear alignment to the criteria set out in legislation, the Priority Statement and Guidelines.	Implemented



Environment,  
Land, Water  
and Planning

## Managing the Municipal and Industrial Landfill Levy

<b>Recommendation 7</b> Improve the quality of advice provided to the minister by providing the assessment against each evaluation criteria (See Section 3.6)	<b>DELWP accepts this recommendation</b> DELWP considers that all requirements are being provided to the Minister. To avoid any doubt, the advice format (template) has been updated to demonstrate clear alignment to the criteria set out in legislation, the Priority Statement and Guidelines.	Implemented
<b>Recommendation 8</b> Relate the number of funding agreement milestones to the value and/or complexity of funded programs and link payment milestones to reporting requirements to minimise administrative burden (See Section 4.2)	<b>DELWP accepts this recommendation</b> In developing funding agreements, DELWP has and will continue to meet with funding recipients to clarify milestones that are proportionate to the value and/or complexity of funded programs/projects.	Implemented
<b>Recommendation 9</b> Examine mechanisms to encourage the earlier development of project plans for approved programs (See Section 4.2)	<b>DELWP accepts this recommendation</b> The project plan development process has been reviewed with all DELWP plans for the 2018-19 budget process now in place. Project plans for any new programs will be established within 60 days of approval.	Implemented
<b>Recommendation 10</b> Require funding recipients to provide key categories of expenditure in support of the financial acquittal of funding agreements to enable the team to review whether the funds have been used for the purpose intended (See Section 4.2)	<b>DELWP accepts this recommendation</b> All new funding agreements are to contain specific requirements to ensure appropriate financial acquittal processes are in place, and where appropriate include categories of expenditure.	Implemented
<b>Recommendation 11</b> Implement the evaluation framework to evaluate outcomes of funded programs to clearly demonstrate the extent to which programs have contributed to the specified legislative objective (See Section 4.6)	<b>DELWP accepts this recommendation</b> DELWP will document the process for capturing program outcomes that contribute to legislative objectives in the Activity Report.  The Activity Report details the Fund's investments and is designed to provide information on the scope of work taking place to support waste reduction, climate adaptation and mitigation, as well as the role the Fund plays in contributing to employment, new technology, innovation and resource efficiency. The evaluation framework, currently under development will inform the content of the Activity Report.	September 2018
<b>Recommendation 12</b> Identify overall Sustainability Fund outcomes to measure the extent to which expenditure has successfully delivered legislative objectives (See Section 4.6)	<b>DELWP accepts this recommendation</b> See Recommendation 11.	September 2018
<b>Recommendation 13</b> Develop a formal process to consistently apply lessons learned including: <ul style="list-style-type: none"> <li>capturing and storing them centrally to enable them to be considered by the committee when assessing proposals</li> <li>sharing them with agencies to enable them to be considered when developing new program</li> </ul>	<b>DELWP accepts this recommendation</b> DELWP will create a central database to capture lessons learned.	December 2018

## Managing the Municipal and Industrial Landfill Levy

proposals (See Section 4.7)

**Recommendation 14**

Publish an annual public report for 2018–19 and future years detailing the activities of the Sustainability Fund and outcomes achieved (See Section 4.8).

**DELWP accepts this recommendation**

See Recommendation 11.

September 2018

**RESPONSE provided by the Chair, SV**



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16 July 2018

Mr Andrew Greaves  
Auditor-General  
Victorian Auditor-General's Office  
Level 31 / 35 Collins Street  
Melbourne Victoria 3000

Dear Mr Greaves

**Performance Audit Report Managing the Municipal and Industrial Landfill Levy**

I am writing in response to your audit report *Managing the Municipal and Industrial Landfill Levy*.

Sustainability Victoria welcomes this review of the management of the Municipal and Industrial Landfill Levy and the Sustainability Fund. Good financial management and transparency is particularly important for trust account expenditure.

We particularly welcome the continual improvement of role clarity of the Sustainability Fund team and Committee to minimise the duplication of existing governance arrangements.

Sustainability Victoria recently commissioned an independent assessment of our programs to objectively quantify the value we provide to the Victorian community. The assessment and its findings are being used to improve our approach to project design effectiveness and the monitoring and evaluation of our ongoing work.

Sustainability Victoria welcomes the recommendations and looks forward to collaborating with the Department of Environment, Land Water and Planning (DELWP) to support implementation of the recommendations, as appropriate.

Yours sincerely

Heather Campbell  
Chair





**RESPONSE provided by the Chair, MWRRG**



Level 4, Tower 4, World Trade Centre  
18-38 Siddley St, MELBOURNE, VIC 3005  
Phone (03) 8698 9800

18 July 2018

Mr Andrew Greaves  
Auditor-General  
Victorian Auditor-General's Office  
Level 24, 35 Collins Street  
Melbourne VIC 3000

Dear Mr Greaves

**PROPOSED PERFORMANCE AUDIT REPORT MANAGING THE MUNICIPAL AND INDUSTRIAL LANDFILL LEVY**

Thank you for your letter dated 2 July 2018 providing the Metropolitan Waste and Resource Recovery Group (MWRRG) with the opportunity to comment, under section 16(3) of the Audit Act 1994, on the audit report on *Managing The Municipal And Industrial Landfill Levy*.

MWRRG has reviewed the report and supports the recommendations made. We find the audit report consistent with past experiences as a recipient of the Sustainability Fund.

We note that MWRRG is not subject to any of the recommendations in the report, however supports;

- A transparent and improved decision making framework for the assessment of initiatives seeking funding from the Sustainability Fund
- Greater accountability in determining value for money and evidence based monitoring and evaluation of the initiative against the agreed objective of the funding
- Compiling and sharing reflective evaluations on the success, challenges and opportunities fund recipients have observed/encountered in undertaking the work through documented corporate knowledge
  - Share case studies
- Improved reporting process to avoid undue administrative burden
- A streamlined process for project planning to reduce the effort of the reporting regime

Please do not hesitate to contact Robert Millard, CEO, should you wish to discuss this further

Yours sincerely,

A handwritten signature in black ink, appearing to read 'Colleen Gates'.

**Colleen Gates**  
Chair  
Metropolitan Waste and Resource Recovery Group

**RESPONSE provided by the Chair, GWRRG**

Gippsland  
Waste and Resource Recovery Group



Ref No:174:RE

18 July 2018

Mr Andrew Greaves  
Victorian Auditor-General  
Level 31/35 Collins Street  
MELBOURNE VIC 3000

Dear Mr Greaves

**PERFORMANCE AUDIT REPORT – MANAGING THE MUNICIPAL AND INDUSTRIAL LANDFILL LEVY**

Thank you for the opportunity to respond to the VAGO Performance Audit Report 'Managing the Municipal and Industrial Landfill Levy (MILL)'. The Gippsland Waste and Resource Recovery Group (WRRG) finds the audit report consistent with our own past experience as a Sustainability Fund recipient, and is supportive of the recommendations contained within the document.

We note that Gippsland WRRG is not subject to any of the recommendations in the report, however supports;

- A transparent and improved decision-making framework for the assessment of initiatives seeking funding from the Sustainability Fund.
- Greater accountability in determining value for money and evidence based monitoring and evaluation of the initiative against the agreed objectives of the funding.
- Compiling and sharing reflective evaluations on the success, challenges and opportunities fund recipients have observed/encountered in undertaking the work through documented corporate knowledge.
- Improved regular reporting process based on a balance between the 'doing' and the 'reporting' to avoid undue administrative burden.
- A streamlined process for project planning (to reduce the effort of the aforementioned reporting regime).

The GWRRG concurs with the audit teams' observation of the opportunity cost in not effectively responding to the needs of the waste and resource recovery sector as exemplified by the recent recycling crisis.

Any personal information about you or a third party in your correspondence will be protected under the provisions of the Privacy and Data Protection Act 2014. It will only be used or disclosed to appropriate Ministerial, Statutory Authority, or departmental staff in regard to the purpose for which it was provided, unless required or authorised by law. Enquiries about access to information about you held by the Group should be directed to the Privacy Coordinator, Gippsland Waste and Resource Recovery Group, PO Box 444, Trafalgar, Victoria 3824.

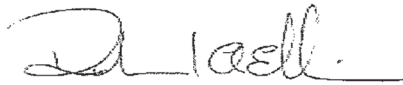
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ABN 68 272 158 677

***RESPONSE provided by the Chair, GWRRG—continued***

Should you have any queries, please do not hesitate to contact our Executive Officer, Matthew Peake on 5633 2744.

Yours sincerely

A handwritten signature in black ink, appearing to read 'R. A. Ellis', with a long horizontal stroke extending to the right.

RICHARD A ELLIS  
**Chair**

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# Auditor-General's reports tabled during 2018–19

Report title	Date tabled
Local Government Insurance Risks (2018–19:1)	July 2018

All reports are available for download in PDF and HTML format on our website  
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