



Auditor-General for the Northern Territory
Auditing for Parliament

October 2012

Report to the Legislative Assembly



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Northern Territory Auditor-General's Office

Auditing for Parliament

The Honourable Speaker of the Legislative
Assembly of the Northern Territory
Parliament House
Darwin NT 0800

31 October 2012

Dear Madam Speaker,

Accompanying this letter is my report to the Legislative Assembly on matters arising from audits conducted during the six months ended 30 June 2012 and I request that you table the report today in the Legislative Assembly.

The larger part of the report deals with the results of performance management system audits, and of compliance audits that were performed to assess the adequacy of controls over the administration of public monies. Also included are the results of audits of financial statements for those institutions that are required to report on a calendar year basis.

I also wish to point out to Members that in this report I have referred to the public sector Agencies as they existed at 30 June 2012 notwithstanding the changed Agency arrangements that have since come into force.

Yours sincerely,

F McGuiness
Auditor-General for the Northern Territory

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Auditor-General's Overview

Audits included in this report

This report outlines the results of audits conducted during the period 1 January 2012 to 30 June 2012.

The audits that are reported here cover four broad areas; financial audits, reviews of major projects or tendering activities, compliance audits and performance management system audits. The results of the various audits and reviews are included as part of this report.

The first half of the 2012 calendar year saw the completion of audits of the financial statements of each the Territory's principal tertiary educational institutions; Charles Darwin University, Menzies School of Health Research and Batchelor Institute of Indigenous Tertiary Education. These institutions report on a calendar year basis and each submitted its financial statements for audit during the first half of 2012.

Financial statements prepared by Agencies each year are not audited as this would first require a direction from the Treasurer to Accountable Officers to submit those statements to the Auditor-General pursuant to section 11(3) of the *Financial Management Act*. Consequently, I place considerable reliance upon what are known as compliance audits to assess the extent to which Agencies' internal control systems function effectively, whether Agencies are complying with prescribed requirements pertaining to internal control and, flowing from that, whether I am able to rely upon the financial information prepared by Agencies at the end of each financial year as part of my audit of the Treasurer's Annual Financial Statements. Compliance audits were conducted in nine Agencies during the period covered by this report and a brief overview of the results of those audits is included here. In addition a review of credit card expenditure was conducted across twelve Agencies to assess the extent to which expenditure incurred by way of corporate credit cards is properly verified and is appropriate.

Auditor-General's Overview cont...

Performance management system audits were conducted at three Agencies, the Department of Health, the Office of the Commissioner for Public Employment and at NT Police, Fire and Emergency Services. The Department of Health places considerable reliance upon non-government organizations in the delivery of health services. The audit sought to ascertain whether the use of those organizations was consistent with the Department's goals and objectives. In the case of the Office of the Commissioner for Public Employment the audit sought to ascertain the extent to which appropriate systems were in place to enable an assessment of whether an employment program was achieving its objectives, while in the case of NT Police, Fire and Emergency Services the audit was undertaken in the wake of the Braddy case to ascertain whether speed detection and breath analysis equipment is calibrated regularly and in accordance with manufacturers' specifications.

Reviews were also conducted at the Department of Construction and Infrastructure to examine the reasons for cost variations on major road construction projects, and at the Department of Lands and Planning to examine the events that occurred between the issue of a request for tenders for the provision of ferry services between Darwin and Mandorah, and the eventual execution of a funding agreement rather than the contract that might have been envisaged by the Department at the commencement of the process.

The Northern Territory Auditor-Generals Office (NTAGO) differs from other Agencies in that the financial statements prepared at the end of each financial year are required to be audited by an appropriately qualified auditor who is appointed by the Administrator. The audit for 2011/12 was completed in September 2012 and the financial statements, together with the report of the auditor were provided by the auditor to the Chief Minister for tabling in the Legislative Assembly.

The way by which my Office undertakes its statutory role differs from other jurisdictions in that a very heavy reliance is placed on staff drawn from local accounting firms and who are appointed as auditors by me pursuant to the provisions of the *Audit Act*.

Reports on the Results of Audits

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Batchelor Institute of Indigenous Tertiary Education

Audit findings and analysis of the financial statements for the year ended 31 December 2011

Background

The Batchelor Institute of Indigenous Tertiary Education (the Institute) is established under the *Batchelor Institute of Indigenous Tertiary Education Act*. Section 46 of the Act requires the Institute to prepare financial statements within 3 months of the end of the Institute's financial year (31 December) and to submit those to the Auditor-General.

Audit Opinion

The audit of the financial statements of the Institute for the year ended 31 December 2011 resulted in an unqualified independent audit opinion. That opinion was issued on 24 May 2012.

Key Findings

Financial analysis

The financial performance and financial position of the Institute are illustrated in the following tables.

Batchelor Institute of Indigenous Tertiary Education cont...

Financial Performance for the year		
	2011	2010
	\$'000	\$'000
Revenue from continuing operations	47,083	44,624
Less expenses from ordinary activities		
Employee Expenses	(24,393)	(22,601)
Depreciation	(1,475)	(1,394)
Other	(15,448)	(23,507)
Total expenses from continuous operations	(41,316)	(47,502)
Operating result before income tax expense	5,767	(2,878)
Less Income tax expense	-	-
Operating result after income tax expense	5,767	(2,878)

The Institute reported an operating surplus for the year ended 31 December 2011 of \$5.767 million, in comparison to a restated loss of \$2.878 million in the prior year. Of this surplus, \$2.771 million related to the core activities of the Institute (2010: surplus of \$0.089 million), the "Away From Base" activity recorded a breakeven result (2010: breakeven), and Project activities recorded a surplus of \$2.996 million (2010: loss of \$2.967 million).

The Institute has reported an overall increase in revenue received during the year, mainly due to an increase in grants from the Australian Government (\$0.436 million), and the Northern Territory Government (\$2.012 million).

The Institute also reported a decline in expenses of \$6.186 million for 2011 when compared with the prior year. That decline reflects the recognition, in 2010, of an expense and an accompanying liability for the value of unspent funds, which were required to be returned to the funding bodies under the terms of the funding arrangements.

Batchelor Institute of Indigenous Tertiary Education cont...

Financial Position at year end

	2011	2010
	\$'000	\$'000
Current Assets	19,541	18,484
Less Current Liabilities	(7,193)	(11,487)
Working Capital	12,348	6,997
Add Non Current Assets	31,301	30,800
	43,649	37,797
Less Non Current Liabilities	(692)	(685)
Net Assets	42,957	37,112
Represented by:		
Reserves	27,550	27,472
Accumulated Funds	15,407	9,640
Equity	42,957	37,112

Some of the funding received for 2010, but not spent in that year was required to be repaid. Consequently, an amount of \$6 million was recognized as a liability at the end of the Institute's financial year, to be repaid in 2011. This is reflected in the decline in current liabilities for 2011.

Charles Darwin University

Audit findings and analysis of the financial statements for the year ended 31 December 2011

Background

The Charles Darwin University (the University) is established under the *Charles Darwin University Act*. The University controls three subsidiary entities; the Menzies School of Health Research, the Charles Darwin University Foundation, a company limited by guarantee and which acts as trustee of the Charles Darwin University Trust, and CDU Amenities Limited, which is also a company limited by guarantee.

The University provides both higher education, and vocational education and training (VET). Higher education funding is provided to the University by the Commonwealth Government through direct grants, and through the proceeds of student loans by the Commonwealth under the auspices of the HECS-HELP Scheme. VET funding is provided by the Northern Territory Government through monies appropriated by the Legislative Assembly to the Department of Education and Training. The University also attracts research funding from a variety of sources.

The University is required by its enabling Act to prepare financial statements as at 31 December each year and to submit those statements to the Auditor-General by 31 March each year.

Audit Opinion

The audit of the financial statements of Charles Darwin University for the year ended 31 December 2011 resulted in an unqualified independent audit opinion. That opinion was issued on 29 May 2012.

Key Findings

Financial Performance and Financial Position of the University

The financial performance of the University, as measured by its operating result, was \$12.0 million (\$15.2 million for 2010). The higher education component of the University achieved a surplus of \$19.6 million for the year, which was offset by a \$7.6 million deficit on the part of the VET component.

Charles Darwin University cont...

Financial Performance for the year – excluding controlled entities

	2011	2010
	\$'000	\$'000
Revenue from ordinary activities		
Financial assistance from the Commonwealth	80,531	83,452
Financial assistance from the Northern Territory Government	58,407	66,846
Other revenue (HECS, fees, interest, etc)	83,322	73,318
Total revenue from ordinary activities	222,260	223,616
Less expenses from ordinary activities		
Employee related costs	(118,417)	(117,399)
Administration, operational and other expenses	(91,814)	(91,012)
Total expenses from ordinary activities	(210,231)	(208,411)
Operating result for the year	12,029	15,205

The decrease in revenue for the year was a result of:

- a decrease in Australian Government grants and Northern Territory Government financial assistance;
- a decrease in HECS – HELP, and Fees and Charges;
- offset by an increase in Fees and Charges mostly attributable to an increase in Fee-paying Overseas Students.

The increase in expenses was predominantly due to an increase in employee related costs, together with an increase in depreciation and amortisation.

I noted that the majority of the surplus reported for the year was attributable to funds received by the University to finance specific projects and which were not, therefore, available to finance the University's discretionary spending.

Charles Darwin University cont...

Financial Position at year end – excluding controlled entities		
	2011	2010
	\$'000	\$'000
Current Assets	94,779	99,810
Less Current Liabilities	(29,572)	(28,625)
Working Capital	65,207	71,185
Add Non Current Assets	384,870	368,021
	450,077	439,206
Less Non Current Liabilities	(1,458)	(1,189)
Net Assets	448,619	438,017
Represented by:		
Reserves, restricted and accumulated funds	448,619	438,017
Equity	448,619	438,017

Charles Darwin University Foundation

Audit findings and analysis of the financial statements for the year ended 31 December 2011

Background

The Charles Darwin University Foundation (the Foundation) is a public company limited by guarantee that acts as trustee of the Charles Darwin University Foundation Trust (the Trust). The Foundation incurs liabilities on behalf of the Trust and discharges those liabilities out of the assets of the Trust.

The Foundation and the Trust were established as the fundraising arm of the University and both are controlled entities of the University within the meaning of section 41 of the *Charles Darwin University Act*.

The purpose of the Foundation is to enhance the relationship between the University and the wider Northern Territory community, and to raise funds for the University. In pursuit of this objective, the Foundation seeks donations and other contributions while also providing assurance to donors that bequests and donations will be applied in accordance with the wishes of the testator or donor.

Audit Opinion

The audit of the financial statements of the Foundation and the Trust for the year ended 31 December 2011 resulted in unqualified independent audit opinions for both entities and these were issued on 16 April 2012.

Key Findings

As noted in previous years, there are instances where in-kind donations are provided to the Foundation without supporting evidence to substantiate the donors' advice as to the value of the donations. However, the risk of misstatement of the financial performance or financial position of the Foundation is not considered to be material given that in-kind donations are recorded as income and expense in the same period in which they are received.

This and previous audits have also identified a weakness in the control over the receipt of "over the counter" cash donations. However, as the amounts received by this method occur relatively infrequently, I did not consider it necessary to qualify my audit opinion in relation to the completeness of revenue.

Charles Darwin University Foundation cont...

Financial Performance for the year – CDU Foundation Trust Only

	2011	2010
	\$'000	\$'000
Revenue from ordinary activities	1,424	1,475
Less expenses from ordinary activities		
Trust donations disbursed	(1,082)	(1,302)
Donations in kind – operational	(49)	(174)
Unrealised revaluation loss on investment	-	-
Other	(21)	(2)
Total expenses from ordinary activities	(1,152)	(1,478)
Net operating result for the year	272	(3)

Charles Darwin University Foundation cont...

Financial Position at year end – CDU Foundation Trust Only

	2011	2010
	\$'000	\$'000
Current Assets	4,529	4,245
Less Current Liabilities	(17)	-
Working Capital	4,512	4,245
Add Non Current Assets	411	411
Net Assets	4,923	4,656
Represented by:		
Investment Revaluation Reserve	66	71
Retained Earnings	4,857	4,585
Equity	4,923	4,656

Department of Construction and Infrastructure

Darwin Correctional Precinct

Background

A high level review of the public-private partnership (PPP) arrangement for the development of a new correctional facility was undertaken with the objective of gaining an understanding of the legal and financial arrangements to enable a preliminary overview of the project to be provided to the Legislative Assembly.

The existing correctional facilities at Berrimah were commissioned in 1979 and are approaching the end of their useful lives. At the same time the prison population now exceeds the design capacity of the Berrimah facility and some criticisms have been made about the extent to which inmates who were deemed mentally unfit to plead are held within a general prison facility.

As a result the Government gave approval in August 2010 for the development of a new prison facility to be located on the Howard Peninsula.

As part of the deliberations leading to the final approval to proceed with development of the new facility, both the traditional design and construct, and the public-private partnership approach were considered. Approval was given to investigate the feasibility of using a public-private partnership approach through the use of a “market sounding exercise”.

The market sounding team, as it was called, was led by the Northern Territory Treasury and included representatives from the Departments of the Chief Minister, Justice, Health, Business and Employment, and Construction and Infrastructure. That team drew upon technical and other expert advice from other Agencies and organisations. As part of its role, the team was also charged with the development of a clearly defined project scope, a preliminary public sector comparator, and the finalisation of the process for the selection of the prison site.

Following the process described above, expressions of interest were sought which resulted in responses being received from three consortia. Each of the respondents was considered capable and a Request for Proposal (RFP) was issued to each respondent.

Department of Construction and Infrastructure cont...

Each of the consortia responded to the RFP and the subsequent evaluation process included seven interactive workshops accompanied by a structured negotiation process. That led to the selection of a preferred consortium and to the execution of the Northern Territory Secure Facilities PPP Project Deed in September 2011 between the Northern Territory of Australia and the joint venturers of CIPL Sentinel Pty Ltd and BBPI Sentinel Pty Ltd (Sentinel).

Description of the Project

The project consists of the design, construction and operation of a new facility that will comprise:

- An 800-bed low, medium and maximum security correctional centre for males and females. The facility will be capable of expansion to 1000 beds if the need should arise.
- A 30-bed mental health behavioural management facility that will comprise low, medium and high dependency units, as well as “step down” cottage accommodation.
- A supported accommodation and program centre that will have capacity for 48 supported accommodation beds and which is intended to provide a range of treatment and training programs for both residential and outreach clients.
- Support facilities and security infrastructure.

Following the commissioning of the facility in 2014, the existing Berrimah Prison will be decommissioned.

The due date for completion of the precinct is 30 June 2014 and the Deed will remain in force for 30 years, with an expected expiry date of 30 June 2044. Following the expiry of the Deed ownership of the precinct will pass to the Northern Territory.

Sentinel, as the owner of the precinct, will be responsible for the management and maintenance of the facility, but staffing of the precinct will be the responsibility of the Northern Territory.

Department of Construction and Infrastructure cont...

Overview of Public Private Partnerships

A public-private partnership (PPP) is an arrangement often employed for the procurement of large and complex infrastructure facilities. PPP's have been used increasingly by governments in a number of countries (and in most states in Australia) to provide infrastructure such as roads, public buildings, health and educational facilities, prisons, public transport and other public services. A review of PPPs suggests that they have been a successful and cost-effective means of delivering public infrastructure in Australia.

A PPP may take a number of forms including:

Design and Build: where the public sector specifies the asset requirements in terms of its functions and desired outcomes. The private sector partner is responsible for designing and building the asset, managing any related risks, and transferring the asset to the public sector to operate.

Build Own and Operate: requiring a private sector partner to develop, finance, build, own and operate a facility for a defined period. At the conclusion of that period the risks of ownership associated with the facility remain with the private sector partner.

Build Own Operate and Transfer: requiring a private sector partner to develop, finance, build, own and operate a facility for a defined period. At the expiration of that period the facility is transferred to the public sector partner.

Build Own and Maintain: requiring a private sector partner to build, own and maintain a facility for a specified period. The facility is leased and staffed by the public sector partner.

The PPP that has been established for the Darwin Correctional Precinct has elements consistent with that of build, own, maintain and transfer. Sentinel will construct, own and maintain the facility for a period of 30 years following which ownership will be transferred to the Northern Territory.

The use of a PPP does not, as a matter of course, offer some low cost means of obtaining public infrastructure. It may provide an opportunity to obtain infrastructure at a cost that is less than might be the case if a government were to construct that infrastructure on its own account, but that may rest on the private sector partners' ability to provide technical and managerial expertise that may not be available in the public sector.

Department of Construction and Infrastructure cont...

What a PPP can offer is an ability to allocate the risks associated with a project between the public and private partners on the basis of which party is best placed to manage the risk in question. At the same time, a PPP can enable a government to reduce its overall capital outlays by having the private sector partner finance a project, but at the expense of being required to meet ongoing financial obligations over some agreed period so that the private sector partner recovers the capital costs associated with construction, together with interest.

The Legal Framework

The PPP for the Correctional Precinct is governed by extensive documentation, but the central document is the Northern Territory Secure Facilities PPP Project Deed that sets out the contractual arrangements that will apply between the Northern Territory and Sentinel. The Project Deed is complemented by a number of side deeds.

The participants in the project are:

- The Northern Territory of Australia.
- The Sentinel Group – the main contracting entity with the Territory. It will be ultimately responsible for the delivery and ongoing operation of the Precinct.
- The Equity Provider – Bilfinger Berger Project Investments Australia and Commonwealth Investments Pty Ltd will provide the total equity required by Sentinel.
- Financiers – Commonwealth Bank of Australia, ANZ, National Australia Bank and West LB will provide debt funding.
- Builders – Boulderstone Pty Ltd and Sitzler Pty Ltd operating as a joint venture will undertake the design and construction of each component of the precinct.
- Facilities Manager – Honeywell Ltd will provide facilities management services across the precinct.

Department of Construction and Infrastructure cont...

Who Bears the Risks?

One of the attractions of a PPP from the perspective of the public sector is the potential that it offers for the allocation of risk to the party that is best able to manage the risk in question. A summary of the types of the risk and the extent to which they will be borne by either the Northern Territory or by Sentinel follows.

Planning risk. Both Sentinel and the Northern Territory are exposed to this risk. The consortium will be responsible for obtaining the development permit. However, the Territory will be required to compensate Sentinel if Sentinel does not receive a development permit within six weeks of correctly lodging an application. The Territory's risk will crystallise only if the application was lodged in accordance with industry best practice and Sentinel has engaged with the appropriate Government agencies in accordance with industry best practice.

Precinct risks. There are three elements to this class of risk. Firstly, responsibility for the precinct and its physical state and conditions. Secondly, the risk that relics may be found on, in or under the precinct. Thirdly, that the precinct is the subject of a Native Title claim.

Risk is borne by the Territory if an environmental notice is served in respect of pollution other than any pollution that was disclosed to Sentinel prior to entry into the Project Deed; and any pollution where compliance with the environmental notice requires remediation to no higher standard than as required under the Project Deed. Otherwise risk is borne by Sentinel.

Where there is a risk that any relics may be found on, in or under the precinct and if the Territory chooses to keep those relics it will be responsible for the reasonable costs incurred by Sentinel in removing the relics in question, otherwise Sentinel will bear the costs of removal and/or destruction.

The risks associated with Native Title claims will borne by the Territory.

Design construction and commissioning risk is the risk that the precinct is not completed on time and/or to budget, that it is not fit for purpose and that no defects are identified following completion. This risk will be borne by Sentinel unless delay is attributable to the Territory or a defect is attributable to the Territory or a Territory related party.

Department of Construction and Infrastructure cont...

Operational risk includes the risk that the facility is not fit for purpose, that operational costs exceed budgeted cost over the services phase of the project and the risks associated with the replacement and refurbishment of the facility over the services phase. This risk will be borne by Sentinel.

Change in law is the risk that a change in law will affect the design and construction of the facility, of the provision of services, or that force majeure or some other specified unforeseen event will affect the construction of the facility or the provision of services.

Finance risks associated with the refinancing of liabilities, insurance and the residual condition of the facility on expiry of the contract are allocated between the Territory and Sentinel. The Territory will share with Sentinel some refinancing losses and all refinancing gains, while also sharing insurance risk.

Department of Construction and Infrastructure cont...

The Cost to the Northern Territory

The total cost faced by the Northern Territory at June 2014 will comprise:

- An amount having a present value of \$521.3 million (based on nominal cash flows of \$1.64 billion over a period of 30 years). This amount represents the repayment of principal, payment of interest and equity returns and also represents the fair value of the asset at the date at which the Northern Territory assumes control of the facility and responsibility for the liability in 2014. It is possible that the present value of this payment may vary if refinancing gains or losses should arise and if the Territory should elect to vary the periodic payment as an alternative to making or receiving a cash payment.
- An amount having a real value of \$300 million. This amount comprises three separate payment streams as follows:
 - a quarterly lifecycle payment, indexed using the Consumer Price Index, for the periodic refurbishment, replacement, and maintenance of the facility. This payment will have a present value of \$146.3 million;
 - a quarterly services amount, indexed using the Consumer Price Index, for facilities management and special purpose vehicle management costs. This payment will have a present value of \$56.9 million; and
 - a quarterly services amount, indexed using the Labour Price Index, for facilities and special purpose vehicle management costs. This payment will have a present value of \$96.8 million.

Both amounts represented commitments of the Northern Territory as at 30 June 2012 and were disclosed appropriately in the notes to the Treasurer's Annual Financial Statements.

The amount of \$300 million which will be payable by the Territory to Sentinel is considered to be appropriate given that Sentinel is required by the Deed to ensure that the facility is in a condition consistent with industry best practice at the date of handover.

Department of Construction and Infrastructure cont...

At the point at which the Territory assumes control of the facility in 2014, the amount of \$521.3 million will satisfy the definition of a liability and will need to be shown as such on the face of the Treasurer's balance sheet. The amount of \$300 million is considered to have the elements of an executory contract which is equally and proportionally unperformed and that amount will continue to be disclosed as a commitment, adjusted from time to time in line with changes to the associated indices, until 2044 when the final payments are made.

As indicated above, the fair value of the facility upon completion will be \$521.3 million, comprising:

	\$ million
Correctional Centre	362.0
Mental Health and Behaviour Management	47.0
Supported Accommodation and Program Centre	16.4
External Facilities	69.6
Total Direct Construction Cost	495.0
<hr/>	
Capitalised Consultancy and Advisory Expenses	26.3
Total Project	521.3

That amount will be paid initially by Sentinel, but repaid by the Territory, by way of the unindexed quarterly services amount, over a period of thirty years, with the first payment being made immediately following the commissioning of the facility. The liability and its repayment structure can be likened to a credit foncier loan arrangement, where each payment by the borrower comprises repayment of part of the principal amount outstanding together with a payment of interest on the outstanding principal balance.

The Extent to Which the Implicit Interest Rate Compares With the Territory's Own Borrowing Costs

For a project such as the development of a correctional complex, the choice was between the Territory undertaking the project on its own account, borrowing the funds necessary to finance construction, or entering into a PPP with a view to having a private sector partner finance the construction of the facility in return for a periodic fee that covers the agreed construction cost.

Department of Construction and Infrastructure cont...

There are sound reasons why a government may choose to enter into a PPP, among them being the ability to reduce exposure to risk by having some of that risk assumed by a partner. It is to be expected that the effective costs of finance that will be faced by the Territory where a PPP approach is used will be higher than might be the case if the Territory chose to construct a facility on its own account. The effective cost of funds that the Territory faces in the case of a PPP will reflect the level of risk assumed by the partner in the project.

The higher cost of funds faced by the Territory by having a private sector partner provide financing can be viewed as the “price” that is paid to have the partner assume risks associated with its construction. This higher cost of funds can be offset by efficiencies that flow from the involvement of a partner that is knowledgeable and skilled in the field of construction leading to lower capital costs as a consequence.

As indicated above, the liability of the Territory to Sentinel arising from the construction of the facility will be \$521.3 million, to be repaid over 30 years by way of a quarterly service payment. This payment is described as “non indexable” (unlike the other periodic payments to be made) and the effective annual interest rate attaching to the unindexed quarterly services amount has been estimated by audit to be 10.3 per cent. This rate can be compared with the Territory’s weighted average cost of borrowing at the time of the agreement which was 6.0 per cent. The weighted average cost has been used for the purposes of comparison as it is considered more likely that any direct borrowing undertaken by the Territory to finance a project of this nature would form part of a pool of borrowings undertaken for capital purposes rather than specific borrowings intended specifically for the construction of the facility.

Department of Construction and Infrastructure cont...

The difference between the Territory's weighted average cost of borrowing and the effective interest rate being faced as a result of the decision to use a PPP structure in this instance is due to two principal factors. Firstly, the transfer of risk from the Northern Territory to the consortium of which construction risk is arguably the largest. The second factor is the state of financial markets in the wake of the Global Financial Crisis of 2008 and 2009, and more recently the difficulties being experienced by the banking system in Europe. Events of recent years have seen a progressive tightening in private debt finance that is available for infrastructure projects, irrespective of whether they involve PPP arrangements leading to banks being the principal source of funding. At the same time banks were facing higher costs as wholesale financial markets became increasingly concerned about the potential for credit losses, leading to banks being required to pay a premium for financing in capital markets, while also finding it difficult to raise debt for more than a 5-year tenor.

The margin between the Territory's weighted average cost of borrowing and the effective interest rate that is implicit in the financing of this PPP may narrow as debt is refinanced over the life of the Deed if conditions affecting financial markets should ease.

Management of the Project

As outlined above, while the legal arrangements governing the PPP remove the Northern Territory from direct involvement in the construction of the facility, the Northern Territory cannot avoid being exposed to the risk that the project may not adhere to its construction schedules, that it may fail to meet the Territory's needs or that one of the PPP partners may be unable to meet its obligations. It is most unlikely that a Northern Territory Government will be able to turn its back upon the project in the event of failure by a partner; to do so would leave that government in the position that prevailed in prior years when the need for a new facility became increasingly urgent. It is more likely that the government would need to intervene directly in the project and face the likelihood of higher costs in order to achieve its policy objectives.

Department of Construction and Infrastructure cont...

This type of risk has been described as the “implied guarantee”. The implied guarantee does not rest on any particular principle or criterion and it may arise irrespective of whether there is government fault, or whether there is government control, or government ownership, or even government financial involvement. The implied guarantee may apply notwithstanding that risks are allocated in formal contracts between a government and a private sector operator or constructor.

An example of how events may unfold thereby crystallising an implied guarantee is illustrated by events affecting a similar PPP project in Victoria which involves the expansion of the Ararat prison. That project encountered difficulty in May 2012 when the project builder was placed into liquidation, with the project company being placed into voluntary administration shortly thereafter when one of the project financiers withdrew. The Ararat project has since recommenced, with two banks agreeing to finance the project, to meet the claims of unpaid subcontractors and to seek a new builder to take over construction of the facility. The new arrangements appear to have been accompanied by an increase in the liability faced by the Victorian Government.

What this suggests is that the public sector must maintain a close involvement in any PPP to ensure that its interests are protected. In the case of the Ararat Prison PPP, risks that were thought to have been shifted contractually eventually returned, to be assumed the Victorian government.

It is notable that a number of the participants involved with the Victorian PPP are also involved with the Northern Territory project. The key difference between the Victorian and Northern Territory projects appears to lie in the capacity of the builders who formed part of the consortium contracted to extend the Ararat prison. Victoria selected a consortium that included builders that may have found the Ararat project challenging. In contrast the consortium for the Northern Territory includes one builder that has operated nationally for many years together with a Territory based builder with a sound reputation. It is more likely that the builders in the Northern Territory case have the capacity to withstand cost and other pressures that can be expected to arise over the life of the project’s construction phase.

Department of Construction and Infrastructure cont...

The risk that surrounds any project such as the correctional precinct, when taken together with the importance of the project, suggests that the Northern Territory cannot view itself simply as a “customer”, but must play an active oversight role in order to ensure that its interests are protected and that the implied guarantee will not be triggered. This role must extend over the life of the contract which expires in 2044. The evidence provided during the course of this review suggests that the Territory has exercised the degree of diligence that might be expected in these circumstances and that reflects the experience gained in other, similar, projects.

Conclusion

It is important that this degree of diligence will need to be maintained until 2044. To reduce the risk of contract failure, the accompanying need for Territory intervention, and the accompanying risk of higher costs it is recommended that one agency has responsibility for the management of the contract over its life.

During the construction phase of the project, that responsibility should rest solely with the Department of Infrastructure.

The most appropriate Agency in the period following commissioning of the precinct is the Department of Correctional Services. Responsibility should be allocated to one unit within that Department with that unit being responsible for ensuring that the Territory's interests are protected. Given the life of the contract, it will be important to ensure that the transfer of knowledge, experience and skills occurs over the years to ensure that the Territory's interests are not compromised.

Department of Construction and Infrastructure

McMinn Street Duplication Project

Objective

This review was undertaken following concerns raised by the former Public Accounts Committee and its objective was to examine the reasons for cost variations for the project.

Background

The project comprised:

- duplication of McMinn Street between Frances Bay and Foelsche Street;
- installation of beautification works including a landscape corridor;
- provision of a disability standard elevated shared path along the western side of McMinn street; and
- provision of a footpath along the eastern side of McMinn Street.

The project was managed by the Department of Construction and Infrastructure (DCI) on behalf of the Department of Lands and Planning.

Key Findings

A contract for the construction of the McMinn Street extension was awarded on 10 August 2009 for completion by December 2009. However the project was not completed until December 2011 with some of the delays being attributed to a failure on the part of a company contracted to provide engineering design services.

Delays were also caused by unforeseen works due to a range of factors that are outlined below and which, in some cases, are related to the design-related delays.

Problems in the design phase of this project were the principal factors behind the delays in completing this project. While the designer undertook redesign work at that firm's own expense, the project was faced with delays and consequential cost increases that flowed from the original design shortcomings.

Department of Construction and Infrastructure cont...

Design and Initial Costings

The initial cost estimate, which was provided by the designer, was \$3.2 million, excluding goods and services tax and contingencies. That estimate was subsequently revised to \$4.2 million in June 2009 following a refinement of the project scope in relation to landscaping, together with increases in the estimated costs for service relocation, retaining works and earthworks.

Project Delays

As indicated above while the project was originally scheduled for completion by December 2009, it was not completed until December 2011 with delays being attributed to a failure on the part of the designer to:

- prepare adequate design drawings. Some drawings proved to be unworkable thereby requiring redesign to be undertaken. In one instance delays in preparing new drawings meant that the isolation of a sewer main was not possible due to the onset of the wet season;
- include sufficient information in the original drawings prepared to enable a contractor to manufacture and install a balustrade;
- identify a water main adjacent to the NT News site during the design phase;
- identify a shallow high voltage cable in a conduit under the pavement. This oversight required a different pavement design in order to raise the pavement levels so as to provide the minimum required level of cover over the cable;
- design a keystone retaining wall that could be constructed in a practicable way;
- take into account as part of the original design illegal storm water outlets from buildings adjacent to McMinn Street thereby requiring a redesign to be undertaken.

Department of Construction and Infrastructure cont...

Delays were also caused by unforeseen works that were due to a range of factors that are outlined below and which in some cases are related to the design-related delays noted above:

- Acquisition of a site adjacent the NT News was not completed at the time of the tender. The Land Administration Division of the Department of Lands and Planning had responsibility for land acquisition; but despite the acquisition process being initiated well in advance, follow up appeared to have been overlooked during the protracted planning period.
- An unidentified storm water service location which if not rectified would have prevented the lowering of other services e.g. sewerage and underground high voltage services.
- Unidentified underground high voltage services that required concrete capping to be installed. That in turn led to the need to adjust the levels of finished pavement surface levels in order to maintain appropriate cover.
- An unstable rock cutting that contained underground storm water services, high voltage lines and telecommunications services.
- The need to construct an earthen platform to provide an adequate and safe working space to stabilize unstable material, construct the retaining wall and install appropriate drainage structures.
- An unidentified water main that would have been located under the new pavement surface and would have had insufficient cover. As a result of this a design change was required to reduce the pavement width therefore necessitating the construction of a foot and cycle path.
- A proposed foot path alignment which was to be constructed was found to contain numerous services valve pit lids and telecommunication pits. These services required lowering or rising to match the finished surface level of the new path.
- An unidentified underground water main conflicted with other services requiring relocation of the water main.

Department of Construction and Infrastructure cont...

- Access to a private development site required the sewerage, water and high voltage services to be lowered. As part of this, the sewerage services had to be redesigned due to previously unidentified connections. However, the high voltage services could not be lowered due to restrictions imposed by the Darwin City Council to protect four trees. As a result significant redesign was required and a temporary high voltage connection had to be established to service the Darwin Waterfront.
- Waste materials that appeared to have been dumped in the period following Cyclone Tracy were found and had to be disposed of.
- A design change required removal of existing street lighting and placement of temporary street lighting to maintain safety for night traffic.

The Final Cost

DCI issued 130 “change orders” against this project, with the final cost (at the time of the review) having increased to \$8.7 million (excluding GST) compared to the initial estimate of \$4.2 million and the tender amount of \$4.5 million.

The most significant variations related to:

- service relocation;
- earthworks;
- concrete works; and
- landscaping.

Conclusions

The contracting of external firms can be a cost effective means of obtaining access to specialized skills and knowledge that may be required by the public sector. The firm that was engaged to provide design services in this instance has a reputation for competence. However, in this case, it appears that the firm’s own systems did not operate in a way that might have been expected in the circumstances leaving DCI to face significant delays to the project and accompanying cost over-runs.

Department of Construction and Infrastructure cont...

The Department of Infrastructure has commented, on behalf of the former Department of Construction and Infrastructure:

I acknowledge the key findings of the review.

This project was identified for a Post Construction Review which is being undertaken by an independent consultant with completion expected early June 2012. That process involves interviews with key stakeholders, followed by a round table meeting and will include recommendations of changes that may be necessary to internal processes.

Following the receipt of the review a lessons learnt exercise will be conducted with staff who are responsible for the delivery of similar type projects.

The delivery of projects within the Department is through a documented process (roadmap) which identifies the various steps necessary for successful delivery. This process has now been embedded into the new Asset Management System which will include better workflow and provide delegated signoff to key activities.

Since the start of the McMinn Street project the Department has also employed an estimator which has improved the quality of estimates at all stages of the design process.

Another area where the Department has looked to improve its processes is with risk assessment, particularly in identifying underground services where additional expenditure in the design phase may result in less construction changes and associated costs.

Department of Construction and Infrastructure

Tiger Brennan Extension

Background

This review arose out of a request by the former Public Accounts Committee and its objective was to examine the reasons for the cost variations for the project described as “Tiger Brennan Stage 1 and Stage 2”.

The Federal and Northern Territory Governments jointly funded the three stage upgrading of the East Arm Port Access Road with the objective of improving access to the Port of Darwin.

The project stages were:

- Stage 1: which included the duplication of Berrimah Road from Wishart Road to Tiger Brennan Drive and the creation of dual turning lanes to ease congestion.
- Stage 2: the design and construction of 7.5 km of road works to extend Tiger Brennan Drive from Berrimah Road to the Stuart Highway, and to provide a grade separated interchange at the intersection of the Stuart Highway and Roystonea Avenue.
- Stage 3: the construction of the Berrimah Road Rail Overpass. Stage 3 did not form part of this review.

Stage 1

The contract for this stage was awarded to the tenderer offering the lowest price of \$6.5 million in January 2008. Stage 1 was planned for completion in late 2008 and was completed early 2009. Extensions of time were granted for inclement weather, additional earthworks and the shutdown over the Christmas-New Year period.

Department of Construction and Infrastructure cont...

The financial result

The final cost for this stage was \$10.6 million compared to an original estimate of \$8.3 million, and the tender price of \$6.5 million (these amounts include goods and services tax).

The increase in cost was attributable largely to:

- time and costs relating to delays and redesigns;
- additional earthworks due to design changes;
- streetlight cabling design alteration;
- substandard substrata material identified during the course of construction;
- the need to lower Telstra fibre optic cables;
- the undergrounding of high voltage lines;
- additional earthwork requirements due to the need to revise earlier estimates of cut and fill quantities; and
- the need for subsurface drainage to remove large volumes of groundwater at the intersection of Tiger Brennan Drive and Berrimah Road.

Department of Construction and Infrastructure cont...

Stage 2

This stage consisted of two phases; the first comprising design and project planning, with the second being the finalisation of design, preparation of construction documentation, and the construction of the infrastructure.

This stage differed from Stage 1 in that it saw the Department undertake some initial concept planning for the project. It was the expectation of the Department that changes to the preliminary design would be required as the planning for this stage evolved. The initial project estimate was \$89 million (including GST).

Stage 2 was also characterised by the use of Early Contractor Involvement (ECI) delivery methodology, the first time that this approach had been used in the Northern Territory.

The ECI methodology was used as it was envisaged that it would provide:

- the ability for the Contractor to bring its own experience to the project during the detailed design stage of the contract;
- synergies arising from the use of a high performance design and construction team working in cooperation with the Northern Territory Government;
- better integration of specific construction methodologies into the design;
- greater flexibility and time for planning in the project;
- likelihood of earlier procurement of critical construction materials;
- earlier dedication of construction resources to the project; and
- negotiated apportionment of risk.

The tender

The contract awarded for Stage 2 was for \$8 million (including GST) in respect of Phase 1 and for \$92.5 million (including GST) in respect of Phase 2.

Department of Construction and Infrastructure cont...

The financial result

Phase 1 – The cost at the time of this review was \$10.4 million compared to the tender of \$8.0 million.

Phase 2 – The cost at 13 December 2011 was \$113.7 million, which included \$19 million that related to the Berrimah Road Rail Overpass that forms part of Stage 3 of the project. Thus the actual comparative figures for Phase 2 are a cost of \$94.7 million compared to the tender of \$92.5 million.

All Including GST	Estimate \$ million	Tender \$ million	Actual \$ million
Stage 2 – Phase 1		8.0	10.4
Stage 2 – Phase 2		92.5	94.7
Total Stage 2	89.0	100.5	105.1

The most significant items of additional costs were related to design amendments that saw:

- the inclusion of slip lanes at the Roystonea Avenue/Yarrowonga Road intersection;
- a redesign of the Marjorie Street off-ramp to assist road trains accessing Marjorie Street from the Stuart Highway;
- the inclusion of an entrance to the new Palmerston Water Park; and
- the realignment of the Tivendale/Wishart Roads intersection.

These design amendments were predominantly a result of the implementation of the 2009 Austroads Road Design Guide, which supplanted the VicRoads Design Guide that had been used by the Department until then.

Department of Construction and Infrastructure cont...

Financial Result – Stage 1 and Stage 2 (both phases)

All Including GST	Estimate \$ million	Tender \$ million	Actual \$ million
Stage 1	8.3	6.5	10.6
Stage 2	89.0	100.5	105.1
Total	97.3	107.0	115.7

Stage 3

Although Stage 3 was out of scope of this review it was noted that there were 2 project delivery options considered for Stage 3. The first delivery option was to call for public tenders with the second option being to vary the Stage 2 contract to include the Berrimah Road Rail Overpass.

The second option (varying the Stage 2 contract) was chosen resulting in that work being undertaken by the successful tenderer for Stage 2.

Department of Health

Grants by the Department to NGO's for the delivery of primary health services

Audit Scope and Objective

This audit was undertaken to determine whether the performance management systems within the Department of Health (DoH) enable the Department to assess whether the activities of NGOs in the delivery of health and related services are consistent with the Department's goals and objectives and are assisting DoH to achieve its stated outcomes.

Audit Opinion

In the last eight years, my Office has conducted two performance management system audits that sought to examine the management of NGOs in the delivery of health services. Those audits were conducted in 2004 and 2010. The findings of both audits noted that the then Department of Health and Families had been active in seeking refinements to the process of managing NGOs, but it is also evident that both the audits found similar issues. This audit identified a number of issues that have arisen since 2004, which appear not to have been satisfactorily resolved.

Background

Non-government organizations (NGOs) play an integral role in the public sector's delivery of the health and related services to the community. In this context NGOs can be viewed as agents of the DoH, working in conjunction with the Department to help achieve its objectives. For 2010/11, DoH made grants totaling \$134 million to NGOs for the delivery of specified services.

The Department has outlined its approach in its corporate plan 2009 to 2012 where it notes that "Continuous system improvement focused on patient and client welfare is central to the DoH Corporate Plan 2009-2012, our blueprint for advancing the vision of Healthy Territorians Living in Healthy Communities". I formed the view during the audit that the evidence submitted to me indicated that the Department has pursued, and continues to pursue, objectives that are consistent with its corporate plan and this includes the implementation of a new grants management system (GMS).

Department of Health cont...

Notwithstanding the progress to date, DoH may face challenges in ensuring that it achieves greater collaboration between the DoH and NGOs in the delivery of health services and in ensuring that DoH's performance management systems are capable of providing information that will enable the DoH to assess whether its objectives in relation to the utilisation of NGOs are being achieved effectively. These challenges include ensuring that:

- DoH's corporate objectives are clearly defined across all programs and linked to the DoH's outputs and to NGO activity levels;
- actions and initiatives to meet these objectives are established with clear links to the corporate objectives;
- performance measures in the DoH's corporate planning documentation are written in comprehensive and measurable terms, and aligned to each business goal; and
- methodologies and systems utilised to collate the required information for the performance measurement and to monitor actions and initiatives are clearly identified, implemented and used by all relevant stakeholders.

As indicated above, a new GMS was under development at the time the audit was conducted and it was apparent that the project had encountered problems with management of the project leading to a deferral of the "go live" date.

In view of the GMS issues, I recommended to DoH that a post-implementation review of the GMS be completed with a further review of the DoH's project management framework to reduce the likelihood of similar issues emerging in the future.

Department of Health cont...

Non-Government Organisations

The DoH, in its Annual Report for 2010/11, indicated that the DoH works in partnership with other government and non-government organisations to ensure the well-being of all Territorians. The key focus areas identified were:

- “Working effectively and proactively with partners in the government, non-government and for-profit sectors to build the best possible service systems for the Northern Territory”. One of the key achievements noted was “a range of strategies aimed at increasing the participation of Aboriginal people into the health and community workforce in joint partnership with key education and non-government health provider partners will be designed and implemented”;
- “Placing clients and their needs at the centre of service planning and service delivery.”

It is apparent, within the Annual Report that DoH relies heavily on NGOs to assist in the delivery of outputs and in this context DoH has defined an NGO as “*any external organisation that receives government funding to provide health or community services or related activities to the NT community.*”

Grants and Funding to NGOs

Information included in DoH’s annual report for 2010/11 indicated that Acute Care Services, Health Protection, Health Services, and one corporate division, Performance and Measures, provided over \$134 million in funding to various organisations. It is likely that NGOs see this type of funding as vital to their continuing ability to fulfill their roles as they typically have limited capacity to generate revenue by other means.

Department of Health cont...

Key Findings

During my audit I took account of DoH's efforts that have been directed towards the establishment of a more robust performance management system for the management of service delivery by NGOs. It is clear that there has been work done by the DoH around policy development and the development of a new GMS. However, my overall finding suggests that the DoH's progress towards implementing an effective, efficient and economical NGO service delivery management system still has some way to go.

It was noted that issues raised with the former Departments of Health and Families, and Health and Community Services following the earlier performance management systems audits had not been addressed satisfactorily and DoH advised that the outstanding issues would be addressed.

I also undertook a 'high-level' review of the GMS project to examine key issues surrounding the project management of the GMS. It is envisaged that the GMS, when complete, will address shortcomings identified during my previous audits, but the successful implementation of the system was being hampered by project management issues.

A consultancy awarded to a large information technology consultancy firm in 2010 was supposed to deliver a business case together with functional requirement specifications, suitable for inclusion in a request for tenders, with sufficient information to enable prospective tenderers to provide high quality responses; and evaluation criteria for assessment of tender responses.

The consultancy firm's response to the tender requirements (which could not be provided by DoH during the course of the audit, but had to be sourced from the firm in question) contained no reference to the DoH-specific requirements. As a consequence, neither DoH, the consultancy firm, nor that firm's sub-contractor, appeared to have understood clearly the fitness for purpose of the product that was selected to meet DoH's requirements.

Neither DoH nor the consultant appeared to have had a good understanding of the architecture of the selected application, particularly what modules would require customisation or those that would require configuration in the DoH environment.

Department of Health cont...

This shortcoming could have been identified at the tender evaluation stage if the functional requirements were included in tender documents, if tender documents had included questions about customisation versus configuration and if sound evaluation criteria had been applied.

Differences in culture, scale, approach and personalities resulted in a mismatch in governance and quality expectations, and a breakdown in communication between all parties. Given that a similar project in another Agency (and involving the same consultant and sub-contractor) was planned to take five months, but took seventeen months, DoH should have been alerted to the potential for development problems.

The consultant prepared a project statement which was accepted by the DoH in September 2011 (two months into the project). That statement makes no reference to the prototyping approach used by the sub-contractor, but rather represents a more traditional systems lifecycle approach to development suggesting that the consultant's methodology clashed with that of the sub-contractor.

The inability to find substantiating documentation, or to determine the author, version, and acceptance of project documentation not only impeded this audit, but also made the transition from the old to the new project managers for both the contractor and for DoH a difficult task.

Department of Health cont...

Recommendations to DoH

As a result of the audit it was recommended to DoH that:

- Clear and consistent definitions and terminology need to be established to distinguish grants from other forms of funding and to separate grant funding to a NGO from other statutory authority.
- More transparent reporting, including public disclosure, in relation to NGOs is required.
- There is a need to develop a departmental policy to deal with the carry-over of unspent grant monies at the end of each funding year.
- The NGO governance framework and arrangements should be reviewed and further enhanced.
- The DoH's objectives in relation to NGOs should be clarified in the DoH's strategic and/or business plans framework/plans. This issue was also raised in the previous audit.
- Information systems supporting the management of the service agreements with NGOs should be reviewed and enhanced.
- The revised GMS user requirements need to be reconfirmed with the respective business divisions as soon as possible.
- Proper project management and governance processes should be re-established for the GMS project.
- Contractual arrangements with the consultant for the development of the GMS need to be updated.
- The DoH should establish good practice documentation and document controls in relation to the project management of the GMS.
- Inter-Agency communication both at the executive and officer level could be improved to bring about better project management practices at the DoH.
- Contingency plans need to be put in place to address risks to the GMS project.

Department of Health cont...

The Department of Health has commented:

The Department has accepted all of the findings and recommendations related to the Grants Management System (GMS).

I am pleased to advise that there has been considerable work undertaken since the Audit was conducted to address the recommendations and most of them have commenced or are completed.

The Department had initiated its own review of the governance and management of the project which resulted in a revised Project Management Plan. We have established clearer reporting lines with the technical development aspects of the system now reporting to an ICT Project Board within the Office of the Chief Information Officer and the Policy Reform aspects of the Project reporting through the Office of the Chief Executive. Key Project staff from both teams meet weekly with the Chief Information Officer and the Office of the Chief Executive to ensure the project is on schedule.

Further there are regular meetings with the project teams and Senior Officers of Department of Health, Department of Family and Children and the vendor to discuss progress and milestones.

I advise that the Project Sponsors have agreed to the Project completion date being extended, with the agreement of key departmental stakeholders to ensure delivery of a quality functioning system that meets the project scope, the needs of the Department's and the Sector.

Further, we have included the Audit findings in our risk register which will also be monitored by the Director of Audit and Risk as well as the Department's Audit and Risk Committee.

Department of Lands and Planning

Review of Assessment of Responses to Request for Provision of Ferry Services

Scope and Objectives

The objectives of this review were to assess whether tenders for the provision of a Darwin to Mandorah ferry service were assessed in accordance with Northern Territory Government Procurement Directions and Guidelines and to ascertain the reasons behind a decision to award and to subsequently revoke preferred tenderer status to one of the tendering firms.

Background

A ferry service was operated between Darwin and Mandorah for a number of years under a concession deed which allowed the operator, Sea-Cat Ferries & Charters Pty Ltd (Sea-Cat), sole access to waters between Cullen Bay and the Mandorah Jetty for the purposes of operating a public ferry service. That deed had an expiry date of 31 December 2011, but it did contain a clause that provided for an extension of the arrangement for a period not exceeding two years. Relying on that clause, the then Department of Lands and Planning (DLP) approached Sea-Cat late in 2010 offering to extend the deed for a further two years. Sea-Cat responded, advising that it wished *“to forego the possibility of extending the current 8 year term, and would prefer to bid for a new contract to commence in January 2012”*. As a result a process was initiated that was intended to culminate in the award of a contract to an operator to provide a ferry service beyond 2011.

Mandorah Ferry Community Reference Group

A Mandorah Ferry Community Reference Group (Reference Group) was appointed by the Minister for Transport early in 2011 to consult with ferry users, business operators and the local Mandorah and Belyuen communities, with the objective of ascertaining the communities' priorities in relation to the timing and frequency of future ferry services.

The Chair of the Reference Group was the then Member for Daly.

An officer of DLP was the secretary to the Reference Group and that officer was also the chair of the tender assessment panel.

Department of Lands and Planning cont...

The Mandorah residents' concerns about the ferry service and their expectations about future services, as expressed to the Reference Group, related to:

- ticketing options / types of tickets
- ticketing technology (e.g. availability of EFTPOS, smart cards, etc.)
- ferry schedules (e.g. providing additional services)
- carriage of bicycles
- security (e.g. installation of CCTV cameras in the ferry, at the Darwin terminal and the Mandorah Jetty).

The First Request for Tenders (Request for Tender No. D11-0196)

A draft tender document was considered by a DLP steering committee in June 2011 at which point approval was given to proceed with the issue of a Request for Tender (RFT) having a response deadline of 10 August 2011. Two firms, Sea-Cat and Fast Ferries Pty Ltd (Fast Ferries) responded to the RFT, with the response from Sea-Cat being received by the time of closing of the tenders while that of Fast Ferries, which was submitted electronically, was not received by the appointed time because of technical issues and was rejected accordingly. Fast Ferries appealed unsuccessfully to the Procurement Review Board against the rejection of its tender. Subsequently, the tender assessment panel identified that the RFT was deficient which resulted in the steering committee instructing that an "Approval to Decline All Tenders" be issued, and that the tender specifications be amended and re-issued as part of a new RFT.

Department of Lands and Planning cont...

The Second Request for Tenders (Request for Tender No. D11-0326)

The second RFT, which included certain fare and ticketing options omitted from the first, was issued with a response deadline of 14 September 2011.

A review of the second RFT suggests that most of the issues raised by ferry users were addressed in that:

- ticketing options / types of tickets were included as part of the second RFT where they were not fully addressed in the first RFT;
- ferry schedules and the provision of additional ferry services were addressed comprehensively in the second RFT. Three different schedules were provided as options;
- the carriage of bicycles was addressed and noted within the vessel specification section; and
- security or the installation of CCTV cameras in the ferry and the jetties was addressed and noted within the vessel specification section.

Tender Assessment and Negotiations with Tenderers

The same two firms, Sea-Cat and Fast Ferries, responded to the second RFT.

There is no evidence to suggest that the tenders were not assessed properly and in accordance with processes set out within Procurement Guidelines. However, the brevity of the tender assessment panel's minutes do deserve some comment. Those minutes are brief and do not appear to reflect the tenor of discussion by the tender assessment panel. In the absence of detail in the panel's minutes, an insight into its deliberations could only be acquired by review of e-mails exchanged between panel members and of the contents of business papers submitted by DLP to the Procurement Review Board (PRB).

The tender assessment resulted in a marginal difference in scores awarded to the two tenderers against the non-financial assessment criteria, with the scoring favouring Fast Ferries.

Department of Lands and Planning cont...

Due diligence visits to Fast Ferries and Sea-Cat were approved by the steering committee and conducted by selected members of the tender assessment panel. The purpose of the visits was to clarify aspects of the tender proposals and to obtain information additional to that provided in the respective tender submissions. The process of seeking further information was consistent with the provisions of the RFT which allowed tenderers to provide additional information to demonstrate to the satisfaction of the assessment panel that tenderers had the capacity to provide the services that were sought.

With regards to the vessels that were proposed to be used, neither of the tenderers offered vessels that complied with the specifications set out in the RFT. However, the tender assessment panel noted that Fast Ferries had a vessel under construction that would comply with specifications, and which was scheduled to be launched, commissioned and positioned in Darwin by April 2012. For the period from 1 January 2012 until the arrival of the new vessel in Darwin, Fast Ferries was to rely upon a chartered vessel. DLP was aware of the risk that accompanied reliance upon the back-up vessel proposed by Fast Ferries as that vessel would require further certification to ensure that it was suitable for the Darwin to Mandorah service. Fast Ferries was confident that certification or the provision of an alternative appropriately surveyed vessel could be achieved.

In the case of Sea-Cat, the tender assessment panel noted that neither of the company's existing vessels complied with the tender specification. While the company advised that one vessel would be upgraded, commencing in April 2012, that upgrade was likely to be limited to engine replacement, and installation of CCTV and Public Address systems. It would not include installation of air-conditioning and other refurbishments. The company advised that it may commission a new vessel in 2013. Sea-Cat also advised that it agreed to the benchmarking of services, but reserved the right to withdraw if it felt that its commercial interests were compromised as a result of benchmarking processes and outcomes.

Department of Lands and Planning cont...

Although the difference between numerical evaluation scores allocated to each tenderer was not great, the committee concluded that Fast Ferries had proposed a better overall service to the public than that proposed by Sea-Cat. Sea-Cat's proposal did not deal satisfactorily with service innovation and was predicated on the operation of the company's existing vessels notwithstanding that the vessels did not comply with the specifications set out in the RFT. In addition, where the tender had required that tenderers submit proposals for ticketing innovations, Sea-Cat proposed the continued use of cash-only payments and ticketing service until a possible upgrade in mid-2012.

Fast Ferries Wins and Loses Preferred Tenderer Status

Following the conclusion of the tender evaluation process, Fast Ferries was recommended to the Procurement Review Board as the preferred tenderer in late-October 2011 and DLP immediately advised Fast Ferries in writing of the company's preferred tenderer status.

However, in mid-November 2011, DLP again wrote to the company to advise that preferred tenderer status had been withdrawn and that negotiations were being terminated. The DLP's decision to shift its preferred tenderer status from Fast Ferries to Sea-Cat is unusual, but the reasons can be summarised in DLP's own words:

"The evaluation of tenders received determined that both Seacat Ferries & Charters Pty Ltd and Fast Ferries were ultimately capable of providing the required ferry services. It should be noted that whilst both companies have been deemed capable, both tenderers failed to provide vessels that are compliant to the RFT specifications, however the evaluation team assessed the risk regarding the quality and safety of the vessels proposed by each tenderer. It should be noted that the non-compliance issues are not broadly comparable.

The evaluation concluded that on balance, Fast Ferries Pty Ltd. proposed a marginally better overall service to the public than that proposed by Seacat Ferries and Charters.

....

Fast Ferries Pty Ltd scored higher than Seacat Ferries and Charters Pty Ltd in non-price evaluation criteria and proposed a lower ferry fare schedule on average.

Department of Lands and Planning cont...

During the evaluation process, it was determined that certain components of the Fast Ferries represented potential risks in their proposed delivery of services. These risks go to the provision and delivery to Darwin in a timely manner, of compliant primary and secondary ferry vessels to provide the services on a temporary basis until their new compliant vessel currently under construction is commissioned in Q2 2012.

Following a tender evaluation process, Procurement Review Board approved on 17 October 2011 the department entering into negotiations with Fast Ferries Pty Ltd, as the preferred tenderer and the tender from Seacat Ferries and Charters Pty Ltd was placed in reserve.

Negotiations have been undertaken in good faith with Fast Ferries Pty Ltd and have now been concluded. Based on advice provided to me I have formed the view that the risks identified in the Fast Ferries Pty Ltd proposal relating to the availability and timely shipment of the primary and backup vessels to the NT have not been addressed to the extent that I am satisfied that satisfactory arrangements can be agreed and settled with the NT in order for the company to meet the commencement date of 1 January 2012.

On that basis I am seeking the Board's approval to return to the tender in reserve and commence negotiations with Seacat Ferries and Charters Pty Ltd. The negotiation focuses on the level of service and structure of future ferry fares of the introduction of the government subsidy."

DLP's *volte face* at a point where the negotiation process was well advanced stemmed from the Department becoming aware that while the tender responses submitted by Fast Ferries identified the vessels that were to be put into service, those vessels were to be replaced with two different vessels. Both the substitute vessels were to be acquired from third parties, with the third parties having fixed and floating charges registered over their assets by financiers. Thus from DLP's perspective, the risks associated with use of Fast Ferries had increased significantly in a short period of time and that, when considered in conjunction with ongoing concerns about the ability of Fast Ferries to position its vessels in Darwin in time to commence services on 1 January 2012, led to a somewhat rapid change in position.

Department of Lands and Planning cont...

As a result of these events the PRB approved the commencement of negotiations between DLP and Sea-Cat and by early December 2011 Sea-Cat was asked to provide its best and final offer. The subsidy sought by Sea-Cat was judged by DLP to be unreasonable when compared with the subsidy paid under the concession deed. The amount sought by Sea-Cat ranged from an increase of 33 per cent for a service level that was less than that provided previously to an increase of 125 per cent for full compliance with the level of services specified in the tender documents. This was substantially more than that sought by Fast Ferries for the provision of a fully compliant service.

Given that acceptance of Sea-Cat's tender would have required the payment of a subsidy that might be seen as excessive in the circumstances, the PRB approved, in early December 2011, DLP's request to decline all tenders and to offer Sea-Cat a two year extension to the concession deed on the terms and conditions that prevailed at the time. Sea-Cat declined that offer on the grounds that any agreement that was for a period of less than eight years was not commercially viable.

The decline by Sea-Cat of the offer of an extension to the concession deed left DLP in a position where, with less than three weeks remaining until the expiry of the deed, the continuation of a ferry service between Darwin and Mandorah was not assured. As a result DLP negotiated and entered into a funding agreement with Fast Ferries under which Fast Ferries agreed to transport Cox Peninsula school students, and residents over the age of 60 years, free of charge and to operate a service under specified conditions in return for an agreed annual fee.

The use of a funding agreement represented a shift from the position adopted at the commencement of the tender process where the arrangement was viewed as one where DLP would acquire services as part of its objective of providing transport systems to one where financial assistance by way of a subsidy would be provided to a private operator for the purpose of enabling designated residents of Cox Peninsula to travel free of charge. In effect, the result is similar to that which prevailed under the previous concession deed.

Department of Lands and Planning cont...

Internal and External Reviews Conducted

Following the conclusion of negotiations and the execution of the funding agreement with Fast Ferries, the DLP initiated two reviews; one by a senior DLP officer to examine the tendering and assessment process and the other by an external consultant to examine concerns that had been raised by one of the tenderers.

Internal Procurement Conduct Review

The first report, noted that:

- advice provided to the tender assessment committee during the procurement activity was process focused;
- due process was followed;
- delegated approval to seek tenders was appropriately given; and
- project team, steering committee and tender assessment teams were comprised of appropriately skilled Northern Territory Government officers.

The report concluded that administration throughout the process could have been improved through better record keeping in respect of meetings, and by demonstrating that the minutes of meetings were circulated, that decisions and dissenting views recorded, that issues raised were addressed and resolved, that actions assigned to team members were recorded, and that a formal record of members' agreement that minutes represented a true record of meeting discussions and decisions be made.

The review also found that documents that emanated from the assessment process indicated that due process was prominent in the committee's deliberations and that each member of the assessment panel had the opportunity to raise issues and potential concerns.

Department of Lands and Planning cont...

External Procurement Process Investigation

The objective of the second review was to examine the procurement process in relation to the second RFT. The catalyst for this investigation was a complaint made by Fast Ferries regarding the withdrawal of its preferred tender status without providing an opportunity to challenge that decision.

The report concluded that, in almost all areas, the tender assessment process was conducted in full compliance with the NT Procurement Framework. The author of the report opined that the areas of probity planning and conflict of interest were well managed, but put the view that the maintenance of minutes of meetings and some elements of record keeping could have been improved.

The report also included some recommendations for amendments to the NT Procurement Framework to assist in improving the procurement processes.

Audit Observations and Conclusions

As indicated above, there was no evidence of a failure to comply with the requirements of Procurement Directions that are issued pursuant to the *Procurement Act*.

While I do not disagree with the findings or conclusions of either of the reports commissioned by DLP in the wake of the execution of the funding agreement with Fast Ferries, I formed the opinion at the conclusion of my review that the level of planning that might have been expected was not adequate. While I understand that potential risks were considered prior to the commencement of the tendering process, that work appears to have been overlooked by both the steering committee and the tender assessment panel. It is notable that a probity auditor was not appointed in this case and that a probity plan was not put into place until the assessment was well advanced.

Department of Lands and Planning cont...

It is not difficult to form a view that DLP delayed too long before commencing the tendering process and that delay may reflect insufficient attention being given to planning for the continuation of service following the expiry of the previous concession deed. That deed was due to expire on 31 December 2011 and Sea-Cat advised in December 2010 that it did not wish to have the deed of concession extended, but preferred to bid for a new contract. It was not until August 2011 that an RFT was issued, leaving only four months for tendering, assessment, negotiation and the award of a contract. It transpired that the RFT was deficient which led to a second RFT being issued in September 2011, further reducing the time for the DLP to manage the project successfully. The decision to embark on a consultation process with residents of Mandorah may not have assisted in this regard as it may have delayed the finalisation of tender specifications by up to twelve weeks.

The Department also appeared to overlook the objective of the exercise. It is possible to draw a distinction between the procurement of supplies in circumstances where the Department or the Government as whole will be the end user of those services, and the provision of funding to enable an external organization to provide services to the community and where members of the community will be the end users. The former requires adherence to the provisions of the *Procurement Act*, the latter may be dealt with by way of a funding arrangement.

Finally, while DLP had staff with appropriate skills and experience who could have provided advice on technical procurement matters to the steering committee and tender assessment panel, those staff were not utilised to any meaningful extent. Instead the Department elected to have an officer seconded from another Agency for the duration of the tendering and assessment exercise to deal with these matters. With hindsight, that approach proved to be ineffective.

Department of Lands and Planning cont...

The Department of Transport, on behalf of the former Department of Lands and Planning, has commented:

I am advised that the procurement of Ferry Services for Mandorah to Darwin presented the former Department with a range of complex challenges. Completion of the process required the achievement of timeliness of process while at the same time delivering of an outcome which balanced the aspirations of community, the creation of value for government and provided a reasonable return for a commercial provider. It is acknowledged that a procurement of this nature is infrequent and tested the capacity of staff.

As your report notes, while the process complied with the requirements of Procurement Directions, and by extension the provisions of the Procurement Act, there were important lessons to be learned. The Department acknowledges the shortcomings in process and planning noted in your report and has taken steps to tighten its procedures to avoid a reputation of these issues in future procurements. In addition, a Senior Contracts Officer has been appointed to provide a single point of reference in complex contract and procurement administration within the Department.

Response by Sea-Cat Ferries & Charters Pty Ltd:

Although the preliminary enquiry by the Auditor General has found that the DLP acted within the NTG procurement rules and guidelines during the assessment and conclusion of the tender for the Mandorah ferry service - Sea-Cat Ferries disagrees that the Department handled the situation well and we have strong criticism of the tender process and of the fact that all major decisions were left until the last moment, - some important costing was left to within a few weeks before the commencement of the new contract.

When the Mandorah Ferry Committee was created early in 2011 to discuss with the community aspects of the ferry service, we were somewhat concerned because the meetings were being chaired by a Government minister who was the member for Daly, and who lived at Mandorah, and who had already voiced his opposition to Sea-Cat Ferries obtaining the new ferry contract again. We believed these meetings and the decision to nominate Sydney company Fast Ferries as the preferred tenderer were influenced by this minister's interference and the fact that his secretary at the ferry meetings was also the Chairman of the DLP assessment panel.

Department of Lands and Planning cont...

Response by Sea-Cat Ferries & Charters Pty Ltd cont...

FIRST TENDER REQUEST

Following the closing date of the (first) tender, NTG Procurement advertised on their web site that only two tenders were received – Sea-Cat Ferries & Charters Pty, Ltd., and Fast Ferries Pty Ltd. Three weeks later Sea-Cat was informed by the head of procurement that the PRB had decided to “decline all tenders” and re-advertise the tender.

Sea-Cat were astonished at this and asked why, - and were told that there were certain safety issues that Sea-Cat had brought up that should have been clarified. When questioned further, the DLP said one of the main issues that we had alerted them to, was that it was not safe to use a gang-plank on the jetty. We protested that such a minor detail as this, and others like it, could easily be sorted out simply as amendments to the original specifications, and that the process was already quite late.

DLP were adamant, and repeatedly insisted that the tender was to be re-advertised.

Weeks later we found out by accident that the only other tenderer, Fast Ferries, had failed to submit their tender on time, - because it was late it had been rejected.

It appeared obvious that this plan to cancel and re-advertise the tender was simply a ruse to bring back the Fast Ferries back into the process. The reasons given for declining all tenders appeared inconsequential. Nearly all the additions listed in the Auditor General’s report as reasons for declining all tenders (new ferry schedules, additional services, carriage of bicycles, installation of CCTV cameras etc.) had already been addressed in the first tender. The DLP did embellish the second tender with various minor amendments to definitions of selected fare types, however Sea-Cat believe that the differences listed between the first and second RFT’s are either non-existent or severely overstated. Certainly the safety issues have not been mentioned in the AG’s report.

Department of Lands and Planning cont...

Response by Sea-Cat Ferries & Charters Pty Ltd cont...

THE SECOND TENDER REQUEST

At this time, it seemed unconscionable that the officers of the assessment panel had now read and had access to all our details, proposals, electronic ticketing system, proposed new vessel specifications, safety aspects from the first tender - and then armed with this knowledge three members of the PRB assessment panel flew down to Sydney for three days, to negotiate with the Fast Ferries. PRB's own lawyer warned them that they should not negotiate with a tenderer, but they all flew off to Sydney regardless. During this visit PRB were never shown any vessel that was suitable for the Mandorah ferry, nor did they inspect the proposed "new" ferry (which was not in Sydney) but arrived back with an assortment of photos of ferries all of which were unsuitable. PRB were only promised that there would be a new and much larger ferry ready by April 2012.

We note that in the Auditor General's report, it states that Department officers stated "neither tenderer had vessels that complied with the tender specification, but that the PRB committee concluded that Fast Ferries proposed a better overall service to the public" This is intriguing since Fast Ferries had absolutely no vessels available that were capable of running a ferry service. Fast Ferries had scored better – with no boats. During the tender process, at no time did members of the PRB assessment panel visit Sea-Cat Ferries.

Following the naming of Fast Ferries as the preferred tender, several weeks later, we were told that the PRB had suddenly changed its mind and that they now would like to negotiate with Sea-Cat.

Sea-Cat commenced what could only be described as, (despite our willingness,) uncomfortable negotiations with representatives of DLP and PRB. Furtive meetings were held at many and various locations around the city, often with the location advised only hour beforehand. The representatives from DLP were clearly not happy with the situation they found themselves in.

The DLP's statement that in the AG's report states Sea-Cats proposed a "cash only payment system" is completely untrue. We advised that we were ready to accept credit-card payments by January 1st and in fact we were trialling the machine in December before the completion of the existing contract. What we did say was that the new RFID Smartcard system may be delayed because of the lateness of the tender negotiations. This will be noted in the minutes of the meetings which were being recorded at the time.

Department of Lands and Planning cont...

Response by Sea-Cat Ferries & Charters Pty Ltd cont...

It became clear at these meetings that the requirements detailed in the RFT would now become obsolete, and a whole new raft of extra demands were now listed as essential, among which were a new fare regime, and a lien over the assets of Sea-Cat Ferries.

The Auditor General's report states "The amount sought by Sea-Cat ranged from an increase of 33% for a service level that was less than that provided previously to an increase of 125% for full compliance with the level of services specified in the tender documents" This statement is both untrue and misleading.

Actual subsidy pricing was never any part of any tender submission, and was only discussed during these eleventh hour negotiations. During these negotiations, as should be evidenced by minutes of meetings in early Dec, numerous "extras" were introduced as "new requirements" by DLP.

Namely-

- *Free "Senior" fares for Cox Peninsula residents, the volume of which, DLP advised Sea-Cat was not available and;*
- *50% discount for all other Australian Senior Card holders, of which would represent 30% of annual custom – a further 15% reduction in earnings.*

Neither of these new "extras" were requirements specified in either of the tender documents, and were only demanded later by DLP during final negotiations.

DLP expected Sea-Cat to absorb these losses, an amount which would have exceeded \$300,000.00 annually. Sea-Cat advised this was unacceptable, and was then directed by DLP to provide their best and final offer, accordingly and did so in a document tabled on 6Dec11 [copy provided to the Auditor-General].

Sea-Cat never offered a reduced service level to what was being provided previously; in fact the minimum offer included an extra 156 runs/year, with the best offer providing 416 extra runs/year. Tabled at meeting with DLP 04Dec11 [copy provided to the Auditor-General].

Department of Lands and Planning cont...

Response by Sea-Cat Ferries & Charters Pty Ltd cont...

We had learnt over the 13 years of operating the service that there was a specific cost to be applied for each and every run, and we used a formula that takes into account the large yearly maintenance costs, the extra staff salaries, CPI, wear and tear on the ferries, fuel costs and inevitable fuel price increases, etc. etc. We advised the committee that we would require considerable more subsidy from the NTG to implement these extra services, especially since now 42% of Cox Peninsula residents were going to travel free. We explained that this would severely reduce our current earnings, by approximately \$300,000 per year, and we would be running at a loss in the Wet Season. We suggested that the best and fairest way of achieving this for both parties was to have a "pay by use" arrangement for these new "free" fares, where Sea-Cat would invoice the NTG every month for actual travel for Seniors and children etc. (this information was available daily from our existing electronic ticket machine computer- data recording system which was already in use and working well). We believed this was the only logical way to approach the problem.

Unfortunately the DLP representatives immediately refused this idea and demanded that we only add in a flat dollar rate to the subsidy and somehow estimate the rate of increase in the Senior population for the next 8 years. Unfortunately we had no way of ascertaining how many seniors might be travelling in the future, and did not want to underestimate in regards to future numbers but we were being forced to guess numbers for free travel. In hind-sight with the recent Census data our estimates were quite accurate.

The free travel for seniors together with the loss of revenue of children travelling free, and combined with the request for many extra ferry runs, was the reason our request for subsidy had to be increased substantially, and we offered 4 different proposals the best of which increased the current subsidy by approx. 30%. The Auditor General's report states that the Department has claimed that Sea-Cat asked for an increase of up to 125% in funding. This is incorrect and we cannot see where this figure came from. It would have brought the subsidy to almost \$1. million and is simply not true.

At 5pm on the 9th December 2011, (name deleted) of PRB emailed Sea-Cat advising PRB had chosen to decline all tenders once again, and that a replacement for (name deleted) would be in contact to arrange a meeting to further negotiate on Monday 12th December 2011.

Department of Lands and Planning cont...

Response by Sea-Cat Ferries & Charters Pty Ltd cont...

At the last meeting with Officers of the Dept. of Lands and Planning on Monday 12th December 2011 the only negotiation DLP were prepared to put forward was an extension of the current arrangements for 2 years. We advised DLP that this was totally unacceptable and the meeting ended.

CONCLUSION

Sea-Cat believe that not only was our tender compromised by the bungling of the first tender process and subsequent decision, once armed with our proposal, to decline the first tender then re-issue the second tender, but also by the creation of the new seniors requirements during the final round of negotiations with DLP. This new set of demands dramatically changed the commercial viability of the service, and put Sea-Cat in a financially compromised position with nowhere to turn, thus ensuring the desired outcome for DLP – being able to enter a newly discovered option for them – a funding agreement with preferred option Fast Ferries.

The Department officers did not seem to have an understanding of costs involved with operations, or difficulties in running the ferry service, and they had no understanding of how much loss of income would occur with all the free travel and extra services they asked for. There did not seem to be anyone in DLP or Procurement who had any experience in maritime services, or boats or ferries despite their respective position titles.

The current dire situation with the ferry service was actually identified as a foreseeable risk which DLP have now chosen to ignore.

None of the vessels promised during the tender process have arrived, and the successful company now operating under the new “funding agreement” has now leased a vessel from Queensland. It appears that after 10 months the Mandorah community has been left with a tentative ferry service, and with no guarantee of continuity as there is only one ferry (that is 17 years old) and no equivalent back-up. The current ferry meets very few of the important criteria and safe-guards originally considered essential, - such as adequate seating out of the weather, back-up vessels, smart-card ticketing passes, CCTV cameras, a new Primary vessel, hiring local staff and supporting local companies.

Department of Resources

Performance Indicators within the Annual Report

With the abolition of the Department of Resources as part of the restructure of the General Government Sector in September 2012, specific recommendations made to that Department are now redundant. Nevertheless other Agencies may be able to draw upon those recommendations when considering the development of, and reporting upon, their performance indicators.

Audit Objectives and Scope

The objective of this audit was to assess the adequacy of records supporting the performance information presented by the former Department of Resources (the Department) to the Legislative Assembly in the Department's Annual Report.

The nexus between performance reporting in the Annual Report (2010/11) and Budget paper No.3 (2010/11) was also examined with explanations obtained for performance measures identified in Budget Paper No. 3, but not reported in the Annual Report.

A sample of performance measures were reviewed in detail to ascertain that the supporting documentation was based on robust and verifiable data.

The audit was not directed to forming an opinion on the accuracy of the reports and documentation arising from the compliance audit.

Audit Opinion

Overall, the adequacy of records supporting the performance information presented by the Department's 2010/11 Annual Report was considered to be reasonable.

This audit noted that the Department has a considerable array of performance indicators publicly reported in its published Annual Report. Based on the audit work performed, the following matters were noted:

- Instances of non-compliance with Treasurer's Direction *Framework – Working For Outcomes*.
- Performance indicators lacked evidence of independent review / assessment of the reported information.
- Some performance indicators lacked formal documentation or sufficient evidence to support some of the performance indicators reported.

Department of Resources cont...

Background

Legislative Requirements

Section 28 of the *Public Sector Employment and Management Act* requires the Chief Executive Officer of an Agency to report to the appropriate Minister on the operations of that Agency during a financial year. The report must contain information including the Agency's operations, initiatives and achievements such as those relating to planning, efficiency, effectiveness and performance.

The Treasurers' Direction: Working for Outcomes – Overview sets out the view that, "Working for Outcomes is the Northern Territory Government's financial and performance management framework." One key element of this framework is that "Agency performance in the delivery of outputs is to be measured in relation to the quantity, quality, timeliness and cost of outputs." (Section F2.1.3)

That Direction goes on to state that "Performance measures assist decision makers, both within and outside the Agency, in determining whether Territory resources are being applied in an efficient and effective manner to achieve Government outcomes."

Legislative Requirements – Application to the Department of Resources

While the Treasurer's Annual Financial Statements are audited, the financial statements of the Department are not. The Chief Executive Officer of the Department reports the Department's financial position and its performance in an Annual Report, which includes the performance indicators, to the Minister who, in turn, tables the Annual Report to the Legislative Assembly.

The accuracy of performance measures indicators, reported to the Minister and tabled in the Legislative Assembly is critical as robust information can:

- inform management and users of the Department's performance;
- ensure an adequate standard of accountability by the Department is upheld and maintained;
- be used to guide policy decisions; and
- assist management to make effective decisions to manage results.

Department of Resources cont...

Effective Performance Indicators / Targets

The “SMART” criterion is a commonly used methodology to determine if performance indicators/targets contain a range of characteristics that allow for the effective delivery of outputs.

The following five characteristics of a performance indicator, which are collectively known as the “SMART” criteria, are defined below:

Performance indicator criteria	Description / characteristic	Considerations factors
Specific	Clear and concise to avoid misinterpretation of what is to be achieved.	Does the performance indicator contain jargon or unexplained acronyms? Are the objectives and performance indicator directly related? Could a reasonable person understand the meaning of the performance indicator?
Measureable	Can be quantified and results can be compared to other data and able to show trends if measured over time.	Is the performance indicator able to be measured and be achievable in a timely manner?
Achievable (action-oriented)	Practical, reasonable and credible given available resources and expected conditions.	Is there an action that the people who are being measured by the performance indicator could do to change the end number?
Relevant (or Realistic)	Informative and useful to stakeholders having regard to the content in which the entity operates.	Is the performance indicator based on facts? Is the data collectable?
Time-bound	Specifies a timeframe for achievement and measurement.	Is there are period of measurement (i.e. monthly, quarterly, yearly)?

Department of Resources cont...

Key Findings

In conducting this compliance audit, I formed the view that the adequacy of records supporting the performance information in the Department's 2010/11 Annual Report was reasonable.

I did note that the performance indicators could have been enhanced in terms of usefulness, relevance and effectiveness and I suggested that the Department consider the following additional recommendations in its performance reporting framework:

Alignment between Performance Indicators and the Department of Resources' Objectives / Business Plans

Performance indicators that are established with a clear and direct link to departmental objectives and the department's business plans can improve:

- the usefulness of the information to management;
- accountability;
- governance by monitoring progress; and
- the Agency's ability to be able to promote its achievements in a more convincing manner.

Based on my review of the performance indicators for each business unit reported in the Department's 2010/11 Annual Report, the linkage between some performance indicators and the respective business unit key objectives was indirect or difficult to determine.

Innovative Uses of Performance Indicators and Enhanced Reporting

My review of the performance indicators also noted that a number of performance indicators reported in the 2010/11 Annual Report could be significantly improved in order to improve the quality of information provided to users of the Annual Report.

Department of Resources cont...

The Department should also consider other uses of its performance indicators and further enhance the performance reporting to promote stronger governance and accountability. Such uses and enhancements include:

- benchmarking: publishing the Department's performance against the benchmarks of other like agencies;
- publish performance indicators not currently disclosed in the Annual Report; and
- reported performance indicators with targets not met should be further explained to users, and actions should be identified to address the shortfalls.

Conclusion

My review of the performance indicators noted that many of the Department's performance indicators did not adequately meet the SMART criteria and that some performance indicators:

- Lacked evidence of independent review / assessment of the reported information.
- Lacked formal documentation (sufficient and appropriate evidence in the documentation) to support some of the performance indicators reported in the Annual Report.

Department Resources cont...

The Department of Primary Industry and Fisheries and the Department of Mines and Energy has commented on behalf of the former Department of Resources:

The Auditor-General's findings are acknowledged and noted. The issues had been referred to the Risk Management and Audit Committee of the former Department of Resources and as a matter of priority will be forwarded to the new relevant areas in the new Department of Primary Industry and Fisheries, and the new Department of Mines and Energy. The Department's will develop and implement systems and procedures to strengthen the collection, testing and verification of performance data, and will review the efficacy, consistency and compliance of the performance measures used by both new departments in future budget papers and annual reports.

Menzies School of Health Research

Audit findings and Analysis of the financial statements for the year ended 31 December 2011

Background

The Menzies School of Health Research (the School) is established under the *Menzies School of Health Research Act* in 1985 and operates as a medical research institute within the Northern Territory. The School is deemed to be controlled by Charles Darwin University by virtue of Section 11(1) of the Act which specifies that the Vice-Chancellor and the Deputy Vice-Chancellor (Research) of the University will be *ex officio* members of the School's Board, and through Section 11(2)(d) which specifies that five of the ten persons appointed to the Board by the Administrator are appointed on the nomination of the University.

Audit Opinion

The audit of the financial statements of Menzies School of Health Research for the year ended 31 December 2011 resulted in an unqualified independent audit opinion, which was issued on 9 May 2012.

Key Findings

New Buildings

The School was granted funding by the Commonwealth and Northern Territory Governments for the purpose of constructing research and training facilities at the Charles Darwin University (CDU) and Royal Darwin Hospital (RDH) sites. The total estimated costs of this project were \$47.2 million.

At the time of the audit the project was in abeyance due to a change in scope of the project pending Commonwealth approval of the revised scope. If that approval had not been forthcoming the funds received by the School to date (approx. \$13.6 million) may have been repayable to the Commonwealth and Northern Territory Governments. The Commonwealth has since approved the revised scope.

It is my understanding that the School intends to transfer ownership of the buildings to the Northern Territory and to CDU respectively upon completion of the works, with the School occupying the buildings for nominal rent thereafter.

Menzies School of Health Research cont...

At 31 December 2011, costs of approximately \$2.2 million relating to survey, architecture and project management expenses had been incurred on the project.

My interpretation of the funding agreement that the School entered into with the Commonwealth Government suggested that no further funds will be forthcoming from that source if the overall project cost should increase beyond the original estimate. Given the delays to date and the possibility that the School may find that this project is required to compete for resources against other significant construction projects that have commenced in the Darwin area, I am concerned that the final project costs may rise above the amount advised to the funding bodies.

Financial Performance for the year

	2011	2010
	\$'000	\$'000
Revenue from continuing operations	37,934	37,342
Less expenses from ordinary activities		
Employee Expenses	(22,383)	(20,895)
Administration, operational and other expenses	(11,762)	(11,668)
Total expenses from ordinary activities	(34,145)	(32,563)
Net operating result for the year	3,789	4,779

There was little change in the School's total revenue from the prior year, with \$37.3 million being recognised in 2010 compared to \$37.9 million in 2011. The School's operating expenditure increased from \$32.6 million in 2010 to \$34.1 million in 2011, mainly due to an increase in employee related expenses of \$1.5 million as a result of higher employee numbers associated with new projects in 2011.

Flowing from the revenues and expenses outlined above, the School achieved an operating surplus of \$3.8 million for the year.

Menzies School of Health Research cont...

Financial Position at year end	2011	2010
	\$'000	\$'000
Current Assets	44,037	41,201
Less Current Liabilities	(4,121)	(3,030)
Working Capital	39,916	38,171
Add Non Current Assets	3,113	876
	43,029	39,047
Less Non Current Liabilities	(414)	(218)
Net Assets	42,615	38,829
Represented by:		
Retained earnings	15,319	3,476
Reserves	27,296	35,353
Equity	42,615	38,829

Northern Territory Police, Fire and Emergency Services

Calibration of speed detection devices and breath testing equipment

Background

Representations were made to me by a member of the Legislative Assembly on in August 2011 requesting “a full audit of records of calibrating procedures for all radar, red light camera, alcohol and drug testing systems...”

The request followed the reporting of the outcome of a court case involving a Mr Braddy who had a speeding fine overturned on the basis that no evidence was submitted to the court to rebut the claim that mobile speed cameras in the Northern Territory may not be accurate.

As a result of the representations and in the light of the general concerns being expressed at the time I decided to conduct an audit of the Northern Territory Police, Fire and Emergency Services (NTPFES) systems with regard to the calibration of speed detection and breath testing equipment. Red light cameras were not included as part of the review as that equipment is maintained by a private sector operator on behalf of another Northern Territory Government agency. I also elected not to review drug testing systems as the current process does not require calibration and re-verification by the Communications and Electronic Services Section (CESS).

I noted that an informal review of the internal controls and processes of the NTPFES to effectively manage, maintain, use and store evidential breath analysis instruments, MPH BEE111 automatic same direction traffic radar and MPH Ultralyte Laser speed detection instruments was completed by the Risk Planning Division within the Agency in November 2011.

I also noted that an assessment by the NSW Police Force of the laboratory standards and quality assurance methods at the NTPFES calibration laboratory was completed in October 2011.

Northern Territory Police, Fire and Emergency Services cont...

Audit Objectives and Scope

The objective of the audit was to determine the extent to which performance management systems of NTPFES enable management to assess whether its objectives in relation to the use of speed detection and breath testing equipment are being achieved effectively, and with regard to efficiency and economy.

The audit concentrated specifically on the 'effectiveness' of the use of the equipment and particularly on how the Department ensures the equipment is fit for purpose.

Fit for purpose includes ensuring the equipment satisfies the requirements of relevant legislation, the courts and police operational needs. It also includes ensuring the equipment is safe to use.

In the context of performance auditing, the following definitions of these characteristics are generally accepted:

- "Effectiveness" means the achievement of the objectives or other intended effects of activities;
- "Efficiency" means the use of financial, human, physical and information resources such that output is maximised for any given set of resource inputs, or input is minimised for any given quantity and quality of output;
- "Economy" means the acquisition of the appropriate quality and quantity of financial, human, physical and information resources at the appropriate times and at the lowest cost.

Audit Opinion

In my opinion the Agency's systems to ensure that speed detection and breath testing equipment is fit for purpose are adequate. However, there are several areas where improvements should be made.

In particular, there was a material absence of documented policies and procedures to provide guidance to staff and support the operations of the CESS. This places undue reliance on the expertise of the technical staff within the section to ensure proper procedures are followed.

Northern Territory Police, Fire and Emergency Services cont...

Key Findings

Lack of documented policy and procedures

Both the NSW Police Force review and the NTPFES' own internal review identified a lack of formalised documentation.

The NSW Police Force review, while assessing technical management as being satisfactory, noted a failure on the part of the laboratory to document and implement a quality system. The review contains numerous comments of *“Unable to be assessed as no document exists. Laboratory needs to develop quality and procedural manuals.”* Importantly, the assessment of the laboratory's test and calibration methods and method validation was favourable. The report commented: *“Testing procedures appear to be adequate as they follow the manufacturer's recommended test procedures. The documentation of these procedures needs to be implemented by way of a separate quality manual for each type of device.”*

The Agency internal review which drew upon the outcome of the NSW Police Force review as well as direct enquires with NTPFES personnel and external parties (Victoria Police Laboratory manager and National Measurement Institute) also highlights the *“absence of quality manual system and any written standard operating procedures for technicians across all apparatus.”*

My audit also confirmed the lack of documented policies and procedures. During the course of the audit a draft 'Communications and Electronic Services Section - Calibration Laboratory Management Manual' was brought to my attention. It is my understanding that the manual is, or will be, based on a similar Queensland Police Force manual and that the first sections of the manual were issued in August and December 2011. I was advised that the drafting of the procedure manuals was proving to be a complicated and time consuming process.

Notwithstanding, the lack of documented policies and procedures for the calibration of speed detection and breath testing equipment continues to be a risk that the NTPFES needs to address.

Northern Territory Police, Fire and Emergency Services cont...

Recording of calibration and testing data

The Braddy case identified weaknesses in the recording of calibration and testing data within an Access database for the device in question. The procedure then in use required the direct input of test data into the database with no separate hand written or printed test sheet being retained. It is my understanding that errors in data recording resulted in the Crown withdrawing the charges laid against Mr Braddy. I note that the device in question was sent to the University of Tasmania for independent testing and that the results of that testing indicated that the equipment was operating within the prescribed parameters.

Since then, new procedures for the recording of test data and/or certification of Speed Detection and Breath Testing Equipment have been introduced. The inventory module within the Agency's asset management system was progressively phased in for each unit as that unit was returned to the CESS for certification. My audit reviewed the current procedures for each equipment type and the findings are discussed further, below.

Ultra Lyte – LTI 2020 100LR Laser speed gun

An excel spread sheet was provided to audit that listed 60 units.

For a sample of units, the documentation to support the most recent certification was reviewed. In all cases the documentation reviewed confirmed that the 100LR laser speed guns are being tested for accuracy and certified in accordance with Northern Territory Government approvals and the operational requirements for the units.

It was confirmed that a separate file is being maintained for each unit in which a signed copy of the certificate of accuracy of a traffic infringement detection advice and a signed copy of the test sheet are kept.

Whilst the current filing system may not be in accord with the NTPFES record keeping policy in that neither the files nor their contents are recorded in TRIM, the records do provide adequate evidence to support NTPFES' assertion that the 100LR laser speed guns were being properly maintained.

Northern Territory Police, Fire and Emergency Services cont...

BEEIII radar unit

An Excel spreadsheet that listed 60 units was provided to me.

The documentation reviewed confirmed that BEEIII radar units were being tested for accuracy and certified in accordance with Northern Territory Government approvals and the operational requirements for the units.

The record keeping procedures that were noted for the BEEIII radar units were the same as that used for the 100LR laser speed guns and the same audit conclusion applies.

A number of technicians within NTPFES who were initially Gazetted as approved to test the accuracy of the units were undergoing refresher training at the time of the audit.

Draeger 7110 MKv Evidential Breath Analyser (EBA)

An Excel spreadsheet that listed 99 units was provided to me.

Prior to August 2011, EBA calibration and certification was undertaken "in-house" within CESS. In 2005 the national standard required a change from %BAC (blood alcohol content) to BrAC (Breath alcohol content). Along with this change was a requirement for the testing laboratory to be accredited. A grandfathering clause was subsequently extended to 31 July 2012 allowing jurisdictions to continue with %BAC.

Under a new contract with the manufacturer that was entered into in August 2011, calibration (annually) and re-verification (6 monthly) is to be conducted by Draeger. These tasks are currently completed by Draeger in Melbourne. While Draeger is accredited it does not currently hold accreditation for the 7110 MKv which necessitates the units being sent to Victoria Police for certification. Correspondence provided to me during the course of the audit indicates that Draeger was seeking appropriate accreditation and is also seeking to extend this accreditation to a Darwin facility. The provision of an appropriately accredited facility in Darwin is a specific requirement of the contract with the NTPFES. Until this occurs the double handling of the EBAs extends the turnaround time for calibration and verification and extends the length of time an EBA is out of service.

Northern Territory Police, Fire and Emergency Services cont...

Documents reviewed during the course of the audit indicate that Draeger may not be achieving the required 10 working day turnaround that is specified in the contract and it would also appear that the time taken to return equipment from police stations to CESS is excessive. CESS, by reference to its records, identifies EBAs requiring calibration or re-verification and forwards a replacement unit to the station in question at which point the station is required to return the unit requiring calibration or re-verification to CESS. It would seem that significant delays can occur between the issue of replacement units by CESS and the receipt from police stations of the unit requiring testing. This may pose some risks in terms of the total number of units required to meet NTPFES' requirements and the possibility that uncalibrated units may be used unwittingly. At the time of the audit CESS was testing a software update that would automatically shut down an EBA when the 6 month limit is reached. If implemented that might be expected to overcome the risk of inappropriate use of an uncalibrated unit.

It was confirmed that a separate file holding all certification documentation received from Victoria Police was being maintained for each unit.

Alcolizer LE

An Excel spreadsheet that listed 215 units was provided to me.

To maintain the standard of accuracy required of a police force, the Australian Standards Certification requires recalibration of Alcolizer units each 6 months and each unit is fitted with an automatic shut down mechanism.

These devices are used to identify drivers suspected of driving under the influence of alcohol. A reading in excess of 0.05 allows a police officer to require a driver to provide a sample of breath which is analysed on the Draeger EBA. It is the Draeger reading that is used to support a prosecution before the Courts.

For a sample of units, the job cards, as recorded in the database, were reviewed to confirm that the units were being recalibrated in accordance with their operational requirements. As the process was considered satisfactory and as there is no Court reliance on the Alcolizer, no further review in respect of this class of devices was considered necessary.

Northern Territory Police, Fire and Emergency Services cont...

The Northern Territory Police, Fire and Emergency Services has commented:

The lack of documented policies and procedures for the Calibration of Speed Detection and Breath Testing Equipment continues to be a risk that the agency needs to address

While the procedures for calibration are appropriate, work continues in relation to the preparation of a Quality Manual. There is still a significant amount of work to be done, as it is estimated that over 50 or more documents will need to be created, drafted, modified, validated and approved. Once complete, the Quality Manual is likely to require review by an external party to ensure it conforms to National Association of Testing Authorities (NATA) standards. Achieving NATA accreditation for the Communications and Electronic Services Laboratory is a medium term goal for the agency. This will ensure ongoing high standards and quality assurance are maintained for all devices requiring calibration and servicing.

Inefficient use of Evidential Breath Analysers (EBAs)

Turnaround times for EBA calibration have drastically reduced as the agency's contractor has received NATA accreditation and is now undertaking calibration work in Darwin. The process and timing of police stations returning units for calibration or re-verification continues to improve following the implementation of new procedures.

The Information and Communication Technology (ICT) risk register does not specifically address the risks associated with Speed Detection and Breath Testing Equipment

All ICT staff, including contractors, have completed risk training. The ICT Branch risk register was updated to highlight the risks associated with Speed Detection and Breath Testing Equipment. The register is reviewed on a regular basis to ensure its currency.

Office of the Commissioner for Public Employment

Project Employment Scheme

Review Objectives and Scope

The objective of the review was to assess the adequacy of the Office of the Commissioner for Public Employment's (OCPE) performance management systems to enable it to assess the effectiveness, efficiency and economy of its operations in relation to the "*Project Employment Scheme*" that was established as part of the Willing and Able strategy.

Review Opinion

In my opinion, the Office of the Commissioner for Public Employment had not established a performance management system that enabled it to assess the effectiveness, efficiency and economy of its operations in relation to the "*Project Employment Scheme*".

Background

The "*Project Employment Scheme*" is an employment program for people with disabilities who may not otherwise be competitive in obtaining a position on the basis of merit. It is funded by way of an annual levy on all Agencies. The funds raised are managed by the OCPE and are used to reimburse the direct wage costs to agencies for the employment of people with intellectual and/or learning disabilities.

In 2004 the "*Project Employment Scheme*" ran concurrently with the separate "*Willing and Able Strategy*". During 2008 and 2009 financial years the "*Project Employment Scheme*" and the "*Willing and Able Strategy*" were merged into the one reporting item referred to as "*Willing and Able*" – sometimes also referred to as the "*Willing and Able Wage Assistance Scheme*".

2010 saw an increase in financial reporting with income of \$0.349 million being reported as the "*Project Employment Scheme*" under the "*Willing and Able*" banner. It appears that in 2010 the "*Project Employment Scheme*" had now become a subset of, or replaced, the "*Willing and Able Strategy*" with the Scheme providing all funding for "*Willing and Able*".

In 2011 the Scheme was again reported under the heading of "*Willing and Able*" with the income being reported as \$0.335 million. In 2012 the Scheme received income of \$0.349 million.

Office of the Commissioner for Public Employment cont...

Finances

A summary of the income and expenditure relating to the “*Project Employment Scheme*” is provided below.

	2007 \$,000's	2008 \$,000's	2009 \$,000's	2010 \$,000's	2011 \$,000's	2012 \$,000's
Income – per annual report	350 ^(a)	349 ^(a)	349	349	335	349
Expenditure ^(b)						
Salary	153	169	151	144	189	262
Disability Works Australia	45	28	67	-	-	-
Non-salary related	77	-	33	16	-	-
	275	197	251	160	189	262
Unexpended levy	75	152	98	189	146	87

(a) The Scheme income was not separately disclosed within the annual report.

(b) Expenditure is not separately disclosed within the annual report therefore data from OCPE files was used to prepare the expenditure comparisons.

Key Findings

The program is in place to foster “*Social Outcomes*” and there were no measures identified at the time of the review that could be considered measures of economy, efficiency or effectiveness.

Whilst OCPE monitored actions in relation to the “*Project Employment Scheme*” it was not able to monitor outcomes or outputs and OCPE was unable to ascertain whether, or not, the jobs funded under the scheme were new positions or existing vacant positions.

Office of the Commissioner for Public Employment cont...

Conclusion

There were no performance management systems in place to enable OCPE to assess the effectiveness, efficiency and economy of its operations in relation to the “*Project Employment Scheme*”.

While the scheme is relatively small, it does, nevertheless, highlight the importance of being able to demonstrate, through the use of appropriate performance measures, whether it is achieving the outcomes that were envisaged at the time of its establishment.

The Office of the Commissioner for Public Employment has commented:

OCPE acknowledges that a comprehensive performance management plan is not in place to fully assess the effectiveness, efficiency and economy of the Project Employment Scheme, however, the scheme is currently being reviewed under the overarching Willing and Able Strategy, and better ways to report on outcomes will be considered as part of that review.

The Project Employment Scheme has been in existence since 1994 with 63 people having the opportunity to work in the NTPS and acquire new skills and knowledge to enable them to compete for positions on merit. Of those, 27 people gained permanent employment in the NTPS. In this regard it is considered a successful program in terms of employment outcomes.

Selected Agencies

Agency Compliance Audits

Audit Objectives and Scope

Agency compliance audits are intended to ascertain the extent to which Agencies' Accountable Officers have implemented and maintained procedures that assist in ensuring that the requirements set out in Acts of Parliament, and subordinate and delegated legislation, are adhered to.

Background

The use of delegated legislation, for example Treasurer's Directions and Procurement Directions, devolve responsibility to Accountable Officers of line Agencies. That devolution has an accompanying requirement for accountability by Accountable Officers to their Ministers. Compliance audits are intended to assess how well that accountability is being discharged. The audits for this period concentrated on the extent to which Agencies had complied with promulgated requirements with respect to:

- the maintenance of registers of financial interests, contingencies, guarantees and indemnities;
- validation of accounts payable and claims for payment, including funds availability;
- compliance with the *Procurement Act*, Regulations made under that Act and Procurement Directions;
- the maintenance of registers of losses, and whether investigation, and reporting and recovery of losses accorded with the requirements of Treasurer's Directions;
- ensuring that expenditure on official travel, telephones and hospitality was properly authorised, recorded and acquitted;
- the recording and accounting for trust monies;
- the legal and statutory arrangements governing the recovery of certain debts, the retention of financial management records, the granting of ex-gratia payments, and the maintenance of Registers of Fees and Charges;
- the control of physical assets; and
- budget management, including financial and performance reporting.

Selected Agencies cont...

Audits were performed in each of the following Agencies during the six months covered by this report:

- Department of Children and Families;
- Department of Education and Training;
- Department of Health;
- Department of Housing, Local Government and Regional Services;
- Department of Justice;
- Department of Lands and Planning;
- Northern Territory Electoral Commission;
- Northern Territory Police, Fire and Emergency Services; and
- Office of the Commissioner for Public Employment.

Key Findings

A number of issues were raised as a result of the audits including:

- lack of compliance with Procurement Directions, and procurement policies;
- weaknesses in the reconciliation of Accountable Officers' Trust Accounts;
- lack of compliance with Treasurers' Directions, particularly in relation to controls over hospitality and travel expenditure;
- deficiencies in controls over fixed assets; and
- weakness in internal audit procedures.

Selected Agencies cont...

The Department of The Attorney-General and Justice has commented, on behalf of the former Department of Justice:

The audit findings and recommendations are acknowledged and the Agency is taking remedial action where required.

The Department of Correctional Services has commented, on behalf of the former Department of Justice:

The audit findings and recommendations are acknowledged and the Agency is taking remedial action where required.

The Department of Housing has commented, on behalf of the former Department of Housing, Local Government and Regional Services:

My department continues to monitor and report on compliance matters include the use of corporate credit cards and has improved internal controls regarding balance sheet reconciliations.

The Department of Local Government has commented, on behalf of the former Department of Housing, Local Government and Regional Services:

My department continues to monitor and report on compliance matters include the use of corporate credit cards and has improved internal controls regarding balance sheet reconciliations.

The Department of Regional Development and Indigenous Advancement has commented, on behalf of the former Department of Housing, Local Government and Regional Services:

My department continues to monitor and report on compliance matters including the use of corporate credit cards and hospitality and travel expenditure.

Selected Agencies

Credit Card Expenditure by Agencies

Audit Objective

The objective of this audit was to examine selected credit card transactions across several agencies with a view to ascertaining the extent to which the transactions complied with prescribed requirements and the extent to which those transactions were considered reasonable in the circumstances.

Background

The Northern Territory Government has used a corporate credit card to facilitate expenditure for lower value transactions for a number of years. The cards were issued by the Westpac Banking Corporation and, more recently, by the National Australia Bank.

The Treasurer has issued a Direction pursuant to the *Financial Management Act* setting out the nature of purchases that may be made using cards and the conditions that attach to the use of the cards. Broadly, Agencies are permitted, as a minimum, to use a Corporate Credit Card for:

- purchases up to or equal to \$500 (GST inclusive);
- official travel and accommodation;
- payments made over the internet or telephone; and
- payments to the Government Printing Office, and the Power and Water Corporation.

Selected Agencies cont...

The extent of the use of the corporate credit card is illustrated in the following table for selected agencies for 2010/11.

	No. Transactions	Total Value \$
Department of Business and Employment	9,846	2,686,621
Department of Children and Families	7,847	1,855,745
Department of Construction and Infrastructure	2,262	837,816
Department of Education and Training	26,286	7,882,981
Department of Health	111,436	28,161,296
Department of Housing, Local Government and Regional Services	9,618	1,892,495
Department of Justice	42,978	13,221,995
Department of Lands and Planning	11,021	2,594,177
Department of Natural Resources, Environment, the Arts and Sport	52,073	7,898,080
Department of Resources	21,253	4,186,056
Northern Territory Police, Fire and Emergency Services	73,114	20,754,178
Tourism NT	20,867	4,291,166
	388,601	96,262,606

The data shown in the table formed the population of transactions for the purposes of the audit from which a sample was selected for closer examination of supporting documentation. The sample size was considered sufficiently large to permit inferences to be made about the population of transactions as a whole, with an acceptable level of confidence.

Selected Agencies cont...

Key Findings

All transactions examined were found to have been properly verified and on that basis they might be said to comply with prescribed requirements.

Where information was sought about the nature of specific transactions and the reasons for those transactions, the information provided was sufficient to provide confidence that the transactions were appropriate.

There was a larger than expected number of transactions with major retailers. A number of those transactions were selected for closer examination and found to be reasonable in the circumstances. However given the number and aggregate value of these transactions for 2010/11, there is a case for Chief Executives to monitor, on an on-going basis, expenses incurred by way of corporate credit cards with a view to satisfying themselves that the expenditure is both reasonable and necessary.

The audit highlighted the importance of ensuring that good physical control is maintained over credit cards and in exercising care when providing card details. The details of two credit cards fell into the hands of unauthorised individuals resulting in transactions that took the form of travel bookings, on-line gambling, and purchases of jewellery being made. At the time of the audit the value of transactions on one of the cards in question had been reversed by the issuing bank, while the bank had been requested to reverse the transactions in the case of the second card.

This audit highlighted the importance of good budgetary control. Cases were noted where individual purchases appeared reasonable and where they were properly verified. However, when the aggregate of those transactions were considered there was a cause for concern. An example concerned the purchase of fuel tags at a remote location where the total number and value of purchases appeared to be excessive when considered in conjunction with the number of vehicles at that location.

Conclusion

The findings noted above are exceptions noted as part of the audit and the conclusion formed was that Agencies were adhering to prescribed requirements and the overall controls over card usage were functioning satisfactorily.

Selected Agencies cont...

The Department of The Attorney-General and Justice has commented, on behalf of the former Department of Justice:

The Agency acknowledges the audit findings and considers that the current processes of central verification of corporate credit card expenses within the Agency is beneficial to ensuring appropriate usage and adherence with prescribed requirements.

The Department of Correctional Services has commented, on behalf of the former Department of Justice:

The Agency acknowledges the audit findings and will investigate opportunities to better monitor expenses incurred by way of corporate credit cards and will maintain good physical controls of corporate credit cards.

The Department of Housing has commented, on behalf of the former Department of Housing, Local Government and Regional Services:

My department continues to monitor and report on compliance matters include the use of corporate credit cards and has improved internal controls regarding balance sheet reconciliations.

The Department of Infrastructure has commented, on behalf of the former Department of Construction and Infrastructure:

Assessments have been made of the nine transactions related to the agency and they were all found to be legitimate purchases and were made in accordance with the Department's corporate policies and procedures.

This Department now has a credit card policy, approved 14 August 2012, that compliments the Dept of Business Credit Card user guides and procedural guidelines. At all times the Department takes measures to ensure that corporate credit cards are used in accordance with the policy, procedures and the Treasurer's Directions.

The Department of Local Government has commented, on behalf of the former Department of Housing, Local Government and Regional Services:

My department continues to monitor and report on compliance matters include the use of corporate credit cards and has improved internal controls regarding balance sheet reconciliations.

Selected Agencies cont...

The Department of Regional Development and Indigenous Advancement has commented, on behalf of the former Department of Housing, Local Government and Regional Services:

My department continues to monitor and report on compliance matters including the use of corporate credit cards and hospitality and travel expenditure.

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Appendices

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Appendix 1: Audit Opinion reports issued since 31 December 2011

Financial Statements for the year ended 31 December 2011

	Date 2011 Financial Statements tabled to Legislative Assembly	Date of Audit report Year ended 31 December 2011	Date of Audit report Year ended 31 December 2010
Batchelor Institute of Indigenous Tertiary Education	Not yet tabled	26 June 12	15 June 11
CDU Amenities Limited	N/A	4 May 12	14 June 11
Charles Darwin University	Not yet tabled	29 May 12	28 June 11
Charles Darwin University Foundation (a company limited by guarantee)	N/A	16 April 12	7 April 11
Charles Darwin University Foundation Trust	N/A	16 April 12	7 April 11
Menzies School of Health Research	N/A	9 May 12	16 May 11

N/A – Not Applicable

Appendix 1: Audit Opinion reports issued since 31 December 2011 cont...

Acquittals or other returns – for the year ended 30 June 2011

	Deadline for submission of Audited Financial Statements	Date of Audit Report Year ended 30 June 2011	Date of Audit Report Year ended 30 June 2010
Charles Darwin University Higher Education Research Data collection	31 August 11	26 June 12	25 May 11

Appendix 2: Status of Audits which were identified to be conducted in the six months to 30 June 2012

In addition to the routine audits, primarily being end of financial year audits of Agencies and of financial statements, and follow-up of outstanding issues in previous audits, the following audits, were identified in Appendix 3 of the February 2012 as being scheduled for the period.

Department of Construction and Infrastructure

Construction works in progress No matters to report

Department of Health

Grants by the Department to NGO's for the delivery of primary health services Refer page 42

Northern Territory Treasury

Treasury web portals No matters to report

NT Police, Fire and Emergency Services

Calibration of speed detection and breath testing equipment Refer page 74

Office of the Commissioner for Public Employment

Project Employment Scheme Refer page 81

Power and Water

Accounts payable data analytics Ongoing

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Appendix 3: Proposed audit activity in the six months ending 31 December 2012

In addition to the routine audits, primarily being end of financial year audits of Agencies and of financial statements, and follow-up of outstanding issues in previous audits the following audits have been scheduled for the period.

Department of Health

Aero Medical Services Contract - Careflight

Department of Housing

National Partnership Agreement on Homelessness

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Appendix 4: Overview of the approach to auditing the Public Account and other accounts

The requirements of the *Audit Act* in relation to Auditing the Public Account and other accounts are found in:

- Section 13, which requires the Auditor-General to audit the Public Account and other accounts, with regard to:
 - the character and effectiveness of internal control, and
 - professional standards and practices.
- Section 25, which requires the Auditor-General to issue a report to the Treasurer on the Treasurer's Annual Financial Statement.

What is the Public Account?

The Public Account is defined in the *Financial Management Act* as:

- the Central Holding Authority, and
- Operating accounts of Agencies and Government Business Divisions.

Audit of the Public Account

Achievement of the requirements of section 13, including the reference to the character and effectiveness of internal control, as defined, can occur through:

- annual financial statement audits of entities defined to be within the Public Account, in particular Government Business Divisions, which have a requirement for such audits under the *Financial Management Act*, and
- an audit approach which the Northern Territory Auditor-General's Office terms the Agency Compliance Audit. This links the existence of the required standards of internal control over the funds administered within the Public Account, to the responsibilities for compliance with required standards as defined for Accountable Officers.

Appendix 4: Overview of the approach to auditing the Public Account and other accounts cont...

Areas of internal control requiring a more in-depth audit, because of materiality or risk, can also be addressed through:

- specific topic audits of the adequacy of compliance with prescribed internal control procedures. These can be initiated as a result of Agency Compliance Audits, or pre-selected because of the materiality or inherent risk of the activity; and
- reviews of the accounting processes used by selected Agencies at the end of the financial year, to detect if any unusual or irregular processes were adopted at that time.

Other accounts

Although not specifically defined in the legislation, these would include financial statements of public entities not defined to be within the Public Account, as well as the Trust Accounts maintained by Agencies.

Audit of the Treasurer's Annual Financial Statement

Using information about the effectiveness of internal control identified in the overall control environment review, Agency Compliance Audits and financial statement audits, an audit approach is designed and implemented to substantiate that balances disclosed in the Statement are in accordance with the disclosure requirements adopted by the Treasurer, and are within acceptable materiality standards.

The audit report on the Statement is issued to the Treasurer. The Treasurer then tables the audited Statement to the Parliament, as a key component of the accountability of the Government to the Parliament.

Appendix 5: Overview of the approach to auditing performance management systems

Legislative Framework

A Chief Executive Officer is responsible to the appropriate Minister under section 23 of the *Public Sector Employment and Management Act* for the proper, efficient and economic administration of his or her agency. Under section 13 (2)(b) of the *Financial Management Act* an Accountable Officer shall ensure that procedures “*in the agency are such as will at all times afford a proper internal control*”. Internal control is further defined in section 3 of the Act to include “*the methods and procedures adopted within an agency to promote operational efficiency, effectiveness and economy*”.

Section 15 of the *Audit Act* complements the legislative requirements imposed on Chief Executive Officers by providing the Auditor-General with the power to audit performance management systems of any agency or other organisation in respect of the accounts of which the Auditor-General is required or permitted by a law of the Territory to conduct an audit.

A performance management system is not defined in the legislation, but section 15 identifies that: “*the object of an audit conducted under this section includes determining whether the performance management systems of an agency or organisation in respect of which the audit is being conducted enable the Agency or organisation to assess whether its objectives are being achieved economically, efficiently and effectively.*”

Appendix 5: Overview of the approach to auditing performance management systems cont...

Operational Framework

The Northern Territory Auditor-General's Office has developed a framework for its approach to the conduct of performance management system audits, which is based on our opinion that an effective performance management system would contain the following elements:

- identification of the policy and corporate objectives of the entity;
- incorporation of those objectives in the entity's corporate or strategic planning process and allocation of these to programs of the entity;
- identification of what successful achievement of those corporate objectives would look like, and recording of these as performance targets;
- development of strategies for achievement of the desired performance outcomes;
- monitoring of the progress with that achievement;
- evaluation of the effectiveness of the final outcome against the intended objectives; and
- reporting on the outcomes, together with recommendations for subsequent improvement.

Performance management system audits can be conducted at a corporate level, a program level, or at a category of cost level, such as capital expenditure. All that is necessary is that there be a need to define objectives for intended or desired performance.

Appendix 6: Agencies not audited in the year ended 30 June 2012

Section 13(3) of the *Audit Act* permits the Auditor General to dispense with an audit of an Agency.

For activities relating to the financial year ended 30 June 2012, no audits were, or are intended to be, conducted at the following Agencies:

- Aboriginal Areas Protection Authority;
- Department of Natural Resources, Environment, The Arts and Sport;
- Department of the Legislative Assembly;
- Ombudsman's Office.

The increasingly stringent requirements of Australian Accounting Standards, and Auditing and Assurance Standards has required that audit effort be directed towards financial audits of those Agencies that are deemed to represent greater materiality and greater risk. It is proposed that each of the listed Agencies will be included in audit coverage at least once every three years.

It is also noted that an independent auditor appointed under section 27 of the *Audit Act* conducts an annual audit of the Auditor-General's Office.

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Appendix 7: Engagement letter

Services provided by the Northern Territory Auditor-General's Office

It is quite common for auditors to issue “letters of engagement” to their clients. These are intended to assist in ensuring that there is a clear understanding between the auditor and the client about the objectives and scope of the audit, the extent of the auditor’s responsibilities and the form of any reports.

In the public sector there is generally no requirement for Auditors-General to issue letters of engagement as the roles and responsibilities are set out in relevant legislation. However, there has been an increasing tendency to provide parliaments with a form of letter of engagement to assist them to have a better understanding of the audit role.

Meeting the Legislative Assembly’s expectations

The principal legislation that governs the conduct of audits in the Northern Territory public sector is the *Audit Act*. That Act:

- requires me to audit the Public Account and other accounts in such manner as I think fit having regard to recognised professional standards and practices;
- permits the Minister to direct me to carry out an audit which I have the power under the Act to carry out; and
- permits me to conduct an audit of performance managements systems of any Agency or other organisation in respect of the accounts of which I am required by a law of the Territory to conduct an audit.

Financial attest and compliance audits

Financial attest and compliance audits are conducted by the Office in accordance with legislated requirements and Australian Auditing Standards. The main purpose of an audit is to add credibility to a financial report by providing an independent audit opinion. When reading an opinion it is essential to have a clear understanding of what it provides and what a financial report audit covers.

Appendix 7: Engagement letter cont...

The audit opinion provides users of a financial report with reasonable assurance that it is free of material error and complies with legislation and applicable accounting standards. It does not:

- provide a guarantee of absolute accuracy in the financial report;
- express a view on the adequacy of the organisation's systems or the efficiency and effectiveness with which management conducts its affairs; or
- provide any assurance about the organisation's future viability.

An audit does not guarantee that every amount and disclosure in the financial report is error free. An audit does not examine every transaction of an organisation, as this would be prohibitively expensive and time-consuming. A financial compliance or attest audit is a combination of systems checks and examination of samples of transactions for all items in the financial report that are considered to be material or of high risk and which, if materially misstated as a result of an error or fraud, could affect the judgements made by users on the basis of that report.

It is also important to understand that the organisation's management, not the auditor, is responsible for:

- maintaining adequate accounting records and preparing the financial report; and
- maintaining a system of internal controls to prevent or detect errors or irregularities.

I recognise that, in the public sector, financial report audit opinions by themselves will not meet the Legislative Assembly's expectations. Firstly, because the principal objective of most public sector Agencies is to provide services rather than to generate profits, their financial reports give only limited information about their performance. Secondly, the Legislative Assembly and the community have higher expectations of probity and proper conduct in public sector Agencies.

Appendix 7: Engagement letter cont...

Accordingly, when the Audit Office conducts financial report audits it has regard to:

- Agency performance;
- wastage of public resources;
- probity or financial prudence in the management of financial resources; and
- compliance by Agencies with legislative requirements and government policies and procedures.

Audit of performance management systems

The *Audit Act* also permits me to conduct an audit of performance management systems of Agencies or entities or other organisations in respect of the accounts or financial report of which I am required or permitted by a law of the Territory to conduct an audit.

The conduct of these audits is governed by Part 3 of the *Audit Act*. These audits may be separate audits or they may be undertaken as part of another audit. The objective is to determine whether the performance management systems of the Agency or organisation enable the Agency or entity to assess whether its objectives are being achieved economically, efficiently and effectively. It is important to note that the provisions of the *Audit Act* do not countenance audits of economy, efficiency or effectiveness per se.

Performance management systems audits can be conducted at a corporate, output or category of cost level. My Office has developed a framework for its approach to the conduct of performance management system audits.

Appendix 7: Engagement letter cont...

Over the years the Northern Territory Auditor-General's Office has encouraged improved reporting of performance by Agencies and other Government entities. It has also encouraged Agencies and other entities to report performance indicators that address the criteria of economy, efficiency and effectiveness. In applying the audit framework referred to above, the Office continues to apply the following definitions that are contained in Australian Auditing Standard ASAE 3500 Performance Engagements:

- Economy – the acquisition of the appropriate quality and quantity of resources at the appropriate times and the lowest cost.
- Efficiency – the use of resources such that output is optimised for any given set of resource inputs, or input is minimised for any given quantity and quality of output.
- Effectiveness – the achievement of the objectives or other intended effects of activities at a program or entity level.

Reporting to the Legislative Assembly

Auditor-General's reports to the Legislative Assembly present the findings of my financial report audits of Agencies and other public sector entities. These reports address high-level issues on Agency operations. Minor matters are reported only where they are symptomatic of a larger problem or where it is considered that insufficient attention has been given by the Agency to addressing issues raised.

I issue two principal reports each year. These cover the results of audits conducted during the previous six months.

Management letters to Agencies

A more detailed report is issued to the Accountable Officers of Agencies on matters identified during audits and these may include recommendations for operational improvements. These matters are in addition to any matters that may be included as part of the Independent Audit Report.

Procedural fairness

The Audit Office submits its draft reports to the relevant Accountable Officers and staff in their Agencies to ensure factual accuracy and to provide an opportunity for Agencies to submit comments on my findings for inclusion in my reports to the Legislative Assembly.

Appendix 7: Engagement letter cont...

Enhancing the value of the audit function

As part of the discharge of my role, I will seek to maximise the value to the Agency, the Government and the Legislative Assembly of all audit work including where appropriate the framing of recommendations to address:

- improvement in the framework of accountability;
- opportunities for cost savings and efficiency gains; and
- recognition of good practice in use by Agencies, entities and units of administration.

Audit fees

Audit fees are not charged by the Audit Office for audits of Agencies or other organisations that form part of the Public Account. In these circumstances the costs of the audit are met from monies appropriated by the Legislative Assembly. However, in some circumstances, the Central Holding Authority may seek to recover from the organisation in question an amount equal to the cost of the audit.

Where an audit is performed in respect of an organisation that does not form part of the Public Account or where the audit is performed for a third party, for example, audits of acquittals of expenditure on behalf of the Commonwealth, the costs of the audit are recovered directly from the organisation in question.

Independence

Independence is the hallmark of audit. It is a fundamental concept that requires me to approach my work with integrity and objectivity. I must both be, and be seen to be, free of any interest which is incompatible with objectivity. It is essential therefore that I am independent of the Agencies being audited and free of interests that could be incompatible with integrity and objectivity.

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Appendix 8: Abbreviations

BAC	Blood Alcohol Content
BrAC	Breath Alcohol Content
CDU	Charles Darwin University
CESS	Communications and Electronic Services Section
DCI	Department of Construction and Infrastructure
DLP	Department of Lands and Planning
DoH	Department of Health
EBA	Evidential Breath Analyser
ECI	Early Contractor Involvement
Fast Ferries	Fast Ferries Pty Ltd
GMS	Grants Management System
GST	Goods and Services Tax
ICT	Information and Communication Technology
NATA	National Association of Testing Authorities
NGO	Non-government Organisation
NSW	New South Wales
NTAGO	Northern Territory Auditor-General's Office
NTPFES	Northern Territory Police, Fire and Emergency Services
OCPE	Office of the Commissioner for Public Employment
PPP	Public-Private Partnership
PRB	Procurement Review Board

Appendix 8: Abbreviations cont...

RFP	Request for Proposal
RFT	Request for Tender
Sea-Cat	Sea Cat Ferries & Charters Pty Ltd
VET	Vocational Education and Training

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