

The Auditor-General
Audit Report No.51 2011–12
Financial Statement Audit

**Interim Phase of the Audits of the Financial
Statements of Major General Government
Sector Agencies for the year ending
30 June 2012**

Australian National Audit Office

© Commonwealth
of Australia 2012

ISSN 1036-7632

ISBN 0 642 81258 6

COPYRIGHT INFORMATION

This work is copyright. Apart from any use as permitted under the *Copyright Act 1968*, no part may be reproduced by any process without prior written permission from the Commonwealth.

Requests and inquiries concerning reproduction and rights should be addressed to:

Executive Director
Corporate Management Branch
Australian National Audit Office
19 National Circuit
BARTON ACT 2600

Or via email:
webmaster@anao.gov.au



Canberra ACT
26 June 2012

Dear Mr President
Dear Mr Speaker

The Australian National Audit Office has undertaken the interim audit phase of the 2011–12 financial statements audits of major General Government Sector agencies in accordance with the authority contained in the *Auditor-General Act 1997*. I present the report of these audits and the accompanying brochure to the Parliament. The report is titled *Interim Phase of the Audits of the Financial Statements of Major General Government Sector Agencies for the year ending 30 June 2012*.

Following its tabling, the report will be placed on the Australian National Audit Office's Homepage—<http://www.anao.gov.au>.

Yours sincerely

A handwritten signature in black ink, appearing to read 'Ian McPhee', is positioned above the printed name.

Ian McPhee
Auditor-General

The Honourable the President of the Senate
The Honourable the Speaker of the House of Representatives
Parliament House
Canberra ACT

AUDITING FOR AUSTRALIA

The Auditor-General is head of the Australian National Audit Office (ANAO). The ANAO assists the Auditor-General to carry out his duties under the *Auditor-General Act 1997* to undertake performance audits, financial statement audits and assurance reviews of Commonwealth public sector bodies and to provide independent reports and advice for the Parliament, the Australian Government and the community. The aim is to improve Commonwealth public sector administration and accountability.

For further information contact:
The Publications Manager
Australian National Audit Office
GPO Box 707
Canberra ACT 2601

Telephone: (02) 6203 7505
Fax: (02) 6203 7519
Email: webmaster@anao.gov.au

ANAO audit reports and information about the ANAO are available at our internet address:

<http://www.anao.gov.au>

Contents

Abbreviations and Acronyms	9
Summary	13
Introduction	13
Developments in financial reporting and auditing frameworks	14
Summary of audit results	15
Future audit coverage	18
1. Introduction	19
Background	19
Report structure	20
Acknowledgements	21
2. Financial Reporting and Auditing Frameworks	22
Introduction	22
Recent changes to the Australian public sector reporting framework	23
Future developments in the Australian public sector reporting framework	25
International developments	28
Legislative changes affecting the financial reporting framework	32
Developments in auditing standards	33
Conclusion	35
3. Summary of Audit Findings and Related Issues	37
Introduction	37
Internal control	39
Control environment	39
Agency risk assessment process	48
Information systems	53
Control activities	54
Monitoring of controls	65
Conclusion	67
4. Information Technology Controls	68
Introduction	68
IT control environment	69
General IT controls	71
Application controls	77
Trends over the period 2007–08 to 2011–12	83
Data centre consolidation	89
Conclusion	90
5. Results of the Interim Audit Phase by Agency	92
Introduction	92

Agriculture, Fisheries and Forestry Portfolio	95
Department of Agriculture, Fisheries and Forestry	95
Attorney-General's Portfolio	99
Attorney-General's Department	99
Australian Customs and Border Protection Service.....	102
Broadband, Communications and the Digital Economy Portfolio	109
Department of Broadband, Communications and the Digital Economy	109
Climate Change and Energy Efficiency Portfolio	113
Department of Climate Change and Energy Efficiency	113
Defence Portfolio.....	117
Department of Defence	117
Defence Materiel Organisation	129
Department of Veterans' Affairs	135
Education, Employment and Workplace Relations Portfolio.....	143
Department of Education, Employment and Workplace Relations	143
Families, Housing, Community Services and Indigenous Affairs Portfolio	149
Department of Families, Housing, Community Services and Indigenous Affairs	149
Finance and Deregulation Portfolio.....	154
Department of Finance and Deregulation	154
The Board of Guardians and the Future Fund Management Agency.....	157
Foreign Affairs and Trade Portfolio	161
Department of Foreign Affairs and Trade	161
Health and Ageing Portfolio	165
Department of Health and Ageing.....	165
Human Services Portfolio.....	169
Department of Human Services	169
Immigration and Citizenship.....	176
Department of Immigration and Citizenship.....	176
Infrastructure and Transport Portfolio	181
Department of Infrastructure and Transport	181
Industry, Innovation, Science, Research and Tertiary Education Portfolio.....	185
Department of Industry, Innovation, Science, Research and Tertiary Education	185
Prime Minister and Cabinet Portfolio.....	190
Department of the Prime Minister and Cabinet.....	190
Regional Australia, Local Government, Arts and Sport Portfolio	194
Department of Regional Australia, Local Government, Arts and Sport	194
Resources, Energy and Tourism Portfolio	199
Department of Resources, Energy and Tourism	199

Sustainability, Environment, Water, Population and Communities Portfolio	202
Department of Sustainability, Environment, Water, Population and Communities	202
Treasury Portfolio	206
Department of the Treasury	206
Australian Office of Financial Management	212
Australian Taxation Office	216
Appendices	223
Appendix 1: Agencies covered by this report	225
Appendix 2: The Accounting and Auditing Standards Frameworks	226
Appendix 3: The Financial Reporting Framework	227
Series Titles	233
Current Better Practice Guides	240
Tables	
Table 4.1 Elements of the IT control environment.....	70
Table 5.1 Significant and moderate findings of agencies grouped by portfolio covered by this report	94
Figures	
Figure 3.1 Assessment of business continuity controls: 2009–10 to 2011–12	50
Figure 3.2 Assessment of disaster recovery controls: 2009–10 to 2011–12.....	50
Figure 3.3 Aggregate audit findings – categories A, B and C	55
Figure 3.4 IT control environment – aggregate audit findings	56
Figure 3.5 Purchases and payables – aggregate audit findings	57
Figure 3.6 Grant accounting – aggregate audit findings.....	58
Figure 3.7 Asset accounting and control of non-financial assets – aggregate audit findings	60
Figure 3.8 Revenue, receivables and cash management – aggregate audit findings	61
Figure 3.9 Human resource management process – aggregate audit findings	63
Figure 3.10 Other control matters – aggregate audit findings	64
Figure 4.1 2011–12 Assessment of IT security management	73
Figure 4.2 2011–12 Assessment of IT change management.....	75
Figure 4.3 2011–12 Assessment of IT incident and problem management.....	77
Figure 4.4 Summary of FMIS applications 2007–08 to 2011–12	78
Figure 4.5 Summary of HRMIS applications 2007–08 to 2011–12	79
Figure 4.6 2011–12 Assessment of FMIS controls.....	80
Figure 4.7 2011–12 Assessment of HRMIS controls.....	82

Figure 4.8	IT security governance: 2007–08 to 2011–12	83
Figure 4.9	Configuration management tools: 2007–08 to 2011–12	84
Figure 4.10	Change management policy and governance frameworks: 2007–08 to 2011–12.....	85
Figure 4.11	FMIS privileged user management: 2007–08 to 2011–12	86
Figure 4.12	FMIS business continuity: 2007–08 to 2011–12	87
Figure 4.13	HRMIS privileged user management: 2007–08 to 2011–12	88
Figure 4.14	HRMIS business continuity: 2007–08 to 2011–12	89
Figure 5.1	Reporting of Defence audit issues	122

Abbreviations and Acronyms

AAO	Administrative Arrangements Order
AAS	Australian Accounting Standard
AASB	Australian Accounting Standards Board
AGD	Attorney–General’s Department
ANAO	Australian National Audit Office
AOFM	Australian Office of Financial Management
ASA	Australian Auditing Standard
ATO	Australian Taxation Office
AUASB	Australian Auditing and Assurance Standards Board
BCM	Business Continuity Management
BCP	Business Continuity Plan
CAC Act	<i>Commonwealth Authorities and Companies Act 1997</i>
CEIs	Chief Executive’s Instructions
CE	Chief Executive
CFO	Chief Finance Officer
CFS	Consolidated Financial Statements
CoC	Certificate of Compliance
Customs and Border Protection	Australian Customs and Border Protection Service
DMO	Defence Materiel Organisation

DAFF	Department of Agriculture, Fisheries and Forestry
DBCDE	Department of Broadband, Communications and the Digital Economy
DCCEE	Department of Climate Change and Energy Efficiency
Defence	Department of Defence
DEEWR	Department of Education, Employment and Workplace Relations
DFAT	Department of Foreign Affairs and Trade
DIAC	Department of Immigration and Citizenship
DI&T	Department of Infrastructure and Transport
DIISRTE	Department of Innovation, Industry, Science, Research and Tertiary Education
DoHA	Department of Health and Ageing
DHS	Department of Human Services
DRET	Department of Resources, Energy and Tourism
DSEWPAC	Department of Sustainability, Environment, Water, Population and Communities
DVA	Department of Veterans' Affairs
FaHCSIA	Department of Families, Housing, Community Services and Indigenous Affairs
FASB	United States Financial Accounting Standards Board
Finance	Department of Finance and Deregulation
FMA Act	<i>Financial Management and Accountability Act 1997</i>
FMIS	Financial Management Information System
FMOs	Finance Minister's Orders
FRSB	New Zealand Financial Reporting Standards Board

GAAP	Generally Accepted Accounting Principles
GFS	Government Finance Statistics
GGs	General Government Sector
HRMIS	Human Resources Management Information System
IAASB	International Auditing and Assurance Standards Board
IASB	International Accounting Standards Board
IFRS	International Financial Reporting Standards
IPSASB	International Public Sector Accounting Standards Board
ISA	International Standards on Auditing
IT	Information Technology
JCPAA	Joint Committee of Public Accounts and Audit
PM&C	Department of the Prime Minister and Cabinet
RBA	Reserve Bank of Australia
Treasury	Department of the Treasury

Summary

Introduction

1. The *Auditor-General Act 1997* establishes the mandate for the Auditor-General to undertake financial statement audits of all Australian Government entities including those of Government agencies, statutory authorities and Government business enterprises.
2. The preparation of audited financial statements in compliance with the Finance Minister's Orders¹ is a key element of the financial management and accountability regime applicable to Australian Government entities. It is generally accepted in both the private and public sectors that a good indicator of the effectiveness of an entity's financial management is the timely finalisation of its annual financial statements, accompanied by an unmodified audit opinion. Australian Government entities, in cooperation with the Australian National Audit Office (ANAO), devote considerable effort to achieving such an outcome.
3. Financial statement audits are an independent examination of the financial accounting and reporting of public sector entities. The results of the examination are presented in an auditor's report, which expresses the auditor's opinion on whether the financial statements as a whole and the information contained therein fairly present each entity's financial position and the results of its operations and cash flows. The accounting treatments and disclosures reflected in the financial statements by the entity are assessed against relevant accounting standards and legislative reporting requirements.
4. Under section 57 of the *Financial Management and Accountability Act 1997* (FMA Act), the Auditor-General is required to report each year to the relevant Minister on whether the financial statements of agencies have been prepared in accordance with the Finance Minister's Orders (FMOs) and whether they give a true and fair view of the matters required by those Orders.
5. To assist agencies to manage their responsibilities, the ANAO periodically publishes better practice guides on a range of aspects of public administration. During 2011–12, the ANAO published three Better Practice

¹ The Finance Minister's Orders (FMOs) made by the Minister for Finance and Deregulation set out the requirements for the preparation of financial statements of all reporting entities covered by the *Financial Management and Accountability Act 1997* and the *Commonwealth Authorities and Companies Act 1997*.

Guides: *Public Sector Audit Committees; Developing and Managing Contracts* and *Public Sector Environmental Management*. An updated guide on *Public Sector Internal Audit* is due to be released early in the next financial year. Better Practice Guides are well received by agencies and contribute to agencies maintaining the maturity of their internal control systems.

6. The interim phase of the audit of agencies encompasses a review of governance arrangements related to agencies' financial reporting responsibilities, and an examination of relevant internal controls, including information technology system controls. The ANAO's examination of these areas is designed to assess the reliance that can be placed on agencies' internal controls to produce complete and accurate information for financial reporting purposes.

7. The audit findings in this report have been reported to the management of each agency and to the responsible Minister(s).

Developments in financial reporting and auditing frameworks

8. The Australian Accounting Standards Board (AASB) has continued to work towards improved financial reporting by adding to or modifying Australian accounting standards. During 2011–12, the changes to standards have only had an impact on a small number of agencies.

9. Future changes to Australian Accounting Standards will be driven largely by developments in accounting standards internationally. Significant changes to accounting standards and the conceptual frameworks used to develop standards are underway, potentially changing reporting requirements in important areas such as financial instruments, revenue and leases. The AASB has also initiated a number of domestic projects. These include a project that considers harmonising reporting by Government entities with the Australian Bureau of Statistics' Government Finance Statistics framework; such an approach has been adopted for reporting by governments but not for Government entities. The AASB is also considering applying the disclosure requirements for related party transactions and executive remuneration to not-for-profit public entities.

10. The Australian Auditing and Assurance Standards Board has commenced a range of activities that relate to the audit of financial statements including: revising its 2008 guide, *Audit Committees: a Guide to Good Practice*;

developing a joint policy paper with the New Zealand Auditing and Assurance Standards Board regarding the harmonisation of Australian and New Zealand auditing standards; revising the 2009 *AuASB Bulletin: Auditing Considerations in an Uncertain Economic Environment*; and revising ASA 610 *Using the Work of Internal Auditors*, in line with changes to the equivalent international standard.

Summary of audit results

Internal control in agencies²

11. A central element of the ANAO's financial statement audit methodology, and the focus of the interim phase of ANAO audits, is a sound understanding of an agency's internal controls to inform our audit approach including the reliance we may place on agency systems to produce financial statements that are free from material misstatement. To do this, the ANAO uses the framework contained in the ASA 315 *Identifying and Assessing the Risks of Material Misstatement through Understanding the Entity and its Environment*. The key elements of internal control, as discussed in ASA 315, are the control environment; the risk assessment process; information systems, including the related business processes relevant to financial reporting, and communication; control activities; and monitoring of controls.

Control environment

12. The ANAO assesses whether an agency's control environment includes measures that contribute positively to sound corporate governance in the context of the preparation of an agency's financial statements. These measures should be designed to mitigate identified risks of material misstatement in the financial statements, and reflect the specific governance requirements of each agency.

13. The ANAO observed that agencies have in place key elements of a financial control environment designed to provide a sound basis for the effective preparation of the agency's financial statements. Audit committees, in particular, continue to have a positive influence on the effectiveness of agencies' control environments particularly in the areas of risk assessment, legislative compliance and financial system controls.

² The term 'agencies' refers to the 25 major General Government Sector agencies referred to in this report. These are listed at Appendix 1.

Risk assessment process

14. An understanding of an agency's risk assessment processes is an essential element of the ANAO's financial statement audits. Agencies are expected to manage the key risks specific to their environment and the interim audit phase includes a review of controls relating to risks that may have a material impact on agencies' financial statements. Generally, the ANAO found that agencies have well-established risk assessment processes, overseen by audit committees or other committees with specific risk management responsibilities.

15. Important elements of the risk assessment process common to all agencies are business continuity and fraud control management. The audit program identified a general improvement in the level of awareness and maintenance of business continuity and disaster recovery controls in agencies. However, a number of agencies did not test their Business Continuity Plans (BCPs) as part of normal business practice. In relation to fraud control, agencies have fraud control plans prepared in accordance with the Commonwealth Fraud Control Guidelines.³ A small number of agencies needed to improve the development and timely updating of fraud control plans.

Information systems

16. Information technology facilitates the way in which Australian Government agencies operate, and supports the business processes that deliver services to the Australian community.

17. Consistent with past practice, during the 2011–12 interim audits, the ANAO assessed the design and operation of key IT controls to determine the effectiveness of these controls and their impact on reducing risks affecting integrity of financial information presented in agencies' financial statements.

18. Overall, the ANAO's assessment of the operation of general and application controls in major agencies had identified no significant changes from 2010–11. While improvements observed in agencies' change management governance and system release management arrangements in 2010–11 have been maintained in 2011–12, the management of user access, particularly the logging and monitoring of user activities for privileged users, and business

³ The Fraud Control Plan for the Department of Regional Australia, Regional Development and Local Government (DRARDLG) was in draft form at the time of the audit.

continuity arrangements for Human Resources Management Information Systems (HRMIS) continued to be areas requiring improvement in some agencies.

Control activities

19. The results of the 2011–12 interim audit activity indicated that, overall, control activities relating to financial and accounting processes have continued to be maintained at an effective level. The total number of significant and moderate audit findings has again decreased, continuing the trend over recent years. Control issues identified by the audits related to areas such as: human resource management processes and a range of IT general application controls, particularly the management of user access to key financial business systems, IT security governance and HRMIS business continuity management. A total of 146 Category A, B, C and L1 findings⁴ were identified in the 2011–12 interim audit phase with the majority of these findings posing a low business or financial management risk, a small reduction compared with the 158 findings identified in 2010–11.

Monitoring of controls

20. Many activities undertaken by agencies contribute to their regime of monitoring controls. These include quality assurance arrangements, internal and external reviews, control self-assessment processes, and internal audit. In particular, all agencies have in place arrangements to enable Chief Executives to provide an annual Certificate of Compliance.

21. The ANAO continues to include an assessment of compliance in relation to annual appropriations, special appropriations, special accounts and the investment of public moneys in its financial statement audits as a result of interest shown by the Joint Committee of Public Accounts and Audit in past years. The 2011–12 interim audits found a high level of compliance in these areas, with the exception of actual or potential breaches of section 83 of the Constitution which provides that expenditure by the Commonwealth must be in accordance with an appropriation made by the Parliament. This matter is discussed at paragraphs 3.37 to 3.47 of Chapter 3 of this report.

⁴ The ANAO rates its audit findings according to a risk scale. Audit findings that pose a significant business or financial management risk to the entity are rated as 'A'. Findings that pose a moderate business or financial management risk are rated as 'B'. Findings that pose a low business or financial management risk are rated as 'C'. Category L1 findings are instances of non-compliance with key legislative requirements.

Agency audit findings

22. The results of the 2011–12 interim audits reflect a continuation of the reduction over recent years in the number of significant (Category A) and moderate (Category B) audit findings. This reflects the general stability and maturity of the control regimes in the majority of agencies and actions taken by agencies to address prior year audit findings.

23. However, as noted above, the audits do continue to identify control weaknesses in a number of areas particularly relating to human resource management processes; the management of user access to key financial systems; IT security governance; and HRMIS business continuity management.

24. Generally, agencies have been positive and timely in their response to ANAO audit findings.

25. The following is a summary of the trend in Category A, B and L1 audit findings between 2010–11 and 2011–12 reported at the completion of the interim audit phase. There was:

- one agency with a Category A audit finding in 2011–12, the same number as in 2010–11;
- one Category A audit finding in 2011–12, a decrease from three in 2010–11;
- thirty-one Category B audit findings across all agencies in both 2010–11 and 2011–12;
- an increase in the number of Category B audit findings in seven agencies; five showed a decrease; and 13 agencies had no Category B findings in either 2010–11 or 2011–12; and
- one agency with a Category L1 finding in 2011–12, the same as in 2010–11.

26. A summary of Category A, B and L1 audit findings by agency is provided in Table 5.1 in Chapter 5.

Future audit coverage

27. In completing the audits of agencies' 2011–12 financial statements, the ANAO will complete its assessment of the effectiveness of internal controls and areas of audit focus in each agency. The summary results of this work will be reported by the ANAO in December 2012.

1. Introduction

This chapter provides background to the audits of the financial statements of Australian Government entities and sets out the structure of this report that covers 25 major General Government Sector agencies.

Background

1.1 In addition to undertaking financial statement audits of individual entities, the ANAO tables two reports annually that summarise the findings of the financial statement audits of public sector entities. These reports also discuss contemporary issues and practices affecting public sector entities' financial reporting responsibilities and the ANAO's responsibilities. This report outlines the ANAO's assessment of the internal controls of major agencies, including governance arrangements, information systems and control procedures. The findings summarised in this report are the results of the interim phase⁵ of the financial statement audits of 25 major General Government Sector agencies that represent some 95 per cent of total General Government Sector⁶ (GGS) revenues and expenses.

1.2 In reporting on the results of the interim phase of the financial statement audit program, the ANAO is providing assurance to the Parliament that the systems, controls and processes that are in place in major Australian Government agencies⁷ are operating in a way that allows agencies to prepare financial statements that give a true and fair view of their financial performance and position at financial year end.

1.3 The audit coverage undertaken forms an integral part of the ANAO's audit of the 2011–12 financial statements of these agencies. This report includes reference to issues that have the potential to have a material impact on

⁵ Financial statement audits are generally performed in two phases—interim and final. The interim phase focuses on an assessment of agencies' key internal controls; in the final audit phase the ANAO completes its assessment of the effectiveness of key controls for the full year, substantively tests material balances and disclosures in the financial statements, and finalises its opinion on the agencies' financial statements.

⁶ The General Government Sector (GGS) comprises all government agencies and other entities that provide largely non-market public services and are funded primarily through taxes. This report covers the portfolio departments and other major GGS entities that comprise approximately 95 per cent of total GGS revenues and expenses.

⁷ The term 'agencies' refers to all organisations subject to the *Financial Management and Accountability Act 1997* (FMA Act). As the organisations covered by this report are 'agencies', this term is used predominantly in the report.

agencies' financial statements and to other control related matters requiring attention by agency management.

1.4 At the individual agency level, a report on the results of the audit is provided to each agency Chief Executive and audit committee. Audit activity can act as a catalyst for improvement and provide a stimulus to agency management for the resolution of issues, where this is warranted.

1.5 The preparation of financial statements in compliance with the Finance Minister's Orders⁸ is a key element of the financial management and accountability regime applicable to Australian Government entities. It is generally accepted in both the private and public sectors that a good indicator of the effectiveness of an entity's financial management is the timely finalisation of its annual financial statements, accompanied by an unmodified audit opinion. Australian Government entities, in cooperation with the ANAO, devote considerable effort to achieving timeliness in financial reporting.

Report structure

1.6 The report is organised as follows:

- Chapter 2 discusses a number of recent developments in accounting and auditing requirements and, in doing so, provides an overview of changes impacting the Australian Government's reporting and accountability frameworks.
- Chapter 3 provides summary observations relating to various elements of agencies' internal controls (including the control environment, the risk assessment process, information systems, control activities and monitoring of controls). This chapter also includes a discussion of: audit findings over the period 2008–09 to 2011–12; and legislative compliance including agencies' assessments of potential breaches of section 83 of the Constitution.
- Chapter 4 outlines findings relating to the audit of Information Technology (IT) systems focusing on the IT control environment, IT security, application controls in financial management information systems, and human resource management information systems.

⁸ The Finance Minister's Orders (FMOs) made by the Minister for Finance and Deregulation set out the requirements for the preparation of financial statements of all reporting entities covered by the *Financial Management and Accountability Act 1997* and the *Commonwealth Authorities and Companies Act 1997*.

- Chapter 5 outlines, for each agency, details of business operations that influence financial statement audit coverage; governance arrangements relevant to the agency's financial statements; areas of audit focus, and significant and moderate audit issues identified by the 2011–12 interim audits. The chapter is structured in accordance with the portfolio arrangements established by the Administrative Arrangements Order (AAO) of 9 February 2012.

Acknowledgements

1.7 Based on the work completed during the interim audit phase, the ANAO is well placed to complete the audit program following the preparation by agencies of their financial statements after the close of the 2011–12 financial year. The contribution and cooperation of Chief Finance Officers, other agency staff, and the key role undertaken by audit committee members is greatly appreciated.

2. Financial Reporting and Auditing Frameworks

This chapter provides commentary on recent developments in the financial reporting and auditing frameworks relevant to the Australian Government and its reporting entities.

Introduction

2.1 The Australian Government's financial reporting framework is based, in large part, on standards made independently by the Australian Accounting Standards Board (AASB). This framework is designed to support decision-making by, and accountability to, the Parliament.

2.2 The AASB bases its accounting standards on the International Financial Reporting Standards (IFRS) issued by the International Accounting Standards Board (IASB). Because IFRS are designed primarily to relate to for-profit organisations, the AASB amends the IFRS to address the financial reporting needs of the public and not-for-profit private sectors. The Finance Minister prescribes additional financial reporting requirements for Australian Government agencies and authorities through the Finance Minister's Orders (FMOs) for Financial Reporting.

2.3 There were few changes to Australian Accounting Standards in 2011–12. The main changes were increased harmonisation between Australian and New Zealand accounting standards; reductions in the requirements to disclose information on financial instruments and transactions with related parties; and additional exemptions from the requirement to prepare consolidated financial statements.

2.4 For the foreseeable future, major developments in accounting standards internationally will drive changes to Australian Accounting Standards. However, the AASB has also initiated a number of domestic projects. The project to harmonise reporting by Government entities with the Australian Bureau of Statistics' Government Finance Statistics (GFS) framework is continuing, with the focus now turning from whole of Government reporting to reporting by Government-controlled entities. The AASB is also considering disclosure requirements for related party transactions and executive remuneration of not-for-profit entities.

2.5 At the international level, significant changes to accounting standards and the conceptual frameworks used to develop standards are underway, potentially changing reporting requirements in important areas such as financial instruments, revenue and leases. During 2011–12, work continued on new conceptual frameworks for financial reporting intended to provide a sound base for the development of future accounting standards.

2.6 Just as Australian Accounting Standards are based on international accounting standards, the Australian Auditing Standards Board (AUASB) bases Australian Auditing Standards on the International Auditing Standards (ISA). The ANAO adopts Australian Auditing Standards.

Recent changes to the Australian public sector reporting framework

Australia-New Zealand convergence

2.7 Following an agreement between the Australian and New Zealand governments to promote closer markets between the two countries, the AASB and the New Zealand Financial Reporting Standards Board (FRSB) acted to remove differences between their respective suites of accounting standards. The primary focus has been on accounting standards relating to the for-profit sector.

2.8 In May 2011, the AASB and the FRSB released new accounting standards⁹ as a first step towards full harmonisation for the for-profit sector. These standards remove many of the differences between Australian and New Zealand accounting standards. The new standards took effect from 1 January 2012.

2.9 Among the changes is a clause permitting certain entities to depart from an Australian Accounting Standard where compliance with the Standard would be so misleading that it would conflict with the objective of the financial statements. This clause is not available to entities reporting under the Corporations Act or to not-for-profit entities.

⁹ The Australian Standards are AASB 2011-1 *Amendments to Australian Accounting Standards arising from the Trans-Tasman Convergence Project*, AASB 2011-2 *Amendments to Australian Accounting Standards arising from the Trans-Tasman Convergence Project – Reduced Disclosure Requirements* and AASB 1054 – *Australian Additional Disclosure*.

Transactions with related parties

2.10 Australian private sector entities must comply with AASB 124 *Related Parties*, which requires entities to disclose transactions with related parties. Related parties of an entity include those entities and persons that manage, control or significantly influence the entity, together with close family members of such persons.

2.11 Commencing for reporting periods on or after 1 July 2011, AASB 124 has been revised to introduce more targeted disclosure of transactions between Government entities. The Standard now requires disclosure of the nature and amount of significant intra-government transactions; for routine and less significant transactions, only an indication of the extent of such transactions is required. For all transactions with other related parties, such as key management personnel and their close family members, the existing AASB 124 disclosures apply.

2.12 Further, in July 2011, the AASB released a proposal to apply AASB 124 to public sector entities. Potentially, all Australian Government entities would be required to provide detailed disclosure of transactions with key management personnel and Ministers. The AASB expects to release a revised AASB 124 incorporating these proposals in the second half of 2012. The proposed commencement date for the revised Standard is 1 July 2013.

Further relief from preparing two sets of financial statements

2.13 AASB 127 *Consolidated and Separate Financial Statements* requires entities with subsidiaries to prepare consolidated financial statements; that is, statements combining the transactions of the entity and its subsidiaries. However, this Standard exempts certain entities from this requirement. For example, a company that was wholly-owned by another company preparing consolidated financial statements in accordance with IFRS, and that had neither traded debt nor equity, would not itself need to prepare consolidated financial statements.

2.14 The AASB has extended this relief to, amongst others, all Government-owned not-for-profit entities¹⁰. Therefore, although governments are still required by Australian Accounting Standards to publish consolidated financial

¹⁰ AASB 2011-5 *Amendments to Australian Accounting Standards – Extending Relief from Consolidation, the Equity Method and Proportionate Consolidation* was released in July 2011 and applies to reporting period beginning on or after 1 July 2011.

statements, Government-controlled entities are not. However, the FMOs currently require all Australian Government entities with subsidiaries, other than companies, to publish consolidated statements. For the new exemption to apply to such entities, the Finance Minister would need to grant an exemption from the FMOs.

Revised disclosures for financial instruments

2.15 AASB 7 *Financial Instruments: Disclosures* has been amended to require additional disclosures where an entity transfers a financial asset to another party but either:

- does not completely remove the asset from its balance sheet; or
- maintains some continuing involvement with the asset.

2.16 These additional disclosures aim to provide users with more information about risk exposures retained by the entity after the transfer. Very few Australian Government entities would undertake these types of transactions.

2.17 The AASB has also clarified and simplified other requirements of AASB 7. The effect of these amendments is that in future, entities will not need to disclose:

- the maximum exposure to credit risk arising from a class of financial instruments, where equal to the amount reported in the balance sheet;
- details of financial instruments where the terms were renegotiated during the year; and
- immaterial items.

Future developments in the Australian public sector reporting framework

Fair value measurement

2.18 Several accounting standards require or allow entities to present their assets and liabilities at fair value in the balance sheet. However, the IASB has identified that guidance on measuring fair value is spread among several standards and is often high-level and sometimes inconsistent between standards. In May 2011, the IASB issued an accounting standard to provide a single source of guidance on fair value measurement. This standard clarifies

the definition of fair value, provides a framework for measuring fair value and enhances the disclosures surrounding fair value measurements. In September 2011, the AASB issued AASB 13 *Fair Value Measurement*, replicating the IASB standard. AASB 13 takes effect from 1 January 2013.

Superannuation

2.19 AASB 119 *Employee Benefits* has been reissued and is applicable to reporting periods beginning on or after 1 January 2013. The revised Standard introduces a single approach for the recognition and measurement of certain superannuation plans. Previously, a number of accounting options were permitted, including the ability to defer certain gains and losses to future periods. Under the revised AASB 119, all gains and losses will be recognised in the period in which they occur. Disclosure requirements have also been revised and now include disclosure of fair value information for plan assets, sensitivity analysis for major assumptions and descriptions of the risks associated with the plan.

2.20 In December 2011, the AASB released further proposals to update the financial reporting requirements for superannuation plans and approved deposit funds. These proposals would bring reporting by these entities more in line with reporting by other entities subject to Australian Accounting Standards. The AASB plans to issue a new standard by the end of 2012.

Income of not-for-profit entities

2.21 Since 2009, the AASB has had a project exploring alternatives to the current requirements for accounting for appropriations, taxes and grants, known collectively as non-exchange transactions. In February 2011, the AASB broadened the focus of the project to all types of revenue earned by not-for-profit entities and develop a standard to replace AASB 1004 *Contributions*. The new standard will be based on the IASB's work in developing an accounting standard on revenue from contracts with customers, with modifications where necessary to address issues specific to the not-for-profit sector.

2.22 Appropriations, taxes and grants are major transactions for many Australian Government entities and changes to the accounting standards could have a significant impact on the timing of revenue recognition by such entities. The AASB plans to issue an exposure draft of a new standard on income of not-for-profit entities in 2012.

GFS-GAAP harmonisation

2.23 Following a post-implementation review of AASB 1049 *whole of Government and General Government Sector Financial Reporting*, the AASB issued amendments to that Standard¹¹. The amendments include:

- confirming that financial reports are required for the General Government Sector (GGS)¹²;
- requiring GGS and whole of Government reports to be cross-referenced and released together;
- clarifying the requirements for presenting budget information in GGS and whole of Government reports; and
- requiring all measures of Government financial performance to be calculated in accordance with Australian Accounting Standards and to clearly identify those measures that do not meet the definition of key fiscal aggregates in AASB 1049.

2.24 The AASB has also progressed its project to consider the application of certain principles in AASB 1049 to the financial reports of not-for-profit entities within the GGS. In June 2011, the AASB released the following key proposals:

- entities to recognise and measure assets and liabilities in accordance with the Australian Bureau of Statistics' Manual on Government Finance Statistics (ABS GFS), where a choice is permitted under Australian Accounting Standards;
- presentation of financial information in line with ABS GFS, to the extent this does not conflict with Australian Accounting Standards. The content may be presented in the main financial statements or as supplementary note disclosure. Items controlled by the entity and those administered on behalf of Government would be presented side by side; and
- a comparison of the original budget with the outcome for the year, explaining major variances from the budget.

¹¹ AASB 2011-13 *Amendments to Australian Accounting Standard – Improvements to AASB 1049* was issued in December 2011. It applies to reporting periods beginning on or after 1 July 2012.

¹² Op cit (refer footnote 6 on pg. 19).

2.25 The AASB is currently considering stakeholder comments on these proposals.

Differential financial reporting - reduced disclosure requirements

2.26 The AASB has developed a differential financial reporting regime that provides an option for the majority of reporting entities to reduce their reporting burden. While the regime was legislated in late 2009–10, the relevant Standards do not come into effect until 2013–14.

2.27 The regime distinguishes two tiers of reporting requirements. Entities in the first tier must prepare financial statements in accordance with the full suite of Australian Accounting Standards. Federal, state and territory governments are included in this tier. Entities in the second tier will prepare similar financial statements, but with substantially reduced disclosure requirements.

2.28 Government controlled entities and universities may opt for either tier, subject to the requirements of their regulator. The differential reporting regime provides an opportunity to reduce the administrative workload of some Australian Government entities and make their financial reports easier to read, while preserving sufficient disclosures to satisfy the needs of the Parliament.

2.29 The Finance Minister, who performs the role of regulator for Australian Government entities, has yet to indicate whether Australian Government entities will be permitted to use the Reduced Disclosure Regime.

Carbon pricing

2.30 The fixed price phase of the Government's carbon pricing scheme commences on 1 July 2012. The AASB does not plan to introduce an Australian Accounting Standard or Interpretation on this issue. However, the staff of the AASB is preparing a paper on accounting for this scheme by both the private and public sectors.

International developments

Conceptual framework projects

2.31 AASB standards comprise mainly Australian equivalents to IFRS. The conceptual framework that underpins Australian Accounting Standards is also largely based on the IASB's conceptual framework.

2.32 The IASB conceptual framework is currently under review by the IASB in partnership with the United States Financial Accounting Standards Board (FASB). The conceptual framework project aims to update and refine the existing concepts to reflect the changes in markets, business practices and the economic environment that have occurred in the two or more decades since the concepts were first developed. Its overall objective is to create a sound foundation for future accounting standards that are principles-based, internally consistent and internationally converged.

2.33 To date, the IASB has finalised chapters dealing with the objective of general purpose financial reporting and the qualitative characteristics of useful financial information. The revised chapter on the objective of financial reporting states that the primary objective of financial statements is to provide information to assist investors, lenders and creditors in making decisions about providing resources to the entity. The other revised chapter states that the fundamental qualitative characteristics of financial reporting are relevance to decision-making and faithful representation of economic transactions and events. In addition, comparability, verifiability, timeliness and understandability are characteristics that enhance financial reporting, while not being themselves fundamental characteristics.

2.34 The AASB has decided that the revised framework will be applicable to all Australian reporting entities, although the project's primary focus is on for-profit entities. The AASB will add to the framework so that it can be applied by not-for-profit entities. It is only in the latter stages of the project that the IASB will consider the applicability of the framework to not-for-profit entities. In light of this, the International Public Sector Accounting Standards Board (IPSASB), in conjunction with the AASB and other national accounting standards boards, have embarked on a separate project for developing a public sector conceptual framework. IPSASB has to date released a range of consultation papers addressing: the objectives and scope of financial reporting; the qualitative characteristics of financial information; the nature of the reporting entity; the recognition and measurement of elements of the financial statements; and presentation in general purpose financial reports.

Long-term sustainability of public finances

2.35 The IPSASB has begun work on a framework for the reporting of information about the long-term fiscal sustainability of Government programs, other than those of Government Business Enterprises. This information would

complement that provided by traditional financial statements by facilitating an assessment of the future viability of Government programs.

2.36 In October 2011, the IPSASB issued recommended guidelines on this topic for public comment. The IPSASB is considering comments with the view to releasing practice guidelines.

Reporting service performance information

2.37 In October 2011, the IPSASB also released a consultation paper, setting out proposals for a framework for reporting of service performance information. Currently, there is considerable diversity between countries in how such information is reported.

2.38 The framework would adopt a principles-based approach to encourage consistent reporting of service performance by public sector entities. To achieve this, the framework proposes standardised service performance terminology and definitions, but does not mandate how an entity would present service performance information. The IPSASB is considering responses before progressing further the project.

Public-private partnerships

2.39 In September 2011, the IPSASB finalised an accounting standard dealing with accounting for Government involvement in public-private partnerships. The standard, IPSAS 32 *Service Concession Arrangements: Grantor*, takes effect from 1 January 2014. Its aim is to ensure governments report public-private partnership assets and their related financing. It also seeks to increase the consistency of public sector reporting of public-private partnerships, which are significant and often complex transactions.

2.40 The AASB is considering developing Australian guidance based on the IPSASB standard.

Financial instruments

2.41 The IASB is progressing a project to improve the usefulness of financial statements by simplifying the classification and measurement requirements for financial instruments. Measurement rules for financial assets will be considerably simplified and more financial assets are likely to be measured at current market values, rather than historical cost. Requirements for financial liabilities will be largely unchanged.

2.42 A new IASB Standard arising from this project was published in November 2009, and was given effect in Australia through AASB 9 *Financial Instruments*, applicable for reporting periods beginning on or after 1 January 2013. The IASB is now working on the requirements for writing down financial assets and for hedging transactions. These additional requirements are expected to be released for public comment later in 2012.

Leases

2.43 The IASB is conducting a project to develop a new approach to lease accounting that would ensure that all assets and liabilities arising under lease contracts are recognised in the balance sheet. Currently, many shorter-term leases are not shown as assets or liabilities on the balance sheet; instead, lease payments are expensed over the lease term. Under the proposals, entities with shorter-term leases, which will include many Australian Government entities, would record the present value of lease payments as assets on their balance sheets, together with corresponding liabilities.

2.44 The IASB is currently reviewing these proposals and expects to seek further public comment during the second half of 2012.

Revenue

2.45 The IASB is progressing a project to provide clearer principles on when revenue should be recognised from contracts with customers and how such revenue should be reported. These principles would apply to all contracts with customers except leases, financial instruments and insurance contracts.

2.46 The main objectives of this project are to:

- remove inconsistencies and weaknesses in existing revenue recognition standards by providing clear principles for revenue recognition in a robust framework;
- provide a single revenue recognition model which will improve comparability over a range of industries, companies and geographical boundaries; and
- simplify the preparation of financial statements by reducing the number of requirements.

2.47 The key principles on which the proposed model is based – revenue is recognised when goods or services are transferred to the customer, measured at transaction price – are generally consistent with current Australian practice.

2.48 The IASB expects to release a new standard during 2012–13.

Consolidation

2.49 In May 2011, the IASB released three accounting standards clarifying the requirements for the consolidation of subsidiaries and special purpose vehicles, and requiring the substance of joint arrangements to be disclosed. The changes are intended to give investors a clearer picture of the nature and extent of an entity's involvement with other entities. In August 2011, the AASB released three Australian Accounting Standards to replicate the IASB standards. These standards will not apply to the not-for-profit sector until the AASB has decided the required modifications for this sector. The AASB expects to release modifications to these standards in the second half of 2012.

2.50 In August 2011, the IASB also released proposals to change the consolidation rules for entities defined as 'investment entities'. Under the proposals, the financial results of such entities would not be consolidated with those of their parent entity. Instead, the parent entity would measure its holding in such entities at fair value, similar to other investments the parent entity might hold.

Legislative changes affecting the financial reporting framework

Changes to the *Financial Management and Accountability Act 1997 and Regulations*

2.51 The *Financial Framework Legislation Amendment Act (No. 1) 2012*¹³ (FFLA Act) amended FMA Act sections 26 and 27 relating to drawing rights. Prior to the amendment, a valid drawing right was required for a Minister or an official to make a payment, request an amount be debited against an appropriation or debit an amount against an appropriation. Following the passage of the amendment, a drawing right is only required for making a payment of public money or requesting an amount to be debited, or debiting an amount, against an appropriation under the *COAG Reform Fund Act 2008* or the *Nation-building Funds Act 2008*.

2.52 In addition, the FFLA Act removed the criminal penalty attached to FMA Act section 26, as other disciplinary arrangements or penalties exist in the

¹³ The *Financial Framework Legislation Amendment Act (No. 1) 2012* received Royal Assent on 4 April 2012.

FMA Act and other legislation,¹⁴ and the penalty attached to section 26 has never been used for a prosecution.

2.53 Other changes under the FFLA Act include:

- allowing the Finance Minister to exercise a discretion to 'set off' amounts owed to the Commonwealth with any amounts payable to the Commonwealth by the same person or entity. Some Commonwealth payments are excluded from this provision relating to social security payments and paid parental leave; and
- allowing determinations to establish Special Accounts at any future date.

2.54 Amendments to FMA Regulation 22C that took effect on 1 July 2011 have enhanced the role and broadened the functions of audit committees to support Chief Executives and agency management. In addition, the Act now requires Chief Executives, wherever practicable, to appoint at least one external member to the audit committee.

2.55 The *Financial Framework Legislation Amendment Act (No. 2) 2012* (FFLA (No. 2) 2012 Act) was introduced into the House of Representatives on 30 May 2012. The Bill, if enacted, would amend 21 Acts across six portfolios to regularise Commonwealth payments supported by special appropriations, including special accounts, consistent with the legislative requirements and section 83 of the Constitution.

Developments in auditing standards

2.56 Section 24 of the *Auditor-General Act 1997* requires the Auditor-General to set Auditing Standards with which persons performing ANAO audits must comply. The ANAO Auditing Standards establish mandatory requirements and provide explanatory guidance for persons performing the audit functions specified in section 24, including the statutory audits of the financial statements of Australian Government bodies. These standards incorporate, by reference, the current version of the Australian Auditing Standards made by the AUASB. As a result, financial statement audits conducted by the ANAO conform with the Standards that apply to the broader auditing profession in Australia.

¹⁴ Including the *Crimes Act 1914*, the *Criminal Code Act 1995* and the *Public Service Act 1999*.

2.57 The AUASB uses International Auditing Standards as the basis for the Australian Auditing Standards. ISAs are made by the International Auditing and Assurance Standards Board (IAASB), an independent standard setting board of the International Federation of Accountants (IFAC). In making its standards and guidance, the AUASB consults formally with organisations representing stakeholders, including users of financial statements, regulators and the accounting profession. The consultative processes are scheduled so that the AUASB can consider stakeholder views in making submissions on proposals from the IAASB.

2.58 In 2012, the AUASB issued a new Guidance Statement (GS) 020 *Special Considerations in Auditing Financial Instruments* that is based on its international equivalent and provides guidance about financial instruments and guidance on audit considerations relating to these instruments.

2.59 The AUASB has commenced a range of activities that relate to the audit of financial statements, including:

- a project, approved in February 2012, that involves working jointly with the Australian Institute of Company Directors and the Institute of Internal Auditors Australia to revise its 2008 guide, *Audit Committees: A Guide to Good Practice* to take account of significant developments relating to the role, responsibilities and operation of audit committees.
- development of a joint policy paper between the AUASB and the New Zealand Auditing and Assurance Standards Board (NZAuASB) regarding the harmonisation of AUASB and NZAuASB standards, which is expected to be finalised by June 2012.
- a project to revise the 2009 AUASB bulletin *Auditing Considerations in an Uncertain Economic Environment*. The revised bulletin will contrast the economic circumstances that existed in 2009 to those in 2012; and
- a revision of ASA 610 *Using the Work of Internal Auditors* in line with the changes to the equivalent international standard to provide a more robust framework for evaluating and using the work of an entity's internal audit function.

2.60 The AUASB will also continue to issue and revise existing guidance, particularly in relation to auditing grant acquittals, using the work of an actuary and investments in associates.

2.61 The IAASB's Strategy and Work Program for 2012–14 identifies a number of future directions in relation to the audit of financial statements, including:

- a focus on auditor reporting – IAASB has approved a project to revise ISA 700 *Forming an Opinion and Reporting on Financial Statements*, and other related ISAs. The project largely aims to improve the communicative value of auditor reporting and narrow the 'expectation gap' and 'information gap' to users of audited financial statements.
- continued work on audit quality – in December 2011 the IAASB considered comments received on the draft *Audit Quality Framework paper: An International Framework*. The IAASB will consider a revised draft of the consultation paper in 2012.
- financial statement disclosures – Consideration of the auditing implications of having disclosures in financial statements that are highly relevant and more detailed, but may be more subjective and less reliable. Such disclosures include disclosures of assumptions, models, alternative measurement bases and sources of estimation uncertainty. In January 2011, a discussion paper *The Evolving Nature of Financial Reporting: Disclosure and Its Audit Implications* was released for comment. In January 2012 the IAASB issued a Feedback Statement that summarises the comments received on the discussion paper.
- revising ISA 720 *The Auditor's Responsibility Relating to Other Information in Documents Containing Audited Financial Statements* to clarify the auditor's responsibilities in this area; and
- revising ISRE 2400 *Engagements to Review Historical Financial Statements* to better assist professional accountants in providing services to small and medium sized entities.

Conclusion

2.62 Ongoing developments in accounting and auditing frameworks and standards continue to have an impact on the financial reporting responsibilities of public sector entities and on the ANAO's auditing methodology. The ANAO continues to devote significant resources to the implementation of revised auditing and accounting requirements. Clients are also supported through client seminars and publications that explain new regulatory and accounting requirements.

2.63 In 2011–12, Australian and New Zealand accounting standards for for-profit entities were more closely aligned, as part of measures to promote greater integration between the two national economies. Other changes to Australian Accounting Standards in 2011–12 reflected international changes in accounting for financial instruments, related party transactions and financial instruments.

2.64 Looking to the future, further changes to the financial reporting framework are under development, both in Australia and internationally. A number of the proposed changes will affect the Australian public sector over the next few years particularly in relation to lease accounting, revenue recognition and the reporting of financial instruments.

3. Summary of Audit Findings and Related Issues

This chapter provides a summary of the ANAO's review of internal controls as part of the audit of the financial statements of major agencies. This includes a discussion of aspects of legislative compliance in relation to special appropriations, special accounts, investments and section 83 of the Constitution.

Introduction

3.1 The Chief Executives of General Government Sector entities subject to the FMA Act are required to prepare annual financial statements and present them to the Auditor-General for audit.¹⁵ For large entities, the audit is conducted in two main phases, interim and final. The interim phase focuses on an assessment of agencies' key internal controls; in the final audit phase the ANAO completes its assessment of the effectiveness of key controls for the full year, substantively tests material balances and disclosures in the financial statements, and finalises its audit opinion on the agencies' financial statements. This report focuses on the results of the interim audit phase of the 2011–12 financial statement audits of all portfolio departments and other major General Government Sector agencies that collectively represent some 95 per cent of total GGS revenues and expenses.

3.2 Chief Executives of FMA agencies are required to manage their affairs in a manner that promotes the efficient, effective, economical and ethical use of resources.¹⁶ This requires the development and implementation of effective corporate governance arrangements and internal controls designed to meet the individual circumstances of each entity and to assist in the orderly and efficient conduct of its business and compliance with applicable legislative requirements, including the preparation of annual financial statements that give a true and fair view.¹⁷

3.3 The overall objective of an audit of an agency's financial statements, as identified in the Australian Auditing Standards, is to form an opinion on

¹⁵ *Financial Management and Accountability (FMA) Act 1997.*

¹⁶ *FMA Act 1997*, section 44.

¹⁷ *FMA Act 1997*, section 49.

whether the financial statements, in all material¹⁸ respects, are in accordance with the Australian Government financial reporting framework.¹⁹ In planning the audit, audit procedures are designed to achieve reasonable assurance that the financial statements taken as a whole are free from material misstatement, whether due to fraud or error. The auditor is concerned with material misstatements, and is not responsible for the detection of misstatements that are not material to the financial statements taken as a whole.²⁰

3.4 A central component of the ANAO's financial statement audit methodology, and the focus of the interim phase of our financial statement audits, is a sound understanding of the agency and its environment, including its internal controls, as they relate to the preparation of the financial statements. This enables the ANAO to make a preliminary assessment of the risk of material misstatement in an entity's financial statements and to plan an audit approach to reduce audit risk to an acceptable level. The ANAO reviews and evaluates an agency's key internal controls to assess their capacity to prevent and detect errors that may result in a material misstatement of the financial statements. In doing so, the ANAO recognises that the reliability of business processes, accounting records and financial systems can be enhanced through effective internal controls, and this influences the timing and extent of audit work required. The auditor's understanding of the agency, its environment and its internal controls, helps the auditor design the work needed and respond to significant risks that bear on financial reporting.²¹ Broad areas of audit focus determined as a result of this planning approach are discussed in Chapter 5 for each agency covered by this report.

3.5 In accordance with generally accepted audit practice, the ANAO accepts a low level of risk that the audit procedures will fail to detect that the financial statements are materially misstated. This low level of risk is accepted because it is too costly to perform an audit that is predicated on no level of risk. Specific audit procedures are performed to ensure that the risk accepted is low. These procedures include, for example, obtaining knowledge of the entity

¹⁸ *AASB 1031 Materiality* states that information is material if its omission, misstatement or non-disclosure has the potential, individually or collectively, to influence the economic decisions of users taken on the basis of the financial statements or affect the discharge of accountability by the management or governing body of the entity.

¹⁹ The key elements of this framework are set out in Appendix 2.

²⁰ *ASA 200 Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with Australian Auditing Standards*, paragraph 6.

²¹ Significant risks are those risks of material misstatement of the financial statements that, in the auditor's judgement, require special audit consideration.

and its environment, reviewing the operation of internal controls, undertaking analytical reviews, testing a sample of transactions and account balances, and confirming year-end balances with third parties.

Internal control

3.6 The ANAO uses the framework in ASA 315 *Identifying and Assessing the Risks of Material Misstatement through Understanding the Entity and its Environment* to consider the impact of different elements of an entity's internal controls on the design and conduct of an audit. These elements, as detailed in ASA 315, are:

- control environment;
- agency risk assessment process;
- the information system, including the related business processes, relevant to financial reporting, and communication;
- control activities relevant to the audit; and
- monitoring of controls.

3.7 This chapter discusses each of these elements and outlines our observations in relation to each one, based on our review of relevant aspects of each agency's control environment and the results of our interim audits. As such it includes, where relevant, summary comments on Category A, B, C and L1 audit findings.²²

Control environment

3.8 An entity's business and operations influence the control environment, which needs to be carefully reviewed as part of the audit process when assessing the risk of material misstatement in financial systems and reports. ASA 315 at paragraph A69 states:

The control environment includes the governance and management functions and the attitudes, awareness, and actions of those charged with governance and management concerning the entity's internal control and its importance in the entity. The

²² Category A findings are significant audit issues. Category B findings are moderate audit issues, Category C findings are minor audit issues and Category L1 findings are instances of non-compliance with key legislative requirements. These categories are explained in Chapter 5, page 93.

control environment sets the tone of an organisation, influencing the control consciousness of its people.

3.9 In conducting an audit of an entity's financial statements, the ANAO focuses on specific elements of the control environment. In doing this, the ANAO establishes whether the environment in place comprises elements that contribute positively to establishing a foundation for effective internal control, and whether it minimises both financial and non-financial risks to the entity. This judgement has a major influence on the way that the audit is conducted, including the amount of audit work needed to form the audit opinion. Generally, the main elements reviewed are:

- **governance arrangements**—including the framework within which an agency's activities for achieving its objectives are planned, executed, controlled and reviewed;
- **audit committee arrangements**—including the assurance and performance role of the audit committee, its use as a forum for communication between management and internal and external auditors, and the degree of independence and expertise of the committee;
- **assurance arrangements**—including the internal audit function and quality assurance systems and processes;
- **systems of authorisation, recording and procedures**—designed to ensure that transactions are processed, recorded and accounted for correctly, including the assignment of appropriate authority and that responsibilities and compliance arrangements accord with applicable legislative requirements; and
- **a financial performance management regime**—that involves the preparation of financial reports, including comparison of actual results to budgets, variance analysis and relevant commentary to provide assurance about the financial performance of the agency.

3.10 The ongoing performance and effectiveness of these measures can make a significant contribution to the level of assurance that agency management and, in turn, the ANAO obtains for financial statement purposes.

Observations

3.11 Agencies have governance arrangements in place to provide direction, guidance and control over the financial management of their organisations.²³ Executive management committees met regularly to plan and monitor strategic direction and performance. Agencies had produced a corporate plan or similar document that outlines the agency's goals and objectives, and thereby facilitate measuring agencies' progress in meeting them. Chief Executives, their senior management group, and audit or risk committees continued to give attention to financial management and audit matters, risk management and performance outcomes.

3.12 Agencies have mature audit committee arrangements. These include a formal charter that outlines each committee's composition, roles, responsibilities and reporting lines, and processes for the regular reporting to the Chief Executive and the periodic self-assessment of performance. To provide guidance to agencies on the composition and role of the audit committee, the ANAO issued a Better Practice Guide *Public Sector Audit Committees* in August 2011. The ANAO observed that generally, agencies have updated their formal charter to incorporate the ANAO's recommended best practice.

3.13 The ANAO observed that agencies review their Chief Executive's Instructions (CEIs) periodically, with the objective of ensuring that they remain relevant. In addition, delegations and authorisations were regularly reviewed and updated.

3.14 Consistent with previous years, consideration of the financial position regarding current and future operations is included on the agenda of agencies' executive management meetings. These meetings are usually held monthly, but some agencies have weekly and fortnightly meetings. Financial performance reports to agencies' executives included budget forecasts and commentary on performance. The financial information provided to the agencies' executives was generally supplemented by non-financial operational information, to provide a balanced view of performance.

²³ As noted at paragraph 5.252, DHS continues to refine certain elements of its governance arrangements following the integration of Medicare Australia and Centrelink into the department on 1 July 2011.

Legislative compliance

3.15 The financial framework for the Australian Government agencies included in this report is established by the FMA Act and its subsidiary legislation. The key feature of the framework is that the Chief Executive of each agency is responsible for the financial management of their agency, including compliance with applicable laws and associated policies.

3.16 In reviewing an agency's control environment, the ANAO assesses whether management has established adequate controls to enable the agency to comply with key aspects of the FMA Act.

3.17 In more recent years, the ANAO has increased its focus on legislative compliance as part of its financial statement audit coverage. This recognises the importance of the authority that the Parliament has conveyed to the executive Government in relation to these arrangements and the concerns expressed by the JCPAA in the past in relation to legislative compliance by agencies.

3.18 The coverage by the ANAO involves assessing key aspects of legislative compliance in relation to annual appropriations, special appropriations, special accounts and the investment of public monies. Audit testing includes confirming the presence of key documents or authorities, and testing of relevant transactions directed at obtaining reasonable assurance about agencies' compliance with these key components of the financial management framework. ANAO audits also review the results of compliance self-assessment and processes and other reviews undertaken in the context of agencies' Certificate of Compliance responsibilities that involve the annual reporting to the Finance Minister of any known breaches of the financial management framework.

Observations

3.19 As in previous years, overall, the ANAO identified a high level of compliance in these areas, except in respect of potential or actual breaches of section 83 of the Constitution, which is discussed at paragraphs 3.37 to 3.46 below.

3.20 The 2011–12 interim audits identified that, generally, agencies continue to maintain listings of the laws, regulations and associated Government policies that are relevant to their responsibilities. Agencies also have well-established processes in place to obtain assurance from line managers

regarding compliance with relevant legislative requirements to enable Chief Executives to provide an annual Certificate of Compliance to their Minister.

3.21 Generally, audit committees are responsible for reviewing the effectiveness of legislative compliance arrangements, particularly in relation to financial management requirements. The internal audit function often assists with the monitoring of these arrangements.

3.22 Agencies also have established a variety of mechanisms to communicate the importance of compliance with legislation through documents such as Chief Executive Instructions, corporate plans, fraud control plans and delegation instruments, as well as through the conduct of targeted training and induction courses.

3.23 The Certificate of Compliance process for FMA Act agencies was introduced in 2006–07 to improve compliance with the Australian Government’s financial management framework and to ensure that Ministers are kept informed of compliance issues within their portfolios. Through the Certificate, agency Chief Executives certify to their Portfolio Minister the agency’s compliance with the components of the Government’s financial management framework for the previous financial year.

3.24 The Certificate requirement that Chief Executives sign-off on compliance with the financial management framework and report identified instances of non-compliance has heightened the focus of agencies on compliance.

3.25 As part of the 2011–12 interim audit the ANAO undertook a high level analysis of agencies’ special appropriations, special accounts and the investment of public monies. The ANAO also reviewed agencies’ progress in undertaking assessments of the risk of breaches of section 83 of the Constitution.

Special appropriations

3.26 A special appropriation is an appropriation that is contained in an Act (other than those in the Annual Appropriation Acts) which appropriates money from the Consolidated Revenue Fund (CRF) for a particular purpose, for example, to finance a particular project or to make social security payments. A special appropriation is included in a specific Act when it is to

provide a payment where an entitlement exists, or a payment of a specified amount is separately identified from an annual appropriation Bill.²⁴

3.27 As at 30 June 2011, agencies covered by this report were responsible for managing approximately 250 special appropriations, with payments in 2010–11 totalling in excess of \$400 billion²⁵. This represented in excess of 80 per cent of all Australian Government expenditure in 2010–11.

3.28 The large majority of the special appropriations are managed by the Treasury and the Department of Finance and Deregulation. The larger special appropriations generally relate to providing financial assistance to the states and territories, pension payments, Parliamentary entitlements and social security and family assistance payments.

3.29 Of the total number of special appropriations as at 30 June 2011 a large number had not been used during 2010–11. The nature of some special appropriations means that they will be used periodically and therefore it is not unusual for some not to be used in any one financial year. The ANAO is also aware that a number of agencies have been reviewing whether there is an ongoing need to maintain particular special appropriations and have taken action to have relevant legislative provisions repealed, where this is warranted. The ANAO encourages agencies to periodically review the ongoing requirement for the special appropriations for which they are responsible.

Special accounts

3.30 A special account is an appropriation mechanism that notionally sets aside an amount with the CRF to be expended for specific purposes. A special account can be established either by a Finance Minister's Determination under section 20 of the FMA Act, or by enabling legislation as recognised under section 21 of the FMA Act. The appropriation authority to draw money from the Consolidated Revenue Fund is either section 20 or 21 of the FMA Act.

3.31 Special accounts may be established when it is clear that other types of appropriations are not suitable. For example, there may be a need for increased transparency, including where activities are jointly funded with other governments. They may also be used for public money that is not held on account of the Commonwealth.²⁶

²⁴ See Budget Paper No. 4 2011–12 *Agency Resourcing*, May 2011.

²⁵ Based on information disclosed in agencies' 2010–11 financial statements.

²⁶ Op cit (refer footnote 24 on pg. 44).

3.32 There were approximately 125 special accounts reported in the 2010–11 financial statements of major agencies, with a combined balance in excess of \$3 billion as at 30 June 2011. During 2010–11, \$83 billion was reported as being credited to special accounts and \$80 billion was paid from these accounts.²⁷ Over time, while there has been a decrease in the number of special accounts, there has been a significant increase in the volume of transactions processed through special accounts as illustrated by the fact that approximately 180 special accounts were reported by major agencies as at 30 June 2003 with a balance of \$2 billion. In 2002–03, \$10.33 billion was credited to special accounts and payments of \$10.06 billion were made.²⁸

3.33 The majority of the 125 special accounts are administered by the departments of Health and Ageing, FaHCSIA and DSEWPaC.

3.34 Approximately 16 per cent (20) of special accounts were dormant in 2010–11, with these accounts not recording any transactions during 2010–11. As is the case with special appropriations, some special accounts are used periodically. Nevertheless, agencies are encouraged to regularly review the need for the special accounts for which they are responsible.

Investments

3.35 In 2010–11, five departments invested public money pursuant to section 39 of the FMA Act under a delegation by the Finance Minister. These are the departments of: Agriculture, Fisheries and Forestry; Families, Housing, Community Services and Indigenous Affairs; Veterans' Affairs and Resources, Energy and Tourism. The Australian Office of Financial Management (AOFM) also makes investments under a delegation from the Treasurer. As at 30 June 2011, the amount invested by these agencies totalled in excess of \$299 billion, with approximately 99 per cent being made by AOFM.

3.36 AOFM has responsibility for investing moneys in the central treasury of the Commonwealth. In other cases, agencies may be delegated the authority to invest public moneys in circumstances where an agency is required to undertake investment activities, such as in implementing a Government policy intention or where investment activities form part of a Commonwealth agreement with an external entity.

²⁷ Op cit (refer footnote 24 on pg. 44).

²⁸ See ANAO Audit Report No. 24 2003–2004 *Agency Management of Special Accounts*.

Section 83 of the Constitution

3.37 Section 83 of the Constitution provides that no money shall be drawn from the Treasury of the Commonwealth except under appropriation made by law. The effect of section 83 is that all spending by the Executive Government from the CRF must be in accordance with an authority given by the Parliament. Breaches of section 83 can occur when conditions are legislated by the Parliament are not met before payments are made from special appropriations and special accounts. In these circumstances the payments may be made without a valid appropriation. This includes situations where an administrative error such as a duplicate payment occurs, even if the overpayment is able to be recovered.

3.38 Potential breaches can take many forms, including:

- a payment or overpayment made as a result of an error, including payments made based on incorrect or inaccurate information used in assessing payment eligibility; or
- a payment made despite certain legislative preconditions, such as those that regulate an entitlement to a payment, not being fulfilled.

3.39 As reported in Audit Report No. 17 2011–12, *Audits of the Financial Statements of Australian Government Entities for the Period Ended 30 June 2011*, the 2010–11 financial statements of 48 agencies, including 20 of the major agencies covered by this report, included a reference to a risk of a breach of section 83 of the Constitution or the need to undertake a risk assessment in relation to payments from special appropriations and special accounts. The auditors' reports on the financial statements of these agencies contained a report on other legal and regulatory requirements²⁹ which drew attention to these disclosures, including proposed follow up action.

3.40 In March 2012, following a comprehensive consultation process involving agencies and the ANAO, the Department of Finance and Deregulation finalised guidance to agencies on how to approach a review of payments made from appropriations. Draft guidance had been issued by Finance in December 2011 to allow agencies to commence their risk assessments. The guidance paper: provided details of potential breaches of section 83; outlined a risk management approach for identifying potential

²⁹ A report on other legal and regulatory requirements is a separate part of the auditor's report on the financial statements and does not affect the auditor's opinion on the truth and fairness of the financial statements.

section 83 breaches; and outlined the approach for implementing remedial action where an agency has assessed the risk of breaches of section 83 as either medium or high.

3.41 As part of the 2011–12 interim audit phase, the ANAO reviewed progress made by agencies in assessing the risk of breaches of section 83 of the Constitution. The guidance indicates that agencies should endeavour to complete the risk assessment process and the implementation of remedial action in 2011–12, to the extent reasonably practicable, noting that this timetable would facilitate review by the agency's audit committee, and ANAO verification of the financial statement note disclosure.

3.42 As at 31 May 2012, 13 major agencies had informed the ANAO that they had completed their initial risk assessment of the risk of breach of section 83 of the Constitution in relation to payments from special appropriations and special accounts. In most cases these agencies have responsibility for managing a small number of special appropriations and/or special accounts and the risk of a breach of section 83 has been assessed as low. A small number of agencies had sought, or were intending to seek, legal advice in respect of particular payments that could potentially involve a breach of section 83 of the Constitution. In the remaining 12 major agencies risk assessments were in progress. The risk assessments undertaken to date in a number of agencies have identified a range of payments from special appropriation and special accounts that are at risk of being in breach of section 83 of the Constitution. A number of these agencies were also in the process of obtaining legal advice in relation to these payments. Details of all confirmed breaches of section 83 of the Constitution are required to be disclosed in agencies' 2011–12 financial statements.

3.43 In addition, as reported in Audit Report No. 17 2011–12, certain payments by the Australian Taxation Office and the Department of the Treasury resulted in breaches of section 83 of the Constitution. Similar breaches have occurred in the ATO in 2011–12 and there is a high risk that similar breaches have occurred in the Treasury in 2011–12. Further discussion of this matter is included in the results of the ANAO's 2011–12 interim audit phase for each agency, outlined in Chapter 5 of this report.

3.44 Agency audit committees were generally taking an active interest in agencies' action to address this matter, consistent with committees' responsibilities in relation to agencies' risk management frameworks and legislative compliance. The ANAO is progressively reviewing agencies'

completed risk assessments and is maintaining an ongoing dialogue with agency CFOs and audit committees in the context of our responsibilities for the audit of agencies' 2011–12 financial statements.

3.45 As mentioned above, section 83 of the Constitution underpins Parliamentary control over expenditure by the Executive. As such, it is important that all agencies ensure that they complete, consistent with Finance guidelines, a self-assessment supported as necessary by legal advice, to: firstly assess the risk of breaches of section 83 of the Constitution; and secondly to address situations where this risk is assessed as medium or high. This process should be subject to review by agency audit committees. Agencies that have yet to complete their self-assessments are encouraged to do so as early as possible in view of the significance of this issue.

3.46 In response to a range of circumstances that could lead to section 83 being breached, the Government introduced the *Financial Framework Legislation Amendment Bill (No.2) 2012* into the House of Representatives on 30 May 2012. The Explanatory Memorandum to the Bill indicates that the Bill would, if enacted, amend 21 Acts across six portfolios to regularise Commonwealth payments supported by special appropriations, including special accounts, consistent with legislative requirements and section 83 of the Constitution.

3.47 Separately, a case before the High Court of Australia, at the time of preparation of this report, could have implications for the Australian Government's interpretation of section 83 of the Constitution.³⁰

Agency risk assessment process

3.48 An understanding of an agency's risk assessment process is essential to an effective and efficient financial statement audit. The ANAO reviews how agencies identify risks relevant to their financial statements, how these risks are managed and considers the risk of material misstatement of an agency's financial statements.

3.49 The ANAO found that most agencies have well established arrangements in place that involve developing and updating risk management plans at the organisational and work area levels. Oversight of the process is provided by the agency's audit committee or a separate committee with specific responsibility for risk management.

³⁰ The *Williams v Commonwealth* case involves consideration of the validity of payments relating to the National School Chaplaincy Program.

3.50 Two common elements of agencies' risk management frameworks that the ANAO reviews as part of its interim audits are business continuity management and fraud control management.

Business Continuity Management

3.51 Business continuity management (BCM) is an essential business practice and an integral component of effective public sector governance. It is a unified process encompassing both business and management disciplines to provide resilience to business processes.

3.52 BCM involves the development, implementation, and maintenance of those policies, frameworks and procedures to assist an agency manage a business disruption. This capability assists in managing, and recovering from the impacts of a disruptive event.

3.53 Defining the approach to preventing and managing a break in business operations is a major role of BCM, requiring non-routine management practices. BCM involves designing business processes and information architecture to limit points of failure, and developing contingency procedures and the steps the agency will take to recover and return to normality. It also includes defining escalation protocols, and obtaining contact details for key personnel and other entities where an important interdependency exists.

3.54 There are two key elements to BCM, supported by a number of activities that interrelate to identify, analyse, and treat continuity risks and deal with the consequences should preventative treatments fail. The two elements are a:

- Business Continuity Plan (BCP)—a collection of procedures and information for maintaining service delivery, that is developed, compiled and maintained in readiness for use in a business disruption event; and
- IT Disaster Recovery Plan (DRP)—the mechanism for recovering computer systems and associated infrastructure following a disruption to services, in line with the needs of the entity.

Observations

3.55 Planning for business continuity continues to be essential in underpinning an agency's ability to maintain key business functions and deliver services. As part of the interim phase of our 2011–12 financial statement

audits, and in line with past practice, the ANAO assessed key BCM control activities in the context of an agency’s ability to recover its key financial information that supports the financial statements in the event of a disruption to the key financial systems. The summarised results of our review of BCM controls for the three years 2009–10 to 2011–12 are illustrated in Figures 3.1 and 3.2 below.

Figure 3.1

Assessment of business continuity controls: 2009–10 to 2011–12

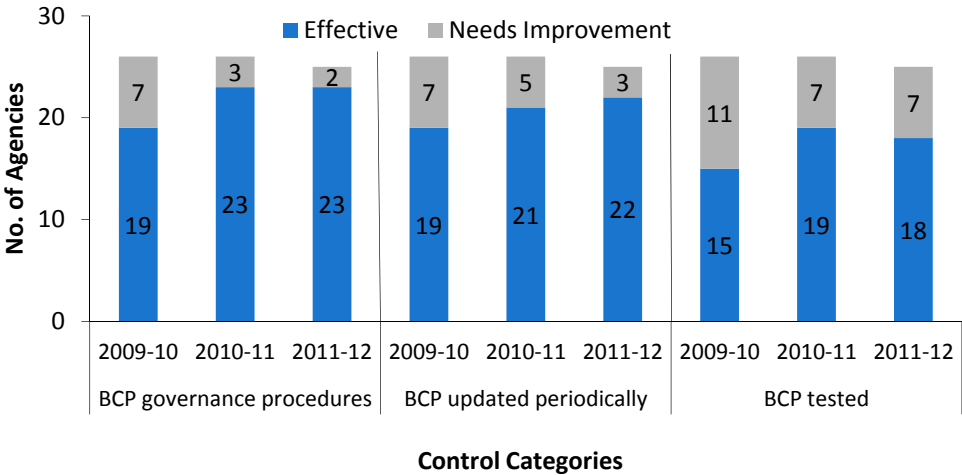
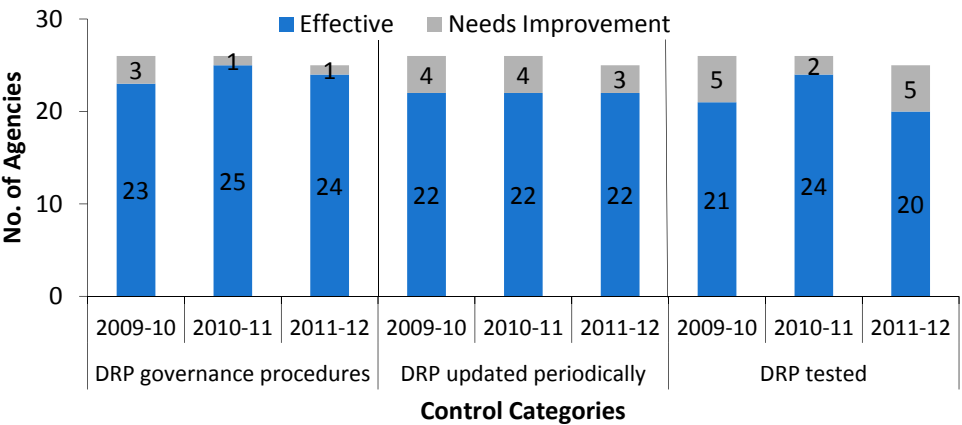


Figure 3.2

Assessment of disaster recovery controls: 2009–10 to 2011–12



3.56 As illustrated in Figures 3.1 and 3.2, our audits identified a general awareness and maintenance of business continuity and disaster recovery controls. However, seven of 25 agencies did not test BCPs as part of normal business practice. This is the same as the position in 2010–11, and indicates that further attention by some agencies to this matter is required. The absence of a properly tested BCP has the potential to put at risk an agency's capacity to deal effectively with a disruptive event.

3.57 Agencies are also addressing the need to establish effective governance procedures in relation to BCPs and DRPs, with almost all agencies achieving a high level of governance. However, three of 25 agencies had not implemented arrangements for the regular updating of BCPs, and the same number of agencies had not implemented arrangements for the regular updating of DRPs. As mentioned above, seven agencies had not implemented arrangements to test BCPs, and five of 25 agencies had not implemented a DRP testing process, a decline in control effectiveness compared to 2010–11.

3.58 Agencies that are not regularly testing their BCP and DRP are not well placed to identify aspects of their plans that require attention, or to integrate lessons learned into revised and updated plans. Regular testing of the operation of BCPs and DRPs assists agencies to establish and maintain appropriate training, effective recovery processes, and up to date BCP and DRP documentation.

3.59 Overall, our assessment of continuity management indicated agencies were aware of the importance of BCP and DRP to the continuing delivery of their services. However, some agencies have still not fully embedded into their normal business activities the establishment, maintenance, and testing of business continuity and recovery plans. These agencies face a continued risk of being unable to recover effectively from an event that disrupts their key financial systems and processes.

Fraud control management

3.60 *The Commonwealth Fraud Control Guidelines* (the Guidelines) outline the principles for fraud control within the Australian Government and set minimum standards to assist agencies in carrying out their responsibilities to combat fraud³¹ against their programs.

3.61 The importance of agencies establishing effective fraud control arrangements is recognised in section 45 of the FMA Act which specifies that Chief Executives must implement a fraud control plan for their agency. The Guidelines require agencies to conduct fraud risk assessments at least every two years. All agencies are required to provide the Australian Institute of Criminology (AIC) with fraud control information for its annual report on fraud against the Australian Government, and fraud control arrangements within Australian Government agencies. This report is titled the *Annual Report to Government: Fraud against the Commonwealth*.

3.62 The report is provided to Government to facilitate analysis of fraud and future policy development. Unaudited data provided to the AIC for the year ended 30 June 2011 showed that:

- the Australian Federal Police investigated 61 referrals of complex cases in 2010–11 and estimated the cost of fraud for these cases to be \$12.8 million;
- 1 746 defendants were referred to the Commonwealth Director of Public Prosecutions for prosecution and 3 152 defendants were prosecuted by the Commonwealth Director of Public Prosecutions; and
- during 2010–11, 2 615 convictions for fraud were achieved and there were 12 acquittals for fraud.

3.63 These results continue to highlight the risk of fraud and the importance of agencies effectively managing their fraud control responsibilities.

³¹ The *Commonwealth Fraud Control Guidelines* define fraud against the Commonwealth as 'dishonestly obtaining a benefit, or causing a loss, by deception or other means'. This definition includes (but is not limited to) theft; accounting fraud (false invoices, misappropriation etc); causing a loss, or avoiding and/or creating a liability; providing false or misleading information to the Commonwealth, or failing to provide information where there is an obligation to do so; misuse of Commonwealth assets, equipments or facilities; making, or using false, forged or falsified documents; wrongfully using Commonwealth information or intellectual property.

3.64 An explanation of an auditor's responsibility for preventing and detecting fraud is provided in Australian Auditing Standard ASA 240 *The Auditor's Responsibilities Relating to Fraud in an Audit of a Financial Report*, which notes in paragraph 4:

The primary responsibility for the prevention and detection of fraud rests with both those charged with governance of the entity and management.

3.65 In considering the risks of material misstatement in the financial statements due to fraud, ASA 240 requires that a number of audit procedures be undertaken. These include making enquiries of agencies regarding their risk assessment processes for identifying and responding to the risks of fraud and the internal controls that management has established to mitigate those risks.

3.66 As with risk management plans, fraud control plans need to be reviewed regularly and updated when significant changes to roles or functions occur, so that they reflect an agency's current fraud risk and control environment. There are benefits in agencies assessing their fraud risks as part of their risk management process.

Observations

3.67 ANAO enquiries, as part of the 2011–12 interim audits, identified that agencies continue to place importance on their adherence with the Guidelines, with fraud control planning being well established in most agencies. The development and updating of fraud control plans is, nevertheless, an area that continues to require attention by a small number of agencies.

Information systems

3.68 In all agencies, information systems are used extensively for financial management and reporting, as well as for human resource management processes. As a consequence, the review of these information systems and their related controls forms a significant part of the ANAO audit examination of internal controls. Information system controls include agency-wide general controls that establish an agency's IT infrastructures, policies and procedures, together with specific application controls that validate, authorise, monitor and report financial and human resource transactions.

Observations

3.69 The ANAO observed that the majority of agencies had effective IT general controls and IT application controls that support the preparation of agencies' financial statements. A detailed commentary on the results of the ANAO's review of information systems that underpin the financial transactions processing within major Australian Government agencies is provided in Chapter 4.

Control activities

3.70 Australian Auditing Standard ASA 315 at paragraph A88 states:

Control activities are the policies and procedures that help ensure that management directives are carried out.

3.71 The auditor is required to obtain an understanding of control activities relevant to the audit, being those that the auditor considers it is necessary to understand in order to assess the risks of material misstatement. Further audit procedures responsive to these risks then need to be designed.

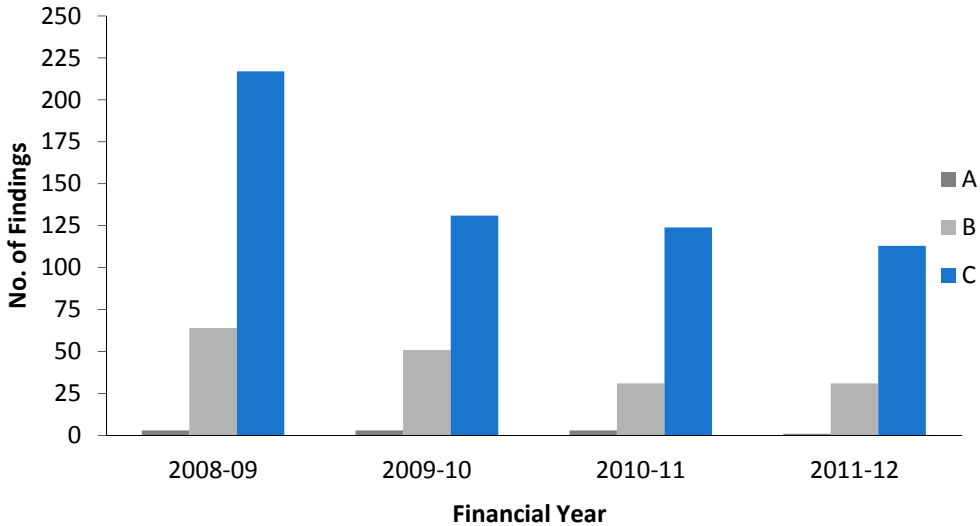
3.72 To illustrate trends in audit findings over time, aggregate details of Category A, B and C findings³² over the last four years have been grouped into the following categories:

- IT control environment;
- purchases and payables;
- grant accounting;
- accounting and control of non-financial assets;
- revenues, receivables and cash management;
- human resource management processes; and
- other control matters.

Aggregate audit findings

3.73 Aggregate audit findings for the last four years are outlined in Figure 3.3 below.

³² These categories are described at paragraph 5.7 of this report.

Figure 3.3**Aggregate audit findings – categories A, B and C**

Note: There is one Category A finding in 2011–12.

3.74 Over the last four years the ANAO's interim audits have identified 772 audit findings. There has been a progressive reduction in the total number of findings over this period with the majority (76 per cent) of findings being Category C findings. The number of Category A and B findings has decreased from 34 in 2010–11 to 32 in 2011–12. Category C findings have also reduced from 124 in 2010–11 to 113 in 2011–12. The general reduction in findings is reflected in the analysis of findings by category outlined below.

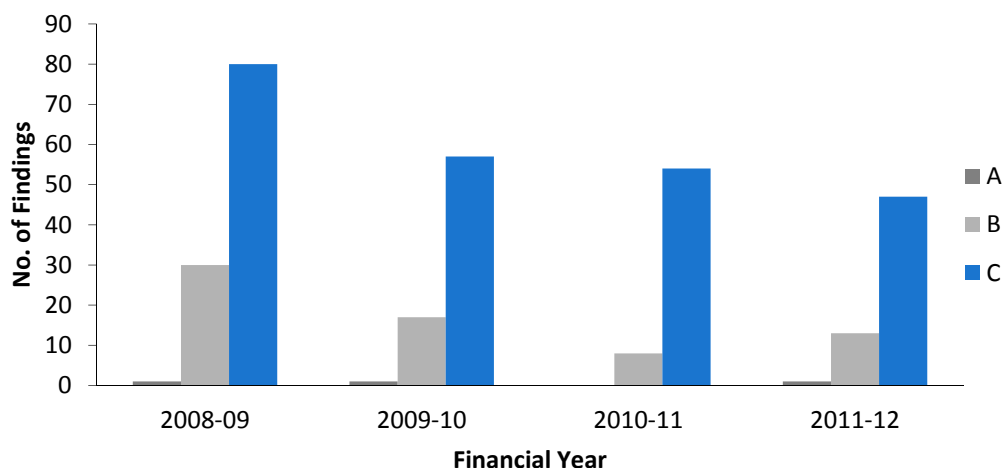
IT control environment

3.75 As mentioned above, the review of information systems and their related controls are an integral part of an agency's internal control environment. The main components reviewed are: IT general controls that encompass an agency's IT infrastructure, policies, procedures and standards that support accounting and business processes; and IT application controls that validate, authorise, monitor and report financial and human resource transactions.

3.76 The number of audit findings over the last four years are outlined in Figure 3.4 below.

Figure 3.4

IT control environment – aggregate audit findings



3.77 Findings in relation to agencies' IT control environments represent 40 per cent of all findings, with 309 findings in total over four years. The ANAO observed an overall improvement in the management of IT controls over the past four years, although the number of category A and B findings has increased in 2011–12 compared with 2010–11.

3.78 Common issues noted over the four years include controls to manage IT incidents and problem management, the regular review and updating of change management processes and segregation of duties within IT systems. Areas where our 2011–12 interim audits have identified the need for improvement are HRMIS business continuity, and the logging and monitoring of user activities for FMIS and HRMIS privileged users.

3.79 A detailed commentary on the results of the ANAO's review of information systems that underpin the financial transactions processing within major Australian Government agencies is provided in Chapter 4.

Purchases and payables

3.80 The main component of purchases and payables is payments to suppliers, including contractor and consultancy expenses, lease payments and general administrative and utility payments. Payments to suppliers generally represent a significant percentage of total departmental expenses incurred by agencies.

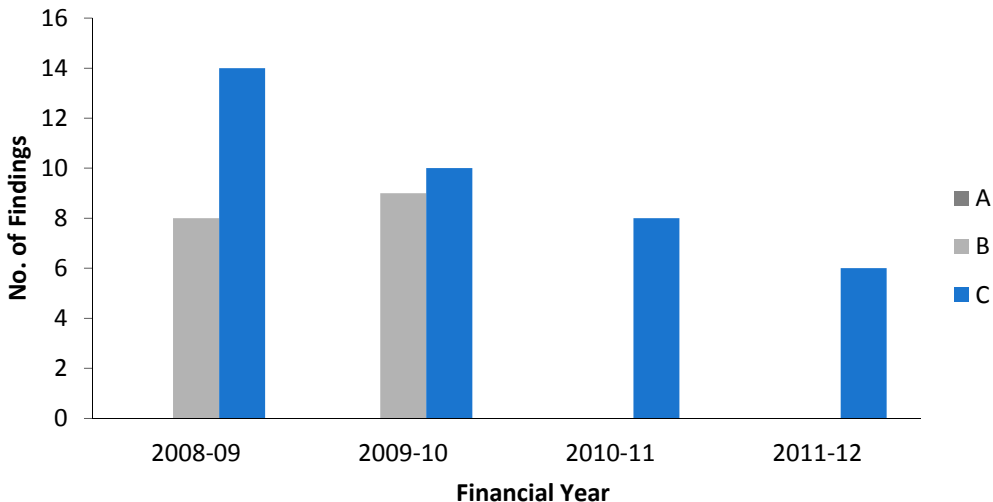
3.81 In 2010–11, the Consolidated Financial Statements (CFS) reported total expenses for the payments of goods and services of \$73.0 billion.

3.82 The main controls over purchases and payables which are given particular focus in our interim audits include: approval of the commitment and expenditure of public monies in accordance with delegations and authorisations; segregation of duties; controls to prevent duplicate payments; reconciliations between the general ledger and subsidiary accounts; and controls over credit card expenditure.

3.83 The number of audit findings over the last four years are outlined in Figure 3.5 below.

Figure 3.5

Purchases and payables – aggregate audit findings



3.84 Over the last four years, agencies' controls over purchases and payables subject to audit review have been generally effective with a relatively small number of audit findings, representing some seven per cent of total audit findings. The results of our 2011–12 interim audits indicate that a number of issues identified in previous audits have been addressed by agencies. These include: a lack of reconciliations of the general ledger with other accounts or key systems; inadequate segregation of duties; inadequate controls designed to prevent duplicate payments; weaknesses in controls designed to ensure the appropriate approval of the payment of public moneys; and lack of controls over credit card expenditure have been addressed by agencies.

Grant accounting

3.85 Many agencies administer grant programs that involve the provision of funds to eligible recipients in accordance with legislative and policy requirements. Grant recipients include state and local governments and community organisations.

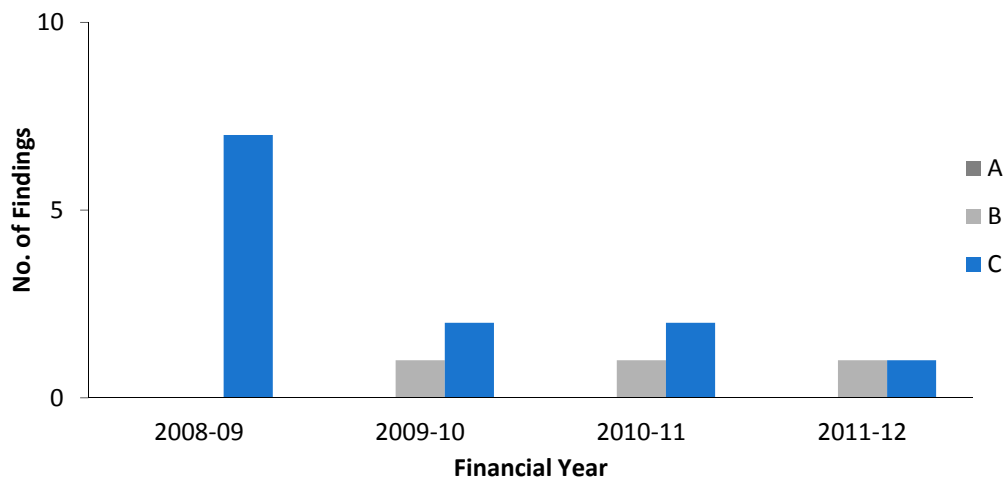
3.86 The main controls over the accounting of grant expenditure include: approval of the commitment and expenditure of grants to eligible recipients; the payment of grants in accordance with funding agreements; and controls over grant acquittals. Our interim audit work reviewed these control areas.

3.87 In 2010–11, the Consolidated Financial Statements reported total grant expenditure of \$124.3 billion.

3.88 The number of audit findings over the last four years are outlined in Figure 3.6 below.

Figure 3.6

Grant accounting – aggregate audit findings



3.89 Agencies’ controls over the payment of grants have been generally effective, with a very small number of audit findings representing some two per cent of total audit findings.

3.90 Audits of the general administration and the effectiveness of grant programs by agencies are included in the ANAO’s performance audit program. These audits generally include: assessment of processes by which

grant applications are sought, received and assessed; the processes for the development and management of funding agreements with grant recipients; and how agencies assess and monitor the achievement of project and program outcomes. Our performance audits continue to identify the need for an improvement in a number of aspects of the administration of grants by agencies, including the assessment and approval of grant applications and the management of funding agreements³³.

Accounting and control of non-financial assets

3.91 The accounting and control of non-financial assets represents an important aspect of agencies' financial management responsibilities. Agencies control a diverse range of non-financial assets on behalf of the Commonwealth, with the main classes of assets being land and buildings, leasehold improvements, infrastructure plant and equipment, inventories and internally developed software.

3.92 In 2010–11, the Consolidated Financial Statements reported total non-financial assets of some \$115.0 billion.

3.93 The main controls over assets that are given particular focus in our interim audits include: the approval of the commitment and expenditure of public monies in accordance with authorisations and delegations; reconciliations between the general ledger and subsidiary asset accounts; the maintenance of a reliable asset register that includes information about assets acquired, disposed of, and asset locations; physical security over assets including asset identification numbers; the appropriateness of depreciation rates and useful lives; approval of, and the accounting for, the disposal of

³³ In the current financial year, the ANAO tabled the following audits that addressed aspects of the administration of grants:

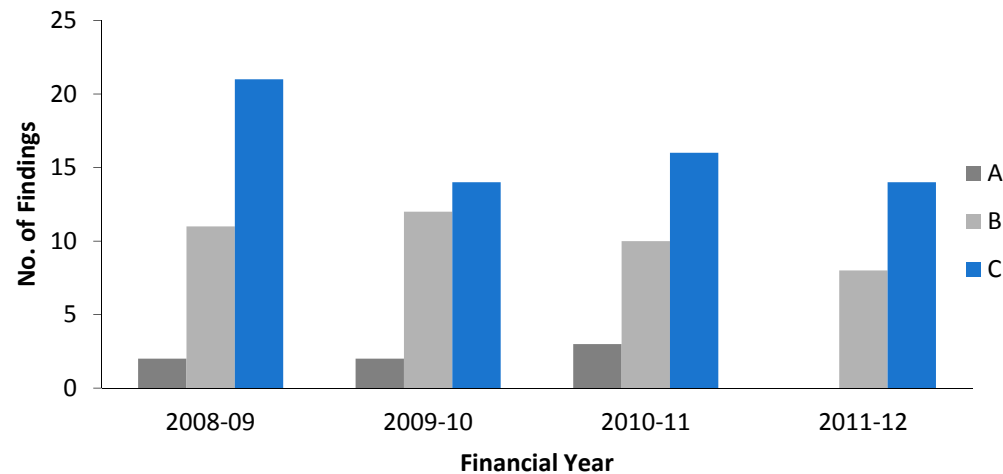
- ANAO Audit Report No.6 2011–12 *Fair Work Education and Information Program*;
- ANAO Audit Report No.7 2011–12 *Establishment, Implementation and Administration of the Infrastructure Employment projects Stream of the Jobs Fund*;
- ANAO Audit Report No.11 2011–12 *Implementation and Management of the Housing Affordability Fund*;
- ANAO Audit Report No.21 2011–12 *Administration of Grant Reporting Obligations*;
- ANAO Audit Report No.26 2011–12 *Capacity Development for Indigenous Service Delivery*
- ANAO Audit Report No.35 2011–12 *Indigenous Early Childhood Development. New Directions: Mothers and Babies Services*;
- ANAO Audit Report No.36 2011–12 *Development and Approval of Grant Program Guidelines*; and
- ANAO Audit Report No.44 2011–12 *Administration of the Primary Care Infrastructure Grants Program*.

assets; and the periodic conduct of stocktakes. The valuation of assets is covered as part of our final audits.

3.94 The number of audit findings over the last four years are outlined in Figure 3.7 below.

Figure 3.7

Accounting and control of non-financial assets – aggregate audit findings



3.95 Over the last four years there have been 113 audit findings relating to the accounting and control of non-financial assets, representing approximately 15 per cent of the total number of audit findings. The results of our 2011–12 interim audits indicate that a number of issues identified in previous audits have been addressed by agencies. These include: timely reconciliations between agencies’ asset registers and agencies’ financial systems; issues around the capitalisation and disposals of assets; the classification of assets between asset classes; the inconsistent application and a lack of clarity in policies and procedures relating to stocktakes; and the absence of a consistent policy on the useful life of assets.

Revenue, receivables and cash management

3.96 The main components of revenue and receivables consist of Parliamentary appropriations, taxation revenue, customs and excise duties and administered levies. Other revenue is also generated by agencies from the sale of goods and services and a range of other sources including from interest

earned from cash funds on deposit. Cash management involves the collection and receipt of public monies and the management of official bank accounts.

3.97 In 2010–11, the Consolidated Financial Statements reported total taxation revenues of \$288.8 billion, and non-taxation revenues of \$33.5 billion and reported cash holdings totalling \$5.5 billion.

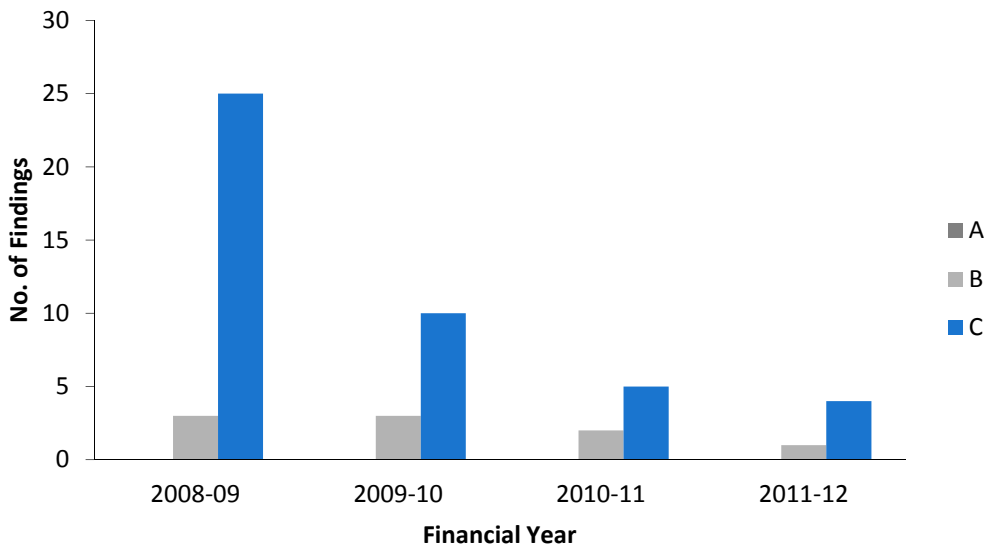
3.98 The main controls over revenue and receivables that are given particular focus in our interim audits include: policies for the recognition of bad and doubtful debts; the regular review of receivables; and the segregation of receipting and recording of cash functions.

3.99 The main controls over the management of cash that are given particular focus in our interim audits include: the approval to open and close bank accounts; the exercise of delegations; and the preparation of bank reconciliations on a regular basis.

3.100 The number of audit findings over the last four years are outlined in Figure 3.8 below.

Figure 3.8

Revenue, receivables and cash management – aggregate audit findings



3.101 Over the last four years, the interim audit phase of the audits has identified that agencies' key controls over revenue, receivables and cash have

generally been effective, with audit findings in respect of these areas representing seven per cent of total findings.

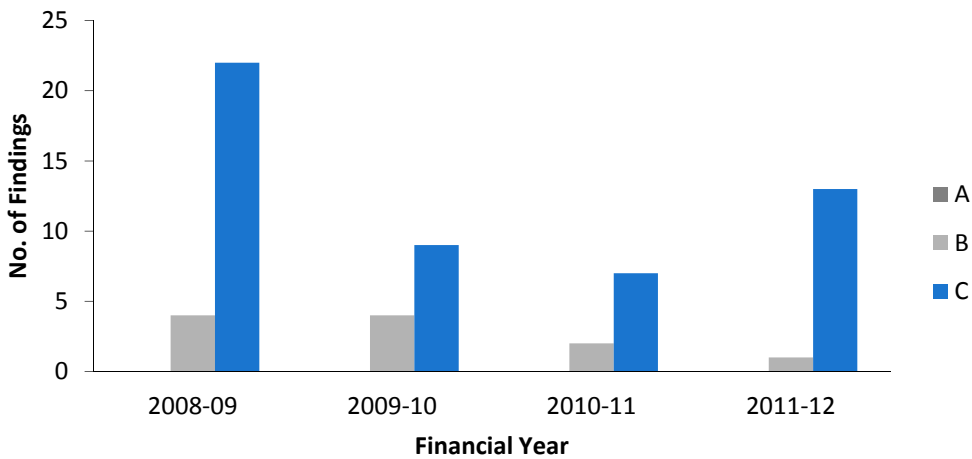
Human resource management processes

3.102 Human resource management processes encompass the day-to-day management and administration of employee entitlements and payroll functions. The main components of employee expenses consist of salary and wages, leave and other entitlements, employer superannuation contributions, separation and redundancy payments and workers compensation expenses. These items represent the second largest departmental expenditure for most agencies. Employee entitlement liabilities, particularly relating to annual and long service leave, generally are one of the larger liabilities on an agency's balance sheet.

3.103 In 2010–11, the Consolidated Financial Statements reported \$38.6 billion in employee benefits expenses.

3.104 The main controls over human resource management processes that are given particular focus in our interim audits include: approvals over new employees; independent checks of employee salary and personnel details entered into the HRMIS; approval of changes of key HRMIS data; independent checks over payroll processes including leave entitlement calculations; the timely conduct and review of reconciliations; and the approval of leave and termination payments.

3.105 The number of audit findings over the last four years are outlined in Figure 3.9 below.

Figure 3.9**Human resource management process – aggregate audit findings**

3.106 Over the four year period, there have been 62 findings in this category, representing approximately eight per cent of total audit findings. There has been an increase in the total number of audit findings in this category in 2011–12. Areas where our 2011–12 interim phase audits have identified weaknesses include controls around employee commencements and terminations processes, and payroll and other related reconciliations.

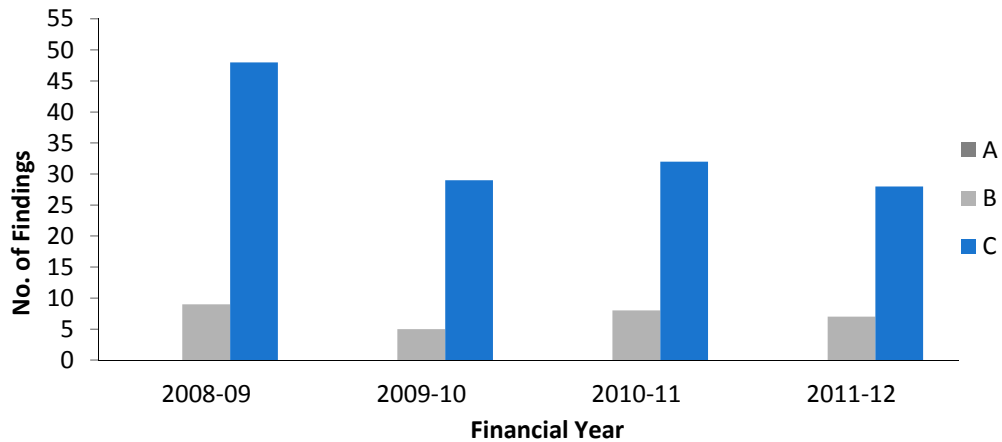
Other control matters

3.107 Our audits also include a review of agencies' general control environments, particularly when they impact on agencies' financial statements. Issues considered include such matters as Business Continuity Management, the management of service level agreements and memoranda of understanding, and risk management and financial statements quality assurance processes.

3.108 The number of audit findings over the last four years are outlined in Figure 3.10 below.

Figure 3.10

Other control matters – aggregate audit findings



3.109 There have been 166 findings in this category, representing approximately 22 per cent of total audit findings. Common issues noted over the four years include: control weaknesses across a range of business processes; quality assurance issues and the absence of, or delays in, conducting reconciliations in respect of a number of accounts or key processes.

Monitoring of controls

3.110 Australian Auditing Standard ASA 315 at paragraph A98 states:

Monitoring of controls is a process to assess the effectiveness of internal control performance over time. It involves assessing the effectiveness of controls on a timely basis and taking necessary remedial actions. Management accomplishes monitoring of controls through ongoing activities, separate evaluations, or a combination of the two. Ongoing monitoring activities are often built into the normal recurring activities of an entity and include regular management and supervisory activities.

3.111 Agencies undertake many types of activities as part of their monitoring of control processes, including external evaluation reviews, control self assessment processes, post-implementation reviews and internal audits. The level of review of different types of activities by the ANAO is dependent on the nature of each entity. However, given the significance of the internal audit function to Australian Government agencies, and the requirements of Australian Auditing Standards, this function is reviewed by the ANAO each year to gain an understanding of its contribution to the overall controls environment.

Internal audit function

3.112 In the public and private sectors, internal audit has long been recognised by better practice entities as a valuable resource, and entities have given internal audit a key role in their governance arrangements.³⁴

3.113 Internal audit is a key source of independent and objective assurance advice on an agency's risk framework and internal control. Depending on the role and mandate of an agency's internal audit function, it can play an important role in assessing the adequacy of both the financial systems that underpin an agency's financial statements, and the preparation process.

3.114 To assist agencies in the management of their internal audit functions, the ANAO issued a Better Practice Guide *Public Sector Internal Audit* in September 2007. The Better Practice Guide outlines the key characteristics of a well performing Internal Audit function. The presence of these characteristics will provide confidence and assurance to Chief Executives and, where relevant, Boards that those financial and operational controls, which manage

³⁴ ANAO Better Practice Guide *Public Sector Internal Audit* September 2007, page 1.

organisational risks, are operating in an efficient and effective manner. The ANAO will issue an update of this Better Practice Guide early in the next financial year.

3.115 As part of its financial statement coverage, the ANAO reviews the activities of internal audit in accordance with Australian Auditing Standard ASA 610 *Using the Work of Internal Auditors*. The ANAO approach takes into account the work completed by internal audit, and, where appropriate, reliance is placed on it to ensure an effective audit approach. Before reliance is placed on specific internal audit work, ASA 610 requires a number of audit procedures to be undertaken. These may include a review of relevant internal audit working papers, examination of a sample of items already examined by internal audit and observation of internal audit procedures.

Observations

3.116 The ANAO observed that internal audit coverage is generally based on a work plan that is aligned with agencies' risk management plans and includes a combination of audits that address assurance, compliance, performance improvements and IT systems reviews. In addition, recommendations from management, audit committees and external influences such as the ANAO work program are factors considered in the development of internal audit work plans.

3.117 Where appropriate, the ANAO places reliance on internal audit work with aspects of the work being used to determine the nature, timing and extent of the ANAO audit procedures. The extent of reliance varies between agencies. Greater reliance is placed on internal audit work where the work is focused on financial controls and legislative compliance. The ANAO continues to encourage agencies to identify opportunities for internal audit coverage of key financial systems and controls as a means of providing increased assurance to Chief Executives to support their expressing an opinion on the agency's financial statements.

3.118 The ANAO also found that the internal audit functions of most agencies are generally subject to annual review by their respective audit committee or by external reviewers. At the time of the interim audit, those internal audit functions that had been reviewed had been assessed as providing a satisfactory service.

Conclusion

3.119 The results of our 2011–12 interim audits identified that the effectiveness of controls over finance and accounting processes in the majority of agencies supports the production of reliable financial statement information, reflecting the general maturity of agencies' control environments. This situation is reflected in the progressive decrease in audit findings over recent years. The ongoing responsibility of agencies to monitor the effectiveness of their systems and related controls to be confident of the integrity of the financial information reported to management and in their financial statements will underpin a continuation of the situation.

4. Information Technology Controls

This chapter presents the results of the ANAO's review of selected elements of the information technology (IT) control environments that underpin financial transaction processing within major Australian Government agencies.

Introduction

4.1 Information Technology (IT) facilitates the way in which Australian Government agencies operate and support the business processes that deliver services to the Australian community. Accordingly, these systems are required to be accurate, reliable, and sustainable.

4.2 The Australian Government Information Management Office (AGIMO) has collated Government IT expenditure and has reported that expenditure for the 2008–09 and 2009–10 financial years³⁵ was around \$5 billion per annum. Previously, the Gershon review commissioned by the Australian Government estimated that the total Government IT expenditure across the General Government Sector (GGS) was in excess of \$5 billion³⁶.

4.3 The business processes that support financial statement preparation and reporting also require the support of IT systems. As a result, the evaluation of the IT control environment is a core component of the overall agency control environment, and the financial statement audit process. The ANAO reviews both IT general controls³⁷ and application controls³⁸ within these environments.

4.4 ANAO audits provide a valuable insight into IT activities across Government. This provides the ANAO with a unique opportunity to analyse and report on key IT general control categories across major GGS agencies,

³⁵ 'Australian Government ICT expenditure, 2008–09 – 2009–10, Version 1.0', Department of Finance and Deregulation.

³⁶ 'Review of the Australian Government's Use of Information and Communication Technology', Sir Peter Gershon, August 2008, p. 46, estimated total government expenditure across the General Government Sector in 2007–08 was \$5.3 billion.

³⁷ IT general controls are agency-wide structures, policies, procedures, and standards applied to information systems that support accounting and business processes. Effective operation of these controls helps make sure IT application controls work as intended throughout the financial year.

³⁸ IT application controls operate at the accounting and business process level, consisting of access, configuration, and reporting controls. Reliance on the effective operation of these controls provides a means to confirm the accuracy and integrity of agencies financial statements, particularly high transaction volume accounts.

providing a broad perspective of the effectiveness of the implementation and operation of key IT controls. The focus of the ANAO's financial statement audits is on risks of material misstatement of agencies' financial statements.

4.5 This chapter also includes a discussion on trends observed in the five year period 2007–08 to 2011–12 in relation to a number of IT control categories.

IT control environment

4.6 The ANAO assesses the design, implementation and operation of key IT controls to determine their effectiveness in reducing risks to the integrity of financial information presented in agencies' financial statements. The ANAO undertakes this assessment each year in accordance with the Australian Auditing Standards³⁹. The accuracy, completeness and integrity of agencies' financial transactions and information are important considerations in formulating agencies' overall audit risk profile and, as such, it is important that controls are well designed and operate effectively.

Changes to the IT control environment

4.7 As part of the overall audit approach, a key step each year is an assessment of significant changes to agencies' control environments. By its nature, the IT control environment is subject to change and modification on a regular basis. For some agencies, changes to their IT systems, applications and processes represent major business change initiatives. Such changes can often have a fundamental impact on the underlying IT control environment.

4.8 In the context of assessing aspects of the IT control environment that could result in the material misstatement of agencies' financial statements, the 2011–12 audits included an assessment, where applicable, of major technology change activities within agencies. One example is agencies' responses to the *Data Centre Strategy 2010-2025*.⁴⁰ The strategy has potential significant implications for agencies' IT control environments and, where necessary, the ANAO will need to tailor audit procedures.

³⁹ Australian Auditing Standards, *ASA 315 Identifying and Assessing the Risks of Material Misstatement through Understanding the Entity and its Environment*, AUSAB June 2011, <www.auasb.gov.au>

⁴⁰ *Australian Government Data Centre Strategy 2010 – 2025*, AGIMO. This strategy proposes a whole of government approach to future data centre requirements.

Elements of the IT control environment

4.9 Table 4.1 below outlines the elements of the IT control environment⁴¹ reviewed by the ANAO as part of the 2011–12 financial statement audits of agencies covered by this report. The total number of agencies in this category can vary from year to year.⁴² Twenty-five agencies have been reported for 2011–12.

4.10 A more detailed discussion of each IT control environment element follows.

Table 4.1

Elements of the IT control environment

Control Area	Control Element	Control Categories
General IT controls	IT security management	Network security Physical security Security awareness and training Security governance Security monitoring and reporting User access management
	IT change management	Approval and tracking Backout procedures Change logs and reporting Emergency changes Policy and governance frameworks Release management
	IT incident and problem management	Analysis and reporting Configuration management tools Incident management processes Link to change management Problem management processes Service desk

⁴¹ Given the extensive number of individual controls assessed by the ANAO each audit; for the purposes of this report controls comprise a series of elements, for example IT Security or IT Change Management, and elements comprise a series of control categories.

⁴² Where comparative data has been included, the data for 2011–12 is for 25 agencies, the data for 2010–11 and 2009–10 is for 26 agencies, the data for 2008–09 is for 25 agencies, and the data for 2007–08 is for 23 agencies.

Control Area	Control Element	Control Categories
Application controls	Financial Management Information System	Application change management Business continuity Masterfile maintenance Payment processing reconciliations Privileged user management User access management User support and training
	Human Resource Management Information System	Application change management Business continuity Masterfile maintenance Payroll processing Privileged user management User access management User support and training

Source: ANAO compilation

4.11 The charts and associated commentary that follow reflect the ANAO assessment of the integrity of general IT controls and application controls, as categorised in Table 4.1 above.

General IT controls

4.12 General IT controls are the foundation of agencies' IT control arrangements. These controls commonly relate to all information systems and establish the environment in which application systems and controls operate. The ANAO's review of IT general controls focused on the controls present in the IT environment relevant to those systems that process financial transactions and information.

IT security management

4.13 The administration of Government programs often involves agencies managing, protecting, and preserving large amounts of financial and personal information. The integrity of such information can be threatened by an IT security event, and risk the accuracy and completeness of agencies' financial information. Some events can also pose a risk to the legal, privacy, and operational responsibilities of agencies, and may result in loss of public confidence.

4.14 IT security management is the primary mechanism used to protect information and information systems from unauthorised access, use, disclosure, modification, or destruction. The minimum standards for the protection of Australian Government information and data that agencies must meet are detailed in the *Protective Security Policy Framework* (PSPF)⁴³ and the *Australian Government Information Security Manual* (ISM)⁴⁴.

4.15 The ANAO reviewed the following categories of IT security management that are fundamental to safeguarding the security and confidentiality of agencies' financial information:

- network security;
- physical security;
- security awareness and training;
- security governance;
- security monitoring and reporting; and
- user access management.

Observations

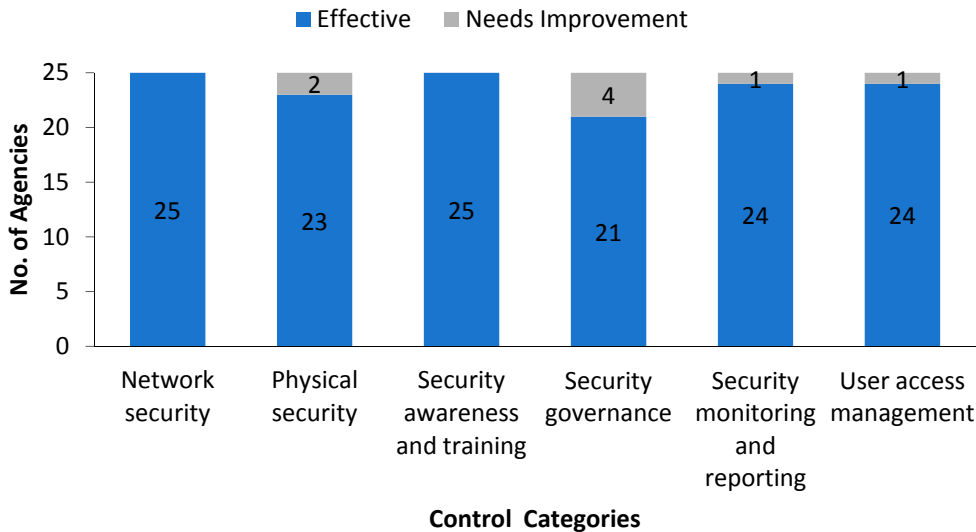
4.16 A summary of the ANAO's assessment of the effectiveness of security control categories within agencies is provided in Figure 4.1 below.

⁴³ The *Protective Security Policy Framework* (PSPF) is the source of policies, procedures, and minimum standards for agencies in setting their protective security arrangements.

⁴⁴ The *Australian Government Information Security Manual* complements the PSPF by providing principles and controls to assist Government agencies to achieve an assured IT security environment.

Figure 4.1

2011–12 Assessment of IT security management



4.17 Overall, the ANAO found the security management controls implemented by agencies were effective. In particular, most agencies had established effective security governance frameworks, and had implemented effective controls for managing their IT security responsibilities. The areas requiring improvement were minor, and, in most cases, were progressively being addressed by agencies.

4.18 The ANAO also observed effective controls in most agencies in the areas of security incident monitoring and reporting, and security awareness and training.

4.19 No systematic security governance or management failures were observed, although the audits identified specific operational security weaknesses in some agencies, such as in relation to consistency of IT security governance arrangements including approved policies and procedures, and appropriate reporting arrangements.

IT change management

4.20 Changes to an agency’s IT environment are generally managed using a standardised approach. A change management process covers changes to all technology and communications components, including networks, hardware

platforms, application software, and requires appropriate supporting documentation. The aim of the change management process is to manage changes in a controlled and timely manner, with a minimal number of incidents or problems occurring on release to the production environment.

4.21 The ANAO tested controls supporting the change management process, for changes made to the key financial systems supporting the preparation of an agency's financial statements, in the following key categories:

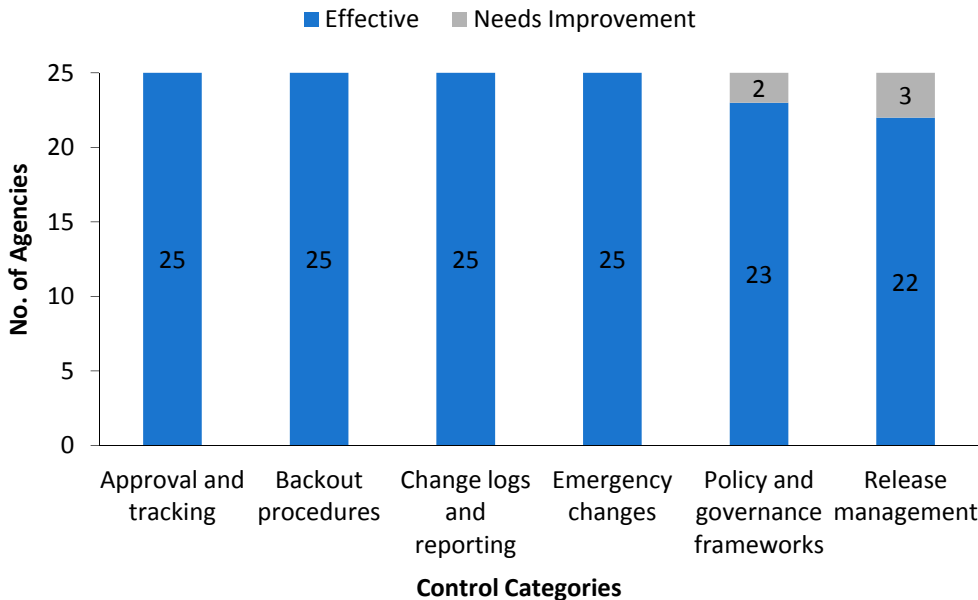
- approval and tracking;
- backout procedures;
- change logs and reporting;
- emergency changes;
- policy and governance frameworks; and
- release management.

Observations

4.22 The findings from the testing of IT change management controls are summarised in Figure 4.2 below.

Figure 4.2

2011–12 Assessment of IT change management



4.23 Most agencies had effective change management policies and governance frameworks, and agencies had implemented most operational change management practices effectively. However, three of 25 agencies had not fully implemented release management processes. This situation reduces the level of oversight and control over system changes, and increases the risk of system changes being implemented that may affect the integrity of financial information.

4.24 Overall, no systematic change management weaknesses were observed, although the audits did identify specific weaknesses in some agencies that are reported in Chapter 5 where the issue was assessed as significant or moderate.

IT incident and problem management

4.25 In the normal course of business operations, agencies will be affected from time to time by IT system incidents. These incidents may interrupt the availability of an IT system, which in turn may affect the quality and accuracy of system data. If the handling of these incidents is not effective, an agency’s level of service delivery may be affected. Incident management refers to the methods and procedures used for handling and resolving these incidents.

4.26 Agencies may also encounter IT problems that affect their operations. This can be as a result of a single incident, or multiple incidents that have a common source. Problem management is the process of finding and resolving the underlying causes of related incidents.

4.27 Agencies commonly use a service desk⁴⁵ approach to establish centralised and structured processes for collecting, managing, and responding to incidents and problems.⁴⁶ Effective implementation of a service desk assists agencies to minimise adverse impacts to service delivery from IT incidents and problems.

4.28 The following control categories for incident and problem management were examined by the ANAO:

- analysis and reporting;
- configuration management tools;
- incident management processes;
- link to change management;
- problem management processes; and
- service desk.

Observations

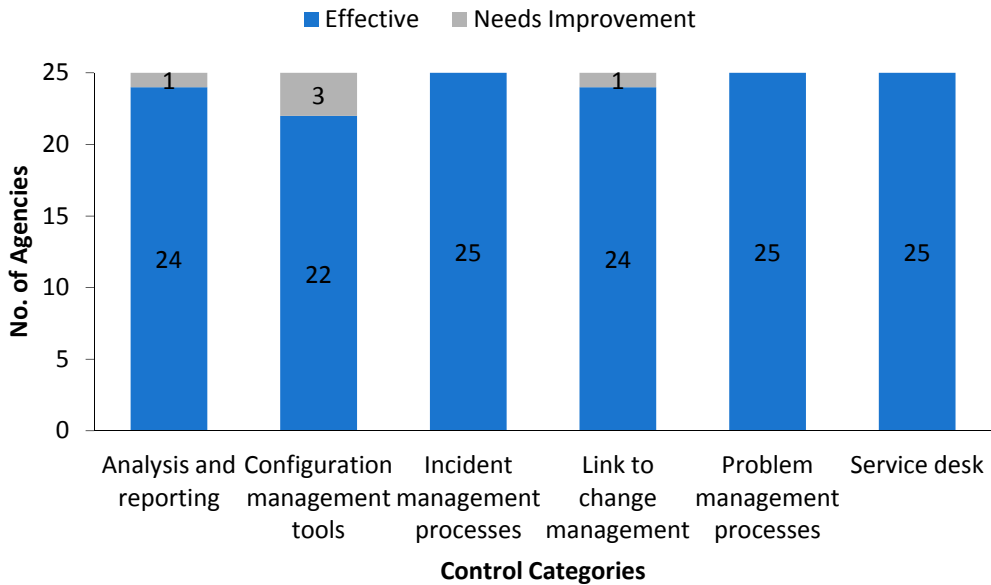
4.29 A summary of the results of the assessment of the control categories for incident and problem management is outlined in Figure 4.3 below.

⁴⁵ Also commonly referred to as an IT Helpdesk.

⁴⁶ IT incidents and problems are generally daily events and are 'business-as-usual' or routine matters that every agency encounters and must manage.

Figure 4.3

2011–12 Assessment of IT incident and problem management



4.30 Overall, the 2011–12 audits identified that agencies had implemented effective incident and problem management controls. In particular, the use of a service desk as a central management point for IT incidents and problems is now well established.

4.31 The most common weakness identified related to the implementation of an integrated configuration management tool, with three of 25 agencies not having implemented this control. Configuration management tools are used to store system hardware and software information in a central location, and in a common format. A lack of centralised information about the IT environment may complicate the installation of new hardware or software, or affect the capacity to recover from a business continuity or disaster recovery event.

Application controls

4.32 Australian Government agencies generally rely on two key financial reporting systems in the preparation of financial information. These are the Financial Management Information System (FMIS) and the Human Resource Management Information System (HRMIS).

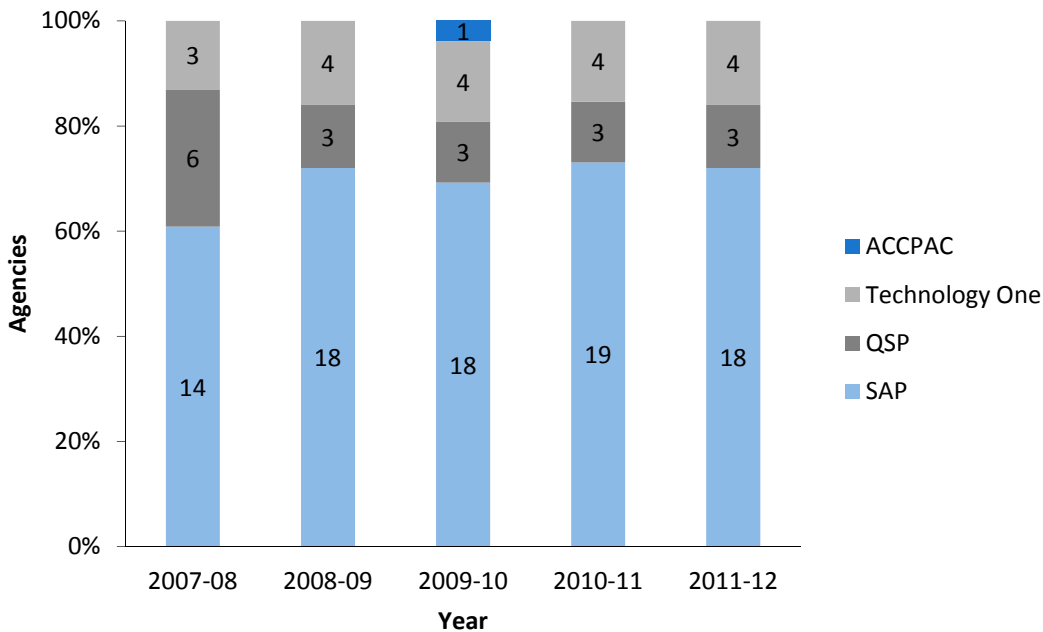
4.33 In view of their importance for financial reporting, the ANAO reviews the key FMIS and HRMIS controls across all agencies.

4.34 The ANAO has published a Better Practice Guide, *Human Resource Information Systems: Risks and Controls*, to assist agencies in managing the risks involved in HRMIS functions.

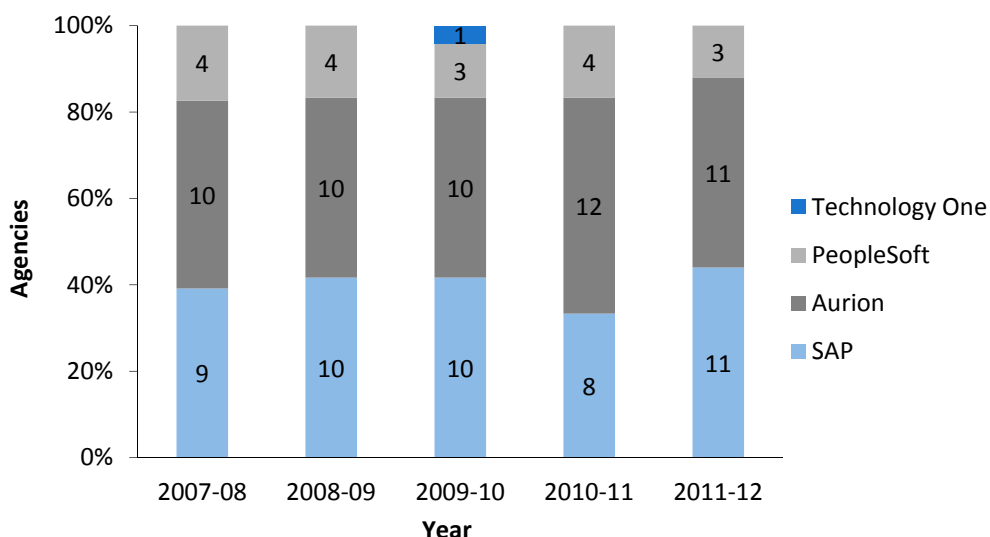
4.35 Figures 4.4 and 4.5 below detail the various FMIS and HRMIS applications used by the agencies covered by this report over the last five years.

Figure 4.4

Summary of FMIS applications 2007–08 to 2011–12⁴⁷



⁴⁷ Op cit (refer footnote 42, pg 70).

Figure 4.5**Summary of HRMIS applications 2007–08 to 2011–12⁴⁸**

4.36 The ANAO observed that there has been little change in the range of applications utilised by agencies over the past five years. The selection and deployment of HRMIS and FMIS are costly projects for agencies and imposes considerable disruption to business operations, and as a result the rate of changing systems to an alternative product can be expected to be low.

Financial management information system (FMIS)

4.37 The FMIS is the IT application that processes financial transactions and summarises financial information. It supports financial management decision-making, budget and financial planning, and the preparation of agency financial statements.

4.38 The following FMIS control categories were reviewed as part of the 2011–12 financial statement audits:

- application change management;
- business continuity;
- masterfile maintenance;
- payment processing reconciliations;

⁴⁸ Op cit (refer footnote 42, pg 70).

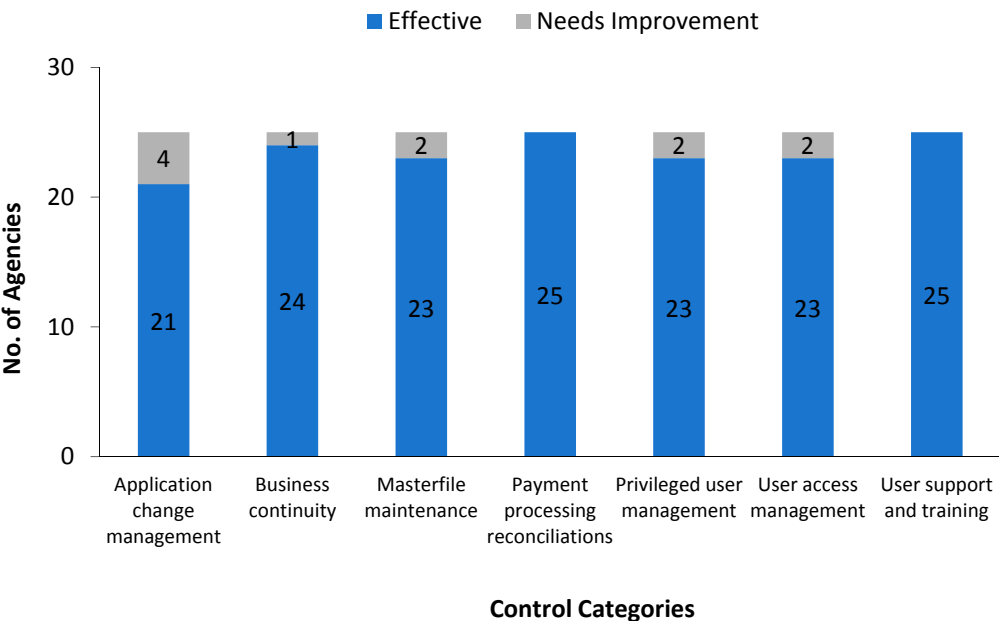
- privileged user management;
- user access management; and
- user support and training.

Observations

4.39 The ANAO’s assessment of the key FMIS control categories integral to effective financial management and reporting, that have implications for the preparation of agencies’ financial statements, is summarised in Figure 4.6 below.

Figure 4.6

2011–12 Assessment of FMIS controls



4.40 The ANAO identified that the key FMIS controls used to support the preparation of financial statements were generally effective in most agencies.

4.41 The ANAO identified four of 25 agencies required improvement in their FMIS change management arrangements. Without sound change management arrangements in place, it is possible for changes to be implemented without appropriate testing, review, and approval.

4.42 FMIS privileged user management remains an area requiring improvement in two of 25 agencies, and FMIS user access management also

required improvement in two agencies. When there is inadequate user access controls, especially those related to the more powerful privileged user access, it is possible for individuals to undertake actions that may undermine the integrity of financial systems and information. It is thus critical that agencies take steps to address any control deficiencies with user access controls.

4.43 In addition, a small number of agencies did not have adequate controls for maintaining master file information. Any failure in the currency or accuracy of master file information can have a significant affect on FMIS calculations and results. As a result, it is important to have well established processes for maintaining master file information, including those related to user access controls.

Human resources management information system (HRMIS)

4.44 The HRMIS is the IT application that facilitates strategic and operational decision-making for payroll and human resource management. The data held in the system is a major component of the financial reporting process.

4.45 The key categories of HRMIS controls reviewed as part of the 2011–12 audit coverage were:

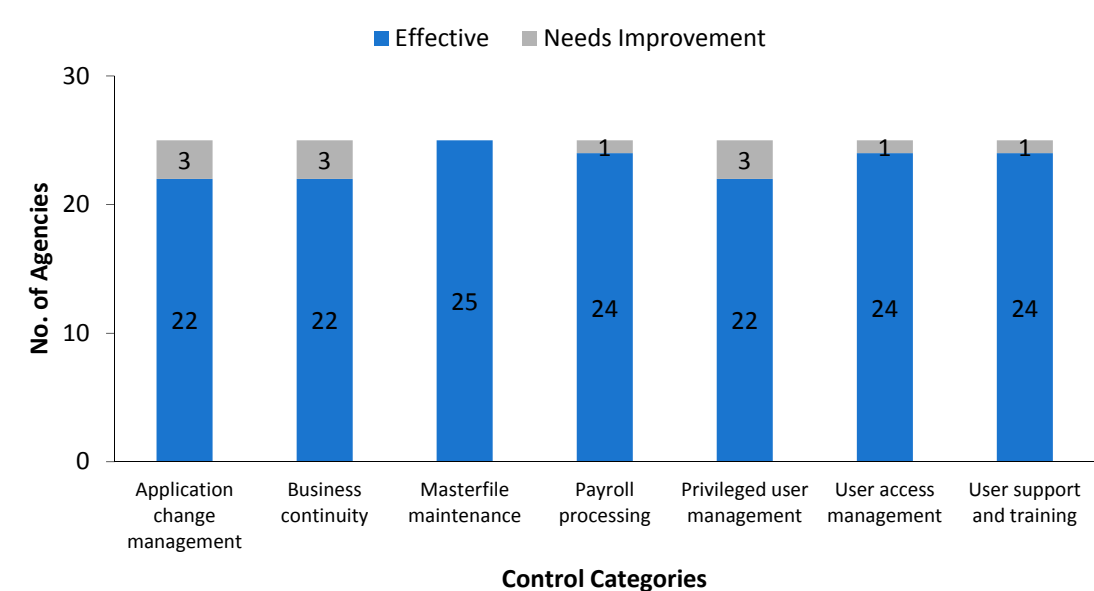
- application change management;
- business continuity;
- masterfile maintenance;
- payroll processing;
- privileged user management;
- user access management; and
- user support and training.

Observations

4.46 The ANAO's assessment of key HRMIS control categories that enhance the completeness and accuracy of HR financial information is outlined in Figure 4.7 below.

Figure 4.7

2011–12 Assessment of HRMIS controls



4.47 The ANAO identified that the key HRMIS controls used to support the preparation of agency’s financial statements were also generally effective in most agencies. However, the ANAO identified inadequate privileged and user access management controls in three agencies. Having appropriate controls for managing HRMIS system administrators and other users who have high levels of access to HRMIS financial transactions and information is required to manage the risk of inappropriate access.

4.48 In addition, the ANAO identified HRMIS change management arrangements required improvement in three agencies. Without sound change management arrangements in place it is possible for changes to be implemented without appropriate testing, review, and approval.

4.49 The ANAO also found three of 25 agencies did not have a comprehensive and tested business continuity plan in place for their HRMIS. Any failure in the HRMIS resulting from a business disruption event could have significant consequences for an agency’s capacity to maintain the completeness, accuracy, and availability of financial information. HRMIS business continuity plans should be subject to regular testing and updating when required.

Trends over the period 2007–08 to 2011–12

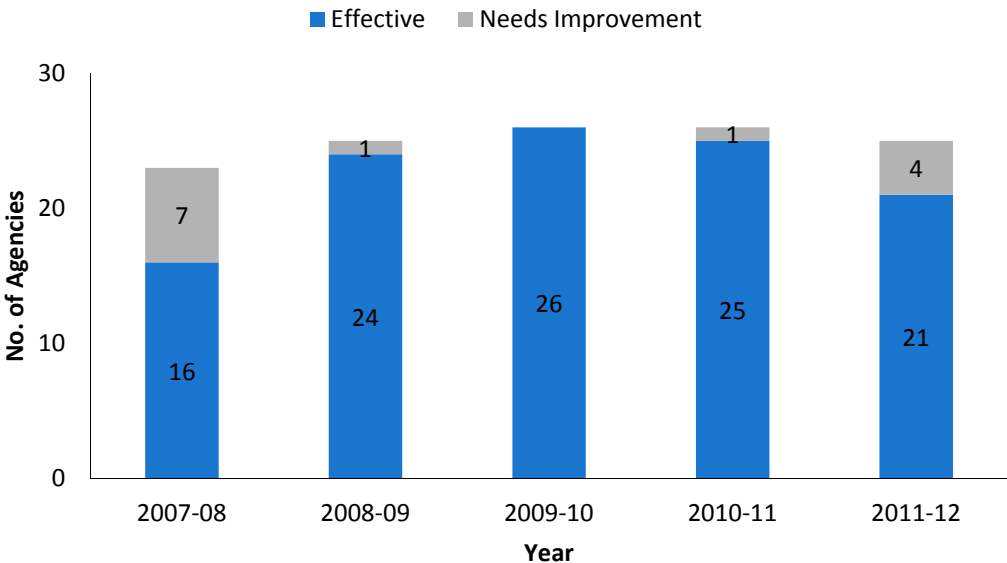
4.50 The ANAO’s ongoing assessment of agencies’ IT control environments has identified a number of trends over the period 2007–08 to 2011–12 for particular control categories. Some trends point to areas that have improved over the last five years, while others suggest that further management attention is required in a number of agencies. The most significant of these trends is discussed below.

IT security governance

4.51 IT security governance frameworks are an overarching set of structures, policies and procedures that address security matters within an agency. As illustrated in Figure 4.8 below, over the years to 2009–10 there was an improvement in the effectiveness of agency security frameworks. This improvement was maintained in 2010–11 with the exception of one agency; however there has been some decline in 2011–12 with four of 25 agencies requiring improvement.

Figure 4.8

IT security governance: 2007–08 to 2011–12⁴⁹



⁴⁹ Op cit (refer footnote 42, pg 70).

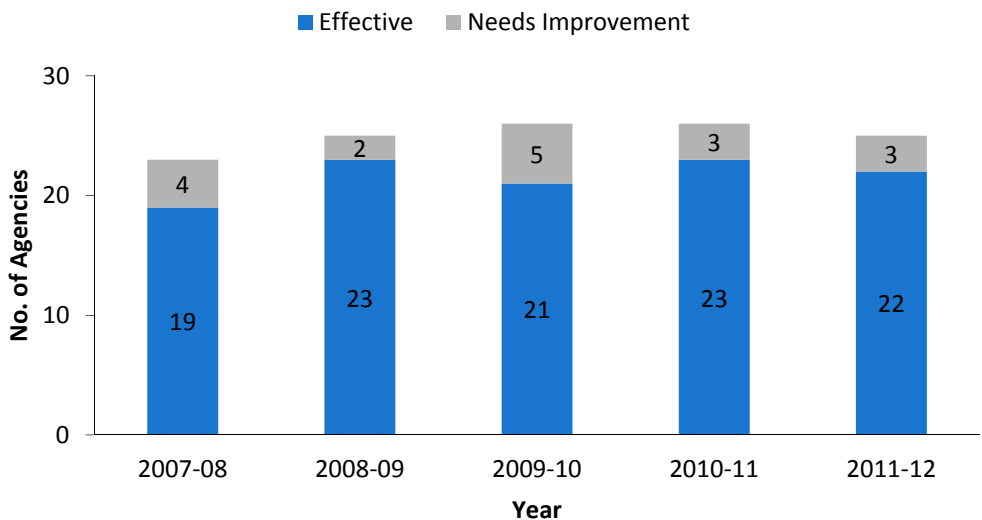
4.52 Effective security governance frameworks support agencies remaining current with technology innovations and organisation changes, and to be better positioned to manage security threats and incidents. Whole of Government security framework changes have occurred in 2011–12, and some agency functions continue to change from time to time. As a result, it is important for agencies to establish and maintain their security governance frameworks, and to have implemented related processes and procedures.

Configuration management tools

4.53 Configuration management tools, such as a Configuration Management Database (CMDB), assist agencies to maintain the integrity of technology systems by storing information about system attributes in a central location and in a common format. The ANAO observations regarding configuration management tools over the last five years are summarised in Figure 4.9 below.

Figure 4.9

Configuration management tools: 2007–08 to 2011–12⁵⁰



4.54 There has been increased use of configuration management tools since 2007–08, although in 2011–12, three of 25 agencies still did not utilise such a tool, or had not implemented a process for regularly updating the tool. While some agencies had initiated projects to create and populate a CMDB, until

⁵⁰ Op cit (refer footnote 42, pg 70).

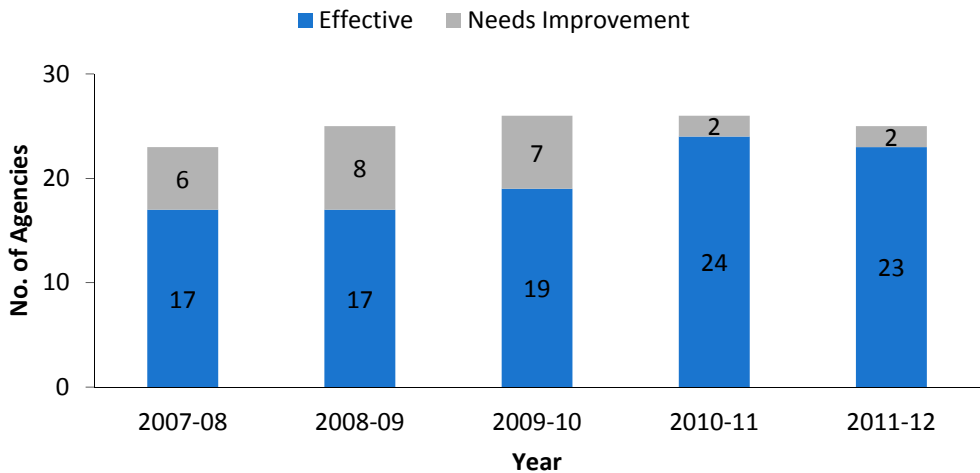
these processes have been implemented, and the CMDB is regularly updated, procedures for managing incidents and problems may be less efficient and effective.

IT change management policy and governance frameworks

4.55 IT change management policy and governance frameworks assist agencies to create a consistent and reliable approach to making changes in their IT environment.

4.56 As agency IT environments change, the controls surrounding change management require regular review to maintain their currency and applicability. The ANAO observations regarding change management policy and governance frameworks over the past five years are summarised in Figure 4.10 below.

Figure 4.10
Change management policy and governance frameworks: 2007–08 to 2011–12⁵¹



4.57 The policy and governance structures that support change management processes showed a marked improvement across agencies in 2010–11 and this improvement has been maintained during 2011–12. From 2007–08 to 2009–10, at least 25 per cent of agencies did not regularly review and maintain their

⁵¹ Op cit (refer footnote 42, pg 70).

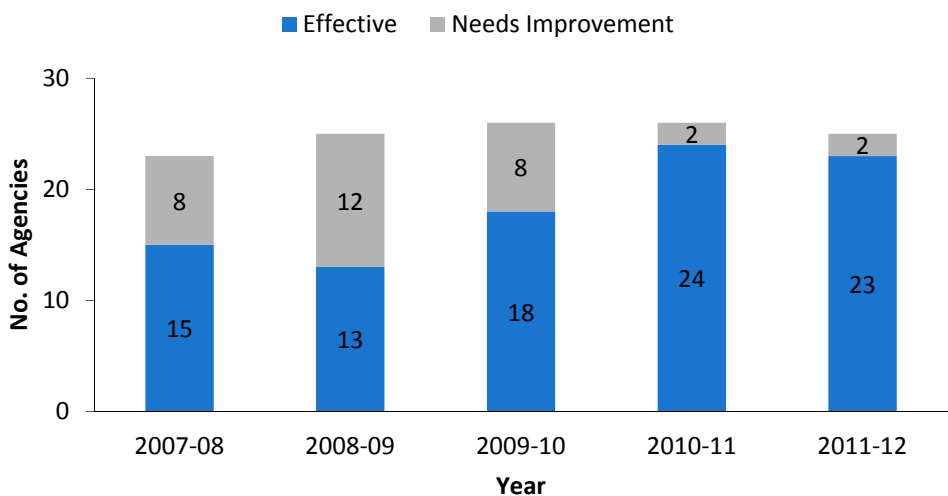
change management policy and governance frameworks, while in 2011–12 ANAO testing identified that almost all agencies effectively met the control.

FMIS privileged user management

4.58 FMIS privileged user management involves implementing a regime of system restrictions on users in respect of their access rights to edit and change data within the FMIS. The ANAO observations regarding FMIS privileged user management over the past five years are summarised in Figure 4.11 below.

Figure 4.11

FMIS privileged user management: 2007–08 to 2011–12⁵²



4.59 The administration of FMIS privileged user accounts has shown marked improvement to 2010–11 compared with the previous three years, and the improvements have been mostly maintained in 2011–12, with most agencies effectively managing the risks arising from this level of access to financial information.

4.60 This improvement indicates that most agencies are now managing, logging, and effectively monitoring privileged user activities. These are important controls to prevent or detect inappropriate use of the greater access afforded to these users.

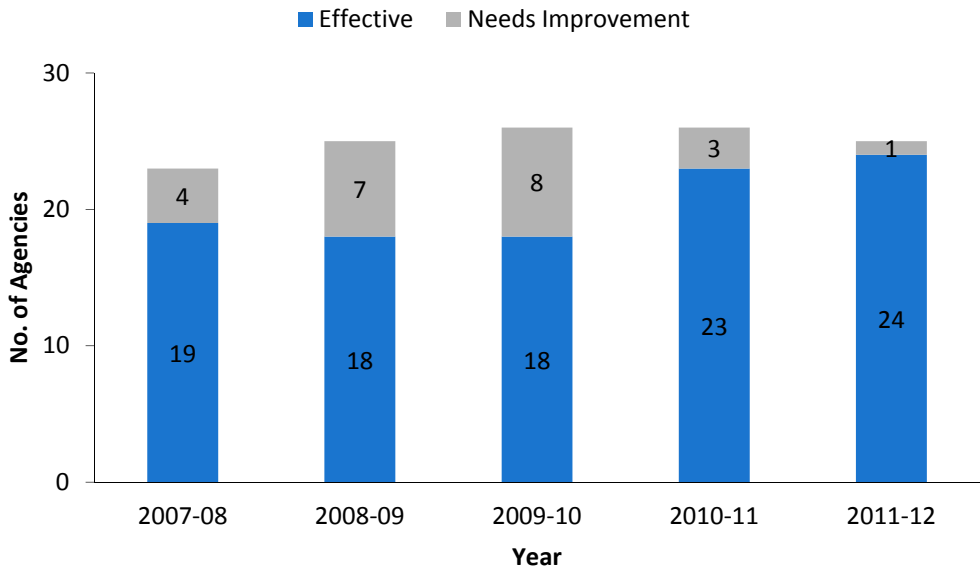
⁵² Op cit (refer footnote 42, pg 70).

FMIS business continuity

4.61 In view of the key role of the FMIS in the effective management of an agency, it is important to have a business continuity plan for the FMIS in place. The ANAO observations regarding the management of FMIS business continuity risks over the past five years are summarised in Figure 4.12 below.

Figure 4.12

FMIS business continuity: 2007–08 to 2011–12⁵³



4.62 The effectiveness of FMIS business continuity arrangements has improved significantly in the past two years. In 2009–10, eight of 26 agencies were not effectively implementing controls to manage business continuity risks. In 2010–11, this had reduced to three of 25 agencies, and in 2011–12 almost all agencies effectively met the control.

4.63 The ongoing management of business continuity risks requires business continuity plans to be well designed, regularly tested, and updated as required. The improvements identified indicate that there is a greater likelihood that agencies will be able to recover financial information if a business disruption occurs.

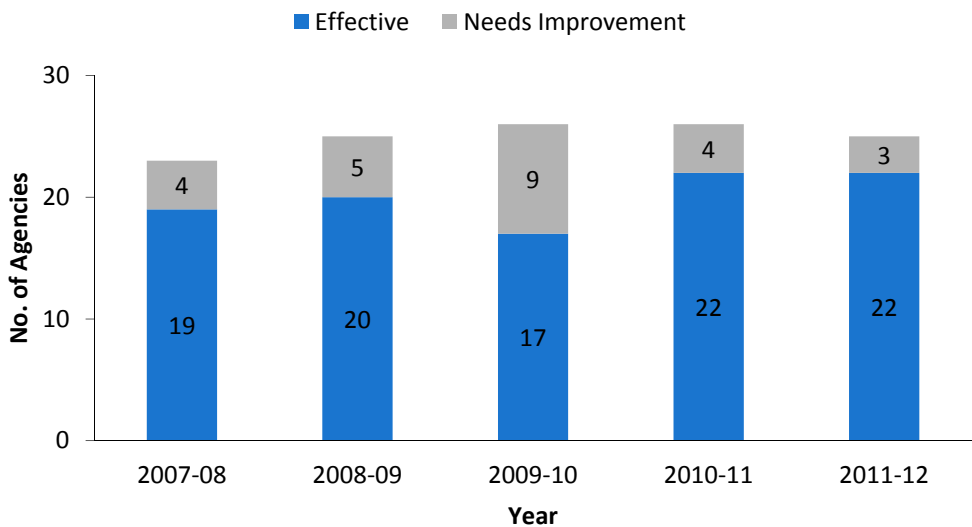
⁵³ Op cit (refer footnote 42, pg 70).

HRMIS privileged user management

4.64 HRMIS privileged user management involves implementing a regime of system restrictions on users in respect of their access rights to edit and change data within the HRMIS. The ANAO observations regarding HRMIS privileged user management over the past five years are summarised in Figure 4.13 below.

Figure 4.13

HRMIS privileged user management: 2007–08 to 2011–12⁵⁴



4.65 In 2010–11 there was a significant improvement in the administration of HRMIS privileged user accounts, and this improvement has been maintained in 2011–12 with most agencies effectively meeting controls in this area. As privileged users typically have full access to all HRMIS financial transactions and information, there remains a risk to the integrity of financial and other information in the HRMIS for agencies concerned, and it is critical that agencies take steps to address any control deficiencies.

HRMIS business continuity

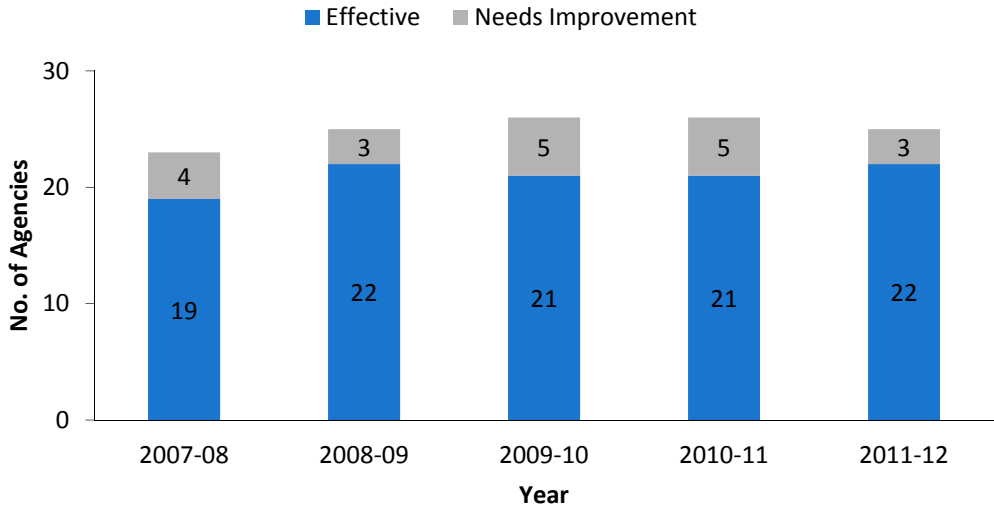
4.66 In view of the key role of the HRMIS in the effective management of an agency, it is important that agencies have a business continuity plan for the HRMIS. The ANAO observations regarding the management of HRMIS

⁵⁴ Op cit (refer footnote 42, pg 70).

business continuity risks over the past five years are summarised in Figure 4.14 below.

Figure 4.14

HRMIS business continuity: 2007–08 to 2011–12⁵⁵



4.67 The effectiveness of HRMIS business continuity arrangements has remained relatively constant over the past five years. A small improvement was observed during 2011–12, and most agencies are effectively meeting business continuity controls.

4.68 Management of business continuity risks requires business continuity plans to be well designed, regularly tested, and updated as required. In agencies that do not have effective business continuity arrangements, there is a continuing risk that some agencies will not be able to fully, or effectively, recover human resources information from a business disruption.

Data centre consolidation

4.69 As part of the ANAO’s annual assessment of the design, implementation and operation of key IT controls, the ANAO reviewed agencies’ IT operations, including the data centre hosting arrangements for financial systems. The review also included agencies’ data centre consolidation

⁵⁵ Op cit (refer footnote 42, pg 70).

progress in light of the whole of Government data centre strategy⁵⁶. This strategy is designed to provide significant efficiencies within and across agencies, avoiding \$1 billion in data centre costs over a 10 to 15 years period. The strategy is also intended to provide for more reliable and controlled systems.

4.70 Data centre consolidation is well underway, with a number of data centres decommissioned or planned to be decommissioned in 2011–12. For some larger agencies there will be significant reductions in the number of data centres. For smaller agencies, particularly where outsourcing arrangements are in place, data centre consolidation may not be possible or practical.

4.71 The ANAO will continue to monitor progress in this area given its relevance to the IT control environment.

Conclusion

4.72 The effective implementation and operation of general and application specific controls assists agencies to provide services in a reliable, timely and consistent manner. Such controls also reduce the risk of financial information being inaccurate, incomplete, or stored insecurely.

4.73 There have been no significant changes across agencies in the 2011–12 financial year. Improvements observed in agencies' change management general control related governance and release management arrangements of 2010–11 have been maintained. Some agencies need to give increased focus on these controls in order to achieve further improvement.

4.74 The 2011–12 audits identified that an increased focus on IT security governance is required by some agencies. IT security governance provides the framework for the way agencies plan and implement their IT security arrangements, and any reduction in attention by agencies may lead to increased risk from security threats.

4.75 The management of user access, particularly the logging and monitoring of user activities for privileged users, remains an area that requires further attention in some agencies. This applies to both FMIS and HRMIS operations. The ongoing effectiveness of user access controls is an important element in maintaining the integrity of agencies' financial information. To

⁵⁶ 'Australian Government Data Centre Strategy 2010-2025', Australian Government Information Management Office, March 2010.

address these weaknesses, agencies should have appropriate user access policies and procedures in place across their entire IT environments. Such policies and procedures should align with agencies' information security policies.

4.76 In addition, the ANAO's assessment of HRMIS business continuity arrangements and application change management arrangements, and FMIS change management, has identified that the effectiveness of these arrangements could be further improved. In the event of a business disruption, there remains risk that some agencies may not be able to effectively recover their human resources information in a timely manner. In relation to HRMIS and FMIS change management, it is important to maintain an understood and controlled approach to ensure the integrity and results of HRMIS and FMIS operations.

4.77 In future audits, the ANAO will continue to focus on the IT general control environment and on FMIS and HRMIS application controls. This will include user access and privileged user access management, IT security governance, and change management. The ANAO will also continue to assess the impact on the IT controls environment of changes arising from major whole of Government change initiatives, including the data centre consolidation strategy. In addition, the ANAO intends to assess the effectiveness of the controls in agencies' legacy systems and the suitability of their general and application controls environments to meet business needs.

4.78 The ANAO will continue to monitor technology trends and the potential for changes to impact on the control environments of agencies.

5. Results of the Interim Audit Phase by Agency

This chapter summarises the results of the interim phase of the 2011–12 financial statement audits of the 25 agencies, grouped by portfolio, covered by this report.

Introduction

5.1 This chapter summarises the results of the ANAO's examination of the internal control of agencies as part of the interim phase of the audits of financial statements for the year ending 30 June 2012. These agencies comprise the portfolio departments and other entities that manage the majority of the GGS financial activities and are listed at Appendix 1.

5.2 The ANAO's audits of Australian Government agencies are designed to be performed progressively to allow agencies to submit audit cleared financial information to the Department of Finance and Deregulation (Finance)⁵⁷ for the purposes of informing the Government of the General Government Sector's financial outcome for the 2011–12 financial year. The audit reports on agencies' financial statements are issued following the receipt of signed financial statements and the completion of all audit procedures.

5.3 The final results of the audits of the agencies covered by this report will be included in the Auditor-General's report on the audits of financial statements of Australian Government agencies for the year ended 30 June 2012, expected to be tabled in December 2012.

5.4 This chapter outlines the following information for each agency:

- a summary of the agency's business operations and the key characteristics of these operations that shape the ANAO's 2011–12 overall risk assessment and audit coverage;
- key financial balances and staffing levels for 2010–11 and 2011–12⁵⁸;
- governance arrangements relevant to the agency's financial management responsibilities;

⁵⁷ The deadlines for the submission of audit cleared information are 15 August for material agencies and 31 August for non-material agencies.

⁵⁸ These figures are sourced from each agency's 2012–13 Portfolio Budget Statements, audited 2010–11 financial statements, or as advised by agencies.

- the key areas of audit focus for the audit of the 2011–12 financial statements; and
- any significant and moderate (Category A, B and L1) audit findings, and the conclusion relating to the audit coverage undertaken to date.

5.5 Category C audit findings reported to management relate to relatively minor matters and are not included in this report's summary of audit results for each agency.

5.6 The ANAO's overall assessment of the risk of material misstatement of the financial statements takes into account, for the purposes of planning the audit coverage, the significance and complexity of each agency's operations as well as the ANAO's knowledge of the agency's internal control. Key audit related business and financial statement risks are also identified and communicated to each agency. The ANAO's interim phase of the audit focuses on the steps taken by agencies to manage risks that have a potential impact on the financial statements, including their systems of internal control.

5.7 Issues identified during our audits are rated in accordance with the seriousness of the particular matter. The ratings are defined as follows:

- Category A: Issues that pose a significant business or financial management risk to the entity; these include issues that could result in the material misstatement of the entity's financial statements.
- Category B: Issues that pose a moderate business or financial management risk to the entity; these may include prior year issues that have not been satisfactorily addressed.
- Category C: Issues that pose a low business or financial management risk to the entity; these may include accounting issues that, if not addressed, could pose a moderate risk in the future.
- L1: Instances of non-compliance with: the Constitution; the agency's enabling legislation; legislation the agency is responsible for administering; and the FMA and CAC Acts.

5.8 Category B or C matters remaining unresolved at the time of the subsequent year's audit, depending on the seriousness of the issue, may be given a higher rating.

5.9 The following table provides details of the number of Category A, B and L1 findings relating to each agency identified in our 2010–11 and 2011–12 interim audits.

Table 5.1

Significant and moderate findings of agencies grouped by portfolio, reported at completion of the 2010–11 and 2011–12 interim audit phases

Entity	2011–12 Rating			2010–11 Rating		
	A	B	L1	A	B	L1
Department of Agriculture, Fisheries and Forestry	0	0	0	0	0	0
Attorney-General's Department	0	0	0	0	1	0
Australian Customs and Border Protection Service	1	3	0	0	2	0
Department of Broadband, Communications and the Digital Economy	0	0	0	0	0	0
Department of Climate Change and Energy Efficiency	0	0	0	0	0	0
Department of Defence	0	13	0	3	14	0
Defence Materiel Organisation	0	1	0	0	3	0
Department of Veterans' Affairs	0	6	0	0	2	0
Department of Education, Employment and Workplace Relations	0	1	0	0	0	0
Department of Families, Housing, Community Services and Indigenous Affairs	0	0	0	0	0	0
Department of Finance and Deregulation	0	0	0	0	0	0
The Board of Guardians and the Future Fund Management Agency	0	0	0	0	0	0
Department of Foreign Affairs and Trade	0	0	0	0	1	0
Department of Health and Ageing	0	0	0	0	0	0
Department of Human Services	0	2	0	0	1*	0
Department of Immigration and Citizenship	0	1	0	0	0	0
Department of Infrastructure and Transport	0	1	0	0	0	0
Department of Innovation, Industry, Science, Research and Tertiary Education **	0	0	0	0	0	0
Department of the Prime Minister and Cabinet	0	0	0	0	0	0
Department of Regional Australia, Local Government, Arts and Sport	0	0	0	0	0	0
Department of Resources, Energy and Tourism	0	0	0	0	0	0
Department of Sustainability, Environment, Water, Population and Communities	0	0	0	0	0	0
Department of the Treasury	0	3	0	0	1	0
Australian Office of Financial Management	0	0	0	0	0	0
Australian Taxation Office	0	0	1	0	6	1
Total	1	31	1	3	31	1

* Formerly a Centrelink finding.

** Formerly the Department of Innovation, Industry, Science and Research.

Source: ANAO

Agriculture, Fisheries and Forestry Portfolio

Department of Agriculture, Fisheries and Forestry

5.10 The Department of Agriculture, Fisheries and Forestry (DAFF) is the primary policy and advisory body to the Australian Government on agriculture, fisheries, forestry and food issues. DAFF's role is to contribute to the overall portfolio aims of enhancing the sustainability, profitability and competitiveness of Australia's agricultural, fisheries and forestry industries. This will be progressed by:

- improving productivity growth and sustainability in agriculture, fisheries, forestry and food production, including through reforming the registration of agricultural and veterinary (agvet) chemicals;
- helping farmers to mitigate and adapt to the effects of a changing climate;
- reforming national drought policy from a crisis management to a preparedness approach;
- managing biosecurity and reforming the system; and
- maintaining and developing overseas markets.

5.11 The key characteristics of DAFF's operations that shaped the ANAO's 2011–12 planned financial statement audit coverage include:

- a self assessment regime for the collection and reporting of levy revenue;
- a dependency on IT business systems and associated processes, particularly those that support grants payments and levies revenue collection;
- a Business Partnership Agreement with the Department of Human Services (DHS) in relation to personal benefit payments processed by DHS on behalf of DAFF;
- a Memorandum of Understanding between DAFF and the Australian Customs and Border Protection Service (Customs and Border Protection) that establishes arrangements for Customs and Border

Protection to collect Australian Quarantine and Inspection Service (AQIS) import fees on behalf of DAFF; and

- a determination issued by the Department of Finance and Deregulation under Regulation 5A of the *Financial Management and Accountability Regulations 1997* which had the effect of AQIS and the National Residue Survey (NRS) ceasing as business operations within DAFF, effective from 29 February 2012. As a result, DAFF will no longer be required to prepare separate financial statements for AQIS and NRS.

5.12 In the light of these characteristics and the ANAO's understanding of the operations of the department, the ANAO has assessed, for the purposes of planning the audit coverage for 2011–12, the risk of a material misstatement as moderate.

Financial overview

5.13 DAFF's key financial balances are:

Key financial balances	Departmental Estimated (\$m) 2011–12	Departmental Actual (\$m) 2010–11	Administered Estimated (\$m) 2011–12	Administered Actual (\$m) 2010–11
Net cost of services	362	345		
Revenue from government	328	354		
Administered income			412	429
Administered expenses			921	955
Total assets	288	297	299	299
Total liabilities	209	211	75	77

DAFF's estimated average staffing level for 2011–12 is 4 546 (2010–11: 4 524).

Governance arrangements

5.14 The department has designed and implemented governance arrangements, a financial reporting regime and an internal control system to enable the achievement of DAFF's business objectives. These arrangements are designed to support DAFF's financial reporting requirements, the effectiveness and efficiency of its operations and compliance with applicable legislative requirements.

5.15 The key elements of DAFF's governance arrangements include:

- a Strategic Statement that sets out the vision, mission, goals and culture that the department commits to collectively and individually. The Statement is underpinned by annual business plans at divisional level. A People Strategy complements the Strategic Statement and focuses particularly on how the department will develop its culture and support its people;
- an Executive Management Team (EMT) that meets monthly, provides leadership to DAFF's divisions on administrative and operational aspects, and provides advice to the Secretary on strategic policy, budgets and performance;
- various governance committees that support the EMT, including an audit committee that meets a minimum of five times a year and focuses on financial reporting, internal control structures, risk management systems, internal and external audit functions, and fraud control;
- a financial statements audit sub-committee that meets at least five times a year and oversees the preparation of the annual financial statements;
- an internal audit function that provides planned risk-based audit coverage of DAFF's operations, including its quarantine and biosecurity functions;
- a risk management process that involves updating strategic risk management plans at the departmental and divisional levels; and
- a fraud control plan which details DAFF's approach to identifying, monitoring and managing the risk of fraud.

Areas of audit focus

5.16 In the light of the ANAO's understanding of DAFF's environment and governance arrangements, including its financial reporting regime and system of internal control, the ANAO's audit approach identifies particular areas of audit focus that have the potential to impact on DAFF's financial statements. Areas highlighted for specific audit coverage in 2011–12 are:

- revenue and receivables in respect of primary industry levies and charges, and the operation of an associated compliance program designed and implemented by DAFF to provide assurance over the completeness and accuracy of levies received;

- quarantine revenue and receivables, of which a significant portion is collected by Customs and Border Protection on behalf of DAFF;
- personal benefit expenses and payables for drought assistance and other rural support programs that are processed by DHS on behalf of DAFF;
- DAFF's unearned revenue accounting policies and procedures, including accounting for non-reciprocal transfers in accordance with AASB 1004 *Contributions*; and
- legislative compliance, particularly the implementation of measures designed to address the risk of breaches of section 83 of the Constitution, referred to in the 2010–11 financial statements.

5.17 As an integral part of the interim audit phase, the ANAO has reviewed the IT general and application controls for key systems that support the preparation of DAFF's financial statements.

Audit results

5.18 Based on audit coverage of the areas of audit focus to date, no significant or moderate issues have been identified. Further audit coverage of the areas of audit focus will be undertaken as part of the 2011–12 final audit phase. The 2010–11 audit did not identify any significant or moderate audit issues.

Conclusion

5.19 Based on audit coverage to date, the ANAO identified that key elements of internal control were operating effectively to support the preparation of financial statements that are free of material misstatement. The effective operation of internal controls for the full financial year will be assessed during the 2011–12 final audit phase.

Attorney-General's Portfolio

Attorney-General's Department

5.20 The Attorney-General's Department (AGD) is the central policy and coordinating department of the Attorney-General's portfolio. AGD contributes to the Australian Government's commitment to a stronger, fairer and more secure Australia by striving to achieve a just and secure society through the maintenance and improvement of Australia's law and justice framework and its national security and emergency management system.

5.21 As a result of the Administrative Arrangements Order (AAOs) dated 19 October 2011, responsibility for the *Freedom of Information Act 1982*, the *Australian Information Commissioner Act 2010* and the *Privacy Act 1988* was transferred to AGD from the Department of the Prime Minister and Cabinet (PM&C).

5.22 Further Machinery of Government (MOG) changes took effect on 14 December 2011, including transferring responsibility for cyber security policy coordination to PM&C.

5.23 The key characteristics of AGD's business operations that shape the 2011–12 financial statement audit coverage include:

- an upgrade of the human resource management information system and payment module within the financial management information system;
- the governance and reporting arrangements relating to the administration of the personal benefit payment by the Department of Human Services, in the event of natural disasters, on behalf of AGD; and
- the overall effectiveness of AGD's internal controls.

5.24 In the light of these characteristics and the ANAO's understanding of the operations of the department, the ANAO has assessed, for the purposes of planning the audit coverage for 2011–12, the risk of a material misstatement as moderate.

Financial overview

5.25 AGD's key financial balances are:

Key financial balances	Departmental Estimated (\$m) 2011–12	Departmental Actual (\$m) 2010–11	Administered Estimated (\$m) 2011–12	Administered Actual (\$m) 2010–11
Net cost of services	241	237		
Revenue from government	207	219		
Administered income			19	32
Administered expenses			514	1 495
Total assets	195	237	463	448
Total liabilities	63	65	16	24

AGD's estimated average staffing level for 2011–12 is 1 482 (2010–11: 1 434).

Governance arrangements

5.26 The department has designed and implemented governance arrangements, a financial reporting regime and an internal control system to enable the achievement of AGD's business objectives. These arrangements are designed to support AGD's financial reporting requirements, the effectiveness and efficiency of its operations and compliance with applicable legislative requirements.

5.27 The key elements of AGD's governance arrangements include:

- a strategic plan that provides an overview of AGD's strategic priorities and goals, including AGD's planning and performance framework;
- the Executive Board that meets regularly to consider key strategic matters of corporate importance and set AGD's strategic direction. The Board comprises the Secretary, and deputy secretaries;
- an audit and risk management committee that meets quarterly and is chaired by an external member. The committee is responsible for overseeing the department's approach to risk management, including AGD's overall control framework and internal audit function;
- an internal audit function that plans and conducts audits based on risk assessments of departmental activities and direction from the audit and risk management committee;

- a risk management framework and risk management plan that addresses a broad range of operational risks; and
- a fraud control plan that is updated and reviewed in line with the Commonwealth Fraud Control Guidelines.

Areas of audit focus

5.28 In light of the ANAO's understanding of AGD's environment and governance arrangements, which includes its financial reporting regime and system of internal control, the ANAO's audit approach identifies particular areas of focus that have the potential to impact on AGD's financial statements. Areas highlighted for specific audit coverage in 2011–12 are:

- the accounting treatment for AGD's development of the Personal Property Security Register (PPSR) and associated ICT infrastructure, hardware and software, used to support the operation of the PPSR function by the Insolvency and Trustee Service Australia;
- grant management arrangements, including compliance with terms and conditions for new grant programs, or existing grant programs that have significantly increased;
- new functionality introduced into AGD's financial management information system; and
- legislative compliance, particularly the implementation of measures designed to ensure compliance with statutory and other legal requirements, including constitutional requirements, relevant to special appropriation and special accounts.

5.29 As an integral part of the interim audit phase, the ANAO has reviewed the IT general and application controls for key systems that support the preparation of AGD's financial statements.

Audit results

5.30 The ANAO has completed a review of internal controls relevant to the preparation of the department's financial statements and no significant or moderate audit issues were identified. The ANAO is undertaking work in relation to the areas of audit focus identified above, that will be completed during the 2011–12 final audit phase.

Conclusion

5.31 Based on our audit coverage to date, the ANAO identified that key elements of internal control were operating effectively to provide reasonable assurance that AGD can prepare financial statements that are free of material misstatement. The effective operation of these internal controls for the full financial year will be assessed during the 2011–12 final audit phase.

Australian Customs and Border Protection Service

5.32 The role of the Australian Customs and Border Protection Service (Customs and Border Protection) is to protect the safety, security and commercial interests of Australians through border protection designed to support legitimate trade and travel. In this role, Customs and Border Protection administers trade measures and certain government industry schemes, as well as collecting trade-related statistics. The collection of border-related revenue including customs duty, passenger movement charges and import processing and depot charges is also undertaken, as is the assessment and collection, where appropriate, of Goods and Services Tax (GST) on imported goods, the Wine Equalisation Tax and the Luxury Car Tax. The Tourist Refund Scheme is also managed by Customs and Border Protection on behalf of the Australian Taxation Office (ATO).

5.33 The key characteristics of Customs and Border Protection's operations that shaped the 2011–12 planned financial statement audit coverage include:

- the self-assessment nature of customs duty and the complexity of the IT infrastructure facilitating the collection of duty and other border related revenue;
- the significant amount of customs duty and GST revenue collected;
- the reporting by Customs and Border Protection of warehoused Excise Equivalent Goods (EEG) that are administered by the ATO; and
- the large number and value of assets controlled by Customs and Border Protection in undertaking their activities.

5.34 In the light of these characteristics and the ANAO's understanding of the operations of Customs and Border Protection, the ANAO has assessed, for the purposes of planning the audit coverage for 2011–12, the risk of a material misstatement as moderate.

Financial overview

5.35 Customs and Border Protection's key financial balances are:

Key financial balances	Departmental Estimated (\$m) 2011–12	Departmental Actual (\$m) 2010–11	Administered Estimated (\$m) 2011–12	Administered Actual (\$m) 2010–11
Net cost of services	1 041	1 013		
Revenue from government	935	934		
Administered income			7 750	6 590
Administered expenses			3	2
Total assets	737	689	165	109
Total liabilities	282	264	8	8

Customs and Border Protection's estimated average staffing level for 2011–12 is 5 225 (2010–11: 5 320).

Governance arrangements

5.36 Customs and Border Protection has designed and implemented governance arrangements, a financial reporting regime and an internal control system to enable the achievement of Customs and Border Protection's business objectives. These arrangements are designed to support Customs and Border Protection's financial reporting requirements, the effectiveness and efficiency of its operations, and compliance with applicable legislative requirements.

5.37 The key elements of Customs and Border Protection's governance arrangements are:

- a risk management framework that has a whole of agency focus and connects the strategic, operational and tactical levels of risk management;
- a strategic outlook document that considers the global context in which border management activities occur and evaluates in detail at the impact on border management developments;
- the preparation of an annual plan that directs the development of divisional and branch business plans. The plans identify major processes and risks which flow from the strategic outlook document described above;

- monthly executive meetings at which performance is evaluated, complemented by a bi-annual meeting of senior executives from central and regional offices to discuss strategic management issues and future directions;
- a Customs and Border Protection Practice Statement Framework which is used to define and implement the agency's national policies;
- an audit committee, with two independent members, that meets at least quarterly and focuses on internal audit and risk management issues;
- an internal audit function that has a planned risk based audit coverage of Customs and Border Protection's activities, including the management of IT systems; and
- a sound fraud control and corruption prevention framework which includes strategies for fraud and corruption preparedness, prevention, detection and resolution.

Areas of audit focus

5.38 In the light of the ANAO's understanding of Customs and Border Protection's environment and governance arrangements, that includes its financial reporting regime and system of internal control, the ANAO's audit approach identifies particular areas of audit focus that have the potential to impact on Customs and Border Protection's financial statements. Areas highlighted for specific audit coverage in 2011–12 are:

- the accuracy and completeness of customs duty collections and refunds in the light of the self-assessment nature of customs duty and the complexity of the related IT infrastructure;
- the measures in place to provide assurance over the completeness of customs duty on warehoused EEGs that are administered by the ATO;
- the completeness of Passenger Movement Charge (PMC) collections, particularly as a result of the self-assessment nature of PMC;
- the accuracy of Customs and Border Protection's assets register, particularly in relation to assets under construction;
- the transition during 2011–12 to a new human resources management information system (HRMIS); and

- legislative compliance, particularly the implementation of measures designed to address the risk of a breach of section 83 of the Constitution, referred to in the 2010–11 financial statements.

5.39 As an integral part of the interim audit phase, the ANAO has reviewed the IT general and application controls for key systems that support the preparation of Customs and Border Protection's financial statements.

Audit results

5.40 The ANAO has undertaken a review of Customs and Border Protection's IT control environment including the implementation and operation of a new HRMIS, the management of assets, and selected administered revenue. The work undertaken identified significant issues in relation to the implementation and operation of the new HRMIS. The one moderate issue from prior years relating to the management of PMC remains outstanding. These matters are detailed below. The ANAO will review selected key controls over the collection of customs duty and continue to review the implementation of the new HRMIS prior to year end, as well as reviewing compliance activity over warehoused excise equivalent goods.

5.41 The following table summarises the status of audit issues reported by the ANAO in 2010–11 and 2011–12.

Status of audit issues raised by the ANAO

Category	Findings outstanding (at the end of the 2010–11 interim audit)	Findings resolved (at the time of the 2010–11 final audit)	New findings (during the 2010–11 final audit)	Findings outstanding (at the end of the 2010–11 final audit)	Findings resolved (at the time of the 2011–12 interim audit)	New findings (during the 2011–12 interim audit)	Closing position (at the end of the 2011–12 interim audit)
A	0	0	0	0	0	1	1
B	2	1*	0	1	0	2	3
Total	2	1*	0	1	0	3	4

* One matter relating to the management of administered receivables was downgraded to a Category C finding.

New audit issues

Implementation of the Human Resources Management Information System (HRMIS)

5.42 Customs and Border Protection implemented a new HRMIS in June 2011. This system processes and records details of employee benefits and calculates and records employee provisions. Customs and Border Protection report employee benefits of approximately \$526 million and employee provisions of approximately \$147 million. A number of significant and moderate weaknesses were identified in the implementation and management of the HRMIS.

Significant audit issue

HRMIS system management, implementation and configuration issues

5.43 The new HRMIS, known as COMPASS, was implemented in June 2011 with a large number of defects and a significant number of processing and administrative controls designed to address the known system defects. There were 182 unresolved system defects at the time of the 2011–12 interim audit, a number of which affected the reliability and integrity of employee benefits and employee provisions. Weaknesses were also identified in the design and effectiveness of elements of IT security management. Separately, work undertaken by Internal Audit found a number of segregation of duty weaknesses.

5.44 These weaknesses and the impact of unresolved implementation defects increase the risk of a material misstatement of employee benefits and employee provisions as at 30 June 2012.

5.45 The weaknesses identified have also resulted in the ANAO placing limited reliance on the system controls supporting the processing and management of salaries and employee entitlements. Customs and Border Protection has committed resources to undertake a substantive review of employee benefits and employee provisions, and to prioritise the resolution of existing system defects.

Moderate audit issues

HRMIS governance arrangements

5.46 Effective governance arrangements are a key component to the design, implementation and operation of IT systems. These arrangements should clearly define processes, roles and responsibilities designed to ensure the effective management of these systems. As part of the 2011–12 interim audit,

the ANAO identified that elements of Customs and Border Protection's management and general IT governance arrangements relating to the HRMIS were not operating effectively. For example, existing change processes did not adequately prioritise and comprehensively test changes, or communicate the impact of changes to appropriate stakeholders. This breakdown in the IT governance arrangements contributed to weaknesses relating to the implementation and configuration issues described above. Customs and Border Protection has advised it is reviewing IT governance arrangements as a matter of priority.

Accuracy of employee benefits and valuation of employee provisions

5.47 The ANAO identified that the large number of unresolved system defects may have affected Customs and Border Protection's capacity to accurately calculate employee benefits and employee provisions. The ANAO considers that Customs and Border Protection will need to perform appropriate remediation work to ensure the accuracy of employee benefits and the correct valuation of employee provisions as at 30 June 2012 for reporting in the 2011–12 financial statements. Customs and Border Protection has advised that in conjunction with the review of system defects, it is undertaking a recalculation of employee transactional information and leave provisions as a matter of priority.

Prior year moderate audit issue

Passenger Movement Charge (PMC)

5.48 The PMC is a charge levied on each departing passenger from Australia. Customs and Border Protection reports PMC revenue of approximately \$615 million as administered revenue in its financial statements. It is applied and collected by airline carriers under the *Passenger Movement Charge Act 1978* and the *Passenger Charge Collection Act 1978*. The 2009–10 audit identified a number of weaknesses in the management of PMC, including a lack of analysis related to a threshold used to assess variances between amounts estimated to be received by Customs and Border Protection and the amounts actually remitted by carriers. The ANAO also identified that internal compliance activity had not been undertaken in accordance with Customs and Border Protection's policies and procedures. During the 2011–12 interim audit phase, Customs and Border Protection advised that a comprehensive review of PMC is planned for late in the 2011–12 financial year.

Conclusion

5.49 Subject to successful completion of remediation work in relation to the audit issues referred to above, the ANAO considers that Customs and Border Protection will be able to prepare financial statements free from material misstatement. The effective operation of internal controls for the full financial year will be assessed during the 2011–12 final audit phase.

Broadband, Communications and the Digital Economy Portfolio

Department of Broadband, Communications and the Digital Economy

5.50 The Department of Broadband, Communications and the Digital Economy (DBCDE) works with industry, consumer groups and regulatory authorities to develop a sustainable and internationally competitive broadband, broadcasting and communications sector that promotes the digital economy for the benefit of all Australians. DBCDE provides strategic advice and support to the Australian Government on a wide range of significant and rapidly changing policy areas including broadband, the switch over to digital television, radio spectrum management and post and telecommunications.

5.51 The key characteristics of DBCDE's business operations that shaped the ANAO's 2011–12 planned financial statement audit coverage include:

- a legislative environment that is subject to ongoing change;
- significant administered activities including programs such as the Digital Television Switchover and the National Broadband Network; and
- the reporting of significant administered assets relating to Australian Government investments in portfolio entities.

5.52 In the light of these characteristics and the ANAO's understanding of the operations of the department, the ANAO has assessed, for the purposes of planning the audit coverage for 2011–12, the risk of a material misstatement as low.

Financial overview

5.53 DBCDE's key financial balances are:

Key financial balances	Departmental Estimated (\$m) 2011–12	Departmental Actual (\$m) 2010–11	Administered Estimated (\$m) 2011–12	Administered Actual (\$m) 2010–11
Net cost of services	134	126		
Revenue from government	127	125		
Administered income			195	82
Administered expenses			1 900	1 322
Total assets	97	99	6 595	5 129
Total liabilities	31	36	29	43

DBCDE's estimated average staffing level for 2011–12 is 672 (2010–11: 651).

Governance arrangements

5.54 The department has designed and implemented governance arrangements, a financial reporting regime and an internal control system to enable the achievement of DBCDE's business objectives. These arrangements are designed to support DBCDE's financial reporting requirements, the effectiveness and efficiency of its operations and compliance with applicable legislative requirements.

5.55 The key elements of DBCDE's governance arrangements include:

- an executive management group, chaired by the Secretary, that meets fortnightly and addresses strategic issues, monitors the department's financial and non-financial performance, oversees the operational performance of divisions, and contributes to the development of DBCDE's policies and procedures;
- a performance reporting committee, chaired by the Secretary, that meets six times a year and oversees the risk management of each of DBCDE's major departmental programs and administered expense items;
- an audit committee that meets at least five times a year and has a focus on internal controls, internal and external audit activity, the management of risks, the review of financial reports, fraud control, and regulatory compliance;

- a financial statements sub-committee of the audit committee that meets at least four times a year and assists with the review of DBCDE's financial statements and other related financial matters as requested by the audit committee;
- an internal audit function that undertakes risk-based audit coverage of the department's activities;
- fraud control and risk management plans that are regularly monitored and updated; and
- a tri-annual and annual Certificate of Compliance regime which forms a key part of DBCDE's corporate governance and compliance framework.

Areas of audit focus

5.56 In the light of the ANAO's understanding of DBCDE's environment and governance arrangements, that includes a financial reporting regime and a system of internal control, the ANAO's audit approach identified particular areas of audit focus that have the potential to impact on DBCDE's financial statements. Areas highlighted for specific audit coverage in 2011–12 are:

- the valuation of administered investments, particularly the significant investments in Australian Government portfolio entities;
- the valuation of the Regional Backbone Blackspots Program reflected as an administered asset in DBCDE's financial statements;
- appropriations reporting and disclosure;
- presentation and disclosure of large administered contingent liabilities and commitments associated with the National Broadband program; and
- administered grants and subsidies expenses.

5.57 As an integral part of the interim audit phase, the ANAO has reviewed the IT general and application controls for key systems that support the preparation of DBCDE's financial statements.

Audit results

5.58 The ANAO has completed its interim audit coverage to assess the effectiveness of internal controls in the areas which had been identified as

significant to the financial statements, including administered grants and subsidies. The remaining areas of audit focus relate to work that will be undertaken as part of the 2011–12 final audit phase.

5.59 No significant or moderate audit issues have been identified during the 2011–12 interim audit phase. The 2010–11 audit did not identify any significant or moderate audit issues.

Conclusion

5.60 Based on our audit coverage to date, the ANAO identified that key elements of internal control were operating effectively to provide reasonable assurance that DBCDE can prepare financial statements that are free of material misstatement. The effective operation of these internal controls for the full financial year will be assessed during the 2011–12 final audit.

Climate Change and Energy Efficiency Portfolio

Department of Climate Change and Energy Efficiency

5.61 The Department of Climate Change and Energy Efficiency (DCCEE) is responsible for policy advice and program delivery in the areas of climate change and energy efficiency. DCCEE's primary objectives are to assist in reducing Australia's greenhouse gas emissions, promote energy efficiency, and to help shape a global climate change solution including adapting to climate change.

5.62 DCCEE's responsibilities were extended with the passage of the *Clean Energy Legislative Package* (CELP) through the Parliament in late 2011. The legislation provides for the establishment of a carbon pricing mechanism. The carbon price will apply to the energy sector, transport, industrial emissions and waste. The CELP also involves \$9.2 billion in industry assistance, establishment of a \$1 billion energy security fund, and on-going house-hold assistance and other clean energy future programs to be delivered across the Commonwealth.

5.63 The key characteristics of the department's business operations and activities that shaped the ANAO's 2011–12 planned financial statement audit coverage largely result from machinery of Government changes and include DCCEE's:

- support for a Clean Energy Regulator that was established on 2 April 2012 to administer the carbon pricing mechanism, renewable energy target, carbon farming initiative and the national greenhouse and energy reporting system, previously managed by the Office of the Renewable Energy Regulator (ORER);
- support for the establishment of a Climate Change Authority from 1 July 2012 to act as an advisor on the carbon pricing mechanism and climate change mitigation initiatives;
- management of the wind-down of the Household Insulation Program (HIP), the Foil Insulation Safety Program (FISP), the Home Insulation Safety Program (HISP), and other remediation programs; and

- consolidation of the department's offices and rationalisation of assets in 2012 as a consequence of the machinery of Government changes.

5.64 In the light of these characteristics and the ANAO's understanding of the operations of the department, the ANAO has assessed, for the purposes of planning the audit coverage for 2011–12, the risk of a material misstatement as moderate.

Financial overview

5.65 DCCEE's key financial balances are:

Key financial balances	Departmental Estimated (\$m) 2011–12	Departmental Actual (\$m) 2010–11	Administered Estimated (\$m) 2011–12	Administered Actual (\$m) 2010–11
Net cost of services	204	176		
Revenue from government	176	221		
Administered income			0	2
Administered expenses			1 342	354
Total assets	210	217	18	18
Total liabilities	40	51	48	36

DCCEE's estimated average staffing level for 2011–12 is 947 (2010–11: 905).

Governance arrangements

5.66 The department has designed and implemented governance arrangements, a financial reporting regime and an internal control system to enable the achievement of DCCEE's business objectives. These arrangements are designed to support DCCEE's financial reporting requirements, the effectiveness and efficiency of its operations and compliance with applicable legislative requirements.

5.67 The key elements of the department's governance arrangements include:

- a strategic business plan that provides an overview of DCCEE's future directions, including corporate outcomes and performance measures;
- an executive board that meets fortnightly to consider the key strategic, operational and system requirements of the department, supported by dedicated sub-committees that focus on performance, people and finance;

- an audit committee with two independent members, that meets at least quarterly and focuses on internal audit and risk management issues;
- a financial reporting framework endorsed by the audit committee;
- a financial statements sub-committee that meets four times a year and assists with the review of the department's financial statements and other related financial matters as requested;
- a structured risk management process that is used to develop and update risk management plans at the organisational and work area levels; and
- an internal audit strategy and plan that addresses key business and financial risks and aims to assist line areas meet their key objectives.

Areas of audit focus

5.68 In the light of the ANAO's understanding of DCCEE's environment and governance arrangements, including its financial reporting regime and system of internal control, the ANAO's audit approach identifies particular areas of audit focus that have the potential to impact on the DCCEE's financial statements. Areas highlighted for specific audit coverage in 2011–12 are:

- accounting for the costs of the department's administrative support for Machinery of Government changes involving the winding up of the Office of the Renewable Energy Regulator, and the establishment of the Clean Energy Regulator and the Climate Change Authority;
- the support for payments totalling \$1 billion to be made by the department in 2011–12 from the energy security fund to assist large scale coal-fired generators; these payments are dependent on the generators' verified emission levels;
- the valuation, including possible impairment, of non-financial assets in view of DCCEE's upgrading of IT infrastructure and the rationalisation of existing assets as part of the department's consolidation of its offices; and
- continuation of audit focus on the department's accounting for grants programs, including HIP remediation costs, HISP and FISP expenditure commitments, and the recovery of overpayments. Closure of the HISP and FISP remediation programs, established in 2009–10 to remediate safety issues identified with the HIP, is planned for 30 June 2012.

5.69 As an integral part of the interim audit phase, the ANAO has reviewed the IT general and application controls for key systems that support the preparation of DCCEE's financial statements.

Audit results

5.70 The ANAO has substantially completed its interim audit coverage to assess the effectiveness of internal control in those areas of audit focus that have the potential to impact on the department's financial statements. Based on audit coverage of the areas of audit focus to date, no significant or moderate issues have been identified. Audit coverage of the areas of audit focus will be completed as part of the 2011–12 final audit phase. The 2010–11 audit did not identify any significant or moderate audit issues.

Conclusion

5.71 Based on our audit coverage to date, the ANAO has identified that key elements of internal control were operating satisfactorily to provide reasonable assurance that DCCEE can prepare financial statements that are free of material misstatement. The effective operation of key controls for the full financial year will be assessed during the 2011–12 final audit phase.

Defence Portfolio

Department of Defence

5.72 The primary objective of the Department of Defence (Defence) is to protect and advance Australia's strategic interests by providing military forces for the direct defence of Australia and its unique strategic interests. To meet this objective, Defence prepares for and conducts military operations and other tasks directed by the Government.

5.73 Defence is responsible for delivering three outcomes to:

- maintain the capacity to support current commitments and provide response options to the Government to meet the range of potential future security contingencies, including working collaboratively with Australia's neighbours and the broader international defence community, and contributing to coalition operations in support of Australia's national interests;
- undertake a range of military operations at the Government's direction to ensure the defence of Australia and its national interests. The Australian Defence Force's military operations and other tasks contribute to the achievement of the Government's strategic objectives, contributing to the security of the immediate neighbourhood and supporting wider interests; and
- provide emergency and non-emergency assistance to the Government and the Australian community in non-combat related roles. These responsibilities may include emergency assistance, search and rescue, disaster recovery, surveillance, security or non-emergency law enforcement roles, and be directed by the Government or requested by other civil authorities, Government departments or agencies.

5.74 The key characteristics of Defence's business operations that shaped the 2011–12 financial statements audit coverage include:

- a multifaceted and diversified business structure that has a significant geographical spread both nationally and overseas, and is governed by an operational tempo that demands capability to deploy resources efficiently;

- changing business and control processes, including changes in accountability, the division of responsibility, shared services arrangements, and financial statements preparation processes;
- the magnitude, complexity and dispersed nature of Defence's operations which comprise inventory and asset management, storage and distribution, significant property estate management, technology research and development and project management in specialised fields such as warfare;
- the variety of information technology systems that operate independently of each other, which together with the significant estimation required for the calculation of a number of balances, contributes to risks associated with the aggregation of financial reporting information; and
- the complex arrangements between Defence and the Defence Materiel Organisation (DMO) in relation to the maintenance, acquisition, construction, and modification of equipment and systems.

5.75 In the light of these characteristics and the ANAO's understanding of the operations of the department, the ANAO has assessed, for the purposes of planning the audit coverage for 2011–12, the risk of a material misstatement as high.

Financial overview

5.76 Defence's key financial balances are:

Key financial balances	Departmental Estimated (\$m) 2011–12	Departmental Actual (\$m) 2010–11	Administered Estimated (\$m) 2011–12	Administered Actual (\$m) 2010–11
Net cost of services	23 304	22 040		
Revenue from government	23 304	21 070		
Administered income			1 333	1 354
Administered expenses			4 179	4 014
Total assets	69 887	68 519	3 058	3 051
Total liabilities	5 163	5 850	47 221	50 118

Defence's estimated average staffing level for 2011–12 is 95 463: 57 882 permanent forces, 21 250 reserves, 15 848 civilian staff and 483 professional service providers (2010–11: 96 670: 59 023 permanent forces, 21 850 reserves, 15 146 civilian staff and 651 professional service providers).

Governance arrangements

5.77 Defence has designed and implemented governance arrangements, a financial reporting regime and an internal control system to enable the achievement of its business objectives. These arrangements are designed to support Defence's financial reporting requirements, the effectiveness and efficiency of its operations, and compliance with applicable legislative requirements.

5.78 The key elements of Defence's governance arrangements include:

- a unique structure that reflects individual responsibilities and accountabilities of the Secretary and the Chief of the Defence Force for joint delivery of Defence's outcomes. Under this structure the Secretary and Chief of the Defence Force (CDF) are guided by a joint Ministerial directive detailing the expectations of the Minister;
- the Defence Committee, chaired by the Secretary, which supports the Secretary and the CDF in meeting their joint responsibilities;
- the Chiefs of Service Committee, which is chaired by the CDF, provides military advice to assist the CDF to discharge his responsibilities in command of the Defence Force and as principal military adviser to the Government;
- a governance committee framework, including the Defence Audit and Risk Committee (DARC), the Defence Capability and Investment Review Committee, and the Secretary and Chief of the Defence Force Advisory Committee;
- an internal audit function, which performs a range of internal audits across Defence and the DMO (a major provider of goods and services to Defence) and reports findings to the DARC and the Defence Executive; and
- the Financial Professionalisation, Controls and Skilling Branch which is responsible for documenting financial management risks, controls and processes, and assigning accountability for effective operation and monitoring of financial controls.

Areas of audit focus

5.79 The ANAO's audit approach identifies areas that have the potential to impact on the 2011–12 audit of Defence's financial statements. The following areas have been identified for specific audit coverage in 2011–12:

- inventory and asset management due to the material nature of the inventory and asset balances and outstanding prior year issues. These relate to weaknesses in management and supply chain business controls, supporting documentation, and the management of inventory and assets holdings at material Defence and DMO sites;
- the valuation and classification of Specialist Military Equipment (SME). These assets are a material asset balance and the assessment of asset values involves a high level of judgement and technical expertise and the accurate and complete recording of operational and capitalised expenditure associated with specialist military assets under construction (AUC). The financial and operational management of AUC is dispersed across a wide variety of projects that have complex contractual arrangements and project management requirements; and
- legislative compliance, particularly the implementation of measures designed to address the risk of a breach of section 83 of the Constitution, referred to in the 2010–11 financial statements.

5.80 In addition, the ANAO will continue to undertake audit coverage in areas previously identified as significant to the financial statements including:

- remediation activities to address weaknesses in the Financial Management Framework;
- the complex estimations involved in calculating a number of balances in Defence's financial statements, including provisions for decommissioning of SME and decontamination and restoration in relation to a large number of Defence sites both nationally and overseas;
- the calculation and reporting of commitments and contingencies that are complex and highly dependent on devolved management activities across Defence and DMO;
- management of Explosive Ordnance, due to the sensitive and material nature of these assets and Defence's remediation activities to address previously reported audit issues;

- Defence's management of complex and diversified human resource management systems; and
- the design and effectiveness of key controls over the purchase of goods and services.

5.81 The ANAO continues to review Defence's IT general and application controls, relating to the financial statements, as an integral part of the interim audit phase.

Audit results

5.82 The ANAO's interim audit phase coverage to date has included a review of the operation and remediation activities associated with the Military Integrated Logistics Information System (MILIS), including the effectiveness of the new governance arrangements, change management controls, upgrades to MILIS databases and the resolution of specific MILIS defects. The ANAO's review indicated an improvement in MILIS project governance and the management of General Stores Inventory (GSI) and Repairable Items (RI) quantities. As a result, these two significant audit issues have been downgraded to moderate. A moderate audit issue relating to payroll reconciliations between the two human resource management systems operated by Defence has also been resolved. Further details on these issues are provided below.

5.83 Other interim audit coverage to date includes Defence's purchasing expenditure, civilian and military employee expenditure, cash management, appropriations management, IT general controls, and specific application controls testing for key financial and business systems. No new significant or moderate audit issues were identified in these areas.

5.84 The other areas of audit focus will be completed as part of the 2011–12 final audit phase.

5.85 The following table summarises the status of audit issues reported by the ANAO in 2010–11 and 2011–12.

Status of audit issues raised by the ANAO

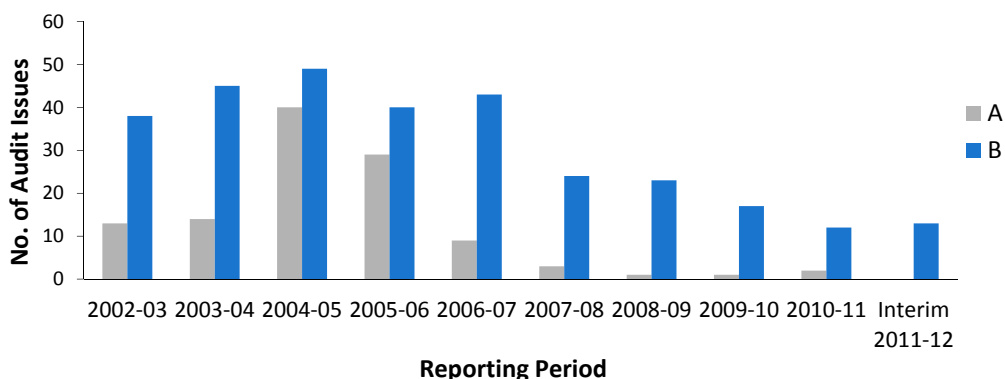
Category	Findings outstanding (at the end of the 2010–11 interim audit)	Findings resolved (at the time of the 2010–11 final audit)	New findings (during the 2010–11 final audit)	Findings outstanding (at the end of the 2010–2011 final audit)	Findings resolved (at the time of the 2011–2012 interim audit)	New findings (during the 2011–2012 interim audit)	Closing position (at the end of the 2011–2012 interim audit)
A	3	(1)	0	2	(2)*	0	0
B	14	(3)	1	12	(1)	2*	13
Total	17	(4)	1	14	(3)	2*	13

* Audit issues relating to MILIS Project Governance and GSI and RI quantities have been downgraded from Category A findings to Category B findings as explained in paragraphs 5.91 to 5.93 and 5.103.

5.86 The following figure illustrates the number of significant and moderate audit issues reported since 2002–03.

Figure 5.1

Reporting of Defence audit issues



Resolved audit issue

Human resource management

5.87 Defence uses two human resource management systems: PMKeyS for all civilian personnel transactions and military leave processing and recording; and ADFPay for military payroll processing. A moderate audit issue was raised in 2008–09 in relation to reconciliation controls between PMKeyS and ADFPay.

5.88 During the 2010–11 audit, Defence implemented a system solution to reconcile the records between PMKeyS and ADFPay. As part of the 2011–12 interim audit phase, the ANAO reviewed the reconciliation arrangements and concluded that the system solution implemented was successful in addressing the issue. As a result, the finding is considered closed.

Outstanding significant and moderate audit issues

Inventory and assets management

5.89 The 2010–11 financial year was the first year of the implementation and operation of MILIS. The impact of the implementation was wide ranging as the system underpins Defence's logistics support to operations, as well as supporting the financial reporting of inventory and asset balances.

5.90 At the conclusion of the 2010–11 audit, the ANAO reported one significant and two moderate audit findings relating to MILIS. These related to significant weaknesses in the MILIS project governance and management arrangements; change management practices, as well as issues concerning data quality.

5.91 In July 2011, Defence engaged an external IT specialist to undertake a Post Implementation Review (PIR) of MILIS. The final PIR report was delivered in October 2011 and contained 29 recommendations designed to address weaknesses in governance, requirements and design, systems integration and project management, organisational change, training and implementation and sustainment. These recommendations are in various stages of completion. Implementation activities for specific PIR recommendations have been incorporated into the MILIS Inventory Assurance Program (MIAP) Phase 3, which also commenced in July 2011. MIAP Phase 3 is focussed on MILIS remediation activities including system software changes, defect remediation, and data analysis and monitoring. These activities, by their nature, have long lead times, or require ongoing monitoring. MIAP Phase 3 forms part of the 2011–12 Inventory Assurance Strategy and is expected to be completed by 30 June 2012.

5.92 The issues raised in relation to MILIS project governance have been the subject of sustained remediation effort. The weaknesses identified included insufficient testing in an environment representative of MILIS's future operating environment; the failure to deliver critical functionality; underestimating the level of resources and problem resolution required for known defects; insufficient preparedness for the impact of the defects on the

user environment and financial statements; and non-adherence to project management procedures.

5.93 While further work is required to resolve all of the issues identified, governance frameworks and accountability lines have been established; independent assurance processes and advice are informing the governance arrangements; and there is direct engagement and feedback into the processes from a broader group of users. Based on the progression of these issues, the ANAO has downgraded the significant issue relating to MILIS project governance to a moderate audit finding. The implementation of outstanding functionality relating to financial reporting is in progress. Defence has advised that the finalisation of these activities is expected to occur by 30 June 2012.

5.94 A moderate audit finding relating to identified weaknesses in MILIS change management practices remains outstanding. The ANAO considered that a review of the design of the change management process should be undertaken, relevant policies and procedures updated and a system of regular compliance monitoring established. Defence has undertaken a review of the change management and configuration management controls and processes, and has updated procedural documentation.

5.95 The ANAO's 2011–12 interim audit phase also identified that instances of non-compliance with accepted change management processes have decreased from the prior year. However, the ANAO considers the improvements in change management compliance are the result of the strengthening in the MILIS governance arrangements and a reduction in the number of changes to the MILIS system, rather than as a result of improvements in the execution of the revised change management policies and procedures.

5.96 In addition, a moderate audit finding relating to MILIS data quality remains outstanding. In response to this finding, Defence established a Data Quality Working Group responsible for the development of MILIS data quality metrics and reports and the monitoring and investigation of data abnormalities. This program of activity forms a critical component of the MIAP Phase 3.

5.97 The ANAO's 2011–12 interim testing confirmed that data quality issues remain, and as a result the finding is outstanding. The work performed by the Data Quality Working Group has, nevertheless, assisted Defence in being able

to quantify the potential affect of the MILIS defects on the 2011–12 financial statements.

5.98 In addition to the audit issues relating to the MILIS system outlined above, at the conclusion of 2010–11 audit, five moderate audit findings relating to the inventory and asset management remained outstanding from previous years. These findings related to the following matters:

- strengthening of controls, documentation and the reporting of the cyclical stocktake program of inventory and assets;
- ensuring appropriate processes are adopted to investigate and resolve discrepancies identified during stocktakes;
- addressing deficiencies in the underlying controls that affect the quality of data within the inventory system;
- improvement of IT and business process controls necessary to ensure the timely and accurate processing of inventory returns;
- strengthening controls over the pricing of general stores inventory;
- improving the retention of supporting documentation relating to the approval to dispose of certain Defence assets; and
- strengthening the estimation processes for obsolete inventory items.

5.99 The status of these activities is discussed in paragraphs 5.100 to 5.105 below.

5.100 The ANAO observed the conduct of the Defence National Census of weapons and controlled items such as body armour and night vision equipment at selected Defence, DMO and contractor sites. While follow up activities by Defence are continuing, and the final report is not due until late June, the ANAO did not identify any issues concerning the conduct of the census at the sites visited.

5.101 The National Asset and Inventory Assurance Strategy (NAIS) is critical to providing assurance over inventory and assets balances at year end and the resolution of the audit issues relating to the stocktake process. The NAIS program involves the verification of a statistical sample of inventory and military support items at locations across Australia. As part of the 2011–12 interim audit phase, the ANAO observed Defence's execution of the NAIS program at multiple sites. The interim results have been positive although a

number of sites with larger inventory and asset holdings will not be subject to the NAIS program until mid-late June.

5.102 The important phase of remediating discrepancies identified by the stocktake activity commenced in May 2012. The manner in which discrepancies are addressed is critical to the ANAO's reliance on the overall stocktake program and the resultant adjustments to the inventory and asset balances. Defence has commenced work on the remediation process. Work in this area will be finalised after 30 June 2012.

5.103 The work undertaken for the NAIS coupled with the remediation work undertaken in relation to MILIS has resulted in the downgrading of the significant audit issue in GSI and RI quantities to a moderate audit issue.

5.104 A moderate audit finding relating to the provision for obsolescence (PFO) has been outstanding since 2008–09. The ANAO recommended that the assessment and calculation of the PFO be reviewed. Defence continues to improve the methodology and calculation of the PFO. During the 2011–12 interim audit phase, the ANAO reviewed the revised processes to confirm the PFO methodology to be used in the calculation of the balance reported in the 2011–12 financial statements. The final PFO calculation will be examined as part of the 2011–12 final audit phase.

5.105 The ANAO continues to consider MILIS managed balances to have a high risk of misstatement. The ongoing focus on MILIS remediation, in particular the successful completion of the MIAP Phase 3 activities, is critical to providing reasonable assurance that the inventory and asset balances in the 2011–12 financial statements are materially correct and controls are effective in managing financial and logistics operations.

Management of Specialist Military Assets

5.106 At the completion of the 2010–11 audit, two moderate audit issues were outstanding in relation to the need for Defence, and DMO on behalf of Defence, to strengthen management assurance processes over:

- the verification and reporting of SME assets such as simulators, computer systems that support operating aircraft and aircraft test engines; and
- assets held by third parties, including the sampling and verification methods used to gain assurance of stock holdings held by contractors.

5.107 Both of these issues remain outstanding.

5.108 The verification and reporting of SME assets is the subject of an ongoing remediation project being undertaken by DMO. The ANAO will review the results of the remediation program as part of the 2011–12 final audit phase. Until the remediation program has been completed, the ANAO will continue to independently verify a sample of these SME assets to ensure the balance is completely and accurately reported in the financial statements. The results of our review of this process will be reported as part of the 2011–12 final audit phase.

5.109 Assets held by third parties are being included as part of the activities being undertaken in the NAIS program. The NAIS program commenced in April 2012 and is expected to be completed in late June 2012. The results of the ANAO's review of this program will be reported as part of the 2011–12 final audit phase.

Financial Reporting Framework – Assurance over DMO services

5.110 The business and operational arrangements between Defence and the DMO includes requirements for DMO to manage and process financial transactions and business processes on behalf of Defence. These arrangements require Defence to have in place structured monitoring and oversight activities to provide assurance that controls over purchasing, logistics, and the acquisition of SME are effective. Weaknesses in these controls increase the risk of inaccurate balances being reported in Defence's financial statements.

5.111 At the completion of the 2010–11 audit, one moderate audit issue relating to weaknesses in the monitoring and oversight of financial transactions and business processes remained outstanding.

5.112 Defence has advised that, in conjunction with DMO, work is continuing on strengthening and documenting the assurance activities between the two agencies and that shared services arrangements relating to financial services and reporting are being implemented. The ANAO will examine the outcome of these processes as part of the 2011–12 final audit phase.

Defence's financial management information system: ROMAN

5.113 At the completion of the 2010–11 audit, one moderate audit finding relating to weaknesses in ROMAN configuration settings was outstanding.

5.114 A risk assessment has been prepared documenting the risk to the financial statements against the business requirements reflected in the current configuration settings in ROMAN. The ANAO will review the risk assessment and the effectiveness of any compensating controls outlined as part of the 2011–12 final audit phase.

IT general controls environment

5.115 In 2009–10, the ANAO reported a moderate audit issue in relation to business continuity management including:

- incomplete group level Business Impact Analysis (BIA); and
- business continuity planning requirements that remained uncompleted.

5.116 Defence has been undertaking a major business continuity project, including the preparation of business impact analyses by group and business continuity plans. Defence has advised that this project is expected to be finalised before 30 June 2012.

Conclusion

5.117 As illustrated in Figure 5.1 above, there has been an overall significant reduction in the severity and number of audit issues since 2002–03. This includes the downgrading, in the 2011–12 interim audit phase, of the remaining significant audit issues relating to inventory and asset management.

5.118 It is important to recognise the substantial improvement that Defence has achieved in its financial reporting systems and processes. The ANAO disclaimed the audit opinions on the department's financial statements for 2003–04 and 2004–05 due to the extent of uncertainty in relation to a range of material account balances which had a pervasive impact on the financial statements taken as a whole. From that time, the department has systematically addressed, in consultation with the ANAO, the weaknesses in its systems and processes to achieve this result in 2011–12.

5.119 While there is still scope for improvement in Defence's financial management processes, and Defence continues to undertake a range of remedial activities to improve key internal controls particularly over inventory and asset management, it is important to recognise the achievement of the department's leadership and staff to address the challenges of earlier years.

5.120 Defence's ability to prepare financial statements for 2011–12 free of material misstatement is dependent on the successful completion of necessary inventory and assets remediation work, and maintenance of the integrity of the wide range of other systems and processes that support the preparation of the department's financial statements. The effective operation of internal controls for the full financial year will be assessed during the 2011–12 final audit phase.

Defence Materiel Organisation

5.121 The Defence Materiel Organisation (DMO) is the primary service delivery agency responsible for the effective support of Australian Defence Force operations through the acquisition of equipment and supplies, sustainment of the Australian Defence Force, and the deployment of specialist staff. The DMO also provides industry and procurement policy and advice to the Department of Defence (Defence) and the Australian Government.

5.122 The DMO employs over 7 400 staff and contractors in over 70 locations within Australia and overseas. It budgets for a break even operating result that reflects the DMO's funding model whereby it is funded for the activities performed. These activities are principally determined by objectives set by the Australian Government, Defence policies and the operational requirements of the Australian Defence Force.

5.123 The DMO receives the majority of its funding from Defence, operating under a number of purchase-provider arrangements. The funding arrangements are formalised in agreements covering key operational areas including acquisition, sustainment, military workforce and shared services. DMO also receives an appropriation for its workforce and operating expenses.

5.124 Expenditure for acquisition activities is expected to decrease from \$5 794 million in 2010–11 to \$4 550 million in 2011–12, and sustainment activities are expected to increase from \$4 754 million to \$5 301 million.

5.125 The key characteristics of DMO's business operations that shaped the ANAO's 2011–12 planned financial statement audit coverage include:

- the effect of the remediation activities of the Military Integrated Logistics Information System (MILIS) on the purchase of inventory and assets on behalf of Defence;
- the number of significant financial statement balances;

- a complex financial statement process that involves collating data from numerous business systems and processes, and involves significant judgement in the calculation of a number of balances;
- DMO's diversified corporate and project management IT applications that operate in a number of locations nationally and overseas; and
- the number of financial and human resource business processes that are managed by Defence and are utilised by DMO.

5.126 DMO is continuing to reform business processes and procurement strategies to increase DMO's ability to deliver and support Australian Defence Force assets and support operations more efficiently and effectively. Areas of reform that have the potential to influence financial management and the 2011–12 financial statements include:

- changes to the design and operation of controls for the approval and monitoring of capital acquisition projects, including an increase in project oversight and assurance activities by capability managers and the expansion of the major capital acquisition project gate review process;
- changes to sustainment activities, in particular, new contractual arrangements and processes to achieve delivery of lower cost outputs;
- new accountability arrangements between Defence and DMO directed towards improving procurement and delivery outcomes; and
- changes to the accountability and operations of financial processes and related controls.

5.127 In the light of these characteristics and the ANAO's understanding of the operations of the DMO, the ANAO has assessed, for the purposes of planning the audit coverage for 2011–12, the risk of a material misstatement as moderate.

Financial overview

5.128 DMO's key financial balances are:

Key financial balances	Departmental Estimated (\$m) 2011–12	Departmental Actual (\$m) 2010–11	Administered Estimated (\$m) 2011–12	Administered Actual (\$m) 2010–11
Net cost of services*	925	791		
Revenue from government	931	847		
Administered income			1	2
Administered expenses			0	0
Total assets	1 931	2	4	13
Total liabilities	1 534	2 013	0	0

* Net cost of services includes payments from and on behalf of Defence of \$9 014m (2010–11: \$ 9 736m).

DMO's total estimated average staffing level is 5 993 (2010–11: 5 533). This staffing level does not reflect an additional 1 410 staff secondments from Defence to DMO.

Governance arrangements

5.129 DMO has designed and implemented governance arrangements, a financial reporting regime and an internal control system to enable the achievement of DMO's business objectives. These arrangements are designed to support DMO's financial reporting requirements, the effectiveness and efficiency of its operations and compliance with applicable legislative requirements.

5.130 The key elements of DMO's governance arrangements include:

- a Materiel Audit and Risk Committee (MARC). The MARC is comprised of four independent members and formally meets up to eight times per year. The MARC oversees the preparation of the financial statements. It formally reports to the CEO annually on matters relating to the governance framework, including:
 - enterprise risk management;
 - the efficiency and effectiveness of the existing acquisition, sustainment and financial control frameworks;
 - external accountability;
 - legislative compliance;

- internal and external audit activity; and
- the implementation of the Smart Sustainment and Procurement streams of Defence's Strategic Reform Program.

The MARC works in conjunction with the Defence Audit and Risk Committee to oversee matters of shared importance to the DMO and Defence;

- an Internal Audit function that is responsible for providing an independent, objective and systematic evaluation of risk management, the control framework, compliance and governance within DMO. Individual internal audit activities are mainly delivered by external providers in accordance with a program that is managed by the Chief Audit Executive;
- an Assurance Rationalisation Program managed by the Director General Governance and Assurance that identifies areas of risk for increased attention and ensures greater rigour and discipline is applied in managing DMO's assurance obligations;
- a Projects of Concern Unit that monitors projects that encounter significant and unanticipated issues. The unit is responsible for devising strategies to address the issues, to examine and report on performance remediation and advise the CEO and Government;
- a range of boards that monitor and report on key areas of accountability within DMO, including:
 - the Defence Strategic Reform Advisory Board (DSRAB), established to oversee the broader Strategic Reform Program in Defence that comprises public sector officials, independent members and the CEO. The chair of the MARC attends as an observer;
 - Gate Review Assurance Boards for all major capital acquisition projects that conduct formal project reviews for selected key project milestones with the aim of assuring a project's status and prospects of achieving the capability required; and
 - Project Manager Stakeholder Groups that regularly review the status and progress of major acquisition projects.

- a Fraud Control Plan supported by fraud risk assessments, an ethics awareness policy, training and Chief Executive Instructions (CEIs) on fraud control; and
- regular management reports to the CEO that detail the status of the delivery of Defence acquisition and sustainment activities. These reports are also provided on a monthly basis to Defence and central agencies.

5.131 During 2010–11, DMO redesigned its Risk Management Framework to align risks to key objectives across the organisation. The implementation of the framework is actively managed by the Director-General Governance and Assurance with regular progress updates to the MARC.

Areas of audit focus

5.132 In the light of the ANAO's understanding of DMO's environment and governance arrangements, that includes a financial reporting regime and a system of internal control, the ANAO's audit approach identified particular areas of audit focus that have the potential to impact on DMO's financial statements. Areas highlighted for specific audit coverage in 2011–12 are:

- the accounting for, and recording of, Cost of Goods Sold which involves a high number of transactions and a significant level of complexity in terms of contractual arrangements and project management requirements, given the wide variety of agreements involved;
- the accounting for, and disclosure of, prepayments which are complex in nature and subject to both material fluctuations as projects and contracts change and increase the risk of inaccurate and incomplete aggregation due to the decentralised manual recording process from which they are derived;
- the accounting for, and the reporting of, unearned income, which is an important measure of DMO's financial performance and is comprised of complex manual calculations and compilation;
- legislative compliance, particularly the implementation of measures designed to address the risk of breaches of section 83 of the Constitution, referred to in the 2010–11 financial statements;

- the aggregation of financial information from different operational areas, systems and processes; and
- the management of internal controls, where inter-dependencies between DMO and Defence systems and processes exist that may impact on financial transactions of DMO.

5.133 As an integral part of the interim audit phase, the ANAO has reviewed the IT general and application controls for key systems that support the preparation of DMO's financial statements.

Audit results

5.134 The following table summarises the status of audit issues reported by the ANAO in 2010–11 and 2011–12.

Status of audit issues raised by the ANAO

Category	Findings outstanding (at the end of the 2010–11 interim audit)	Findings resolved (at the time of the 2010–11 final audit)	New findings (during the 2010–11 final audit)	Findings outstanding (at the end of the 2010–11 final audit)	Findings resolved (at the time of the 2011–12 interim audit)	New findings (during the 2011–12 interim audit)	Closing position (at the end of the 2011–12 interim audit)
A	0	0	0	0	0	0	0
B	3	(2)*	0	1	0	0	1
Total	3	(2)	0	1	0	0	1

* One moderate audit issue relating to the reporting of commitments was downgraded to a Category C finding.

Prior year moderate audit issues

Bureau Service Arrangements between Defence and DMO

5.135 Defence manages IT systems and business processes on behalf of DMO. These systems and processes form an integral part of DMO's internal control framework to support the production of its financial statements.

5.136 DMO expects to receive assurance over the integrity of transactions processed by the systems managed by Defence, and the effectiveness of manual controls supporting these processes, as these transactions are included in the balances reported in DMO's financial statements. The ANAO has previously identified that the existing arrangements between Defence and DMO do not provide mechanisms that assist DMO to obtain the necessary

assurance from Defence over the effectiveness of controls in the following areas:

- the financial management controls and financial management information system (ROMAN);
- the human resource management system; and
- system security and change management processes.

5.137 The ANAO has also previously reported that existing shared service agreements, or other formal agreements, should include control and monitoring activities that allow DMO to obtain the necessary assurance from Defence over the effectiveness and adequacy of controls in the areas referred to above.

5.138 DMO has undertaken an assessment of the effectiveness of these controls and detailed the activities that address the risks identified by the ANAO in a position paper that has been provided to the MARC and the ANAO. In addition DMO and Defence are currently developing a new shared service arrangement to address these issues.

5.139 The activities detailed in DMO's position paper will be assessed against the revised shared services agreement during the 2011–12 final audit phase.

Conclusion

5.140 Based on audit coverage to date, and subject to resolution of the shared services issue referred to above, the ANAO considers DMO's key internal controls were operating satisfactorily to support the preparation of financial statements that are free of material misstatement. The effective operation of these internal controls for the full financial year will be assessed during the 2011–12 final audit phase.

Department of Veterans' Affairs

5.141 The Department of Veterans' Affairs (DVA) is the primary service delivery agency responsible for developing and implementing programs that assist the veteran and defence force communities. DVA also provides administrative support to the Repatriation Commission and the Military Rehabilitation and Compensation Commission.

5.142 DVA's responsibilities include:

- maintaining and enhancing the financial wellbeing and self-sufficiency of eligible persons and their dependants through access to income support, compensation, and other support services, including advice and information about entitlements;
- maintaining and enhancing the physical wellbeing and quality of life of eligible persons and their dependants through health and other care services that promote early intervention, prevention and treatment, including advice and information about health service entitlements; and
- acknowledging and commemorating those who served Australia and its allies in wars, conflicts and peace operations through promoting recognition of service and sacrifice, preservation of Australia's wartime heritage, and official commemorations.

5.143 The key characteristics of DVA's business operations that shaped the ANAO's 2011–12 planned financial statement audit coverage include:

- a complex legislative environment surrounding the provision of benefits to veterans and defence personnel;
- the diverse range of entitlements administered by DVA, and the reliance placed on voluntary disclosure of information by recipients;
- complex IT systems, including a number of legacy systems, to process a significant number of high volume, low value transactions on a regular basis; and
- extensive contractual arrangements with service providers, institutions, and state and Territory Governments.

5.144 In the light of these characteristics and the ANAO's understanding of the operations of DVA, the ANAO has assessed, for the purposes of planning the audit coverage for 2011–12, the risk of a material misstatement as moderate.

Financial overview

5.145 DVA key financial balances are:

Key financial balances	Departmental Estimated (\$m) 2011–12	Departmental Actual (\$m) 2010–11	Administered Estimated (\$m) 2011–12	Administered Actual (\$m) 2010–11
Net cost of services	321	317		
Revenue from government	296	290		
Administered income			9	9
Administered expenses			12 120	12 370
Total assets	230	242	1 316	1 309
Total liabilities	136	148	3 881	3 634

DVA's estimated average staffing level for 2011–12 is 1 990 (2010–11: 1 971).

Governance arrangements

5.146 The department has designed and implemented governance arrangements, a financial reporting regime and an internal control system to enable the achievement of DVA's business objectives. These arrangements are designed to support DVA's financial reporting requirements, the effectiveness and efficiency of its operations and compliance with applicable legislative requirements.

5.147 The key elements of DVA's governance arrangements include:

- a corporate plan that sets out DVA's focus and direction as well as the risks and challenges facing DVA. In order to assess progress against the priorities identified in the corporate plan, DVA has a monthly report card process, which includes financial, operational and strategic analysis;
- an executive management group that meets monthly to determine and evaluate progress on the agreed strategic directions of DVA. The group is supported by sub-committees that assess the overall performance of DVA's operations through a variety of reporting mechanisms;
- a financial reporting framework that involves monitoring the performance and financial management of key business areas and the preparation and monitoring of monthly financial reports;

- an information and communication technology strategic plan aimed at developing the future DVA business model and programs and corresponding IT requirements;
- a governance committee framework, including an audit and risk committee that provides independent assurance and assistance in relation to all matters relating to risk management, the control and compliance framework and external accountability. The committee also has a monitoring role in relation to the progress of internal audit and the financial statements preparation process;
- an internal audit function that develops an internal audit strategy, undertakes risk profiling across DVA and conducts an internal audit program that addresses business and financial risks;
- a fraud risk profile, which is undertaken every two years and a framework for incorporating risk management into DVA's broader management and business processes; and
- mechanisms to facilitate internal and external assurances around financial integrity, including the effectiveness of internal controls that impact on the financial statements and the Secretary's annual Certificate of Compliance.

Areas of audit focus

5.148 In the light of the ANAO's understanding of DVA's environment and governance arrangements, that includes its financial reporting regime and system of internal control, the ANAO's audit approach identifies particular areas of audit focus that have the potential to impact on DVA's financial statements. Areas highlighted for specific audit coverage in 2011–12 are:

- the significant amount of high volume, low value transactions being processed on a regular basis by complex and ageing information systems;
- the quality assurance framework over the payments made for income support and rehabilitation and compensation for veterans and their dependents;
- the complexity of assumptions and calculations underpinning the actuarial assessment of the military compensation provision;

- IT general and application controls as they relate to the financial statements; and
- legislative compliance, particularly the implementation of measures designed to address the risk of a breach of section 83 of the Constitution, referred to in the 2011–12 financial statements.

5.149 As an integral part of the interim audit phase, the ANAO has reviewed the IT general and application controls for key systems that support the preparation of DVA's financial statements.

Audit results

5.150 The ANAO's interim audit phase has focussed on the review of DVA key controls, including the design and implementation of its quality assurance framework.

5.151 The ANAO will review DVA's ongoing actions to address matters arising from the 2010–11 audit relating to: future claims for military compensation; the liability for outstanding eligible hospital payments; and the management of waivers pursuant to the *Veterans' Entitlement Act 1986* (VE Act) as part of the 2011–12 final audit phase.

5.152 The following table summarises the status of audit issues reported by the ANAO in 2011–12 and 2010–11.

Status of audit issues raised by the ANAO

Category	Findings outstanding (at the end of the 2010–11 interim audit)	Findings resolved (at the time of the 2010–11 final audit)	New findings (during the 2010–11 final audit)	Findings outstanding (at the end of the 2010–11 final audit)	Findings resolved (at the time of the 2011–12 interim audit)	New findings (during the 2011–12 interim audit)	Closing position (at the end of the 2011–12 interim audit)
A	0	0	0	0	0	0	0
B	2	(2)	2	2	0	4	6
L1	0	0	1	0*	0	0	0**
Total	2	(2)	3	2*	0	4	6**

* Legislative breaches are treated on a year by year basis.

** The position in respect of potential breaches relating to waivers will be assessed as part of the final phase of the 2011–12 audit.

Unresolved prior year moderate audit issues

Management of waivers

5.153 During the 2010–11 audit, the ANAO identified several instances where debts had been waived under provisions of the VE Act without a determination of the Repatriation Commission. The VE Act requires all waivers to have such a determination, which serves as a control for the waiving of debts.

5.154 In January 2012, DVA implemented a range of remedial measures, including issuing further advice to relevant staff, and subsequent reviews to ascertain the level of compliance with the VE Act. DVA will also need to evaluate the risk that further instances of waivers without a determination occurred before the new measures were implemented.

5.155 The ANAO will complete its review of this matter during the 2011–12 final audit phase, when the new measures will be well established and the work has been completed for the full financial year.

New moderate audit issues

Quality assurance framework

5.156 DVA has a quality assurance (QA) framework that is designed to provide assurance regarding the correctness of administrative decisions, the achievement of program and policy outcomes, and the completeness and accuracy of financial statement reporting. This framework consists of 18 individual QA programs. Two programs, the Income Support and the Rehabilitation and Compensation programs, are designed to provide a necessary level of assurance relating to veterans' income, widow/ers and disability support expenses of \$6.3 billion and military compensation expenses of \$0.9 billion⁵⁹.

5.157 During the 2011–12 interim audit phase, a number of weaknesses were identified in the design, implementation and oversight of the Income Support and Rehabilitation and Compensation QA programs. The audit identified a lack of financial quantification of identified errors, inadequate segregation of duties within the IT application used for quality assurance, a lack of an audit trail for actions completed within this application, inadequate documentation of completed procedures, and the existence of errors not previously identified by DVA.

⁵⁹ 2010–11 DVA financial statements.

5.158 The ANAO's review of the IT application (QUASARS) used in selecting samples of decisions and payments for quality assurance review and the reporting of quality assurance activities in DVA, also identified a large number of users with high levels of access, without logging and monitoring of actions performed by users within the system. This access includes the ability to amend underlying data, sample selections, and quality assurance results.

5.159 The non-quantification of QA results, together with the resolution of the above weaknesses will be addressed by DVA and the ANAO as part of the preparation and audit of the 2011–12 financial statements.

Management of user access

5.160 During 2010–11, a DVA internal audit of the Review of Application Access Controls identified weaknesses in the controls relating to access and segregation of duties for legacy systems, including the Compensation Claims Processing and the Pension Information Processing system (CCPS and PIPS). In response to that report, DVA implemented a number of additional mitigating controls.

5.161 The ANAO's 2011–12 interim audit phase identified a significant number of users who continued to have user access that resulted in inadequate segregation of duties within key payment systems, including the CCPS, PIPS, Direction Deduction and Participation Registration systems. In addition, there was no monitoring of user access. While DVA has established a number of controls seeking to address the resulting risks of providing extensive user access, the ANAO identified that these did not adequately address the risks involved. This situation significantly increases the risk of incorrect payments being made through these systems.

5.162 It was also identified that a number of the users with inadequate segregation of duties within key payment systems, also held high level access to DVA's QA IT application (QUASARS) (paragraph 5.158 above refers). The absence of a separation between payment functions and independent assurance activities without appropriate logging and monitoring of actions performed by users is a significant weakness that increases the risk that unauthorised payments are made and remain undetected.

Treatment account system

5.163 The processing of medical, hospital and allied health services claims through the treatment accounts system is performed on behalf of DVA by the Department of Human Services (DHS). To facilitate treatment in private

hospitals, DVA negotiates contracts with all private hospitals that provide for payments to be made based on an agreed schedule of fees. The claims made by the hospitals are processed either manually or online by DHS.

5.164 The ANAO identified that the treatment account system had not been configured to enforce the agreed fees for online claims. As such, there is a risk that online claims, without operator intervention, will be processed at an incorrect rate, resulting in either over or under payments.

Reconciliations

5.165 During the 2011–12 interim audit phase, the ANAO identified reconciliations between the general ledger and subsidiary systems for payroll, accounts receivable, and accounts payable, were not always completed and reviewed in a timely manner, with variances remaining unresolved for significant periods of time. Similar observations were made during the 2009–10 and 2010–11 audits in relation to payroll reconciliations. In addition, there were instances of a lack of evidence that appropriate reconciliations had been performed and reviewed for one bank account.

5.166 Overall, these weaknesses increase the risk that financial transactions are not accurately recorded and reported.

5.167 At the time of preparation of this report, DVA was finalising its responses to these issues.

Conclusion

5.168 Subject to the successful remediation of the quality assurance framework, management of segregation of duties and reporting of future claims for military compensation referred to above, the ANAO considers that DVA will be able to prepare financial statements free of material misstatement. The effective operation of internal controls for the full financial year will be assessed during the 2011–12 final audit phase.

Education, Employment and Workplace Relations Portfolio

Department of Education, Employment and Workplace Relations

5.169 The Department of Education, Employment and Workplace Relations (DEEWR) provides policy advice and administers programs to achieve the Government's objectives in the areas of education and workplace training, transition to work and workplace conditions.

5.170 The Machinery of Government changes that took effect on 14 December 2011 changed the structure and responsibilities of DEEWR. The responsibility for Tertiary Education, Skills and International functions and policy was transferred to the Department of Industry, Innovation, Science, Research and Tertiary Education (DIISRTE). Programs transferred included Higher Education Support, the Higher Education Loan Program (HELP), Tertiary Student Assistance programs and Vocational Education and Training programs.

5.171 DEEWR's responsibilities include:

- program management and delivery aimed at providing universal access to high quality education, world-class teaching and learning in schools;
- investment in employment and training services for the unemployed and disadvantaged to support the Government's workforce participation and social reform agendas; and
- the delivery of personal benefits including child care benefit, child care rebate and parenting allowance that aim to remove barriers to employment and education opportunities.

5.172 The key characteristics of DEEWR's business operations that shaped the ANAO's 2011–12 financial statements audit coverage include:

- the significance and diversity of administered activities including personal benefits, employment service payments and a large number of diverse grant programs;

- reliance on data from third parties to support personal benefit payments, including those relating to employment services, child care benefits and rebates; and
- a complex financial statement process that involves using data from a number of business systems and other agencies.

5.173 In the light of these characteristics and the ANAO's understanding of the operations of the department, the ANAO has assessed, for the purposes of planning the audit coverage for 2011–12, the risk of a material misstatement as moderate.

Financial overview

5.174 DEEWR's key financial balances are:

Key financial balances	Departmental Estimated (\$m) 2011–12	Departmental Actual (\$m) 2010–11	Administered Estimated (\$m) 2011–12	Administered Actual (\$m) 2010–11
Net cost of services	845	852		
Revenue from government	740	740		
Administered income			682	1 359
Administered expenses			36 605	42 550
Total assets	449	475	924	19 938
Total liabilities	274	275	3 489	8 711

DEEWR's estimated average staffing level for 2011–12 is 4 738 (2010–11: 5 089).

Governance arrangements

5.175 DEEWR has designed and implemented governance arrangements, a financial reporting regime and an internal control system to provide reasonable assurance about the achievement of DEEWR's business objectives. These arrangements are designed to support the achievement of DEEWR's financial reporting requirements, the effectiveness and efficiency of its operations and compliance with applicable legislation requirements.

5.176 The key elements of DEEWR's governance arrangements include:

- an executive management group that meets regularly and addresses strategic issues, monitors DEEWR's financial performance, and oversees the operational performance of groups and programs;

- a governance committee framework, including an audit committee. The audit committee meets at least quarterly and focuses attention on the effectiveness and probity of audit activities including risk assessment and management;
- a structured system of internal control;
- an internal audit function providing a risk based audit coverage of DEEWR's activities;
- mechanisms to facilitate internal and external assurances in relation to financial integrity, including the effectiveness of internal controls that may impact on the financial statements and the Secretary's annual Certificate of Compliance;
- a framework for incorporating risk management and the consideration of fraud risk into DEEWR's broader management and business planning processes; and
- a financial reporting framework that involves the monitoring of the performance and financial management of key business areas and the preparation and monitoring of monthly financial reports.

Areas of audit focus

5.177 In the light of the ANAO's understanding of DEEWR's environment and governance arrangements, that includes a financial reporting regime and system of internal control, the ANAO's audit approach identifies particular areas of audit focus that have the potential to materially affect DEEWR's financial statements. Areas highlighted for specific audit coverage in 2011–12 are:

- compliance activities and assurance processes underpinning personal benefits, child care and employment related payments;
- the financial management of grants as the management of grants is dispersed across a wide variety of programs and different business systems;
- the judgements and estimates in DEEWR's financial statements including the accrual elements of administered programs required to be reported at year end;

- legislative compliance, particularly the implementation of measures designed to address the risk of breaches of section 83 of the Constitution, referred to in the 2010–11 financial statements;
- the completeness and accuracy of balances transferred to DIISRTE as a result of the Machinery of Government changes in December 2011; and
- progress in addressing the significant audit finding in 2010–11 relating to user access controls and the change management process for the Training and Youth Internet Management System (TYIMS).

5.178 As an integral part of the interim audit phase, the ANAO has reviewed the IT general and application controls for key systems that support the preparation of DEEWR's financial statements.

Audit results

5.179 The ANAO has reviewed the compliance activities and assurance processes relating to personal benefits and child care related payments, as well as the grant management processes. No new significant or moderate issues have been identified. The remaining areas of audit focus relate to work that will be undertaken as part of the 2011–12 final audit phase.

5.180 The following table summarises the status of audit issues reported by the ANAO in 2010–11 and 2011–12.

Status of audit issues raised by the ANAO

Category	Findings outstanding (at the end of the 2010–11 interim audit)	Findings resolved (at the time of the 2010–11 final audit)	New findings (during the 2010–11 final audit)	Findings outstanding (at the end of the 2010–11 final audit)	Findings resolved (at the time of the 2011–12 interim audit)	New findings (during the 2011–12 interim audit)	Closing position (at the end of the 2011–12 interim audit)
A	0	0	1	1	(1)*	0	0
B	0	0	0	0	0	1	1
Total	0	0	1	1	(1)	1	1

* This matter has been downgraded from a Category A to a Category B finding as explained in paragraphs 5.181 to 5.184 below.

Prior year significant audit issue

IT system access and change management

5.181 In 2010–11, the ANAO reviewed the access controls and change management processes for the Training and Youth Internet Management System (TYIMS) and identified that there was a significant risk that unauthorised changes could be made to the software application without being detected. TYIMS is an IT application that manages payments under the Australian Apprentices Incentive Program to Australian Apprenticeship Centres, apprentices and employers of apprentices. These payments totalled approximately \$1 280 million in 2010–11 and in 2011–12 the total budgeted payments are approximately \$704 million. This program was transferred to DIISRTE as part of the Administrative Arrangements Order of 14 December 2011.

5.182 During the 2011–12 interim audit phase, the ANAO identified that DEEWR had implemented access controls to reduce the risk of unauthorised changes being made to the TYIMS production environment. DEEWR had also migrated TYIMS to the department's standard change management process that included new IT access arrangements.

5.183 The ANAO identified that, during the September 2011 quarter, the new access arrangements had been bypassed. In the September quarter, revised access arrangements were followed that enabled software developers to make changes to the TYIMS production environment. Under these arrangements system changes were unable to be monitored. This situation increased the risk that unauthorised changes could again be made to the software application in the production environment without being detected. Following the changes, DEEWR reverted to the department's standard change management process.

5.184 The implementation of access controls and the migration of TYIMS to the standard change management process have reduced the risk that unauthorised changes can be made. As a result, this issue has been downgraded to a moderate audit issue. However, where access is granted outside these controls a moderate business risk including potential fraud exposure still remains. The ANAO will undertake additional audit procedures including a review of DEEWR's change management process for the full financial year to gain assurance that payments disclosed in the financial statements are not materially misstated.

Conclusion

5.185 Based on audit coverage to date, the ANAO identified that key elements of internal control were operating effectively to support the preparation of financial statements that are free of material misstatement. The effective operation of internal controls for the full financial year will be assessed during the 2011–12 final audit phase.

Families, Housing, Community Services and Indigenous Affairs Portfolio

Department of Families, Housing, Community Services and Indigenous Affairs

5.186 The role of the Department of Families, Housing, Community Services and Indigenous Affairs (FaHCSIA) is to provide social policy advice to the Australian Government and deliver the Australian Government's social policy agenda. FaHCSIA aims to improve the lives of Australians by creating opportunities for economic and social participation by individuals, families and communities. The seven core areas in which FaHCSIA seeks to assist people are: families and children; housing; community capability and the vulnerable; seniors; disability and carers; women; and Indigenous.

5.187 As result of the Administrative Arrangements Order (AAO) of 14 December 2011, responsibility for affordable housing, which includes the National Rental Affordability Scheme, the Housing Affordability Fund, and the Building Better Regional Cities sub-programs, was transferred to FaHCSIA from the Department of Sustainability, Environment, Water, Population and Communities.

5.188 FaHCSIA has four key modes of business delivery to achieve its aims:

- payments to individuals—FaHCSIA makes a range of direct payments to individuals through DHS, and other agencies including the Age Pension, the Disability Support Pension and the Family Tax Benefit;
- working with the states and territories—FaHCSIA works with the states and territories to achieve outcomes in their areas of responsibility including housing, disability services, addressing Indigenous disadvantage, concessions and the welfare of children;
- payments for community services—FaHCSIA funds community-based organisations to deliver a range of local services, including family relationship services, emergency relief and supported employment for people with a disability; and
- policy development, leadership, advice and coordination—FaHCSIA supports its Ministers in their policy roles by providing advice on social policy, building the evidence base for decisions and action and in

whole of Government policy coordination for Indigenous affairs and for women.

5.189 The key characteristics of FaHCSIA's business operations that shaped the ANAO's 2011–12 planned financial statement audit coverage include:

- reliance on other Government agencies to deliver personal benefit payments that are reported in FaHCSIA's financial statements;
- significant judgements involved in estimating material financial statement balances, such as the Family Tax Benefit provision;
- the need to comply with numerous grant payment conditions, and a decentralised grant management function; and
- the legislative and accounting standards compliance regime relating to high value and complex transactions.

5.190 In the light of these characteristics and the ANAO's understanding of the operations of the department, the ANAO has assessed, for the purposes of planning the audit coverage for 2011–12, the risk of a material misstatement as moderate.

Financial overview

5.191 FaHCSIA's key financial balances are:

Key financial balances	Departmental Estimated (\$m) 2011–12	Departmental Actual (\$m) 2010–11	Administered Estimated (\$m) 2011–12	Administered Actual (\$m) 2010–11
Net cost of services	592	583		
Revenue from government	533	519		
Administered income			178	440
Administered expenses			79 850	72 862
Total assets	334	362	5 456	5 066
Total liabilities	130	129	8 349	8 048

FaHCSIA's estimated average staffing level for 2011–12 is 2 754 (2010–11: 2 686).

Governance arrangements

5.192 The department has designed and implemented governance arrangements, a financial reporting regime and an internal control system to enable the achievement of FaHCSIA's business objectives. These arrangements are designed to support FaHCSIA's financial reporting requirements, the effectiveness and efficiency of its operations and compliance with applicable legislative requirements.

5.193 The key elements of FaHCSIA's governance arrangements include:

- an Executive Management Group (EMG) that meets fortnightly. The EMG takes an active interest in the financial operations of FaHCSIA and receives monthly detailed reports from the Chief Financial Officer (CFO);
- a committee framework, including the Assurance, Audit and Risk Committee (AARC). The AARC meets at least quarterly and focuses attention on risk management and the effectiveness of the control environment, particularly in relation to financial systems, accounting processes and related controls. A financial statements sub-committee, comprising an independent AARC member, the CFO and a FaHCSIA Branch Manager, monitors and reviews FaHCSIA's financial reporting timetable and requirements;
- an Audit, Assurance and Risk Branch that undertakes risk-based audit coverage of FaHCSIA's activities;
- a risk management framework that promotes a coordinated risk management regime, and a risk management toolkit that encourages staff to apply risk management principles. FaHCSIA has recently initiated a project to review its approach to risk management with a view to strengthening the department's risk management framework; and
- a fraud control plan.

Areas of audit focus

5.194 In the light of the ANAO's understanding of FaHCSIA's environment and governance arrangements, that includes its financial reporting regime and system of internal control, the ANAO's audit approach identifies particular

areas of audit focus that have the potential to impact on FaHCSIA's financial statements. Areas highlighted for specific audit coverage in 2011–12 are:

- personal benefits payments and related debts that are processed by DHS;
- FaHCSIA's management controls over personal benefit payments as it has ultimate responsibility for the administration, funding and reporting of the benefit payments;
- the valuation of personal benefit related asset and liability balances; and
- legislative compliance, particularly the implementation of measures designed to address the risk of non-compliance with section 83 of the Constitution, referred to in the 2010–11 financial statements.

5.195 The ANAO's audit coverage includes the following areas which have previously been identified as having a significant impact on the financial statements:

- the financial management of grants, including the adequacy of supporting documentation on action taken on grant acquittals;
- the identification and valuation of investments in fixed deposits and Government securities; and
- accounting processes and controls designed to ensure that transactions relating to various special accounts comply with their legislative purpose.

5.196 As an integral part of the interim audit phase, the ANAO has reviewed the IT general and application controls for key systems that support the preparation of FaHCSIA's financial statements.

Audit results

5.197 The ANAO has substantially completed its interim audit phase coverage to assess the effectiveness of internal controls in those areas of audit focus that have the potential to impact on FaHCSIA's financial statements, including audit coverage of IT application controls and grants accounting. Further audit work on those areas of audit focus will be completed as part of the 2011–12 final audit phase.

5.198 No significant or moderate audit issues have been identified during the 2011–12 interim audit phase. The 2010–11 audit did not identify any significant or moderate audit issues.

Conclusion

5.199 Based on audit coverage to date, the ANAO identified that key elements of internal control were operating effectively to support the preparation of financial statements that are free of material misstatement. The effective operation of these internal controls for the full financial year will be assessed during the 2011–12 final audit phase.

Finance and Deregulation Portfolio

Department of Finance and Deregulation

5.200 The Department of Finance and Deregulation (Finance) assists the Government to achieve its outcomes in a variety of policy and program areas, particularly with regard to its fiscal and economic plans, deregulation reform and the operations of Government. Services delivered by Finance include assisting Government to make informed decisions on Government finances and regulation making through: budgetary management and advice; transparent financial reporting; implementation of a robust financial framework; and best practice regulatory processes. Finance also has a focus on improving Government administration and operations through policy, systems and advice on: procurement; Commonwealth property management and construction; Government enterprises; risk management; and the application of information and communications technology. Finance also provides support for Parliamentarians, organisations and others with entitlements as approved by Government, through the delivery of entitlements and targeted assistance.

5.201 The key characteristics of Finance's business operations that shaped the ANAO's 2011–12 planned financial statement audit coverage include:

- a number of financial statement balances that require significant judgement, or the use of specialists, to estimate;
- a complex financial statement process that involves using data from a number of business systems; and
- numerous arrangements with service providers that effect key financial statement balances.

5.202 In the light of these characteristics and the ANAO's understanding of the operations of the department, the ANAO has assessed, for the purposes of planning the audit coverage for 2011–12, the risk of a material misstatement as moderate.

Financial overview

5.203 Finance's key financial balances are:

Key financial balances	Departmental Estimated (\$m) 2011–12	Departmental Actual (\$m) 2010–11	Administered Estimated (\$m) 2011–12	Administered Actual (\$m) 2010–11
Net cost of services	192	256		
Revenue from government	233	240		
Administered income			2 320	4 489
Administered expenses			11 586	10 703
Total assets	2 369	2 150	17 812*	22 603**
Total liabilities	498	504	91 379	95 484

* The 2011–12 Administered Estimated figure excludes the cash held in the Official Public Account as this is not included in Finance's estimate.

**The 2010–11 Administered Actual total assets figure has been adjusted to exclude the Official Public Account (\$747m).

Finance's estimated average staffing level for 2011–12 is 1 645 (2010–11: 1 560).

Governance arrangements

5.204 The department has designed and implemented governance arrangements, a financial reporting regime and an internal control system to enable the achievement of Finance's business objectives. These arrangements are designed to support Finance's financial reporting requirements, the effectiveness and efficiency of its operations and compliance with applicable legislative requirements.

5.205 The key elements of Finance's corporate governance are:

- an executive board that meets monthly and addresses policy, program, strategic and management issues and oversights Finance's operational and financial performance;
- an audit committee, chaired by an independent member, that meets at least quarterly and focuses on risk management, internal controls, compliance, financial reporting and ANAO activities;
- an internal audit function providing an internal audit strategy and plan that addresses key business and financial risks and aims to assist line areas meet their key objectives;

- mechanisms to facilitate internal and external assurances around financial integrity, including the effectiveness of internal controls that impact on the financial statements and Finance's annual Certificate of Compliance;
- a risk management process that includes an assessment of inherent and control risks, identification of the controls in place to address these risks both at an organisational and discrete activity level, and an understanding of the residual risks that remain and how these can be managed to an acceptable level;
- a financial reporting framework that involves the monitoring of the performance and financial management of key business areas and the preparation and monitoring of monthly financial reports; and
- a fraud risk assessment process and fraud control plan.

Areas of audit focus

5.206 In the light of the ANAO's understanding of Finance's environment and governance arrangements, that includes its financial reporting regime and system of internal control, the ANAO's audit approach identifies particular areas of audit focus that have the potential to impact on Finance's financial statements. Areas highlighted for specific audit coverage in 2011–12 are:

- the complexity of the assumptions and calculations underpinning the actuarial assessment of the public sector unfunded superannuation liability;
- the valuation of the Australian Government's domestic property portfolio and the adequacy of asset management procedures;
- the financial management of the Australian Government's self-managed general insurance fund (Comcover);
- the control regime in relation to entitlements paid to Parliamentarians and their staff; and
- legislative compliance, particularly the implementation of measures designed to address the risk of a breach of section 83 of the Constitution, referred to in the 2010–11 financial statements.

5.207 As an integral part of the interim audit phase, the ANAO has reviewed the IT general and application controls for key systems that support the preparation of Finance's financial statements.

Audit results

5.208 No significant or moderate audit issues have been identified during the 2011–12 interim audit phase. The 2010–11 audit did not identify any significant or moderate audit issues.

Conclusion

5.209 Based on audit coverage to date, the ANAO identified that key elements of internal control were operating effectively to provide reasonable assurance that Finance can prepare financial statements that are free of material misstatement. The effectiveness of these internal controls for the full financial year will be completed during the 2011–12 final audit phase.

The Board of Guardians and the Future Fund Management Agency

5.210 The Future Fund Management Agency (FFMA) was established by the *Future Fund Act 2006* to support and advise the Future Fund Board of Guardians (Board) in its task of investing the assets of the Future Fund.

5.211 The FFMA's responsibilities include:

- continued development and implementation of an investment strategy for the Future Fund and the three Nation Building Funds – the Building Australia Fund, the Education Investment Fund and the Health and Hospitals Fund, agreed by the Board and consistent with the investment mandate from Government;
- investing the assets of the Future Fund and the three Nation Building Funds in accordance with the relevant investment strategies; and
- maximisation of returns earned on contributions to the Future Fund over the long term, in line with the investment mandate.

5.212 The key characteristics of the FFMA's business operations that shaped the ANAO's 2011–12 planned financial statement audit coverage include:

- complexities associated with the valuation of different investment instruments;

- the use of external service providers to support the investment management function; and
- a complex organisational structure involving a number of subsidiaries, used as special purpose investment vehicles, and associated tax implications.

5.213 In the light of these characteristics and the ANAO's understanding of the operations of the FFMA, the ANAO has assessed, for the purposes of planning the audit coverage for 2011–12, the risk of a material misstatement as moderate.

Financial overview

5.214 FFMA's key financial balances⁶⁰ are:

Key financial balances	Estimated (\$m) 2011–12	Actual (\$m) 2010–11
Total Income	2 975	8 640
Total Expenses	328	615
Operating Result	2 647	8 025
Total assets	78 261	77 512
Total liabilities	307	2 205

FFMA's estimated average staffing level for 2011–12 is 86 (2010–11: 75).

Governance arrangements

5.215 The Board, supported by the FFMA, has designed and implemented governance arrangements, a financial reporting regime and an internal control system to about the achievement of the Board's business objectives. These arrangements are designed to support the organisation's (Board and FFMA) financial reporting requirements, the effectiveness and efficiency of its operations, and compliance with applicable legislative requirements.

5.216 The key elements of the FFMA's governance arrangements include:

- a strategic asset allocation that provides an overview of the Board's investment plan;

⁶⁰ The Future Fund presents its financial statements in a format consistent with that used in the funds management industry and the funding of the FFMA is drawn from the investment special account. For 2011–12 this funding is estimated to be \$35 million.

- meetings of the Future Fund Board of Guardians at least 10 times per year;
- a governance committee framework, including a Board audit committee and a FFMA operational risk and compliance committee;
- an internal audit function providing an internal audit strategy and plan that addresses key business and financial risks and is approved by the Board audit committee;
- mechanisms to facilitate internal and external assurances in respect of financial integrity, including the effectiveness of internal controls that impact on financial records;
- the use of a Risk and Control matrix to support the FFMA in monitoring the key risks of the organisation;
- a financial reporting framework that involves the monitoring of the performance and financial management of key business areas including the preparation of monthly financial reports; and
- significant operational controls that reside with the outsourced custodian. These controls are subject to an independent bi-annual internal controls audit which tests that the controls are appropriately designed and are operating effectively. A substantive independent audit is also undertaken at 30 June each year to confirm the existence and valuation of investment assets.

Areas of audit focus

5.217 In the light of the ANAO's understanding of the FFMA environment and governance arrangements, that includes its financial reporting regime and system of internal control, the ANAO's audit approach identifies particular areas of audit focus that have the potential to impact on FFMA financial statements. Areas highlighted for specific audit coverage in 2011–12 are:

- the valuation of investments from the perspectives of governance, financial accuracy and regulatory oversight;
- the compliance function that reinforces internal assurance procedures;
- the processes for monitoring external service providers, including the custodian;

- group consolidation and tax implications relating to wholly owned subsidiaries; and
- ensuring that the FFMA operations, as reflected in the special accounts, meet constitutional requirements.

5.218 As an integral part of the interim audit phase, the ANAO has reviewed the IT general and application controls for key systems that support the preparation of FFMA's financial statements.

Audit results

5.219 There were no significant or moderate audit issues identified during the 2011–12 interim audit phase. The 2010–11 audit did not identify any significant or moderate audit issues.

Conclusion

5.220 Based on audit coverage to date, the ANAO identified that key elements of internal control were operating effectively to provide reasonable assurance that FFMA can prepare financial statements that are free of material misstatement. The effectiveness of these internal controls for the full financial year will be completed during the 2011–12 final audit phase.

Foreign Affairs and Trade Portfolio

Department of Foreign Affairs and Trade

5.221 The Department of Foreign Affairs and Trade's (DFAT) role is to advance the interests of Australia and Australians internationally.

5.222 DFAT's outcomes include:

- the advancement of Australia's international strategic, security and economic interests through bilateral, regional and multilateral engagement on Australian Government foreign and trade policy priorities;
- the protection and welfare of Australians abroad and access to secure international travel documentation through timely and responsive travel advice, and consular and passport services in Australia and overseas; and
- a secure Australian Government presence overseas through the provision of security services and information and communications technology infrastructure, and the management of the Australian Government's overseas owned estate.

5.223 The key characteristics of DFAT's business operations that shaped the ANAO's 2011–12 planned financial statement audit coverage include:

- the geographical spread of operations;
- the importance of DFAT's IT environment; and
- the reliance on external service providers for key operations and financial information. Under service level arrangements with DFAT, these service providers provide revenue collection services for passport applications and undertake a range of property, financial and facilities management services for the overseas estate.

5.224 In the light of these characteristics and the ANAO's understanding of the operations of the department, the ANAO has assessed, for the purposes of planning the audit coverage for 2011–12, the risk of a material misstatement as low.

Financial overview

5.225 DFAT's key financial balances are:

Key financial balances	Departmental Estimated (\$m) 2011–12	Departmental Actual (\$m) 2010–11	Administered Estimated (\$m) 2011–12	Administered Actual (\$m) 2010–11
Net cost of services	861	846		
Revenue from government	824	876		
Administered income			423	421
Administered expenses			294	286
Total assets	3 027	2 935	505	415
Total liabilities	259	262	56	65

DFAT's estimated average staffing level for 2011–12 is 3 916 (2010–11: 3 855).

Governance arrangements

5.226 DFAT has designed and implemented governance arrangements, a financial reporting regime and an internal control system to provide reasonable assurance about the achievement of DFAT's business objectives. These arrangements are designed to support the achievement of DFAT's financial reporting requirements, the effectiveness and efficiency of its operations and compliance with applicable legislative requirements.

5.227 The key elements of DFAT's governance arrangements include:

- an executive committee that oversees the operational performance of divisions and posts, reviews departmental wide issues, monitors financial performance and considers reports prepared and referred by other management committees;
- a governance committee framework including an audit and risk committee. This committee meets at least quarterly and has a focus on the efficiency, effectiveness and probity of activities including risk assessment and management, internal audit planning and results, fraud control and ANAO audit activities;
- a risk management framework and plan that identifies and assists in the management of risk at the strategic, business and project levels, and also at specific locations overseas; and

- an internal audit strategy and plan that aligns with the department's risk assessment and management priorities.

Areas of audit focus

5.228 In the light of the ANAO's understanding of DFAT's environment and governance arrangements, including the financial reporting regime and system of internal control, the ANAO's audit approach identifies particular areas of audit focus that are significant in DFAT's financial statements. Areas highlighted for specific audit coverage in 2011–12 are:

- revenue generated from passport operations. A majority of the passport revenue collections are outsourced to the Australian Postal Corporation;
- the completeness of departmental revenue for rental accommodation and services provided to other Government agencies at overseas posts;
- valuation of the Australian Government's overseas property;
- the accounting treatment and disclosure of the transactions in the National Interest Account (NIA). The NIA manages transactions undertaken by the Export Finance and Insurance Corporation as directed by the Minister after consideration of whether they are in the national interest; and
- executive remuneration and appropriation note disclosures.

5.229 As an integral part of the interim audit phase, the ANAO has reviewed the IT general and application controls for key systems that support the preparation of DFAT's financial statements.

Audit results

5.230 To date, the ANAO's audit coverage of IT general and application controls and overseas operations has not identified any significant or moderate audit issues.

Conclusion

5.231 Based on audit coverage to date, the ANAO identified that key elements of internal control were operating effectively to support the preparation of financial statements that are free of material misstatement. The effective operation of internal controls for the full financial year will be assessed during the 2011–12 final audit phase.

Health and Ageing Portfolio

Department of Health and Ageing

5.232 The role of the Department of Health and Ageing (DoHA) is to achieve better health and active ageing for all Australians. DoHA works to achieve this through its policy advice, management of programs, research and regulation activities, and working closely with other governments, Government agencies, consumers and other stakeholders.

5.233 DoHA's responsibilities relate to: population health; pharmaceutical services; medical services; aged care and population ageing; primary care; rural health; hearing services; Indigenous health; private health; health system capacity and quality; mental health; health workforce capacity; acute care; and biosecurity and emergency response.

5.234 The key characteristics of DoHA's business operations that shaped the ANAO's 2011–12 planned financial statements audit coverage include:

- a complex operating environment that involves working with multiple government jurisdictions and agencies, and a range of other stakeholders;
- the significant size of administered payments, which include high volume and complex Medicare and pharmaceutical personal benefits and aged care subsidies processed by the Department of Human Services on behalf of DoHA, and significant grant payments to State and Territory Governments, other service providers and program recipients;
- a complex funding model and extensive appropriations disclosure in relation to the department's 14 outcomes; and
- the consolidation of departmental business operations in DoHA's financial statements.

5.235 In the light of these characteristics and the ANAO's understanding of the operations of the department, the ANAO has assessed, for the purposes of planning the audit coverage for 2011–12, the risk of a material misstatement as moderate.

Financial overview

5.236 DoHA's key financial balances are:

Key financial balances	Departmental Estimated (\$m) 2011–12	Departmental Actual (\$m) 2010–11	Administered Estimated (\$m) 2011–12	Administered Actual (\$m) 2010–11
Net cost of services	659	617		
Revenue from government	627	600		
Administered income			975	1 306
Administered expenses			49 519	44 721
Total assets	462	462	1 087	945
Total liabilities	272	263	2 703	2 851

DoHA's estimated average staffing level for 2011–12 is 4 758 (2010–11: 4 753).

Governance arrangements

5.237 DoHA has designed and implemented governance arrangements, a financial reporting regime and an internal control system to provide reasonable assurance about the achievement of DoHA's business objectives. These arrangements are designed to support the achievement of DoHA's financial reporting requirements, the effectiveness and efficiency of its operations and compliance with applicable legislative requirements.

5.238 The key elements of DoHA's governance arrangements include:

- an executive committee, chaired by the Secretary, that is responsible for the management and oversight of all major department policy, financial and operational decision making;
- a governance committee framework including an audit committee that includes two independent members, one of whom is the Chair, meets at least quarterly and provides advice and assistance on risk, control and compliance frameworks;
- an internal audit function that has primary responsibility for promoting and improving corporate governance within DoHA and operates under the direction of the Secretary and the audit committee;

- a risk management framework including Chief Executive Instructions, Procedural Rules, a Risk Management Policy and an Enterprise Risk Management Plan;
- a fraud control plan that is monitored and reviewed on a cyclical basis in line with the Government's fraud control policy;
- a Certificate of Compliance regime that incorporates semi-annual control self assessment, that form a key part of DoHA's corporate governance and compliance framework; and
- governance arrangements with the Department of Human Services to manage the relationship between the two agencies regarding significant administered payments.

Areas of audit focus

5.239 In the light of the ANAO's understanding of DoHA's environment and governance arrangements, that includes a financial reporting regime and system of internal control, the ANAO's audit approach identified particular areas of audit focus that have the potential to impact on DoHA's financial statements. Areas highlighted for specific audit coverage in 2011–12 are:

- the high volume and complex administered personal benefits and subsidies;
- actuarial estimation for the reporting of the Government's liabilities under the medical indemnity program;
- the diverse range of administered grant payments;
- the complexity of appropriations reporting and disclosure; and
- legislative compliance, particularly the implementation of measures designed to address the risk of non-compliance with section 83 of the Constitution, referred to in the 2010–11 financial statements.

5.240 As an integral part of the interim audit phase, the ANAO has reviewed the IT general and application controls for key systems that support the preparation of DoHA's financial statements.

Audit results

5.241 The ANAO has completed its interim audit phase coverage to assess the effectiveness of internal controls in the areas which had been identified as

significant to the financial statements, including administered grants, personal benefits and subsidies. The remaining areas of audit focus relate to work that will be undertaken as part of the 2011–12 final audit phase.

5.242 No significant or moderate audit issues were identified during the 2011–12 interim audit phase.

5.243 The following table summarises the status of audit issues reported by the ANAO in 2010–11 and 2011–12.

Status of audit issues raised by the ANAO

Category	Findings outstanding (at the end of the 2010–11 interim audit)	Findings resolved (at the time of the 2010–11 final audit)	New findings (during the 2010–11 final audit)	Findings outstanding (at the end of the 2010–11 final audit)	Findings resolved (at the time of the 2011–12 interim audit)	New findings (during the 2011–12 interim audit)	Closing position (at the end of the 2011–12 interim audit)
A	0	0	0	0	0	0	0
B	0	0	1	1	(1)	0	0
Total	0	0	1	1	(1)	0	0

Prior year moderate audit issue

Handling of public monies by external parties

5.244 The ANAO reported one moderate issue during the 2010–11 final audit phase in relation to the Therapeutic Goods Administration (TGA). The issue related to appropriate agreements not being in place between TGA and two external companies that collect public monies on behalf of TGA, and weaknesses in controls relating to the collection process. In 2011–12, the ANAO identified that appropriate processes are in place and controls are operating effectively to address the reported weaknesses.

Conclusion

5.245 Based on audit coverage to date, the ANAO identified that key elements of internal control were operating effectively to provide reasonable assurance that DoHA can prepare financial statements that are free of material misstatement. The effective operation of these internal controls for the full financial year will be assessed during the 2011–12 final audit phase.

Human Services Portfolio

Department of Human Services

5.246 On 1 July 2011 the *Human Services Legislation Amendment Act 2011* integrated the services of Medicare Australia and Centrelink into the Department of Human Services (DHS). This represented a significant step in the Government's Service Delivery Reform (SDR) program announced in December 2009 by the then Minister for Human Services. SDR is a long-term Government initiative that commenced in 2010 and is expected to run until 2015.

5.247 DHS delivers a range of Government and other payments and services to individuals, families and communities. DHS also provides policy advice on service delivery matters to Government designed to ensure effective, innovative and efficient implementation of Government service delivery.

5.248 DHS offers a range of health, social and welfare payments and services through:

- the **Medicare program** which supports the health of Australians through the delivery of programs such as the Medicare Benefits Scheme, Pharmaceutical Benefits Scheme, the Australian Childhood Immunisation Register and the Australian Organ Donor Register;
- the **Centrelink program** which delivers a range of payments and services for retirees, the unemployed, families, carers, parents, people with disabilities, Indigenous Australians, and people from diverse cultural and linguistic backgrounds, and provides services at times of major change;
- the **Child Support program** which provides support to separated parents to have the financial and emotional support necessary for their children's wellbeing; and
- **CRS Australia** which provides disability employment services to help people with a disability, injury or health condition to get or keep a job; and help their employers to keep their workplaces safe.

5.249 The key characteristics of DHS's integrated business operations that shaped the ANAO's 2011–12 financial statements audit coverage include:

- voluntary disclosures of information by customers in relation to the assessment and payment of personal benefits;
- the quality assurance mechanisms implemented by the department to gain assurance over the accuracy of personal benefit payments;
- the complexity of the IT environment to support significant business operations, including developing and managing internal systems for personal benefit payments;
- management of agreements and arrangement with policy departments and agencies relating to service delivery responsibilities;
- the impact of the service delivery reforms that took effect on 1 July 2011; and
- child support arrangements, particularly in relation to child support assessments and payments that are subject to complex legislative requirements.

5.250 In the light of these characteristics and the ANAO's understanding of the operations of the department, the ANAO has assessed, for the purposes of planning the audit coverage for 2011–12, the risk of a material misstatement as moderate.

Financial overview

5.251 DHS's key financial balances are:

Key financial balances	Departmental Estimated (\$m) 2011–12	Departmental Actual (\$m) 2010–11	Administered Estimated (\$m) 2011–12	Administered Actual (\$m) 2010–11
Net cost of services	4 185	4 017		
Revenue from government	3 933	3 643		
Administered income			1 314	1 250
Administered expenses			1 303	1 229
Total assets	1 912	1 839	626	627
Total liabilities	1 261	1 229	621	620

Note: Figures provided for 2010–11 represent combined amounts for DHS, Medicare Australia and Centrelink prior to their integration and reflect actual amounts as per agencies' annual reports.

DHS estimated average staffing level for 2011–12 is 32 714 (2010–11: 34 973. Note: the average staffing level for 2010–11 comprises: DHS 5 733; Medicare Australia 5 330 and Centrelink 23 910 prior to integration on 1 July 2011).

Governance arrangements

5.252 DHS has established a new governance framework following the integration of Medicare Australia and Centrelink into the department on 1 July 2011. The framework is designed to support the achievement of DHS's financial reporting requirements, the effectiveness and efficiency of its operations and compliance with applicable legislative requirements. While the new governance arrangements are being consolidated into DHS, certain elements of the framework are at various stages of maturity and subject to further refinement.

5.253 The key elements of DHS governance framework in place at the time of the 2011–12 interim audit phase include:

- a strategic planning and performance framework focusing on priorities and the effective use of DHS resources;
- a governance committee structure comprising an Executive Committee chaired by the Secretary and seven supporting governance committees, including an audit committee, to provide oversight of the delivery and monitoring of DHS's outcomes;

- an organisation structure providing lines of accountability and responsibility to enhance DHS's compliance and decision making processes; and
- an internal audit function reporting directly to the Secretary and the audit committee in the conduct of risk based audits addressing the main aspects of DHS business operations.

In addition, DHS is continuing to refine its risk management processes and has made substantial progress in establishing a framework that is designed to manage risks at a strategic level.

Areas of audit focus

5.254 Following the integration of Medicare Australia and Centrelink into the department on 1 July 2011, the ANAO gained assurance over the processes for the migration of data from DHS, Medicare Australia and Centrelink financial management information systems (FMIS) into a consolidated portfolio wide system for recording financial transactions in 2011–12. The ANAO also conducted audit procedures to confirm the accuracy of the 1 July 2011 opening financial statement balances, and the accounting treatment for recognising assets in the accounting records of DHS from 1 July 2011.

5.255 In light of the ANAO's understanding of the new DHS environment and maturing governance arrangements, including its financial reporting regime and system of internal control, the ANAO's audit approach identified particular areas that have the potential to impact on DHS's financial statements and the financial information provided to other agencies. Areas highlighted for specific audit coverage in 2011–12 are:

- programs and related payments delivered by DHS on behalf of other agencies, including the Departments of Health and Ageing, Veterans' Affairs, Families, Housing, Community Services and Indigenous Affairs and Employment and Workplace Relations;
- child support transactions, specifically focusing on IT system controls and the valuation methodology used to determine child support liabilities not paid by the paying parent;
- legislative compliance, particularly the implementation of measures designed to address the risk of a breach of section 83 of the Constitution, referred to in the 2010–11 financial statements of DHS and Medicare Australia;

- the valuation and measurement of intangible assets; and
- employees benefit payments, noting the implementation of a new Enterprise Agreement during 2011–12 and the consequential revised actuarial calculation for determining employee provision balances.

5.256 The ANAO will also provide audit coverage over those areas that have been identified as significant to the financial statements, including the valuation of non-financial assets and liabilities, supplier expenses, revenue and receivables following the passage of the *Human Services Legislation Amendment Act 2011*.

5.257 As an integral part of the interim audit phase, the ANAO has reviewed the IT general and application controls for key systems that support the preparation of DHS's financial statements.

Audit results

5.258 The ANAO has substantially completed its interim audit phase coverage to assess the effectiveness of internal controls in those areas of audit focus that have the potential to impact on the 2011–12 financial statements, including audit coverage over personnel benefit payments on behalf of other agencies, including IT general and application controls. Further audit work on these areas of audit focus will be completed as part of the 2011–12 final audit phase.

5.259 The following table summarises the status of audit issues reported by the ANAO in 2010–11 and 2011–12.

Status of audit issues raised by the ANAO

Category	Findings outstanding (at the end of the 2010–11 interim audit)	Findings resolved (at the time of the 2010–11 final audit)	New findings (during the 2010–11 final audit)	Findings outstanding (at the end of the 2010–11 final audit)	Findings resolved (at the time of the 2011–12 interim audit)	New findings (during the 2011–12 interim audit)	Closing position (at the end of the 2011–12 interim audit)
A	0	0	0	0	0	0	0
B	1	(1)	0	0	0	2	2
Total	1	(1)	0	0	0	2	2

Note: The 2010–11 findings represent combined numbers for DHS, Medicare Australia and Centrelink prior to integration on 1 July 2011.

Moderate audit issues

Update to Personal Benefit fee details

5.260 DHS processes medical, hospital and allied health services claims on behalf of the Department of Veterans' Affairs (DVA) through the Treatment Accounts System (TAS). The amount that can be claimed (the fee) for each type of service provided is detailed in the Schedules of Benefits that are approved and managed by DVA. However, updates to the fee details in TAS are the responsibility of DHS and these details are updated manually to reflect the items listed in the Schedules of Benefits. The ANAO identified numerous discrepancies between the information contained in the Schedules of Benefits and the fee details recorded in TAS, resulting in a risk of incorrect benefit payments being processed and paid by DHS.

5.261 The ANAO considered controls over change management and quality assurance processes in relation to the updating of the fee details should be strengthened to ensure they are aligned with the Schedules of Benefits. DHS advised that it recognises the issue but considers that the total error resulting from this issue is of low material value and a number of steps have been taken to mitigate the potential risk. Further action has commenced to implement and improve controls over updating the fee details in TAS.

Electronic payment records

5.262 Payment records are created from the department's FMIS and forwarded to the Reserve Bank of Australia (RBA) in an electronic file format for payments to be made to DHS customers and suppliers. The 2011–12 interim audit phase identified that there were a number of users in DHS who had been given responsibilities to edit these files. The activities of these users with edit access rights were logged but had not been monitored. The ANAO also identified that there were a number of users who did not require these editing access rights. In addition, there were instances of insufficient documentation to support the authorisations of the edits made to the files.

5.263 The ANAO recommended that all user access to edit payment files forwarded to the RBA should be reviewed, user logs monitored and the details of edits to payment files appropriately documented at the time of authorisation. DHS has advised that the number of users with access rights to edit the payment files has been reduced, controls will be modified to ensure logs of changes to payment files are monitored and documentation strengthened to support all authorisations to edit payment files.

Conclusion

5.264 Based on audit coverage to date, the ANAO has identified that key elements of internal control, except for the issues outlined above, were operating satisfactorily to provide reasonable assurance over the financial information used in the preparation of the financial statements. The ANAO will assess the actions taken by DHS in relation to the matters referred to above as part of the 2011–12 final audit phase.

Immigration and Citizenship

Department of Immigration and Citizenship

5.265 The Department of Immigration and Citizenship (DIAC) is responsible for the delivery of a range of programs and services for the purpose of building Australia's future through the well-managed entry and settlement of people into Australia.

5.266 DIAC's responsibilities include:

- administering the Australian Government's immigration laws and migration programs;
- development of migration policy and managing migration;
- protecting refugees and contributing to humanitarian policy internationally;
- contributing to Australia's security through border management and traveller facilitation;
- delivering services to support migrants and refugees to settle into the Australian community and participate in Australian society; and
- promoting Australian citizenship and a multicultural Australia.

5.267 The key characteristics of DIAC's operations that shape the ANAO's 2011–12 financial statement audit include the:

- expansion of the immigration detention network, as a result of an increase in the number of people in immigration detention;
- completion in 2011 of DIAC's major business transformation program, titled *Systems for People*, which has resulted in significant changes in DIAC's information technology and business information systems;
- fluctuating business activity, which affects the amount of DIAC's appropriation revenue and, in turn, affects staffing and property requirements;
- decentralised processing of visa application charge revenue across DIAC's Australian and overseas offices, supported by multiple IT systems with the involvement of the Department of Foreign Affairs and Trade, and, to a lesser extent, the Australian Trade Commission;

- new contractual arrangements for two administered programs relating to English learning and humanitarian settlement of migrants in Australia; and
- increase in visa application volumes and visa revenue, as a result of a decision to increase the number of places in the migration program and proposed changes to visa application fees.

5.268 In the light of these characteristics and the ANAO's understanding of the operations of the department, the ANAO has assessed, for the purposes of planning the audit coverage for 2011–12, the risk of a material misstatement as moderate.

Financial overview

5.269 DIAC's key financial balances are:

Key financial balances	Departmental Estimated (\$m) 2011–12	Departmental Actual (\$m) 2010–11	Administered Estimated (\$m) 2011–12	Administered Actual (\$m) 2010–11
Net cost of services	1 359	1 252		
Revenue from government	1 279	1 188		
Administered income			1 217	977
Administered expenses			1 308	1 100
Total assets	811	745	1 027	788
Total liabilities	403	381	182	285

DIAC's estimated staffing level for 2011–12 is 8 682 (2010–11: 7 824).

Governance arrangements

5.270 The department has designed and implemented governance arrangements, a financial reporting regime and an internal control system to enable the achievement of DIAC's business objectives. These arrangements are designed to support DIAC's financial reporting requirements, the effectiveness and efficiency of its operations and compliance with applicable legislative requirements.

5.271 The key elements of DIAC's governance arrangements include:

- an executive management committee, which assists the Secretary in setting corporate priorities and determining the standards by which success in achieving its priorities are measured;

- a corporate leadership group which focuses on key strategic topics and the communication of key messages;
- governance committees with oversight of particular risk areas in DIAC, including fraud, integrity and security, people management, systems, performance management, and values and standards;
- an audit committee that focuses on matters relating to risk management, internal audit, external audit, fraud control and financial reporting;
- a financial statement sub-committee that meets regularly, focussing on financial statement issues, risks and deliverables; and
- an internal audit function that delivers a strategic risk-based internal audit plan designed to assist line areas meet their key objectives via a combination of performance and compliance based audits.

5.272 DIAC has a monthly financial reporting process that provides reports to the executive and divisions for review and analysis. The reports include a summary of the key financial issues to be considered by management, actual versus budgeted departmental revenue and expenditure by division, projected operating results, expenditure against capital budgets and a cash impact statement.

Areas of audit focus

5.273 In the light of the ANAO's understanding of DIAC's environment and governance arrangements, including its financial reporting regime and system of internal control, the ANAO's audit approach identifies particular areas of audit focus that have the potential to impact on DIAC's financial statements. Areas highlighted for specific audit coverage in 2011–12 are:

- accounting for expenditure incurred, and the increase in administered fixed assets purchased, as a result of the expansion of the immigration detention network;
- accounting for the impact of new contractual arrangements for the two administered programs relating to English learning and humanitarian settlement of migrants in Australia;
- appropriation revenue recognised under DIAC's funding agreement with the Department of Finance and Deregulation;

- the valuation of internally developed software, particularly in view of the finalisation of the *Systems for People* program towards the end of 2010–11;
- accounting for, and disclosure of, liabilities and potential liabilities arising from litigation in view of an increase in litigation in relation to the management of the immigration detention network; and
- legislative compliance, particularly the implementation of measures designed to address the risk of a breach of section 83 of the Constitution, referred to in the 2010–11 financial statements.

5.274 As an integral part of the interim audit phase, the ANAO has reviewed the IT general and application controls for key systems that support the preparation of DIAC's financial statements.

Audit results

5.275 A moderate issue arose during the 2011–12 interim audit phase relating to DIAC's enterprise resource planning system that supports both departmental and administered business and accounting processes. The ANAO reviewed the access controls and change management processes and identified that there was a risk that unauthorised business transactions and system changes could be made without being detected. DIAC advised that it is planning to introduce access controls and change management to support monitoring of access and segregation of duties which, will be implemented by 30 June 2012.

5.276 The following table provides a summary of the status of issues identified by the ANAO in 2010–11 and 2011–12.

Status of audit issues raised by the ANAO

Category	Findings outstanding(at the end of the 2010–11 interim audit)	Findings resolved(at the time of the 2010–11 final audit)	New findings (during the 2010–11 final audit)	Findings outstanding (at the end of the 2010–11 final audit)	Findings resolved (at the time of the 2011–12 interim audit)	New findings (during the 2011–12 interim audit)	Closing position (at the end of the 2011–12 interim audit)
A	0	0	0	0	0	0	0
B	0	0	0	0	0	1	1
Total	0	0	0	0	0	1	1

Conclusion

5.277 Based on interim audit phase coverage to date, the ANAO identified that key elements of internal control were operating effectively to support the preparation of financial statements that are free of material misstatement. Additional audit procedures have been undertaken to address the risks arising from the moderate audit issue referred to above. The effective operation of internal controls for the full financial year will be assessed during the 2011–12 final audit phase.

Infrastructure and Transport Portfolio

Department of Infrastructure and Transport

5.278 The Department of Infrastructure and Transport (Infrastructure) provides a range of programs that include investment in the coordination of transport and other infrastructure and services; regulation and monitoring of the transport system; and information to, and in partnership with, Government, industry and the broader community.

5.279 The key characteristics of Infrastructure's business operations that shaped the ANAO's planned 2011–12 financial statement audit coverage include:

- the level and complexity of the large number of grant and subsidy programs administered by the department; and
- the significant administered asset balances reported in the department's financial statements in respect of the Australian Government's investments in portfolio agencies.

5.280 In the light of these characteristics and the ANAO's understanding of the operations of the department, the ANAO has assessed, for the purposes of planning the audit coverage for 2011–12, the risk of a material misstatement as moderate.

Financial overview

5.281 Infrastructure's key financial balances are:

Key financial balances	Departmental Estimated (\$m) 2011–12	Departmental Actual (\$m) 2010–11	Administered Estimated (\$m) 2011–12	Administered Actual (\$m) 2010–11
Net cost of services	206	199		
Revenue from government	192	189		
Administered income			2 486	1 065
Administered expenses			3 409	1 962
Total assets	131	139	4 699	4 392
Total liabilities	73	70	21	26

Infrastructure's estimated average staffing level for 2011–12 is 987 (2010–11: 953).

Governance arrangements

5.282 The department has designed and implemented governance arrangements, a financial reporting regime and an internal control system to enable the achievement of the department's business objectives. These arrangements are designed to support the department's financial reporting requirements, the effectiveness and efficiency of its operations and compliance with applicable legislative requirements.

5.283 The key elements of Infrastructure's governance arrangements include:

- an executive management group that meets weekly, addresses strategic issues, monitors Infrastructure's financial performance, and oversees the operational performance of divisions;
- a governance committee framework, including an audit committee that meets regularly and focuses attention on internal control, management of risks, review of financial reports, control of public monies and regulatory compliance;
- an internal audit function that addresses key business and financial risks and aims to assist the department to meet its key objectives;
- a fraud control plan that is in line with the Commonwealth Fraud Control Guidelines;
- a Certificate of Compliance regime which forms a key part of Infrastructure's corporate governance and compliance framework;
- a framework for incorporating risk management into Infrastructure's broader management and business processes; and
- a financial reporting framework that involves monitoring the performance and financial management of key business areas, and the preparation and monitoring of monthly financial reports.

Areas of audit focus

5.284 In the light of the ANAO's understanding of Infrastructure's environment and governance arrangements, that includes its financial reporting regime and system of internal control, the ANAO's audit approach identifies particular areas of audit focus that have the potential to impact on Infrastructure's financial statements. Areas highlighted for specific audit coverage in 2011–12 are:

- the financial management and reporting of grant and subsidy programs administered by the department;
- the carrying value of administered investments, which represent a significant balance in Infrastructure's financial statements; and
- legislative compliance, particularly the implementation of measures designed to address the risk of a breach of section 83 of the Constitution, referred to in the 2011–12 financial statements.

5.285 As an integral part of the interim audit phase, the ANAO has reviewed the IT general and application controls for key systems that support the preparation of Infrastructure's financial statements.

Audit results

5.286 The ANAO's interim audit activity has focussed on the financial management and reporting of grant and subsidy programs, and IT general and application controls as they relate to the financial statements. One moderate audit issue has been identified in 2011–12, details of which are discussed below.

5.287 The following table summarises the status of audit issues reported by the ANAO in 2011–12 and 2010–11.

Status of audit issues raised by the ANAO

Category	Findings outstanding (at the end of the 2010–11 interim audit)	Findings resolved (at the time of the 2010–11 final audit)	New findings (during the 2010–11 final audit)	Findings outstanding (at the end of the 2010–11 final audit)	Findings resolved (at the time of the 2011–12 interim audit)	New findings (during the 2011–12 interim audit)	Closing position (at the end of the 2011–12 interim audit)
A	0	0	0	0	0	0	0
B	0	0	0	0	0	1	1
Total	0	0	0	0	0	1	1

Moderate audit issue

Financial statements preparation

5.288 The 2010–11 audit identified that the financial statement preparation process could be improved by strengthening of quality assurance and review procedures and further application of project management practices that facilitate more timely identification and communication of any delays in the preparation process.

5.289 The 2011–12 interim audit phase has identified a deterioration in the financial statement preparation process, particularly the application of project management practices that contribute to timely and accurate completion of financial statement information. This resulted in additional delays in the preparation of the 31 March 2012 interim financial statements that are likely to have flow-on implications for the material clearance⁶¹ and timing of the year-end financial statements. This audit issue has now been elevated to a moderate audit issue. This new moderate audit issue will be reassessed during the 2011–12 final audit phase.

Conclusion

5.290 Based on our audit coverage to date, the ANAO has identified that key elements of internal control, except for the issue outlined above, were operating effectively to provide reasonable assurance that Infrastructure can prepare financial statements that are free of material misstatement. The ANAO will review the effective operation of internal control for the full financial year during the 2011–12 final audit phase.

⁶¹ For 2011–12, material entities are required to submit audit cleared financial information to the Department of Finance and Deregulation by 15 August 2012.

Industry, Innovation, Science, Research and Tertiary Education Portfolio

Department of Industry, Innovation, Science, Research and Tertiary Education

5.291 The Department of Industry, Innovation, Science, Research and Tertiary Education (DIISRTE) aims to create an environment where new ideas are nurtured and innovation drives productivity, economic growth and social well being, by strengthening the links between science, research, industry and tertiary education. DIISRTE is responsible for developing policies and delivering programs, in partnership with stakeholders, designed to provide lasting economic benefits ensuring Australia's competitive future.

5.292 As a result of the Administrative Arrangements Order of 14 December 2011, the Tertiary, Skills and International functions of the Department of Education, Employment and Workplace Relations (DEEWR) were transferred to DIISRTE.

5.293 DIISRTE's main responsibilities are:

- contributing to the sustainable development and growth of Australian industry, particularly the manufacturing, services and small business sectors, by encouraging businesses to innovate, collaborate, and commercialise ideas, and by delivering business advice, assistance and services;
- contributing to the production, use and awareness of science and research knowledge, by supporting research activity; training and infrastructure; science communication; skill development, and collaboration, within the research sector and between researchers and industry, domestically and internationally; and
- achieving growth in skills, qualifications and productivity through funding to improve teaching quality, learning and tertiary sector infrastructure, international promotion of Australia's education and training sectors, and partnerships with industry.

5.294 The key characteristics of DIISRTE's business operations that shaped the ANAO's 2011–12 planned financial statement audit coverage include:

- the changing nature of the department's operations as a result of assuming the Tertiary, Skills and International functions from DEEWR. The impact on DIISRTE's operations is likely to be significant and includes:
 - the transfer of approximately 1,000 staff from DEEWR (including support staff such as IT and corporate staff);
 - short term challenges around accommodation for these staff, as the current premises will not accommodate the additional staff; and
 - the need to manage a number of large administered balances, including items requiring fair value adjustments.
- the number and complexity of administered programs. The number and extent of programs is also changing as a result of new Government initiatives and the winding down of existing programs. The number of programs increased significantly with the addition of the operations for Tertiary, Skills and International function which involves arrangements with third parties including the Australian Taxation Office and the Department of Human Services; and
- the complex ownership structures for administered investments, including the Innovation Investment Fund programs.

5.295 In the light of these characteristics and the ANAO's understanding of the operations of the department, the ANAO has assessed, for the purposes of planning the audit coverage for 2011–12, the risk of a material misstatement as moderate.

Financial overview

5.296 DIISRTE's key financial balances are:

Key financial balances	Departmental Estimated (\$m) 2011–12	Departmental Actual (\$m) 2010–11	Administered Estimated (\$m) 2011–12	Administered Actual (\$m) 2010–11
Net cost of services	366	330		
Revenue from government	331	306		
Administered income			1 422	540
Administered expenses			11 448	4 026
Total assets	334	321	24 072	3 123
Total liabilities	128	113	5 648	239

DIISRTE's estimated average staffing level for 2011–12 is 2 527 (2010–11: 2 276). As the 2011–12 staffing level is an average figure it does not fully reflect the staff transfers referred to in paragraph 5.294.

Governance arrangements

5.297 DIISRTE has designed and implemented governance arrangements and a financial reporting framework to provide reasonable assurance about the achievement of DIISRTE's business objectives. These arrangements are designed to support the achievement of DIISRTE's financial reporting requirements, the effectiveness and efficiency of its operations and compliance with applicable legislative requirements.

5.298 The key elements of DIISRTE's governance arrangements include:

- a strategic plan that provides an overview of DIISRTE's future directions;
- meetings of the Secretary and senior managers held regularly to discuss key aspects of DIISRTE activities, including program management and financial performance;
- a structured framework for incorporating risk management into the broader management and business processes, including the development and maintenance of a fraud control plan;
- an audit committee that meets bi-monthly and focuses on the enhancement of the control framework and risk management

arrangements to improve the objectivity and reliability of externally published financial and other information;

- a financial reporting framework that involves the monitoring of the performance and financial management of key business areas and the preparation and monitoring of monthly financial reports; and
- an internal audit function that addresses key business and financial risks and aims to assist line areas meet their key objectives.

5.299 In addition, DIISRTE put in place governance arrangements to address the Machinery of Government (MoG) changes referred to above. These arrangements include:

- the establishment of two committees, one departmental and one cross-agency; and
- assigning a Transition Management Team to the MoG process, including the allocation of senior staff to manage the process.

Areas of audit focus

5.300 In the light of the ANAO's understanding of DIISRTE's environment and governance arrangements, that includes its financial reporting regime and system of internal control, the ANAO's audit approach identifies particular areas of audit focus that have the potential to impact on DIISRTE's financial statements. Areas highlighted for specific audit coverage in 2011–12 are:

- the accounting for the transfer and integration of the Tertiary, Skills and International functions transferred from DEEWR;
- the actuarial valuation of key administered balances;
- the implementation controls for the Grant Management Information System and grant programs migrated during the year; and
- legislative compliance, particularly the implementation of measures designed to address the risk of a breach of section 83 of the Constitution, referred to in the 2010–11 financial statements.

5.301 As an integral part of the interim audit phase, the ANAO has reviewed the IT general and application controls for key systems that support the preparation of DIISRTE's financial statements.

Audit results

5.302 A moderate audit issue was identified in relation to the TYIMS system during the 2010–11 DEEWR audit. The TYIMS system manages payments under the Australian Apprentices Incentive Program. This program was transferred from DEEWR to DIISRTE as part of the Administrative Arrangements Order of 14 December 2011. The TYIMS system continues to be managed by DEEWR on behalf of the department.

5.303 As the system is managed by DEEWR, the issue is reported in the results of the DEEWR audit at paragraphs 5.181 to 5.184 above.

5.304 Based on audit coverage of the areas of audit focus to date in DIISRTE, no significant or moderate issues have been identified. Further audit coverage of the areas of audit focus will be undertaken as part of the 2011–12 final audit phase. The 2010–11 audit did not identify any significant or moderate audit issues.

Conclusion

5.305 Based on our audit coverage to date, the ANAO identified that key elements of internal control were operating effectively to provide reasonable assurance that DIISRTE can prepare financial statements that are free of material misstatement. The effective operation of these internal controls for the full financial year will be assessed during the 2011–12 final audit phase.

Prime Minister and Cabinet Portfolio

Department of the Prime Minister and Cabinet

5.306 The principal functions of the Department of the Prime Minister and Cabinet (PM&C) are to provide policy advice and support to the Prime Minister, the Cabinet Secretary and the Cabinet, and to achieve a coordinated and innovative approach to the development and implementation of Government policies.

5.307 PM&C is also responsible for:

- ensuring that policy proposals provided to the Prime Minister, other ministers in the portfolio, and to Cabinet are developed in a coherent, informed and coordinated fashion;
- the coordination and monitoring of the implementation and delivery of Government decisions, policies and priorities, where appropriate;
- supporting the Prime Minister and the Government in managing the business of Government in an efficient, effective and coordinated manner;
- providing administrative support to the Prime Minister, the Cabinet Secretary, the Cabinet and its committees; and
- coordinating and facilitating Government administration, intergovernmental relations and communications with State and Territory Governments.

5.308 The Administrative Arrangements Order (AAO) of 19 October 2011 resulted in a number of Machinery of Government (MOG) changes, including responsibility for the *Freedom of Information Act 1982* and the *Privacy Act 1988* being transferred to the Attorney-General's Department.

5.309 Further MOG changes that took effect on 14 December 2011 resulted in significant changes to the structure and operations of PM&C. These changes have resulted in responsibility for:

- the arts and culture function and the sport and recreation function being transferred to the Department of Regional Australia, Local Government, Arts and Sports;

- the national security science and innovation function being transferred to the Department of Defence; and
- cyber security policy coordination being transferred from the Attorney-General's Department to PM&C.

5.310 In addition, on January 2012 the establishment of the National Mental Health Commission, which previously operated within PM&C, was established as an executive agency under the *Public Service Act 1999*.

5.311 The key characteristics of PM&C's business operations that shaped the 2011–12 planned financial statement audit coverage include:

- the significant impact of multiple MOG changes on the structure and operations of the department;
- the relatively non-complex nature of PM&C's IT systems; and
- the overall effectiveness of PM&C's internal controls.

5.312 In the light of these characteristics and the ANAO's understanding of the operations of the department, the ANAO has assessed, for the purposes of planning the audit coverage for 2011–12, the risk of a material misstatement as moderate.

Financial overview

5.313 PM&C's key financial balances are:

Key financial balances	Departmental Estimated (\$m) 2011–12	Departmental Actual (\$m) 2010–11	Administered Estimated (\$m) 2011–12	Administered Actual (\$m) 2010–11
Net cost of services	181	157		
Revenue from government	171	156		
Administered income			0	3
Administered expenses			595	401
Total assets	79	250	3	7 332
Total liabilities	48	60	10	18

PM&C's estimated average staffing level for 2011–12 is 712 (2010–11: 780).

Governance arrangements

5.314 The department has designed and implemented governance arrangements, a financial reporting regime and an internal control system to enable the achievement of PM&C's business objectives. These arrangements are designed to support PM&C's financial reporting requirements, the effectiveness and efficiency of its operations and compliance with applicable legislative requirements.

5.315 The key elements of PM&C's arrangements include:

- an executive group comprising the Secretary and associate and deputy secretaries. The group considers strategic issues that impact on PM&C and also monitors the performance and budget in delivering PM&C's outcomes;
- a senior management group that meets regularly to discuss key business issues for PM&C, including business priorities and key commitments. The group comprises the executive group and division heads;
- an audit committee that is chaired by the Deputy Secretary Governance and meets quarterly. The audit committee is responsible for overseeing the department's approach to risk management, including PM&C's overall control framework;
- an internal audit function that plans and conducts audits based on risk assessments of departmental activities and direction from the audit committee;
- a risk management framework and plan that identifies and assists in the management of risk at the strategic, business and project level;
- a fraud policy statement and fraud control plan that is updated and reviewed in line with Commonwealth Fraud Control Guidelines; and
- a governance unit that oversees PM&C's governance arrangements.

Areas of audit focus

5.316 In the light of the ANAO's understanding of PM&C's environment and governance arrangements, which includes its financial reporting regime and system of internal control, the ANAO's audit approach identifies particular

areas of audit focus that have the potential to impact on PM&C's financial statements. Areas highlighted for specific audit coverage in 2011–12 are:

- the management, finalisation and financial reporting of the Commonwealth Heads of Government meeting, that was held in October 2011;
- the incorporation and transfer of functions resulting from the multiple MOG changes that took place during 2011–12; and
- accounting for the various sports and arts programs for which PM&C was responsible until December 2011.

5.317 As an integral part of the interim audit phase, the ANAO has reviewed the IT general and application controls for key systems that support the preparation of PM&C's financial statements.

Audit results

5.318 The ANAO has completed a review of internal controls relevant to the preparation of the department's financial statements and no significant or moderate findings have been identified.

5.319 No significant or moderate findings were identified in the 2010–11 audit.

Conclusion

5.320 Based on audit coverage to date, the ANAO identified that key elements of internal control were operating effectively to provide reasonable assurance that PM&C can prepare financial statements that are free of material misstatement. The effective operation of these internal controls for the full financial year will be assessed during the 2011–12 final audit phase.

Regional Australia, Local Government, Arts and Sport Portfolio

Department of Regional Australia, Local Government, Arts and Sport

5.321 The department was established on 14 September 2010 to administer regional development and local Government programs which were transferred from the former Department of Infrastructure, Transport, Regional Development and Local Government, and the administration of Australian Territories which was previously the responsibility of the Attorney-General's Department. Arts and sport responsibilities were added as a result of the Administrative Arrangements Order (AAO) of 14 December 2011, when the department also moved from the Prime Minister and Cabinet portfolio to become a separate portfolio department. Appropriations were amended under section 32 of the FMA Act, effective from 1 February 2012.

5.322 The principal responsibilities of the portfolio are:

- regional Australia policy and co-ordination;
- support for Ministers and Parliamentary Secretaries with regional responsibilities;
- regional development, and the delivery of regional and rural specific services;
- matters relating to local Government, including financial assistance grants to councils and shires;
- planning and land management of the Australian Capital Territory;
- administration of the Jervis Bay Territory, the Territory of Cocos (Keeling) Islands, the Territory of Christmas Island, the Coral Sea Islands Territory, the Territory of Ashmore and Cartier Islands, and the Commonwealth responsibilities on Norfolk Island;
- sport and recreation;
- cultural affairs, including movable cultural heritage and support for the arts;
- management of Government records;

- constitutional development of the Northern Territory and the Australian Capital Territory; and
- management of Old Parliament House.

5.323 The key characteristics of DRALGAS's business operations that shaped the ANAO's 2011–12 planned financial statement audit coverage include:

- accounting for the functions, staff and related financial reporting balances transferred to the department as a result of the machinery of Government changes arising from the AAO of 14 December 2011;
- the establishment and operation of shared service arrangements with the Departments of Infrastructure and Transport, and Prime Minister and Cabinet;
- the geographical spread of operations, including the large number of grant programs administered by the department, diverse revenue items associated with the department's administration of Territories and non-financial assets located in the administered Territories; and
- continuing refinement of the department's maturing control environment.

5.324 In the light of these characteristics and the ANAO's understanding of the operations of the department, the ANAO has assessed, for the purposes of planning the audit coverage for 2011–12, the risk of a material misstatement as moderate.

Financial overview

5.325 DRALGAS's key financial balances are:

Key financial balances	Departmental Estimated (\$m) 2011–12*	Departmental Actual (\$m) 2010–11**	Administered Estimated (\$m) 2011–12*	Administered Actual (\$m) 2010–11**
Net cost of services	93	38		
Revenue from government	84	38		
Administered income			31	24
Administered expenses			3 555	2 502
Total assets	166	21	8 168	789
Total liabilities	23	18	42	51

* The 2011–12 estimates include the transfer of resources for the arts and sport outcomes for the five month period February to June 2012.

** The 2010–11 financial year figures represent the first nine months of operation of the former department.

DRALGAS's estimated average staffing level for 2011–12 is 476 (2010–11: 311).

Governance arrangements

5.326 The department has designed and implemented governance arrangements, a financial reporting regime and an internal control system to enable the achievement of DRALGAS' business objectives. These arrangements are designed to support DRALGAS' financial reporting requirements, the effectiveness and efficiency of its operations and compliance with applicable legislative requirements.

5.327 Governance arrangements developed by DRALGAS include:

- an executive management group that meets weekly to address strategic issues, monitor financial performance, and oversee operational and performance issues;
- a governance committee framework, including a risk and audit committee that meets at least quarterly which focuses attention on internal control, management of risks, review of financial reports, control of public monies and regulatory compliance;
- a financial statements sub-committee that provides advice to the risk and audit committee regarding the preparation and certification of the financial statements;

- a fraud control plan and a financial statements risk plan;
- development of a risk management framework and plan that identifies, and assists management of risk at various levels of the department; and
- establishment of an internal audit function.

Areas of audit focus

5.328 In the light of the ANAO's understanding of DRALGAS's environment and governance arrangements, that includes its financial reporting regime and system of internal control, the ANAO's audit approach identifies particular areas of audit focus that have the potential to impact on the department's financial statements. Areas highlighted for specific audit coverage in 2011–12 are:

- the transfer of appropriations, the establishment of delegations, and accounting for balances transferred to DRALGAS as a result of the machinery of Government changes;
- the effectiveness of internal controls designed to ensure the accurate and complete processing of transactions undertaken by the Departments of Infrastructure and Transport and Prime Minister and Cabinet on behalf of DRALGAS, in accordance with shared services arrangements with those agencies;
- control activities and financial reporting arrangements in respect of large grant programs administered by the department, administered revenue, and non-financial assets held in dispersed locations; and
- legislative compliance, particularly the implementation of measures designed to address the risk of a breach of section 83 of the Constitution, referred to in the 2011–12 financial statements of the former Department of Regional Australia, Regional Development and Local Government.

5.329 As an integral part of the interim audit phase, the ANAO has reviewed the IT general and application controls for key systems that support the preparation of DRALGAS's financial statements.

Audit results

5.330 The ANAO has completed a review of internal control relevant to the department's IT systems and controls relating to major grant programs. Work

in relation to the responsibilities transferred from the Department of Prime Minister and Cabinet and the department's administered asset portfolio will be finalised as part of the 2011–12 final audit phase.

5.331 No significant or moderate audit issues have been identified during the 2011–12 interim audit phase. The 2010–11 audit did not identify any significant audit issues.

Conclusion

5.332 Based on our audit coverage to date, the ANAO identified that key elements of internal control were operating effectively to provide reasonable assurance that DRALGAS can prepare financial statements that are free of material misstatement. The effective operation of internal controls for the full financial year will be assessed during the 2011–12 final audit phase.

Resources, Energy and Tourism Portfolio

Department of Resources, Energy and Tourism

5.333 The Department of Resources, Energy and Tourism (RET) is responsible for enhancing Australia's economic prosperity by improving the productivity, competitiveness, security and sustainability of the resources, energy and tourism sectors. RET pursues these objectives by providing policy advice and program delivery services for the Australian Government.

5.334 RET's strategic directions are structured around four key areas: strategic policy development; enhancing productivity and international competitiveness; enhancing environmental and social sustainability; and enhancing national security.

5.335 RET's business operations include:

- providing advice to the Australian Government on the impact of policies in the resources, energy and tourism sectors;
- providing assistance to State and Territory Governments for resources and energy; and
- developing policies and the delivery of programs to provide resources, energy and tourism related initiatives.

5.336 The key characteristics of RET's business operations that shaped the ANAO's 2011–12 planned financial statement audit coverage include:

- the management of a large range of administered programs; and
- the department's responsibility for the collection of petroleum and uranium royalties. These royalty collections are generally managed by other Government jurisdictions on behalf of RET.

5.337 In the light of these characteristics and the ANAO's understanding of the operations of the department, the ANAO has assessed, for the purposes of planning the audit coverage for 2011–12, the risk of a material misstatement as moderate.

Financial overview

5.338 RET's key financial balances are:

Key financial balances	Departmental Estimated (\$m) 2011–12	Departmental Actual (\$m) 2010–11	Administered Estimated (\$m) 2011–12	Administered Actual (\$m) 2010–11
Net cost of services	111	86		
Revenue from government	109	86		
Administered income			1 701	1 664
Administered expenses			789	540
Total assets	48	43	819	830
Total liabilities	42	40	16	15

RET's estimated average staffing level for 2011–12 is 549 (2010–11: 471).

Governance arrangements

5.339 The department has designed and implemented governance arrangements, a financial reporting regime and an internal control system to provide reasonable assurance about the achievement of RET's business objectives. These arrangements are designed to support RET's financial reporting requirements, the effectiveness and efficiency of its operations and compliance with applicable legislative requirements.

5.340 The key elements of RET's governance arrangements include:

- an Executive Board that meets regularly to discuss key aspects of RET activities, including program management and financial performance;
- a structured framework for incorporating risk management into the broader management and business processes, including the development and maintenance of a fraud control plan;
- an audit committee that meets quarterly and focuses on the enhancement of the department's control framework and risk management arrangements to improve the objectivity and reliability of externally published financial and other information; and
- an internal audit function that examines key business and financial risks and aims to assist line areas to meet their key objectives.

Areas of audit focus

5.341 In the light of the ANAO's understanding of RET's environment and governance arrangements, that includes its financial reporting framework and system of internal controls, the ANAO's audit approach identifies particular areas of audit focus that have the potential to significantly impact on RET's financial statements. Areas highlighted for specific audit coverage in 2011–12 include:

- the valuation of the Commonwealth's investment in the Snowy Hydro Limited (SHL) that is recognised as an administered investment in RET's financial statements;
- accrued revenue relating to petroleum royalties, given the volatility of revenue streams and their material impact on the financial statements; and
- legislative compliance, particularly the implementation of measures designed to address the risk of a breach of section 83 of the Constitution.

5.342 As an integral part of the interim audit phase, the ANAO has reviewed the IT general and application controls for key systems that support the preparation of RET's financial statements.

Audit results

5.343 The ANAO has undertaken testing of the key elements of RET's internal control and audit coverage of the areas of audit focus outlined above. No significant or moderate issues have been identified in 2011–12. The ANAO will complete its review of internal controls and the valuation of the Commonwealth's investment in SHL during the 2011–12 final audit phase.

5.344 No significant or moderate findings were identified in the 2010–11 audit.

Conclusion

5.345 Based on audit coverage to date, the ANAO identified that key elements of internal control were operating effectively to provide reasonable assurance that RET can prepare financial statements that are free of material misstatement. The effective operation of these internal controls for the full year will be assessed during the 2011–12 final audit phase.

Sustainability, Environment, Water, Population and Communities Portfolio

Department of Sustainability, Environment, Water, Population and Communities

5.346 The Department of Sustainability, Environment, Water, Population and Communities (DSEWPaC) provides policy advice and administers programs to achieve the Government's objectives in the areas of the environment, water availability, heritage and culture, as well as the development of the sustainable population strategy. DSEWPaC is also responsible for supporting Australia's Antarctic activities.

5.347 Machinery of Government changes that took effect in December 2011 resulted in housing affordability policy matters being transferred from DSEWPaC to the Department of Families, Housing, Community Services and Indigenous Affairs (FaHCSIA) and housing supply policy matters being transferred from DSEWPaC to the Department of the Treasury.

5.348 DSEWPaC's main responsibilities are:

- conserving and protecting Australia's terrestrial and marine biodiversity and ecosystems, through supporting research, developing information, supporting natural resource management, regulating matters of national environmental significance and managing Commonwealth protected areas;
- improving the sustainability of Australia's population, communities and environment through the coordination and development of sustainable population and communities policies, and the reduction and regulation of waste, pollutants and hazardous substances;
- advancing Australia's strategic, scientific, environmental and economic interests in the Antarctic by protecting, administering and researching the Antarctic region;
- developing strategies in relation to climate change including wise water use, securing water supplies and improving health of rivers, waterways and freshwater ecosystems by supporting research, and reforming the management and use of water resources; and

- increasing protection, awareness and appreciation of Australia's environment and heritage through regulating matters of national environmental significance and the identification, conservation and celebration of natural, indigenous and historic places of national and World Heritage significance.

5.349 The key characteristics of DSEWPaC's business operations that shaped the ANAO's 2011–12 planned financial statement audit coverage include:

- significant administered asset balances reported in DSEWPaC's financial statements, particularly the Australian Government's investments in water assets;
- the significant and diverse grant programs administered by DSEWPaC; and
- the ongoing management of Australia's Antarctic bases, including management's estimate of the cost to restore the bases.

5.350 In the light of these characteristics and the ANAO's understanding of the operations of the department, the ANAO has assessed, for the purposes of planning the audit coverage for 2011–12, the risk of a material misstatement as moderate.

Financial overview

5.351 DSEWPaC's key financial balances are:

Key financial balances	Departmental Estimated (\$m) 2011–12	Departmental Actual (\$m) 2010–11	Administered Estimated (\$m) 2011–12	Administered Actual (\$m) 2010–11
Net cost of services	544	463		
Revenue from government	481	405		
Administered income			15	34
Administered expenses			888	1 280
Total assets	506	518	3 000	2 436
Total liabilities	445	426	48	55

DSEWPaC's estimated average staffing level for 2011–12 is 2 289 (2010–11: 2 406).

Governance arrangements

5.352 DSEWPaC has designed and implemented governance arrangements, a financial reporting regime and an internal control system designed to provide reasonable assurance about the achievement of DSEWPaC's business objectives.

5.353 The key elements of DSEWPaC's governance arrangements include:

- a strategic plan that provides an overview of DSEWPaC's strategic priorities and goals, including the department's planning and performance framework;
- a management board, which includes the Secretary and the Deputy Secretaries, that meets regularly to evaluate DSEWPaC's strategic direction, financial planning and operational results;
- an audit committee that includes four independent members including the chair. The audit committee meets regularly and focuses on risk management, the control environment, a review of financial reports and DSEWPaC's compliance with laws and regulations;
- a framework for incorporating risk management into the broader management and business processes including the development of a fraud control plan that is being refreshed based on learning from recent reviews of the department's operations; and
- an internal audit function that plans and conducts audits based on risk assessments of departmental activities.

Areas of audit focus

5.354 The department has designed and implemented governance arrangements, a financial reporting regime and an internal control system to provide reasonable assurance in relation to the achievement of DSEWPaC's business objectives. These arrangements are designed to support DSEWPaC's financial reporting requirements, the effectiveness and efficiency of its operations and compliance with applicable legislative requirements. Areas highlighted for specific audit coverage in 2011–12 are:

- the accounting and valuation of water assets;
- the model adopted by DSEWPAC to estimate their obligation to restore the Antarctic bases, particularly the appropriateness of assumptions used;

- the financial management and reporting of grants, including those related to the Caring for Our Country program, Water Smart Australia and the Sustainable Rural Water Use and Infrastructure program; and
- legislative compliance, particularly the implementation of measures designed to address the risk of a breach of section 83 of the Constitution, referred to in the 2010–11 financial statements.

5.355 As an integral part of the interim audit phase, the ANAO has reviewed the IT general and application controls for key systems that support the preparation of DSEWPaC's financial statements.

Audit results

5.356 The ANAO has commenced work on the areas relating to financial management and reporting of grants and the implementation of measures designed to address the risk of a breach of section 83 of the Constitution.

5.357 No significant or moderate issues have been identified during the 2011–12 interim audit. The 2010–11 audit also did not identify any significant or moderate audit issues.

5.358 The remaining areas of audit focus relate to work that will be undertaken as part of the 2011–12 final audit phase.

Conclusion

5.359 Based on audit coverage, the ANAO identified that key elements of internal control were operating effectively to provide reasonable assurance that DSEWPaC can prepare financial statements that are free of material misstatement. The effective operation of these internal controls for the full financial year will be assessed during the 2011–12 final audit phase.

Treasury Portfolio

Department of the Treasury

5.360 The Department of the Treasury (the Treasury) is the primary advisory body to the Australian Government on economic policy and development. The Treasury develops and implements policies to improve the wellbeing of the Australian people, by achieving strong, sustainable economic growth, through the provision of advice to the Australian Government and the efficient administration of federal financial relations.

5.361 The Treasury's business operations include:

- supporting a sound macroeconomic environment through monitoring and assessing economic conditions and prospects, both in Australia and overseas;
- providing advice on the formulation and implementation of effective macroeconomic policy, including monetary and fiscal policy, and labour market issues;
- providing advice on budget policy issues, trends in Commonwealth revenue and major fiscal and financial aggregates, major expenditure programs, taxation policy, retirement income, Commonwealth-State financial policy and actuarial services;
- addressing effective taxation and retirement income arrangements through the provision of advice, and assisting in the formulation and implementation of Government taxation and retirement income policies and legislation as well as providing information on material changes to taxation revenue forecasts and projections; and
- providing advice on policy processes and reforms that promote a secure financial system and sound corporate practices, removing impediments to competition in product and services markets and safeguarding the public interest in matters such as consumer protection and foreign investment.

5.362 The key characteristics of the Treasury's business operations that shaped the ANAO's 2011–12 planned financial statement audit coverage include:

- the Council of Australian Governments (COAG) federal financial relations framework reflected in the *Federal Financial Relations Act 2009*. Under this framework, individual agencies have policy responsibility for the performance of programs and advise the Treasury of details of specific purpose payments and amounts payable to the States and Territories under National Partnership Agreements;
- the Treasury's responsibility for monitoring the guarantees of deposits and wholesale funding and the temporary and voluntary guarantees over State and Territory Government borrowings that were first put in place following the global financial crisis. From 31 March 2010 no new wholesale funding arrangements have been entered into and, from 31 December 2010, the Australian Government guarantee of State and Territory borrowings closed to new issuance of guaranteed liability; and
- the Treasury's responsibility for managing investments in overseas financial institutions and the impact of the increased volatility affecting overseas markets, particularly in Europe.

5.363 In the light of these characteristics and the ANAO's understanding of the operations of the department, the ANAO has assessed, for the purposes of planning the audit coverage for 2011–12, the risk of a material misstatement as moderate.

Financial overview

5.364 The Treasury's key financial balances are:

Key financial balances	Departmental Estimated (\$m) 2011–12	Departmental Actual (\$m) 2010–11	Administered Estimated (\$m) 2011–12	Administered Actual (\$m) 2010–11
Net cost of services	176	167		
Revenue from government	156	158		
Administered income			4 925	3 645
Administered expenses			85 728	86 961
Total assets	116	129	12 911	14 326
Total liabilities	51	50	11 401	16 049

The Treasury's estimated average staffing level for 2011–12 is 1 006 (2010–11: 1 010).

Governance arrangements

5.365 The department has designed and implemented governance arrangements, a financial reporting regime and an internal control system to enable the achievement of Treasury's business objectives. These arrangements are designed to support Treasury's financial reporting requirements, the effectiveness and efficiency of its operations and compliance with applicable legislative requirements.

5.366 The key elements of the Treasury's corporate governance arrangements include:

- an executive board that meets at least monthly and is responsible for high level policy issues relating to the Treasury's strategic leadership and management;
- a committee framework including an audit committee that meets at least six times a year and focuses attention on corporate governance, internal audit, external audit, fraud and risks faced by the Treasury;
- a comprehensive and coordinated framework for incorporating risk management into broader management and business processes;
- an internal assurance function that has a planned risk based coverage of the Treasury's activities; and
- periodic fraud risk assessment undertaken in line with the Commonwealth Fraud Control Guidelines.

Areas of audit focus

5.367 In the light of the ANAO's understanding of the Treasury's environment and governance arrangements, that includes its financial reporting regime and system of internal control, the ANAO's audit approach identifies particular areas of audit focus that have the potential to impact on the Treasury's financial statements. Areas highlighted for specific audit coverage in 2011–12 are:

- the recognition and measurement of grant payments under the federal financial relations framework as reflected in the *Federal Financial Relations Act 2009*;
- the methodology used to estimate the provision for the Natural Disaster Relief and Recovery Arrangements (NDRRA);

- the disclosure of administered commitments in view of their nature and complexity;
- the Treasury's administration of the guarantees of deposits and wholesale funding and the temporary and voluntary guarantees over State and Territory Government borrowings;
- the administration of the *Commonwealth Places (Mirrors Taxes) Act 1998* and the treatment of notional payments to State and Territory Governments under the Act;
- the valuation of the Treasury's financial investment in international financial institutions, in light of increased volatility experienced in overseas markets;
- the administration of the Energy Security Council loans made under the Australian Government's Clean Energy Future initiative; and
- compliance with relevant aspects of the Commonwealth's financial framework and the implementation of measures designed to address the risk of a breach of section 83 of the Constitution referred to in the 2010–11 financial statements.

5.368 As an integral part of the interim audit phase, the ANAO has reviewed the IT general and application controls for key systems that support the preparation of the Treasury's financial statements.

Audit results

5.369 To date, our audit coverage of the key areas of audit focus have not identified any new significant or moderate audit issues.

5.370 The following table summarises the status of audit issues reported by the ANAO in 2011–12 and 2010–11.

Status of audit issues raised by the ANAO

Category	Findings outstanding (at the end of the 2010–11 interim audit)	Findings resolved (at the time of the 2010–11 final audit)	New findings (during the 2010–11 final audit)	Findings outstanding (at the end of the 2010–11 final audit)	Findings resolved (at the time of the 2011–12 interim audit)	New findings (during the 2011–12 interim audit)	Closing position (at the end of the 2011–12 interim audit)
A	0	0	0	0	0	0	0
B	1	(1)	3	3	0	0	3
L1	0	0	1*	0	0	0	0**
Total	1	(1)	4*	3	0	0	3**

* The breaches in 2010–11 relate to section 83 of the Constitution.

**The position in respect of potential breaches in 2011–12 relating to section 83 of the Constitution will be assessed as part of the final phase of the 2011–12 audit.

5.371 The 2010–11 financial statements made reference, at notes 25 and 26, to a number of breaches of section 83 of the Constitution. The Treasury sought legal advice on whether overpayments to States and Territories made in accordance with the Inter-governmental Agreement could be offset against future payments. The legal advice concluded the payments could be offset, but indicated the overpayments would be a breach of section 83 of the Constitution.

5.372 The breaches related to errors arising during the eligibility assessment process. Eligibility for grant payments is assessed by the relevant department with the Treasury being responsible for making payments to the States and Territories, based on advice received from the relevant department. The errors resulted in eight overpayments totalling \$26 million. All overpayments were subsequently offset against future payments or recovered from the State or Territory.

5.373 The auditor's report on the financial statements was unmodified as the financial statements fairly presented the financial operations and position of the Treasury at year end. However, the report did include a reference to the breaches of section 83 of the Constitution under Other Legal and Regulatory Requirements.

5.374 The Treasury is exploring options, including a possible amendment to the Inter-governmental Agreement, to eliminate the risk of a breach of section 83 of the Constitution resulting from the overpayment of grant monies. Nevertheless, on the basis that the same circumstances are applicable to

financial transactions in 2011–12, there is a high risk that similar breaches of section 83 have occurred in 2011–12.

Moderate audit issues

Monitoring of legislative compliance

5.375 The ANAO identified an issue during the 2010–11 interim audit phase relating to the Treasury’s monitoring of portfolio legislation under the Administrative Arrangements Order (AAOs). The ANAO also identified additional monitoring issues during the 2010–11 audit that have an impact on the appropriation note disclosure in the financial statements. The ANAO identified an additional 45 special appropriations that required disclosure in the Treasury’s Appropriation Note, and noted deficiencies in presentation and disclosure requirements.

5.376 The Treasury has commenced the process of repealing special appropriation clauses that are no longer required, and is taking steps to address other disclosure matters. The ANAO will review progress in addressing this issue, as well as compliance with special appropriation disclosure requirements, as part of the 2011–12 final audit phase.

Accounting for the National Disaster Relief and Recovery Arrangements

5.377 The 2010–11 final audit phase identified that the Treasury relied on the forward estimates provided by the States and Territories in assessing the provision for the NDRRA. The ANAO considered that greater assurance was required in relation to:

- methodologies and assumptions applied in the 2010–11 financial statements, by the States and Territories in collating estimates data;
- the level of confidence the States and Territories had in the reliability of the estimates; and
- whether the data had been reviewed or endorsed by an independent expert.

5.378 The ANAO’s review during the 2011–12 interim audit phase identified that the Treasury has undertaken an internal audit review of the level of confidence obtained from internal financial statement processes where reliance is placed on third party information. The review included an examination of the consolidated NDRRA estimate. In addition to the recommendations previously made by the ANAO, the internal audit review recommended the Treasury consult with an actuary for assistance in determining the reliability of

the data used to calculate the NDRRA estimate. The Treasury has held some initial discussions with an actuary, and has also commenced work to implement the ANAO's recommendations. The ANAO will review the Treasury's progress as part of the 2011–12 final audit phase.

Quality Assurance over financial reporting

5.379 The 2010–11 final audit phase identified that the quality assurance processes in place over the financial statements could be improved including through the reinforcement of existing review activities designed to identify potential exposures that may result in significant issues in the preparation of the financial statements.

5.380 The Treasury has commenced work to address this issue and the ANAO will review progress during the 2011–12 final audit phase.

Conclusion

5.381 Based on our audit coverage to date, the ANAO identified that key elements of internal control, except for the issues outlined above, were operating satisfactorily to provide reasonable assurance that the Treasury will be able to prepare financial statements free of material misstatement. The effective operation of these internal controls for the full financial year will be assessed during the 2011–12 final audit phase.

Australian Office of Financial Management

5.382 The Australian Office of Financial Management (AOFM) is responsible for the management of Australian Government debt and financial assets. The AOFM issues Treasury Bonds, Treasury Indexed Bonds and Treasury Notes, manages the Government's cash balance and invests in financial assets. Over the years, the Government has issued Treasury Bonds to maintain liquid and efficient Bond and Bond futures markets, reflecting the important role that these markets play in the Australian financial system.

5.383 The AOFM's business operations include:

- funding the Australian Government's Budget through the issuance of Australian Government debt;
- managing the Australian Government's daily cash balances through short term borrowings and investments;

- undertaking investments in financial assets in accordance with Government policy objectives;
- managing its portfolio of debt and financial assets cost effectively, subject to acceptable risk; and
- supporting the efficient operation of Australia's financial system.

5.384 The key characteristics of AOFM's business operations that shaped the ANAO's 2011–12 planned financial statement audit coverage include:

- the volume of investment activity of financial assets and issuance of financial liabilities, that are material to both the agency and the Consolidated Financial Statements;
- a continuation of the issuance of Treasury Indexed bonds to meet the Government's funding requirements; and
- material and complex financial assets and liabilities and their associated fair value assessment.

5.385 In the light of these characteristics and the ANAO's understanding of the operations of the AOFM, the ANAO has assessed, for the purposes of planning the audit coverage for 2011–12, the risk of a material misstatement as moderate.

Financial overview

5.386 The AOFM's key financial balances are:

Key financial balances	Departmental Estimated (\$m) 2011–12	Departmental Actual (\$m) 2010–11	Administered Estimated (\$m) 2011–12	Administered Actual (\$m) 2010–11
Net cost of services	11	11		
Revenue from government	12	16		
Administered income*			1 622	1 376
Administered expenses*			11 632	9 273
Total assets	25	20	32 313	27 651
Total liabilities	2	2	234 899	201 771

* Administered income is before gains and re-measurements. Administered expenses are before losses and re-measurements.

AOFM's estimated average staffing level for 2011–12 is 40 (2010–11: 37).

Governance arrangements

5.387 The agency has designed and implemented governance arrangements, a financial reporting regime and an internal control system to enable the achievement of AOFM's business objectives. These arrangements are designed to support AOFM's financial reporting requirements, the effectiveness and efficiency of its operations and compliance with applicable legislative requirements.

5.388 The key elements of AOFM's corporate governance arrangements include:

- an advisory board accountable to the Secretary of the Treasury that meets quarterly and provides general counsel and guidance on debt management policy, operational strategy and the performance of the AOFM;
- a governance committee framework, including an audit committee which focuses attention on internal and external audit; fraud control and the statutory financial statements. Other committees include:
 - an Executive Committee that coordinates the overall management of the agency, including the consideration of strategic issues; coordination of priorities, financial management, organisational arrangements and resource management;
 - an Asset and Liability Committee that advises the Chief Executive Officer on operational debt policy and financial management issues;
 - a Human Resources Committee that advises on the management of human resources, including employment policies, training and development, recruitment, performance management and remuneration;
 - an Information Technology Steering Committee that oversees current and planned information technology projects and operations; and
 - an Operational Risk Committee that manages operational risk of the agency. This committee determines the compliance priorities and control procedures and oversees the identification, categorisation and prioritisation of operational risks.

- an internal audit function that provides a risk based coverage of AOFM's activities;
- a framework for incorporating risk management into AOFM's broader management and business processes; and
- a financial reporting framework that involves the monitoring of the performance and financial management of key business areas and the preparation and monitoring of monthly financial reports.

Areas of audit focus

5.389 In the light of the ANAO's understanding of AOFM's environment and governance arrangements, that includes its financial reporting regime and system of internal control, the ANAO's audit approach identifies particular areas of audit focus that have the potential to impact on AOFM's financial statements. Areas highlighted for specific audit coverage in 2011–12 are:

- the complex fair value measurement of financial assets and liability securities;
- financial instrument presentation and disclosures, including the impact of AASB 7 *Fair-value Hierarchy* and changes to AASB 139 *Financial Instrument: Measurement and Recognition*; and
- legislative compliance, particularly the implementation of measures designed to address the risk of breaches of section 83 of the Constitution.

5.390 The ANAO will continue to provide audit coverage of the following areas which have previously been identified as having a significant impact on the financial statements:

- the control environment and the establishment of adequate controls to enable compliance with aspects of relevant financial management legislation;
- AOFM's management and control framework with the issuance of debt instruments, Treasury Bond and Notes; and
- the internal assurance activities, including the Certificate of Compliance process, and fraud prevention activities.

5.391 As an integral part of the interim audit phase, the ANAO has reviewed the IT general and application controls for key systems that support the preparation of AOFM's financial statements.

Audit results

5.392 No significant or moderate audit issues have been raised by the ANAO as a result of the audit coverage of the areas of audit focus to date. The 2010–11 audit did not identify any significant or moderate audit issues.

5.393 The areas of financial instruments and fair value measurements, including presentation and disclosures in the financial statements, will be reviewed as part of the 2011–12 final audit phase.

Conclusion

5.394 Based on our audit coverage to date, the ANAO identified that key elements of internal control were operating effectively to provide reasonable assurance that AOFM can prepare financial statements that are free of material misstatement. The effective operation of these internal controls for the full financial year will be assessed during the 2011–12 final audit phase.

Australian Taxation Office

5.395 The Australian Taxation Office (ATO) is the Australian Government's principal revenue management agency. In 2011–12, the ATO is expected to collect some \$307 billion in revenue, representing approximately 91 per cent of the Australian Government's revenue.

5.396 The ATO's responsibilities include:

- management of Australia's taxation, excise and superannuation systems that fund services for Australians, giving effect to social and economic policy;
- addressing broader issues affecting Australia's revenue system, such as aggressive tax planning, persistent tax debtors, globalisation and the cash economy;
- supporting delivery of community benefits with roles in other services, including private health insurance, family assistance and fuel grants schemes;

- providing cross agency support by working with: Centrelink to reduce benefit fraud; the Child Support Agency to ensure income transfer for the care of children; and the Australian Bureau of Statistics to reduce the cost to the community of collecting statistical data; and
- business operations of the Australian Valuation Office.

5.397 The key characteristics of ATO's business operations that shaped the ANAO's 2011–12 financial statement audit coverage include:

- a voluntary self assessment regime for the collection of taxation revenues;
- the basis of recognition for administered revenue and expenses;
- a complex financial statement process that involves using data from a number of business systems and the calculation of estimates for balances of a number of financial statement items;
- valuation of provision for taxation receivables doubtful debts including the impact of economic conditions;
- extensive IT-based business systems and associated processes; and
- legislative compliance in light of breaches of section 83 of the Constitution identified in previous years.

5.398 In the light of these characteristics and the ANAO's understanding of the operations of the ATO, the ANAO has assessed, for the purposes of planning the audit coverage for 2011–12, the risk of a material misstatement as moderate.

Financial overview

5.399 ATO's key financial balances are:

Key financial balances	Departmental Estimated (\$m) 2011–12	Departmental Actual (\$m) 2010–11	Administered Estimated (\$m) 2011–12	Administered Actual (\$m) 2010–11
Net cost of services	3 309	3 144		
Revenue from Government	3 131	3 016		
Administered income			307 344	280 888
Administered expenses			13 600	13 779
Total assets	1 156	1 061	28 856	26 939
Total liabilities	1 076	973	6 114	6 227

ATO's estimated average staffing level for 2011–12 is 21 991 (2010–11: 21 764).

Governance arrangements

5.400 The agency has designed and implemented governance arrangements, a financial reporting regime and an internal control system to enable the achievement of ATO's business objectives. These arrangements are designed to support ATO's financial reporting requirements, the effectiveness and efficiency of its operations and compliance with applicable legislative requirements.

5.401 The key elements of the ATO's governance arrangements include:

- a strategic statement and plan that provide an overview of the ATO's directions for the future, including corporate outcomes and performance measures. The ATO implements strategies through a comprehensive planning process based on the ATO's corporate priorities;
- a well defined structure of governance committees and forums that includes an executive committee, an audit committee and an annual plenary governance forum;
- an internal audit function, which provides an internal audit strategy and plan that addresses key business and financial risks and aims to assist line areas to meet their key objectives;
- mechanisms to facilitate internal and external assurances around financial integrity, including the effectiveness of internal controls that

impact on the financial statements and the Commissioner's annual Certificate of Compliance;

- a framework for incorporating risk management into the ATO's broader management and business processes; and
- a financial reporting framework that involves the monitoring of the performance and financial management of key business areas and the preparation and monitoring of monthly financial reports.

Areas of audit focus

5.402 In the light of the ANAO's understanding of the ATO's environment and governance arrangements, that includes its financial reporting regime and system of internal control, the ANAO's audit approach identifies particular areas of audit focus that have the potential to impact on the ATO's financial statements. Areas highlighted for specific audit coverage in 2011–12 are:

- the compliance programs in relation to the collection of taxation revenues, especially the ATO's risk management approach to compliance activities in a self-assessment and voluntary compliance regime;
- complex estimation and allocation processes associated with financial reporting of taxation revenue that entail the application of significant judgement and specialist knowledge;
- processes for determining the impairment of taxation receivables, with a focus on the impact of economic conditions;
- the ATO's reliance on IT business systems and associated processes, particularly in relation to system interfaces; and
- legislative compliance, including the implementation of measures designed to ensure compliance with section 83 of the Constitution.

5.403 The ANAO will continue to provide audit coverage over areas that support ATO's operations and are significant to the financial statements, specifically accounting process related to employees, suppliers, asset management and executive remuneration.

5.404 As an integral part of the interim audit phase, the ANAO has reviewed the IT general and application controls for key systems that support the preparation of ATO's financial statements.

Audit results

5.405 The ANAO's interim audit phase has focused on ATO's control environment, taxation administration for the collection and reporting of taxation revenue, internal assurance activities, and key IT systems used as the source of data for financial statement balances. Actions taken by the ATO to address prior year audit findings has also been reviewed.

5.406 The ANAO will complete audit coverage of areas identified as significant to the financial statements, including matters associated with legislative compliance and the valuation of provisions relating to non-collectable receivables, and estimation processes, during the 2011–12 final audit phase.

5.407 The following table summarises the status of audit issues reported by the ANAO in 2011–12 and 2010–11.

Status of audit issues raised by the ANAO

Category	Findings outstanding (at the end of the 2010–11 interim audit)	Findings resolved (at the time of the 2010–11 final audit)	New findings (during the 2010–11 final audit)	Findings outstanding (at the end of the 2010–11 final audit)	Findings resolved (at the time of the 2011–12 interim audit)	New findings (during the 2011–12 interim audit)	Closing position (at the end of the 2011–12 interim audit)
A	0	0	0	0	0	0	0
B	6	(3)	0	3	(3)	0	0
L1	0	0	1*	0	0	1*	1
Total	6	(3)	1*	3	(3)	1*	1

* Legislative breaches are treated on a year by year basis. The breaches in 2010–11 and 2011–12 relate to section 83 of the Constitution and are similar to the breaches that have been reported in previous years.

Legislative audit issue from prior years

Breaches of the Constitution

5.408 The 2010–11 financial statements made reference, in Note 24C, to a number of breaches of section 83 of the Constitution. The note to the financial statements indicates that, from time to time, as a result of processing errors outside the assessment process, incorrect payments are made by the ATO. In these circumstances a payment is made to a taxpayer without any legislative basis, representing a breach of section 83 of the Constitution which requires that no money shall be drawn from the Treasury of the Commonwealth except under an appropriation made by law.

5.409 A total of 59 542 incorrect payments totalling \$12.8 million were identified during 2010–11 comprising a very small percentage of some 14 million payments made during the year. At the time of signing the 2010–11 financial statements, over 48 per cent of the incorrect payments had been recovered.

5.410 The audit opinion on the financial statements was unqualified as the financial statements fairly presented the financial operations and position of the ATO at year end. However, the opinion did include a reference to the breach of section 83 of the Constitution under Other Legal and Regulatory Requirements.

5.411 In 2011–12, similar breaches have continued to occur. The *Financial Framework Legislation Amendment Bill (No.2) 2012* was introduced into the House of Representatives on 30 May 2012 to address, amongst other things, these section 83 breaches in the future.

Prior year moderate audit issues

5.412 During the 2011–12 interim audit phase, ANAO identified that ATO had resolved three moderate audit issues that had been previously identified. Two issues related to IT security and access and one issue related to a control weakness in processing income tax returns.

IT security and access

5.413 In 2009–10, the ANAO noted control weaknesses in respect of the granting of access to functions in the Integrated Core Processing (ICP) system used to process income tax returns. The ANAO identified a high number of discrepancies between the type of access granted and the level of access required. The ATO took immediate remedial action to reduce the number of users with this access. Documented policies and procedures for regular monitoring of user access, to prevent this reoccurring, were subsequently implemented in 2012.

5.414 In 2009–10, the ANAO conducted a review of privileged users of the IT network who have special access to ATO systems and data. The ANAO identified a high number of privileged users. The ANAO confirmed during the 2011–12 interim audit phase that in late 2011, the ATO had reduced the number of privileged users and implemented monitoring and reporting controls designed to ensure an appropriate level of authorised privileged users is maintained.

Income Tax processing—control weaknesses in ICP

5.415 The ICP system requires manual intervention where it identifies errors on income tax returns. In 2009–10, the ANAO identified that the ICP system did not maintain an audit trail of errors once corrected. In addition, the ANAO was unable to confirm appropriate quality assurance processes were in place to ensure that correction of errors had been processed accurately. During the 2011–12 interim audit phase the ANAO confirmed that the ATO implemented enhancements to the ICP system that included an audit trail for corrected tax return errors, and had implemented a quality assurance program.

Conclusion

5.416 Based on our audit coverage to date, the ANAO identified that key elements of internal control were operating effectively to provide reasonable assurance that the ATO can prepare financial statements that are free of material misstatement. The effective operation of internal controls for the full financial year will be assessed during the 2011–12 final audit phase.



Ian McPhee

Auditor-General

Canberra ACT

26 June 2012

Appendices

Appendix 1: Agencies covered by this report⁶²

Department of Agriculture, Fisheries and Forestry

Attorney-General's Department

Australian Customs and Border Protection Service

Department of Broadband, Communications and the Digital Economy

Department of Climate Change and Energy Efficiency

Department of Defence

Defence Materiel Organisation

Department of Veterans' Affairs

Department of Education, Employment and Workplace Relations

Department of Families, Housing, Community Services and Indigenous Affairs

Department of Finance and Deregulation

The Board of Guardians and the Future Fund Management Agency

Department of Foreign Affairs and Trade

Department of Health and Ageing

Department of Human Services

Department of Immigration and Citizenship

Department of Infrastructure and Transport

Department of Innovation, Industry, Science, Research and Tertiary Education

Department of the Prime Minister and Cabinet

Department of Regional Australia, Local Government, Arts and Sport

Department of Resources, Energy and Tourism

Department of Sustainability, Environment, Water, Population and Communities

Department of the Treasury

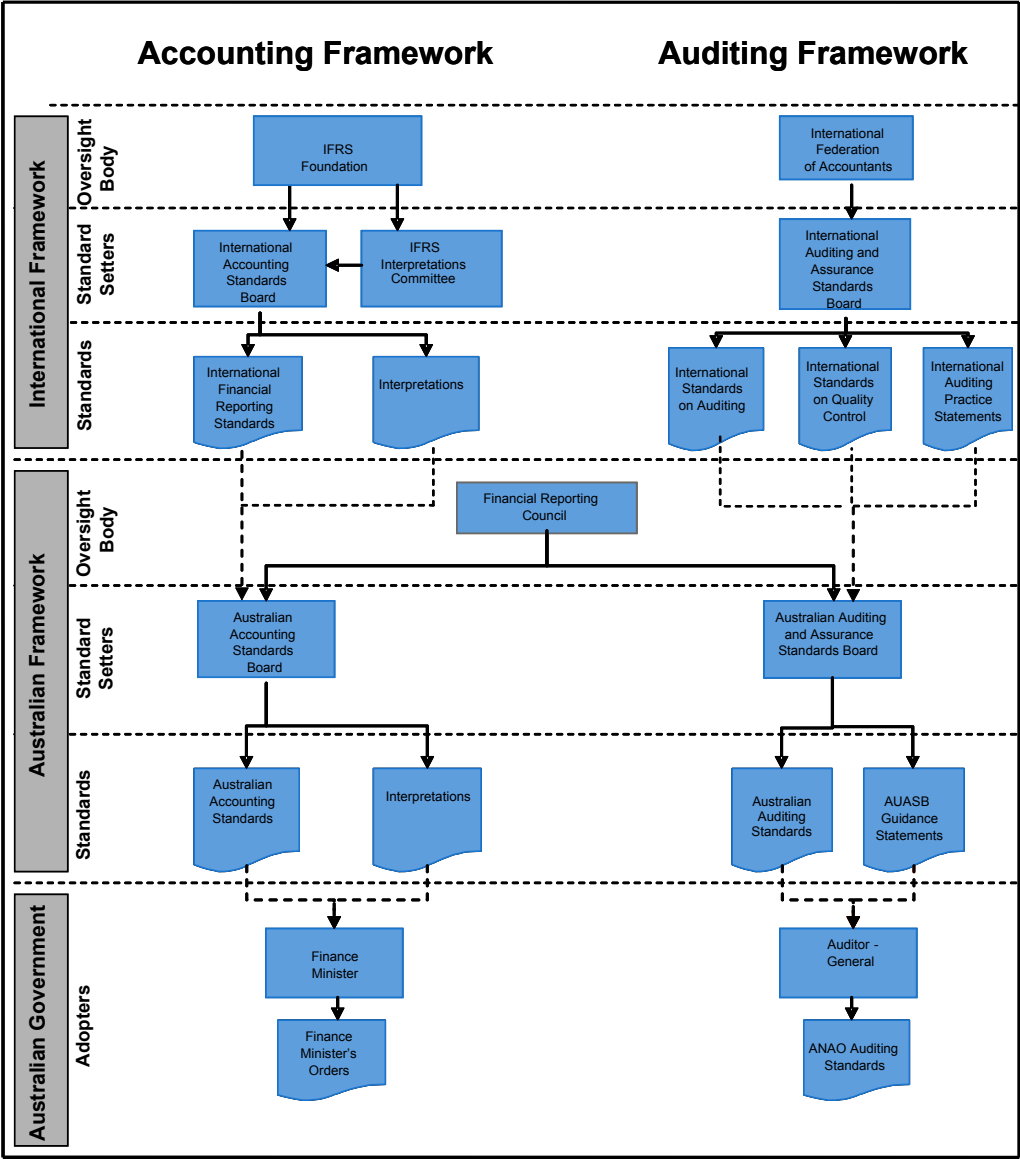
Australian Office of Financial Management

Australian Taxation Office

⁶² Agencies are grouped by portfolio.

Appendix 2: The Accounting and Auditing Standards Frameworks

The figure below depicts the standard setting framework, for accounting and auditing, in the Australian Government context.

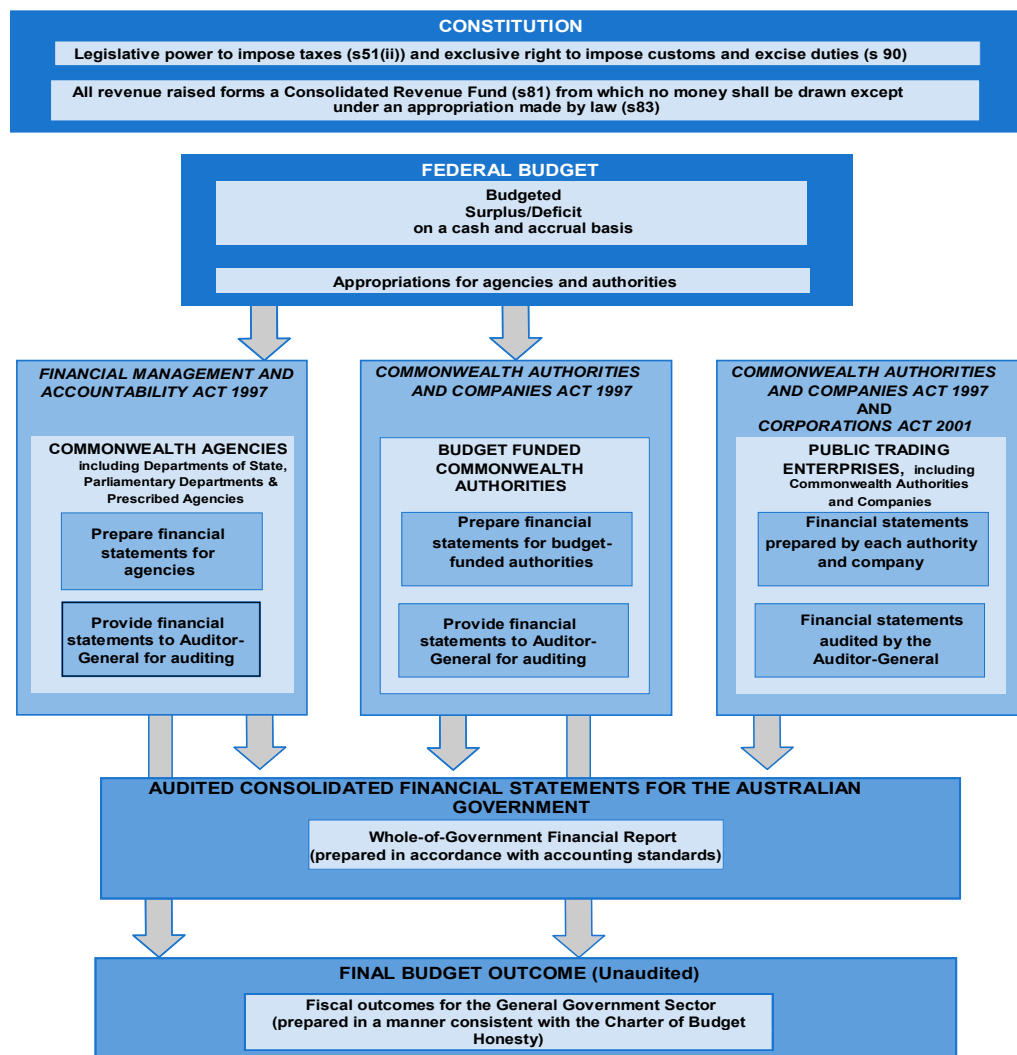


Source: ANAO

Appendix 3: The Financial Reporting Framework

Key elements of the Australian Government's financial reporting framework are outlined in the diagram below. An overview of the financial reporting requirements for the various types of Australian Government entities covered by the framework and the audit approach for the financial statements of these entities is also described below.

Key Elements of the Financial Reporting Framework



Source: ANAO

Australian Government Reporting Entities

Commonwealth Government of Australia

Section 55 of the FMA Act requires the Finance Minister to prepare annual financial statements for the Commonwealth Government of Australia. These financial statements are a general purpose financial report consolidating the financial activities and financial position of all agencies, authorities and other entities controlled by the Commonwealth Government.

Australian Government agencies

Australian Government agencies, comprising departments of state, parliamentary departments and prescribed agencies, are subject to the provisions of the FMA Act.

The FMA Act prescribes the FMOs as the applicable financial reporting framework for agencies. The FMOs include a requirement that the financial statements comply with the ASA) issued by the AASB.

Commonwealth authorities and subsidiaries

Commonwealth authorities are bodies corporate that hold money on their own account and have been created by the Parliament to perform specific functions. Commonwealth authorities operate under their own enabling legislation and also must comply with relevant provisions of the CAC Act.

The CAC Act prescribes the FMOs as the applicable financial reporting framework for Commonwealth authorities. The financial reporting framework applicable to subsidiaries of Commonwealth authorities depends on the nature of the subsidiary.

Commonwealth companies and subsidiaries

Commonwealth companies are companies that are controlled by the Australian Government through majority share holdings or voting rights, or via control over the composition of the company's board. Commonwealth companies operate and prepare financial statements under the Corporations Act.

The applicable financial reporting framework for Commonwealth companies is the Corporations Act, including the ASAs and the Corporations Regulations.

The financial reporting framework applicable to subsidiaries of Commonwealth companies depends on the nature of the subsidiary.

Other bodies

The ANAO also audits the financial statements of other bodies under “by arrangement” provisions in section 20 of the *Auditor-General’s Act 1997*. These bodies consist primarily of trusts or joint ventures entered into by Commonwealth bodies.

Audit of Australian Government entity financial statements

Audit scope

The Chief Executives of agencies, and the directors of authorities and companies, are responsible for the preparation and presentation of the financial statements and for maintaining records, internal controls, procedures and processes that support the preparation of those statements. The ANAO’s independent audits of financial statements are undertaken to form an opinion whether the financial statements are free from material misstatement.

The audits are conducted in accordance with the ANAO Auditing Standards, which incorporate the Australian Auditing Standards (ASAs), to provide reasonable assurance as to whether the financial statements are free of material misstatement.

Audit procedures include examination of the entity’s records and its internal control, information systems, control procedures and statutory disclosure requirements. Evidence supporting the amounts and other information in the statements is examined on a test basis, and accounting policies and significant accounting estimates are evaluated.

The entity’s internal control relevant to the entity’s preparation and fair presentation of the financial statements is considered in order to design audit procedures that are appropriate in the circumstances. In some audits, audit procedures concentrate primarily on substantiating the amounts appearing in the financial statements and do not include detailed testing of systems and internal controls.

The primary responsibility for the prevention and detection of fraud and error rests with both those charged with the governance and the management of an entity. An audit conducted in accordance with ASAs is designed to provide

reasonable assurance that the financial statements, taken as a whole, is free from material misstatement, whether due to fraud or error. The fact that an audit is carried out may act as a deterrent to fraud. However, the auditor is not responsible for the prevention of fraud and error.

The auditor's report on financial statements

The ANAO auditor's report on the financial statements includes a statement of the auditor's opinion as to whether the financial statements give a true and fair view of the entity's financial position, the results of its financial operations and its cash flows in accordance with the applicable financial reporting framework.

If the auditor is not satisfied that the financial statements are true and fair, the auditor's opinion is modified, with the reasons being indicated.

The auditor's report on the financial statements will include the auditor's opinion and may include an 'emphasis of matter' or 'other matters' paragraphs. A report on other legal and regulatory requirements may accompany the auditor's report on the financial statements.

Form of auditor's opinion

An auditor's opinion is described as 'unmodified' when the auditor concludes that the financial statements are prepared, in all material respects, in accordance with the applicable financial reporting framework.

An auditor's opinion may be "modified" in one of three ways.

- A 'modified opinion' is expressed when the auditor, having obtained sufficient appropriate audit evidence, concludes that misstatements, individually or in aggregate, are material but not pervasive to the financial statements. A 'modified opinion' is also expressed when the auditor, having been unable to obtain sufficient appropriate audit evidence, concludes that the possible effects on the financial statements of undetected misstatements could be material but not pervasive.
- A 'disclaimer of opinion' is expressed when the auditor, having been unable to obtain sufficient appropriate audit evidence on which to base the opinion, concludes that the possible effects on the financial statements of undetected misstatements could be both material and pervasive.
- An 'adverse opinion' is expressed when the auditor, having obtained sufficient appropriate audit evidence, concludes that misstatements

individually or in aggregate, are both material and pervasive to the financial statements.

Emphasis of matter

An 'emphasis of matter' paragraph is included in the auditor's report when the auditor considers it necessary to draw to users' attention a matter presented in the financial statements that, in the auditor's judgement, is of such importance that it is fundamental to the users' understanding of the financial statements. The auditor's opinion is not modified in respect of the matter emphasised. The circumstances in which an emphasis of matter is used include:

- when material uncertainty exists relating to an event or condition that may cast significant doubt on an entity's ability to continue as a going concern;
- when financial statements and the auditor's report have been issued and a fact is discovered that leads to revised financial statements and a new auditor's report being prepared; and
- when financial statements have been prepared in accordance with a special purpose framework, and as a result the financial statements may not be suitable for another purpose⁶³.

Other matters

The auditor's report on the financial statements may also include a reference to 'other matters'. This allows the auditor to communicate a matter other than a matter that is presented or disclosed in the financial statements that, in the auditor's judgement, is relevant to users' understanding of the audit, the auditor's responsibilities or the auditor's report.

Report on other legal and regulatory requirements

The auditor's report on the financial statements may also include a report on other legal and regulatory requirements. This report covers matters that the Auditor-General is required by law to report on in conjunction with the financial statements audit that do not affect the truth and fairness of the financial statements.

⁶³ Under the Clarity ASAs, the Auditor-General is required to include an emphasis of matter where a special purpose framework is adopted. Auditor's reports which include this mandatory requirement have not been included in this Report.

For example, section 57 of the FMA Act requires that, where the Auditor-General is of the opinion that a Chief Executive has contravened section 48⁶⁴ of the FMA Act, the Auditor-General must state in the auditor's report, the particulars of the contravention.

A report on other legal and regulatory requirements may also be used to draw attention to other legislative issues such as issues relating to agencies' compliance with section 83 of the Constitution.

⁶⁴ Section 48 of the FMA Act requires the Chief Executive to keep proper accounts and records.

Series Titles

ANAO Audit Report No.1 2011–12

The Australian Defence Force's Mechanisms for Learning from Operational Activities
Department of Defence

ANAO Audit Report No.2 2011–12

Confidentiality in Government Contracts: Senate Order for Departmental and Agency Contracts (Calendar Year 2010 Compliance)

ANAO Audit Report No.3 2011–12

Therapeutic Goods Regulation: Complementary Medicines
Department of Health and Ageing

ANAO Audit Report No.4 2011–12

Indigenous Employment in Government Service Delivery

ANAO Audit Report No.5 2011–12

Development and Implementation of Key Performance Indicators to Support the Outcomes and Programs Framework

ANAO Audit Report No.6 2011–12

Fair Work Education and Information Program
Department of Education, Employment and Workplace Relations

ANAO Audit Report No.7 2011–12

Establishment, Implementation and Administration of the Infrastructure Employment Projects Stream of the Jobs Fund
Department of Infrastructure and Transport

ANAO Audit Report No.8 2011–12

The National Blood Authority's Management of the National Blood Supply
National Blood Authority

ANAO Audit Report No.9 2011–12

Indigenous Secondary Student Accommodation Initiatives

Department of Families, Housing, Community Services and Indigenous Affairs

Department of Education, Employment and Workplace Relations

ANAO Audit Report No.10 2011–12

Administration of the National Partnership on Early Childhood Education

Department of Education, Employment and Workplace Relations

ANAO Audit Report No.11 2011–12

Implementation and Management of the Housing Affordability Fund

Department of Families, Housing, Community Services and Indigenous Affairs

Department of Sustainability, Environment, Water, Population and Communities

ANAO Audit Report No.12 2011–12

Implementation of the National Partnership Agreement on Remote Indigenous Housing in the Northern Territory

Department of Families, Housing, Community Services and Indigenous Affairs

ANAO Audit Report No.13 2011–12

Tasmanian Freight Equalisation Scheme

Department of Infrastructure and Transport

Department of Human Services

ANAO Audit Report No.14 2011–12

Indigenous Protected Areas

Department of Sustainability, Environment, Water, Population and Communities

ANAO Audit Report No.15 2011–12

Risk Management in the Processing of Sea and Air Cargo Imports

Australian Customs and Border Protection Service

ANAO Audit Report No.16 2011–12

The Management of Compliance in the Small to Medium Enterprises Market

Australian Taxation Office

ANAO Audit Report No.17 2011–12

Audits of the Financial Statements of Australian Government Entities for the Period Ended 30 June 2011

ANAO Audit Report No.18 2011–12

Information and Communications Technology Security: Management of Portable Storage Devices

ANAO Audit Report No.19 2011–12

Oversight and Management of Defence's Information and Communication Technology
Department of Defence

ANAO Audit Report No.20 2011–12

2010–11 Major Projects Report
Defence Materiel Organisation

ANAO Audit Report No.21 2011–12

Administration of Grant Reporting Obligations
Department of Finance and Deregulation

ANAO Audit Report No.22 2011–12

Administration of the Gateway Review Process
Department of Finance and Deregulation

ANAO Audit Report No.23 2011–12

Administration of the National Greenhouse and Energy Reporting Scheme
Department of Climate Change and Energy Efficiency

ANAO Audit Report No.24 2011–12

Administration of Government Advertising Arrangements:
March 2010 to August 2011

ANAO Audit Report No.25 2011–12

Administration of Project Wickenby
Australian Taxation Office
Australian Crime Commission
Australian Federal Police

ANAO Audit Report No.26 2011–12

Capacity Development for Indigenous Service Delivery

Department of Families, Housing, Community Services and Indigenous Affairs

Department of Education, Employment, and Workplace Relations

Department of Health and Ageing

ANAO Audit Report No.27 2011–12

Establishment, Implementation and Administration of the Bike Paths Component of the Local Jobs Stream of the Jobs Fund

Department of Regional Australia, Local Government, Arts and Sport

Department of Infrastructure and Transport

ANAO Audit Report No.28 2011–12

Quality On Line Control for Centrelink Payments

Department of Human Services

ANAO Audit Report No.29 2011–12

Administration of the Australia Network Tender Process

Department of Foreign Affairs and Trade

Department of Broadband, Communications and the Digital Economy

Department of the Prime Minister and Cabinet

ANAO Audit Report No.30 2011–12

Fighting Terrorism at its Source

Australian Federal Police

ANAO Audit Report No.31 2011–12

Establishment and Use of Procurement Panels

Australian Securities and Investments Commission

Department of Broadband, Communications and the Digital Economy

Department of Foreign Affairs and Trade

ANAO Audit Report No.32 2011–12

Management of Complaints and Other Feedback by the Department of Veterans' Affairs

Department of Veterans' Affairs

ANAO Audit Report No.33 2011–12

Management of ePassports

Department of Foreign Affairs and Trade

ANAO Audit Report No.34 2011–12

Upgrade of the M113 Fleet of Armoured Vehicles

Department of Defence

Defence Materiel Organisation

ANAO Audit Report No.35 2011–12

Indigenous Early Childhood Development. New Directions: Mothers and Babies Services

Department of Health and Ageing

ANAO Audit Report No.36 2011–12

Development and Approval of Grant Program Guidelines

Department of Finance and Deregulation

ANAO Audit Report No.37 2011–12

The Child Support Program's Management of Feedback

Department of Human Services

ANAO Audit Report No.38 2011–12

Administration of the Private Irrigation Infrastructure Operators Program in New South Wales

Department of Sustainability, Environment, Water, Population and Communities

ANAO Audit Report No.39 2011–12

Management of the National Solar Schools Program

Department of Climate Change and Energy Efficiency

ANAO Audit Report No.40 2011–12

Interpretative Assistance for Self Managed Superannuation Funds

Australian Taxation Office

ANAO Audit Report No.41 2011–12

National Partnership Agreement on Literacy and Numeracy

Department of Education, Employment and Workplace Relations

ANAO Audit Report No.42 2011–12

Management of the Multicultural Servicing Strategy for the Delivery of Centerlink Services

Department of Human Services

ANAO Audit Report No.43 2011–12

National Partnership Agreement on Remote Service Delivery

Department of Families, Housing, Community Service and Indigenous Affairs

ANAO Audit Report No.44 2011–12

Administration of the Primary Care Infrastructure Grants Program

Department of Health and Ageing

ANAO Audit Report No.45 2011–12

Administration of the Health and Hospitals Fund

Department of Health and Ageing

ANAO Audit Report No.46 2011–12

Administration of Northern Australia Quarantine Strategy

Department of Agriculture, Fisheries and Forestry

ANAO Audit Report No.47 2011–12

Small Business Superannuation Clearing House

Department of the Treasury

Department of Human Services

Australian Taxation Office

ANAO Audit Report No.48 2011–12

Administration of Mental Health Initiatives to Support Younger Veterans

Department of Veterans' Affairs

ANAO Audit Report No.49 2011–12

Security Assessments of Individuals

Australian Security Intelligence Organisation

ANAO Audit Report No.51 2011–12

Interim Phase of the Audits of the Financial Statements of Major General
Government Sector Agencies for the year ending 30 June 2012

ANAO Audit Report No.50 2011–12

Processing and Risk Assessing Incoming International Air Passengers

Australian Customs and Border Protection Service

Current Better Practice Guides

The following Better Practice Guides are available on the ANAO website.

Public Sector Environmental Management	Apr 2012
Developing and Managing Contracts	
Getting the right outcome, achieving value for money	Feb 2012
Public Sector Audit Committees	Aug 2011
Human Resource Information Systems	
Risks and Controls	Mar 2011
Fraud Control in Australian Government Entities	Mar 2011
Strategic and Operational Management of Assets by Public Sector Entities –	
Delivering agreed outcomes through an efficient and optimal asset base	Sep 2010
Implementing Better Practice Grants Administration	Jun 2010
Planning and Approving Projects	
an Executive Perspective	Jun 2010
Innovation in the Public Sector	
Enabling Better Performance, Driving New Directions	Dec 2009
SAP ECC 6.0	
Security and Control	Jun 2009
Preparation of Financial Statements by Public Sector Entities	Jun 2009
Business Continuity Management	
Building resilience in public sector entities	Jun 2009
Developing and Managing Internal Budgets	Jun 2008
Agency Management of Parliamentary Workflow	May 2008
Public Sector Internal Audit	
An Investment in Assurance and Business Improvement	Sep 2007
Fairness and Transparency in Purchasing Decisions	
Probity in Australian Government Procurement	Aug 2007
Administering Regulation	Mar 2007
Implementation of Programme and Policy Initiatives:	
Making implementation matter	Oct 2006
Legal Services Arrangements in Australian Government Agencies	Aug 2006