AUDITOR-GENERAL
FOR THE NORTHERN TERRITORY

FEBRUARY 2001 REPORT

TO THE LEGISLATIVE ASSEMBLY

Auditing for Parliament...
providing independent analysis
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providing independent analysis

The Auditor-General’s powers and responsibilities are established by the Northern Territory's Parliament, the Legislative Assembly, in the Audit Act. The Auditor-General is required to report to the Legislative Assembly at least once per year on any matters arising from the exercise of the auditing powers established in that Act.

In doing so, the Auditor-General is providing information to the Parliament to assist its review of the performance of the Executive Government, particularly the Government’s responsibility for the actions of the public sector entities which administer its financial management and performance management directives. The Parliament has a responsibility to conduct this review as the representative of the people of the Northern Territory.

The Auditor-General is also able to report to management of public sector entities on matters arising from the conduct of audits.

Reports provided to Parliament and public sector managers should be recognised as a useful source of independent analysis of Government information, and of the systems and controls underpinning the delivery of that information.

The Auditor-General is assisted by personnel of the Northern Territory Auditor-General’s Office who plan projects for conduct by private sector authorised auditors.

The cover of the Report depicts an artist’s impression of sittings of the Northern Territory Legislative Assembly. In that forum, information provided by the Auditor-General can be used to support questions and debates.
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Sir,

I request that you table today in the Legislative Assembly my report on matters arising from audits undertaken in the six months to 31 December 2000. I separately reported on 28 November 2000 my analysis of the Treasurer’s 1999/2000 Annual Financial Statement, to allow Members more timely access to that information.

This Report is focused on providing independent analysis of the financial and performance information which is produced by the Government, primarily in Agency Annual Reports, when accounting for its performance to the Legislative Assembly.

Other matters reported include my findings from two audits on topics which have had high levels of Parliamentary and public interest – the Power & Water Authority’s acquisition in November 2000 of the Darwin to Katherine Transmission Line; and expenditure on public information advertising and community attitudes research.

This Report is intended to provide an independent source of information which Members can use when conducting their important role of analysing, questioning and debating the Government’s performance in managing public funds, and in achieving its public policy goals.

Yours sincerely

Iain Summers
Auditor-General for the Northern Territory
Major Findings

Acquisition of the Darwin to Katherine Transmission Line

- The Darwin to Katherine Transmission Line (the Line) was acquired by the Power & Water Authority in November 2000 through the settlement by the Government of a legal dispute.
- The $43 million settlement amount was paid by the Government based on its desire to remove the risks entailed in an expensive legal action which had uncertain outcomes, and on its assessment that acquiring the Line as part of the settlement terms delivered strategic benefits.
- The $43 million settlement was a negotiated position which the Government recognised was greater than their estimates of the value of the Line, but less than their obligations under the original construction and financing arrangements for the Line.
- The difference between the commercial value of the Line and the $43 million settlement is the premium which the Government has paid to obtain the risk minimisation and strategic benefits it sought. The value of the Line may be determined once the Utilities Commissioner rules on revenue to be earned from ownership of the Line from 1 July 2001.
- While the final decision required the exercise of judgement by the Government, the processes which delivered the advice to the Government, and which eventually lead to the approval of the settlement offer, were appropriate to the circumstances.

Refer page 10 to 21 for further comments

Management of the Information Technology outsourcing policy

- Processes have been established to allow information technology and telecommunications outsourcing contracts to be effectively implemented and managed.
- However, opportunities exist to improve the management of existing contracts with reference to the established performance measurement and service delivery standards.

Refer pages 77 to 78 for further comments
Major Findings

Public information advertising and community attitudes research

General principles are needed about:
♦ using public funds to obtain and disseminate community attitudes research information, and
♦ placing public information advertisements and announcements, particularly during election periods.

General principles would provide guidance to Ministers, the Leader of the Opposition and public administrators about acceptable practices.

The potential for political advantage to be gained from publicly funded community attitudes research could be removed by:
♦ public disclosure or,
♦ if more appropriate, disclosure to elected representatives of other political parties.

Refer pages 22 to 25 for further comments

Performance information in Agency Annual Reports for 1999/2000

♦ Performance information in Annual Reports of Agencies is again generally unable to provide a comprehensive insight into the extent of their contribution to the achievement of Government policy outcomes.

♦ Financial information included in Annual Reports generally lacks integration with the performance reporting.

♦ The Government has announced its intention to develop a financial and performance management framework.

♦ During the development of this performance accountability framework, the Legislative Assembly could also discuss what level, if any, of independent audit assurance it requires over performance information provided to it by the Government.

Refer pages 74 to 76, and 82 to 86 for further comments
What is selected for reporting to the Legislative Assembly?

In reporting on the results of audits completed in the six months, this Report outlines only those matters which the Auditor-General considers would contribute fresh and useful information to the Members of the Northern Territory Legislative Assembly.

Records of Parliamentary debates, interviews with Members by the Auditor-General, and public interest in issues, influence the decisions on the selection of audits topics, and matters to be reported. Matters in the Report include compliance by public sector managers with legislative requirements for financial and performance management; analysis of financial and other performance information; as well as general comments on matters arising from audits conducted.

Members have the opportunity to use the information in reviewing the performance of public sector administration, for which the Executive Government is responsible to the Parliament.

What other reporting arises from audits?

More detailed findings from audits are included in reports issued to the appropriate chief executive officer after each audit.

How is this Report to the Legislative Assembly structured?

This Report presents findings in relation to the audit mandate provided by the Audit Act, that is:

− audits of the Public Account and other accounts (described in Appendix 4), and
− audits of performance management systems (described in Appendix 5).

Topical issues are also included, being matters drawn from, or explaining the context in which, the planning and conduct of audit work occurs.

Where appropriate, this Report updates the status of significant audit findings in previous Reports to the Legislative Assembly.

Are entities able to include their responses in the Report?

The Audit Act enables entities referred to in the Report to provide comments for publication. These comments, or an agreed summary, must be included in this Report. Where no comment is shown in this Report, the relevant Agency has decided not to provide a response for publication.
## Entities referred to in this Report

### By Ministerial Portfolio:

#### Chief Minister; Attorney-General

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Auditing the Public Account and other accounts

Acquisition of the Darwin to Katherine Transmission Line

KEY FINDINGS

♦ The Darwin to Katherine Transmission Line (the Line) was acquired by the Power & Water Authority in November 2000 through the settlement by the Government of a legal dispute.

♦ The $43 million settlement amount was paid by the Government based on its desire to remove the risks entailed in an expensive legal action which had uncertain outcomes, and on its assessment that acquiring the Line as part of the settlement terms delivered strategic benefits.

♦ The $43 million settlement was a negotiated position which the Government recognised was greater than its estimates of the value of the Line, but less than its obligations under the original construction and financing arrangements for the Line.

♦ The difference between the commercial value of the Line and the $43 million settlement is the premium which the Government has paid to obtain the risk minimisation and strategic benefits it sought. The value of the Line may be determined once the Utilities Commissioner rules on revenue to be earned from ownership of the Line from 1 July 2001.

♦ While the final decision required the exercise of judgement by the Government, the processes which delivered the advice to the Government, and which eventually lead to the approval of the settlement offer, were appropriate to the circumstances.

♦ No obligation by the Government existed with sufficient likelihood to require any further disclosures in the 1999/2000 Treasurer’s Annual Financial Statement.

Background to the audit

Considerable Parliamentary and public interest followed the Government’s announcement of the terms of the settlement of a legal dispute with the Power Facilities Group of companies on 10 November 2000 for $43 million. This dispute was to be heard in the New South Wales Supreme Court to resolve whether the Government and the Power & Water Authority (PAWA) were required to guarantee the purchase of the Darwin to Katherine Transmission Line (the Line) between September 1998 and September 2008. (This dispute was separate to another legal action initiated in the Federal Court by the same litigant relating to access rights
Auditing the Public Account and other accounts
Acquisition of the Darwin to Katherine Transmission Line

Background to the audit (continued)

to PAWA’s distribution network. That action had been heard between August 1999 and March 2000, with judgement now awaited).

The terms of the settlement announced on 10 November 2000 included the acquisition by PAWA of the Line. The public and Parliamentary debate interpreted the $43 million payment as the cost of purchasing the Line, and questioned whether that was a reasonable price.

Public uncertainty also emerged over whether the Government had accepted that it was required to make the payment in accordance with the pre-existing guarantee obligation. If so, that would have been required to be disclosed as a contingent liability in the Treasurer’s Annual Financial Statement (the Statement) which had been tabled in the Legislative Assembly on 19 October 2000. The Statement did refer to previous Government guarantees associated with the financing of the Line’s construction, but highlighted that, on legal advice, these were no longer considered to exist. My audit opinion on the Statement had been issued on 13 October 2000.

The Government also announced that it would need to finance the $43 million settlement offer entirely through borrowings, and that it was PAWA which would make the payment and also carry the borrowings of $43 million as a liability.

The annual financial statements of PAWA had included as a Note an unquantified reference to its acquiring the Line as being a significant after balance date event. My audit opinion on the financial statements of PAWA was issued on 9 November 2000. I was first made aware earlier in the week commencing 6 November of an impending arrangement which would see PAWA acquiring the Line. The transaction was identified as unquantifiable to PAWA as at the date of my signing on 9 November, as the terms of the legal settlement and the financing arrangements between it and the Government’s Treasury Corporation had not been sufficiently finalised.

The Annual Report of PAWA containing the audited financial statements and the Note disclosure was tabled at the next sittings day of the Legislative Assembly, which was 28 November 2000, and during the debate in the Assembly on the purchase of the Line.

In the context of my audits both of PAWA and of the Treasurer’s Annual Financial Statement, I advised the Treasurer on 17 November 2000 that I wished to inquire into the transaction.

I advised the Chief Executive Officer of PAWA on 21 November 2000 of the terms of my intended audit which would be an audit of transactions in the Public Account, in accordance with my powers under Section 13 (1) of the Audit Act. The objective of the audit would be to identify whether:

- appropriate procedures were adopted to recommend and approve the expenditure of public monies for this settlement and acquisition of the Line, and
- disclosures in the 1999/2000 Treasurer’s Annual Financial Statement were sufficient.
Auditing the Public Account and other accounts
Acquisition of the Darwin to Katherine Transmission Line

Background to the audit (continued)

In conducting the audit, and in preparing my findings, I took account of the comments of Parliamentarians in the Legislative Assembly debate on 28 November 2000, and the request to me by the Leader of the Opposition of 15 November 2000 to inquire into the transaction.

My audit entailed inspecting documentation held principally by Northern Territory Treasury, and the Power and Water Authority, and by making inquiries of officers of those Agencies, and also of the Utilities Commissioner.

In conducting an audit examination of the $43 million settlement, I gained an understanding of the arrangements for the original financing and construction of the Line, from which the legal action had subsequently arisen, and obtained an understanding of the advice which had been provided to Government upon which it agreed to the settlement terms.

Background to the financing, construction and ownership of the Line

Construction of the Line from 1988 to 1990

The construction of the Line was financed through a “Build, Own, Operate” arrangement with a private sector participant, with an option for a “Transfer” to the Government after ten years, if the operator did not acquire the financing units, and therefore the ownership, of the Line. A “Build, Own, Operate, Transfer” arrangement is proposed for the Alice Springs to Darwin Railway construction, and similar arrangements have been used for large infrastructure projects in other Australian jurisdictions.

A Government study prior to 1988 had identified that the Line would be beneficial by improving reliability of power supply to the Katherine region and by allowing generating efficiencies through increased output of the large base load generators at the Channel Island power station. An ancillary benefit would be that the Line would also meet the expected power needs of any new mining ventures along the transmission route. It was also hoped that it would be used to link power supplies to the Jabiru mine and township.

The Line was constructed over the period July 1988 to July 1990, a time when prevailing interest rates in Australia were at an historical high.

Northern Territory Treasury advised at the time that Commonwealth Government Loan Council approval for funding would not be available in the required planning timeframe to allow the Government access to such funding. This resulted in the Northern Territory Government seeking private sector interest to build, own and operate the Line. Agreement was reached with Balfour Beatty to finance and construct the Line. On completion, the builder was to sell the Line to a financing and ownership trust. PAWA would then pay the owner and operating company for its use of the line.

The ownership trust structure took advantage of the then taxation benefits when funding infrastructure project, and the trust financiers were expected to provide finance a few points below the prevailing interest rates.
Auditing the Public Account and other accounts
Acquisition of the Darwin to Katherine Transmission Line

The total sum requiring funding amounted to $52.1 million. This is analysed as follows:

<table>
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<tr>
<td>Construction cost</td>
<td>39.19</td>
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<tr>
<td>Management fees to the scheme promoter (Allco Nominees Ltd)</td>
<td>0.54</td>
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<tr>
<td>Interest on funds borrowed during the construction</td>
<td>10.60</td>
</tr>
<tr>
<td>Legal fees</td>
<td>0.02</td>
</tr>
<tr>
<td>Total cost</td>
<td>50.35</td>
</tr>
<tr>
<td>Add: cash deposit with the finance unitholder</td>
<td>1.75</td>
</tr>
<tr>
<td>Total financing required by the arrangement</td>
<td>$52.10m</td>
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Significantly, the interest cost of $10.6 million incurred during the construction phase, was included in the total cost which was then re-financed through the ownership trust. While this is a common accounting treatment in private sector projects, in public sector projects such as the Northern Territory’s State Square, interest on construction funding was not included in the cost calculations.

Ownership from September 1990 to September 1998

The Line was owned by a finance brokerage entity Allco Nominees Ltd as trustee of the NT Power Trust.

Ownership was financed by the National Australia Bank subscribing for approximately $52 million of finance units in the NT Power Trust. NT Power Transmission Pty Ltd (formerly NT Power Pty Ltd) held a different class of ownership in the Trust, called sponsor units. The finance units had contractual rights to 16 half yearly distribution payments, representing interest on the financed amount, up until 28 September 1998.

The Power Facilities Group acquired ownership of the sponsor units, and the operating company NT Power Transmission Pty Ltd, from Balfour Beatty in 1991.

The Line and related easements and operating licenses were leased by the trustee to NT Power Transmission Pty Ltd for an 18 year term commencing 1990. The rent was agreed only for the first 8 years, after which it was to be renegotiated. However, the expectation of the ownership structure entered into in 1990 was that the arrangements would be refinanced and ownership issues reviewed in September 1998. Two options were built into the agreement which allowed either the Power Facilities Group to acquire the National Australia Bank financing units and become the owner as well as the operator of the Line, or, if they did not or defaulted, then for the National Australia Bank to require PAWA to pay the value of the finance units and acquire ownership. The Government indemnified PAWA’s commitments which were to pay a sufficient amount to enable the Group to meet the rent on the Line and to pay out the value of the financing units, if so required.
Auditing the Public Account and other accounts
Acquisition of the Darwin to Katherine Transmission Line

Ownership from September 1990 to September 1998 (continued)

This was the obligation which subsequently was at the centre of the dispute between the Government and the Power Facilities Group.

PAWA sold and bought electricity to and from the Power Facilities Group in accordance with sale/purchase agreements, which were for the same duration and for the same amount as the lease of the Line by Power Facilities Group from the ownership Trust. If the price payable by PAWA was not successfully renegotiated after the eighth year (ie September 1998) PAWA was required to pay a minimum half yearly fee of $2.018 million through until 28 September 2008 irrespective of supply. This was the Group’s minimum lease obligations to the ownership Trust.

The payments by PAWA to the Power Facilities Group enabled it to meet its costs including paying the rent due to the NT Power Trust, which in turn paid the distributions due to the financiers.

The September 1998 change in ownership

28 September 1998 was the date at which Power Facilities Group had an option to acquire the Line, or if they did not do so, the National Australia Bank had the option to require the Government to acquire it, for the value of the financing units at that date.

The Power Facilities Group did acquire the financing units on 28 September 1998. It was the contention of the Power Facilities Group that the Government’s guarantees and indemnities to them as the holder of the financing units, to pay out the value of those units as and when required, continued through as before until 2008.

Legal advice provided to the Government in early June 1998 indicated that the 1988 agreements did not clearly spell out the rights and obligations of the various parties, and there was uncertainty over the continuity of the Government’s guarantees/indemnities, subsequent to a change in the finance unitholder.

The Government subsequently accepted further legal advice that the manner of the acquisition of the financing units by the Power Facilities Group in September 1998 was outside the intent of the original agreements, and so this voided the guarantees and indemnities in those agreements.

Legal action disputing that view was then commenced by the Power Facilities Group against the Government.

Audit findings

How the decision to settle the litigation was justified

The Government’s view in June 1998, when the Power Facilities Group was considering exercising its option to acquire the Line, was that the Government would always eventually be liable to pay out the finance unitholder for the liabilities existing in the financing arrangement.
Audit findings (continued)

The Government’s view was that there was insufficient commercial viability for a private sector owner/operator to acquire the asset because PAWA’s commitment to using the Line expired in 2008, as did the rights over use of the easement used by the Line, which were issued by the NT Government. Negotiations with the Power Facilities Group for a new agreement over the use of the Line, which the original agreements had expected would occur by September 1998, had also broken down.

Accordingly, the Government expected to be required to acquire the Line for $49 million in September 1998, being the $52 million original cost of financing its construction, less the $3 million which by then was the balance, after accumulating interest, of the cash deposit established at the commencement of the project in 1988. However, despite this expectation, the acquisition was uncertain, and so no amount was included in the 1998-99 capital expenditure Budget of the Government.

When the Power Facilities Group did acquire the financing units from the National Australia Bank in September 1998, it did so in the expectation that not only the income stream from PAWA would continue for the next 10 years, but also the right to require the Government to pay out the value of the financing units at any time.

With continuation of the indemnity obligation being disputed by the Government, the net result was that both the Power Facilities Group and the Government were left in a position they were not expecting. Uncertainty existed over the likely outcome of the Court action and, from late 1998, substantial legal costs commenced being incurred.

In the context of this background, negotiations between Government and the Power Facilities Group had commenced by July 1999 to explore the option of the Government acquiring the Line.

Although originally seeking $49 million, by April 2000 the Power Facilities Group were offering a settlement of $45 million. The Government meanwhile had agreed in principle that if it were to settle this litigation, it was to be at a cost less than what it would have been required to incur in September 1998. The settlement offer approved by the Government was $41 million, which was in effect a gross amount of $44 million, less the $3 million cash deposit which would accompany acquisition of the Trust.

The offer amount was derived with reference to the original $49 million obligation of the Government. In establishing this offer, the Government was focusing on the intent in the original agreement to transfer the financing costs of the Line’s construction to its next owner, rather than on any assessment of either the commercial value of the Line or its replacement value. This principle then directed the subsequent negotiations by the Government.
Audit findings (continued)

Having established the offer to settle in quantifiable terms, the benefits of the settlement were not so readily quantifiable. The risk minimisation benefits identified by the Government were:

♦ discontinuing the expense of the legal action with the Power Facilities Group;
♦ removing the uncertainty of the results of the legal action, and the possibility that a loss would expose the Government to having to continue its indemnity to pay out the financing units at some future time, or at September 2008 at the latest; and
♦ removing uncertainty about the extent of additional legal exposures to the Government which may have been entailed with arrangements entered into by the Power Facilities Group from financing their September 1998 acquisition of the Trust;

while the strategic benefits which were identified included:

♦ developing a stable long-term ownership framework for electricity supply by bringing the Line into the regulatory framework to which the rest of the power transmission infrastructure was subject.

Because the Line was owned privately, it was excluded from the regulatory regime administered by the independent Utilities Commissioner. While the Utilities Commissioner preferred to see the Line brought under the regulatory regime, he had adjusted for the former ownership circumstances which prevailed in the pricing model through to 30 June 2001, but he considered this to be transitional, and to be subject to further review. The pricing model did entail recovering a usage fee from the Power Facilities Group from 1 October 2000.

However, this process would have continued to have been complicated for the Utilities Commissioner because of his need to negotiate pricing arrangements in the hostile and litigious environment which existed between PAWA and the Power Facilities Group.

♦ obtaining total ownership of the northern distribution network, which provided the Government with control over the future use of those assets, and the future revenue sources which may become available.

By June 2000, the Government was aware of public statements that John Hancock Financial Services Inc. of the USA had substantial investment interests in the Power Facilities Group. The Government was aware that this company was also considering an investment in the Darwin to Alice Springs Railway construction. It noted the desirability of resolving the timing of the negotiations over the ownership of the Line so that this issue did not spill over into the Railway financing negotiations. When the Government finally agreed on 26 October 2000 to finalise the offer, it agreed to set the offer date as 10 November, so that concerns over this issue could be removed as early as possible.

By June 2000, the negotiations with Power Facilities Group centred on bargaining the Government’s $41 million offer with their alternative $45 million offer, the ownership of the Power Facilities premises at Palmerston, and access to land by the Power Facilities Group to develop a new power generation site.
Auditing the Public Account and other accounts
Acquisition of the Darwin to Katherine Transmission Line

Audit findings (continued)

While the strategic benefits, and the costs and uncertainty of the outcome of the court action brought by Power Facilities Group, remained the primary justifications behind the Government’s desire to acquire the Line, these benefits remained unquantifiable.

The cost of the eventual agreement is set out below:

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<th>$ million</th>
</tr>
</thead>
<tbody>
<tr>
<td>Settlement of the litigation</td>
<td>43.0</td>
</tr>
<tr>
<td>Waiver on standby fee for six months *</td>
<td>0.8</td>
</tr>
<tr>
<td>(Maximum that could be received)</td>
<td></td>
</tr>
<tr>
<td>Waiver of Power Facilities use of the line from 1/4/2000 to 1/10/2000</td>
<td>0.3</td>
</tr>
<tr>
<td>Cost of settlement</td>
<td>$44.1</td>
</tr>
</tbody>
</table>

* As part of the settlement PAWA has provided a six months holiday to Power Facilities Group under the standby generation agreement, so that it would not have to pay PAWA for standing ready to provide back up capacity to supply its customers during that period. The estimated maximum that would have been payable is $841,500. Power Facilities Group were still obliged to pay for electricity usage over that period.

Legal costs of $1.92 million had also been funded by the Government from 1998 to September 2000 for this matter.

As well, the Power Facilities Group were contracted to operate and maintain the facility for two years with the operating budget to be agreed by both parties each year. At the time of this audit the budget was yet to be agreed.

Power Facilities Group was also allowed to retain its head office at Palmerston. Although built on land of the Power Facilities Group, this was an asset of the entities being acquired by the Government, and its depreciated cost value was $554,000.

Power Facilities Group were also granted access to 1 hectare of land at Channel Island to construct new power generation facilities. The Government accepted that this was in keeping with the National Competition Policy expectations. Access was agreed to be at the Australian Valuation Office’s valuation of $100,000 for a 49 year lease, with rights to pay for an extension of that term to 99 years.

Although half yearly payments of $4 million to $5 million have also been made by PAWA to the Power Facilities Group since 1992, these were part of the operating costs of PAWA.
Audit findings (continued)

Advice provided to Government about the value of the Line

Advice from Northern Territory Treasury during June 1998, in the lead up period to the exercise of the option by the Power Facilities Group, was that the line was likely to be worth approximately $30 million, with a replacement cost of $35 million. In June 2000, during the later phases of the negotiations, Treasury advised that the value was likely at best to be $35 million to $40 million, although these were estimates, not formal valuations.

It is apparent that the Government had been advised that the value of the Line in commercial and replacement terms was less than the $43 million, and that the settlement offer was not intended to reflect the value of the Line. Justification for the $43 million settlement amount could only be assessed in terms of the value of the benefits additional to the commercial value of the Line, but these were not clearly quantifiable at the time of the settlement.

The uncertainty of the outcome of the legal action makes an analysis of the purchase decision inconclusive.

If the Government had not settled the legal action, but had been successful in its defence, it would still have been required to pay $4 million per year up until 2008 for access to the Line. PAWA and Power Facilities Group would have needed then to renegotiate a new agreement if PAWA wished to continue to access the Line after 2008. If the Power Facilities Group instead wished to sell the Line at that time to PAWA, the Government would not have been required to pay Power Facilities Group the financing amount as calculated in accordance with the original 1988 Agreements. It could have offered an amount calculated on its assessment of the economic benefit to the Northern Territory, or some other basis.

However, if the Government was to have lost the court action it would still be obligated to pay the Power Facilities Group a minimum of $4 million per year for access to the Line up until 2008, but with the additional obligation to purchase the finance units at any time up until 2008 at a price up to $49 million.

Since the outcome of the legal action will never be known, any attempt now to assess the financial benefit or cost of the Government’s decision to purchase the Line rather than pursuing its other major option of continuing to defend the legal action, will be speculative and inconclusive.

A subsequent commercial valuation of the Line would assist in identifying the premium paid for the additional benefits the Government sought from the settlement.

Now that the Line has been acquired by PAWA, it will need to record the Line in its 30 June 2001 balance sheet using Accounting Standards applying at that date. That would most likely need to be at a valuation reflecting the commercial returns available from the revenues the Line derives. The rulings of the Utilities Commissioner on the Authority’s network pricing would be referred to when establishing that valuation. The Utilities Commissioner published an Issues Paper on this topic on 2 February 2001. He proposes to have determined a revenue basis for the Line, or possibly for PAWA’s electricity network as a whole, for use commencing 1 July 2001. If specific revenues are identified for the Line, these can be
Audit findings (continued)

referred to when estimating future revenues over the life of the Line. This would then form
the basis for calculating the commercial value of the Line to include in the balance sheet of
PAWA. If, however, the Line is incorporated into the whole network infrastructure of
PAWA, it may be that the entire infrastructure is then valued, not the Line separately. In that
case, it may be more difficult to establish a specific value for the Line.

The difference between the commercial value of the Line and the $43 million outlay would
establish the premium which the Government has paid to obtain the strategic and risk
minimisation benefits. That premium will not be identifiable until the commercial value of
the Line is established.

Financial impact/returns achieved from the 5% ownership in the operator of the Line by
Darnor Pty Ltd.

Although PAWA, through its wholly owned subsidiary company, Darnor Pty Ltd, owned 5%
of NT Power Transmission Pty Ltd, the Power Facilities Group company which operated the
Line, that ownership was non-beneficial, so PAWA did not derive profits or dividends. The
net value to the Government of the ownership was assessed during the settlement
negotiations to be nil.

Impact of the acquisition on the commercial results of the Power & Water Authority

The advice provided to Government during the negotiations for the settlement did not focus
on the commercial impact on PAWA, except to the extent of the savings by replacing
operating costs with interest costs. Audit has calculated that saving to be $814,000 per
annum until 2008, based on the current interest cost of the borrowings by PAWA, and the
continuity of the minimum payment of $4.036 million each year.

From the settlement, PAWA has acquired an infrastructure asset which is yet to be valued for
inclusion into its accounting records, and for disclosure in its balance sheet as at 30 June
2001. PAWA has estimated that the Line has a future operating life of a further 38 years at
the date of acquisition. If the Line retains its economic benefits for that term, the value will
need to be depreciated as an additional cost each year over that period. The depreciation cost
will offset the savings each year through to 2008, but will then continue on beyond that date.

As well, in the 2000/01 year, PAWA will need to write off as a cost against its operating
results for that year the difference between the $43 million it has paid for the settlement, and
any separate commercial value for the Line which it will be recording.

Impact of the acquisition on the Net Worth of the Government

PAWA has paid the settlement entirely through borrowing the $43 million from the Northern
Territory Government’s Treasury Corporation, on “interest only” payment terms. Even if
PAWA re-negotiates a principal reducing loan facility, the Government itself has increased
its gross borrowings by $43 million, being a further 2% of its expected 30 June 2001 gross
debt level.
Audit findings (continued)

As with PAWA, the $43 million settlement amount entails more than the cost of the Line, so the accounting records of the Government, and the Treasurer’s Annual Financial Statement at 30 June 2001 should record as capital expenditure only that component of the $43 million which relates to the acquisition of the Line.

**Conclusion as to whether appropriate procedures were adopted to recommend and approve the expenditure of public monies for this settlement and acquisition of the Line**

The following comments summarise the context of the advice and approval for the expenditure of $43 million for the settlement of the litigation over the financing arrangements for the Line:

- The Government expected to be required to acquire the Line for $49 million in September 1998.
- While the strategic benefits of the Line, and the costs and uncertainty of the outcome of the court action brought by Power Facilities Group, remained the primary justifications behind the Government’s desire to acquire the Line, these benefits were unquantifiable.
- The negotiations with Power Facilities Group centred on bargaining the Government’s $41 million offer with their alternative $45 million offer.

A substantial process of research, strategy discussion, legal advice, and negotiations within a litigious and hostile setting lead to the acceptance of the final settlement offer of $43 million. While the final decision required the exercise of judgement by the Government, the processes which delivered the advice to the Government, and which eventually lead to the approval of the settlement offer, were appropriate to the circumstances.

**Disclosures in the 1999/2000 Treasurer’s Annual Financial Statement**

Since 30 June 1988, reference to the Government’s indemnity of PAWA’s guarantee of the operating lease payments to the owners of the Line has been made each year in the Treasurer’s Annual Financial Statement. Since 30 June 1999, the reference had removed the specific recognition of the indemnity as a contingent liability, but referred to the litigation surrounding the matter and the amount of the contingency existing at 30 June 1998. This was the latest date the contingency was measured, prior to the change of ownership on 28 September 1998 and the subsequent legal action over whether the contingency continued.

Section 9 (d) of the Financial Management Act requires the Treasurer to disclose material contingent liabilities, except if the contingent event is unlikely to occur. The Treasurer in his Preface to the Treasurer’s Annual Financial Statement has determined that this is not to include contingencies relating to litigation action.

Legal opinion was obtained by Northern Territory Treasury during the audit of the 1999/2000 Treasurer’s Annual Financial Statement which reaffirmed for audit purposes that the Government’s grounds for defending the legal action were strong, and the prospects for successfully defending the action were very good.
Audit findings (continued)

The legal advice indicated that if that view was correct, there was no contingent liability to the Government at 30 June 2000.

The disclosure of the litigation and of the value of the guarantee at 30 June 1998 in the Contingent Liabilities section in the 1999/2000 Treasurer’s Annual Financial Statement, was a sufficient response in light of the uncertainties which existed, and in regard to the legal advice which was held.

Future audit involvement

I will be involved in reviewing the carrying value of the Line in the financial statements of the Authority, and I will comment on this in a future Report to the Legislative Assembly.

There is also an issue of taxation implications for PAWA arising from the acquisition of the Line. Under the settlement PAWA will arrange to wind up the existing complex financial arrangements for the ownership of the Line which may result in a tax liability to PAWA under the tax equivalent regime. I will investigate and inquire into that matter and similarly report my findings.
Public information advertising and community attitudes research

KEY FINDINGS

General principles are needed about:

♦ using public funds to obtain and disseminate community attitudes research information, and
♦ distributing public information advertisements and announcements, particularly during election periods.

General principles would provide guidance to Ministers, the Leader of the Opposition and public administrators about acceptable practices, and allow better scrutiny of how public funds have been used for these purposes.

There is potential for party-political benefit to accrue from any community attitudes research information when its circulation is only within Government. The potential for political advantage to be gained from publicly funded community attitudes research could be removed by:

♦ public disclosure or,
♦ if more appropriate, disclosure to elected representatives of other political parties.

Background

The audit objective was to determine whether there is reasonable assurance that publicly funded community attitudes research polling and public information advertising conducted by the Government are predominantly for the benefit of the public, ahead of any party-political benefits that may accrue.

This was an audit of the appropriateness of expenditures made from the Public Account.

The general criterion applied in this audit is that expenditure by Governments should be predominantly for the public benefit rather than for the political benefit of the party in Government. The same criteria should also apply to expenditure by the Leader of the Opposition.

Audit findings

There are no principles or guidelines established by the Northern Territory Government or the Legislative Assembly for determining what constitutes acceptable practice.
Audit findings (continued)

Audits undertaken on similar topics in other jurisdictions in Australia, and observation of recent debates in the Northern Territory, have identified the following criteria:

♦ the closer that advertising and communication with the public occurs to an election, the more the government should be publicly differentiating its government funded purpose from its party-politically funded purpose;

♦ consultancy briefs for community attitudes research should be issued with specific terms of reference which define the intended use of the research, against which the consultancy output can be compared;

♦ the administration and supervision of the consultancies awarded for advertising and research should be handled by departmental officers, not Ministerial advisers;

♦ public benefit will be more evidently obtained if research results are tabled promptly in the Parliament, or otherwise made public;

♦ where confidentiality of the results is justified, political advantage will be removed from publicly funded research if the results are shared with members of other parties in the Parliament.

♦ The cost of research into community attitudes can be a legitimate expense of government. However because of the overlap between members of government and members of political parties, it may not always be straightforward to determine whether the primary purpose of research is for government or party-political benefit. The potential for “party-political” use is increased when government withholds research for its exclusive use.

♦ Public information advertising can be used by the Government and by the Opposition parties to promote their policies, but in doing so should not criticise the policies of other political parties, and so gain electoral advantage.

The following examples drawn from instances of Government expenditure highlight why guidelines and principles are needed.

Example 1  

Research and advertising for mandatory sentencing in February and March 2000 could reasonably be seen to have had both a public information purpose, and a party-political purpose.

The initiation of the campaign was identified to have been to defend the Northern Territory’s mandatory sentencing legislation in the face of an inquiry in the Federal Parliament into that legislation, and a campaign by some Federal Parliamentarians to use Commonwealth powers to overturn the legislation.

However, the Chief Minister also stated that the Port Darwin by-election in March 2000 would be fought on the mandatory sentencing issue.

While the political benefit may have been incidental to the main intention of the campaign, it was still achieved using public funds. Twenty-five percent of the total $63,000 expended on the advertising campaign was incurred in media accessed in the Darwin region.
Example 1 continued:
Guidelines or principles in these circumstances may have recommended more disclosure about costs incurred by the Government to inform the Port Darwin electorate about the mandatory sentencing policy during the by-election period. This may be particularly appropriate whenever the timing of a by-election coincides with a high profile political issue.

Public information benefit was achieved from the expenditure incurred on the polling because the poll results were published as part of the campaign strategy. This is an example of how public access to such information should generally be provided.

Example 2  The 1998 native title legislation attitudes poll, funded by the Northern Territory, Western Australia and Queensland Governments, was intended to obtain political influence with the Commonwealth Government.

The Northern Territory’s contribution to this poll was $49,373, being one third of the total cost. Since the purpose of the polling was for a national issue, the research was conducted mostly in Victoria, Western Australia and Queensland.

Information from this poll was shared between parties with a recognised common political viewpoint, but not with other political parties or with the public. Public disclosure of the results could have provided more explicit public benefit.

Example 3  Commissioning of the community attitudes polling contract awarded to Wirthlin Worldwide AustralAsia Pty Ltd (Wirthlin) in June 2000 for a value of $300,000 did not sufficiently demonstrate that value for money was sufficiently considered before awarding the contract. Results are generally not being made public.

Wirthlin were contracted to conduct market research into attitudes both within and outside the Northern Territory, into living and working in the Northern Territory.

A Certificate of Exemption from calling tenders for this contract was approved. However, in so doing, the Government’s assessment to favour Wirthlin was identified not to be based on a formal assessment of the consultant’s capabilities. Rather the assessment was based on undocumented views developed over a period of time that the Managing Director of the company, and its principal investigator, Mr Mark Textor, had the best experience in performing both Northern Territory and national research. However, the Government had been prepared to use Newspoll in February 2000 to conduct the mandatory sentencing polling, both locally and interstate. It was not apparent from records prepared by the Government Communication Office of the Department of the Chief Minister why other consultants such as Newspoll were not also asked to provide a proposal and fee offer for this task.

With a high level of parliamentary and public interest entailed in how the processes of community attitudes polling are arranged, the achievement of value for money should be well documented when procuring such services.

Public disclosure of the results of this polling could also provide more explicit public benefit. If confidentiality is required because the information may provide a competitive advantage for the Northern Territory, the results should at least be disclosed to elected representatives of other political parties, so that the potential for political advantage is removed.
Auditing the Public Account and other accounts
Public information advertising and community attitudes research

Current procedural arrangements
Since its establishment in April 2000, the Government Communications Office has provided professional and administrative support to community attitudes research and public information advertising. However, its role is primarily focused on support to the Government’s Foundations for Our Future vision statements, particularly “Preserve and Build on the Lifestyle of all Territorians”. Publicly funded information advertising and communication is still produced from the offices of Ministers and the Leader of the Opposition. In October 2000, the Chief Minister’s Office produced the “Territory Today” public information brochure, without reference to the Government Communications Office specifically, or to the Department of the Chief Minister generally. The Leader of the Opposition also directly issues a publicly funded “Parliamentary Report” for public information purposes.

Conclusion and recommendations
The development of general principles for obtaining and disseminating research information, and for Government advertising during election periods, is needed both as a guide to Ministers, the Leader of the Opposition and public administrators, and to allow better scrutiny of how public funds have been used.

A committee of the Legislative Assembly, possibly the Public Accounts Committee, could oversight the drafting process and table the recommendations in the Assembly for debate and eventual adoption. In this way, the principles which are adopted should stand above criticism of undue influence by the Government.


The Department of the Chief Minister has commented:
Public officials involved in public information programs refer to a range of existing legislation, conventions and guidelines in performing their duties including the Electoral Act, caretaker conventions and the NTPS Code of Conduct.

The purpose of the Wirthlin market research is to provide the basis for marketing the Northern Territory as the preferred location in the region to live, work and invest. The reason for seeking a tender from a single supplier was documented in the Certificate of Exemption which was approved by the Procurement Review Board. Further explanation has been provided to the Auditor-General as to why other companies, and particularly Newspoll, were not considered for this project.

The Government Communications Office has extensive experience in managing contracts for market research of this type and was satisfied that the Wirthlin contract represented value for money when compared with other research contracts.
 Auditing the Public Account and other accounts

Analysis of the 1999/2000 financial statements of:

Northern Territory Treasury Corporation

**KEY FINDINGS**

- Total borrowing costs remained comparable to the previous year, but should rise in 2000/01 following the increased borrowings obtained for the Government late in the financial year, and the increased interest rates on the new borrowings.

- The policy for limiting interest rate exposure above an upper limit of maturing debt was varied by increasing the upper limit from approximately $200 million to approximately $250 million in any one year.

- The fall in the Corporation’s operating surplus to $15.4 million this year, from $20.6 million last year, was primarily the result of a reduction in the margin applied on the interest it charges the Government for the Government’s general debt holdings. This was changed within Government, not by market forces, so this limits the usefulness of the operating profit as a performance measure.

**Brief financial statistics**

<table>
<thead>
<tr>
<th></th>
<th>2000</th>
<th>1999</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total Assets</td>
<td>2,205.5</td>
<td>2,082.7</td>
</tr>
<tr>
<td>Total Liabilities</td>
<td>2,171.9</td>
<td>2,049.1</td>
</tr>
<tr>
<td>Net investment of public funds in the entity</td>
<td>33.6</td>
<td>33.6</td>
</tr>
<tr>
<td>Operating Revenue</td>
<td>186.7</td>
<td>193.0</td>
</tr>
<tr>
<td>Operating Surplus</td>
<td>15.4</td>
<td>20.6</td>
</tr>
<tr>
<td>Dividend</td>
<td>15.4</td>
<td>20.6</td>
</tr>
</tbody>
</table>

**Background**

The Northern Territory Treasury Corporation manages the Northern Territory Government’s borrowings, and the placement of those borrowings, in a manner consistent with the Government’s financial framework and strategies. The Corporation is also responsible for the investment of the cash balances of the Northern Territory, on behalf of the Government.

It prepares financial statements in accordance with Australian Accounting Standards applicable to profit making entities.
Audit analysis

Managing the borrowing requirements of the Government

The Corporation is pursuing its role of minimising the cost of borrowings to the Government in a professional manner. A primary performance target of the Corporation is to minimise the Government’s cost of borrowings for the year, and consequently the total cost of borrowed funds.

The average interest rate across all its borrowings was reduced to 8.9% for the year, down from 9.1% in the previous year. However, the average interest rate on new borrowings during the year increased to 5.6%, from 5.0% the previous year, reflecting the strengthening of longer term interest rates in the market. The interest rate trend in recent years is shown in the following chart.

The continued fall in the average interest rate for all borrowings, when compared with the increased rate on new borrowings for 1999/2000 is attributable to the refinancing of old debt at more favourable interest rates, and the effect of the new borrowings occurring late in the financial year.

In comparison with the New South Wales Treasury Corporation long term bond rate, which is a benchmark used by the Corporation, the Corporation’s borrowing rate showed a margin of 0.21%, an increase of 0.09% since the previous year. This follows a 0.07% increase in the previous year. Although the increases are small, the trend for the margin to be increasing in a period in which gross borrowing levels are also increasing should be noted.

Net borrowings managed by the Corporation, net of foreign currency movements which are hedged through currency swap arrangements, increased by $88 million to $2.017 billion. Interest costs incurred remained almost unchanged, being $167.8 million compared to $167.9 million in the previous year. However the $100 million new borrowings which occurred in June 2000, had negligible impact on borrowing costs for 1999/2000, but will increase overall borrowing costs for 2000/01. The 2000/01 Budget expects interest paid to grow to $184.7 million for that year.
To limit risk on future maturities of its borrowings, the Corporation entered interest rate “swap” arrangements from the 1998/99 financial year. While initially triggered for maturities in any one year which exceed $200 million, or about 10% of gross debt, the upper band now targets a level of approximately $250 million in any one year. The borrowings late in 1999/2000 have resulted in interest rate exposures of debt maturing in 2003 to 2004 approaching this upper level, before declining thereafter to below $200 million.

Managing the portfolio of lendings to Government entities, and the general debt levels of the Government.

The Corporation is able to generate its operating surpluses from the margin it achieves on interest revenue as compared to interest expense. A fall in its operating surplus to $15.4 million this year, from $20.6 million last year, was primarily the result of a reduction in the margin applied by the Corporation when charging interest on the general government component of the Corporation’s lending portfolio. In June 2000, the margin applicable for the 1999/2000 year to that component of the Corporation’s portfolio was reduced from 50 basis points to 10 basis points (i.e. 0.5% to 0.1%). The margin was changed by a decision made within Government, and not by market forces. This limits the usefulness of the operating profit of the Corporation as a performance measure.

By contrast, rates on lendings to specific entities, such as the Government Business Divisions of Darwin Port Corporation, Power and Water Authority and Territory Housing Business Services, in respect of loans made on a fixed term and fixed interest rate basis, remained at the levels in place when the loan arrangements were made in times of higher prevailing market rates.

The profit which is derived by the Corporation is returned in full to the Government as a dividend.

Managing the investment of the Government’s cash balances

An additional performance measure of the Corporation is the return achieved from its investment of the cash balances of the Northern Territory. The Corporation identified that the earnings rate achieved was 5.69%, which increased from 5.0% in the previous year in line with increases in available market rates. For 1999/2000 the earnings rate exceeded its performance benchmark of 5.45%, whereas it equaled the benchmark in the previous year.

Interest earned for the Northern Territory on cash was $13.8 million. These are earnings of the Government, but for budgetary purposes, the Corporation retains those funds. This reduced the funds needed from the Government when it paid the interest of $114 million to the Corporation on the $1.25 billion of general Government borrowings which are included in the assets of the Corporation. The Corporation has not yet adopted market valuation accounting for its assets and liabilities. Such accounting is used by State Treasury Corporations. So the Corporation’s profit result should not be compared to these entities.
Auditing the Public Account and other accounts
Northern Territory Treasury Corporation

Northern Territory Treasury has commented:

The NT Treasury Corporation calculates interest on its loans to the Northern Territory of Australia based on the Corporation's weighted average cost of funds plus an appropriate margin. During the 1990-00 financial year the Corporation conducted a review of its lending practices. The review led to a reduction in the margin applied to floating rate loans to local authorities and Government Business Divisions from 0.70% to 0.50% and to 0.10% for general government debt.

The change in policy resulted from an assessment of the profile and associated risk of the debt. The Corporation does not use operating profit as a performance measure.
Analysis of the 1999/2000 financial statements of Government Business Divisions (GBDs)

General Overview

KEY FINDINGS

- Most GBDs now have clear commercial performance targets in the form of operating surpluses, and the associated dividends to be returned to Government.
- However, the variability between budgeted and actual results which occurred for the 1999/2000 year lessens the usefulness of the budgets as forecasts of commercial performance.
- Disclosure of Community Service Obligation (CSO) funding can still be improved.
- Narrative analysis of financial statements provided by GBDs in their host Agency’s Annual Report would be more informative if they provided comments on why actual results, financial position and cash flows varied from budget expectations.

Analysis of performance expectations and results

The audited financial statements of GBDs should serve a role in assessing how well each GBD is meeting the commercial performance expectations of the Government. GBDs were first established in 1995 to meet requirements of the Commonwealth Government’s National Competition Policy, and to encourage the more vigorous pursuit of operational efficiencies by these entities. With budgets for GBDs now prepared to show their balance sheet, operating statement and cash flow statement, each GBD now has a clearer understanding of its commercial performance expectations, expressed in terms of net worth, operating surpluses, and dividends, which are expected to be 50% of the annual operating surpluses.

Comparison of budget, estimates, and actual operating surpluses provides one high level indicator of the commercial performance of a GBD. However, as identified in the following table, there were considerable variations between final results and both original budgets and mid-year estimates published with the subsequent budget papers. These variations were often caused by unforeseen year end adjustments, but serve to lessen the usefulness of the budgets as forecasts of commercial performance, and as valid goals for performance.
For 1999/2000, a comparison of the expected and actual operating surplus or (deficit) for each GBDs is shown in the following table:

<table>
<thead>
<tr>
<th>GBDs</th>
<th>1999/2000 Budget $000</th>
<th>May 2000 Estimate $000</th>
<th>1999/2000 Actual $000</th>
</tr>
</thead>
<tbody>
<tr>
<td>Construction Agency</td>
<td>101</td>
<td>(3)</td>
<td>1,681</td>
</tr>
<tr>
<td>Darwin Bus Service</td>
<td>189</td>
<td>310</td>
<td>216</td>
</tr>
<tr>
<td>Darwin Port Corporation</td>
<td>(696)</td>
<td>11,002</td>
<td>(48,918)</td>
</tr>
<tr>
<td>Government Printing Office</td>
<td>531</td>
<td>308</td>
<td>118</td>
</tr>
<tr>
<td>Information Technology Management Services</td>
<td>250</td>
<td>2,875</td>
<td>1,412</td>
</tr>
<tr>
<td>NT Fleet</td>
<td>3,475</td>
<td>3,114</td>
<td>4,419</td>
</tr>
<tr>
<td>Territory Housing Business Services</td>
<td>11,275</td>
<td>7,912</td>
<td>5,943</td>
</tr>
<tr>
<td>PAWA</td>
<td>28,953</td>
<td>27,403</td>
<td>44,743</td>
</tr>
<tr>
<td>Territory Discoveries</td>
<td>0</td>
<td>(919)</td>
<td>(1,071)</td>
</tr>
<tr>
<td>Territory Wildlife Parks</td>
<td>(1,423)</td>
<td>(1,516)</td>
<td>(1,112)</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>42,655</strong></td>
<td><strong>50,486</strong></td>
<td><strong>7,431</strong></td>
</tr>
</tbody>
</table>

This illustrates a significant variance in expectations for commercial performance as between GBDs, and a significant variance in actual, estimated actual and budgeted results for each of them.

Narrative analysis and discussion of financial statements of GBDs could include explanations of variances from budget information.

The annual budgets and estimates for GBDs which are presented to, and subsequently adopted by, the Legislative Assembly include the operating statement, balance sheet and cash flow statement.

Once the actual versions of these are finalised after the end of the financial year, comparisons with the budget and estimates versions should be an important performance monitoring tool for a commercial GBD. Comments on causes of variations between actual and budgets could be included in the narrative analysis of the financial statements in the Annual Reports of each GBD’s host Agency.
Auditing the Public Account and other accounts
Government Business Divisions General Overview

Disclosure of the impact of CSO funding on financial results

The Darwin Port Corporation once again provided the best disclosure in its annual financial statements about the impact of Community Service Obligation funding on its profitability in the year, because the extent of any over or under funding of its needs was reported. I continue to encourage this form of disclosure by other GBDs who receive CSO funding.

The use of CSO funding in different ways for dealing with similar situations occurred this year with respect to the Territory Wildlife Parks and Territory Discoveries GBDs. In Territory Discoveries, substantial revenue shortfalls were funded partly by CSO, with a large residual operating loss then being funded by equity contributions from the Government. This is in contrast to how the Government funds the operating losses of the Territory Wildlife Parks GBD. In that case, the cash based operating losses are all funded through a CSO, so the losses reported are then minimised. It is arguable whether the likelihood of achieving a profitable status is any stronger in Territory Discoveries than in Territory Wildlife Parks, yet the difference in the allocation of CSO funding leads to a much less favourable result for Territory Discoveries. Inconsistencies in application of CSO funding contributes to the lack of usefulness of financial results as valid performance measures.

**Parks and Wildlife Commission has commented:**

*Re: the comparison of the methods of funding for Community Services Obligations to Territory Wildlife Parks and Territory Discoveries. The budget for the Parks and Wildlife Commission included a Community Service Obligation for Territory Wildlife Parks. This was to purchase particular outputs that are clearly detailed in Budget Paper Number 2, and are beyond the scope of a commercial enterprise. It is logical that the outputs funded be subject to clear budget processes, rather than funded after they have been provided without budget.*

**A further instance of commercial asset valuations being inappropriate for Whole of Government financial reporting occurred.**

In my February 2000 Report, I highlighted that the Power and Water Authority, and some assets of the Darwin Port Corporation and Territory Housing Business Services were required for commercial accounting purposes to be shown at a valuation much less than the replacement value which would need to be met by the Government. In the case of the PAWA assets, that difference was approximately $500 million.

This year, the new East Arm Port was revalued in the Darwin Port Corporation’s balance sheet at the commercial value of $19 million. Its construction cost, and therefore its estimated replacement value, was $86.7 million. While the commercial valuation of $19 million is appropriate for the commercial accounts of the Corporation, the Treasurer’s Annual Financial Report for 1999/2000 has also disclosed the Corporation’s assets at their commercial value in the unaudited Schedule 6.3. From a Government service provision perspective, these assets would be better disclosed at their replacement value of $86.7 million. The Government as a whole is not a commercial activity, and replacement valuations should be more relevant for decision making and accountability.
Analysis of the 1999/2000 financial statements of GBDs

Power and Water Authority

KEY FINDINGS

♦ While the operating surplus for the year of $45 million compares favourably to $27 million in the previous year, revenues fell in the core businesses of electricity and water.

♦ In particular, electricity sales decreased over the previous year due to the loss of two major customers following the deregulation of the electricity industry on 1 April 2000.

♦ Abnormal and additional Community Service Obligations (CSO) revenues contributed to the profit increase which was recorded.

<table>
<thead>
<tr>
<th>Brief financial statistics</th>
<th>2000</th>
<th>1999</th>
</tr>
</thead>
<tbody>
<tr>
<td>$ million</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total Assets</td>
<td>881.9</td>
<td>875.5</td>
</tr>
<tr>
<td>Total Liabilities</td>
<td>300.1</td>
<td>312.0</td>
</tr>
<tr>
<td>Net investment of public funds in the entity</td>
<td>581.8</td>
<td>563.5</td>
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<tr>
<td>Operating Revenue</td>
<td>403.2</td>
<td>381.3</td>
</tr>
<tr>
<td>Operating Surplus after income tax</td>
<td>44.7</td>
<td>26.9</td>
</tr>
<tr>
<td>Dividend</td>
<td>26.5</td>
<td>12.8</td>
</tr>
</tbody>
</table>

Background

The Power & Water Authority is the primary provider of electricity generation and distribution services, and the sole provider of water and sewerage services in the Northern Territory. It electricity generation market was opened to a competitor during the year, and it is also required to restructure its business operations to meet the requirements of the National Competition Policy. It is also required by Government to achieve a $30 million financial improvement target over the three year period 1999 to 2001.

A governing Board of Directors was also appointed during the year.

The GBDs annual financial statements should be an important source of information to assess how well it is achieving its financial goals in a competitive market environment.
Audit analysis

Operating results

While the operating surplus for the year of $45 million compares favourably to $27 million in the previous year, revenues fell in the core businesses of electricity and water.

Lower electricity and water revenues have been partially offset by revenue from Network Access, System Control and Generation revenue. These are three new revenue sources arising from the new competition regime. Details are shown in the following table.

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>$ million</td>
<td>$ million</td>
<td>$ million</td>
<td>%</td>
</tr>
<tr>
<td>Electricity Sales</td>
<td>212.9</td>
<td>217.5</td>
<td>(4.6)</td>
<td>(2.1)</td>
</tr>
<tr>
<td>Water sales</td>
<td>31.0</td>
<td>31.3</td>
<td>(0.3)</td>
<td>(1.0)</td>
</tr>
<tr>
<td>Network access regime</td>
<td>0.8</td>
<td>-</td>
<td>0.8</td>
<td></td>
</tr>
<tr>
<td>System Control and generation revenue</td>
<td>0.4</td>
<td>-</td>
<td>0.4</td>
<td></td>
</tr>
<tr>
<td>Sewerage</td>
<td>18.1</td>
<td>17.6</td>
<td>0.5</td>
<td>2.8</td>
</tr>
<tr>
<td>Gas sales</td>
<td>3.5</td>
<td>2.8</td>
<td>0.7</td>
<td>25.0</td>
</tr>
</tbody>
</table>

The statistics published in the Authority’s 1999/2000 Annual Report indicate that the volume of electricity sold decreased from 1,484,231MWh in 1998/99 to 1,437,530MWh in 1999/2000, a fall of 3.1%. The main cause of the fall in electricity sales was attributed to the loss of two major customers as a result of the deregulation of the electricity industry on 1 April 2000. The full year effect of the decrease in commercial electricity tariffs introduced in April 1999 also affected revenues.

While the volume of electricity sold decreased, the published statistics advised that over the period the Authority’s installed capacity increased by 15.4% from 338MW to 390MW. The Authority needs to retain sufficient capacity to meet peak demands and to allow for routine maintenance of its generators.

Water volumes and revenues also reduced in comparison with the previous year. PAWA has identified the prolonged northern Wet Season as the cause.

Revenue from sewerage charges increased by 2.8% over the prior year as the development of new suburbs in Darwin and Palmerston increased the number of connections.

PAWA buys gas from producers in the Palm Valley Gas Field and transports the gas to Alice Springs. PAWA sells gas to three customers as well as using the gas for its own electricity generation. Energy purchases which include distillate and electricity, as well as gas, were $138.8 million, which compares with $132.1 million in the previous year. PAWA’s purchase price for gas was increased during the year.
The 1999/2000 budget issued in April 1999 had predicted a net operating surplus for the year of $20.3 million. This estimate was revised to $27.4 million by May 2000 which then compares to the actual result of $44.7 million.

Significant contributors to the $18 million increase in the operating profit over the previous year, and in comparison with budget expectations, include an additional $11.2 million in Community Service Obligation (CSO) revenue from the Government; $5 million in additional customer and developer contributions; and $3.6 million of revenue earned in prior years being claimed from the Department of Defence.

In total, PAWA has recognised as revenue in the year $4.5 million of undercharging to the Department of Defence in regard to electricity supplies to the Larrakeyah Army Base. Of this amount, the $3.6 million is attributable to prior years and has been disclosed as an abnormal item in PAWA’s financial statements. The undercharging was identified after the Department of Defence transferred their electricity requirements to a private sector provider. PAWA has entered into negotiations with the Department of Defence to recover the shortfall.

PAWA recognises as Customer and Developer revenue contributions, the value of electricity, sewerage and water infrastructure included in residential and industrial developments of private sector providers when control of this infrastructure is passed to PAWA. Recognised revenue increased from $16.5 million to $26 million. Continuation of these levels of revenues is dependent on the extent of private sector development projects in any year.

Impact of CSO funding

CSO funding for the year at $58.9 million represents 14.6% of the Authority’s operating revenue. A change in the method of calculating the uniform tariffs CSO accounted for $10.1 million of the overall increase in CSO revenue. PAWA currently does not provide in its annual financial reporting an understanding of how the CSOs are determined from year to year and the actual costs to PAWA for delivering the CSOs. This reduces the validity of comparing the annual operating results of PAWA year by year when assessing its commercial performance.

Net Worth

The 1999/2000 budget had estimated the net worth of PAWA to be $777 million by 30 June 2000. When the 2000/01 budget was delivered in May 2000 the estimated net worth by year end was predicted to be at $573 million, a reduction of $204.18 million over the original budget. The actual 30 June 2000 net worth of PAWA was $582.3 million. The main reason for the difference between the original budget delivered in April 1999 and the later estimate and actual result was the revaluation of property, plant and equipment at 30 June 1999 which resulted in a $211 million reduction in the value of these assets.
Cash Flows

The original budget had planned for capital expenditure of $35.0 million, however by the May 2000 estimates this figure was revised to $69.14 million due to an earlier than scheduled purchase of a new generator at Channel Island for $33 million. Actual capital expenditure for the year was $60.5 million.

The original budget also allowed for a dividend to Government of $3.5 million, which was increased in the May 2000 estimates, and in the final results, to $12.6 million.

Cash flow sourced from the operating surplus was able to fund the increased capital expenditure and the dividend to Government, while available cash balances generated in previous years were able to fund the net $20.1 million repayment of borrowings.

Competition focus

The Authority is responding to the challenges that have arisen as a result of the introduction of the Government’s electricity reform policies. In particular:

♦ the appointment of a Board of Directors to increase the commercial focus;
♦ establishment of an Internal Audit Committee and Internal Audit Charter;
♦ progress with the $30 million improvement program;
♦ significant progress in understanding the National Competition Council’s requirements for ring fencing, and progressing to compliance; and
♦ restructuring of the general ledger for income and expenditure items.

Currently, whilst much has been done to prepare for the ring fencing requirements, PAWA has some way to go to ensure compliance with the ring fencing code. The systems in place within PAWA that support the financial management activities have been reviewed by consultants and I note that significant recommendations have been suggested to overcome the functional inadequacy in PAWA’s present systems.

Strengthening accounting controls

A number of opportunities to improve the accounting controls have been identified, especially:

♦ all aspects of accounting for PAWA’s $766 million of property plant and equipment. The written down replacement value of this equipment is $1.2 billion;
♦ delivery of the planned internal audit activity; and
♦ preparing commercially focused financial information for management and the Board to assist decision making. In this regard, the Board recently approved the calling of tenders for the replacement of PAWA’s financial management system.
Analysis of the 1999/2000 financial statements of GBDs

Territory Housing Business Services

KEY FINDINGS

♦ An operating profit has been achieved for the first time resulting primarily from increased CSO funding and relief from the high debt burden.

♦ Notwithstanding accumulated losses of $4.8 million as at 30 June 2000, the net investment of public funds in the entity was $690 million at 30 June 2000, and remains strong as a result of asset revaluations, and retention of equity from housing stock sales.

Brief financial statistics

<table>
<thead>
<tr>
<th></th>
<th>2000</th>
<th>1999</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total Assets</td>
<td>1056.7</td>
<td>1110.1</td>
</tr>
<tr>
<td>Total Liabilities</td>
<td>366.1</td>
<td>473.3</td>
</tr>
<tr>
<td>Net investment of public funds in the entity</td>
<td>690.6</td>
<td>636.8</td>
</tr>
<tr>
<td>Operating Revenue</td>
<td>90.8</td>
<td>72.5</td>
</tr>
<tr>
<td>Operating Surplus/(Deficit) after abnormal items and income tax</td>
<td>5.9</td>
<td>(27.6)</td>
</tr>
<tr>
<td>Dividend</td>
<td>2.9</td>
<td>nil</td>
</tr>
</tbody>
</table>

Background

This GBD controls and manages the Government’s rental housing stocks, and the mortgage assets arising from sales of the housing stocks.

In previous years, this GBD incurred significant levels of operating losses, because of inadequate Community Service Obligation (CSO) funding, and a high debt burden.

Audit analysis

Operating results

An operating surplus was achieved for the first time because CSO funding was increased to more appropriate levels, and the high debt burden was reduced.
The operating surplus of $5.9 million in the 1999/2000 financial year was a turnaround of $33.6 million from the deficit of $27.6 million in 1998/99. The turnaround resulted from:

♦ CSO funding being increased by $14.1 million, of which $12.8 million was to bridge the gap between actual rebated rent received and market rent;

♦ Borrowing costs falling by $13.5 million as a result of transferring loans of $105 million back to general Government debt from the commencement of the financial year;

♦ Repairs and maintenance expenditure falling by $3 million. This resulted mainly from a change in the accounting treatment of minor capital works and upgrade costs. Previously, this expenditure was expensed against profit, but in 1999/2000 the expenditure was capitalised.

**Impact of CSO funding**

Disclosures in the financial statements allow the impact on the profit for the year of some of the CSO funding to be assessed. Funding for the Interest Subsidy Scheme, and rent reductions was $28.5 million, whereas $26.8 million was reported as expenditure for those categories. The $1.7 million difference is likely to relate to the interest rate differential between market rates and the low interest rates offered through Government policy, but this information is not discernible from the financial statements. As CSO funding is intended to be profit neutral, information about expenditures relating to significant CSO funding levels would be relevant when assessing commercial performance.

**Dividends paid**

A $2.9 million dividend to government, representing 50% of the $5.9 million profit for the year, has been provided for in the financial statements, even though the GBD still showed accumulated trading losses of $4.8 million as at 30 June 2000. The Financial Management Act provides that the Treasurer may determine that a GBD is to pay a dividend to the Territory, if the Treasurer is satisfied that the GBD has sufficient resources to do so.

**Net worth**

Notwithstanding that the GBD still had accumulated operating losses of $4.8 million as at 30 June 2000, the net investment of public funds in the entity increased from $636.8 million to $690.6 million during the year. This is the result of the accumulation over time of asset revaluations totaling $411.7 million, and the retention as equity of $235.7 million of accumulated proceeds from housing stock sales.

With a policy of revaluing urban properties to market values every three years and the increasing value of urban real estate, values of housing stocks have increased over time. The revaluation increments are transferred directly to Reserves, rather than being included in the operating surplus. This is in accordance with Australian Accounting Standards.

The Reserves in respect of property revaluations of $411.7 million which had accumulated by 30 June 2000 represent 52% of the $792.6 million of housing stock value carried in the balance sheet of the GBD. Additionally, when properties are sold, the revaluation component is transferred to a separate Reserve. The accumulated balance of this Reserve at 30 June 2000 of $235.7 million represents the gain to the GBD, and to the Government, on the sale of housing assets. Its retention by the GBD represents an equity investment by the Government, although the $2.9 million dividend for the year would have been sourced from this Reserve.
Auditing the Public Account and other accounts

Analysis of the 1999/2000 financial statements of GBDs

Darwin Port Corporation

**KEY FINDINGS**

- Stage 1 of the East Arm Port was written down from its cost of $86.7 million to its commercial value of $19 million.
- As a consequence, the net worth of the Corporation fell by $48 million.

<table>
<thead>
<tr>
<th>Brief financial statistics</th>
<th>2000</th>
<th>1999</th>
</tr>
</thead>
<tbody>
<tr>
<td>$ million</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total Assets</td>
<td>67.9</td>
<td>135.6</td>
</tr>
<tr>
<td>Total Liabilities</td>
<td>41.6</td>
<td>61.7</td>
</tr>
<tr>
<td>Net investment of public funds in the entity</td>
<td>26.2</td>
<td>73.9</td>
</tr>
<tr>
<td>Operating Revenue</td>
<td>17.7</td>
<td>17.1</td>
</tr>
<tr>
<td>Operating (Deficit) after income tax</td>
<td>(48.9)</td>
<td>(0.8)</td>
</tr>
<tr>
<td>Dividend</td>
<td>nil</td>
<td>1.37</td>
</tr>
</tbody>
</table>

**Background**

The Corporation manages a portfolio of wharf and other marine assets in Darwin, including the infrastructure developed for the new port facility at East Arm in Darwin Harbour. That facility was officially opened in February 2000 and in time is expected to handle all industrial port requirements. The former wharf infrastructure adjacent to the Darwin central business district is to be reserved for cruise ships, visiting naval vessels and other tourism related activities.

**Audit analysis**

*Operating results*

The operating profit, before abnormal items, increased by $1.5 million to $4.2 million.

Contributing to the increase in the surplus was the impact of CSO funding, as detailed below, and also:

- a decrease in interest charges of $413,000, due to a $20.5 million reduction in debt in exchange for government of surplus Corporation land and buildings to that value;
- a 3.7% or $427,000 increase in sales revenues, arising from increases in both charge rates and shipping visits, which more than offset the reduction in cargo tonnages handled.
Impact of CSO funding

A surplus arising from CSO funding of $371,000 followed a deficit of some $1 million in the previous year. Timing of the receipt of CSO revenues has impacted that comparison. $500,000 was received in the year for work funded in the previous year, although $100,000 of that is to be expended by the Corporation in 2000/01. Adjusting for the effect of this net $400,000 surplus from timing variations, indicates that CSO funding would have been at levels appropriate to the needs of the Corporation.

Dividends paid

Despite an operating profit from trading, the impact of the loss on the write-down of the East Arm Port infrastructure meant that a net loss for the year was incurred, and no dividend was paid.

Net worth

The net worth of the Corporation fell by $48 million during the year. This was due to a write off of $67 million from the original cost of the completed Stage 1 of the East Arm Port. This was offset to an extent by the operating profit for the year, and by a profit of $8.6 million recorded on the transfer of surplus land to Government, at a valuation of $20.5 million.

The new East Arm Port is carried in the Corporation’s balance sheet at the commercial value of $19 million. This valuation was calculated by the Australian Valuation Office using the recoverable amounts test, which looks at the commercial returns available from the facility. Its construction cost, and therefore its replacement value, as at 30 June 2000 was $86.7 million.

The Corporation’s borrowings from Government are $35 million. Borrowings were adjusted down from $56 million, by offsetting the land transfer at the value of $20.5 million.

This level of borrowings is funding the $56 million carrying value of the land and infrastructure assets of the Corporation, of which the East Arm facility is valued at $19 million. The “old” Port facilities are carried at $33 million. That valuation is dependent on the Northern Territory Treasury compensating the Corporation at those values, when these assets reach the end of their useful life as operations transfer to the East Arm Port. The compensation values were determined in 1996 as the recoverable amounts. A review of those valuations during 2000/01 is expected.

Although complying with Australian Accounting Standards, the application of the recoverable amounts test to the East Arm Port is potentially misleading to users of the financial statements since it understates the replacement value to the Northern Territory of Stage 1 of the Port. The Darwin Port Corporation may be required by the Northern Territory Government to replace the infrastructure, if necessary, regardless of its recoverable amount, to continue to meet the Northern Territory’s future needs. I referred to this difference in the valuation bases in my audit opinion on the Corporation’s annual financial statements. I did so because I saw that it was necessary on this occasion to highlight the very different values derived depending on how a reader viewed this major asset – that is, purely as contributing to a commercial operation, or as transport infrastructure essential to the Government’s transport policies.
Analysis of the 1999/2000 financial statements of GBDs

TAB

KEY FINDINGS

♦ The TAB ceased trading on 30 June 2000 upon the sale of its assets to the new Totalisator Licence holder.
♦ The sale process demonstrated accountability and ethical practice.
♦ The independent assessment of the bids from the two preferred bidders, based on the key evaluation criteria, recommended the TABQ bid as it presented the least risk to the Territory.

Brief financial statistics

<table>
<thead>
<tr>
<th></th>
<th>2000</th>
<th>1999</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>$ million</td>
<td>$ million</td>
</tr>
<tr>
<td>Total Assets</td>
<td>4.9</td>
<td>5.6</td>
</tr>
<tr>
<td>Total Liabilities</td>
<td>4.9</td>
<td>2.9</td>
</tr>
<tr>
<td>Net investment of public funds in the entity</td>
<td>-</td>
<td>2.7</td>
</tr>
<tr>
<td>Operating Revenue</td>
<td>14.5</td>
<td>14.9</td>
</tr>
<tr>
<td>Operating Surplus</td>
<td>4.8</td>
<td>6.1</td>
</tr>
<tr>
<td>Distributions</td>
<td>7.5</td>
<td>7.0</td>
</tr>
</tbody>
</table>

Background

The TAB was a business unit of the Racing Commission, and was administered by the Department of Industries and Business. During the year, the Government called for submissions from private sector parties to purchase the Totalisator operating rights in the Northern Territory. That process concluded on 30 June 2000 with the issue of the license to NT TAB Pty Ltd, a subsidiary of TAB Queensland Limited (TABQ). The TAB ceased trading on 30 June 2000 with the sale of its assets to the new Totalisator Licence holder.
Audit analysis

Distributions from the GBD for the year
As the TAB had no ongoing role, the retained earnings previously held in reserves were distributed with the operating surplus for the year. In concluding the affairs of the TAB, costs to transfer the operations of the business of the TAB from the Territory to TABQ included $318,850 of severance pay, long service leave entitlements of $30,888, and the $958,000 write-down of capital assets.

$2.662 million was distributed from Reserve Accounts of the TAB straight to the Government’s Consolidated Revenue Account, while $1.5 million was distributed to the Industry Assistance Fund (IAF). With the repeal of the Totalisator Administration and Betting Act on 12 June 2000, all remaining funds in the IAF were also transferred to the Consolidated Revenue Account.

Previously, in July 1999, as part of the Northern Territory Racing Industry Agreement, the Government paid out the loans due by the Alice Springs and Darwin Turf Clubs, of $0.4 million and $2.9 million respectively, which had been guaranteed by the Racing Commission.

Sale of the TAB
The sale of the TAB (NTTAB) business to TABQ was settled on the 30 June 2000 for the following amounts:

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Capital assets</td>
<td>325,000</td>
</tr>
<tr>
<td>Agents’ cash floats</td>
<td>68,000</td>
</tr>
<tr>
<td>Less: Leave adjustment for transferring employees</td>
<td>(17,156)</td>
</tr>
<tr>
<td>Less: Agents Cash bonds held by NTTAB to be replaced by TABQ</td>
<td>(42,000)</td>
</tr>
<tr>
<td>Payment to NTTAB</td>
<td>$333,844</td>
</tr>
<tr>
<td>Payment to NT Government for Totalisator Licence</td>
<td></td>
</tr>
<tr>
<td>Licence amount</td>
<td>7,675,000</td>
</tr>
<tr>
<td>GST</td>
<td>767,500</td>
</tr>
<tr>
<td></td>
<td>$8,442,500</td>
</tr>
</tbody>
</table>

The audit found that the sale process had demonstrated accountability and ethical practice.
Sale of the TAB (continued)

This opinion was based on the following:

- an information memorandum was supplied to all potential purchasers that clearly set out:
  - the sale process;
  - the structure of the sale;
  - the structure of indicative offers; and
  - the sale criteria;
- an independent assessment was made against the sale criteria for each bid to identify the preferred purchaser;
- the selection of the preferred purchaser was in accord with the independent advice;
- the probity auditor engaged to oversee the process and attend meetings with proposed purchasers confirmed the equity of the process and confirmed that no probity issues arose; and
- the Minister provided a full and open disclosure of the sale process to the Legislative Assembly on 14 June 2000.

By March 2000 there remained two preferred bidders – International All Sports (IAS) and TAB Queensland (TABQ).

The independent assessment by Macquarie Bank Limited of the bids from the two preferred bidders, based on the key evaluation criteria recommended the TABQ bid as it presented the least risk to the Territory. In particular:

- IAS’s bid was considered to have greater risks as it could not guarantee access to another TAB’s pool;
- TABQ could provide a seamless transition from a Territory owned business to a private operator and TABQ are an experienced organisation in totalisator management; and
- TABQ has greater financial capacity.

While the IAS bid provided a substantially higher up front payment of $15 million as compared to the TABQ payment of $8 million, the lower tax rate proposed by IAS (30% versus TABQ 40%) over the life of the Licence results in the net present value of the bids (not adjusted for risk) being similar, at $58 million.

At discussions with both bidders held in April 2000 the possibility of non-exclusivity regarding the pari mutuel (a form of betting in which winners divide the losers’ stakes less a percentage for management) sports betting licence was raised. TABQ advised that this proposal would have no effect on its bid (as it already holds this licence in Queensland) while IAS suggested that this was a major part of the assets it wished to acquire.

The decision was made by Government on 6 June 2000 to offer the sale to TABQ with non-exclusivity regarding the pari mutuel sports betting licence as this offered the maximum benefit to the Northern Territory. This would allow IAS and others to enter the global pari mutuel sports betting market. On 13 June 2000 Government approved the granting of a sports Totalisator Licence to IAS.
Analysis of the 1999/2000 financial statements of GBDs

Territory Wildlife Parks

KEY FINDINGS

♦ With the incorporation of the Alice Springs Desert Park into the reported operations of the GBD the operating deficit of the GBD increased from $119,000 in 1998/99 to $1.112 million in 1999/2000.

♦ Community Service Obligation funding of $7.3 million contributed 73.9% of the GBD’s total revenue.

♦ It continues to be unlikely that Territory Wildlife Parks will meet the expectations for commercial performance which characterise a GBD.

<table>
<thead>
<tr>
<th>Brief financial statistics</th>
<th>2000</th>
<th>1999</th>
</tr>
</thead>
<tbody>
<tr>
<td>$ million</td>
<td>$ million</td>
<td></td>
</tr>
<tr>
<td>Total Assets</td>
<td>24.8</td>
<td>6.70</td>
</tr>
<tr>
<td>Total Liabilities</td>
<td>0.8</td>
<td>0.50</td>
</tr>
<tr>
<td>Net investment of public funds in the entity</td>
<td>24.0</td>
<td>6.20</td>
</tr>
<tr>
<td>Operating Revenue</td>
<td>9.9</td>
<td>4.00</td>
</tr>
<tr>
<td>Operating Deficit after abnormal items and income tax</td>
<td>(1.1)</td>
<td>(0.03)</td>
</tr>
<tr>
<td>Dividend</td>
<td>nil</td>
<td>nil</td>
</tr>
</tbody>
</table>

Background

This GBD includes the Territory Wildlife Park near Darwin, and from 1 July 1999, the Alice Springs Desert Park. The GBD has always required substantial funding from the Government which has been characterised as Community Service Obligation (CSO) funding, but which is arguably more an operating subsidy.

The host Agency is the Parks and Wildlife Commission.
Audit analysis

Operating results

With the inclusion of the Alice Springs Desert Park, the operating deficit of the GBD increased from $119,000 in 1998/99 to $1.112 million for 1999/2000. The Desert Park brought the value of its infrastructure into the financial statement of the GBD, and the consequential increase in depreciation has led to the much larger operating deficit.

Impact of CSO

Community Service Obligation (CSO) funding of $7.3 million contributed 73.9% of the GBD’s total revenue. However, $2 million was returned to various Agencies, including the Parks and Wildlife Commission, as payment for corporate support and other services.

It is likely that large operating deficits will continue to be recorded in future, since the CSO funding only meets cash expenses of the Parks. The dependency of the GBD on CSO subsidies, and its likely continuation of operating deficits, questions whether Territory Wildlife Parks will ever meet the expectations of a GBD, which is:

‘to operate as a fully commercial business, undertaking only those activities that it would ordinarily undertake for commercial reasons.’

Source: Budget Paper No. 3, 2000-01– page 118

Parks and Wildlife Commission has commented:

Re: the operating deficit. It should be noted that Territory Wildlife Parks performed $311,000 better than forecast, and that this was achieved during a year when the GBD was massively increased in size with the addition of the Alice Springs Desert Park.
Analysis of the 1999/2000 financial statements of GBDs

 Territory Discoveries

KEY FINDINGS

♦ An operating deficit of $1.07 million was funded by an equity injection of $1.02 million.

♦ Large operating deficits and offsetting equity injections are expected to continue in future.

♦ The financial performance of the GBD does not appear to be a primary performance indicator.

Brief financial statistics

<table>
<thead>
<tr>
<th></th>
<th>2000</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>$ million</td>
</tr>
<tr>
<td>Total Assets</td>
<td>0.06</td>
</tr>
<tr>
<td>Total Liabilities</td>
<td>0.11</td>
</tr>
<tr>
<td>Net deficiency of public funds in the entity</td>
<td>(0.05)</td>
</tr>
</tbody>
</table>

<p>| | |</p>
<table>
<thead>
<tr>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Operating Revenue</td>
<td>1.36</td>
</tr>
<tr>
<td>Operating Deficit</td>
<td>(1.07)</td>
</tr>
<tr>
<td>Dividend</td>
<td>Nil</td>
</tr>
</tbody>
</table>

Background

Territory Discoveries was established to allow Northern Territory tourist businesses, including the many small operators, to gain exposure in holiday brochures distributed to travel agents nationally and internationally. Territory Discoveries, among other things, packages holiday options, and produces and distributes brochures with these packages through a network of travel agencies. Revenue is from commission on sales of its holiday packages through the Northern Territory Tourist Commission’s Holiday Centre, and through the marketing service it provides to the Northern Territory Tourist Commission, which is funded as a Community Service Obligation. It was declared a Government Business Division by the Treasurer, with from effect 1 July 1999. Its host Agency is the Northern Territory Tourist Commission.
Audit analysis

Operating results

At the time the GBD was established, its funding was expected to be operating revenue from commissions, as well as Community Service Obligation (CSO) funding to substantially offset overall operating costs.

CSO funding for 1999/2000 was budgeted as $1.72 million, although Budget Paper No. 2 for 1999/2000 had foreshadowed that the capital structure of the GBD would be reviewed during the financial year.

During the financial year, the value of the CSO component, in terms of the Government’s GBD policy, was assessed by the Northern Territory Tourist Commission to be only $700,000. At that level, this left the GBD with an operating deficit of $1.072 million. However $1.02 million was provided by the Government as an equity injection, to substantially offset the cash flow impact of that deficit.

The Territory budget for 2000/01 indicates a further expected operational deficit for 2000/01 of $996,000, after CSO funding of $776,000. This deficit is budgeted to be funded again by an equivalent equity contribution. The Balance Sheet of the GBD for the year ending 30 June 2001 will then show large accumulated deficits substantially offset by almost equally large equity contributions.

Net Worth

The Net Worth of Territory Discoveries shows an excess of liabilities over assets. In cash flow terms, the GBD ended the year receiving $40,000 more cash than it expended. Once creditors and employee entitlements were brought to account, liabilities exceeded assets by $51,000.

Financial disclosure in the Annual Report could be improved.

Because of the importance of Government support to the GBD, by way of CSO funding or equity contributions, the Notes to the financial statements, in future years, should include greater disclosure in relation to the basis on which the CSO was derived and the costs associated with performing the services for which the CSO was provided.

The performance of Territory Discoveries is discussed in the Northern Territory Tourist Commission’s Annual Report, in narrative terms. Further comment may be appropriate in the financial analysis section of the Report if the financial result is not the only, or even the most, relevant indicator of its operational objectives. This could include comment and analysis of what the success factors are on which the GBD’s performance is assessed.

NT Tourist Commission has commented:

The 1999/2000 financial year was the first year of operations for Territory Discoveries. The community Service Obligation (CSO) amounts are clearly identified and transparent. The CSO amounts are the costs for Territory Discoveries to deliver those required services that a commercial operator would not deliver. Additionally, the NT Government decided to provide equity to Territory Discoveries progressively over the initial years of operation.
Auditting the Public Account and other accounts

Analysis of the 1999/2000 financial statements of GBDs

Darwin Bus Service

KEY FINDING

♦ Revenue has peaked at around $5.7 million each year, while costs continue to rise, resulting in falling profitability.

### Brief financial statistics

<table>
<thead>
<tr>
<th></th>
<th>2000</th>
<th>1999</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>$ million</td>
<td>$ million</td>
</tr>
<tr>
<td>Total Assets</td>
<td>9.10</td>
<td>9.10</td>
</tr>
<tr>
<td>Total Liabilities</td>
<td>1.30</td>
<td>1.40</td>
</tr>
<tr>
<td>Net investment of public funds in the entity</td>
<td>7.80</td>
<td>7.70</td>
</tr>
<tr>
<td>Operating Revenue</td>
<td>5.70</td>
<td>5.80</td>
</tr>
<tr>
<td>Operating Surplus after income tax</td>
<td>0.22</td>
<td>0.43</td>
</tr>
<tr>
<td>Dividend</td>
<td>0.11</td>
<td>0.26</td>
</tr>
</tbody>
</table>

### Background

The Darwin Bus Service, together with private sector operators, contracts for the provision of buses to the Northern Territory Government in the Darwin and rural area. The Darwin Bus Service earns its revenue from charging the Department of Transport & Works on a “kilometres provided” basis. Bus fares are collected on behalf of the Department of Transport and Works and are revenues of that Department. The GBD earns revenues from the Department at its contracted rate even when it provides free services to the public for special occasions, at the direction of Government.

The Department separately reports the costs of its public transport services, which includes the Darwin Bus Service, in its Annual Report. For 1999/2000 that was a net cost, after accounting for fares received, of $14.1 million.

The Department of Transport & Works is the host Agency of this GBD.
Audit analysis

Operating results

Because of the fixed workload allocated by the Department of Transport & Works, revenue has peaked at around $5.7 million each year. Costs continue to rise, particularly for fuel, which contributed a $43,000 increase in the year.

The downward trend on the profitability of the Darwin Bus Service has been factored into its 2000/2001 budget. The results for the 1999/2000 are very close to the original budget, but are below the May 2000 estimate.

Cash Flow statement

The Cash Flow Statement highlights that the $607,000 cash surplus generated from operations in the year together with the cash balance brought forward from last year, contributed to financing the $1 million used for new bus acquisitions, and the dividend paid of $213,000.
Analysis of the 1999/2000 financial statements of GBDs

NT Fleet

KEY FINDING

♦ The operating surplus after tax for 1999/2000 of $4.4 million contrasts with the deficit of $47,000 in 1998/99. Adjustment of hire rates and asset values has achieved the return to profitability.

<table>
<thead>
<tr>
<th>Brief financial statistics</th>
<th>2000</th>
<th>1999</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>$ million</td>
<td>$ million</td>
</tr>
<tr>
<td>Total Assets</td>
<td>71.9</td>
<td>65.60</td>
</tr>
<tr>
<td>Total Liabilities</td>
<td>16.5</td>
<td>12.40</td>
</tr>
<tr>
<td>Net investment of public funds in the entity</td>
<td>55.4</td>
<td>53.20</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Operating Revenue</td>
<td>24.8</td>
<td>22.20</td>
</tr>
<tr>
<td>Operating Surplus/(Deficit) after income tax</td>
<td>4.4</td>
<td>(0.05)</td>
</tr>
<tr>
<td>Dividend</td>
<td>2.2</td>
<td>1.26</td>
</tr>
</tbody>
</table>

Background

NT Fleet was established in 1993 to manage the motor vehicles of the NT Government and in 1995 became a GBD. All but a few Agencies have their motor vehicles supplied through NT Fleet. Police, Fire and Emergency Services is one significant Agency which does not use NT Fleet.

Most vehicle servicing is outsourced to private sector providers.

The GBD does not receive direct funding from Government, other than for a minor Community Service Obligation contribution. Its revenues are derived from charges levied to Agencies for vehicles supplied and maintained. Its charges are approved by Government. The Department of Transport & Works is the host Agency of this GBD.
Audit analysis

Operating results

The operating surplus after tax for 1999/2000 was $4.4 million. This contrasts with the deficit of $47,000 in 1998/99. In the previous year, almost $6.5 million of vehicle resale losses and consequential write downs in vehicle values impacted that year’s results.

Increases in hire rates in expectation of lower asset resale values has achieved the return to a profitable operation.

The previous year’s write downs in vehicle values has achieved better alignment of the book value of assets with market values. Sales in 2000 have confirmed the reasonableness of the residual values determined during 1998/99.

Net worth

After allowing for payment of the dividend, the net worth of the GBD increased by $2.2 million.

The cash balance of $6.25 million is also required to fund not only the dividend, but also the GBD’s tax liability of $2.5 million, and a repayment of borrowings of $3.3 million, although at the time of audit, this repayment was being renegotiated with Northern Territory Treasury Corporation.

Cash Flow Statement

The Cash Flow Statement provides a useful summary of how new vehicle fleet acquisitions are financed. It shows the $12.77 million cash surplus from vehicle hire revenues, together with the $19.97 million generated mainly from the sale of vehicles, was available to finance the $28.64 million of new vehicle acquisitions. The balance of funds generated in the year contributed to NT Fleet’s cash holdings as at 30 June 2000.

The operating surplus for the year is reflected in the cash balance at 30 June 2000 of $6.275 million. Dividends of $2.2 million relating to the 1999/2000 year are payable from these funds.
Auditing the Public Account and other accounts

Analysis of the 1999/2000 financial statements of GBDs

Construction Agency

KEY FINDINGS

♦ The financial results reflect a more commercial position than previously, with the partial implementation of a fee offer system in 1999/2000.

♦ The new method of charging appears to have generated unexpected revenues and profits.

Brief financial statistics

<table>
<thead>
<tr>
<th></th>
<th>2000</th>
<th>1999</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total Assets</td>
<td>$11.7</td>
<td>$10.7</td>
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<tr>
<td>Total Liabilities</td>
<td>$10.6</td>
<td>$10.4</td>
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<tr>
<td>Net investment of/(liability for) public funds in the entity</td>
<td>$1.1</td>
<td>$(0.3)</td>
</tr>
<tr>
<td>Operating Revenue</td>
<td>$35.6</td>
<td>$33.6</td>
</tr>
<tr>
<td>Operating Surplus/(Deficit) after income tax</td>
<td>$1.7</td>
<td>$(1.0)</td>
</tr>
<tr>
<td>Dividend</td>
<td>$0.8</td>
<td>$0.14</td>
</tr>
</tbody>
</table>

Background

Construction Agency is responsible for the project management of the Government’s capital works program and repairs and maintenance program.

A fee offer system was partially implemented in the Construction Agency in 1999/2000.

Professional service entities operating in the Building and Construction industry usually operate on a fee offer system. The charging methods are either “fixed fee”, or a percentage of the program value. These methods place pressure on the entity to achieve efficiencies and to retain costs within the fee range. This is in contrast to the former system of charging based on time worked. That system did not encourage the improvements in efficiency and productivity which were being sought from the GBD.

The GBD does not receive Community Service Obligation funding from Government.

The Department of Transport & Works is the host Agency of this GBD.
Audit analysis

Operating results

The financial results reflect a more commercial position than previously, with the partial implementation of a fee offer system in 1999/2000.

The new method of charging appears to have generated unexpected revenues and profits.

The operating result shows a turnaround from a deficit of $1.005 million in 1999 to a surplus of $2.06 million in the 2000 financial year. A major contribution to this $3.065 million improvement was the additional $2.021 million revenue from billings to client agencies. Revenue was $1.448 million greater than the original budget, and $3.5 million greater than the 1999/2000 estimates included in the 2000/01 Budget Papers.

The improved result also reflects a significant change in accounting for funding received from Treasury for redundancy costs in the year. Funding of $294,000 received for redundancy payouts has been classified as revenue this year. Last year’s funding of $753,000 was allocated as a part recovery from the Recoverable Establishment Fund asset, not into revenue, so the increase in the results between the two years should be reduced by this amount for proper comparison.

Additional funding of $206,000 was received for other eligible employee entitilements and correctly classified as a reduction of the Recoverable Establishment Fund. The Recoverable Establishment Fund is not a pool of cash, but rather an entitlement to draw additional funds from Treasury to meet the annual leave and long service leave entitlements inherited at the time this GBD was created in 1995.
**Analysis of the 1999/2000 financial statements of GBDs**

**Information Technology Management Services (ITMS)**

**KEY FINDING**

- The operating surplus before abnormal items and income tax at $2.207 million for the year was slightly down on the prior year’s $2.235 million. It was achieved during a period of outsourcing of various activities, resulting in an overall reduction in both revenue and expenditure.

### Brief financial statistics

<table>
<thead>
<tr>
<th></th>
<th>2000 $ million</th>
<th>1999 $ million</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total Assets</td>
<td>14.6</td>
<td>15.9</td>
</tr>
<tr>
<td>Total Liabilities</td>
<td>12.3</td>
<td>14.3</td>
</tr>
<tr>
<td>Net investment of public funds in the entity</td>
<td>2.3</td>
<td>1.6</td>
</tr>
<tr>
<td>Operating Revenue</td>
<td>58.2</td>
<td>58.7</td>
</tr>
<tr>
<td>Operating Surplus after abnormal items and income tax</td>
<td>1.4</td>
<td>0.5</td>
</tr>
<tr>
<td>Dividend</td>
<td>0.7</td>
<td>0.6</td>
</tr>
</tbody>
</table>

**Background**

ITMS is currently in transition from being the main provider of IT services to Government, to being a facilitator and consultant to Agencies for their IT needs. Through a process of outsourcing IT service delivery to private sector providers, the GBD now manages contracts for the delivery of e-mail services and advanced communications. The GBD also called for tenders for the provision of desktop/LAN services to government and the provision of mainframe and non-mainframe application support. The GBD continues to manage the Data Centre. The host Agency is the Department of Corporate and Information Services.
Audit analysis

Operating results

The operating surplus before abnormal items and income tax at $2.207 million for the year was slightly down on the prior year's $2.235 million. The result was achieved during a period in which the outsourcing of several of its activities resulted in an overall reduction in both revenue and expenditure.

Lower levels of expenditure in the communications activities due to the outsourcing of Voice and Data in March 2000 were largely offset by an increase in IT Consultants expenditure for Y2K readiness.

Actual revenue for the year of $57.5 million was significantly lower than the May 2000 estimate of $62.1 million published in the Budget Papers. The difference primarily related to the incorporation of internal sales in the May estimates for both actual revenue and expenditure, whereas internal sales were eliminated from the commercial format financial statements for external reporting purposes.

The estimates for expenditure were approximately $3.6 million more than the actual expenditure reported. This also resulted from the elimination of internal sales of about $5 million, offset by an underestimate in outsourcing related costs for personnel terminations and for legal expenses.
Auditing the Public Account and other accounts

Analysis of the 1999/2000 financial statements of GBDs

Government Printing Office

KEY FINDING

♦ Operating profit declined unexpectedly this year, in comparison with the prior year and with budget expectations.

Brief financial statistics

<table>
<thead>
<tr>
<th></th>
<th>2000</th>
<th>1999</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total Assets</td>
<td>4.20</td>
<td>4.40</td>
</tr>
<tr>
<td>Total Liabilities</td>
<td>1.50</td>
<td>1.80</td>
</tr>
<tr>
<td>Net investment of public funds</td>
<td>2.70</td>
<td>2.60</td>
</tr>
<tr>
<td>Operating Revenue</td>
<td>6.90</td>
<td>7.30</td>
</tr>
<tr>
<td>Operating Surplus after tax</td>
<td>0.12</td>
<td>0.36</td>
</tr>
<tr>
<td>Dividend</td>
<td>0.06</td>
<td>0.41</td>
</tr>
</tbody>
</table>

Background

All Government Agencies are expected to use the Government Printing Office (GPO) for their printing and publication needs. The GPO does outsource some work to private sector providers. The host Agency is the Department of Corporate and Information Services.

Audit analysis

Operating results

The operating surplus after income tax for this GBD has been reasonably consistent over the past few years in the range of $300,000 to $400,000 per year. This year’s surplus of $118,000 is noticeably lower. The surplus and dividend results are also lower than the original budget for the year, and the estimates made in May 2000 for the year. These were predicting results at similar levels to past years.

The cause of the drop in profitability, and therefore its dividend, is identified by the host Agency in its Annual Report as being due to lower margins recoverable from Agencies on outsourced work. Payments to subcontractors in the year did increase by $195,000, or 14.6%, over the previous year.
A change in accounting policy required internal sales to be eliminated from revenue and costs for the year. This makes inappropriate any comparison of total sales and total costs between this year and the previous year. For example, if the policy had not changed, operating revenue in 1999/2000 as reported in Note 2 in the financial statements would have been seen to increase by $294,000 or 4.5%, rather than decrease by 3%, as is now shown.

Cash Flow statement

The GPO’s cash balances continue to be applied to the purchase of capital equipment and repayment of borrowings. Cash balances will be further eroded in 2000/01 if budgeted profit levels are not achieved. In that regard, expenses forecast in the 2000/01 Budget are significantly lower than the actual expenses recorded in 1999/2000, so the budgeted profit may be difficult to achieve.
Auditing the Public Account and other accounts

Analysis of the 1999/2000 financial statements of Superannuation Funds

Northern Territory Government and Public Authorities Superannuation Scheme (NTGPASS)

KEY FINDING

♦ The trend of underestimating the emerging cost to the Territory continues, as employees exit the scheme faster than anticipated.

Brief financial statistics

<table>
<thead>
<tr>
<th></th>
<th>2000</th>
<th>1999</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total Assets</td>
<td>303.6</td>
<td>260.8</td>
</tr>
<tr>
<td>Total Liabilities</td>
<td>15.1</td>
<td>16.3</td>
</tr>
<tr>
<td>Net Assets</td>
<td>288.5</td>
<td>244.5</td>
</tr>
<tr>
<td>Change in Net Assets</td>
<td>44.0</td>
<td>30.4</td>
</tr>
<tr>
<td>Vested Benefits</td>
<td>640.5</td>
<td>558.3</td>
</tr>
</tbody>
</table>

(The value of benefits payable on voluntary withdrawal from the scheme at that date.)

Background

NTGPASS was opened to new members on 1 July 1985, and closed to new members on 9 August 1999. It is a defined benefits scheme which means that the Government must provide a specified amount of benefits upon withdrawal from the Scheme, based on the members' contribution rate while in the Scheme.

The future liability of the Government and each year’s emerging costs for providing benefits to withdrawing members is calculated by actuarial measures. Accrued benefits are determined on the basis of the present value of expected future payments which arise from membership of the plan up to the measurement date. The liability for Accrued Benefits is not included in the calculation of net assets. The last Actuarial Review was as at 30 June 1998. The next triennial actuarial review is due at 30 June 2001.

Audit analysis

The increase in net assets of the fund for the year was $44.0 million compared to $30.4 million in the previous year. Significant contributors to the $13.6 million increase include an additional $13.8 million in changes in the net market value of investments; and the additional $9.5 million received as transfers and rollovers; offset by the additional $11.0 million in benefits paid. The Superannuation surcharge expense of $716,000 was recognised in the financial statements for the first time.
Auditing the Public Account and other accounts
NTGPASS

The change in the net market value of investments for the year was $26.1 million, being $13.1 million higher than the $12.3 million recorded in the previous year. This is due to the strong performance of managed investment funds generally in Australia during the year.

William M. Mercer Ltd (Mercers) was appointed during the year by the Superannuation Investment Board to perform an evaluation of investment fund managers. Arising from Mercers’ advice, a revised investment strategy was adopted by the Board. Mercers were then retained as transitional fund managers with the assistance of National Custodian Services and County Investment Management. These interim managers were responsible for arranging transfers from existing funds to suit the new investment strategy, which resulted in the funds being held fairly equally between MLC, Credit Suisse and Vanguard Investments. Stamp duty of $45,000 and the Mercers’ fee of $135,000 were additional costs incurred in changing the investment portfolio.

Actual Territory contributions payable to NTGPASS in 1999/2000 were $33 million, which compares to the budget estimate made in 1998 that payments in the year would be $27.8 million. As the following chart illustrates, this continues the trend of underestimating the emerging cost to the Territory while overestimating the accrued liability, as employees exit the scheme faster than anticipated.

The Department of Corporate and Information Services has commented:

*The estimates are based on 3-yearly trends, and the next update is due at 30 June 2001. The 3-yearly Actuarial Review will incorporate the past trends, and provide a new estimate of the Territory's accrued liability.*
Auditing the Public Account and other accounts

Analysis of the 1999/2000 financial statements of Superannuation Funds

Legislative Assembly Members' Superannuation Trust

KEY FINDING

♦ Government contributions to the Trust were maintained at $1.28 million.

<table>
<thead>
<tr>
<th>Brief financial statistics</th>
<th>2000</th>
<th>1999</th>
</tr>
</thead>
<tbody>
<tr>
<td>$ million</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total Assets</td>
<td>31.9</td>
<td>28.1</td>
</tr>
<tr>
<td>Total Liabilities</td>
<td>0.4</td>
<td>0.2</td>
</tr>
<tr>
<td>Net Assets</td>
<td>31.5</td>
<td>27.9</td>
</tr>
<tr>
<td>Change in Net Assets</td>
<td>3.6</td>
<td>2.7</td>
</tr>
<tr>
<td>Vested Benefits</td>
<td>29.9</td>
<td>28.4</td>
</tr>
</tbody>
</table>

(The value of benefits payable on voluntary withdrawal from the scheme at that date.)

Background

This is the only fully funded superannuation scheme administered by the Government. That is, the vested benefit liabilities of the Fund are matched by the assets held by the Trust. These assets are established from Member’s contributions, and from investment returns earned on the Funds, less payouts to retiring members. When benefits to members were increased in 1998, the Government re-commenced making contributions of public funds. Investment earnings in the several years prior to 1998, together with Members' contributions, had been sufficient to fund the emerging liabilities.

Audit Analysis

For the third year, Government contributions to the Trust were maintained at $1.28 million.

Recovery in the growth in the value of the Trust’s managed superannuation funds, together with the continuing contributions of funds by the Government, which are at rates higher than the 1998 actuarial assessment, has contributed to net assets now exceeding vested benefits at 30 June 2000. Accrued benefits are determined on the basis of the present value of expected future payments which arise from membership of the plan up to the measurement date. The liability for Accrued Benefits is not included in the calculation of net assets. The Actuarial Review was as at 30 June 1998. The next full actuarial valuation at 30 June 2001 should be expected to review the extent of on-going public funding.
KEY FINDINGS

♦ A moderate improvement in underwriting result, together with a significant improvement in investment income, contributed to a $4.6 million turnaround from the 1998/99 loss to the 1999/2000 operating profit before tax of $1.4 million.

♦ The sustainability of this improved performance will depend on TIO’s ability to keep the underwriting loss to a manageable level and the continuance of the higher levels of investment income.

Brief financial overview:

The 1999/2000 operating result appears to be a reversing of the noticeable downward trend in operating results since 1995/96. The following chart illustrates this:

![TIO Operating Results Chart]

Source: Territory Insurance Office Annual Reports

Background

TIO is a wholly owned entity of the Government. It operates with its own Governing Board, but can take direction from the Government. Its mandate from the Government allows it to only write insurance business in the Northern Territory, except for its reinsurance business, where it is accepting risk from national and international sources.
Audit analysis

Operating result

A moderate improvement in underwriting result, together with a $4.2 million improvement in investment income, contributed to a $4.6 million turnaround from the 1998/99 loss to the 1999/2000 operating profit before tax of $1.4 million.

The sustainability of this improved performance will depend on TIO’s ability to keep the underwriting loss to a manageable level and the continuation of the higher levels of investment income.

Premium revenue for the Motor Accidents Compensation Scheme (MACA) increased by $3.8 million or 12% over the previous year, however the underwriting loss during the same period increased by $8.15 million. The increase in net claims expense of $11.6 million was due mostly to an actuarial reassessment of the claims liability of previous years. The fund was able to obtain an operating profit of $2 million for the year, although this was less than half the previous year’s result, due mainly to the higher levels of investment income achieved.

Net worth

Total assets of TIO increased during the year by $40.5 million to $473.5 million, while total liabilities increased by $38.4 million to $440.5 million.
Auditing the Public Account and other accounts

Department of Education

Indigenous Education Strategic Initiatives Program (IESIP)

KEY FINDINGS

♦ Documentation should more adequately evidence that important performance requirements of the IESIP Agreement are being met.

♦ In the absence of suitable documentation, the audit opinion covering the IESIP funding during the year ended 31 December 2000 may be unable to confirm that all funding conditions have been complied with.

♦ The Department was progressing with addressing and implementing recommendations arising from its 1999 internal review of IESIP administration.

Background

The Indigenous Education Strategic Initiatives Program (IESIP) is a Commonwealth funded program intended to contribute to the achievement of improved outcomes in Indigenous education. Funding is subject to Indigenous Education Agreements between the Northern Territory and the Commonwealth which include performance measures, targets and strategies, and reporting on these by the Northern Territory.

An Indigenous Education Agreement covering the funding of the IESIP program in the Northern Territory for 1997 to 1999 was replaced with a new Agreement for the period January to June 2000, and a further Agreement for the period July to December 2000. The Commonwealth had indicated during 2000 that it was intending to establish an Indigenous Education Agreement for the period 2001 to 2004. Reporting on the January to June 2000 Agreement was examined by my Office.

The use of funds provided under IESIP was debated in the Legislative Assembly on 21 October 1999. In the course of the debate findings from an internal Departmental review on IESIP were tabled. This review was critical of aspects of the administration of IESIP funds by the Department, and provided recommendations for management. A Ministerial statement in the Legislative Assembly on 10 May 2000 indicated action had been taken to address IESIP concerns.
Auditing the Public Account and other accounts
Indigenous Education Strategic Initiatives Program

The following table shows IESIP funding from 1997 to June 2000.

<table>
<thead>
<tr>
<th></th>
<th>1997</th>
<th>1998</th>
<th>1999</th>
<th>2000 (Jan-Jun)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Unexpended funds approved for carryover from previous year</td>
<td>$0</td>
<td>$825,558</td>
<td>$118,985</td>
<td>$187,087</td>
</tr>
<tr>
<td>Commonwealth funds provided in the acquittal period</td>
<td>$9,917,762</td>
<td>$9,917,762</td>
<td>$10,057,782</td>
<td>$5,056,929</td>
</tr>
<tr>
<td>Interest/royalties/other income derived from the funds</td>
<td>$36,874</td>
<td>$29,040</td>
<td>$23,772</td>
<td>$6,351</td>
</tr>
<tr>
<td>Total funds to be acquitted for this period</td>
<td>$9,954,636</td>
<td>$10,772,360</td>
<td>$10,200,539</td>
<td>$5,250,367</td>
</tr>
<tr>
<td>Funds expenditure during acquittal period</td>
<td>$9,129,078</td>
<td>$10,653,375</td>
<td>$9,778,846</td>
<td>$5,063,430</td>
</tr>
<tr>
<td>Commitment (made before 31 December)</td>
<td>$825,558</td>
<td>$118,985</td>
<td>$187,087</td>
<td>$291,024</td>
</tr>
</tbody>
</table>

Audit Findings

An important aspect of the audit was establishing that acquittal reports provided by the Northern Territory to the Commonwealth satisfied the obligations required of the Northern Territory.

The Department’s January to June 2000 financial and performance reports to the Commonwealth on the IESIP were in compliance with the agreed reporting criteria, except for the provision of an audit opinion as per Clause 8.2 of the Agreement. The Department understands that an audit opinion was required only for the 2000 calendar year, and advised that an appropriate Commonwealth Government representative has orally advised that an audit opinion is not required for this half year period, despite the inclusion of the requirement in the Agreement.

The Agreement for the six months to June 2000 required that money paid by the Commonwealth under the Agreement shall not be spent on activities which were not related to achieving the listed performance targets, and that the Northern Territory had agreed not to use IESIP funds for the provision of education to Indigenous students that would normally be provided from other sources.

While the activities comprising the IESIP program for the six month period to 30 June 2000 appear to be broadly consistent with IESIP requirements, the audit was unable to establish whether the Department complied with the above restrictions concerning the use of funds. Documentation should more adequately evidence that these important requirements of the IESIP Agreement are met. If documentation does not provide a sufficient audit trail, the audit opinion covering the IESIP funding during the year ended 31 December 2000 may be unable to confirm that all funding conditions have been complied with.

Documentation sighted in the audit indicates that performance measurement for Indigenous education is a difficult and evolving process, and involves the coordination of the efforts of many parties in Federal, State and Territory Governments, as well as community consultative groups.
Auditing the Public Account and other accounts  
Indigenous Education Strategic Initiatives Program

The Department’s progress in addressing and implementing recommendations arising from the 1999 IESIP internal review included:

♦ reduction of the on-costs levy applied to projects from 46.5% on salaries to 10% on total grant;
♦ review of the programs in existence in 1999 resulted in some programs ceasing at the beginning of 2000, or being merged with the new initiatives;
♦ improvement in data collection for analysis of program performance and achievement of program outcomes;
♦ documentation of the intended outcomes for projects nominated for the 6 months to December 2000; and
♦ a strategic planning review of the Indigenous Education Branch, including an increase in the number of core funded positions in the Indigenous Education Branch structure.

The Department of Education has commented:

The first finding refers to the period from January to June 2000, and the Department notes the recommendations that IESIP initiatives be distinguished from its core activities and that each initiative be clearly articulated with regard to outcomes, objectives, budget and risks. The very nature of the IESIP funding is for supplementation, which implies a close linkage with core activities. Therefore, there are instances where it is not practical for IESIP funded activities to be reported as discrete outcomes.

On the second key finding, which refers to the period to the end of December 2000, it should be noted that since July 2000 the Department has had in place detailed and targeted plans for each initiative and more stringent audit trails. This should ensure that future audits will be able to confirm that all funding conditions have been complied with.

On the third key finding, you should be aware that the recommendations of the 1999 internal review have already been implemented and that significant changes have been made to Indigenous education services as a result of the Indigenous Education review (Learning Lessons), other Departmental reviews and restructures.

The Indigenous Education Branch has developed a five-year strategic plan and a range of project and program plans that are monitored.

While the Department agrees with the recommendation that the causes for not achieving targets be identified and addressed, it should be appreciated that Commonwealth requirements have been met as is indicated in the financial acquittal letter received from DETYA in January 2001. Remedial actions such as more rigorous planning and monitoring of programs and expanded data collection of performance information have been put in place. The Department will continue to examine current structures, risks and processes to identify areas for improvement.

The question of whether an audit report was required for the six months from January to June 2000 (Clause 8.2 of the Agreement) was dealt with over the phone and by email between officers of Financial Services and the Commonwealth, with confirmation that such a report was not needed.
Natural Disasters Relief Arrangements Acquittal

KEY FINDINGS
- $34.5 million of the $55.5 million incurred by the Northern Territory on Disaster Relief expenditures in the years 1996/97 to 1998/99 has been recovered from the Commonwealth under National Disaster Relief Arrangements.
- The Commonwealth Department of Finance and Administration has yet to confirm its final acceptance of the amount funded to the Northern Territory.
- If the 1996/97 and 1997/98 claims are treated separately, the Commonwealth assistance would be reduced by $1.26 million.

Background
Under the Commonwealth National Disaster Relief Arrangements (NDRA) the Northern Territory is able to claim reimbursement from the Commonwealth for eligible expenditure relating to natural disasters such as cyclones.

In the three years from 1996/97 to 1998/99 the following claims were made and audit opinions issued thereon:
- 1996/1997 - Cyclone Rachel
- 1998/1999 - Cyclone Rachel, Les and Thelma

Audit Findings
I issued qualified audit opinions on the acquittal statements for each of the three years in respect to the omission from the statements of the financial assistance calculation. The calculation was omitted as the Northern Territory was negotiating with the Commonwealth Department of Finance and Administration in respect of how the calculation should be interpreted.

Documentation supporting some of the original claims was found to be insufficient, and some claims made were removed due to ineligibility. Whilst it was recognised that the records maintained to support eligibility improved for the 1997/98 and 1998/99 claims, it was recommended that further improvement in the documentation trail be considered.
In total, $55.5 million was incurred by the Northern Territory on eligible Disaster Relief expenditures in the years 1996/97 to 1998/99. Commonwealth assistance due for this expenditure has been calculated by the Northern Territory at $34.5 million of which $2.5 million consisted of repayable loans. Loans are repayable to the Commonwealth in eight equal annual installments.

Although this amount has been fully funded by the Commonwealth, the Department of Finance and Administration has not yet confirmed its acceptance of the Northern Territory Government’s calculation. The Northern Territory claim has sought to combine the 1996/97 and 1997/98 claims as one claim which eliminates the 1996/97 base amount from the calculation of the Commonwealth contribution. If the 1996/97 and 1997/98 claims are treated separately the Commonwealth assistance will be reduced by $1.26 million.
Finalisation of matters arising from the sale of Ayers Rock Resort

KEY FINDING
♦ $2.4 million in cash, and $2.2 million in property plant and equipment of the former Yulara Town Council has been distributed for the benefit of the Yulara community.

Background

The Government’s ownership of the Ayers Rock Resort ceased in December 1997 with the sale of its remaining 60% share of the business. It retained the former ownership entity, the Ayers Rock Resort Corporation, which received the assets of the Yulara Town Council. The Council was dissolved by the Government at the time of the sale of the Resort.

Audit findings

The remaining assets of the former Council which were held by the Ayers Rock Resort Corporation were distributed on 15 September 2000 with the closure of the Corporation’s bank account.

In total, $2.4 million in cash, and Council property plant and equipment with a written down value of $2.2 million, were distributed for the benefit of the Yulara community. A summary of the distribution is included in the table on the following page.
### Auditing the Public Account and other accounts

#### Sale of Ayers Rock Resort

<table>
<thead>
<tr>
<th></th>
<th>97/98</th>
<th>98/99</th>
<th>99/00</th>
<th>00/01</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>$’000</td>
<td>$’000</td>
<td>$’000</td>
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<tr>
<td><strong>Received</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Cash</td>
<td>2,213</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>2,213</td>
</tr>
<tr>
<td>Council property plant and equipment at written down value</td>
<td>2,207</td>
<td>-</td>
<td>-</td>
<td>-</td>
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</tr>
<tr>
<td>Interest included in distribution</td>
<td>-</td>
<td>136</td>
<td>68</td>
<td>-</td>
<td>204</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>4,420</td>
<td>136</td>
<td>68</td>
<td>-</td>
<td>4,624</td>
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<tr>
<td><strong>Distributed as grants and donations</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Assets gifted for the benefit of the community</td>
<td>367</td>
<td>25</td>
<td>-</td>
<td>1,815</td>
<td>2,207</td>
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<tr>
<td>Donation to Royal Flying Doctor Service</td>
<td>48</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>48</td>
</tr>
<tr>
<td>Library grants</td>
<td>13</td>
<td>22</td>
<td>-</td>
<td>-</td>
<td>35</td>
</tr>
<tr>
<td>Communications upgrade</td>
<td>10</td>
<td>96</td>
<td>32</td>
<td>-</td>
<td>138</td>
</tr>
<tr>
<td>Recreation Hall extension</td>
<td>15</td>
<td>(15)</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Grants to Yulara Child Care Centre Inc</td>
<td>4</td>
<td>6</td>
<td>-</td>
<td>-</td>
<td>10</td>
</tr>
<tr>
<td>Grants to Community Resource Centre</td>
<td>2</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>2</td>
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<tr>
<td>Grant to Community Recreation and Leisure Association</td>
<td>20</td>
<td>6</td>
<td>-</td>
<td>-</td>
<td>26</td>
</tr>
<tr>
<td>Funding to construct swimming pool</td>
<td>-</td>
<td>650</td>
<td>215</td>
<td>-</td>
<td>865</td>
</tr>
<tr>
<td>Funding for Yulara Oval lighting</td>
<td>-</td>
<td>62</td>
<td>(62)</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Playground equipment</td>
<td>-</td>
<td>42</td>
<td>-</td>
<td>-</td>
<td>42</td>
</tr>
<tr>
<td>BMX bike track</td>
<td>-</td>
<td>-</td>
<td>3</td>
<td>-</td>
<td>3</td>
</tr>
<tr>
<td>Trust account to build Yulara Education Centre</td>
<td>-</td>
<td>-</td>
<td>1,250</td>
<td>-</td>
<td>1,250</td>
</tr>
<tr>
<td>Sundry savings from projects</td>
<td>-</td>
<td>-</td>
<td>(2)</td>
<td>-</td>
<td>(2)</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>479</td>
<td>909</td>
<td>1,421</td>
<td>1,815</td>
<td>4,624</td>
</tr>
</tbody>
</table>

Sundry income of $2,000, comprised of bank interest received from 1 July 2000 to closure of the bank account, was applied to the sundry operating expenses of the Corporation so that by 20 September 2000 the Corporation had no assets. Liabilities remaining consisted of accounting and auditing fees which are to be met by the Government.

The intention of Government now is to dissolve the Corporation by repealing the Ayers Rock Resort Corporation Act.

This completes the process commenced in 1992 when the Government accepted $274 million of debt from the Resort’s former operating structure, which it also then wholly owned, and transferred the ownership into the Ayers Rock Resort Corporation. The Government sold 40% of its ownership interest in 1993 for $24 million, and the remaining 60% in 1997 for $103.4 million. $100 million of the 1997 sales proceeds are earmarked for the Government’s contribution to the Alice Springs to Darwin Railway construction.
Auditing the Public Account and other accounts

Costs arising from BTEC litigation

KEY FINDINGS

♦ For a program costing approximately $237 million in the Northern Territory, of which the NT Government was required to fund around $80 million, BTEC litigation has to date cost the Government a further $6.9 million.

Background

The Brucellosis and Tuberculosis Eradication Campaign (BTEC) commenced in 1970 and was completed in 1998. The program was established to eradicate Brucellosis and Tuberculosis from cattle and buffalo in Northern Australia. Pursuant to an agreement dated 1 May 1984 the program became a joint operation between the Commonwealth and the Northern Territory.

The majority of the program and expenditure occurred in the Northern Territory in the years from 1982/83 to 1992/94, with a substantial expenditure in 1990/91 due to increased funding in response to a need which had been identified to accelerate the program, as illustrated in the following chart.

![BTEC Annual Expenditure - Northern Territory](chart.png)

In recognition of the transition from eradication to monitoring, a new agreement was signed on 24 May 1993 that applied through to 31 December 1997. However, there was a carry over of expenditure and the program was effectively completed on 30 June 1998.
Audit findings

Litigation costs have been incurred for legal fees in defending actions brought against the Government by pastoralists claiming additional financial losses in relation to the Government’s administration of the BTEC scheme, and for payments made to some of the plaintiffs in out of court settlements.

Although financial records were maintained by the Department of Primary Industry and Fisheries (DPIF), Northern Territory Attorney-General’s Department and Northern Territory Treasury on litigation costs paid by the respective agencies, no central record of these costs had been maintained.

Accordingly, there has been to date no accurate reporting of the total costs of Government arising from litigation against the NT Government for its administration of the BTEC scheme.

The exercise to identify the total BTEC litigation costs proved to be a difficult task with the information not readily available from the various Agencies concerned with the litigation. The use of Treasurers Advance, DPIF operating account and the Attorney-General’s Department trust account had fragmented the record keeping. With the first litigation costs arising in 1992/93, the time span hampered the ready access to supporting records.

The exercise has highlighted the need for the lead agency in a project, in this case the DPIF, to maintain a consolidated record of the project expenditure, including litigation, to ensure control over costs and accurate reporting. I understand that the ongoing litigation costs are now handled directly by DPIF.

Within the constraints of the records available, and with the assistance of the relevant agencies, the audit identified that for a program costing approximately $237 million in the NT, of which the Northern Territory Government was required to fund around $80 million, BTEC litigation has cost the NT to date a further $6.9 million. Of that, $4.3 million was paid in settlements to three plaintiffs with the balance of $2.6 million being the legal costs in defending the actions.

At the time of audit there were eight open litigation cases.

_The Department of Primary Industry and Fisheries has commented:_

_In relation to the eight "open" litigation cases, the Territory has been awarded costs on appeal in relation to one matter, the costs could be in the order of $1.5 million, although they are yet to be quantified._

_A second matter has been struck out with costs to be settled and in relation to a third matter, no Statement of Claim has been received after several years._
Matters arising from performance management system audits

<table>
<thead>
<tr>
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<th>Page/s</th>
</tr>
</thead>
<tbody>
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<td>Performance information in Agency Annual Reports for 1999/2000</td>
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<tr>
<td>Management of the Information Technology Outsourcing Policy</td>
<td>77-78</td>
</tr>
<tr>
<td>Northern Territory Police, Fire &amp; Emergency Services - How well does Information Technology meet business needs?</td>
<td>79-80</td>
</tr>
</tbody>
</table>
Matters arising from performance management system audits

Performance information in Agency Annual Reports for 1999/2000

KEY ISSUES

♦ Performance information in Annual Reports of Agencies is again generally unable to provide a comprehensive insight into the extent of their contribution to the achievement of Government policy outcomes.

♦ Financial information included in Annual Reports generally lacks integration with the performance reporting.

♦ The Government has announced its intention to develop a financial and performance management framework, focusing on outputs.

♦ During the development of this performance accountability framework, the Legislative Assembly could also discuss what level, if any, of independent audit assurance it requires over performance information provided to it by the Government.

Background

In my August 2000 Report to the Legislative Assembly, I outlined that generally Agencies were not comprehensively compiling and reporting information in their Annual Reports which addressed the extent of their achievement of the performance outcomes which had been listed in their budgets submitted to the Legislative Assembly. Instead, Agencies were reporting performance in terms of processes, tasks and outputs, but not clearly whether outcomes of Government’s public policy aspirations were being achieved.

These comments followed on from similar findings included in my February 2000 Report, in which I also identified that: “The format and content of Annual Reports is still largely at the discretion of Agencies, and this leads to wide variations in the quality of performance information presented. Unless all performance in Budget Papers is reliably reported upon, there is no safeguard against, for example, selective reporting of favourable performance only.”

For the Agencies and their policy or program responsibilities for which I conducted performance management system audits in 1999/2000, and on which I commented in my August 2000 Report, I reviewed the related performance information included in their 1999/2000 Annual Reports.
Matters arising from performance management system audits
Performance information in Agency Annual Reports for 1999/2000

Audit findings

Linking performance reporting to Budget Papers

As foreshadowed in my August 2000 Report, without having identified appropriate performance measures for policy outcomes, and without systems to monitor and report these measures, performance information in Annual Reports of Agencies is again generally unable to provide a comprehensive insight into the extent of their contribution to the achievement of Government policy outcomes.

A number of Annual Reports included in their performance information a narrative on the extent of their achievement of the outputs they had identified in Budget Papers. Some did not even provide that level of linkage.

Some Annual Reports did include reporting on some of the outcomes of Government policy for which they recognised responsibility for the implementation or monitoring of achievement. One good example of reporting on policy outcomes was Territory Health Services in its reporting of the status of the Aboriginal Health policy. Performance information provided in its Annual Report has been specifically expressed in the terms of the Aboriginal Health policy, which is the desire to narrow the gap between Aboriginal and non-Aboriginal health standards. However, the reporting was not able to be linked to outcomes and outputs identified in Budget Papers, because the Aboriginal health policy was not separately identified in the Agency’s Budget Papers.

Integrating financial reporting with performance information

Financial information included in Annual Reports generally lacks integration with the performance reporting.

Instances were noted where increases in funding to Agency programs was identified but this was not compared with increases in service demands, or whether the increased financial allocations to initiatives are better contributing to desired outcomes.

Narrative analysis and discussion of financial information is now regularly included by GBDs in the Annual Reports of their host Agency, and increasingly by general Government Agencies for their cash based financial reporting. These narratives are one suitable location to integrate the financial information provided with operational reporting. Reporting on program evaluations is another suitable mechanism for formally identifying and reporting such results.

The Government has announced its intention to develop a new financial and performance management framework, focused on outputs

In December 2000, the Government announced its “Working for Outcomes” proposals. These would see the introduction of accrual budgeting, accounting and reporting by Government entities in full operation for the 2002/03 year. This would enable Agencies to identify and cost their program outputs in their budgets, and to subsequently report actual costs and performance of outputs achieved.
Matters arising from performance management system audits  
Performance information in Agency Annual Reports for 1999/2000

The Government has announced its intention to develop a financial and performance management framework (continued)

The announcements did not indicate how reporting the extent of achievement of the Government’s public policy outcomes would feature in the proposals. The focus of the proposal seems limited to desired financial outcomes, particularly the desire to limit the growth in the net Government debt per capita, rather than broader public policy outcomes.

However, accountability for outcomes of publicly announced policies, which are pursued through the allocation and use of public funds, remains a primary responsibility of the Government in our system of parliamentary democracy.

The Government has already introduced a structure for performance accountability requirements for the major Local Government councils, the results and analysis of which was most recently reported by the Department of Local Government in the first edition of its publication “Northern Territory Local Government Performance.” In the Annual Report of the Department of Local Government, it highlighted that its use of the performance information has assisted it in focusing on issues and allocating resources when providing support to councils. This experience with performance management structures for Local Government should provide valuable background for the Government when it further develops the design of the performance management framework it will apply to itself.

During the development of this performance management and accountability framework, the Legislative Assembly could also discuss what level, if any, of independent audit assurance it requires over the output and outcome performance information to be provided to it by the Government.

I comment further on desirable features of performance management frameworks in the Topical Issues section of this Report.

Northern Territory Treasury has commented:

Performance information included in Agency annual reports is determined by Chief Executive Officers having regard to the most appropriate measure available.

This can include a range of qualitative and quantitative performance measures where they are available. Quantitative measures, reviewed annually are generally not appropriate for outcomes given their long term nature.

The performance information included in Budget Papers and Annual Reports will be reviewed as part of the Working for Outcomes project.
Matters arising from performance management system audits

Management of the Information Technology outsourcing policy

KEY FINDINGS

♦ Processes have been established to allow information technology and telecommunications outsourcing contracts to be effectively implemented and managed.

♦ However, opportunities exist to improve the management of existing contracts with reference to the established performance measurement procedures and service delivery standards.

Background

A major element of the Planning for Growth strategy announced by the Government in 1998 was the outsourcing of Information Technology and Telecommunications (IT&T) services. The Government established a policy to develop the information technology industry within the Territory, with the proviso that IT&T services were to be obtained by the Government with reasonable value for money.

The outsourcing of IT&T Services by the Department of Corporate and Information Services (DCIS) was initially subject to audit in 1999 to determine how well the Agency was managing the achievement of the government policy. My February 2000 Report summarised the results of the audit at that time.

I have continued to monitor the IT&T outsourcing arrangements and a follow up audit was conducted in the latter half of 2000. In this report I summarise the findings of the latest audit.

Audit findings

The outsourcing projects had progressed significantly since the previous audit.

♦ The electronic messaging and groupware (eMAG) contract had been in place for over a year.

♦ The Advanced Communications contract had commenced.

♦ Other IT Service tenders had been called for the Desktop/LAN Services, mainframe application support and non-mainframe application support.

This audit focused on the first two contracts. I intend to review the remaining contracts in 2001.
Matters arising from performance management system audits
Management of the Information Technology outsourcing policy

The audit concluded that the DCIS Contract Management Group had established processes to ensure that the outsourcing contracts were being effectively implemented and managed. Ongoing management of the existing IT&T contracts and project management of the Other IT Services tenders involved procedures to support the outsourcing objectives endorsed by Cabinet.

However, opportunities to improve the management of existing contracts with reference to performance measurement and service delivery standards were identified. In particular, there was no strategy in place to independently verify performance information provided by the vendors.

Performance management processes were in place for the Computer Support and Maintenance (CSM) e-mail (eMAG) contract, however, the processes needed to be extended to measure all Key Performance Indicators within the contract. Errors in message billing needed to be fully investigated.

At the time of the audit performance management processes had not been finalised for the Advanced Communications contract.

A number of independent reviews had been performed by nationally recognised industry consultants, to assess the delivery of communications infrastructure and the cost effectiveness of the Advanced Communications contract. These independent reviews and discussions with contract managers indicated that many of the outsourcing objectives had been achieved, although a formal review had not been conducted for the existing contracts to assess the overall success in meeting the outsourcing objectives.

The eMAG and the Advanced Communications contracts provide the Government with the power to regularly assess the cost of services being provided against industry statistics. A benchmarking review performed on the Advanced Communications contract has supported the cost effectiveness of the Advanced Communications Services, however, a similar review had not been performed for the eMAG services due to difficulties in identifying a consultant with appropriate benchmarking information.

In March 2000, consultants Bentley MRI were engaged to perform an independent assessment of the IT&T costs within each Agency and the whole of government. In addition, DCIS performed an analysis of transactions recorded in the Government Accounting System to identify existing IT&T expenditure for each Agency. These cost estimations were being presented to Agencies for final comment at the time of the audit. They should be available when assessing future IT outsourcing tenders.

The Department of Corporate and Information Services has commented:

An internal audit was commissioned to review message billing and made a number of recommendations to improve the system which will now be taken up with the service provider and agencies. The audit noted "no instances of overcharging relating to eMAG email message billing".

As discussed with the Auditor-General, it was too early in the life of the existing contracts to assess overall success in meeting outsourcing objectives, but it was agreed a process would be put in place for the future.
Northern Territory Police, Fire and Emergency Services - How well does IT fit the agency’s business needs?

**KEY FINDING**
- The Agency has made significant progress in the replacement of aging applications with new operational applications to meet the business needs.

**Background**

I last reviewed the IT strategy of the Agency in 1996/97 and reported the results of the audit in my August 1997 Report to the Legislative Assembly.

In the earlier audit I identified that the Agency faced the risk that its IT Strategic Plan initiatives would not proceed due to insufficient funding. As well, the impact to the existing systems of the then impending Y2K problem needed to be addressed by the Agency.

From 1998, my IT audits at the Agency have been concerned with the Agency’s readiness for Y2K. The results of these audits have been included in my Reports to the Legislative Assembly over the last few years.

Now that the Y2K risk has passed and the Agency has established a number of new IT systems and applications, it was opportune to revisit how well the new applications were supporting the business needs of the Agency.

**Audit findings**

Since my earlier reports the Agency has implemented the:
- Police Real Time Online Management Investigation System (PROMIS); and
- Integraph Computer Aided Dispatch (I-CAD); as part of
- Single Point of Entry And Retrieval (SPEAR) project; and
- the NT Fire Service’s automated alarm monitoring system (NTFAST).

I concluded that the Agency has clearly documented the integration and management of its IT facilities with its business needs for communication. Its strategic direction was outlined in a presentation titled “SPEAR project and Communications Strategy”.

Project justifications for new applications had also been documented as part of the Cabinet submission process.
Matters arising from performance management system audits
Northern Territory Police, Fire and Emergency Services - How well does IT fit the agency’s business needs?

However, the approach to Information Technology strategic planning was identified as inconsistent throughout the Agency. An Agency wide IT Strategic Plan, covering future requirements and focussing on the need to consolidate and enhance the new applications, was recommended.

Post implementation reviews for these projects although planned, had not been completed at the time of the audit.
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<thead>
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<tr>
<td>Financial and performance management frameworks</td>
<td>82-86</td>
</tr>
</tbody>
</table>
Topical Issues

Financial and performance management frameworks

KEY ISSUES

♦ Financial and performance management systems of a Government should deliver information which allows the Parliament and the public to understand how the Government has used public funds to achieve policy outcomes

♦ A clear understanding of the intended performance outcomes for Government policies is an essential component for the design of policy delivery strategies, and for the design of systems to measure and report achievements.

Background

Arising from my mandate, under the 1995 Audit Act of the Northern Territory, to conduct audits of performance management systems, I have been commenting regularly in my Reports to the Legislative Assembly about what elements should be evident in a well designed performance management system.

In my August 2000 Report, I highlighted that performance reporting by Governments should be expected to provide information about the extent of achievement of the Government’s public policy aspirations which were being allocated public funding. In my Reports in February and August 2000, I highlighted that performance reporting by the Northern Territory Government, through Agency Annual Reports, was generally focused on processes, tasks, and outputs, not on the achievement of policy outcomes.

“Working for Outcomes”

Previously there has not been a description from the Northern Territory Government about what it expects in Agency performance management systems. However, in December 2000, the Government announced a financial and performance management framework in its “Working for Outcomes” project.

This announced the decision of the Government to convert to accrual budgeting, accounting and reporting with effect from 2002/03. It will require action by the Government in this financial year to commence converting budgeting and accounting systems, and defining Agency performance expectations in measurable ways.

The measurement focus defined for Agencies is outputs, and it seeks to have Agencies provide budgeted costs for their major outputs. These are then to be compared with the subsequent measures of actual costs for management use, and for the external reporting of performance accountability.
Financial and performance management frameworks

Outputs are tasks or products which contribute towards outcomes. For example, in the Government’s media release on 15 December 2000 about the project, it used the examples of the cost per patient bed day, and average cost per Government primary school student, as the type of information which can be produced, and used for management and public accountability purposes.

However, that type of information does not reveal whether related policy outcomes, such as narrowing the gap between Aboriginal and non-Aboriginal health standards, or achieving the desired level of educational standards, are being achieved. How to report whether such outcomes are being achieved is yet to be detailed in the “Working for Outcomes” project. Currently, the “outcomes” targeted appear to be more the financial outcomes of limiting the growth of net Government debt per capita in the Northern Territory.

Linking to “Foundations for our Future”

The costing information in the examples noted above from the Government’s media release also does not contribute to the type of outcomes included in the Government’s Foundation for our Future vision statements, which it first announced in June 1999. (http://www.foundations.nt.gov.au)

For example, in the Foundation for our Future “Working Together” document, the Chief Minister identifies under the “Lifestyles” Foundation, that “Territorians will enjoy good health, respect as individual, and opportunities to grow and develop as valued members of our community”. This vision links to both the health and education services delivered by Government, but understanding the extent of the achievements requires measures of whether Territorians are, or see themselves as, healthy and well educated.

Triple bottom line reporting

Designing a new financial and reporting framework allows the Government to consider whether it wishes to structure its performance impacts in terms of the triple bottom line of social, environmental and financial. I outlined in my February 2000 Report to the Legislative Assembly how this was being used in some corporate and government entities as a means of recognising and reporting about the wider relationships and responsibilities they had with society.

At the core of Triple Bottom Line reporting is the recognition of the need for sustainable development practices, so that resources needed for future generations are protected or replenished. The Government has expressed its recognition of sustainable development in outcome statements of Agencies responsible for management of natural resources, although not with specifically identifiable and measurable outcomes.
Topical Issues
Financial and performance management frameworks

The Government has also recognised sustainable development and triple bottom line themes in its “Foundations for our Future” vision statements. For example, in the “Working Together” document, the Chief Minister identified “While our economic prosperity is important to us all, my Government also continues to protect those elements which make the Territory special – our pristine wilderness, strong sense of community, urban areas designed for people, clean environment and access to a wide range of leisure activities”. How these potentially competing needs are balanced is the focus of triple bottom line reporting.

Other frameworks do focus on outcomes reporting


The Government of Tasmania in its “Tasmania Together” initiative, (http://www.tastogether.asn.au) has also been conducting extensive community consultations throughout 2000, leading to the design of Government performance expectations and outcomes measures, following closely the Alberta Government’s model. These frameworks adopt triple bottom line classifications such as “people”, “prosperity” and “preservation” as a focus for performance goals and measurements.

Consultation in the development of new systems and expectations is needed

While community consultation occurred in the Northern Territory in July to September 1999, during the preparation of the more detailed statements issued for each of the six Foundations for our Future, performance expectations were not captured in a measurable way as has occurred in Alberta, and New South Wales, and is now occurring in Tasmania.

There is a risk that unless this is done, the “Working for Outcomes” project will not provide clear measures of performance about how the Government’s Foundations for our Future is being achieved. Following from the Tasmanian example, there is an opportunity now for the Government to consult with Territorians on what they see as performance expectations from the Foundations statements, and indeed any issues which they may see as not adequately addressed in the Foundations documents.

There is also a need to consult with Northern Territory Government Agencies about how they can influence the Government’s policy outcomes with outputs of their Agency, and for which they will now be accountable for the costs. While extensive communication with Agencies is in the strategy plan for “Working with Outcomes”, for Agencies to commit to the changes, they will need to understand how the proposed budgeting, accounting and reporting will assist their business needs and responsibilities.
Annual Reporting is a key to providing transparency in the performance management framework

In this Report, and in my Reports of February and August 2000, I highlighted that there is inconsistency in how performance information is included by Agencies in their Annual Reports. In particular, there has been no consistent recognition of the need to report performance in terms of the outcomes and outputs included to date in the Agency’s Budget information which is provided to the Legislative Assembly, in return for funding approval. In Australia, most jurisdictions have recently addressed or are now addressing their expectations for performance information in Annual Reports.

Under the “Working for Outcomes” project, there is an expectation that performance information will show the cost, timeliness and quality of outputs in Agency Annual Reports for comparison with Budget expectations, and for proper transparency, explanations should be provided for why variations occurred.

How outcomes and their achievement are to be defined and reported is yet to be identified in the project, but at a minimum a report on the level of actual achievement of outcome expectations shown in Budget Papers, which are then clearly defined in measurable terms, should be available annually to the Legislative Assembly.

In this regard, Anthony Mason, former Chief Justice of the High Court of Australia, observed that “until the political process trusts the people with information, it is unlikely that the people will trust the political process”. (Canberra Bulletin of Public Administration June 2000 p 92)

Conclusion

The Northern Territory, through the “Working for Outcomes” project has a timely opportunity to build systems which deliver relevant information about its performance, and in so doing, build and preserve public trust in its use of public funds.

Allied to this is the opportunity to improve financial and performance management practices within the ranks of the Northern Territory’s professional public administrators.

Experience in other jurisdictions has shown that both of these outcomes will require consultation with citizens, and public administrators, so that information provided is considered to be useful and reliable.

*Northern Territory Treasury has commented:*

*The Working for Outcomes project will enhance existing resource allocation processes. The focus will be on the identification of outputs and their link to outcomes.*

*Outcomes are high level objectives or goals included in broad policy directions. Foundations for our Future sets out a range of outcomes which encompass many areas of government services. Outcomes have a medium to long term focus and thus are difficult to measure in a quantitative sense, year on year.*
Topical Issues
Financial and performance management frameworks

*Northern Territory Treasury has commented (continued):*

*Outputs are the services that Agencies deliver to the Territory community.*

*Performance measures relating to the quality, quantity, timeliness and cost of outputs facilitate assessments of Government services. Such measures are not appropriate for assessment of outcomes which require broader consideration including those matters which are outside of government's control.*
## Status of other matters previously reported

| Firearms Buy-Back Scheme | 88 |

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Status of other matters previously reported

NT Police Fire and Emergency Services / Department of Industries and Business

Firearms Buy-Back Scheme

**KEY FINDINGS**

- By 30 June 2000 compensation payments for loss of business totaling $641,553 were paid to 18 licensed firearms dealers.
- All claims have now been finalised.

In my February 2000 Report I provided details of the expenditure by the Northern Territory government in the conduct of the largely Commonwealth funded firearms buy-back scheme initiated in 1997. Other than compensation payments to firearms dealers for loss of business, the expenditure required under the scheme was completed by 30 June 1998, with payments totaling $5.25 million, of which the Northern Territory directly contributed $215,000.

Loss of business compensation claims were finalised during the year ended 30 June 2000 with a further four dealers paid compensation totaling $299,659 and one dealer withdrawing his claim.

Compensation payments under the Scheme for loss of business totaled $641,553. This has been paid to a total of 18 licensed firearms dealers.

This completes the administration of the firearms buy-back scheme in the Northern Territory.
### Appendix 1 - Audit opinion reports issued since 30 June 2000

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<th>Date of Audit Report Year ended 30 June 1999</th>
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<td>Nitmiluk (Katherine Gorge) National Park Board</td>
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<td>Surveyors Board of the NT</td>
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<td>Northern Territory Government Conditions of Service Trust</td>
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<td>Northern Territory Police Supplementary Benefits Scheme</td>
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<td><strong>Agency Financial Statements at the request of the Agency</strong></td>
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<td>Interstate Road Transport</td>
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<td>Local Government Financial Assistance</td>
<td>asap</td>
<td>4 December 2000</td>
<td>12 October 99</td>
</tr>
<tr>
<td>Road Safety (Black Spot) Program</td>
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<td>Iwupataka Water Supply Project</td>
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<tr>
<td>Imangara Power Supply Project</td>
<td>30 September 2000</td>
<td>30 September 2000</td>
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<td>National Disaster Relief Arrangements</td>
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<td>1998/99</td>
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<td>Vocational Education and Training Financial Data</td>
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Not yet finalised - as at 31 December 2000
Not yet tabled - as at 31 December 2000
N/A - Not applicable
ASAP - As soon as possible after the financial year end 30 June 2000
Appendix 2 - Status of Audits which were identified to be conducted in the August 2000 Report

In addition to the routine audits, primarily being end of financial year audits of Agencies and of financial statements, and follow-up of outstanding issues in previous audits, the following audits were identified in Appendix 3 of the August 2000 Report as being scheduled for the period.

Various Agencies


Department of Corporate and Information Services

Review of the managing of outsourcing of IT services

Department of Education

A compliance audit of the Indigenous Education Strategic Initiatives Program

Department of Transport and Works

An IT review of the MOVERS computer application. Satisfactory

Procurement in Alice Springs Satisfactory

Northern Territory Police, Fire and Emergency Services

How well does IT fit the agency’s needs? Refer pages 79 - 80
In addition to the routine audits, primarily compliance audits of selected agencies, interim audits of entities requiring financial statements opinions, and follow up of outstanding issues in previous audits, the following audits have been scheduled for the period.

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<tr>
<th>Department/Agency</th>
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| Department of Industries and Business | Financial assistance to Industry and equity investments  
Measuring achievement of outcomes: Work Health and Major Project Support Group |
| Department of Lands, Planning & Environment | Release of land for development |
| Northern Territory Treasury | Taxes, Fees and Fines  
Alice Springs Convention Centre |
| Selected Agencies | Adequacy of capital assets records for financial reporting by government  
How well does TRIM support business needs? |
| Department of Education | Schools: Our Focus  
Review of IT strategy, including implementation of IT in schools |
| Territory Housing | Housing 2003 |
| Department of Corporate & Information Services | Fringe Benefit Tax  
Achievement of Government Expectations (response to Winlaw report)  
IT Outsourcing (continuation of review) |
| Territory Health Services | Nurses Rostering System - Royal Darwin Hospital  
Assess the IT security, systems acquisition and development, Information Systems (IS) support and IS operations over the CARESYS application  
Capital Works - Alice Springs Hospital  
Delivery of Government Policy: Disability Services |
| Northern Territory Police, Fire & Emergency Services | Delivery of Government Policy: NTSafe |
## Appendix 3
Proposed Audit Activity in the six months to 30 June 2001

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<td>Northern Territory Correctional Services</td>
<td>Matching infrastructure development to agency needs</td>
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<tr>
<td>Department of Arts &amp; Museums</td>
<td>Alice Springs Cultural Precinct, including compliance audit of Araluen Centre</td>
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The requirements of the Audit Act in relation to auditing the Public Account are found in:

♦ Section 13, which requires the Auditor-General to audit the Public Account and other accounts, with regard to:
  - the character and effectiveness of internal control, and
  - professional standards and practices.

♦ Section 25, which requires the Auditor-General to issue a report to the Treasurer on the Treasurer’s Annual Financial Statement.

What is the Public Account?

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

a) the Consolidated Revenue Account, and
b) Operating accounts of agencies and Government Business Divisions

Audit of the Public Account

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

1. annual financial statement audits of entities defined to be within the Public Account, in particular Government Business Divisions, which have a requirement for such audits under the Financial Management Act;

2. an audit approach which the Northern Territory Auditor-General's Office terms the Agency Compliance Audit.

This links the existence of the required standards of internal control over the funds administered within the Public Account, to the responsibilities for compliance with required standards as defined for Accountable Officers.

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

3. specific topic audits of the adequacy of compliance with prescribed internal control procedures. These can be initiated as a result of Agency Compliance Audits, or pre-selected because of the materiality or inherent risk of the activity; and

4. reviews of the accounting processes used by selected agencies at the end of the financial year, to detect if any unusual or irregular processes were adopted at that time.
Appendix 4
The approach to auditing the Public Account and other accounts

Other accounts

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

Audit of the Treasurer's Annual Financial Statement

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

The audit report on the Statement is issued to the Treasurer. The Treasurer then tables the audited Statement to the Parliament, as a key component of the accountability of the Government to the Parliament.
Appendix 5
Overview of auditing performance management systems

Legislative Framework

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

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

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

Operational Framework

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

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

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

This Report, and further information about the Northern Territory Auditor-General’s Office is available on our Homepage at:


Further copies of the February 2001 Report are also available from the Northern Territory Auditor-General’s Office.

The next general Report by the Auditor-General to the Legislative Assembly is scheduled to be tabled in the August 2001 sittings.