

Western Australian Auditor General's Report



Control of Monies Held for Specific Purposes



Report 19: 2019-20
30 April 2020

Office of the Auditor General Western Australia

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The Office of the Auditor General acknowledges the traditional custodians throughout Western Australia and their continuing connection to the land, waters and community. We pay our respects to all members of the Aboriginal communities and their cultures, and to Elders both past and present.

WESTERN AUSTRALIAN AUDITOR GENERAL'S REPORT

Control of Monies Held for Specific Purposes

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April 2020



**THE PRESIDENT
LEGISLATIVE COUNCIL**

**THE SPEAKER
LEGISLATIVE ASSEMBLY**

CONTROL OF MONIES HELD FOR SPECIFIC PURPOSES

This report has been prepared for submission to Parliament under the provisions of section 25 of the *Auditor General Act 2006*.

The report summarises the results of my Office's focus area audit in the State government sector, which assessed whether 8 entities have effective controls of monies held for specific purposes.

Focus area audits have a limited scope, and normally focus on specific areas of financial controls. We conducted this audit at a sample of entities, to identify any financial management vulnerabilities as well as to provide an insight to good practice, so all agencies holding specific purpose monies, including those not audited, can consider their own performance.

As some entities are likely to hold and distribute funds for the social and economic recovery from the COVID-19 public health situation, I trust this report, and particularly the better practice principles in the Appendix, will provide them with useful guidance for managing those funds.

I wish to acknowledge the entities' staff for their cooperation with this report.

A handwritten signature in black ink, appearing to read 'Caroline Spencer'.

CAROLINE SPENCER
AUDITOR GENERAL
30 April 2020

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Executive summary

Background

State government entities are often required to hold monies used for specific purposes. These are held in special purpose accounts. Common examples are government and private sector grants, donations and funding specified by legislation. How these funds are to be used is usually specified through a legal instrument such as a contract or legislation. Effective management and processes are required to ensure that the funds are used for their intended purposes.

We previously performed this audit in 2013 and found that while restricted funds were being used for their intended purpose, policies, procedures, and accounting practices relating to their management could be improved.

Conclusion

We found entities generally had adequate controls in place to support the control of monies held for specific purposes. Our testing did however identify a few instances of payroll costs incorrectly funded from specific purpose accounts. There is also a need to improve reconciliation of special purpose accounts and recordkeeping. Further, policies and procedures to assist in the control of these monies require improvement at 6 of the 8 entities.

What we did

The focus of this audit was to determine if entities are properly managing their funds held for specific purposes and in particular, if these restricted funds are being used for their intended purpose.

We assessed the policies, procedures, practices and transactions at 8 entities, of varying size and location, using the following criteria:

- Are sound policies and documented procedures in place for managing the funds?
- Was expenditure in accordance with the intended purpose?

The audit examined whether controls were in place to support effective management of funds, and whether adequate records were maintained to ensure that funds were being used for their intended purpose.

Detailed findings have been reported to the individual entities as part of this audit. The audit committees of these entities should follow up to ensure audit findings and recommendations are appropriately addressed by management in a timely manner.

We tested a sample of 787 payment transactions totalling \$2.4 billion, out of expenditure totalling \$4.5 billion from 56 specific purpose accounts. The audit covered the period from 1 July 2018 to 30 April 2019.

We conducted this audit under section 18 of the *Auditor General Act 2006* and in accordance with Australian Auditing and Assurance Standards. The approximate cost of undertaking the audit and reporting is \$236,500.

Entities included in our audit

Focus area audits assess entities against common business practices to identify good practices, and control weaknesses and exposures so that all entities, including those not audited, can evaluate their own performance.

We selected a sample of 8 entities for this focus audit. When selecting the entities to be included, we considered the size of the entities and the nature of restricted monies to ensure we were covering a wide variety in our sample.

The following 8 entities were included in this audit:

Entities	Number of restricted fund accounts selected in our sample	Total expenditure of these accounts 1 July 2018 – 30 April 2019
Child and Adolescent Health Services	10	\$54.9 m
Department of Biodiversity, Conservation and Attractions	10	\$8.5 m
Department of Communities	4	\$24.8 m
Department of Jobs, Tourism, Science and Innovation	4	\$37.8 m
Department of the Premier and Cabinet	3	\$0.7 m
Department of Treasury	13	\$4,034.5 m
Mental Health Commission	1	\$223.5 m
Western Australia Police Force	10	\$89.9 m
Total	55	\$4,474.6 m

Source: OAG

Table 1: Entities included in our sample

What we found

Policies and procedures could be improved

The *Financial Management Act 2016* (FMA) and Treasurer's Instructions (TIs) specify requirements for the administration, accounting, and disclosure of special purpose accounts. Accounts are also supported by either a special purpose trust statement approved by the Treasurer, or an agreement or legislation which specifies conditions and restrictions, as well as administration, accounting and reporting requirements.

Within this complex framework, policies and procedures are of heightened importance to provide clarity to staff by summarising requirements in a single repository or reference, which is tailored for the entity's systems, processes and delegations. Comprehensive, overarching policies and procedures ultimately help to ensure that specific purpose monies are being identified, managed and reported appropriately – and, moreover, spent for the purpose intended. Policies and procedures are particularly important to manage the risk of mismanagement of special purpose funds where accounts are transferred between entities.

We noted that the level of detail in entity policies and procedures directly correlated with the number and complexity of specific purpose monies held. Overall, we identified instances where policies and procedures were lacking in detail or not present due to entities placing too much reliance on the FMA, TIs and supporting statements, agreements, and legislation to govern the management and use of specific purpose monies.

We found that 2 of the 8 entities had good policies and procedures. Two entities did not have any policies and procedures, while 4 had policies and procedures requiring improvement. Some of the documentation reviewed appeared to be outdated, for example, 1 entity's document did not reflect the impact of recent machinery of government changes.

Special purpose account reconciliations were not always performed regularly

Regular monitoring of account balances is essential for effective cash management and ensuring specific purpose monies are being used for their intended purpose. Receipts and payments should be verified on a regular basis, and closing balances should be checked against the cash position.

We found 1 entity did not prepare and review reconciling items in a timely manner as part of the bank reconciliation process, resulting in a temporary negative cash position of an account. At another entity, we could not evidence independent review of the reconciliation prepared for a special purpose account. Inadequate oversight of key reconciliations can result in financial reporting errors or fraud passing undetected.

Expenditure transactions were not always appropriately scrutinised and recordkeeping was sometimes inadequate

Regular independent scrutiny of expenditure is required to ensure that monies are spent appropriately and transactions allocated to an account are valid and appropriate.

For 1 entity we found insufficient recordkeeping of transactions allocated to a special purpose account. Invoices were raised by the entity in 2013-14 but were not paid over a number of years. When debtors requested further information, staff could not substantiate these debts due to inadequate records, and recently reversed the invoices by using credit notes. These debts should have been written off with appropriate senior management approval.

We also found weaknesses in key controls such as the checking of eligibility and approving the charging of payroll expenses against special purpose accounts. These included:

- For 1 entity there were insufficient controls to ensure accurate and appropriate allocation of employee expenditure to the special purpose account. We found an instance where an employee's time representing operational expenditure was being funded from the special purpose account. This resulted in funds being used for purposes other than the intended purpose of the special purpose account.
- Two errors in an employee's timesheet which resulted in an overpayment of the employee costs being inappropriately charged to the special purpose account.
- For the same entity, we also noted that for 2 special purpose accounts a number of accounting journal entries were not independently reviewed. These journal entries related to the transfer of employees between cost centres and allocation of payroll expenses.

Special purpose accounts with nil balances not reported

At 2 entities where special purpose accounts had a nil balance, this had not been reported in the financial statements.

TI 1103 requires disclosure of the purpose, the opening and closing cash balances and the total cash receipts and payments for special purpose accounts. This also applies to special purpose accounts with a nil balance.

Specific purpose monies were not always reported appropriately in the financial statements

TI 1103 requires specific purpose monies held by the entity for the benefit of the State to be recognised as restricted cash in the balance sheet, with a disclosure describing the nature of the restriction. Funds held by the entity on behalf of a beneficiary other than the State are considered to be private monies, and should not be recognised on the entity's balance sheet and should be disclosed in the notes to the financial statements.

We found 1 instance where an entity had recognised private monies held on behalf of a beneficiary as part of their restricted cash balance on the balance sheet. The total value of trust monies incorrectly recognised in the balance sheet in 2017-18 was \$34.1 million. Once identified by our audit, the entity was able to correct this error as part of their 2018-19 financial report.

We also noted that the same entity did not correctly disclose some specific purpose monies as restricted cash in their balance sheet. The funds, totalling \$17.8 million, were recognised as part of the general operating cash balance.

Recommendations

1. Public sector entities should have appropriate policies and procedures for managing monies held for specific purposes.
2. Policies and procedures should be reviewed on a regular basis and updated as appropriate to ensure they are current.
3. Entities should ensure payroll cost allocations are formally reviewed by relevant account managers. Cost allocations should be supported by sufficient and appropriate evidence such as:
 - a. time records
 - b. employment contract or job description form details
 - c. documentation such as project or human resource records to support employees allocated to the special purpose account, including where an employee transitions to or from the special purpose account.
 - d. entity framework for cost allocations
 - e. fund agreement details.
4. Entities should ensure all transactions allocated to special purpose accounts are supported by relevant and appropriate evidence and adequate records are maintained.
5. Special purpose accounts should be regularly reconciled and reported to those charged with governance.
6. Entities should review financial reporting disclosures annually against the requirements of the *Financial Management Manual 2006* and TIs to ensure accurate and complete reporting of restricted specific purpose monies and trust monies in the financial statements.

Response from entities

Entities in our sample generally accepted the recommendations and confirmed that, where relevant, they have amended policies and administrative systems, or will improve practices for managing special purpose accounts.

Appendix 1: Better practice principles

The following table shows the control principles on which our audit focused. They cover a number of sound practices and controls related to the management of specific purpose monies and are not intended as an exhaustive list.

Specific purpose monies	Focus area	What we expected to see
Policy and procedures	Identification and classification of funds	<ul style="list-style-type: none"> • An outline of how specific purpose monies and assets are identified, classified and accounted for in the financial system. • Requirements for establishing and closing accounts. • Documentation supporting the establishment, nature and categorisation of each account.
	Expenditure controls	<ul style="list-style-type: none"> • Controls established to ensure monies are appropriately spent and monitored. • Purpose of accounts are clearly defined to avoid potential misuse of monies.
	Recordkeeping	<ul style="list-style-type: none"> • Recordkeeping requirements are specified to ensure that adequate evidence is maintained to demonstrate that monies are spent in accordance with the intended purpose.
	Monitoring of fund balances	<ul style="list-style-type: none"> • Requirements for account receipts, payments and closing balances to be regularly reconciled and independently reviewed. • Regular reporting of account balances and reconciliations to those charged with governance. • An outline of how unspent and overspent accounts are to be dealt with.
	Roles and responsibilities	<ul style="list-style-type: none"> • Clearly defined roles and responsibilities for key processes.
	Compliance with policies and procedures	<ul style="list-style-type: none"> • Mechanisms in place to ensure policies and procedures are regularly and effectively communicated to staff. • Processes in place for non-compliance with policies and procedures.
	Relevant legislation	<ul style="list-style-type: none"> • References to appropriate sections in the <i>Financial Management Act 2006</i> and Treasurer's Instructions be included within entity policies and procedures.
	Review of policies and procedures	<ul style="list-style-type: none"> • Regular review of policies and procedures for adequacy and appropriateness.

Establishment of specific purpose monies	Authorisation	<ul style="list-style-type: none"> • Appropriate underlying records and authorisations have been obtained in line with the nature and categorisation of specific purpose monies. • The purpose of the monies is clearly articulated including the purposes for which expenditure may be used from these monies.
	Recordkeeping	<ul style="list-style-type: none"> • Adequate controls and processes are established to ensure that monies are received as appropriate and are accounted for correctly. • Debts requiring write off should follow the same processes and authorisations as applicable to all entity debt. • Adequate records should be maintained to evidence that terms and conditions applying to specific purpose monies has been complied with. • Clear guidelines on how monies are to be dealt with on closure of a specific purpose account.
Expenditure of specific purpose monies	Authorisation	<ul style="list-style-type: none"> • Expenses and cost allocation journals are independently, appropriately, and timely reviewed to ensure transactions are compliant with intended purposes.
	Recordkeeping	<ul style="list-style-type: none"> • Sufficient and appropriate evidence to support that the expense was compliant with the intended purpose. • Appropriate documentation or frameworks are in place to support cost allocations.
	Reconciliation	<ul style="list-style-type: none"> • Special purpose accounts should be regularly reconciled with reconciling items investigated and resolved in a timely manner.
	Reporting	<ul style="list-style-type: none"> • Special purpose accounts should be regularly reported to those charged with governance for their review and scrutiny. This should extend beyond an annual review that is performed at financial year end as part of financial statement reporting processes.
Financial Reporting	Disclosure	<ul style="list-style-type: none"> • Financial report disclosures are reviewed annually against the requirements of the <i>Financial Management Act 2006</i> and Treasurer's Instructions to ensure specific purpose monies are accurately and completely reported.

Source: OAG, based on the *Financial Management Act 2006* (Divisions 3 and 4) and Treasurer's Instructions (801, 802, 805, 806, 950, 1103)

Auditor General's reports

Report number	2019-20 reports	Date tabled
18	Information Systems Audit Report 2020 – State Government Entities	6 April 2020
17	Controls Over Purchasing Cards	27 March 2020
16	Audit Results Report – Annual 2018-19 Financial Audit of Local Government Entities	11 March 2020
15	Opinion on Ministerial Notification	28 February 2020
14	Opinion on Ministerial Notification	31 January 2020
13	Fee-setting by the Department of Primary Industries and Regional Development and Western Australia Police Force	4 December 2019
12	Audit Results Report – Annual 2018-19 Financial Audits of State Government Entities	14 November 2019
11	Opinion on Ministerial Notification	30 October 2019
10	Working with Children Checks – Follow-up	23 October 2019
9	An Analysis of the Department of Health's Data Relating to State-Managed Adult Mental Health Services from 2013 to 2017	9 October 2019
8	Opinions on Ministerial Notifications	8 October 2019
7	Opinion on Ministerial Notification	26 September 2019
6	Opinions on Ministerial Notifications	18 September 2019
5	Fraud Prevention in Local Government	15 August 2019
4	Access to State-Managed Adult Mental Health Services	14 August 2019
3	Delivering Western Australia's Ambulance Services – Follow-up Audit	31 July 2019
2	Opinion on Ministerial Notification	26 July 2019
1	Opinions on Ministerial Notifications	19 July 2019

**Office of the Auditor General
Western Australia**

7th Floor Albert Facey House
469 Wellington Street, Perth

Perth BC, PO Box 8489
PERTH WA 6849

T: 08 6557 7500
F: 08 6557 7600
E: info@audit.wa.gov.au
W: www.audit.wa.gov.au

 @OAG_WA

 Office of the Auditor General for
Western Australia