Tasmanian Audit Office

Accountability on Your Behalf

Government Departments and Public Bodies 2005-2006

EXECUTIVE SUMMARY

Report of the Auditor-General
Report No. 2

November 2006

THE ROLE OF THE AUDITOR-GENERAL

The roles and responsibilities of the Auditor-General, and therefore the Tasmanian Audit Office, are set out in the *Financial Management and Audit Act 1990.*

Our major responsibility is to conduct financial or 'attest' audits of State public sector agencies' annual financial reports. We also audit the Treasurer's Annual Financial Statements which report on financial transactions in the Public Account, and the consolidated whole of government financial report.

Audits of financial reports are designed to add credibility to assertions made by management in preparing their financial reports, enhancing their value to end users. Also, the existence of such audits provides a constant stimulus to agencies to ensure sound financial management.

In the main financial reports by agencies are prepared consistent with Accounting Standards and other mandatory professional requirements in Australia. On occasion reports are "special purpose financial reports" such as the Treasurer's Annual Financial Report. In all cases our audits are conducted in accordance with Australian Auditing Standards.

Following a financial audit, the Office issues a variety of reports to agencies and reports periodically to the Parliament. In combination these reports give opinions on the truth and fairness of financial reports, and comment on agencies compliance with certain laws, regulations and Government directives. They may comment on financial prudence, probity and waste, and recommend operational improvements.

We also conduct performance audits and compliance audits. Performance audits examine whether an agency is carrying out its activities effectively and doing so economically and efficiently and in compliance with relevant laws. Audits may cover all or part of an agency's operations, or consider particular issues across a number of agencies.

Compliance audits are aimed at ensuring compliance by agencies of directives, regulations and appropriate internal control procedures. Audits focus on selected systems (including information technology systems), account balances or projects.

Performance and compliance audits are reported separately and at different times of the year, with all financial audits included in one of the regular volumes of the Auditor-General's reports to the Parliament normally tabled in November each year. In doing so the Auditor-General is providing information to the Parliament to assist both Houses in their review of the performance of executive Government.

Management of agencies are provided with opportunity to comment on any matters reported. Where they choose to do so, their responses are detailed within the reports.

2006 (No. 13)

2006

PARLIAMENT OF TASMANIA

REPORT OF THE

AUDITOR-GENERAL

GOVERNMENT DEPARTMENTS

AND PUBLIC BODIES 2005-2006

Executive Summary

No. 2 of 2006

November 2006

Presented to both Houses of Parliament in accordance with the requirements of Section 57 of the Financial Management and Audit Act 1990

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Auditor-General's reports are available from the Tasmanian Audit Office, HOBART. This report and other recent reports published by the Office can be accessed via the Office's home page. For further information please contact:

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21 November 2006

President
Legislative Council
HOBART

Speaker
House of Assembly
HOBART

Dear Sirs

In accordance with the requirements of Section 57 of the *Financial Management and Audit Act 1990,* I have pleasure in presenting my Report on the audit of the Treasurer's Annual Financial Report (my audit report covers the Public Account Statements and the Budget Outcomes Statements only), Government Departments, Government Business Enterprises, State-Owned Corporations and other public bodies for the year ended 30 June 2006.

Yours sincerely

H M Blake

AUDITOR-GENERAL

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EXECUTIVE SUMMARY

1 INTRODUCTION

This Report deals with the outcomes from financial statement audits of the Public Account Statements, the Budget Outcomes Statements, Government Departments, State-Owned Corporations, Statutory Authorities, Government Business Enterprises and other public bodies together with special comments on various other issues. Local Government Authorities have not been included and will be dealt with in a separate report at a later date.

FORMAT OF THE REPORT

Unless specifically indicated, comments in this Report are current as at 31 October 2006.

The Report is based on the administrative arrangements set out under the provisions of the *Administrative Arrangements Act 1990* as at 30 June 2006 and has been prepared in accordance with the following classifications:

Executive Summary	Introduction;
	Guide to using this Report;
	Matters of Significance and Follow-Up of Matters Previously Reported;
	Treasurer's Annual Financial Report – Budget Outcomes Statements And Public Account Statements;
	Timeliness and Quality of Financial Statements;
	AIFRS Readiness and Impact; and
	Audits dispensed with.
Volume 1	Executive and Legislature;
	Ministerial Departments;
	Superannuation Funds; and
	Other Authorities.
Volume 2	Government Businesses;
	Government Business Enterprises; and
	State-Owned Corporations.

This classification does not attempt to recognise any lines of responsibility that some Statutory Authorities have through Ministerial Departments to the appropriate Minister, however the Portfolio or Responsible Minister is stated in each case.

In previous years this Report included a volume reporting on the outcomes of audits of Local Government Authorities. At the time of preparing this Report, these audits were not sufficiently advanced to enable inclusion. A stand-alone report dealing with Local Government Authorities will be prepared and tabled later.

FORMAT OF THE FINANCIAL ANALYSIS

Each entity's financial performance is analysed by discussing the Income Statement, Balance Sheet and Cash Flow Statement supplemented by financial analysis applying the indicators documented in the Financial Analysis section of this Report. The layout of some of these primary statements has been amended to, where appropriate:

- Make the statements more relevant to the nature of the entity's business; and
- Highlight the entity's net working capital, which is a useful measure of liquidity.

Previous Reports included financial results and commentary for the current financial year and the previous four years. This Report includes, for all entities, except Government Departments, details of amounts or balances at 30 June 2005 presented in accordance with Australian Generally Accepted Accounting Principles (AGAAP) and in accordance with Australian Equivalents to International Financial Reporting Standards (AIFRS), with commentary to explain the effects of the move to the new accounting standards. Such commentary has not been presented for Government Departments because of the limited extent of change. Further details of the impact of adopting AIFRS are discussed later in this Report.

The decision to exclude financial results for the previous three financial periods was made due to:

- In the case of all entities other than Government Departments, because the impact of the transition to new accounting standards made comparison with results reported under the previous standards applied in those years less relevant; and
- In the case of Government Departments, because of the decision to report their balance sheets based on a liquidity presentation rather than on a basis of current and non-current assets and liabilities.

For Departments that have disclosed budget amounts in their primary statements and where the variances from budget were explained, details and commentary have been included in this Report.

STATUS OF AUDITS

The majority of audits for the year ended 30 June 2006 have been completed with some exceptions as detailed in the preamble under each Volume of this Report. Outcomes from incomplete audits will be reported to Parliament in the first half of 2007.

AUDITS CONDUCTED FOR THE FIRST TIME

New audits completed this year were:

- Tasmanian Ports Corporation Pty Ltd;
- Tasmanian Ambulance Service Superannuation Scheme; and
- State Fire Commission Superannuation Scheme.

AUDITS DISPENSED WITH

Section 41 of the *Financial Management and Audit Act 1990* (FMAAor the Act) provides the Auditor-General with the discretion to dispense with certain audits. The section reads as follows:

41. Power of Auditor-General to dispense with audits of certain public bodies

(1) The Auditor-General may dispense with the audit of a particular public body or the audits of public bodies included in a class or category of public bodies if, in the opinion of the Auditor-General, there is sufficient cause to do so.

(2) The Auditor-General may exercise any of the powers and perform any of the duties of the Auditor-General under this Act in respect of the audit of a public body notwithstanding that the audit of that public body has been dispensed with pursuant to subsection (1).

I have interpreted this discretion as requiring that I exercise it annually and prior to 30 June each year. The reason for including this legislative requirement in this Report is to satisfy this requirement. In order to exercise this discretion, I need to ascertain which are the public bodies to which section 41 is referring. A public body is defined in the FMAA as follows:

"public body" means –

(a) A State authority; or

(b) A local authority; or

(c) The council, board, trust, trustees or other governing body (however designated) of, or for, a corporation, body of persons, institution, district or place, whose accounts are by law made subject to *Part 3*, to the *repealed Act* or to examination by the Auditor-General; or

(d) Any such council, board, trust, trustees or other governing body in receipt of a subsidy or grant-in-aid made by the Crown or a State authority –

and includes the corporation, if any, of which the public body is the governing body.

This is an extremely broad definition and captures, for example, the many entities that receive grant funding from the State Government.

Details of dispensed with audits are included in chapter 7.

FINANCIAL ANALYSIS

The following table illustrates the methods of calculating performance indicators used in the financial analysis sections of this Report, together with a number of benchmarks used to measure financial performance.

Financial Performance Indicator	Benchmark*	Method of Calculation
Financial Performance		
Result from operations ($'000s)		Operating Revenue less Operating Expenses
EBIT ($'000s)		Result from Ordinary Activities before Tax and before Gross Interest Expense
EBITDA ($'000s)		Result from Ordinary Activities before Tax, before Gross Interest Expense, Depreciation and Amortisation
Operating margin	>1.0	Operating Revenue divided by Operating Expenses
Return on assets		EBIT divided by Average Total Assets
Return on equity		Result from Ordinary Activities after Taxation divided by Average Total Equity
Return on investments	5.5%	Net Investment income divided by Average Investments
Financial Management		
Debt to equity		Debt divided by Total Equity
Debt to total assets		Debt divided by Total Assets
Interest cover – EBIT	>3	EBIT divided by Gross Interest Expense
Interest cover – Cash from operations	>3	Cash from Operations plus Gross Interest Expense divided by Gross Interest Expense
Current ratio	>1	Current Assets divided by Current Liabilities
Leverage ratio		Total Assets divided by Shareholders' Equity
Cost of debt	7.5%	Gross Interest Expense divided by Average Borrowings (include finance leases)
Debt service ratio		Borrowing costs plus Repaid borrowings divided by Operating revenue
Debt collection	30 days	Receivables divided by billable Revenue multiplied by 365
Creditor turnover	30 days	Payables divided by credit purchases multiplied by 365

Financial Performance Indicator	Benchmark*	Method of Calculation
Capital expenditure/ depreciation	100%	Payments for Property, plant and equipment divided by Depreciation expenses
Solvency ratio (relevant to the MAIB)		Net Assets less DTA less dividend payable divided by provision for outstanding claims
Returns to Government		
Dividends paid or payable ($'000s)		Dividends paid or payable that relate to the year subject to analysis
Dividend payout ratio	50%	Dividend divided by Result from Ordinary Activities after Tax
Dividend to equity ratio		Dividend paid or payable divided by Average Total Equity
Income tax paid or payable ($'000s)		Income Tax paid or payable that relates to the year subject to analysis
Effective tax rate	30%	Income Tax paid or payable divided by Result form Ordinary Activities before Tax
Total return to the State ($'000s)		Dividends plus Income Tax and Loan Guarantee fees
Total return to equity ratio		Total Return divided by Average Equity
Other information		
Staff numbers FTEs		Effective full time equivalents
Average staff costs ($'000s)		Total employee expenses (including capitalised employee costs) divided by Staff Numbers
Average annual and long service leave per FTE ($'000s)		Total employee annual and long service leave entitlements divided by Staff Numbers

** Benchmarks vary depending on the nature of the business being analysed. For the purposes of this Report, single generic benchmark have been applied where appropriate.*

An explanation of the performance indicators is provided below:

- Result from operations – summarises revenue transactions and expense transactions incurred in the same period of time and calculates the difference;
- Earnings before income tax (EBIT) – measures how well an entity can earn a profit, regardless of how it is financed (debt or equity) and before it has to meet external obligations such as income tax. This is a measure of how well it goes about its core business;

- Earnings before income tax, depreciation and amortisation (EBITDA) – measures how well an entity can generate funds without the effects of financing (debt or equity), depreciation and amortisation and before it has to meet external obligations such as income tax. This measure is of particular relevance in cases of entities with large amounts of non-current assets as the distortionary accounting and financing effects on the entity's earnings are removed, enabling comparisons to be made across different entities and sectors;
- Operating margin – this ratio serves as an overall measure of operating effectiveness;
- Return on assets – measures how efficiently management used assets to earn profit. If assets are used efficiently, they earn profit for the entity. The harder the assets work at generating revenues, and thus profit, the better the potential return for the owners;
- Return on equity – measures the return the entity has made for the shareholders on their investment;
- Return on investments – in the case of superannuation funds the measure indicates the return on funds invested on behalf of superannuants;
- Debt to equity – an indicator of the risk of the entity's capital structure in terms of the amount sourced from borrowings and the amount from Government;
- Debt to total assets – an indicator of the proportion of assets that are financed through borrowings;
- Interest cover – EBIT – an indicator of the ability to meet periodic interest payments from current profit (before interest expense). The level of interest cover gives a guide of how much room there is for interest payments to be maintained in the face of interest rate increases or reduced profitability.;
- Interest cover – Cash from operations – examines the exposure or risk in relation to debt – an indicator of the ability to meet periodic interest payments from funds from operations (before interest expense). The level of interest cover gives a guide of how much room there is for interest payments to be maintained in the face of interest rate increases or reduced funds from operations;
- Current ratio – current assets should exceed current liabilities by a 'considerable' margin. It is a measure of liquidity that shows an entity's ability to pay its short term debts;
- Leverage ratio – measures the proportion of equity funding in the asset base;
- Cost of debt – reflects the average interest rate applicable to debt;
- Debt service ratio – indicates the capacity of the entity to service debt by repaying principal as well as interest on borrowings;
- Debt collection – indicates how effectively the entity uses debt collection practices to ensure timely receipt of monies owed by its customers;
- Creditor turnover – indicates how extensively the entity utilises credit extended by suppliers;

- Capital exenditure/depreciation – indicates whether the entity is maintaining its physical capital by reinvesting in or renewing non-current assets;
- Solvency ratio – solvency is the ability of an insurance company to pay future claims. In order to remain solvent, insurance companies must always keep an adequate surplus of funds in case an unforseen increase in claims occurs;
- Dividends paid or payable – payment by the entity to its shareholders (whether paid or declared as a payable);
- Dividend payout ratio – the amount of dividends relative to the entity's net income;
- Dividend to equity – the relative size an entity's dividend payments to shareholders' equity. A low dividend to equity ratio may indicate that profits are being retained by the entity to fund capital expenditure;
- Income tax paid or payable – tax payments (paid or payable) by the entity to the State;
- Effective tax rate – is the actual rate of tax paid on profits;
- Total return to the State – is the funds paid to the Government consisting of income tax, dividends and guarantee fees;
- Total return to equity ratio – measures the Government's return on its investment in the entity;
- Staff numbers FTEs – as at the end of the reporting period the number of staff employed expressed as full-time equivalents (FTEs);
- Average staff costs – measures the average cost of employing staff in the entity for the year; and
- Average leave balances per FTE ($'000s) – indicates the extent of unused leave balances at balance date.

The above indicators are used because they are commonly applied to the evaluation of financial performance. Care should be taken in interpreting these measures, as by definition they are only indicators, and they should not be read in isolation.

The ratio showing Average leave balances per FTE has been included for the first time.

2 GUIDE TO USING THIS REPORT

This Report is prepared under Section 57 (1) of the *Financial Management* and *Audit Act 1990,* which requires the Auditor-General, on or before 31 December in each year to report to Parliament in writing on the audit of Government departments and public bodies in respect of the preceding financial year. The issue of more than one report now satisfies this requirement each year.

During the 2006 calendar year two reports were tabled:

- Report No. 1 of 2006 tabled on 22 June 2006 – this report dealt with June 2005 financial statement audits incomplete at the time of tabling the November 2005 report, financial statement audits with 31 December 2005 balance dates; and
- Report No. 2 of 2006 tabled on 21 November 2006 – which is this Report. It deals with those audits of financial statements of entities with a 30 June 2006 financial year-end completed on 31 October 2006. The outcomes from audits completed after this date will be reported in the first half of 2007.

This Report comprises three volumes:

- Executive Summary – which includes an analysis of the Budget Outcomes Statements and of the Public Account Statements;
- Volume 1 – Executive and Legislature, Ministerial Departments and Other Authorities; and
- Volume 2 – Government Businesses and State Owned Corporations.

In previous years a fourth document was included – Volume 3 – Local Government Authorities. Local government audits are still being completed and a separate Report dealing with audit outcomes will be finalised in the next few months.

Where relevant, Agencies and Entities are provided with the opportunity to comment on any of the matters reported. Where they choose to do so, Agency Responses are detailed within that particular section.

3 MATTERS OF SIGNIFICANCE AND FOLLOW-UP OF MATTERS PREVIOUSLY REPORTED

This Report contains analysis of financial information of Ministerial Departments, Government Businesses (including State-Owned Companies), Statutory Authorities and other public bodies. Comparative information is also provided for groups of similar entities such as energy entities.

The accompanying text summarises significant matters identified from our analysis of the financial statements. A cross reference to the relevant detailed report is provided. Not included are financial and reporting matters that are common across public sector entities, such as timeliness of reporting, because these are dealt with separately in this Executive Summary. In addition, not included are matters dealt with in the analysis of the Treasurer's Annual Financial Report.

The Report includes details of matters raised with entity management during the course of audits but only where the matter(s) raised was significant. The rationale for inclusion or otherwise rests on my perception of the public interest in each point and the need to confine comments to those matters that have more than a managerial dimension. Also included below are summaries of the more significant accounting changes impacting some entities.

A section is again included here following up matters reported in previous reports to Parliament. This section does not include Local Government entities, which will be subject to a separate report in early 2007.

MATTERS IDENTIFIED IN PREVIOUS REPORTS

National Trust of Australia (Tasmania) – Qualified audit opinion (30 June 2005 Financial Statements)

- **June 2006 Report No. 1, Page 221**

My audit report on the financial report of the National Trust of Australia (Tasmania) (the Trust) for 2004-05, continued to include a qualified audit opinion relating to:

- Its inclusion in revenue of amounts relating to proceeds from functions, fundraising activities, donations and admittance fees, totalling \$0.184m (2004, \$0.222m) over which it is not practicable to establish accounting controls prior to receipt of such funds due to the cash nature of that revenue. Accordingly, it was not practicable for my examination to extend beyond amounts recorded as having been received and as shown in the accounting records; and
- Failure by the Trust to comply with Australian Accounting Standards as they relate to depreciation of freehold buildings and leasehold improvements, the non-recognition of certain heritage collections and to determine and disclose current valuations for land and buildings measured on a cost basis.

In addition, my audit report drew attention to an inherent uncertainty as to whether the Trust is able to continue as a going concern.

The above matters have not been followed up in 2005-06 because the financial statements of the Trust for this financial year have not been received.

Aboriginal Land Council - Qualified audit opinion (30 June 2005 Financial Statements)

- **June 2006 Report No. 1, Pages 21 and 207**

The Council's financial statements for 2004-05 were qualified as a result of it failing to adopt the requirements of two Australian Accounting Standards in that:

- Additional lands vested in the Council during 2004-05 were not brought to account in its financial statements at 30 June 2005; and
- The Council's asset revaluations for land and building assets were not kept up to date to ensure that the carrying amount of each asset in the class does not differ materially from its fair value at the reporting date. The Valuer-General undertook the most recent revaluation of the Council's land and buildings at 30 June 1998.

It was noted that the Council contacted the Valuer-General's Office during the preparation of the 2004-05 statements with a view to having the valuation completed for inclusion in the 30 June 2005 statements, but the matter did not progress any further.

At that time the Council had taken steps to obtain a valuation, by 30 June 2006, for all controlled land and buildings, which should enable it to satisfy the requirements of Australian Accounting Standards.

I also reported that, under the provisions of the Council's enabling legislation, it must submit financial statements to the Auditor-General for audit by 31 August each year. This timeframe has not been met in recent years and the Council has been requested to provide financial statements by the legislative deadline in future.

The above matters have not been followed up in 2005-06 because the financial statements of the Council for this financial year have not been received.

Use of "emphasis of matter" paragraphs in audit reports Revaluations of non-current assets

- **November 2005 Report No. 2, Page 40**

Audits identified some entities adopting the fair value basis of accounting in relation to land, buildings and infrastructure assets whose valuations were regarded by me as being out of date. Increases in property valuations, building costs and costs to construct infrastructure such as roads and other local facilities in recent years have meant that valuations carried out as recently as two years ago may be out of date.

Attention to this fact was documented in audit reports at the following entities:

- The Office of the Governor;
- Department of Health and Human Services;
- Housing Tasmania;
- Inland Fisheries Service; and
- Southern Regional Cemetery Trust.

In each case I recommended that revaluations be brought up to date prior to 30 June 2006. In a number of other cases, particularly within local government, my Office, based on relevant indices, initiated late adjustments to the carrying values of infrastructure assets. Whilst these were acceptable short-term solutions, the entities concerned were also advised to update valuations of the assets concerned.

It is pleasing to note that in each case the entities have carried out revaluations or made appropriate adjustments in 2005-06 thereby avoiding the need for me to refer to such issues in this year's audit opinions.

Clyde Water Trust

- **June 2006 Report No.1, Page 212**

The Clyde Water Trust (the Trust) prepares special purpose financial reports (SPFR). During the 2004-05 audit cycle I completed two audits:

- Of the 2003-04 SPFR which was completed on a cash basis; and
- Of the 2004-05 SPFR which was completed on a modified accrual basis.

During 2003-04 the Trust experienced financial difficulty due to large expenditures on infrastructure development and the need to borrow funds. This led to the Rivers and Water Supply Commission being appointed as administrator of the irrigation scheme. The financial situation did not significantly change in 2004-05 and the Trust still did not have the cash to pay its creditors at 30 June 2005.

As noted in its financial statements, the Trust is dependent upon the Commission for its ongoing viability. My 2003-04 and 2004-05 audit reports drew attention to this reliance on the Commission.

In preparation for the 2005-06 audit, a number of recommendations were made to the Trust in order to improve its financial reporting disclosures and corporate governance practices including:

- Preparation of full accrual general purpose financial statements;
- Clear documentation of all liabilities;
- Disclosure of interest owing on advances;
- Depreciation to be included as an expense;
- Disclosure of income and expenditures earned/made on behalf of the Trust which are not recorded in the Trust's accounts; and
- Good corporate governance principles including a record of all decisions made.

Some progress had been made in respect to a business plan, which will eventually see the Trust's assets, liabilities and operations being passed to a new entity. It was understood that this new entity will assume responsibility for the River Clyde Irrigation district and that it would be set up in order to meet contemporary business standards and governance principles.

At the time of writing this Report the final audit of the financial statements for 2005-06 had not yet commenced. Whilst signed financial statements were forwarded to me on 17 July 2006, these statements were incomplete.

Matters arising from audits brought to the attention of management

- **June 2006 Report No.1, Page 57 - Department of Health and Human Services (DHHS) and Housing Tasmania**
- **November 2006 Report, Volume 1 (this Report)**

Recent reports have commented on internal control weaknesses and related matters at DHHS. I note that there has been an improvement in many areas previously reported including those relating to the use of the Tasmanian Government Card, although some control weaknesses were again identified and brought to the attention of management. Matters identified during the 2005-06 financial audit are noted in the separate DHHS chapter in Volume 1 of this Report.

Timeliness of Financial Reporting by Councils

- **June 2006 Report No. 1, Page 22**
- **November 2006 Report Executive Summary (this Report)**

The *Local Government Act 1993* requires Councils to provide financial statements to me as soon as practicable after 30 September each year. Satisfaction of this requirement facilitates the completion of annual reports and their tabling at annual general meetings to be held by 15 December each year.

I have interpreted the 30 September requirement as one where the financial statements submitted to me for audit must be complete in all respects, including certification by the General Manager. A number of Councils failed to meet this requirement in the 2004-05 financial reporting cycle. They were:

Council	Final Signed Financial Statements Received
Brighton Council	28 October 2005
Flinders Council	22 November 2005
Glamorgan-Spring Bay Council	23 November 2005
Kentish Council	11 November 2005
Sorell Council	25 November 2005
West Coast Council	5 December 2005

At that time, I wrote to these and all other Councils reminding them of their financial reporting obligations and advising that we would be seeking to address this as part of planning 2005-06 audits.

It is disappointing to note that the situation worsened considerably in 2005-06 as outlined in the Timeliness and Quality of Financial Statements section of this Report. While I acknowledge that the implementation of new accounting standards may have contributed to this in some degree, the new standards and dates for first time adoption have been known for a considerable time and with adequate planning should not have created such difficulties.

MATTERS IDENTIFIED DURING 2005-06 AUDITS

This section summarises significant matters highlighted for information as well as matters that I consider may require management attention. Matters dealt with are entity specific. Further details are provided in specific chapters for each entity.

Use of "emphasis of matter" paragraphs in audit reports

Department of Justice

- **November 2006 Report, Volume 1 (this Report)**

The Department's financial statements received an unqualified audit opinion in 2005-06. However, the audit report does include an emphasis of matter paragraph referring readers of the financial statements to the disclosure in the financial statements regarding the matter outlined below. It is essential that the Department develop systems enabling it to objectively determine the amount by which it impairs gross receivables for fines and penalties.

Administered Receivables primarily relates to outstanding fines and penalties. The net receivable balance comprises:

- Gross receivables of \$42.962m in 2005-06 (\$39.573m, 2004-05);
- Provision for impairment of \$25.569m in 2005-06 (\$23.555m); and
- Provision for expected remissions of \$2.387m in 2005-06 (\$2.387m).

The \$25.569m impairment provision has been recognised based on a set percentage (59.5%) of gross fines receivables. This percentage was determined in 1999 based on a level of financial analysis conducted at that time. The new accounting standard AASB 139 *Financial Instruments: Recognition and Measurement* requires receivables to be measured at amortised cost, and discounted to present value where relevant, and financial assets to be assessed for impairment on the basis of objective evidence. Due to the current restrictions of the fines receivable subsidiary ledger and its inability to provide appropriate data and reports to management, the Department is unable to obtain objective evidence to support the validity of the estimated impairment losses as determined by applying the 59.5% and the expected timing of cash flows from fines receivables as at 30 June 2006.

A new Fines Receivable System is currently being developed which is expected to assist the Department in obtaining appropriate objective evidence to support the impairment of fines receivables and expected timing of cash flows. This new system is expected will be completed and implemented in the 2007 financial year. Movements of 1%, 5% and 10% in the current 59.5% applied to calculate the provision for impairment losses would result in this provision changing by \$0.429m, \$2.148m and \$4.296m, respectively. This would directly impact Administered Income and Expenses and based on the current Administered fines infringement revenue of \$15.915m any such adjustment, should it be required, could be material to the financial statements.

OTHER MATTERS ARISING FROM 2005-06 AUDITS

Departments of Justice, Police and Emergency Management, Health and Human Services and Education – Increased Expenditures

- **November 2006 Report, Volume 1 (this Report)**

As noted in my comments on the Treasurer's Annual Financial Statements, total General Government Sector (GGS) expenditure increased by 10% (2005, 7.61%). A significant driver of this increase related to Employee expenses, which represent 46.68% (2004-05, 46.14%) of total expenditure and this cost increased by 11.32% or $164m in 2005-06.

While the overall increase in employee costs in 2005-06 of $164m is manageable in an environment of strong revenue growth and positive net operating results, as occurred in 2005-06, this is a cost that requires careful management particularly as it is increasing at a rate in excess of the rate of growth in revenues.

Increases in Employee costs were greatest in the Departments of Justice, Police and Emergency Management, Health and Human Services and Education as noted below. Please refer to respective Chapters in Volume 1 for more details.

Justice - increased employee expenses from $49.622m in 2004-05 to $62.787m in 2005-06 was due to significant pay rises for Custodial and Parole Officers under new agreements, $3.000m, and the administrative restructure of the Department, $3.000m. The FTEs increased from 740 to 808 (excluding the administrative restructure), which resulted in additional expenses of $4.000m primarily relating to prison employees.

Police and Emergency Management - employee costs rose by $10.886m due to 115 additional staff, an 8% pay rise for Police officers from December 2005 and a 3.5% pay rise for non-commissioned staff.

Health and Human Services - employee costs rose by $96.695m in 2005-06 or 17%. The increases were caused by award wage rises and recruitment of an additional 670 FTEs (or 8%). Employee leave provisions also increased as a result. Increases in FTEs, assuming an average salary rate of $63,000 contributed $42.210m to the higher employee costs.

Education - employee expenses increased by $38.320m in 2005-06, due to increases in staff numbers by 140, salaries for teachers of 6.41% and staff under the State Service Wage Agreement (SSWA) of 3.5%.

Department of Infrastructure, Energy and Resources (DIER)

- **November 2006 Report, Volume 1 (this Report)**

During the course of the audit, the Department was queried on the;

- Extended period of time (since 1996) it had used indices to update bridge asset valuations; and the
- Currency of its review of useful lives used to determine the annual depreciation expense.

AASB 116 *Property Plant and Equipment* requires the valuation of assets to be conducted with sufficient regularity so as to ensure the carrying amount equates to fair value. The use of indexation over an extended period is discouraged and, in order to ensure compliance with this accounting standard, full revaluations should be undertaken on a periodic basis.

In addition, AASB 116 also requires that the depreciation method applied shall be reviewed at least at the end of each annual reporting period.

DIER's management has responded to these observations in the DIER chapter of this Report.

In addition, a review of expenditure identified two payments that related to the 2006-07 financial year. The payments were:

- TOTE, $1.060m for 2006-07 Racing Industry Assistance (as per appropriation); and
- Marine and Safety Tasmania, $0.600m for 2006-07 CIP – Jetties (as per appropriation).

In accounting terms, the payments should not have been expensed, as they are a prepayment in nature. The financial statements were amended accordingly.

Department of Justice

- **November 2006 Report, Volume 1 (this Report)**

Prison Infrastructure Redevelopment Program (PIRP) – During 2005-06 the PIRP continued with expenditure totalling $47.712m. In addition, the Secure Mental Health facility at the Risdon Prison was transferred to the Department of Health and Human Services, $22.990m.

Expenditure of $47.712m on the PIRP in 2005-06 was funded by:

- ANZ bank loan, $32.083m;
- Capital appropriation, $15.495m; and
- Special capital investment funds, $0.134m.

It is anticipated that construction of the PIRP will be completed in late 2006. The final cost is expected to considerably exceed the original budget, $53.300m, due to:

- Amendments to approximately double the capacity of the Secure Mental Health Unit;
- Unforseen growth in the Building Activity Index;
- Provision of three additional medium security units and an additional workshop; and
- Capitalised interest costs.

Department of Tourism, Arts and the Environment – Tasmanian Museum and Art Gallery

- **November 2006 Report, Volume 1 (this Report)**

The Department recorded a net surplus of $344.612m in 2005-06, of which $343.729m was from the initial recognition of the Tasmanian Museum and Art Gallery (TMAG) collection. This resulted in an increase in Property, plant and equipment in 2005-06 of $379.801m, which also included the revaluation of land, buildings and infrastructure, $33.639m.

Retirement Benefits Fund Board

- **November 2006 Report, Volume 1 (this Report)**

The Retirement Benefits Fund Board (RBFB) is responsible for the management and administration of the Funds established under the *Retirement Benefits Act 1993*, *Retirement Benefits Regulations 1994*, the *Public Sector Superannuation Reform Act 1999*, and the *Retirement Benefits (Parliamentary Superannuation) Regulations 2002.*

The fully funded Tasmanian Accumulation Scheme (TAS) was established under the provisions of the *Public Sector Superannuation Reform Act 1999* and replaced the unfunded RBF non-contributory scheme on 25 April 2000. The Fund now has two Schemes (Contributory and Tasmanian Accumulation Scheme - TAS) and an Investment Account, each of which have separate financial statements and specific governing rules within the Regulations. The Contributory Scheme has been closed to new members since 15 May 1999.

During 2005-06 the *Tasmanian Ambulance Service Superannuation Scheme* and the *State Fire Commission Superannuation Scheme* were transferred to the RBF as sub-funds with the RBFB becoming the corporate Trustee of these sub-funds.

In total, at 30 June 2006 the RBFB had Net assets under management of $2.759bn (2005, $2.203bn).

RBFB is not responsible for managing the whole of Government unfunded liability. This liability is met on an emerging cost basis. The Contributory Scheme represents the largest portion of this unfunded liability.

Forestry Tasmania

- **November 2006 Report, Volume 2 (this Report)**

The 2005-06 financial year was a difficult one for Forestry Tasmania. Forest sales revenue decreased significantly primarily due to a decline in price and volume of wood products. This saw a reduction in gross sales of approximately $30.000m with most of the change relating to hardwood pulpwood. The main factors contributing to this outcome included the strong Australian dollar, which negatively affected export sales, increased freight costs and boycotting of Tasmanian wood products by some buyers. Contractor expenses and other associated costs, such as external plant hire and transport costs, declined as a result.

Despite the drop in sales revenue, Forestry Tasmania maintained a profit of around $18.000m before recording the impact of the movement in the net market value in the plantation forest and before the impact of the change in the unfunded superannuation liability. A significant contributor to this $18.000m profit was the revenue of $17.716m flowing from the Tasmanian Community Forest Agreement (TCFA). However, this $17.716m was largely matched by expenditure incurred under the TCFA on current year plantation establishment costs, future crop expenditure (primarily contractor costs) and on other operating expenditure including some payroll costs.

The $18.000m profit was also achieved due to an increase in other operating revenue in 2005-06 due mainly as a result of payments by Newood Holdings Pty Ltd to Forestry Tasmania for development fees for the Smithton and Huon Wood Centre sites. This was in part offset by higher depreciation expense due to increased capitalised expenditure on Forestry Tasmania's road network.

Tasmanian Community Forest Agreement – The TCFA was signed in May 2005 between the State and Federal Governments. To date $35.481m has been received by Forestry Tasmania with $17.716m earned so far and the balance of $17.765m carried forward to future years to match expenditure still to be incurred. This agreement is designed to enhance the productivity of the forest, improve timber value recovery and capitalise on tourism opportunities from the substantially enlarged conservation reserves.

The decrease in the value of the native forest of $25.135m was principally due to a reduction in wood flows arising from the TCFA. This reduction includes additional native forest being transferred into conservation reserves and restrictions on clear felling of old growth forests into the future. An increase in the discount rate from 8.89% to 9.12% also contributed to the reduction in value.

Hydro-Electric Corporation (Hydro Tasmania)

- **November 2006 Report, Volume 2 (this Report)**

When assessing Hydro's operating performance in 2005-06, it is noted that this financial year was the first full year of trading in the National Electricity Market (NEM), the commencement of physical operations of Basslink and the deconsolidation of the R40s group. These events, along with the introduction of AIFRS, make it difficult for year on year comparisons to be meaningful.

The introduction of AIFRS has seen the structure of the Balance Sheet significantly changed. However, Hydro continues to generate strong operating cash flows and profits before interest and tax. However, in my view, Hydro's liquidity and balance sheet position is tight and its challenge is to determine a sustainable level of expenditure to enable it to balance a reasonable return to Government, preservation of its assets and investment in growth opportunities while not increasing its borrowings to an unsustainable level.

The summary below highlights some of the major events that have transpired and the accounting treatments.

Basslink Project - on adoption of new Australian Accounting Standard AASB 139 *Financial Instruments: Recognition and Measurement* on 1 July 2005, Hydro recognised the fair value of the contractual rights and obligations of the Basslink contracts (Basslink Services Agreement and Basslink hedging arrangements) as a financial asset of $151.300m and financial liabilities of $895.300m. In addition, AASB 139 required Hydro to recognise the Gas Pipeline Capacity Agreement as a financial liability of $56.200m. It is emphasised that these financial instruments were recognised on 1 July 2005, not on 30 June 2005. The fair value of these financial assets and financial liabilities must be reassessed at the end of each year with any change being reported in the Income Statement. With respect to the Basslink financial instruments the net gain was $9.900m and for the gas pipeline capacity agreement there was an expense of $4.800m.

With the separate recognition of the Basslink financial instruments on 1 July 2005 there was a related increase of $748.300m in the carrying value of Property, plant and equipment. This resulted in additional depreciation expenses of $17.800m in the 2006 financial year.

It is noted that the Hydro Balance Sheet at 30 June 2005, prepared in accordance with AIFRS applicable at that date, recognised generating assets on a net basis (the Basslink and related obligations were netted against the carrying values of these assets) with the Basslink related financial instruments disclosed in the notes to the Hydro financial statements.

Bell Bay Power Pty Ltd (BBP) – BBP owns and operates the Bell Bay power station. Following commissioning of Basslink, the Bell Bay power station was no longer required by Hydro for drought relief backup. Under market structure proposals made by the State to the Australian Competition and Consumer Commission, it was expected that BBP would be separated either to a third party or as a separate State owned entity. Until the separation of the Bell Bay plant as a viable operation can be achieved, the Bell Bay plant is expected to be held by BBP in a standby state. At the date of this Report the plant had been operating intermittently since the end of the previous financial year. However, it remains the Hydro position that, in the long term, the station has little prospect of providing future economic benefit to the Corporation. This resulted in the Bell Bay power station asset being assessed as impaired and the carrying value of $22.435m written down to nil with an expense recorded in the financial statements.

Bell Bay Three Pty Ltd – this company was incorporated on 7 December 2005. It constructed three 38.75MVA gas turbine units during the 2005-06 financial year that have since been commissioned. The turbines were installed at a project cost of $52.409m.

Roaring 40s Renewable Energy Pty Ltd – on 17 October 2005, CLP Asia Renewable Projects Limited became an equal co-investor in R40s thus reducing Hydro's interest from 100% to 50%. At the time of deconsolidation, Hydro's investment in this former subsidiary was reclassified as an investment in a joint venture and revalued to 50% of the fair value of the total equity of R40s at that date. This revaluation resulted in a gain of $35.044m that has been included in revenue in the Income Statement. The transaction with CLP Asia resulted in Hydro also deconsolidating a number of other former subsidiary companies.

In addition to the $35.044m gain referred to above, the financial impact of the deconsolidation of R40s resulted in a number of changes to Hydro's consolidated balance sheet when compared to the financial position at 30 June 2005. The main changes were a reduction in Property, plant and equipment of approximately $128.900m and a decrease in Borrowings of approximately $90.000m.

Revaluation of generation assets - there was a material revaluation decrement, under AGAAP, of $523.033m in the fair value of Hydro's generating assets during 2004-05. This decrement is reported as an adjustment to the asset revaluation reserve. Under AIFRS this decrement is reported as an impairment of Property, plant and equipment in the Income Statement. The impairment under AIFRS was $542.269m.

Deferred Tax Liability - under AIFRS the deferred tax liabilities and tax assets are calculated on a different basis to that used under previous accounting standards. The impact of AIFRS at 30 June 2005 was an increase in the Deferred tax liabilities of $416.200m. At 30 June 2006 this net liability decreased by $24.657m primarily due to the bringing to account of the Basslink financial instruments and related balances.

Aurora Energy Pty Ltd

- **November 2006 Report, Volume 2 (this Report)**

In 2005-06 Aurora's Result from ordinary activities before taxation decreased by $10.197m or 24% to $32.076m. There are a number of factors that contribute to this and these are detailed in the Aurora chapter of this Report. In overview, however, it is noted that in the last 2 to 3 years Aurora had a substantial capital investment program to improve reliability and to prepare for entry into the NEM. This is reflected in depreciation expense increasing by $8.181m or 15% in 2005-06. Aurora also experienced increases in other inputs including copper and aluminium used in distribution lines, and energy and transmission costs which reflect increases approved by the independent electricity regulator. These have taken place in an environment where Aurora's revenues are capped by the independent regulator and can only be changed at specified intervals.

In addition, Aurora's cash position at 30 June 2006, $12.359m (2005, $56.634m) deteriorated due to:

- Its ongoing capital investment program and its investment in information technology, which totalled net $132.931m in 2005-06; and
- These investments were funded by new borrowings of only $24.529m with the remainder funded from existing cash reserves and from cash generated from operations.

Based on the 2005-06 results, Aurora will find it increasingly difficult to maintain similar levels of capital investment without resorting to higher levels of borrowings.

Aurora is trading in a more competitive environment at a time when its liquidity is tightening. Management will need to manage carefully the risks associated with this.

TT-Line Company Pty Ltd

- **November 2006 Report, Volume 2 (this Report)**

The Company's 2005-06 results reflect increased competition from budget airlines and a continued negative impact following the introduction of Spirit III and the Devonport to Sydney operation. With a view to improving the Company's financial position, the decision was made to sell Spirit III and the sale was finalised in September 2006. This resulted in the revaluation upwards of TT-Line's three ferries and:

- Inclusion on the Balance Sheet of an asset classified as an Asset Held for Sale rather than an item of Property, plant and equipment in the amount of $109.646m. Similarly, Current liabilities include $7.725m for costs incurred in relation to the sale of Spirit III but not yet paid; and
- Reversal of the impairments totalling $43.237m recognised at 30 June 2005.

Prior to these accounting adjustments, TT-Line incurred an operating loss for the year of $33.445m (2004-05 - $36.911m).

The Company's difficult financial position was acknowledged in its 30 June 2006 financial statements when a note was included reflecting its present reliance on the State

Government for financial support. During 2005-06 this support totalled $62.267m.

Tasmanian Ports Corporation Pty Ltd (Tas Ports)

- **November 2006 Report, Volume 2 (this Report)**

This was the first period of operations for TasPorts. Its financial statements report operating results for the six months ended 30 June 2006.

TasPorts has adopted a cost basis for recording non-current assets. Whilst the cost basis adopted meets the requirements of Australian Accounting Standard AASB 116 *Property Plant and Equipment*, I believe that, for long-lived assets, adoption of a fair value basis would provide a better indication of TasPorts' financial position and of the stewardship by it of these assets.

4 TREASURER’S ANNUAL FINANCIAL REPORT – BUDGET OUTCOMES STATEMENTS AND PUBLIC ACCOUNT STATEMENTS

INTRODUCTION

The Budget Outcomes Statements are a special purpose financial report prepared on an accrual Uniform Presentation Framework basis (UPF). These Statements comprise an Operating Statement, Balance Sheet, Cash Flow Statement and notes thereto for the General Government Sector (GGS). The Statements are a special purpose report because they have not been prepared in accordance with existing Australian Accounting Standards.

Explanations of the UPF basis for preparing the statements are provided in note 1 to these Statements and are not repeated here.

The Public Account Statements are a special purpose financial report prepared on a cash accounting basis. Explanations for applying this basis for preparing the Public Account Statements are provided in note 1 to these Statements and are not repeated here.

LEGISLATIVE REQUIREMENTS

The Treasurer and the Secretary of the Department of Treasury and Finance sign both of these Statements, which are chapters within the Treasurer’s Annual Financial Report (the TAFR).

The requirement for the TAFR to be prepared is spelt out in section 26A of the *Financial Management and Audit Act 1990,* which requires that:

1) As soon as practicable after the end of each financial year, the Treasurer is to prepare an annual report for that financial year.

2) The annual report is to contain for the financial year to which the report relates:

    a) The original estimates disclosed in the budget papers in respect of the major Government Finance Statistics statements; and

    b) The results in respect of the major Government Finance Statistics statements; and

    c) Statements reporting on the transactions within the Public Account during that financial year and the balances in the Public Account at the end of that financial year; and

    d) An explanation of any significant variations between the results for the financial year and the financial estimates and projections described in the budget papers; and

    e) The Auditor-General’s report on the results and statements referred to in *section 26B.*

3) The Treasurer may include in the annual report, in such form or manner as the Treasurer may determine, any other financial or statistical report.

The Budget Outcomes Statements satisfy the requirements specified in section 26A (2) (a) and (b) above and the Public Account Statements satisfy the requirements specified in section 26A (2) (c) above.

ACCOUNTING DEVELOPMENTS

A number of recent accounting developments will have major impacts on future financial reporting in the public sector. These flow from work currently underway by the Australian Accounting Standards Board (AASB) to:

- Harmonise the reporting requirements of the Australian Generally Accepted Accounting Principles (AGAAP) and the Government Finance Statistics (GFS) frameworks. In September 2006, the AASB issued a new accounting standard dealing with the reporting by governments of general government sector operations. This new accounting standard will be applicable for accounting periods beginning from 1 July 2008 although earlier adoption is allowable. This standard will require that governments prepare and issue the GGS financial report and the separate consolidated Whole of Government financial report (prepared under a different accounting standard) at the same time; and
- Review several current public sector-specific accounting standards with the view to their integration with other "sector neutral" standards and/or the creation of new public sector topic specific standards.

I will continue to monitor the development of accounting standards and their application in contributing to the enhancement of the overall quality of financial reporting by the State.

AUDIT OF THE 2005-06 BUDGET OUTCOME STATEMENTS AND PUBLIC ACCOUNT STATEMENTS

Section 26B, referred to in section 26A(2)(e) above, requires that the statements referred to in sections 26A(2)(b) and (c) must be submitted to the Auditor-General for audit before 30 September in each year. Signed Budget Outcomes Statements and signed Public Account Statements were submitted to me on 29 September 2006.

To enable the Treasurer to table audited Budget Outcomes Statements and audited Public Account Statements by no later than 31 October 2006, I must complete my audits of these statements prior to this date. Separate unqualified audit opinions were issued on 24 October 2006.

BUDGET OUTCOMES STATEMENTS

This analysis focuses on the Budget Outcomes Statements (referred to from now onwards as 'the Statements'). The format of the analysis is consistent with that applied to individual entities reported elsewhere in this Report. The analysis is limited to the last three financial years because preparation of the Statements in their current form commenced in the 2003-04 financial year.

The TAFR includes commentary explaining the 2005-06 financial results against prior years and budget. This analysis does not comment on performance against budget.

In preparing this analysis some material does not appear in the Statements and has been extracted from other chapters in this Report. Examples include full time equivalent staffing numbers for the last three years and details of grants paid.

Readers of this Report should note that the Statements comply partially with Australian equivalents to International Financial Reporting Standards (AIFRS) to the extent that they:

- Consolidate financial reports of agencies that have complied with AIFRS; and
- Include on the balance sheet the State's investment in the net assets of Government Business Enterprises and State-Owned Corporations (GBEs and SOCs) all of which have complied with AIFRS.

The implementation of AIFRS has significantly impacted the net assets of certain GBEs and SOCs, which has had a flow-on effect on the GGS balance sheet.

Comparative information in the Statements is reported on the basis of accounting standards developed under the former (AGAAP).

FINANCIAL RESULTS

OPERATING STATEMENT

	2005-06 $m	**2004-05 $m**	**2003-04 $m**
Revenue			
Grants and subsidies	2 215	2 115	1 997
Taxation revenue	703	686	631
Sales of goods and services	299	248	237
Interest income	33	43	33
Dividends and income taxes	188	190	181
Other revenue	134	96	134
Total Revenue	**3 572**	**3 378**	**3 213**
Expenditure			
Employee expenses	1 612	1 448	1 321
Other operating expenses	874	765	819
Grants and transfers	596	578	433
Depreciation	206	183	165
Nominal superannuation expense	137	115	112
Other interest payable	27	49	67
Total Expenditure	**3 453**	**3 138**	**2 916**
Net Operating Result	**120**	**240**	**296**
Less Net acquisition of non-financial assets:			
Purchase of non financial assets	(293)	(254)	(161)
Less Sale of non financial assets	50	42	69
Less Depreciation	206	183	165
Net acquisition of non financial assets	**(37)**	**(29)**	**73**
Fiscal Surplus (also referred to as Fiscal Balance)	**83**	**211**	**369**

Comment

Both the Net operating result and the Fiscal surplus are positive for each of the three years under review although these surpluses have been tracking downwards.

In its Preliminary Outcomes Report 2005-06 issued in August 2006 the Department of Treasury and Finance noted, at that time, the Fiscal Surplus was estimated would be $63m compared with the original Budget, which was for a deficit of $5m. The financial outcome compared to the original budget saw an improvement of $88m predominantly due to:

Revenue up by $168m reflecting increases in:

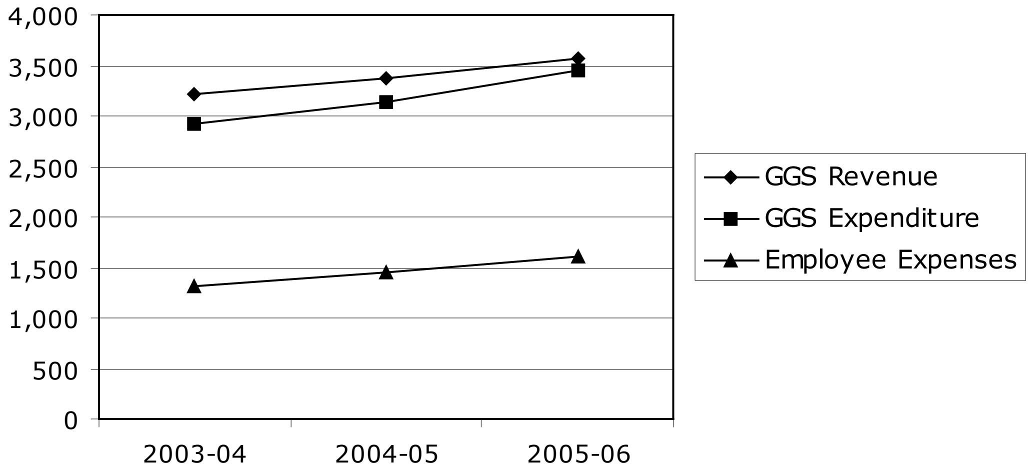
- Payroll and Land tax;
- Hospital inpatient fees;
- Mineral royalties; and
- One-off revenue receipts.

Offset partly by Expenses increasing by $78m reflecting increases in:

- Depreciation;
- Employee expenses; and
- Maintenance costs.

Figure 1 presents revenue, expenditure and employee cost trends for the GGS over the past three years. It indicates that the rate of expenditure growth from 2003-04 to 2005-06 (annual average of 8.82 per cent) has exceeded the rate of revenue growth (annual average of 7.22 per cent).

Figure 1: GGS Revenue and Expenditure ($Million)



Grants and subsidies revenues primarily comprise revenues from the Commonwealth in the form of GST, specific purpose grants and capital grants. In percentage terms the GST represents 42% of the State's revenues as illustrated below:

Revenues expressed as a percentage

	2005-06	2004-05	2003-04
GST (Commonwealth)	42	42	43
Specific purpose grants (Commonwealth)	12	13	12
Capital grants (Commonwealth)	1	1	1
Total revenue from the Commonwealth	**55**	**56**	**56**
Other grants and subsidies	6	6	6
Payroll tax	6	6	5
State taxes on property	7	8	8
Other State taxes	7	7	7
Sales of goods and services	8	7	7
Dividends and income taxes	5	6	6
Interest income	1	1	1
Other revenues	5	3	4
Total	**100**	**100**	**100**

In 2005-06 total State revenues increased by 5.74% or $194m with State taxes increasing by 2.48% ($17m) and Commonwealth grants by 4.73% ($100m). However, as can be seen from the summary, by percentages the sources of revenue have remained unchanged suggesting that Tasmania is no more or less reliant on the Commonwealth for funding.

Employee expenses in 2005-06 represent 46.68% (2004-05, 46.14%) of total expenditure and this cost increased by 11.32% or $164m in 2005-06. The increase from 46.14% to 46.68% equates to approximately $18.650m in additional costs as a percentage of total State recurrent expenditure.

The GGS is primarily comprised of Government Departments and their full time equivalent staffing levels at 30 June 2006 were 6.15% greater than the position at 30 June 2005 (10.04% greater than in 2003-04) as is evident from the table below. (Note that these are not the average staffing levels and impacts on costs should be viewed with caution.)

Government Departments	FTE at 30 June 2006	FTE at 30 June 2005	FTE at 30 June 2004
Economic Development	232	211	200
Education	8 151	8 010	7 799
Health and Human Services	8 685	8 015	7 251
Infrastructure, Energy and Resources	512	618	674
Justice	808	740	710
Police and Emergency Management	1 652	1 589	1 535
Premier and Cabinet	454	407	406
Primary Industries and Water	976	1 085	1 040
Tourism, Arts and the Environment	785	664	607
Treasury and Finance (excluding GPOC)	324	316	297
Total	**22 579**	**21 271**	**20 519**

In some cases, reasons for increases in staff numbers include transfer of staff from one department to another – for example staff were transferred into the Department of Tourism, Arts and the Environment from the Department of Primary Industries and Water, due to restructuring arrangements. Where material, reasons for other movements in staff numbers are explained within individual chapters for each agency within this Report. However, and again acknowledging that the staff numbers should be considered with caution, the total increase in employee expenses over the period 2003-04 to 2005-06, as it relates to these departments, can be attributed to:

- Additional staff numbers over the period June 2004 to June 2006 totalled 2,060 FTEs which, at an approximate annual average employee cost of $60 000 gives rise to new costs of $123.600m; and
- Salary increases in accordance with awards.

While the overall increase in employee costs in 2005-06 of $164m is manageable in an environment of strong revenue growth and positive net operating results, as occurred in 2005-06, this is a cost that requires careful management particularly as it is increasing at a rate in excess of the rate of growth in revenues.

Expenditure on grants and transfers increased by $145m or 33% in 2004-05. This primarily represented increases in:

- Current grant expenses by $98m to $446m;
- Expenditure on capital grants of $30m (2003-04, nil). This included $14.500m incurred in relation to the Tasmanian Community Forest Agreement; and
- Grants to Local Government Councils from $64m to $75m.

In contrast, Grants and transfers increased by only 3% ($18m) in 2005-06.

Depreciation expense increased by 12.5% in 2005-06 (2004-05, 10.91%), primarily due to investment in Property, plant and equipment and as a result of infrastructure and building upward revaluations.

Other operating expenses increased by 14.24% in 2005-06 due to a variety of reasons including higher building maintenance, minor equipment and supplies and consumables.

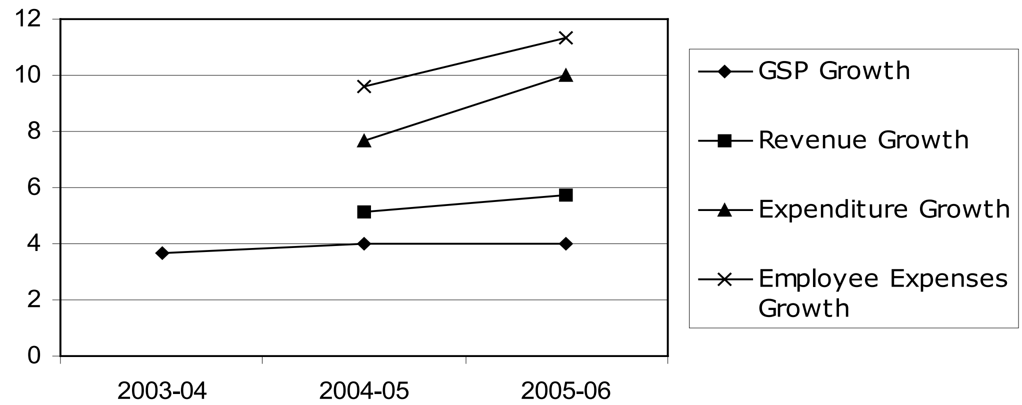
Nominal superannuation expense represents nominal interest on the unfunded superannuation liability. The basis of the calculation changed from July 2005, which resulted in changes to the discount rate as applied by the State Actuary. This had the effect of increasing this expense item in 2005-06 by 19% or $22m.

In total GGS expenditure increased by 10% (2005, 7.61%) and because revenue growth was lower at 5.74% (2005, 5.14%), the net operating result, declined by $120m (2005, $56m).

The investment in non-financial assets in 2005-06 was $39m (2005, $93m) higher, which contributed to the overall decline in the Fiscal Surplus of $128m. Expenditure on non-financial assets is commented upon in the Balance Sheet section of this chapter.

Figure 2 compares the growth in revenues, expenditures and employee expenses with the growth in the State economy – Gross State Product (GSP) over the past 3 years. Because preparation of the Statements in their current form commenced in the 2003-04 financial year, growth rates for revenues and expenditures are only measurable from 2004-05 onwards.

Figure 2: General Government Sector, Revenue and Expenditure Growth compared to GSP Growth (%)



Note: The growth rates in revenue and expenditure for 2003-04 to 2004-05 are based on AGAAP, while the growth rates for 2005-06 are based on AIFRS.

GSP data for financial years up to 2004-05 is sourced from the ABS, while the estimated GSP for 2005-06 is sourced from the Department of Treasury and Finance. GSP is defined equivalently to Gross Domestic Product (GDP) but refers to production at a state level. Therefore, GSP is the total market value of goods and services produced in Tasmania within a given period, after deducting the cost of goods and services used up in the process of production, but before deducting allowances for the consumption of fixed capital.

Figure 2 shows that both GGS revenue and GGS expenditure have been growing at a faster rate than the Tasmanian economy in 2005-06, revenue by 5.71% and expenditure by 10%. As previously mentioned the major contributors to increased 2005-06 expenditures were employee expenses, other operating expenses and nominal superannuation expense. The growth in employee expenses for the year was 11.32%, which has had a significant impact on the overall expenditure increase and as mentioned below is an area requiring careful management.

Factors which pose a degree of risk and that could have major impacts on the State's financial performance and condition include:

- The performance of the national economy, including decisions of the Commonwealth Government, which influence the level of Commonwealth grants to the State;
- The performance of the State economy and property markets, which influence state-sourced revenues;
- The performance of financial and equity markets, which influence the investment revenues and superannuation expenses of the State;
- Changes in the State's population; and
- Wage and salary growth pressures, which contribute to increased employment costs.

While some of these factors are outside the State's control, Figure 2 reconfirms the need to manage expenditure, in particular employee related expenditures, a matter also noted in my analysis of the Whole of Government financial report for the year ended 30 June 2005.

BALANCE SHEET

		2006 $m	2005 $m	2004 $m
Assets				
Financial assets				
Cash and deposits	A	607	623	685
Advances paid	A	56	42	66
Investments. Loans and placements	A	2	10	12
Other non-equity assets	B	1 038	334	314
Equity in GBEs and SOCs	B	3 049	3 782	4 206
Total financial assets	***C***	***4 752***	***4 791***	***5 283***
Non-financial assets				
Land and other fixed assets		8 584	7 633	6 323
Other non-financial assets		58	61	22
Total non-financial assets		***8 643***	***7 694***	***6 345***
Total assets	***D***	***13 395***	***12 487***	***11 628***
Liabilities				
Advances received	E	248	261	273
Borrowings	E	157	387	603
Superannuation	F	3 199	2 292	2 242
Other employee provisions		356	329	311
Other non-equity liabilities		327	210	218
Total liabilities	***G***	***4 287***	***3 479***	***3 647***
Net Worth	**D-G**	**9 108**	**9 008**	**7 981**
Net Financial Worth	**C-G**	**464**	**1 314**	**1 636**
Net Financial Liabilities	**H+F**	**(2 940)**	**(2 264)**	**(2 355)**
Net Debt	**H=A-E**	**259**	**28**	**(113)**

Comment

The GGS had negative net debt for the second consecutive year, with debt related financial assets exceeding gross debt liabilities by $259m as at 30 June 2006.

Other non-equity liabilities include $60m prepaid funding from the Commonwealth, received in June 2006, for the redevelopment of the East Tamar Highway. This was treated as income in the financial statements of the Department of Infrastructure, Energy and Resources (prepared under Australian Accounting Standards AAS 29) but the UPF basis requires that the $60m be treated as unearned income at 30 June 2006 in the GGS Statements.

This $60m contributed significantly to the negative net debt of $259m because it is included in financial assets but not in financial liabilities. Without this receipt, net debt would have been $199m.

The State's investments in its GBEs and SOCs represent 100% of the audited net assets of these entities, which at 30 June 2006 were:

GBE/SOC	2006 $m	2005 $m	2004 $m
Forestry Tasmania	569	697	727
Hydro Tasmania	907	1 538	2 056
Motor Accidents Insurance Board	249	173	122
Port Arthur	11	12	10
Printing Authority	3	3	3
Private Forests Tasmania	1	1	1
The Public Trustee	4	4	3
Rivers and Waters Supply Commission	14	43	36
Southern Regional Cemetery Trust	7	6	6
Tascorp	20	20	10
Aurora Energy	333	404	376
Burnie Port Corporation**	0	21	19
Hobart Ports Corporation**	0	64	59
Metro Tasmania	21	21	21
Port of Devonport Corporation**	0	38	37
Port of Launceston Corporation**	0	27	27
Tasmanian Ports Corporation	146	0	0
TOTE Tasmania	40	40	16
Transend Networks	529	572	552
TT-Line Company	188	110	114
Total net assets	**3 042**	**3 793**	**4 195**
Amount recorded as Equity	**3 043**	**3 775**	**4 196**
Variance accepted as not material*	**1**	**(18)**	**1**

** Variance arises because the Budget Outcomes Statements are completed prior to finalisation of audits of GBEs and SOCs.*

*** Transferred to Tasmanian Ports Corporation on 1 January 2006.*

In almost all cases the State's GBEs and SOCs operated profitably in 2005-06 with MAIB standing out in relative terms. The significant decrease of $733m in net assets was primarily caused by the impact of the adoption of the new accounting standards under

AIFRS (2004-05 figures are based on AGAAP). A separate section in the Executive Summary of this Report highlights the impact of AIFRS on the financial reports of GBEs and SOCs.

In summary, the changes arose primarily from:

- The requirement to use the bond rate in setting discount rates applied to assessing the unfunded superannuation liabilities of these entities;
- The application of the balance sheet approach to determining the carrying amount of deferred tax liabilities; and
- The need to impair assets particularly at Hydro Tasmania.

Changes in the net assets of GBEs and SOCs not caused by AIFRS included:

- TT-Line – net equity improved by $78m due to an equity injection of $62.267m by Government. It also earned an after tax profit due to upwards revaluation of Spirits I and II and because Spirit II was recorded at selling price (improvement arose due to strengthening of the Australian dollar relative to the Euro); and
- Strong investment performance and low claims experience by the MAIB.

Other non-equity assets increased by $704m (from $334m to $1 038m) in 2005-06, due principally to deferred income tax assets, which reflect changes resulting from the introduction of AIFRS. These amounts are shown as liabilities in the accounts of GBEs and SOCs.

Land and other fixed assets increased by $951m (2005, $1.310bn) primarily due to:

- Asset construction/acquisitions in Education, Health, DIER, Tourism, Justice and Treasury, $244m;
- Museum collections valued for the first time, $344m; and
- Net revaluation surpluses in Education, Health, DIER, Tourism and DPIW, $488m.

Offset by

- Depreciation of $170m.

Significant capital expenditures in 2005-06 included:

- Redevelopment of the Royal Hobart Hospital, $63.390m;
- Housing dwelling stock, $41.570m;
- Prison redevelopment, $47.712m;
- Improvements to road infrastructure, $57.246m; and
- Redevelopment of school buildings, $31.245m.

Borrowings decreased consistent with Government policy of reducing net debt. During the year Borrowings reduced by $230m which contributed significantly to the negative net debt of $259m. However, net financial liabilities remains high at $2.940bn almost all of which comprises unfunded superannuation liabilities.

The Superannuation liability increased by $907m in 2005-06, due to changes in actuarial assumptions, particularly the discount rate applied by the State Actuary, on application of the new accounting standards under AIFRS.

Net worth grew by $100m in 2005-06 to $9.108bn. The Budget Outcomes Statements includes a reconciliation of movements in Net Worth, which is repeated below as follows:

	$m
Opening Net Worth	9 008
Add net operating result	120
Add net revaluations of non-financial assets	214
Add assets brought to account for the first time	353
Add equity investment revaluations	102
Less revaluation of superannuation liability	(808)
Add other changes in net assets	119
Closing Net Worth	**9 108**

The main components in this reconciliation have been commented upon previously.

CASH POSITION

		2005-06 $m	2004-05 $m	2003-04 $m
Cash receipts from operating activities	A	3 680	3 417	3 269
Cash payments for operating activities	B	(3 229)	(2 971)	(2 776)
Net Cash Inflows from operations	C=A-B	**451**	**447**	**493**
Net acquisition of non-financial assets				
Sale of non-financial assets		50	42	76
Purchase of non-financial assets		(262)	(241)	(169)
Net acquisition of non-financial assets	D	**(213)**	**(199)**	**(93)**
Net cash flows from investments in financial assets for policy purposes	E	**5**	**22**	**69**
Net cash flows from investments in financial assets for liquidity purposes	F	8	0	(11)
Net cash flows from financing activities				
Advances received		(13)	(13)	(50)
Net borrowings repaid		(254)	(242)	(145)
Other financing		(16)	(106)	(20)
Net cash flows from (on) financing activities	G	(283)	(360)	(215)
Cash surplus/(deficit)*	H=C-D	238	248	400
Net increase/(decrease) in cash held	I=H+G+E+F	(31)	(90)	243
Cash at beginning of year		623	685	441
Cash at end of year		607	623	685

** Cash surplus/(deficit) is equal to net cash flows from operating activities plus net cash flows from investments in non-financial assets.*

Comment

Reasons for movements in the State's cash flows are consistent with the commentary already provided relating to the Operating Statement and Balance Sheet.

	2005-06 Actual $'000	**2004-05 Actual** $'000	**2003-04 Actual** $'000
Special deposits and trust fund	1 783 242	1 539 679	1 446 193
Balance 30 June (before Temporary debt repayments)	**1 783 242**	**1 539 679**	**1 446 193**
Less Temporary debt repayments	(1 203 160)	(973 086)	(822 330)
Balance 30 June (after Temporary debt repayments)	**580 082**	**566 593**	**623 863**
REPRESENTED BY:			
Westpac Banking Corporation	(34 999)	19 016	(11 498)
Treasurer's account fixed deposits	584 339	519 780	608 000
Advances to Heads of Agency	210	210	210
Specific trust account fixed deposits	30 532	27 587	27 151
Balance 30 June	**580 082**	**566 593**	**623 863**

PUBLIC ACCOUNT STATEMENTS

Comment

The Special Deposits and Trust Fund (SDTF) consists of various accounts established by the Treasurer. The majority of these funds represent departmental operating accounts, where funds appropriated from the Consolidated Fund by the annual Consolidated Fund Appropriation Act are deposited. These operating accounts also retain funds that are not identified for return to the Consolidated Fund.

Other accounts in the SDTF include trust, approved overdraft, whole-of-government, business unit accounts and accounts established under legislation.

Surplus cash is used to repay maturing debt within a financial year, thus delaying any refinancing until the latest possible time and to minimise borrowing costs. This is shown above as Temporary debt repayments.

CONSOLIDATED FUND OUTCOME

	2005-06 Original Budget $'000	2005-06 Actual $'000	2004-05 Actual $'000
BALANCE 1 JULY	0	0	0
Receipts			
Recurrent receipts	2 986 282	2 993 767	2 917 054
Capital receipts	67 938	46 435	45 147
Total	**3 054 220**	**3 040 202**	**2 962 201**
Expenditure			
Recurrent services	2 891 007	2 861 599	2 699 784
Works and services	157 810	161 973	253 815
Total	**3 048 817**	**3 023 572**	**2 953 599**
Consolidated Fund Outcome	**5 403**	**16 630**	**8 602**
Financing			
Net loan repayments	(5 403)	(16 630)	(8 602)
Total	**(5 403)**	**(16 630)**	**(8 602)**
BALANCE 30 JUNE	0	0	0

Comment

Recurrent receipts in 2005-06 increased by $76.713m compared to 2004-05 and were also above budget by $7.485m. The major factors for variations over the prior year include increases in:

- GST revenue from the Commonwealth of $60.282m;
- State taxation of $23.116m, mainly in the areas of payroll tax, land tax and stamp duties;
- Departmental fees and recoveries of $2.758m;
- Sale of government property of $5.397m; and
- Resource rents and royalties of $5.487m with the most significant being Mineral royalties.

These were offset in part by:

- Decreases in receipts from GBEs/SOCs of $7.296m, due to lower levels of profitability; and
- Decreases in Other revenue of $11.775m due primarily to reductions in interest on investments resulting from the use of funds to repay debt by $240.000m.

Capital receipts in 2005-06 increased by $1.288m compared to 2004-05, but was $21.503m below budget. The main factor causing this budget variance was:

- A reduction in proceeds from the sale of government assets. The original budget included proceeds from the sale of buildings transferred from the Hobart Ports Corporation Pty Ltd with the expectation that this would occur in 2005-06. This was delayed and consequently no proceeds were available in this year.

Recurrent expenditure increased by $161.815m in 2005-06 compared to 2004-05 but was under budget by $29.408m. The major factors for this higher expenditure compared to 2004-05 include:

- Education expenditures increasing by $46.249m, principally due to wage increases of $31.000m;
- Health and Human Services expenditures increasing by $110.587m due mainly to higher staffing levels in hospitals as well as salary increments;
- Justice expenditures increasing by $16.174m, principally due to additional staff, operational costs in correctional services (mainly salary increases), and transfers due to administrative restructuring;
- Police expenditures increasing by $13.703m, principally to fund salary increases and additional police officers; and
- Tourism expenditures increasing by $8.787m, principally due to TMAG infrastructure improvements, inclusion of Environment Division operational costs from 1 April 2006 resulting from the administrative restructure and funding for a legal compensation payment.

These were offset in part by:

- Finance-General expenditures reducing by $42.443m due to provision for wage increases, $13.070m and the Treasurer's Reserve, $20.000m not being required. These were the main factors in total expenditures being under budget for the year.

Works and Services expenditure decreased in 2005-06 by $91.842m compared to 2004-05. The major factors for this include:

- In 2004-05 an amount of $60.000m was allocated for the Royal Hobart Hospital redevelopment;
- Reduced activity in redevelopment of facilities within the Education Department;
- One-off funding for the Better Roads Fund in 2004-05; and
- Completion of the capital phase of the Affordable Housing Strategy at the end of 2004-05.

Instances where Departments required additional funding through "Requests for Additional Funds" included increases for:

- National Highway Funding of $2.974m for the Department of Infrastructure, Energy and Resources;
- Payroll tax on the 27th pay of $1.125m and Vocational Education and Training of $1.606m for the Department of Education;
- Legal settlement costs of $2.250m for the Department of Tourism, Arts and the Environment;
- The Meander Dam Project of $0.300m and Legal costs of $0.746m for the Department of Primary Industries and Water; and
- A range of items including additional police numbers, State security unit and a helicopter contract for the Department of Police and Emergency Management.

ASSESSMENT OF SIGNIFICANT ITEMS IMPACTING THE GENERAL GOVERNMENT SECTOR

This section provides brief commentary on significant matters impacting financial reporting in 2005-06.

Unfunded Superannuation Liability

The Tasmanian Government's unfunded superannuation liability is an estimate of the obligations of the State with respect to past service liabilities arising from current and former members of unfunded or partially funded Public Sector superannuation schemes.

At 30 June 2006, the State's unfunded superannuation liability totalled $3.199bn, which was $907.000m or 40 per cent more than the previous year (previous year was based on AGAAP). The significant increase was due to the actuarial revaluation of the liability as part of the adoption of AIFRS, due mainly to a change in the discount rate applied. The increase of $907.000m is charged directly to equity in the Statements and did not impact the Net Operating Result.

The extended target date for elimination of the unfunded liability from 2018 to 2033 has been reflected in reduced contributions from the Consolidated Fund to the Superannuation Provision Account. This, according to the Department of Treasury and Finance, provides additional budget flexibility to apply this funding to other areas. According to the Department, the likely impact will be to reduce the Fiscal Balances and reduce the improvement in Net Debt over this period.

Valuation of Tasmanian Museum and Art Gallery (TMAG) Collections

During 2005-06 the TMAG Collections were valued and recognised for the first time in the financial statements of the Department of Tourism, Arts and the Environment at a value of $344.000m. This added 3.82% to the State's net worth.

Transfer of Port assets to Finance - General in the Department of Treasury and Finance

On 1 July 2005, the Tasmanian Ports Corporation Pty Ltd was incorporated, bringing together Tasmania's four major port companies into one single port entity with effect from 1 January 2006. Assets with a book value of $25.575m were transferred to the Department of Treasury and Finance from the former Hobart Ports Corporation Pty Ltd as at 31 December 2005 on the basis of an equity withdrawal.

Funding for the East Tamar Highway

The $60.000m received prior to 30 June 2006 and allocated to DIER has the effect of increasing the State's financial assets at 30 June 2006 and reducing net debt.

OVERALL COMMENT

The State's financial position is sound.

My audits of the 2005-06 Budget Outcomes Statements and of the Public Account Statements were completed with satisfactory results.

5 TIMELINESS AND QUALITY OF FINANCIAL STATEMENTS

STATUTORY FINANCIAL REPORTING REQUIREMENTS

Under section 28 of the *Financial Management and Audit Act 1990* (FMAA) and section 52 of the G*overnment Business Enterprises Act 1995* (GBE) specific dates are set by when relevant entities are to provide financial statements to Audit to formally allow the audit process to commence. The dates specified are as follows:

- FMAA: Within 45 days after the end of the financial year; and
- GBE: Within 45 days after the end of the financial year.

Whilst no specific deadline is set for completion of financial statements of Statutory Authorities, I have taken the view that similar deadlines apply.

In most cases entities have a 30 June financial year making 15 August the statutory date by when financial statements are to be transmitted to my Office.

What is not absolutely clear is just what is meant by "… provide financial statements to Audit….". I have interpreted this as requiring that the financial statements submitted to my Office for audit are complete in all respects including that they are certified by the responsible authority – in the case of Departments this is the Secretary and in the case of GBEs and Statutory Authorities this is the Board of Directors. In some instances entities signed their financial statements by 15 August, but did not provide them to my Office until a few days later.

These dates have been set to allow sufficient time for the audit to be completed and for the reporting entities to prepare their Annual Reports for tabling in Parliament by 31 October each year. To facilitate this I set an internal deadline requiring my staff and my contractors to complete audits by no later than 15 October.

For Local Government, Council General Managers are, pursuant to the *Local Government Act 1993*, required to prepare financial statements within 90 days after the end of the financial year, which I have interpreted as 30 September and submit them to me as soon as practicable. State-Owned Companies must comply with the reporting requirements detailed in the *Corporations Act 2001.*

There are no exemptions from meeting the statutory date under either the FMAA or the GBE Act, nor are there penalties for not meeting this date.

SIGNED STATEMENTS NOT RECEIVED ON OR BEFORE STATUTORY DEADLINES

Listed below are entities whose signed financial statements were not received prior to the statutory deadline. Dates shown in brackets represent the date signed financial statements were received, unless otherwise stated.

15 AUGUST DEADLINE

Executive and Legislature

- Office of the Governor (21 August 2006).

Government Business Enterprises

- Southern Regional Cemetery Trust (21 September 2006);
- The Public Trustee (1 September 2006); and
- Tasmanian International Velodrome Management Authority (7 September 2006).

Other Statutory and Public Bodies

Under FMAA the entities listed below are required to submit completed financial statements within 45 days of financial year-end:

- Legal Aid Commission (18 September 2006);
- Marine and Safety Authority (28 September 2006);
- Nominal Insurer (30 August 2006);
- Royal Tasmanian Botanical Gardens (29 September 2006);
- Private Forests Tasmania (18 August 2006);
- Council of Law Reporting (4 October 2006);
- Teachers Registration Board (3 October 2006);
- Sullivans Cove Waterfront Authority (18 August 2006);
- Work Cover Tasmania Board (1 September 2006);
- Wellington Park Management Trust (25 August 2006);
- Tasmanian Museum and Art Gallery (13 October 2006);
- Tasmanian Heritage Council (17 October 2006); and
- Tasmanian Dairy Industry Authority (21 August 2006).

31 AUGUST DEADLINE

Statutory Bodies

- Aboriginal Land Council *(outstanding);*
- Ben Lomond Skifield Management Authority (20 October 2006); and
- Local Government Association of Tasmania *(outstanding).*

30 SEPTEMBER DEADLINE

Local Government

- Burnie City Council *(outstanding);*
- Brighton Council (October 2006);
- Latrobe Council (13 October 2006);
- Sorell Council (Draft received, 6 October 2006); and
- Flinders Council *(outstanding).*

31 OCTOBER DEADLINE

Statutory Bodies

- Tasmanian Beef Industry (Research & Development) Trust *(outstanding).*

National Trust of Australia (Tasmania)

Under section 17 of the *National Trust of Australia (Tasmania) Act 1975,* a copy of the Trust's annual financial statements is required to be submitted to the Minister by 30 September of each year. As of the time of printing this Report, these statements were still outstanding.

Reporting Timeframes

With the tighter reporting timeframe now in place for FMAA entities and GBEs, together with an increased desire by Boards or others charged with governance to achieve earlier sign off, an effective internal quality assurance process and accurate work papers supporting all elements of the financial statements are essential. Work papers should contain sufficient detail to enable verification by both management and my staff when conducting audits.

It is apparent from the number of entities listed above that more entities failed to meet reporting deadlines than in recent years. While the implementation of AIFRS may have contributed to some degree, the new standards and dates for first time adoption have been known for a considerable time and with adequate planning should not have created any difficulties.

Steps taken by Audit to facilitate earlier financial reporting

My Office continues to assist public sector entities to achieve early financial reporting. This year we have again taken the following two steps towards helping entities to meet their financial reporting requirements:

- Based on completion of 2004-05 financial audits, presented awards for best working papers supporting financial statements. Separate awards were made for the different types of public sector entities, details of which are shown below. The purposes of effective financial statement working papers include:
    - A framework for the compilation of financial statements by current and future preparers;
    - A central reference to the evidence required to support transactions, balances and estimates disclosed in the financial statements;
    - A trail between the entity's financial records for the year and the financial statements for the year, which can be followed by persons having a quality assurance function; and
    - A record of the quality control processes employed in the preparation of the financial statements.

This process assists my staff in the conduct of audits and, more importantly, assists entity accounting staff in the timely completion of accurate and quality assured statements; and

- Held a series of seminars for entity accounting staff dealing with changes to accounting standards and related matters. These sessions were held in June 2006 in Hobart and Launceston and provided guidance on steps to take to facilitate earlier financial reporting.

Annual Working Paper Awards

Category	Overall Winner	Highly Commended
Agencies	Premier and Cabinet	Education
Local Government	West Tamar	Derwent Valley Devonport City
GBEs and SOCs	Aurora Energy	Metro
Statutory Authorities	Esk Water	RBF

6 AIFRS READINESS AND IMPACT

Australia adopted Australian equivalents to International Financial Reporting Standards (AIFRS) for reporting periods commencing on or after 1 January 2005. All Public Sector entities adopted these standards for the first time in their financial statements for the year ended 30 June 2006, or 31 December 2005 for those entities with calendar financial years.

IMPACT OF AIFRS

Public sector entities changed accounting policies to comply with AIFRS on the date of transition to AIFRS being 1 July 2004. Previously the entities reported under the superseded Australian Generally Accepted Accounting Principles (AGAAP). This meant that, in preparing financial statements for the year ended 30 June 2006, the 2004-05 comparative balances were restated from the previous AGAAP. AASB 1 *First-time Adoption of Australian Equivalents to International Financial Reporting Standards* provided an exemption from having to apply the new standards to comparative period balances related to financial instruments. Most Tasmanian Public Sector entities took up this option.

AASB 1 required entities to explain how the transition from the previous AGAAP to AIFRS affected their reported financial position, financial performance and cash flows. As such, reconciliations and other disclosures can be found in the notes to the financial statements of all public sector entities for the year ended 30 June 2006.

QUANTIFICATION OF IMPACTS

The impact of the new standards varied depending on individual entities' business and scope of financial operations. The most significant impacts related to:

- Valuation of unfunded superannuation liabilities;
- Valuation of deferred tax assets and liabilities;
- Valuation and recognition of financial instruments;
- Valuation and impairment of non-current assets;
- Valuation and classification of employee benefit liabilities; and
- Recognition and measurement of provisions for restoration or reinstatement (make-good provisions).

The Department of Treasury and Finance recorded AIFRS adjustments reducing Finance General's Administered Equity by $1.896bn at 30 June 2005, as shown in the table below. This amount includes AIFRS required reductions to net assets of the Government Business Enterprises (GBEs) and State Owned Companies (SOCs), $880.662m, and a $1.016bn increase in the unfunded superannuation liability.

Table 1: Treasury Administered Equity – Finance – General ($m)				
Entity	***Tax***	***Superannuation***	***Other***	***Reduction in Equity***
Department of Treasury and Finance	-	1 015.884	880.702	1 896.586

Some of the larger changes relating to SOCs and GBEs are shown in Table 2 below:

Table 2: AIFRS Reduction in (Increases to) Equity 30 June 2005 ($m)

Entity	***Tax***	***Superannuation***	***Other***	***Reduction in Equity***
Hydro Tasmania	416.200	72.600	107.200[1]	596.000
Forestry Tasmania	102.811	29.303	2.365	134.479
Aurora Energy	77.227	15.813	(0.335)	92.705
Motor Accidents Insurance Board	(3.677)	0.572	11.047	7.942
Transend Networks	71.584	5.766	0.332	77.682
Metro Tasmania	-	5.342	-	5.342
TT-Line Company	-	1.124	0.355	1.479
Rivers and Water Supply Commission	-	0.451	40.994[2]	41.445
State Fire Commission	-	6.508	-	6.508
Tasmanian Ambulance Service	-	1.001	-	1.001

[1] *Includes impairment losses $19.3m, deemed cost transitional valuation adjustment $51.5m and RBF liability recalculation recognised as an expense $31.1m.*

[2] *Impairment losses.*

Overall, Tasmanian Public Sector entities were well prepared for the implementation of AIFRS. However, most entities underestimated the time required to determine the impacts of the new standards, to deal with unforseen interpretation issues and to tailor financial statements. This resulted in some delays in the completion of audits.

My review of the financial statement disclosures relating to the implementation and first time full adoption of AIFRS concluded that they were satisfactory and complied with professional financial reporting requirements.

7 AUDITS DISPENSED WITH

Specific audits

Section 41 of the *Financial Management and Audit Act 1990* permits the Auditor-General to dispense with audits. The decision to dispense with an audit is made annually with information provided to Members of Parliament in these reports to Parliament. The Auditor-General's No 1 Report for 2006, tabled on 22 June 2006, listed 31 entities the audits of which had been dispensed with. Since that time the following two audits were dispensed with on the basis that, for the 2005-06 financial year only, the audits were conducted by the private sector:

- Travel Agents Licensing Board; and
- Council of Law Reporting.

Categories of audits

Those public bodies that receive grant funding from the State Government via its various Departments.

Annual audits of these Departments continue to include audit work of their grant programs, one objective of which is to ensure that appropriate internal control arrangements are in place for making grant payments and for the acquittal thereof by the public bodies concerned. As a result, my Office did not conduct separate audits of these entities and I have not specifically dispensed with these audits.

8 APPENDIX 1 – ACRONYMS AND ABBREVIATIONS

AASB	Australian Accounting Standards Board
ACCC	Australian Competition and Consumer Commission
AFSL	Australian Financial Services Licence
AGAAP	Australian Generally Accepted Accounting Principles
AHCA	Australian Health Care Agreement
AIFRS	Australian International Financial Reporting Standards
APRA	Australia Prudential Regulation Authority
ASOSC	Antarctic and Southern Ocean Science Centre Pty Ltd
BBP	Bell Bay Power Pty Ltd
CAMP	Capital Asset Pricing Model
CHWB	Community Health and Well Being
CIP	Capital Investment Program
CLAF	Crown Land Administration Fund
CRM	Client Management System
CSA	Community Service Agreement
CSHA	Commonwealth State Housing Agreement
CSO	Community Service Obligation
DEST	Department of Education, Science and Training
DHHS	Department of Health and Human Services
DIER	Department of Infrastructure, Energy and Resources
DPIW	Department of Primary Industry and Water
DPIWE	Department of Primary Industries Water and Environment
DTA	Deferred Tax Assets
DTAE	Department of Tourism Arts and the Environment
DTL	Deferred Tax Liability
EBA	Enterprise Bargaining Agreement
EBIT	Earnings before interest and tax
EBITDA	Earnings before interest, tax, depreciation and amortisation
ESIF	Economic and Social Infrastructure Fund
FMAA	Financial Management and Audit Act 1990
FTE	Full-time equivalent
GBE	Government Business Enterprise
GDP	Gross Domestic Product
GFS	Government Finance Statistics
GGS	General Government Sector
GMO	Grantham, Mayo and Otterloo
GPOC	Government Prices Oversight Commission

GSP	Gross State Product
HACC	Home and Community Care
HOAP	Home Ownership Assistance Program
IFAC	Inland Fisheries Advisory Council
MAIB	Motor Accidents Insurance Board
MIC	Member Investment Choice
MPEP	Monetary Penalty Enforcement Project
NDLERF	National Drug Law Enforcement Research Fund
NEM	National Electricity Market
NEMMCO	National Electricity Market Management Company Limited
PCA	Gas Pipeline Capacity Agreement
PIRP	Prison Infrastructure Redevelopment Program
PRFB	Parliamentary Retiring Funds Benefit
PSF	Parliamentary Superannuation Fund
R40s	Roaring 40s Renewable Energy Pty Ltd
RBFB	Retirements Benefits Fund Board
RFA	Regional Forest Agreement
SCIF	Special Capital Investment Funds
SESDMF	State Emergency Service Disaster Mitigation Funding
SFCSS	State Fire Commission Superannuation Scheme
SOC	State Owned Company
SSA	State Service Act
SSWA	State Service Wage Agreement
TAFR	Treasurers Annual Financial Report
TAS	Tasmanian Ambulance Service (DHHS)
TAS	Tasmanian Accumulation Scheme (RBFB)
TASCORP	Tasmanian Public Finance Corporation
TasPorts	Tasmanian Ports Corporation Pty Ltd
TASSS	Tasmanian Ambulance Service Superannuation Scheme
TCFA	Tasmanian Community Forest Agreement
TMAG	Tasmanian Museum and Art Gallery
TNSP	Transmission Network Service Provider
UPF	Uniform Presentation Framework
VET	Vocational Education and Training
WACC	Weighted Average Cost of Capital
WST	Workplace Standards Tasmania

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AUDIT MANDATE AND STANDARDS APPLIED

MANDATE

Section 39 of the *Financial Management and Audit Act 1990* states that the Auditor-General is:

> '… the auditor of the accounts of the Treasurer, of all Government departments and public bodies and of the financial administration of each appropriation referred to in Column 1 of Schedule 2. …'

The conduct of such audits is generally known as financial auditing.

Under the provisions of section 40, the Auditor-General:

> '… (1) On performing an audit under this or any other Act of the financial statements of the Treasurer, a Government department, a public body or the financial administration of an appropriation referred to in Column 1 of Schedule 2, the Auditor-General must, except as provided by any other written law, make a report on those financial statements in accordance with this section.
>
> (2) Subject to subsection (3), a report made under subsection (1) -
>
> *(a)* is to include an opinion as to whether the financial statements have been drawn up so as to present fairly the financial transactions during the period specified in the statements and the financial position at the end of that period; and
>
> *(b)* may include particulars of any other matter arising from the audit which the Auditor-General considers should be included in the report.
>
> (3) Where, under this or any other Act, the financial statements are not required to make full disclosure of financial position, the Auditor-General's opinion as to financial position may be limited to such components of financial position as may be specified in the Treasurer's Instructions and such other components of financial position as are included in those statements. …'

STANDARDS

Section 43 specifies that:

> '… The Auditor-General shall perform the audits required by this or any other Act in such manner as the Auditor-General thinks fit having regard to -
>
> *(a)* this Act and any other relevant written law relating to the financial management of the Government department or public body concerned; and
>
> *(b)* recognised professional auditing standards and practices. …'
>
> The auditing standards referred to above are Australian Auditing Standards as produced by the Australian Auditing and Assurance Standards Board.

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