

Auditing for the Australian Capital Territory

The Auditor-General is head of the Auditor-General's Office. He and his Office act independently of the Government. The Office assists the Auditor-General to carry out his duties, which are set out in the Auditor-General Act 1996, by undertaking audits of management performance and the financial statements of public sector bodies. The aim is to improve public sector management and accountability by firstly, ensuring the Legislative Assembly and the electorate are provided with accurate and useful information about the management of public sector resources and secondly, by providing independent advice and recommendations for improving the management of public resources.



AUDITOR-GENERAL
AUSTRALIAN CAPITAL TERRITORY



PA 99/03

10 December 2001

The Speaker
ACT Legislative Assembly
South Building
London Circuit
CANBERRA ACT 2601

Dear Mr Speaker

In accordance with the Authority contained in the *Auditor-General Act 1996*, I transmit to the Legislative Assembly my Report titled "*Agents Board – Financial Administration of Training Program Grant*".

This Audit was undertaken with the assistance of KLA Australia.

Bernie Sheville of this office managed the Audit.

Yours sincerely

A handwritten signature in black ink, appearing to read 'John A Parkinson'.

John A Parkinson

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1 REPORT SUMMARY

INTRODUCTION

1.1 The Agents Board of the ACT (the Agents Board) is a body corporate constituted under the *Agents Act (1968)*.

1.2 The Agents Board is the licensing authority for the real estate and travel industries in the ACT. The Agents Board aims to protect consumer interests by maintaining an effective licensing system and a compensation scheme for real estate consumers.

1.3 As part of its activities, the Agents Board provided training grant funding to the Real Estate Institute of the ACT (REIACT) to provide education programs on real estate matters for real estate agents and the general public.

1.4 On 8 November 1996, the Agents Board entered into a three year agreement (the Agreement) with REIACT. Under the Agreement, REIACT was to develop and provide the training courses initially specified in the Agreement and subsequently others as approved by the Board.

REASONS FOR THE AUDIT

1.5 Following increasing concerns by the Agents Board regarding REIACT's apparent non compliance with its Agreement, the Agents Board decided to conduct an evaluation of REIACT's performance in delivering the training program. To this end the Board contracted a suitably qualified consultant to conduct a review of qualitative aspects of REIACT's performance. The consultant noted several unsatisfactory matters but concluded:

‘the basis has been established for the provision of high quality training for the real estate industry.’

1.6 The Agents Board's concerns regarding REIACT's apparent non compliance with the financial requirements of the Agreement were, among others, that financial reports provided by REIACT were not in the format required by the Agreement and that these reports indicated that the estimates which had formed the basis for setting the first year's funding were likely to have been significantly understated. The Board

was also of the view that there seemed to be an excessive amount of expenditure being charged against the training grant. As a result of its concerns the Board requested the Auditor-General to perform an audit of the financial aspects of the training grant.

1.7 The Auditor-General decided to perform this performance audit of the financial compliance with the Agreement on the basis that the findings of this Audit could be relevant to other agencies which use public funds to acquire services from external service providers under similar arrangements. The Audit included a consideration of the Agents Board's management of the training grant funds.

AUDIT APPROACH

1.8 In undertaking this work the Audit included a review of:

- the requirements of the Agreement;
- approved documentation for funding provided to REIACT;
- audited and unaudited financial reports provided by REIACT to the Agents Board under the Agreement;
- Agents Board's submissions and minutes relating to REIACT and correspondence between the Agents Board and REIACT; and
- information provided by REIACT and the financial information and documentation held by REIACT.

1.9 Consultations were also held with staff of the Agents Board and REIACT.

1.10 The Audit was focussed on the financial aspects of the administration of the training grant. The Audit did not assess the quality or effectiveness of the training courses provided as this was not within the scope of the Audit.

1.11 The Audit was conducted in accordance with Australian Auditing Standards.

AUDIT OPINIONS

1.12 Several audit opinions were formed as a result of the Audit. These are set out on page 3 of this Report.

Management of the Agreement's Financial Arrangements (Chapter 2)

- The management actions taken by the Agents Board when it became aware there were problems were sensible management actions and were as effective as the circumstances would allow.

Training Grant Expenditure (Chapter 3)

- Even though a majority of expenditure charged against training grant funds complied with the Agreement a significant amount of expenditure was incorrectly charged.

Recording Grant Expenditure (Chapter 4)

- REIACT did not maintain proper and adequate books of account for training grant expenditure as required by the Agreement.

Training Grant Revenue (Chapter 5)

- Some revenue derived by REIACT from training activities was not derived in accordance with the Agreement.

Financial Reporting (Chapter 6)

- REIACT did not comply with its financial reporting obligations under the Agreement.

Conflict of Interest Issues (Chapter 7)

- The REIACT directors did not formally disclose their REIACT directorships at a meeting of the Board.
- The REIACT directors did not contravene the conflict of interest provisions contained in the *Agents Act 1968*.
- The Audit was unable to conclude on whether the REIACT directors met their fiduciary duties to avoid a potential conflict of interest situation through their REIACT directorships being disclosed to the other Board members by means other than formal disclosures at a Board meeting¹.
- The *Agents Act (1968)* does not provide an adequate legislative framework for addressing conflict of interest matters.

¹ It should be noted no evidence came to notice during the conduct of this audit which indicated that the REIACT Directors used their positions on the Agents Board for any purpose of self-interest, personal gain or impropriety.

BASES FOR THE AUDIT OPINIONS

1.13 A summary of the reasons for the audit opinions follows. More detail is provided in the later chapters of this Report.

Management of the Agreement’s Financial Arrangements (Chapter 2)

1.14 The audit opinion that *‘management actions taken by the Board when it became aware there were problems were sensible and effective’* is based on the following.

1.15 The Board was confronted with a difficult problem. To satisfy itself that REIACT was complying with the financial arrangements set in the Agreement with REIACT the Board’s expectations were that it would be able to rely on the information provided to it by REIACT and REIACT’s auditors. This turned out not to be the case.

1.16 On one hand the Board was generally of the view that the training courses being provided by REIACT were producing beneficial results by the generation of improved real estate practices in the ACT. On the other hand there were indicators that REIACT was not complying with the Agreement’s requirements in relation to the financial arrangements.

1.17 The Board was satisfied before the end of the first year of the three years of the training program that REIACT had not properly accounted for funds advanced to it. The Board, however, was of the view that this was probably a result of teething problems often encountered at the beginning of a project or program.

1.18 As further indications emerged that REIACT was not complying with the Agreement the Board responded by taking ‘a number of actions’.

1.19 Documentation reviewed by the Audit indicates that the Board made significant attempts to persuade REIACT to comply with the Agreement short of terminating the Agreement. Minutes of Board meetings indicate that the Board, because of the perceived benefits of the training courses, was unwilling to terminate the Agreement even though it was aware that significant non compliance with the Agreement by

REIACT was occurring². One member strongly recommended the agreement be terminated.

1.20 Over a lengthy period Board representatives held discussions with REIACT and its auditors and correspondence was exchanged. The discussions and correspondence however did not resolve the situation.

1.21 The Agents Board eventually addressed REIACT's non compliance with the Agreement by requesting an audit of the financial aspects of the training grant to be performed by the Auditor-General's Office. This request was made prior to the Board suspending further payment i.e. third year funding was not paid to REIACT.

Training Grant Expenditure (Chapter 3)

1.22 The Audit opinion that *'even though a majority of expenditure charged against training grant funds complied with the Agreement a significant amount of expenditure was incorrectly charged'* is based on the Audit's estimate that \$67,500³ (approximately 25%) of the total expenditure of \$262,200 was incorrectly charged against training grant funds.

Recording Grant Expenditure (Chapter 4)

1.23 The Audit opinion that *'REIACT did not maintain proper and adequate books of account for training grant expenditure as required by the Agreement'* is based on the Agreement's specific requirement that proper accounts be maintained. The requirement for 'proper' accounts extends beyond the maintenance of an adequate accounting system. In addition to its accounting system being adequate REIACT also needed to ensure that expenditure recorded in the accounting system as training grant expenditure was supported by sufficient and appropriate supporting documentation. REIACT did not have supporting documentation for a significant amount of the expenditure recorded.

² Meeting No. 98/9 of 22 September 1998.

³ This calculation is based on a conservative audit estimate of \$67,515 in non complying expenditure reported in Chapter 3 of this report. If a narrower legal interpretation received from the ACT Government Solicitor was adopted then the amount of non complying expenditure would be \$88,312.

Training Grant Revenue (Chapter 5)

1.24 The Audit opinion that ‘*some revenue received by REIACT from training activities had not been derived in accordance with the Agreement*’ is based on the finding that REIACT charged fees for training courses without written consent from the Agents Board as required by the Agreement.

Financial Reporting (Chapter 6)

1.25 The Audit opinion that ‘*REIACT did not comply with its financial reporting obligations under the Agreement*’ is based on the findings that the audited and unaudited financial reports were not provided within the timeframes prescribed in the Agreement and were unsuitable for assessing the financial accountability of REIACT.

Conflict of Interest Issues (Chapter 7)

1.26 The Audit opinion that ‘*the REIACT directors did not formally disclose their REIACT directorships at a meeting of the Board*’ is based on the Audit’s review of the Board’s minutes of meetings and information provided by other Board members and the Registrar of Agents. There is no record of disclosure in the Board’s minutes and the other Board members and the Registrar advise they do not recall formal disclosures occurring.

1.27 The Audit opinion that ‘*the REIACT directors did not contravene the conflict of interest provisions in the Agents Act 1968*’ is based on the following.

1.28 Section 16(8) of the *Agents Act (1968)* states that:

‘A member of the Board shall withdraw from any meeting of the Board when ... another matter *directly affecting* the member is being dealt with by the Board’ (emphasis added).

1.29 Legal opinions on interpretation of the words ‘directly affecting’ differ.

1.30 The ACT Government Solicitor provided advice that the words ‘directly affecting the member’ were capable of either a broad or narrow interpretation but concluded that a broad interpretation should be

adopted. The Solicitor said ‘in my opinion it is reasonable to conclude that matters relating to the grant by the Board to REIACT are matters directly affecting a member who is a director of REIACT.’ However, even though the advice indicated a broad interpretation of the section was possible, the advice did not conclude that there had been a breach of Section 16(8).

1.31 Legal advice provided to the REIACT directors and sighted by the Audit argued that the specific use of the term ‘directly affecting’ drew a narrower interpretation. The advice was that the REIACT directors were entitled to participate in the Board’s deliberations on the REIACT grant and need not withdraw from the Board considerations⁴.

1.32 As the ACT Government Solicitor’s advice stopped short of concluding that a breach of Section 16(8) had occurred, and the other legal advice sighted by the Audit was that REIACT directors did not contravene section 16(8), the Audit’s conclusion, on balance, is that the directors did not contravene the Act’s requirements.

1.33 The restrictive nature of Section 16(8) appears to be at odds with legislative intentions as expressed in recent legislation establishing ACT statutory authorities. The question as to whether the existing Agents Act provides an appropriate framework for addressing conflict of interest issues was considered in the Audit and comments are provided later in this Chapter.

1.34 The audit opinion that ‘*the audit was unable to conclude on whether the REIACT directors met their fiduciary duties to avoid a potential conflict of interest situation through their REIACT directorships being disclosed to the other Board members by means other than formal disclosures at a Board meeting*’ is due to conflicting information being provided to the Audit on the disclosures actually made. In the absence of consistent evidence regarding the disclosures made, the Audit was unable to ascertain whether the other Board members were aware, or unaware, that the REIACT directors were Board members at the same time as they were REIACT directors.

⁴ Elrington Boardman Allport advice of 7 December 1998 and Phelps Reid advice of 21 December 2000.

1.35 The audit opinion that *'the Agents Act (1968) does not provide an adequate legislative framework for addressing conflict of interest matters'* is based on the Audit's comparison of the *Agents Act (1968)* to recent legislation. Unlike the *Agents Act (1968)* recent legislation is significantly broader in its application to conflict of interest situations. Recent legislation also sets out responsibilities for disclosure and the associated record keeping requirements. The recent legislation is also more flexible in allowing the continued participation of a Board Member in discussions on a matter in which the Member has disclosed a potential conflict. Continued participation is allowed provided the reasons are specified and documented and a Board/Ministerial determination is made. It is the Audit view that the recent legislation is significantly better than the *Agents Act* in its treatment of conflict of interest issues.

POSSIBLE IMPLICATIONS FOR OTHER GOVERNMENT AGENCIES

Use of Cost Based Funding Arrangements

1.36 The Agreement between REIACT and the Agents Board included a cost based funding arrangement. Under this arrangement there was no provision for REIACT to earn profits from delivering the training program. Similarly the Board was to pay no more to REIACT than REIACT's actual costs of providing the agreed services.

1.37 Similar cost based methods of funding to that used by the Board may be being used by other government agencies to deliver services.

1.38 Generally when cost based funding is adopted, the government funding agency will rely on reviewing audited and unaudited financial reports to confirm that the funds it has provided are being used only for the purposes for which the funds were provided. The reporting and audit requirements are generally contained in an agreement or contract which the funding agency enters into with the service deliverer.

1.39 This Report describes problems which the Agents Board encountered in the management of its cost based financial arrangements with REIACT.

1.40 The Audit is of the view that the problems may have been avoided if the Board had taken certain actions prior to the commencement of the Agreement. These actions included setting the

basis for REIACT charging each category of cost along with the requirements for associated supporting documentation; agreeing with REIACT on a format for the financial reports; and briefing REIACT's auditors verbally and in writing on how the auditors' work would be used. More detail on these procedures is included in Chapter 2 of the Report.

1.41 Agencies with cost based arrangements should take note of the Agents Board's difficulties and review their own procedures to ensure their procedures are sound for ensuring the funds they provide are used only for meeting the service deliverer's relevant costs.

1.42 The Audit's view is that a competitive selection process should be preferred wherever possible over cost based arrangements. If sound competitive selection processes are used to select service deliverers it would generally be unnecessary for a cost verification process to be used. This is because the competitive selection process, if carried out properly, will have settled a fair price. A 'fair price' for the purpose of this discussion is the amount which a purchaser would pay to a supplier if the purchaser and the supplier were knowledgeable and willing parties participating in an arm's length transaction.

1.43 Once a fair price is established, the funding agency only needs to verify that the services are being satisfactorily delivered in accordance with an agreed specification. A need for detailed monitoring of the costs actually incurred by the service deliverer is significantly reduced or, in some cases, may be eliminated.

FUTURE ACTIONS

By the Agents Board

1. *Recovery of Costs* – the Audit estimated that at least \$47,000 in grant funding has been received by REIACT in excess of REIACT's actual costs. This is contrary to the Agreement. The Agents Board should therefore seek to recover this excess from REIACT.

2. *Review of Procedures* – if the Agents Board decides to continue having training programs delivered under the current arrangement, then the Agents Board will need to review its procedures to ensure that the Agents Board funding only meets independently verifiable costs of delivering the program.

By All Agencies

3. *Review of Cost Based Funding Arrangements* – all agencies acquiring services under cost based funding arrangements should review the effectiveness of their existing arrangements in view of the findings of this report. Agencies should evaluate whether their cost based funding arrangements are an effective means of funding the delivery of services.

4. *Review of Procedures* – agencies with cost based funding arrangements should evaluate whether their procedures ensure that they only pay for the actual and independently verifiable costs of the service provider. Where agencies are relying on an independent audit being performed to provide assurance that they only pay for the actual costs of the service provider, the agency should ensure that the auditors are properly briefed on the funding arrangements and how the agency plans to use the auditor's work.

By Statutory Authorities

5. *Addressing Potential Conflict of Interest Issues* – statutory authorities should review their procedures for addressing conflict of interest matters. As a minimum, these procedures should ensure that potential conflicts of interest are properly disclosed and recorded.

By the Government

6. *Review of the Agents Act* – the *Agents Act (1968)* should be amended to provide an adequate legislative framework for addressing conflict of interest matters.

7. *Review of Statutory Authorities Legislation Generally* – legislation relating to other authorities should be reviewed and, if required, amended to provide an adequate legislative framework for addressing conflict of interest matters.

AGENTS BOARD RESPONSE TO THE REPORT

1.44 In accordance with Section 18 of the *Auditor-General Act 1996*, a final draft of this report was provided to the Agents Board for consideration and comments. The Agents Board's responded that, after examining the proposed final draft of the report, that it did not wish to provide further written comments. The Agents Board also noted the Audit's advice that its responses to earlier report drafts had been taken into account in finalising the report.

DEPARTMENT OF TREASURY RESPONSE

1.45 The Department of Treasury, as part of the Government's Public Service Renewal Program, is reviewing governance arrangements for ACT statutory authorities. This Report included an assessment of conflict of interest matters. It also includes suggested future actions arising from the assessment. The manner in which statutory authorities manage conflict of interest issues is a governance matter. Accordingly the Department of Treasury has been asked to respond generally in relation to the conflict of interest issues in the Report.

1.46 The Department's response follows.

'I thank you for your letter dated 20 September 2001 inviting the Department of Treasury (Treasury) to provide comments on the above Audit report and apologise for the delay in responding.

As indicated in your letter, Treasury is undertaking a comprehensive review of ACT corporate governance arrangements. As part of this process, the enabling legislation of statutory authorities, general legislation such as the Territory Owned Corporations Act 1990 and the Financial Management Act 1996, and relevant legislation and corporate governance arrangements in other jurisdictions are being examined.

Further, as noted in your letter of 6 September 2001 to the Chief Executive of the Chief Minister's Department, we will continue to consult with your Office in reviewing the governance arrangements. This process will result in a comprehensive policy paper covering not only corporate governance guidelines, but also any legislative options for the Government's consideration.

In addition to the governance issues for ACT statutory authorities, I note that the findings and the recommendations of the Audit report also raised various issues concerning how the Government purchases services. The following general comments from Treasury are limited to the conflict of interest issues, in response to your request for input for inclusion in paragraph 1.46 of the Report:

- *Treasury considers there is a need for statutory authorities to have in place sound corporate governance practices to assist in managing contentious issues and help resolve disputes in conflict of interest and other cases.*

- *Treasury agrees that a perceived conflict of interest can be as damaging as an actual one. This issue will be addressed as part of a comprehensive audit of corporate governance arrangements of all government business entities (territory owned corporations, statutory authorities and government business units). Once the audit of corporate governance arrangements is finalised, recommendations will be made to the Government on the options for improved arrangements, including whether to amend legislation where necessary, develop guidelines for Boards, and to frame new umbrella legislation.*
- *In the interim, Treasury endorses statutory authorities reviewing their procedures for addressing conflict of interest matters and that, as a minimum, these procedures should ensure potential conflicts of interest are properly disclosed and recorded. Treasury would support Boards adopting a policy of the formal inclusion of Directors' Potential Conflicts of Interest in all Board meeting agendas to facilitate identification of potential conflicts at the outset. Where declarations are made, the Board is in a position to assess the extent of potential conflicts and make a subsequent decision on whether to have a director stand aside for consideration of the issue, or to participate in the discussion and/or the decision making process.*
- *Where the Board is unsure of the scope or complexity of a potential conflict of interest, it may be appropriate for the Treasury probity adviser, PricewaterhouseCoopers, or another probity adviser appointed by the Board, to review the circumstances before a decision is made.*

In relation to your request for input into the recommended future actions 3 and 4 of page 9, Treasury notes the Audit report indicates that a competitive selection process should be preferred wherever possible over cost based arrangements. This approach is supported by Treasury, as it is in keeping with government procurement policy that states 'all purchasing is to be conducted in an environment where open and effective competition is a prime operating principle'. It is evident that effective market testing for service delivery requires sound contract management, including effective monitoring and evaluation controls.

2 MANAGEMENT OF THE AGREEMENT'S FINANCIAL ARRANGEMENTS

INTRODUCTION

2.1 This Chapter considers the effectiveness of the Agents Board's management in ensuring REIACT was paid only the training grant funds to which it was entitled under the agreement made between it and the Board (the Agreement).

2.2 The Chapter describes the purposes and nature of the financial arrangements set out in the Agreement. The provisions in the Agreement which were intended to facilitate the Board managing the funding arrangements are outlined in the Chapter. An assessment is provided as to whether the Board effectively used the Agreement's provisions to manage the funding arrangements. The Chapter includes a summary of the actions which the Board carried out to manage the funding arrangements and assesses whether these actions were effective.

2.3 In preparing this Chapter, the Audit considered:

- the Agents Board's approach to the management of the Agreement's funding arrangements as evidenced in the Board minutes and related correspondence;
- the relevant provisions of the Agreement;
- the Agents Board's responses to evidence that REIACT was not complying with the Agreement;
- audit findings reported in later Chapters of this report;
- documentation relating to the training grant such as training grant financial reports, REIACT's training grant applications and other related correspondence; and
- comments provided by the Board in relation to the content of drafts of this Chapter.

SIGNIFICANT FINDINGS FROM THIS CHAPTER

- *The agreement between REIACT and the Agents Board provided a suitable framework for the Board to implement effective procedures to manage the financial arrangements related to the training grant program.*

- *Independent verification by REIACT’s auditors of the financial information provided by REIACT to the Board was expected to be the key component on which the Board would rely to satisfy itself that REIACT had complied with the training grant program’s financial arrangements.*
- *Reviews by the Board disclosed that the financial information and auditor’s reports could not be relied on as the Board had expected.*
- *The Board’s reviews of the financial information supplied by REIACT indicated that REIACT was not complying with various aspects of the Agreement.*
- *The several actions which the Board took when it became aware of the problems with REIACT’s compliance with the Agreement were sensible management actions and were as effective as the circumstances would allow.*
- *If certain procedures had been put in place by the Agents Board prior to the commencement of the Agreement the risk of REIACT not complying with the Agreement would have been significantly reduced.*

THE AGREEMENT’S FINANCIAL ARRANGEMENTS

The Agreement’s Intentions on Funding for REIACT

2.4 In its submission⁵ to the relevant Minister recommending that the Minister approve the provision of training grant funding to REIACT, the Agents Board stated that:

‘...the Board would not anticipate a significant hands-on role, however, control regarding the accountability of any funds provided to REIACT would be exercised through the agreement that the Board would enter into with REIACT should you approve the Board’s submission. That agreement would provide adequate opportunity for the Board to discontinue funding should any aspect not be satisfactory.’⁶

⁵ Agents Board’s submission dated 26 September 1996 to the Minister for Business, Employment and Tourism. The Minister subsequently agreed to the Agents Board’s submission on 11 October 1996.

⁶ Paragraph 6 of the Agents Board’s submission dated 26 September 1996 to the then Minister for Business, Employment and Tourism.

Audit Comments

2.5 The submission effectively advised the Minister that the content of the Agreement would create the means to facilitate the Board holding REIAC T accountable for its use of training grant funds. The submission also made the significant point that the Agreement would allow the Board to discontinue funding if any aspect of REIAC T's performance was unsatisfactory.

2.6 In effect the Board did not intend that the arrangements being put in place would prevent non-compliant expenditure being made by REIAC T. Rather the intention was that the Board would have the ability to react effectively if information provided retrospectively by REIAC T and/or REIAC T's auditors indicated that non compliance was occurring. The arrangements allowed the Board to discontinue funding and recover any non-compliant expenditure.

General Nature of the Agreement's Financing Arrangements

2.7 The Agreement contains no provision for REIAC T to earn profits from delivering the training program. Similarly it provides for the Board to pay no more to REIAC T than REIAC T's actual costs. The Agreement sets an upper limit on the total amount which can be paid to REIAC T and as well identifies upper limits for specific categories of expenditure. The Agreement includes 'rules' for accounting for the funds advanced.

2.8 Although payments to REIAC T were to be made annually in advance, the Agreement was essentially a cost based funding arrangement since the Agreement required REIAC T to repay to the Board any unexpended portions of the advance payments.

BOARD'S MANAGEMENT OF THE FINANCIAL ARRANGEMENTS

2.9 The Agreement contained several provisions to facilitate the Board's management of the financing arrangements.

2.10 In summary the provisions:

- required REIAC T to maintain good financial records (including records supporting its expenditure);

- required REIACT to provide audited and unaudited financial reports to the Agents Board on its expenditure of training grant funds; and
- allowed the Agents Board to obtain further information from REIACT on training grant matters.

Audit Comments

2.11 In the Audit's view the provisions in the Agreement provided a suitable framework for the Board to implement effective procedures to manage the Agreement's financial arrangements.

Intended Use of Audited Financial Reports

2.12 Reviews by the Board of the audited financial reports provided to the Board by REIACT would have been expected to be the prime source for the Board to confirm that expenditure which had been charged by REIACT against the grant funds complied with the Agreement.

2.13 If the audited financial statements indicated that expenditure had not been in compliance with the Agreement the Board had the power to obtain further information from REIACT, obtain repayments from REIACT, and, if necessary, terminate the Agreement.

2.14 Given the importance of the audited financial reports to the Board's management of the financial arrangements some further brief explanatory comments follow.

2.15 To enable the Board to confirm that REIACT was complying with the Agreement's financial arrangements, the Agreement required an independent audit to be performed on the financial reports provided by REIACT to the Board. Under the Agreement, REIACT was required:

‘at the end of each calendar year and at the expense of the service provider [i.e REIACT] have its books of accounts of the Program audited and provide a copy of the audited accounts to the Board within ninety days of the end of the calendar year. The audit certificate is to state that the funds provided by the Board have been expended for the purposes set out in this Agreement’.

2.16 The provision set out in the previous paragraph required REIACT to arrange for its auditor to examine evidence which supported the

expenditure REIACT had charged against training grant funds and to provide a written report to the Board on whether the expenditure shown in the financial report was properly related to training grant activities. An unqualified audit report would indicate that sufficient and appropriate supporting evidence had been sighted by the auditor to confirm that the expenditure shown in the financial report properly related to training grant activities.

2.17 It should be noted that REIACT's auditors had no legal relationship with the Board and owed no contractual duty of care to the Board.

Audit Comments

2.18 As stated previously, the provisions in the Agreement created a sound framework for the Board's management of the Agreement's financial arrangements. Independent verification and report by REIACT auditors was the key component of the framework.

PROCEDURES FOLLOWED BY THE BOARD

2.19 The procedures which the Board followed are outlined following.

Board's Recognition that Problems Potentially Existed

2.20 During the first and second year of the Agreement it became apparent to the Board that REIACT was not complying with the Agreement. Indicators noted by the Board that REIACT were not complying included:

- the financial reports provided by REIACT were not in the format required by the Agreement;
- the reports, although not in the format required, indicated that the estimates which had formed the basis for setting the first year's funding were likely to have been significantly understated; and
- the level of the expenditure being charged seemed excessive.

2.21 The Board was satisfied before the end of the first year of the three years of the training program that REIACT had not properly accounted for funds advanced under the particular headings set out in the Schedule to the Agreement. The Board, however, was of the view that

this was probably a result of ‘teething problems often encountered at the beginning of a project or program’. The Board took the following steps:

- the Deputy Chair reviewed REIACT’s accounting for funds advanced for the first year; and
- after the Deputy Chair’s review, it made appropriate adjustments to reduce the second year’s funding subject to the submission of the audit report.

2.22 Documentation reviewed by the Audit indicates that the Board subsequently made significant attempts to persuade REIACT to comply with the Agreement short of terminating the Agreement. Minutes of Board meetings indicate that the Board, because of the perceived benefits of the training courses, was unwilling to terminate the Agreement even though it was aware that significant non compliance with the Agreement by REIACT was occurring⁷. One member strongly recommended the Agreement be terminated.

2.23 As indications emerged that REIACT was not complying with the Agreement the Board responded by taking ‘a number of actions’.

2.24 The Board took these actions as neither REIACT nor its auditors were supplying the Board with timely or reliable information. Over a lengthy period Board representatives held discussions with REIACT and its auditors and correspondence was exchanged. The discussions and correspondence however did not resolve the situation.

2.25 The Agents Board eventually addressed REIACT’s non compliance with the Agreement by requesting an audit of the financial aspects of the training grant to be performed by the Auditor-General’s Office. This request was made prior to the Board suspending further payment i.e. third year funding was not paid to REIACT.

2.26 As would be expected the Board’s procedures could not ensure that funding advanced would be actually expended for training grant purposes. The procedures were effective for identifying that problems existed however they were not effective in solving the problems. The results from the Audit’s review of REIACT’s claims about its

⁷ Meeting No. 98/9 of 22 September 1998.

expenditure from the funding advanced by the Board disclosed in *Chapter 3 Training Grant Expenditure*.

2.27 As indicated previously, the Board did not anticipate a significant “hands on role” regarding its management of the Agreement’s financing arrangements. The primary provisions upon which the Board intended to rely were the six monthly unaudited and the annual audited financial reports prepared by REIACT for review by the Board together with monitoring by the Board’s Deputy Chair who has experience in these types of matters.

2.28 As it eventuated the audited financial reports could not be relied upon by the Board because:

- the financial reports were not in a form which facilitated a direct comparison of actual expenditure on the Agreement’s approved funding categories with the approved amounts;
- information arising from the audit process was not available to the Board until after further training funds had been paid to REIACT; and
- a significant amount of expenditure included in the audited reports was incorrectly charged and/or inadequately supported by evidence.

Audit Comments

2.29 The Board was confronted with a difficult problem. When the Agreement with REIACT had been arranged the Board’s expectations were that it would be able to rely on the information provided to it by REIACT and REIACT’s auditors. This turned out not to be the case.

2.30 On one hand the Board was generally of the view that the training courses being provided by REIACT were producing beneficial results in the sense of improving real estate practices in the ACT. On the other hand there were indications that REIACT was not complying with the Agreement’s requirements in relation to the financial arrangements.

2.31 The Audit has carefully considered the circumstances which existed and the actions taken by the Board. The Audit is of the view that the actions taken were sensible management actions and were as effective as the circumstances would allow.

ACTIONS WHICH IF UNDERTAKEN MAY HAVE ASSISTED MANAGEMENT OF THE AGREEMENT

2.32 The previous parts of this Chapter outlined problems which the Board encountered in its management of the Agreement's financial arrangements. The Audit is of the view that the problems may have been avoided if the Board had taken certain actions prior to the commencement of the Agreement. These actions are:

- the Board could have analysed the likely training costs in more detail and agreed a regime for the charging of these costs with REIACT. This 'charging regime' would have set the basis for charging each category of costs along with associated supporting documentation requirements;
- the Board could have settled with REIACT on a format for the financial reports. The agreed format should have been one which allowed a direct comparison with the approved categories and amounts of expenditure. The Board should have required REIACT to provide explanations on significant variations from the amounts approved under each funding category;
- the Board could have ensured that the Agreement included a requirement that a satisfactory audit report on the annual financial report was to be issued before further training funds would be provided; and
- the Board could have briefed the auditors on how the auditors' work would be used. Had the Board taken steps to ensure that the auditor understood the Agreement, the associated funding arrangements and the agreed basis for the charging of expenditure to the training grant, there would have been more likelihood that the audit process would have served the purpose which the Board expected.

2.33 The Audit acknowledges that the outlined procedures would not have ensured that REIACT would implement proper systems and provide reliable financial reports or that the independent auditor would have correctly certified the expenditure charged to training grant funds. However, the Audit considers that the procedures would have significantly reduced the risk of REIACT not complying with the Agreement. The audit process would have been more effective if the audit certification had been required prior to provision of further funds and the auditor had been able to refer to a Board and REIACT agreed

cost charging regime to assess whether expenditure was being correctly charged to the training grant.

CONCLUSION

2.34 The Audit has concluded that the management actions which the Board took once it became aware that there were problems were sensible responses. The responses, however, may not have been necessary if appropriate actions had been taken prior to the commencement of the Agreement.

3 TRAINING GRANT EXPENDITURE

INTRODUCTION

3.1 This Chapter outlines the requirements in the Agreement between the Agents Board and REIACT which applied to the expenditure of training grant funds. The Chapter also includes an assessment of whether REIACT complied with these requirements.

3.2 The Audit:

- reviewed the Agreement's requirements regarding REIACT's use of training grant funds and maintenance of financial records;
- reviewed the financial reports submitted to the Agents Board by REIACT;
- examined payments made from training grant funds and related supporting documentation;
- reviewed explanations obtained from REIACT on certain expenditure;
- considered comments provided by the Agents Board, REIACT and its auditors in relation to the opinions expressed in this Chapter; and
- considered a legal opinion prepared by the ACT Government Solicitor on the interpretation of the Agreement and its application to training grant expenditure.

SIGNIFICANT FINDINGS FROM THIS CHAPTER

- *A majority of expenditure charged to the training grant funds complied with the Agreement.*
- *Even though a majority of expenditure complied with the Agreement approximately 25% to 34% of this expenditure was incorrectly charged.*
- *Based on the available information, the Audit estimates that \$67,500 to \$88,300 was incorrectly charged to the training grant funds.*

KEY REQUIREMENTS OF THE AGREEMENT FOR EXPENDITURE

3.3 *Clause 7.2* of the Agreement states:

‘The Service Provider (i.e. REIACT) shall apply the funding for the purposes of developing, co-ordinating or delivering, as the case may be, the Program and associated administrative costs and for no other purpose.’

3.4 *Clause 5.1* of the Agreement states:

‘The Service Provider (i.e. REIACT) undertakes to:

(a) keep at all times proper and adequate books of account in relation to the Program;

(b) record all expenditure relating directly or indirectly to and all income arising directly or indirectly from the Program, separate from all other income and expenditure of the Service Provider; and

(c) at the end of each calendar year and at the expense of the Service Provider, have its books of accounts of the Program audited and provide a copy of the audited accounts to the Board within ninety (90) days of the end of the calendar year. The audit certificate is to state that the funds provided by the Board have been expended for the purposes set out in this Agreement.’

3.5 *Clause 7.5* states:

‘In the event that the Service Provider’s actual costs are less than the amount of the approved funding any excess funds are to be repaid to the Board.’

Audit Comments

3.6 The effects of the clauses set out are that:

- REIACT expenditure was only to be charged to the training grant funds if the expenditure had been incurred in developing, delivering and coordinating the approved training program;
- REIACT was required to maintain proper and adequate records of all expenditure charged; and

- REIACT was required to provide regular financial reports of its training program expenditure to the Agents Board.

Expenditure Charged Against the Training Grant Funds

3.7 The following Summary of Transactions to 31 December 1998 shows that REIACT, according to its records, spent \$20,324 more on the training program than the total of the grants provided to it. The table also shows the results of the Audit’s review of REIACT expenditure. The Audit figures show that REIACT expenditure was at least \$47,191⁸ less than the total of the grants provided to it.

	REIACT \$	Audit \$
Expenditure	262,247	194,732
Less income	27,141	27,141
Net expenditure	235,106	167,591
Grants provided	214,782	214,782
Expenditure in excess of grants provided	\$20,324	
Excess of grants provided over expenditure		(\$47,191)

3.8 The grants of \$214,782 shown in the summary comprise the first two years grants provided for in the Agreement. At the time of this report, the third year grant had not been paid to REIACT pending the results of this audit.

3.9 The Agents Board is currently assessing the continued provision of training grant funds to REIACT. It is the Audit view that at least \$47,191⁹ should be refunded by REIACT to the Agents Board.

⁸ This calculation is based on a conservative audit estimate of \$67,515 in non complying expenditure reported in Chapter 3 of this report. If a narrower legal interpretation received from the ACT Government Solicitor was adopted then the amount of non complying expenditure would be \$88,312 and the excess of grants provided over expenditure would be \$67,988.

⁹ \$67,988 should be returned to the Agents Board if the narrower legal interpretation received from the ACT Government Solicitor was to be adopted.

THE AUDIT'S REVIEW OF EXPENDITURE CHARGED

Introduction

3.10 The Audit reviewed all payments and related supporting documentation for the period from 11 November 1996 to 30 June 1998.

3.11 Where the available supporting documentation, financial records and explanations from REIACT did not provide sufficient and appropriate evidence that the expenditure complied with the Agreement's requirements, the expenditure was brought to the attention of REIACT and the Agents Board. The Audit requested further information from REIACT on the apparently non complying expenditure.

3.12 In several cases the Audit was unable to form a view on whether or not expenditure charged to the training grant funds complied with the Agreement. This inability to form a view was the result of REIACT's records and/or responses not being sufficiently reliable, complete or comprehensive to permit the Audit to evaluate whether the expenditure was complying or non complying.

Audit Comments

3.13 The Audit's review showed that a majority of expenditure complied with the Agreement in that the expenditure was incurred for the purposes of developing, co-ordinating or delivering the training program. The review however also showed that there were significant charges which did not comply with the Agreement.

3.14 The Audit attempted to assess the reasonableness of the amounts charged for which supporting records and responses were inadequate. In some of the cases the charges seemed reasonable and therefore were accepted as being correctly charged against training grant funds.

3.15 The Audit acknowledges that the Agents Board could validly assess the entire amount of inadequately supported expenditure as non complying. This approach would be supported by a legal advising provided by the ACT Government Solicitor which, in reference to the appropriate interpretation of the provisions of the Agreement, states that 'clearly this provision places an onus on REIACT to have appropriate supporting documentation for all expenditure incurred in relation to the program'.

INCORRECT AND INADEQUATELY SUPPORTED EXPENDITURE

3.16 The following table summarises the results of the Audit work outlined in the preceding part of this Chapter.

Table 3.2: Estimate of Non Complying Expenditure

Expenditure Category	(A) Amount Incorrectly Charged	(B) Charges not Supported by Adequate Documentation	(A) + (B) Total of Incorrect Charges and Charges Not Supported by Adequate Documentation
	\$	\$	\$
Rent of Training Room and Other Facilities	40,153 ¹⁰	0	40,153
Telephone	5,411 ¹¹	4,220	9,631
Seminars and Conferences	0	0	0
Fringe Benefits Tax	0	578	578
Post Course Functions	0	0	0
Photocopying	3,533	0	3,533
Speakers, Catering and Other Costs	18,023 ¹²	879	18,902
Legal	395	0	395
Administration	0	15,120	15,120
	\$67,515	\$20,797	\$88,312

¹⁰ *Rent of Training Room and Other Facilities* – Although provided with the opportunity REIACT did not provide any information supporting the costs it claims to have incurred in providing training room and other facilities. REIACT advised it considers that, as a result of providing a training room and office in its premises, it has foregone revenue. The foregone revenue is the rent it would have been paid if it had leased the training space to another party. The Agreement however provides only for actual costs to be met from training grant funds. Foregone revenue is therefore not relevant.

¹¹ *Telephone* – the audit has accepted the amount of \$4,220 as reasonable. However, the Agents Board could treat the entire amount as non complying as there are no records to support the amount estimated to be complying.

¹² *Speakers, Catering and Other Costs* – the non complying amount of \$18,023 is comprised of a 1998 amount of \$11,593 acknowledged by REIACT as non complying and an amount of \$6,430 estimated by the audit. The entire amount of \$18,902 claimed for *speakers and catering* could be treated as non complying as REIACT did not provide sufficient and appropriate documentation to the audit to support the charge.

CONCLUSION

3.17 As shown in the above table, the Audit estimates that \$67,515 to \$88,312¹³ of the total of \$262,247 charged to the training grant funds was incorrectly charged.

¹³ The figure of \$67,515 is a conservative audit estimate that makes some allowance for expenditure that was reasonable but not fully supported by direct evidence. The higher estimate of \$88,312 treats all expenditure not properly supported by direct evidence as non complying in accordance with the advice received from the ACT Government Solicitor.

4 RECORDING GRANT EXPENDITURE

INTRODUCTION

4.1 This Chapter describes the Agreement's requirements for recording the expenditure of training grant funds and assesses whether the requirements were complied with.

4.2 In forming the opinions expressed in this Chapter, the Audit:

- examined the accounting system and related supporting records used by REIACT to record expenditure relating to grant funded programs; and
- considered comments provided by the Agents Board, REIACT and its auditors in relation to the opinions expressed in this Chapter.

SIGNIFICANT FINDINGS FROM THIS CHAPTER

- *REIACT did not maintain proper and adequate books of account for training grant expenditure as required by the Agreement.*

KEY AGREEMENT REQUIREMENTS

4.3 Under Clause 5.1(a) of the Agreement REIACT is required to maintain proper and adequate accounting records of its expenditure of training grant funds.

Audit Comments

4.4 The Agreement's requirement to maintain proper accounts extends beyond the maintenance of an adequate accounting system. It requires that expenditure related to the delivery of training grant activities be accounted for separately from other REIACT expenditure and that expenditure be properly supported by sufficient and appropriate evidence.

PROPER AND ADEQUATE BOOKS OF ACCOUNT

4.5 All expenditure charged to the training grant was processed by REIACT through a widely used accounting software system, known as

‘Mind Your Own Business’ (MYOB). Posting codes have been established for the training grant within MYOB allowing for separate accounting and reporting of training grant activities. Separate cheque books are maintained for training grant program costs and all expenditure is recorded to a training grant posting code.

Audit Comments

4.6 The Audit verified that payments made during the period 11 November 1996 to 30 June 1998 were posted to the appropriate training grant posting code and that the accounting system was being used.

4.7 The Audit view is that REIACT has maintained an adequate accounting system.

4.8 Although REIACT has maintained an adequate accounting system REIACT has not complied with *Clause 5.1(b)* of the Agreement to maintain proper and adequate books of account.

4.9 The opinion is based on incorrect expenditure being recorded in REIACT’s accounting system and the inadequacy of supporting expenditure records, rather than the system itself.

CONCLUSION

4.10 REIACT’s incorrect charging of significant amounts of expenditure to training grant funds and REIACT’s inability to provide sufficient and appropriate documentation for a significant amount of the charges are described in *Chapter 3 Training Grant Expenditure*. The incorrect charging and the lack of supporting documentation is sufficient evidence to conclude that REIACT did not maintain proper and adequate books of account for training grant expenditure as required by the Agreement.

REIACT’S COMMENTS ON THE AUDIT CONCLUSION

4.11 REIACT has responded that:

‘we disagree with the opinion that proper books of account were not maintained for the training grant as required by the Agreement.

We concede that there have been lapses in the quality of the accounting records, which we attribute to the high level of turnover of our accounting staff. We also concede that some items of expenditure have been claimed in error. We acknowledge that the Auditor-General takes a view in respect of certain items, such as legal costs and rent which differs from our interpretation in the way in which the grant should be administered. We do not agree that these lapses and differences of interpretation constitute a failure to maintain proper and adequate records¹⁴.

Audit Comments

4.12 The Audit maintains that the lapses in the accounting records and the absence of supporting documentation noted in *Chapter 3 Training Grant Expenditure*, are significant and represent a breach of the Agreement's requirement to keep 'proper and adequate' records.

¹⁴ REIACT's letter of 2 March 2000.

5 TRAINING GRANT REVENUE

INTRODUCTION

5.1 This Chapter describes the Agreement’s requirements relating to revenue derived from the training courses to be delivered by REIACT under the Agreement. The Chapter also outlines the audit work performed and evidence obtained to support the significant findings from the Chapter in relation to training grant revenue.

5.2 In forming the opinions expressed in this Chapter, the Audit reviewed:

- the Agreement’s requirements relating to training grant revenue;
- REIACT’s accounting records for recording training programs revenue;
- REIACT’s reporting of revenue in its annual financial statements;
- the audit workpapers prepared by REIACT’s auditors; and
- considered any comments provided by the Agents Board, REIACT and its auditors in relation to the opinions expressed in this Chapter.

SIGNIFICANT FINDINGS

- *The Agreement required the written consent of the Board before REIACT was permitted to run specific courses using grant funds.*
- *As courses were run and fees were charged for training courses without written consent from the Agents Board, revenue has not been derived in accordance with the Agreement.*

CHARGING FEES

5.3 The following table shows fees received by REIACT from the training grant courses:

Table 5.1: Fees Received by REIACT

AGENTS BOARD – FINANCIAL ADMINISTRATION OF TRAINING PROGRAM GRANT

Training Course	1997	1998
	\$	\$
Introduction to Residential Property Management	2,730	—
Real Estate Sales and Marketing	9,463	—
Principals’ Refresher Workshops	3,955	8,460
	\$16,148	\$8,460

AGENTS BOARD APPROVAL FOR CHARGING FEES

5.4 Under the Agreement REIACT was not permitted to charge fees for training courses provided under the Agreement without the Agents Board’s prior written consent.

5.5 *Clause 3.3* of the Agreement states:

‘The Service Provider (i.e. REIACT) will not charge any course fees or costs for any part of the Program described in Schedule 1 of this Agreement without the prior written consent of the Board.’

Audit Comments

5.6 REIACT did not obtain prior written consent from the Agents Board for charging fees or recovering costs for the ‘Principals’ Refresher Workshops’ it conducted. REIACT therefore did not comply with the Agreement.

CONCLUSION

5.7 REIACT ran unapproved courses and charged fees for training courses without obtaining the prior written consent from the Agents Board required by the Agreement. This is probably an indication that REIACT did not understand its Agreement with the Agents Board.

6 FINANCIAL REPORTING

INTRODUCTION

6.1 This Chapter describes the Agreement's requirements for REIACT's financial reporting to the Agents Board. The Chapter also outlines the audit work performed and evidence obtained to support the significant findings from this Chapter in relation to financial reporting.

- 6.2 In forming the opinions expressed in this Chapter, the Audit:
- reviewed the Agreement's financial reporting requirements;
 - examined the financial reports provided by REIACT to the Agents Board; and
 - considered any comments provided by the Agents Board, REIACT and its auditors in relation to the opinions expressed in this Chapter.

SIGNIFICANT FINDINGS FROM THIS CHAPTER

- *REIACT did not comply with its financial reporting obligations under the Agreement.*
- *Financial reports submitted by REIACT to the Agents Board were unsuitable for assessing the financial accountability of REIACT.*

KEY REPORTING REQUIREMENTS

6.3 Reporting requirements were clearly described in the Agreement.

6.4 *Clause 5(1)(c)* of the Agreement requires annual audited financial statements as follows:

‘at the end of each calendar year and at the expense of the Service Provider (i.e. REIACT), to have its books of accounts of the Program audited and provide a copy of the audited accounts to the Board within 90 days of the end of the calendar year. The audit certificate is to state that the funds provided by the Board have been expended for the purposes set out in this Agreement.’

6.5 The Agreement also required REIACT to provide half yearly unaudited financial reports to the Board. *Clause 5.3* requires REIACT to advise of its progress in respect of the Program, including the level of success in meeting objectives and shall include an accounting of the expenditure and acquittal of the funds in accordance with the headings referred to in the Agreement.

Audit Comments

6.6 In summary, clear requirements were set for REIACT to provide audited calendar year financial reports and unaudited six monthly financial reports to the Agents Board on its training grant activities.

COMPLIANCE WITH FINANCIAL REPORTING REQUIREMENTS

6.7 The Audit reviewed the financial reports received by the Agents Board and compared these reports to the Agreement’s requirements.

6.8 The financial reports did not comply with the Agreement’s requirements in important respects as follows:

- the audited financial reports were not always provided within 90 days of the end of the calendar year;
- unaudited financial reports were not provided within six months of the initial transfer of funds; and
- REIACT’s audited and unaudited financial statements did not follow the formats prescribed in the Agreement. It was not possible therefore, to directly compare the expenditure charged against training grant funds as per the financial reports to the expenditure approved in the Agreement.

CONCLUSION

6.9 REIACT did not comply with its financial reporting obligations under the Agreement.

7 CONFLICT OF INTEREST ISSUES

INTRODUCTION

7.1 The community has a right to expect that public sector staff and officials (including Statutory Authority Board members) will perform their duties in a fair and balanced way and that decisions they make are not affected by self interest or personal gain. Conflicts of interest arise where public sector staff or officials are influenced or appear to be influenced by self interest or personal gain when performing their duties. The perception of a conflict of interest can be as damaging as an actual conflict because it undermines confidence in the integrity of the organisation involved and its officials.

7.2 At Agents Board meetings where REIACT matters were being considered Board members were in attendance who were REIACT directors at the same time as being Agents Board members. This raised a question for the Audit to review as to whether conflict of interest issues, potential or actual, were properly dealt with.

7.3 It should be noted that no evidence came to notice during the conduct of the Audit which indicated that the REIACT directors used their positions on the Agents Board for any purpose of self-interest, personal gain or impropriety.

7.4 In forming the opinions expressed in this Chapter the Audit considered the:

- legislative requirements contained in the *Agents Act 1968* for Board members in relation to conflicts of interest (Section 16(8)); and
- Board member's fiduciary duties relating to conflicts of interest.

7.5 The Audit considered legal advice on the interpretation of Section 16(8) and on directors' fiduciary duties to avoid conflicts of interest.

SIGNIFICANT FINDINGS FROM THIS CHAPTER

- *There was no formal record of disclosure of the REIACT directorships to the Board.*

- *Conflicting and inconclusive information was provided to the Audit on the disclosures made by the REIACT directors.*
- *The conflict of interest provisions in recent legislation creating statutory authorities are significantly broader in their application to conflict of interest situations than the Agents Act (1968); recent legislation includes clearer procedures for the disclosure of conflict of interests and subsequent actions.*

POTENTIAL CONFLICT OF INTEREST

7.6 As previously stated, there were directors of the Agents Board who were also REIACT directors when the Board considered REIACT matters. (These directors are referred to as ‘REIACT directors’ in this Chapter.)

7.7 The REIACT matters considered by the Agents Board included deliberations on REIACT’s first and second applications for training grant funding and REIACT’s non compliance with the Agreement¹⁵.

7.8 The presence of members of the Agents Board who were also directors of REIACT created potential for a conflict of interest to arise.

7.9 The following comments provide an overview of the Board’s actions, as the Audit understands them, in relation to the conflict of interest issues.

BACKGROUND

7.10 The Board minutes indicate that, over the period of the training grant, the Board considered REIACT’s training grant applications, course content and other training grant matters. REIACT directors were on the Agents Board for much of this period.

¹⁵ From 26 February 1996, the period when the Agents Board invited REIACT to provide its views on the possible uses of the Agents Board’s surplus funds, REIACT’s application for the funding of 1 April 1996 to the Agents Board approval of the first year’s training grant on 11 October 1996 there was one member of the Board of the Agents Board who was on the Board of REIACT.

There were two members of the Board of the Agents Board who held positions on the Board of REIACT during the period from 22 July 1997. During this period, REIACT submitted its application for second year funding, the Agents Board was reviewing REIACT’s application and was considering reports of REIACT’s non-compliance with the Agreement.

7.11 Over this period the Board's concerns relating to REIACT's administration of the Agreement increased. In September 1998 the Board considered whether to terminate its Agreement with REIACT¹⁶.

7.12 Concerns regarding the 'probity of Board decisions in relation to the administration and acquittal of the Board's grant program' were raised in a later Board meeting held on 1 December 1998¹⁷. The Chair advised the Board that the ACT Government Solicitor had been requested to provide a legal opinion on the potential conflict of interest¹⁸.

7.13 The ACT Government Solicitor advised that 'there would be a clear conflict of interest on the part of any Board member who was also a REIACT director when the Board considered matters relating to the REIACT grant'. The Solicitor also advised that he 'had not concluded that a breach of Section 16(8) of the Act had occurred'¹⁹. (Comments on Section 16(8) are provided later in this Chapter.) The Solicitor recommended that the Board should (if it had not already done so) implement a framework within which such issues could be dealt with. Following this legal advice the REIACT directors agreed to adopt a 'cautious approach' to conflict of interest matters and absent themselves from any Board deliberations on the training grant²⁰.

7.14 The Board accepted that the REIACT directors had not received a direct benefit from the REIACT grant. The Board also accepted that the REIACT directors had not acted dishonestly or improperly and that any possible conflict of interest that might have occurred had arisen from oversight²¹.

7.15 Nevertheless, to provide itself with some assurance that decisions affecting REIACT were not unduly affected by the presence of REIACT directors on the Board, the Board agreed to review two important decisions in relation to the training grant²². As a result of the review the Board confirmed its earlier decision to:

¹⁶ Agents Board – Board Meeting No. 98/9 of September 1998.

¹⁷ Agents Board – Board Meeting No. 98/13 of 1 December 1998.

¹⁸ Agents Board – Board Meeting No. 98/13 of 1 December 1998

¹⁹ Agents Board – Board Meeting No. 98/14 of 16 December 1998.

²⁰ Agents Board – Board Meeting No. 98/14 of 16 December 1998.

²¹ Agents Board – Board Meeting No. 98/14 of 16 December 1998.

²² Agents Board – Board Meeting No. 98/14 of 16 December 1998.

- approve the second year’s application for training grant funding; and
- obtain an independent evaluation of the effectiveness of training grant program and the accountability of grant funds.

7.16 The Board also undertook to advise the Minister of the potential conflict of interest²³.

7.17 The following comments consider the Agents Act’s legislative requirements in relation to conflict of interest matters.

SECTION 16(8) OF THE AGENTS ACT (1968)

7.18 Section 16(8) of the *Agents Act (1968)* states that:

‘A member of the Board shall withdraw from any meeting of the Board when ... another matter *directly affecting* the member is being dealt with by the Board’ (emphasis added).

Legal Interpretations of Section 16(8)

7.19 Legal opinions on interpretation of this section differ.

7.20 The ACT Government Solicitor recognised that the words ‘directly affecting the member’ were capable of either a broad or narrow interpretation but concluded that a broad interpretation should be adopted. The Solicitor said ‘in my opinion it is reasonable to conclude that matters relating to the grant by the Board to REIACT are matters directly affecting a member who is a director of REIACT.’

7.21 However, even though the advice indicated a broad interpretation of the section was possible, the advice stopped short of concluding that there had been a breach of Section 16(8).

7.22 Legal advice provided to the REIACT directors argued that the specific use of the term ‘directly affecting’ drew a narrower interpretation. The advice was that the REIACT directors were entitled to

²³ Agents Board – Board Meeting No. 98/14 of 16 December 1998.

participate in the Board’s deliberations on the REIACT grant and need not withdraw from the Board’s considerations²⁴.

Audit Comments

7.23 Under Section 16(8), there is no discretion provided to the Board to permit a director to participate in matters which ‘directly affect’ that particular director. Once it has been established that a matter ‘directly affects’ a director, the director is compelled to immediately withdraw from the meeting.

7.24 The ACT Government Solicitor’s advice stopped short of concluding that a breach of Section 16(8) had occurred. Other legal advice provided to the REIACT directors suggests that the use of the word ‘directly’ in Section 16(8) significantly restricts the potential application of this section.

7.25 It is doubtful that the matters discussed by the Board ‘directly affected’ the REIACT directors in a legal sense. Consequently, the REIACT directors were not legally required by the provisions of the Agents Act to withdraw from meetings when the REIACT matters were being considered.

7.26 The restrictive application of Section 16(8) appears to be at odds with legislative intentions as expressed in recent legislation establishing ACT statutory authorities. The question as to whether the existing legislation provides an appropriate framework for addressing conflict of interest issues is considered later in this Chapter.

FIDUCIARY DUTIES

7.27 Fiduciary duties also apply to directors. These duties apply in addition to the legislative responsibilities imposed by Section 16(8). Fiduciary duties require directors to always act in the interests of the entities of which they are directors. A director is required to:

- (a) act honestly and in the interests of the [entity] as a whole;

²⁴ Elrington Boardman Allport advice of 7 December 1998 and Phelps Reid advice of 21 December 2000.

- (b) exercise powers for the purpose for which they were conferred and not for any collateral or improper purpose; and
- (c) avoid being placed in the position of conflict of interest²⁵.

7.28 The following sections consider the fiduciary duty of Agents Board directors to avoid being placed in a position of conflict of interest.

7.29 The ACT Government Solicitor advised that:

‘the primary relevant fiduciary obligation is on the individual Board member to avoid actual or potential conflicts of interest relating to that member. Other members of the Board would not normally be responsible for a breach of duty by an individual member. This does not mean that the Board members can ignore issues relating to conflict of interest on the part of another Board member, as this could raise a suggestion that the Board members are not promoting the purposes for which the Board exists’²⁶.

7.30 The ACT Government Solicitor also recommended that the Board implement procedures for formally disclosing director’s interests and for the conduct of Board meetings when a conflict arises. The ACT Government Solicitor recommended that the Board should, if it had not already done so, adopt:

- procedures for obtaining, from each of its members, a declaration of interests; and
- policies and procedures so that, unless otherwise determined by the Board, a member does not receive any papers, and does not participate in any meetings of the Board, concerning a matter in which the member has an interest²⁷.

7.31 A further consideration relates to disclosure of a potential conflict of interest by a Board member. Legal advice provided to the REIACT directors included that fiduciary obligations require a board member to divulge, by full disclosure to the Board, any matter which may impact upon the decision making processes in terms of any potential conflict of interest or perceived conflict of interest. It then becomes a matter for the Board to form a view as to whether in all the circumstances it is

²⁵ ACT Government Solicitor’s letter of 4 December 1998.

²⁶ ACT Government Solicitor’s letter of 28 February 2001.

²⁷ ACT Government Solicitor’s letter of 4 December 1998.

appropriate for the member to remain involved in the Board’s decision making process on the particular issue.²⁸

Audit Comments

7.32 The Audit acknowledges that the presence of REIACT directors on the Agents Board would not have automatically impaired the Board’s overall independence in its consideration of REIACT matters. There were only two REIACT directors on the Board. Consequently a significant majority of the seven member Board was independent of REIACT.

7.33 The Audit is of the view that membership of both Boards would not have, of itself, automatically created a conflict for every training grant issue. For example, REIACT directors may have beneficially used their industry experience to provide information to other Board members on industry training needs and the general relevance of the content of the training grant courses. The Audit, however, is also of the view that when the Board was considering REIACT’s non compliance with the Agreement, a potential conflict of interest situation existed for the REIACT directors.

7.34 The legal advice indicates that, as part of meeting their fiduciary duty to avoid being placed in an actual position of conflict of interest, the REIACT directors should have fully disclosed to the Board the potential for a conflict of interest situation to arise. The Board would then have had the responsibility to appropriately address the potential conflict situation.

Disclosure by the REIACT Directors

7.35 To clarify the situation on disclosure by the REIACT directors the Audit requested further information on any disclosures made.

7.36 The Agents Board advised the Audit that most if not all of the other Board members were aware that the REIACT directors were members of REIACT and were or had some level of involvement in REIACT’s affairs. The Agents Board, however, also advised that the Board members were not aware of the specifics of this involvement until

²⁸ Phelps Reid advice of 21 December 2000 to (names supplied).

the ACT Government Solicitor's legal opinion was provided to them in December 1998²⁹.

7.37 The Registrar has no record of formal disclosures to him by the REIACT directors³⁰.

7.38 The REIACT directors, in contrast to the information described in the previous paragraphs, advised the Audit that the other members of the Board were fully aware of their REIACT directorships. The REIACT directors advised the Audit of a number of documents provided to the Board, and other communications to the Board, which identified the directors as REIACT directors³¹. The directors stated the documents were provided, and the communications made, prior to REIACT's apparent non compliance being raised.

7.39 The REIACT Directors also advised that the annual reports of the Real Estate Institute provided to the Board each year contained details of the membership of the REIACT Board and as such, the REIACT directors contend the Board, through the Registrar, were on notice of the directors' position.

Audit Comments

7.40 The Audit considers that the potential conflict of interest situation was a matter that required clear and formal disclosure at a Board meeting. The Audit is satisfied that the required formal disclosures were not made. Disclosure by indirect means or by inference is inadequate and cannot be considered to constitute notice.

7.41 The disclosure should have provided details of the nature and extent of the interest and the relationship of the interests to the affairs of the Board, sufficient for the Board to have considered the significance of the interest in the particular circumstances. The disclosures if made should have been recorded in the Board minutes.

²⁹ Agents Board correspondence of 31 January 2001 to the ACT Auditor-General's Office.

³⁰ Agents Board letter of 7 March 2000, to (names supplied).

³¹ (Names supplied) letter of 18 February 2001 and 15 February 2001 respectively.

Conclusion

7.42 It seems that the Agents Board's processes for ensuring that Board members were aware of their duty to disclose actual conflict of interests, and also to disclose situations which could create perceptions of conflicts of interests were not effective. The Audit's view is that potential for conflicts of interest to arise clearly existed. It is also clear that the REIACT directors did not make formal disclosures of their interests.

7.43 Because of the restricted wording of the conflict of interest section in the Agents Act no legal breach of the Act actually occurred. The Audit's view is that the legislation should be amended. Further discussion on this follows.

REVIEW OF SECTION 16(8)

7.44 The wording in the conflict of interest provisions in more recent legislation establishing statutory authorities is considerably broader than the *Agents Act (1968)*. For example, Section 15 of the *Canberra Tourism and Events Corporation Act (1997)* states that:

'15.(1) *A member who has a direct or indirect pecuniary or personal interest in a matter which has been submitted for consideration by the Corporation shall disclose the nature of the interest at a meeting of the Corporation as soon as practicable after the relevant facts have come to the member's knowledge.* (emphasis added)

- (2) The member presiding at a meeting at which an interest is disclosed shall cause that disclosure to be recorded in the minutes of the meeting.
- (3) A member disclosing an interest shall not, unless the Minister or the Corporation determines otherwise-
 - (a) be present during any deliberation of the Corporation with respect to the relevant matter; or
 - (b) take part in any decision of the Corporation with respect to that matter.
- (4) A member disclosing an interest shall not-

- (a) be present during any deliberation of the Corporation with respect to a determination referred to in subsection (3); or
 - (b) take part in any decision of the Corporation with respect to such a determination.
- (5) The Chairperson shall give a written report to the Minister about any determination of the Corporation under subsection (3) specifying the nature of the interest disclosed and the reasons for the determination’.

7.45 Similar provisions exist in the *Stadiums Authority Act (2000)*.

Audit Comments

7.46 Recent legislation specifies that ‘indirect’ and ‘pecuniary interests’ must be disclosed by statutory authority directors. The Agents Act requires only ‘direct’ interests to be disclosed. The newer legislation is therefore significantly broader in its application to potential conflicts of interest situations than is the Agent’s Act.

7.47 The recent legislation requires directors to formally disclose potential conflicts of interest at each meeting and ensure that their disclosure is recorded in the minutes of that meeting. The legislation places the onus on the directors to review the matters before the Board for potential conflict of interest situations and make formal disclosure at each meeting if any potential situation exists. Under the legislation directors cannot rely on earlier disclosures or on assumptions that other Board members are aware of their interests. This is in contrast to the Agents Act which does not include these types of requirements.

7.48 The recent legislation sets out detailed procedures for the documentation of Board actions on conflict of interest matters. The *Agents Act (1968)* does not set out procedures for the Agents Board to follow.

7.49 Under the recent legislation a director with a conflict of interest is not necessarily required to withdraw from a meeting. A director may still take part in Board deliberations and decisions provided a Board/Ministerial determination is obtained. The legislation requires the Chair of the Board to provide a written report to the Minister specifying

the interest and the reasons for the Board's determination on the involvement (if any) of the director. The Agents Act does not include these requirements.

7.50 The Audit considers that the *Agents Act (1968)* does not provide an adequate legislative framework for addressing conflict of interest matters. Consideration should be given to bringing it into line with the more recent legislation.

Annexure

Reports Published in 1996

- 1 Legislative Assembly Members - Superannuation Payments/Members' Staff - Allowances and Severance Payments**
- 2 1995 Taxi Plates Auction**
- 3 VMO Contracts**
- 4 Land Joint Ventures**
- 5 Management of Former Sheep Dip Sites**
- 6 Collection of Court Fines**
- 7 Annual Management Report For Year Ended 30 June 1996**
- 8 Australian International Hotel School**
- 9 ACT Cultural Development Funding Program**
- 10 Implementation of 1994 Housing Review**
- 11 Financial Audits with Years Ending to 30 June 1996**

Reports Published in 1997

- 1 Contracting Pool and Leisure Centres**
- 2 Road and Streetlight Maintenance**
- 3 1995-96 Territory Operating Loss**
- 4 ACT Public Hospitals - Same Day Admissions
Non Government Organisation - Audit of Potential Conflict of Interest**
- 5 Management of Leave Liabilities**
- 6 The Canberra Hospital Management's Salaried Specialists Private Practice**
- 7 ACT Community Care - Disability Program and Community Nursing**
- 8 Salaried Specialists' Use of Private Practice Privileges**
- 9 Fleet Leasing Arrangements**
- 10 Public Interest Disclosures - Lease Variation Charges and Corrective Services**
- 11 Annual Management Report for Year Ended 30 June 1997**
- 12 Financial Audits with Years Ending to 30 June 1997**

Annexure (continued)

13 Management of Nursing Services

Reports Published in 1998

- 1 Management of Preschool Education**
- 2 Lease Variation Charges - Follow-up Review**
- 3 Major IT Projects - Follow-up Review**
- 4 Annual Management Report for Year Ended 30 June 1998**
- 5 Management of Housing Assistance**
- 6 Assembly Members' Superannuation and Severance Payments to Former Members' Staffers**
- 7 Magistrates Court Bail Processes**
- 8 Territory Operating Losses and Financial Position**
- 9 Financial Audits with Years Ending To 30 June 1998**
- 10 Management of Schools Repairs and Maintenance**
- 11 Overtime Payment To A Former Legislative Assembly Member's Staffer**

Reports Published in 1999

- 1 Stamp Duty on Motor Vehicle Registrations**
- 2 The Management of Year 2000 Risks**
- 3 Annual Management Report for Year Ended 30 June 1999**
- 4 Financial Audits With Years Ending to 30 June 1999**

Reports Published in 2000

- 1. Bruce Stadium Redevelopment — Summary Report**
- 2. Bruce Stadium Redevelopment — Value for Money**
- 3. Bruce Stadium Redevelopment — Costs and Benefits**
- 4. Bruce Stadium Redevelopment — Decision to Redevelop the Stadium**
- 5. Bruce Stadium Redevelopment — Selection of the Project Manager**
- 6. Bruce Stadium Redevelopment — Financing Arrangements**

Annexure (continued)

7. **Bruce Stadium Redevelopment — Stadium Financial Model**
8. **Bruce Stadium Redevelopment — Actual Costs and Cost Estimates**
9. **Bruce Stadium Redevelopment — Market Research and Marketing**
10. **Bruce Stadium Redevelopment — Stadium Hiring Agreements**
11. **Bruce Stadium Redevelopment — Lawfulness of Expenditure**
12. **Bruce Stadium Redevelopment — Governance and Management**
13. **Annual Management Report for the Year Ended 30 June 2000**

Reports Published in 2001

1. **Financial Audits with Years Ending to 30 June 2000**
2. **Enhancing Professionalism and Accountability**
3. **Market Research and Marketing (Second Report)**
4. **Peer-Based Drug Support Services Tender – 1998**
5. **The Administration of Payroll Tax**
6. **Annual Management Report for the Year Ended 30 June 2001**
7. **Managing Canberra Urban Parks and Open Spaces**
8. **Canberra Tourism and Events Corporation – Relocation of Brindabella Business Park**

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