

MEDIA RELEASE**18 December 2015**

2014-15 Financial Audits

Today, the ACT Auditor-General, Dr Maxine Cooper, presented the report on **2014-15 Financial Audits** to the Speaker for tabling in the ACT Legislative Assembly.

This report presents information on two key issues for the Territory:

- the financial sustainability of the ACT Government's strategies and policies, particularly when assessed over time – as reflected in the financial operating results (operating balance and operating surplus/deficit); and
- the capacity of the ACT Government to meet its financial obligations over the short and long-term – as reflected in its net asset position, short-term assets to short-term liabilities, and financial assets to liabilities.

Dr Cooper said 'With respect to financial sustainability, there are challenges for the Territory as it incurred a **deficit** in the net operating balance (i.e. expenses exceeded revenue) of **\$646 million** in 2014-15. This deficit exceeds the budgeted deficit of **\$537 million** and the prior year deficit of **\$309 million**. The higher than expected deficit includes large unbudgeted costs of **\$336 million** relating to 'Mr Fluffy' (Loose-Fill Asbestos Eradication Scheme).'

The **2014-15 Financial Audits** report highlights financial challenges for the Territory, including:

- the unfunded superannuation liability (\$5 158 million at 30 June 2015). Further large cash injections may be required in future years to meet the ACT Government's objective of it being fully funded by 30 June 2030; and
- repaying borrowings (\$4 593 million at 30 June 2015). These are expected to increase to fund major capital projects such as the light rail, construction of the ACT Court facilities and duplication of major roads in Gungahlin (Horse Park Drive and Gundaroo Drive) and Tuggeranong (Ashley Drive).

Dr Cooper said 'The capacity of the ACT Government to meet its financial obligations will require, as always, giving attention to managing risks. If unexpected adverse events occur, or forecast costs of major capital projects significantly increase, then the challenge of meeting financial obligations increases. Mr Fluffy was an unexpected event in 2014-15 which has had significant adverse affects on the Territory's finances.

'All 70 financial statements audited in 2014-15 received an unqualified audit report indicating their quality was sound 'said Dr Cooper.

Dr Cooper said 'Computer systems are fundamental to effective provision and management of ACT Government services. The ACT Government is encouraged to develop whole of government policies to better guide its management of computer information systems. Of the six recommendations in the report, five related to:

- protecting systems from security vulnerabilities or malicious attacks;
- promptly restoring computer services, without the loss of information in the event of a disaster or other major disruption; and
- improving security over access, storage, transmission and disposal of information.'

Please note that:

The report considers the consolidated financial results of the Territory as reported in the audited 2014-15 financial statements of the Territory and budget information, including budget forecasts, as presented in the 2015-16 Budget Papers released in June 2015.

The budget information, which was recently revised for the 2015-16 mid-year review, and reported on in today's media is not considered in this report. Furthermore, the revised estimate of the 2015-16 deficit of \$479 million reported in today's media refers to the 'headline net operating balance' for the General Government Sector and not the consolidated financial results of the Territory.

The Summary chapter of the report is attached to this media release.

Copies of the full report are available from the ACT Audit Office's website www.audit.act.gov.au and the Office (please telephone (02) 6207 0833)

SUMMARY

The Audit Office issues independent audit reports containing opinions on the financial statements and reports of factual findings prepared by the ACT Government agencies and other entities in which the ACT Government has a direct financial interest. These reports are addressed to the members of the ACT Legislative Assembly and included in the annual reports of these agencies and other entities.

This report provides:

- a summary of the results of the audits of financial statements and reviews of statements of performance for the reporting periods ending 31 December 2014, 30 June 2015 and for periods within the 2014-15 financial year;
- the Audit Office's assessment of the overall quality and timeliness of reporting by agencies and other entities; and
- a summary of the major audit findings and information on progress made by agencies and other entities in resolving previously reported findings. These audit findings were identified by the Audit Office during the audits and reported to audited agencies and other entities.

Key findings

RESULTS OF THE FINANCIAL AUDIT PROGRAM

Paragraph

Results of the audits

All 70 financial statements audited in 2014-15 materially complied with the relevant reporting and accounting requirements and presented a true and fair view of the financial position and performance of the reporting agencies. 1.12

No qualified audit reports were issued in 2014-15 (five were issued in 2013-14). 1.13

The matter that resulted in five qualified audit reports being issued in 2013-14 on the 2013-14 financial statements of the ACT Public Cemeteries Authority and the related Perpetual Care Trusts (Gungahlin Cemetery Perpetual Care Trust, Hall Cemetery Perpetual Care Trust, Woden Cemetery Perpetual Care Trust and Woden Mausoleum Perpetual Care Trust) was resolved in 2014-15. The Audit Office therefore issued unqualified audit reports on the 2014-15 financial statements of the Authority and the related Perpetual Care Trusts. 1.15

Results of the reviews of statements of performance

One of the 30 reports of factual findings issued on statements of performance in 2014-15 was qualified. 1.22

A qualified report of factual findings was issued on the statement of performance of the former Economic Development Directorate for the period from 1 July 2014 to 6 July 2014. The statement of performance prepared by the former Economic Development Directorate did not comply with Section 30(2) of the *Financial Management Act 1996* as targets for accountability indicators had not been established and reported against. 1.23

AUDIT FINDINGS

Paragraph

Status of audit findings

The performance of reporting agencies in resolving previously reported audit findings improved in 2014-15 as: 2.7

- 60 percent (74 of 124) of previously reported audit findings were resolved in 2014-15 compared to 52 percent (76 of 145) in 2013-14; and
- previously reported audit findings that were either partially resolved or not resolved decreased by 28 percent (19 audit findings) from 69 (44 partially resolved and 25 not resolved) in 2013-14 to 50 (28 partially resolved and 22 not resolved) in 2014-15.

Financial and performance reporting

Quality of financial statements

The percentage of financial statements submitted by reporting agencies for audit that were rated as satisfactory or good increased from 81 percent (49 of 60¹) in 2013-14 to 88 percent (54 of 62) in 2014-15. This improvement largely resulted from two reporting agencies improving the quality of six of the seven financial statements that were rated as unsatisfactory in 2013-14. 2.11

¹ To provide a good indication of the overall quality of reporting by agencies, the number of financial statements submitted by reporting agencies for audit excludes financial statements that were prepared for a special purpose, such as those prepared to acquit the spending of funding received from the Commonwealth Government.

Timeliness of financial statements

Compliance with the whole of government reporting timetable for financial statements remained high as 92 percent (33 of 36²) of the reporting agencies complied with the reporting timetable in 2014-15. It was 92 percent (35 of 38) in 2013-14. 2.15

Quality of statements of performance

The quality of the statements of performance submitted by agencies for review decreased in 2014-15 compared to 2013-14 as the percentage of statements of performance assessed as: 2.20

- good decreased from 69 percent (20 of 29) in 2013-14 to 47 percent (14 of 30) in 2014-15; and
- unsatisfactory increased from none in 2013-14 to 7 percent (two of 30) in 2014-15.

Timeliness of statements of performance

Compliance with the whole of government reporting timetable for statements of performance remained high in 2014-15 as 85 percent (22 of 26³) of the reporting agencies complied with the reporting timetable. It was 96 percent (27 of 28) in 2013-14. While 15 percent (four of 26) of the reporting agencies did not submit their statement of performance to the Audit Office on time in 2014-15, these were provided shortly after the due date. 2.24

Annual reporting

Timeliness of annual reports

All reporting agencies complied with the requirement of the Annual Report Directions issued under the *Annual Reports (Government Agencies) Act 2004* to place a copy of their annual report on the relevant website on the same day it was tabled in the ACT Legislative Assembly. 2.25

² To provide a good indication of the overall timeliness of reporting by agencies, the number of reporting agencies only includes reporting agencies that were required to comply with the whole of government reporting timetable for the year ended 30 June 2015.

³ To provide a good indication of the overall timeliness of reporting by agencies, the number of reporting agencies only includes reporting agencies that were required to comply with the whole of government reporting timetable for the year ended 30 June 2015.

Inclusion of audited documents in annual reports

All reporting agencies included the correct version of their financial statements and statement of performance in their annual report. However: 2.27

- two agencies did not include the audit report on their financial statements;
- one agency did not include the full audit report on their financial statements; and
- two agencies did not include the report of factual findings on their statement of performance.

These reporting agencies subsequently corrected the printed and website versions of their annual report to include these reports.

COMPUTER INFORMATION SYSTEMS

Paragraph

Environment controls

Environment controls were assessed as satisfactory, however, there are several areas where improvements are needed. 3.7

Governance arrangements

System vendor support for operating systems

As system vendor support is only provided for a limited time, Shared Services has: 3.13

- developed and approved plans and strategies to anticipate any future loss of support for operating systems;
- upgraded its operating systems for which vendor support had ceased; and
- provided regular updates to ACT Government agencies on critical systems and applications that were operating without vendor support and sought to raise agency awareness of the associated risks.

Despite this, there are several ACT Government network servers that use operating systems which are no longer supported by the system vendor. Shared Services advised that it cannot require agencies to upgrade their operating systems which do not have vendor support.

Externally hosted websites

Shared Services ICT Security performs quarterly penetration testing for internally hosted websites to assess their strength against malicious attacks. However, it advised that it does not have the authority to impose the same level of security on websites which are maintained on infrastructure that is not owned or operated by the ACT Government. 3.18

Alternative information technology infrastructure arrangements

Alternative information technology infrastructure (e.g. data centre) arrangements are not provided for all critical systems that require a high level of availability. This presents a risk that information technology infrastructure will not be available, in a timely manner, if there were to be an incident which destroyed or rendered information technology infrastructure unavailable for an extended period of time. 3.25

Shared Services advised that it cannot require ACT Government agencies to have alternative information technology infrastructure (e.g. data centre) arrangements for their critical systems. 3.26

Shared Service's Quality Management System

Documents in the Quality Management System were not reviewed and updated in accordance with required timeframes. When this occurs, there is a risk that the documentation in the Quality Management System will not reflect the procedures, processes and practices that are being used. 3.30

Information security management processes

Password controls

Shared Services reduced the risk of inappropriate access, including unauthorised or fraudulent access, to the ACT Government's network, applications and data by implementing the ACT Government Password Standard. This included: 3.35

- requiring users to use a ten digit password with a combination of uppercase and lowercase letters, numbers and special characters; and
- continuing to perform regular audits of the complexity of passwords for compliance with the ACT Government Password Standard.

Security over access to data centres

Shared Services performed a review of access by its staff to data centres which was aimed at: 3.38

- removing access by staff who no longer needed it; and
- restricting access by staff to those areas of the data centres that were needed to enable duties to be performed.

However, at two data centres:

- 23 percent (15 of 65) of staff at one data centre and 22 percent (16 of 72) of staff at the other had access even though they were no longer employed by Shared Services; and
- an excessive number of spare access passes were being kept for temporary use.

This presents a risk of irregular access (including unauthorised, inappropriate or fraudulent access) to data centres. 3.39

Access to the ACT Government network

While Shared Services reviewed privileged user accounts, this was confined to user accounts in the Shared Services' operations team and did not cover privileged user accounts in other areas of the ACT Government. Furthermore: 3.43

- some privileged user accounts did not have a mandatory requirement to have a password when the user account was created; and
- 20 percent of the privileged user accounts were not used in 2014-15. This indicates these accounts are not needed and should have been deactivated.

Furthermore, Shared Services did not undertake: 3.44

- six-monthly reviews of standard user access to the ACT Government network; or
- a review of active generic accounts so that functionality which permits the confidentiality or integrity of critical data to be compromised could be disabled.

These weaknesses present a risk of unauthorised (including fraudulent) access to applications and data on the ACT Government network. 3.45

Management of patches to applications

Shared Services maintained its sound approach to patching operating systems, however, applications were not routinely patched. Additionally, there was no documented or defined patch management strategy that outlined the planned approach for patching. Furthermore, key financial systems were not being routinely scanned to identify security vulnerabilities. 3.49

This presents a risk that ACT Government systems will be susceptible to security vulnerabilities and of data being lost through cyber security intrusions. 3.50

Whitelisting of applications

Shared Services does not have a strategy for the whitelisting of applications on server or desktop operating environments in the ACT Government network. 3.53

This presents a risk that systems may be compromised by the exploitation of vulnerabilities or introduction of malicious programs (viruses). 3.54

Security of information

In 2013-14, Shared Services launched a trial of a document security classification system for Microsoft Office documents. The system was expected to be available for use by ACT Government agencies in July 2014. Although the new security classification system is available to be used or enforced, its application in all ACT Government agencies has not been mandated. A whole of government policy is recommended so that the new security classification system is effectively implemented by ACT Government agencies. 3.58

Business continuity and disaster recovery arrangements

Shared Services Information and Communication Technology (ICT) performed backup and recovery procedures to facilitate the continuation of operations and access to data. However: 3.62

- the restoration of data from backup files was not being periodically tested to minimise the risk of loss of service and/or corruption of business and financial data; or
- disaster recovery exercises were not undertaken for applications assessed to be 'government-critical' or 'business-critical' in 2014-15.

Shared Services have advised that they cannot require ACT Government agencies that 'own' the critical systems to implement effective business continuity arrangements. A whole of government approach is recommended so that business continuity arrangements provide assurance that critical systems are:

- operating appropriately and available when required; and
- restored in a complete and timely manner in the event of a disaster, disruption or other adverse event.

Change management processes

Shared Services did not: 3.71

- log changes to critical software or hardware for high risk or suspicious changes; or
- perform reviews of changes made to critical software or hardware to check that all changes were authorised.

This presents a risk of erroneous or fraudulent changes being made to critical hardware or software. 3.72

Contract management arrangements

While an annual analysis of expenditure records is occurring to identify new or amended information and communication technology contracts under the responsibility of the Information and Communication Technology (ICT) Contract and Licensing section, the current contract management guidelines and procedures have not been updated to provide guidance on the need for this analysis. 3.79

Project management arrangements

No significant weaknesses in project management arrangements used to initiate, plan and complete an information technology project were identified in 2014-15. 3.83

Application controls

Data processing controls

No significant weaknesses in data processing controls were identified in 2014-15. 3.89

Information security management

Management of user access

There was an improvement in the management of user access for Maze, MyWay, Cashlink and Territory Revenue System. However, management of user access in relation to one application (Oracle Financials) needed to be improved by reducing the number of logons for three individual users from two to one⁴. 3.96

Reviewing of audit logs

Directorates improved their processes for reviewing audit logs for several applications (Maze, Cashlink, MyWay, Territory Revenue System and Homenet⁵). However, it is recommended that practices for reviewing audit logs for two applications be improved by: 3.110

- ensuring that the System Security Plan defines the requirements for logging and monitoring of changes to the database server and having approved procedures for the review of audit logs (Community 2011⁶); and
- logging the activities of privileged users and routine monitoring of their financial transactions by a team that is independent of the privileged users. Furthermore, there should be independent monitoring of creation of user accounts and changes to user roles and authorisations for privileged users in the Financial Applications Support Team to minimise the risk of users being able to perform incompatible functions (Oracle Financials).

Password controls over access to key systems, application and data

In 2014-15, the Chief Minister, Treasury and Economic Development Directorate reduced the risk of irregular access, which may be erroneous or fraudulent, to the TM1⁷ application and data by increasing the level of password complexity required to access TM1 to comply with the ACT Government Password Standard. 3.119

⁴ These applications (i.e. Maze, MyWay, Cashlink, Territory Revenue System and Oracle Financials) are described on page 55.

⁵ The Homenet application is described on page 55.

⁶ The Community 2011 application is described on page 55.

⁷ The TM1 application is described on page 55.

Business continuity and disaster recovery arrangements

Three Directorates should improve their processes so that their business continuity plans and disaster recovery arrangements are effective by: 3.124

- having an approved and tested business continuity and disaster recovery plan (rego.act⁸);
- testing the restoration of data from backup files (Community 2011, Territory Revenue System and Homenet); and
- ensuring that business continuity and disaster recovery plans reflect the current recovery arrangements. These should also be updated, approved and tested (MyWay and TM1).

Change management processes

The Territory and Municipal Services Directorate implemented new procedures for making changes to MyWay. These include a plan for testing of changes with the results of testing changes (including the success or failure of changes) to MyWay being documented. 3.141

This reduces the risk of changes to MyWay not operating as intended and disruption to services that rely on MyWay. 3.142

Change management requests for changes to Oracle Financials were not always tracked prior to the implementation of the change. This presents a risk: 3.143

- that the changes made in Oracle Financials may not have been successfully tested prior to their release into production; and
- of Oracle Financials not operating as intended and of disruption to operations that rely on Oracle Financials.

THE TERRITORY'S FINANCIAL STATEMENTS

Paragraph

Operating results

The Territory incurred a deficit in the net operating balance (i.e. expenses exceeded revenue) of \$646 million in 2014-15. This exceeded the budgeted deficit (\$537 million) by \$109 million and prior year's deficit (\$309 million) by \$337 million. 4.5

⁸ The rego.act application is described on page 55.

The larger than expected deficit in the net operating balance was due mainly to: 4.6

- the unbudgeted payment of grants to purchase properties affected by the Loose-Fill Asbestos Eradication Scheme (\$336 million); and
- unanticipated employee and superannuation expenses (an increase of \$144 million) due mainly to:
 - the difference between the current interest rate (4.08 percent) used to estimate the present value of the superannuation liability and the long-term rate (six percent) used to prepare the budget estimate of the present value of this liability; and
 - an increase in staff numbers.

The Territory's net operating balance has declined from a small surplus of \$1.0 million in 2010-11 (a breakeven result) to a deficit of \$646 million in 2014-15 as the costs of providing services by the ACT Government have exceeded revenue increases. In 2014-15, these higher costs included the cost of the Loose-Fill Asbestos Eradication Scheme (\$336 million). 4.8

The Territory incurred an operating deficit of \$415 million in 2014-15. This exceeded the budgeted deficit (\$359 million) by \$56 million and prior year's deficit (\$26 million) by \$389 million. 4.11

The larger than expected operating deficit was mainly due to the unbudgeted payment of grants to purchase properties affected by loose-fill asbestos and higher employee and superannuation expenses. The Chief Minister, Treasury and Economic Development Directorate has advised that 'the consolidated budget estimates were updated for the payment of grants affected by loose-fill asbestos in the 2014-15 Budget Review'. 4.12

There has been a decline in the Territory's net operating result from an operating surplus of \$123 million in 2010-11 to an operating deficit of \$415 million in 2014-15. This was due to the costs of services provided by the ACT Government exceeding the revenue increases over this period. 4.13

The Territory estimates that it will incur another operating deficit in 2015-16 of \$391 million before generating an operating surplus of \$17 million in 2016-17, an operating deficit of \$24 million in 2017-18 and then an operating surplus of \$188 million in 2018-19. The achievement of an operating surplus of \$188 million in 2018-19 depends on achieving the planned large reduction in the deficits in the net operating balance and generating a large increase in other economic inflows in 2018-19. 4.15

A surplus of \$188 million in 2018-19 depends on: 4.16

- achieving the planned large reduction of \$430 million (an average annual decrease of 16.5 percent) in the deficits incurred in the net operating balance from \$646 million in 2014-15 to \$216 million in 2018-19; and

- generating a large increase in other economic flows in 2018-19. This large increase from the amount generated in 2013-14 and the forward years leading up 2018-19 depends on achieving budgeted gains on the sale of remediated land that the Territory acquired as part of the Loose-Fill Asbestos Eradication Scheme.

The planned deficits in the net operating balance and small operating results over the forward years from 2015-16 to 2018-19 mean that, if unexpected adverse events occur, the Territory is exposed to a risk of incurring large deficits. This can be addressed by raising taxes and rates, reducing or reprioritising expenses, increasing borrowings or selling assets and/or absorbing deficits. 4.17

Financial position

Assets to liabilities coverage

The Territory's net assets (\$14 674 million) at 30 June 2015 were less than the budgeted amount (\$17 062 million) by \$2 388 million due mainly to a higher than expected unfunded superannuation liability. 4.18

The increase of \$3 767 million (an average annual increase of 4.3 percent) in the Territory's assets from \$21 735 million at 30 June 2011 to \$25 502 million at 30 June 2015 was mainly due to: 4.20

- upward revaluations of property, plant and equipment and the Territory's investment in the ActewAGL Joint Venture due to an increase in the valuation of ActewAGL's property, plant and equipment; and
- capital expenditure on property, plant and equipment (in particular, land, buildings and infrastructure assets). In 2014-15, the Territory also purchased properties as part of the Loose-Fill Asbestos Insulation Eradication Scheme.

The short-term financial position of the Territory at 30 June 2015 is stronger than the position anticipated in the budget but weaker than the position that existed at 30 June 2014. The Territory had \$1.57 in short-term assets available to cover each dollar of short-term liabilities at 30 June 2015 compared to \$1.80 at 30 June 2014. This weaker position is due mainly to liabilities incurred to acquire asbestos affected properties and pay for the costs of the land remediation under the Loose-Fill Asbestos Insulation Eradication Scheme. 4.23

Short-term assets to short-term liabilities coverage

The Territory's short-term financial position is expected to significantly weaken from a net asset position of \$795 million at 30 June 2015 to net liability position of \$331 million at 30 June 2019. 4.24

Financial assets to liabilities coverage

The long-term financial position of the Territory is much weaker than the budgeted and prior year positions and has significantly weakened since 30 June 2011. 4.27

Unfunded liabilities at 30 June 2015 (\$8 630 million) exceeded the budgeted unfunded liabilities (\$6 004 million) and unfunded liabilities at 30 June 2014 (\$7 081 million) by \$2 626 million and \$1 549 million respectively. Unfunded liabilities have increased by \$5 125 million (an average annual increase of 36.6 percent) from \$3 505 million at 30 June 2011 to \$8 630 million at 30 June 2015. 4.28

The expected strengthening in the Territory's long-term financial position over the forward years of 2015-16 to 2018-19 is based on the assumption that there will be a substantial decrease in the unfunded superannuation liability from that which existed at 30 June 2015. This decrease is assumed to be sufficient to counter the expected large increase in borrowings to fund major capital works projects in the Territory's Infrastructure Program. 4.30

The large decrease in the unfunded superannuation liability of \$2 473 million (an average annual decrease of 13.3 percent) from \$5 158 million at 30 June 2015 to \$2 415 million at 30 June 2019 depends significantly on the rate used to measure the present value of superannuation payments in these future years. 4.31

Borrowings are expected to increase significantly by \$1 779 million (an average annual increase of 9.7 percent) from \$4 593 million at 30 June 2015 to \$6 372 million at 30 June 2019 to fund major capital works projects in the Territory's Infrastructure Program. These projects include the Territory's light rail project, construction of the ACT Court facilities, and duplication of major roads in Gungahlin (Horse Park Drive and Gundaroo Drive) and Tuggeranong (Ashley Drive). 4.32

Recommendations

The following recommendations relate to significant findings in the report. Recommendations relating to other report findings have been provided to agency heads, governing boards and relevant Ministers through audit management reports.

RECOMMENDATION 1 (CHAPTER 3) SYSTEM VENDOR SUPPORT FOR OPERATING SYSTEMS

The Chief Minister, Treasury and Economic Development Directorate should develop and foster the implementation of a whole of government strategy to guide the upgrading of operating systems for which vendor support has ceased. This should include specifying when upgrades are to occur.

RECOMMENDATION 2 (CHAPTER 3) EXTERNALLY HOSTED WEBSITES

The Chief Minister, Treasury and Economic Development Directorate should develop and foster the implementation of a whole of government strategy for managing security vulnerabilities relating to externally hosted websites.

RECOMMENDATION 3 (CHAPTER 3) ALTERNATIVE INFORMATION TECHNOLOGY INFRASTRUCTURE ARRANGEMENTS

The Chief Minister, Treasury and Economic Development Directorate should develop and foster the implementation of a whole of government strategy for alternative information technology infrastructure arrangements for critical systems.

RECOMMENDATION 4 (CHAPTER 3) SECURITY OF INFORMATION

The Chief Minister, Treasury and Economic Development Directorate should develop and foster the implementation of a whole of government policy on the introduction of the new security classification system.

RECOMMENDATION 5 (CHAPTER 3) BUSINESS CONTINUITY AND DISASTER RECOVERY ARRANGEMENTS

The Chief Minister, Treasury and Economic Development Directorate should develop and foster the implementation of a whole of government policy on business continuity arrangements, which provide assurance that critical systems are operating and available when required and restored in a complete and timely manner in the event of a disaster, disruption or other adverse event.

RECOMMENDATION 6 (CHAPTER 3) BUSINESS CONTINUITY AND DISASTER RECOVERY ARRANGEMENTS

ACT Government agencies should have business continuity plans and disaster recovery arrangements that are up-to-date.