

Submission

No 6

INQUIRY INTO FINANCIAL REPORTING

Organisation: NSW Department of Health
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Telephone: 02-9391 9000
Date Received: 12/07/2010

Theme:

Summary

Mr Paul Gibson, MP
Chair
NSW Public Accounts Committee
Parliament of New South Wales
Macquarie Street
SYDNEY NSW 2000



Dear Mr Gibson

Inquiry into Financial Reporting

I would like to express my appreciation to the Committee for the invitation to NSW Health to provide a submission to assist the inquiry.

I note that in your invitation you identify concerns raised by the Auditor-General regarding the "quality of financial reporting and consistent significant budget overruns of some large agencies in Volume Four of the 2009 Financial Audit" as the primary motivation for the inquiry.

Please find attached the NSW Health submission to the Inquiry into Financial Reporting being undertaken by the Committee, provided in respect of the Committee's Terms of Reference.

Should you require further advice in regard to this submission, please contact Mr John Roach, Chief Financial Officer, NSW Health on 9391 9178 or Mr Philip West, Director Finance, NSW Health, on 9391 9165.

Yours sincerely

Debora Picone, AM
Director-General

Inquiry into the Quality and Timeliness of Financial Reporting

NSW Health's comments in relation to the Terms of Reference of the Inquiry:

The following advice is provided in relation to the terms of reference of the inquiry –

“That the Committee examine the quality and timeliness of financial reporting by NSW government departments with particular regard to:

1. The adequacy of current processes in place to identify and correct errors in accounts in a timely manner
2. Identification of best practice procedures for financial reporting
3. Impediments to the implementation of best practice procedures
4. Any related matter”

1. In relation to the Adequacy of Current Processes

Financial reporting in NSW Health covers a continuum from cost centres in local hospital facilities, to Health Services, to the Department, and finally to NSW Treasury.

Financial reporting is undertaken on a monthly and annual basis.

Monthly financial reporting incorporates the reporting of budget and actual results on a month to date basis, on a year to date basis, and also includes the provision of a full year forecast of the expected actual Net Cost of Service result.

Controlled Entity Reporting to NSW Department of Health

NSW Health controlled entities submit monthly financial data via the Department of Health Reporting System (DoHRS). This system is used to consolidate financial data from across the NSW Health system with the Department of Health's financial data.

The Department collects Operating Statement, Balance Sheet and Cash Flow information both for year-to-date actuals and for the year end projection.

A comprehensive narrative report is prepared each month to accompany the monthly financial reports. Information required to be reported by Health's controlled entities includes:

- Net Cost of Services (NCoS) - month to date and full year performance against budget;
- Detailed narrative on NCoS performance against budget;
- Explanations of causes for variance to budget;
- Cash at bank (including projected full year balance);
- Working capital – movements in “actual” month to date and full year projections;
- Repairs & Maintenance to be transferred to capital;
- Debtors movement – in year and projected full year balance;
- Creditors movement – in year and projected full year balance;

- Ageing of creditors;
- Capital expenditure;
- Salary packaging; and
- Staffing

A sample of the templates used by NSW Health for monthly financial reporting is provided at Attachment 1.

In addition to monthly financial reporting, NSW Health prepares both activity and statistical reports on a monthly basis to support the financial reporting. It is a Departmental requirement that each report is certified by the Chief Executive to attest his/her satisfaction with the results reported.

Each monthly report is subject to Departmental analysis, following which feedback to Health Services is routinely provided.

The Department's performance is monitored through the Finance, Risk and Performance Management Committee which duly considers the inter-relationships of recurrent asset acquisition and disposal programs and activity, data, as well as overseeing risk management performance. Dialogue with Health Service senior executives is maintained throughout the year, providing a forum to raise emerging issues, identify / appraise budgetary performance and consider budget strategies which need to be implemented.

NSW Health Reporting to Treasury

Each month NSW Health is required to input its consolidated financial data into the Treasury reporting system, TOES.

The financial data entered into the TOES system includes initial budget, month to date budget and actual data, year to date budget and actual data, full year forecast, for all Balance Sheet and Income and Expenditure items.

From this data input, NSW Treasury is able to prepare monthly NCoS, Balance Sheet and Cash Flow statements.

The on-line reports are prepared with narrative reports which are reflective of the inputs of the Finance, Risk & Performance Management Committee and senior management.

NSW Health Annual Reporting

The annual financial statements of NSW Health are prepared at 30 June each year in accordance with Australian Accounting Standards (which include Australian Accounting Interpretations) and the requirements of section 45E of the *Public Finance and Audit Act 1983* and the Public Finance and Audit Regulation 2005 and the Financial Reporting Directions published in the Financial Reporting Code for Budget Dependent General Government Sector Agencies or issued by the Treasurer under Section 9(2)(n) of the Act and the Health Administration Act 2000 and its regulations.

Annual financial statements are prepared by NSW Health (parent and consolidated), NSW Health statutory health corporations, the Health Administration Commission, and other controlled entities.

2. In relation to Best Practice Procedures

In Volume One of the 2009 Financial Audit report to Parliament, the Auditor-General made a specific recommendation to NSW Health in regard to the timeliness and quality of its end of year financial reporting.

In response to this recommendation, NSW Health undertook an aggressive program of process improvement for the preparation of its 2008/09 financial statements.

Subsequently, within the space of six months, NSW Health was able to improve its compliance with statutory reporting deadlines, and improved the quality of its financial reporting from being criticised in Volume One of the 2009 Financial Audit to being commended by the Auditor-General in Volume Eleven of the 2009 Financial Audit.

To assist the Committee in understanding the processes undertaken by NSW Health, a case study is provided at Attachment 2.

It should be noted, that while NSW Health was faced with the need to improve timeliness and quality of its annual financial reporting, it is noteworthy that NSW Health received an unqualified audit report.

The term "best practice" is a well used but is not a well understood term and implies that there is no room for improvement once "best practice" has been achieved. Thus, it is preferable to characterise the financial reporting processes of NSW Health as being "good practice" rather than "best practice". There is always room in the financial reporting processes of NSW Health to accommodate ideas that will enhance the existing high levels of performance currently achieved.

3. In relation to Impediments to the Implementation of Best Practice Procedures

When considering the challenges presented by the Auditor-General in Volume One of the 2009 Financial Audit report, there were a number of factors which had contributed to the difficulties faced by NSW Health in preparing its 2006/07 and 2007/08 annual financial statements, namely:

- In 2005/06 there was a major restructure of NSW Health:
 - Reduction from 17 Area Health Services to 8
 - Reduction in corporate support staff of over 1,000 FTE

The restructure required NSW Health to rebuild its accounting processes to accommodate the revised structure, but with significantly less staff. The revised processes would require time to "mature".

- The transition to a shared corporate services model for accounting transaction processing
- The introduction of a new Standard Chart of Accounts across all of NSW Health
- Late advice on revaluations, actuarial assessments of leave from external advisors
- Late advice from Treasury in regard to changes to the reporting code
- Late advice issuing from the Department to the Health Services

Whilst some of these difficulties were unique to NSW Health, such as the introduction of the Standard Chart of Accounts and the restructure, the remaining difficulties will present challenges to the introduction of good practice across Government.

The case study attached provides insights as to how NSW Health addressed these potential impediments.

The Department wishes to highlight the significant role that the Treasury plays in the successful production of timely and accurate reports.

NSW Health, through its consolidation processes for 13 distinct reporting entities, operates as a "mini-Treasury" and it is important that the Department is able to issue clear instruction on reporting requirements well before year end. The capacity to comply with reporting requirements is seriously impeded through any late changes in Treasury reporting requirements.

In this regard, improvements in Treasury's performance have been clearly evident in the past two years.

Treasury has also embarked on a program of further improvement, earmarked by concentration on the benefits of conducting a hard close around March of each year and promoting early substantiation by the Audit Office. The Department is united with Treasury in this endeavour but wishes to highlight that, to be truly effective, it will be important to build the hard close into the Audit Client Service Plan and lock both entity management and the Audit Office into a formal commitment.

Timeframes also need to be examined with each of the Health Services having only two weeks to submit their yearend statements to the Department for consolidation by 30 July. Audit is then permitted 10 weeks to complete its audit review per Section 45F of the *Public Finance and Audit Act*. Shrinking of this timeframe should be possible as a result of early substantiation procedures thereby enabling annual reports to be produced earlier in response to parliamentary and public expectations.

Director-General
 NSW Department of Health
 73 Miller Street
 NORTH SYDNEY NSW 2059

Attention: Finance Branch

Dear Sir

**AREA HEALTH SERVICE
 FINANCIAL and ACTIVITY REPORT
 Month Ending**
EXECUTIVE SUMMARY

1. FINANCIAL PERFORMANCE

1.1 Net Cost of Services (Summary)

	Year to Date \$000				Full Year \$000			
	Adj Budget	Actual	Variance	%	Adj Budget	Projected	Variance	%
Expenses								
General Fund								
-Employee Related								
-VMO's								
-Other Operating								
-Maintenance								
-Depreciation								
-Grants & Subsidies								
-Other Services								
-Third Schedule Hospitals								
Total General Fund								
Special Purposes & Trust								
Total Expenses								
Revenue								
General Fund								
-Patient Fees								
-Other Revenue								
Total General Fund								
Special Purposes & Trust								
Total Revenue								
Net Cost of Services								
General Fund NCoS								
Special Purposes & Trust NcoS								
Total NcoS								

Variance: (-) is favourable (+) is unfavourable

Reported results are to be consistent with results reported in DOHRS, to Finance Committee and details at 1.1.1 and 1.1.2.

Comment

It should be noted that it is the clear responsibility of local management to ensure that financial performance is closely aligned with allocations provided. Where necessary, additional strategies are to be developed to ensure a budget result is achieved.

Comments are required where variations to budget are being reported. Such comments are to address

- the cause,
- corrective strategies in place or to be implemented. If projected results are not on budget advice is to be provided as to why strategies are not working, with advice of further proposals to achieve an on budget result.
- Status of discussions between Chief Executive, 2nd tier managers and relevant managers on budget and activity management performance.

1.1.2 Net Cost of Services: General Fund - General Variance

Facility/Cost Centre	Year-to-Date NCOS Variance (\$000)	Full Year NCOS Budget (\$000)	Full Year NCOS Projection (\$000)	Projected Full Year NCOS Variance (\$000)	Projected Full Year NCOS Variation (%)
Hospital A					
Hospital B					
Hospital C					
Other					
Total Variance					

- Variance: (-) is favourable (+) is unfavourable
- Total must agree with General Fund - General variance and commentary in paragraph 1.1.1.
- To include comment on any internal unfavourabilities.

1.2 Cash at Bank -- General Fund (\$000) as per bank statement

	30.6.10 Balance	Current Month End Balance	Cash Plan Projected 30.6.11 Balance (1)	Revised 30.6.11 Balance	Variance Revised to Cash Plan
Operating Bank Account					
Capital Bank Account					
Total per Bank Statement					
Less: Total unrepresented cheques					
Add: Other Adjustments					
Cash Book Balance					
Comprising:					
- Operating Cash Book Balance					
- Capital Cash Book Balance					

(1) This amount is to be fixed by 31 July 2010 per 2010/11 allocation letter. Advice of projected component is required.

Comments are to focus upon –

- any negative Bank Account balances
- any negative Cash Book balances
- any internal offsets between operating/capital
- strategies required to achieve projected result
- reasons for any projected 30.6.11 deterioration compared to 30.6.10)

1.3 Working Capital and Balance Sheet – General Fund (\$000)

	30.6.10 Balance	Current Month			Full Year			Variance Projected Movement To Budgeted Movement
		Month End Balance	Movement from 30.6.10	Movement to Prior Month	Projected 30.6.11 Balance	Projected Movement	Budgeted Movement	
Current Assets:								
- Cash at Bank & Investments								
- Debtors								
- Other Current Assets								
Total Current Assets								
Current Liabilities:								
- Loans								
- Creditors and Accruals								
- Leave Liabilities								
- Other Current Liabilities								
Total Current Liabilities								
Working Capital								
Non-Current Assets								
Non-Current Leave Liabilities								
Other Non-Current Liabilities								
Net Assets								
Equity:								
- Accumulated prior year surplus (deficit)								
- Current Year NCoS								
- Subsidy Received:-								
State & Industry Contributions – Recurrent								
State & Industry Contributions - Capital								
- Other Movements								
Total Equity								

Comment

- Working Capital represents Current Assets less Current Liabilities
- Cash at Bank represents the reconciled Accounting System balance (i.e. Cash Book Balance) as per 1.2 above and not that shown on the Bank Statements
- Comment must focus on movements (and any consequential trends) in working capital and must also address any significant variances in other line items.
- Details must be provided for "Other Movements" in Equity.

1.4 RMR > \$10,000 projects and Funding for Capital Items

Comment

There will be high level scrutiny of decisions by Health Service CE's in respect of decisions to re-allocate recurrent funding, provided for day to day services, to the purchase of capital type assets.

Health Services monthly reporting requires completion of separate Excel spreadsheets detailing the budgeted, forecast and actual incurred payments for Capital program Items including RMR >10,000.

Separate reporting schedules will be required for each category of Capital payments.

The Capital reporting categories are:-

- a) Minor equipment \$10k to \$250K
- b) Locally funded initiatives over \$250,000
- c) Major/Minor Works

Monthly narrative information is to be provided in respect of any comment where project funding from own source revenues varies to the initial budget proposals.

Directors of Financial Operations and Health Service Capital Program Managers are to ensure that consistent information to the Department via the monthly narrative, DOHRS and CAPDOHRS is provided

Health Service Directors of Financial Operations have previously been advised of the level of cash funded support provided by the Department for RMR>\$10,000 items which is paid separately in monthly installments to Health Services

It should be noted that it is the clear responsibility of local management to ensure that financial performance is closely aligned with allocations provided. Where necessary, additional strategies are to be developed to ensure a budget result is achieved.

1.5 Debtors

	1 July 2010		Year-to-Date		30 June 2011 Projection	
	Total \$000	>* days \$000	Total \$000	>* days \$000	Total \$000	>* days \$000
Patient Fees – Chargeable						
Patient Fees - Compensable						
Patient Fees - Ineligible						
Other User Charges						
Other Intra Health User Charges						
Other Revenue						
GST						
Total Debtors						

Note: Chargeable, User Charges, Other Revenue * = 45 days
 Ineligible * = 150 days
 Compensable * = 150 days

The reported amounts in the Debtor categories are prior to allowance for Provision for Doubtful Debts.

Comment

Comments must focus on movements from 1 July 2010 levels

1.6 Creditor Performance

1.6.1 Recurrent (General Fund and SP&TF)

	1 July 2010		Year to Date		Projected Balance 30 June 2011	
	Total \$000	> 45 days \$000	Total \$000	> 45 days \$000	Total \$000	> 45days \$000
* GENERAL						
Health Services						
Business Units						
Total - General (Line 188)						
*						
HEALTH SERVICES - OTHER						
Salaries & Wages (Line 186)						
VMOs (Line 213)						
Intra Health (excluding Business Units) (Line 214)						
Contracted Patient Services (Line 215)						
GST (Line 242)						
Total Health Services - Other						
Total Creditors						
Comprising:-						
General Fund (1)						
SP&T						

Reconciliation of General Fund Creditors

	1 July 2010		Year to Date		Projected Balance 30 June 2011	
	Total \$000	> 45 days \$000	Total \$000	> 45 days \$000	Total \$000	> 45days \$000
Total General Fund Creditors (1)						
Less Salaries, Accruals, Holds						
Creditors on Hand (Agrees with Attachment A)						

1.6.2 Recurrent Creditor Ageing

Comment

In addition to the above table Health Services are to complete the Excel creditor ageing report for recurrent / operating budget item (Attachment A).

Health Services are to provide comment in the monthly narrative where creditors are over 45 days on a projected basis.

1.6.3 Capital Creditors

1 July 2010		Year to Date		Projected Balance 30 June 2011	
Total \$000	>45 \$000	Total \$000	>45 \$000	Total \$000	>45 \$000
			(1)		

1.6.4 Capital Creditor Ageing

45-59	60-89	90-119	120+	Total
				(1)

Comment

The benchmark level for capital creditors has been retained at less than 45 days for all health services for the 2010-11 reporting year.

If any exceed 45 days Health Services are to identify;

- causes
- corrective action proposed.

2. OUTSTANDING FINANCIAL ISSUES WITH FINANCE BRANCH

Relevant correspondence that has been submitted to Finance Branch prior to the month being reported should be nominated.

3. OTHER COMMENTS

- Comment is required for items remaining on the Financial Check Report.
- Reporting of bank overdrafts (Department's letter of 22 April 1998 refers).
- Include Special Projects reporting pro forma.
- Use of this heading is otherwise left to the discretion of each health service.
- Should any problems be experienced in completion of the monthly DOHRS and narrative reports, health services are encouraged to contact their nominated Finance Branch officer for the clarification required.

4 CERTIFICATION WAITING LIST DATA

I certify the accuracy of the waiting list data. The waiting list data has been prepared in accordance with Policy Directive PD2009_018 dated 9 April 2009 "Waiting Time and Elective Patient Management Policy."

Attachments:

- A CREDITOR REPORT
- B CAPITAL REPORTING (4 PAGES)
- C SALARY PACKAGING
- D SPECIAL PROJECT REPORTING
- E WORKFORCE
- F INTRA HEALTH CREDITORS REPORT
- G OUTSTANDING SUPPLEMENTATIONS/LINE ITEM ADJUSTMENTS

KPI Activity is to be provided using the web based application introduced during 2005/06.

Yours sincerely

Chief Executive

ATTACHMENT 2 : CASE STUDY

ISSUE

The 2009 Auditor-General's report on the 2007/08 NSW Health Financial Audit highlighted deficiencies in the quality and timeliness of the financial statements lodged by NSW Health in both 2006/07 and 2007/08. These deficiencies led to the following recommendation from the Auditor-General:

"We recommend both the Department and its controlled entities review and significantly improve year-end reporting processes to enable the consolidated entity to meet its statutory reporting timetable. Improvements should include quality control processes and more timely consideration and resolution of accounting and related issues for dissemination to the controlled entities. The Department needs to take decisive action to remedy the continuing unsatisfactory situation. Appropriate accountabilities should be included in staff performance agreements for Departmental and controlled entities' staff."

(Source: Auditor General's Report, Health Overview, Vol. 1, 2009)

Therefore, there were two substantive issues to be addressed by NSW Health namely, timeliness and quality.

CONTRIBUTING FACTORS

The ability of NSW Health to meet its statutory reporting requirements in both 2006/07 and 2007/08 was impaired by a number of factors including:

- In 2005/06 there was a major restructure of NSW Health:
 - Reduction from 17 Area Health Services to 8
 - Reduction in corporate support staff of over 1,000 FTE

The restructure required NSW Health to rebuild its accounting processes to accommodate the revised structure, but with significantly less staff. The revised processes would require time to "mature".

- The transition to a shared corporate services model for accounting transaction processing
- The introduction of a new Standard Chart of Accounts across all of NSW Health
- Late advice on revaluations, actuarial assessments of leave from external advisors
- Late advice from Treasury in regard to changes to the reporting code
- Late advice issuing from the Department to the Health Services

SOLUTIONS

The Department considered the best way to simultaneously address both the issue of timeliness and the issue of quality was to:

- (1) Implement an "early close" process, where the early close is a simulation of the end of financial year processes and is conducted prior to 30 June; and
- (2) Enhance the governance of its end of financial year milestone reporting.

Early Close

- The Department chose to undertake its early close as at 31 March 2009.
- All NSW Health's controlled entities (and parent) were required to "close" financial systems and prepare pro-forma end of year financial statements as at 31 March 2009.
- Full working papers were prepared by NSW Health's controlled entities (and parent), noting there were some limitations on available information, such as revaluations, actuarial adjustments (which are not always available until late in the financial year).
- The pro-forma financial statements were required to be submitted by the controlled entities to both the Department and also to the entity's auditors by the end of April, 2009.

Milestone Reporting

- A detailed list of milestone targets has been established for each of the controlled entities and the parent.

The setting of milestone targets involves the collation of end of financial year tasks into sequential order, assigning responsibility for achievement of tasks to an individual, and then assigning dates for completion of the tasks so as to coincide with the statutory reporting deadlines.

- Controlled entities (and the parent) are required on a monthly basis (from April to July) to report on progress in meeting the milestone targets.
- Milestone reports include a requirement for the controlled entity to advise which milestones were being achieved and where milestones were not achieved, to advise the remedial action initiated.
- On a monthly basis the Department reviews the progress of the controlled entities (and the parent) in meeting their milestones and works cooperatively with entities that were required to implement remedial actions to address non-achievement of milestones.
- Milestone targets and reporting has been a long standing feature of the NSW Health end of financial year process. However, in 2009 the governance surrounding the milestone reporting process was significantly enhanced whereby the milestone report was, for the first time, required to be co-signed by the Chief Executive and the Chair of the Audit Committee before submission to the Department.

Communication

To support the milestone reporting and the introduction of the early close, the Department initiated a comprehensive communication plan, including:

- In January 2009 correspondence issued from the Deputy Director-General Health System Support to Chief Executives regarding the need to improve the timeliness and quality of end of-year financial reporting;
- In early March 2009 a meeting was convened (including video conferencing facilities) with all Senior Finance Staff in NSW Health in attendance;
- Formal correspondence issued from the Chief Financial Officer, DOH regarding the need to improve the timeliness and quality of end of year financial reporting

including outlining the roles, responsibilities and obligations of the controlled entities (and the parent) in supporting the early close and milestone reporting processes;

- Monthly feedback, where appropriate, on progress in achieving milestone targets; and
- Ad hoc, informal liaison with Health Services and controlled entities.
- The involvement of Treasury in consideration of the more complex emerging issues.

Benefits

- The March 2009 early close allowed DOH to test its end of financial year processes some 3 months in advance of the end of financial year. This allowed NSW Health to identify any process weaknesses with sufficient time to initiate remedial action
- The Audit Office was provided the opportunity to undertake early substantiation of financial transactions processed between July 2008 and March 2009
- The early close, when combined with the milestone reporting, increases the focus of accounting and corporate staff to ensure progress in completing end of financial year tasks in sufficient time to meet the statutory deadlines without compromising the quality of supporting paperwork

OUTCOME

In the space of less than six months, the Department moved from a position of being criticised for the timeliness and quality of its financial reporting, to being commended. The 2008/09 Auditor General's report included a commendation for NSW Health:

"There has been a significant improvement this year, and the Department and its agencies are to be commended. I received the financial reports of all Area Health Services (AHSs), and of the Health Administration Corporation and the Department within the statutory timeframe. In addition, the majority of AHSs provided adequate working papers to support their financial reports."

(Source: Auditor General's Report, Health Overview, Vol. 11, 2009)

CRITICAL SUCCESS FACTORS

When considering this significant achievement, NSW Health Finance Branch consider the critical success factors to be:

- Strong leadership and improved governance
- Support from:
 - Deputy Director-General, Health System Support
 - Chief Executives
 - Auditors
 - Audit & Risk Committees
 - Treasury
 - Health Services' Directors of Financial Operations & Directors of Finance

- Communication
- The cooperative approach of all parties involved to achieving a shared vision

CONSOLIDATING THE CHANGE

Whilst significant, the achievements of 2008/09 need to be consolidated into the culture of NSW Health to ensure sustained quality and long term compliance with statutory reporting deadlines.

In 2009/10 NSW Health will again implement an early close with milestone reporting.

Actions implemented to date include:

- Communication has commenced
- A "Lessons learned" workshop for Health Services and controlled entities was held in March 2010
- 2009/10 early close conducted in March 2010
- Audit & Risk Committee Chairs met in mid April 2010 at which time a workshop was also conducted to acquaint key finance/accounting personnel with their 2009/10 reporting responsibilities
- Monthly milestone reporting has commenced