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Audit Report No. 21, 2005-06, Audit of Financial Statements of Australian Government Entities for the Period Ended 30 June 2005

Background

9.1 At the close of each financial year the Government prepares two key financial reports: the Consolidated Financial Statements of the Australian Government (CFS); and the Final Budget Outcome Report (FBO Report) – required by the *Charter of Budget Honesty Act 1998*.

9.2 Under the *Financial Management and Accountability Act 1997* (FMA Act), the Auditor-General is required to report each year to the relevant Minister(s) whether government entities' financial statements give a true and fair view of the matters required by applicable legislation, Accounting Standards and other mandatory financial reporting requirements in Australia. This is one of the key responsibilities of the Auditor-General.

9.3 Audit Report No. 21, 2005/06 provides a summary of the results of the ANAO's audits of the financial statements of all Australian government reporting entities, including the Consolidated Financial Statements of the Australian Government.

9.4 Audit Report No. 21 is the second report on these audits for the financial year ended 30 June 2005, and complements Audit Report No.56 2004-2005. The latter outlined audit findings relating to government departments' control structures, including governance arrangements, information systems and control procedures, which supported the reporting of public sector financial performance and accountability, through to March 2005.

9.5 The ANAO is responsible for the audit of the financial statements of 252 government entities. For 2004-05, the ANAO issued the following opinions:

- 213 'clear' opinions;
- 4 'qualified' opinions;
- 3 containing an 'emphasis of matter'; and
- 18 containing 'other statutory matters'.

9.6 The four qualified audit reports were those of the Consolidated Financial Statements (outlined further below); the Department of Defence (ongoing from 2003-04); and Centrum Insurance Brokers Pty Old and Northern Insurance Brokers Pty Ltd (as a result of uncertainties over opening balances).

9.7 The three audits containing an 'emphasis of matter' were those of Adelaide Symphony Orchestra, Queensland Orchestra, and Symphony Australia Holdings Pty Ltd. Each of these entities disclosed a significant uncertainty surrounding their ability to continue as a going concern.[1]

9.8 Audit reports containing 'statutory matters' largely related to breaches of Section 48 of the FMA Act[2], and agencies' compliance failures on Net Appropriation agreements (examined further in Chapter 10 of this report).

Audit risk scale

9.9 The ANAO rates its audit findings according to a risk scale. Audit findings which pose a significant business or financial risk to the entity and which must be addressed as a matter of urgency, are rated as 'A'. Issues that pose a moderate business or financial risk are rated as 'B'. Issues that are procedural in nature, or reflect relatively minor administrative shortcomings are rated as 'C'.

1 ANAO Audit Report No. 21, 2005-06: *Audits of the Financial Statements of Australian Government Entities for the Period Ended 30 June 2006*; Commonwealth of Australia; 21 December 2005.

2 Section 48 o the FMA Act states that: (1) A Chief Executive must ensure that accounts and records of the agency are kept as required by the Finance Minister's Orders; and (2) The Finance Minister is entitled to full and free access to the accounts and records kept under subsection (1). However, the Finance Minister's access is subject to any law that prohibits disclosure of particular information.

9.10 The following agencies attracted the highest number of A and B category audit findings, and were invited to a public hearing to explain their actions to address the audit findings:

- Department of Environment and Heritage (DEH);
- Department of Families, Community Services and Indigenous Affairs (FaCSIA); and
- Australian Taxation Office (ATO).

9.11 The Department of Finance and Administration (Finance) and the Australian National Audit Office (ANAO) were also witnesses at the hearing.

Qualification of whole-of-government statements

9.12 The Consolidated Financial Statements of the Australian Government were signed by the Minister on 8 December 2005, and were issued on 12 December 2005. The ANAO's audit opinion indicated that the financial statements were true and fair, except for qualifications relating to six material issues. Four of these were related to the scope limitations on Defence financial information. These matters were examined by the JCPAA as part of its inquiry into financial management and equipment acquisition at the Department of Defence and Defence Materiel Organisation (DMO).[3] The other two qualifications were in relation to underestimates of taxation revenue (discussed below).

GST and related Grants expense

9.13 As in the previous year, the 2004-05 CFS did not recognise the Goods and Services Tax (GST) as a revenue of the Australian Government. The then Government's reason for not recognising GST revenue, and associated grants payment to the States and Territories, was based on the view that the GST is a State tax collected by the Australian Government in an agency capacity.[4] The 2006-07 Budget Papers explain the Government's position:

> Australian Accounting Standards would suggest the gross amount of goods and services tax (GST) be included in the Australian Government's financial statements. However, under the

3 See inquiry website: http://www.aph.gov.au/house/committee/jpaa/defence/index.htm.

4 ANAO Audit Report No. 21, 2005-06, p. 30.

> *Intergovernmental Agreement on the Reform of Commonwealth-State Financial Relations,* GST is collected by the Australian Taxation Office as an agent for the States and Territories (the States), and appropriated to the States. Therefore, accrued GST revenues and associated payments to the States are not recorded in the financial statements.[5]

9.14 However, the ANAO argued that in substance, and from an accounting perspective, the GST is a revenue of the Australian Government, because:

- it is imposed under Australian Government legislation – the decision to enter into an agreement to pass on the GST revenue to the State and Territories is a separate transaction; and
- the GST revenue is distributed based on population share adjusted by a relativity factor, determined by the Treasurer.

9.15 According to the ANAO, the effect of not recognising the GST revenue was to understate the net result at year end by $35.8 billion for revenue, and $35.5 billion for expenses, and hence the Net Result (surplus) of $0.3 billion.[6]

9.16 The ANAO also points out that individual Commonwealth agencies report the GST as an Australian Government tax (ATO) and as grant expenses (Treasury).

9.17 The Committee notes that the GST has subsequently been recognised by the Australian Government as a Commonwealth tax.

Taxation revenue

9.18 Since 1998-99 the ANAO has qualified its audit opinion on the CFS based on a belief that the taxation revenue in the financial statements should be measured using the Economic Transaction Method (ETM). For the 2004-05 statements, taxation revenue was measured on a Tax Liability Method (TLM), which recognised taxation revenue the earlier of when an assessment of tax liability is made, or payment is received by the ATO or the Australian Customs Service.[7]

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5 Budget 2006-07 Budget Paper No. 1, Statement 10: *Australian Accounting Standards Financial Statements*, available at: http://www.budget.gov.au/2006%2D07/bp1/html/bp1_bst10-01.htm; accessed September 2006.

6 ANAO Audit Report No. 21, 2005-06, p. 31.

7 ANAO Audit Report No. 21, 2005-06, p. 32.

9.19 Under the ETM, taxation revenue would be recognised when the Government, through the application of legislation to taxable and other relevant activities, gains control of the future economic benefits that flow from taxes and other statutory charges.

9.20 Due to the ongoing disagreement over treatment of GST revenue, the ANAO and the Department of Finance and Administration (Finance) reviewed the methods of recognising taxation revenue. However, the two agencies could not come to an agreement. The Government asked the ANAO and Finance to conduct another review, with the aim of resolving the matter and incorporating any changes into the 2006-07 Budget year and the forward years – flowing onto future budget outcomes and the CFS.[8]

9.21 The Committee asked for an update on this review and was told that the ANAO and Finance had agreed to move to adopt the fuller accrual method favoured by the ANAO, except for certain items which would remain on the old methodology because they are not accurately available in the accrual methodology.[9]

9.22 The new accounting method, and its exclusions, is further explained in the 2006-07 Budget Papers:

> Australian Accounting Standards [AAS] seeks to recognise tax revenue when the economic event giving rise to the taxpayer's liability occurs. The budget and related outcomes adopt this treatment for measuring and recognising revenue of all categories of taxation [*Committee note: this is the ANAO's preferred methodology*].
>
> For individuals, company and superannuation revenue, such an estimation method is unreliable and tax revenue is recognised the earlier of when an assessment of a tax liability is made or cash payment is received by the Australian Taxation Office or the Australian Customs Service. This method is permitted under AAS when there is an inability to reliably measure taxation revenues at the time the underlying transaction or event occurs. Accordingly, for these categories of taxation revenue, there is a short lag between the time at which the underlying economic activity giving rise to the tax liability occurs and when the revenue is recognised.

8 ANAO Audit Report No. 21, 2005-06, p. 33.

9 Ms Anne Hazell, Department of Finance and Administration, *Transcript of Evidence* 2 June 2006, p. 6.

> Longer lags occur for some elements of company and superannuation funds taxation.[10]

Financial statement preparation

9.23 Under the *Charter of Budget Honesty Act 1998*, the Final Budget Outcome (FBO) must be published within three months of the end of the financial year (i.e. 30 September). Given the Commonwealth's move to an accrual budgeting and reporting framework in 1999-2000, Final Budget Outcome reports now incorporate audit cleared accrual based revenue and expenses, balance sheet and cash flow information. This information is obtained from the annual process of compilation of the Consolidated Financial Statements.[11] In practice, the imposition of the 30 September deadline for the FBO has tightened the timeframe for preparation of agency financial statements (even though they are not due to be tabled until 30 November each year), as audited financial statements are required to complete the FBO.

9.24 Under Section 55 of the FMA Act, the Finance Minister must present the CFS to the Auditor-General for audit as soon as practicable after the end of the financial year. If, after five months (ie 30 November), the CFS have still not been provided to the Auditor-General, the Finance Minister must table an explanation in both Houses of Parliament.[12]

9.25 In recent years, the CFS have not been provided to the Auditor-General by the 30 November deadline, because of late submission of audit-cleared material by 'key agencies' (including Defence).[13]

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10 Budget 2006-07 Budget Paper No. 1, Statement 10: *Australian Accounting Standards Financial Statements*, available at: http://www.budget.gov.au/2006%2D07/bp1/html/bp1_bst10-01.htm, accessed September 2006.

11 Department of Finance and Administration, *Annual Financial Reporting*, available at: http://www.finance.gov.au/budgetgroup/Annual_and_Monthly_Reporting_P/annual_financial_reporting.html, accessed August 2006.

12 *Financial Management and Accountability Act 1997*, available at CommLaw: http://www.comlaw.gov.au/ComLaw/Legislation/ActCompilation1.nsf/0/7FE7DA07542D4C39CA257156000A3646?OpenDocument, accessed August 2006.

13 See Department of Finance and Administration Annual Reports 2003-04 and 2004-05, available at: http://www.finance.gov.au/Publications/Annual_Reports.html, accessed August 2006.

9.26 Under guidelines issued by Finance in 2002, all government entities are required to provide audit-cleared financial statements[14] to Finance by 20 July. For the financial year ending 30 June 2005, Finance revised this date back to 30 July. The ANAO strongly supported this move, given the imposition of new Australian Equivalents to International Financial Reporting Standards (AEIFRS), and other resource pressures on entities.

9.27 However, despite the 10-day reprieve, the ANAO noted that for the 2004-05 financial year only 76 percent of general government sector entities were able to provide audit cleared statements to Finance by 30 July. This represented a deterioration from the previous year.

9.28 The ANAO noted that a key driver in an effective financial statement preparation process is project management. [15] The tight timeframe allows little 'fat' in the management process, and factors such as staff shortages or lack of experienced staff, exacerbates any existing problems.

9.29 To assist in better project management of the financial statements process, in April 2006 the ANAO released a *Better Practice Guide* on preparation of financial statements. The Committee has reviewed this Guide and commends the Audit Office on its publication. The Guide provides agencies with a comprehensive document outlining the financial framework and the essential steps in preparing financial statements, including checklists and examples. [16]

9.30 Finance also produces guidance in the form of its A-Model better practice guides – these are dummy statements to guide agencies in presentation of information.[17]

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14 The term 'audit cleared' means that although the ANAO has not issued an audit report, the audit of material balances has not disclosed any reasons that would prevent Finance from consolidating financial information for the purpose of preparing the FBO and CFS.

15 ANAO Audit Report No. 21, 2005-06, p. 53.

16 ANAO: *Preparation of Financial Statements by Public Sector Entities*, 13 April 2006, available at: http://www.anao.gov.au/WebSite.nsf/ViewPubs!ReadForm&View=BetterPracticeGuidesByDate&Title=Better%20Practice%20Guides%20by%20Date%20(Latest%20First)&Cat=&Start=1&Count=10, accessed August 2006.

17 A-Model guides available at: http://www.finance.gov.au/ace/amodel_2005-2006.html, accessed August 2006.

Implementation of AEIFRS

9.31 As the Committee has heard in its Defence inquiry, the implementation of the Australian Equivalents to International Financial Reporting Standards has placed a significant burden on public sector entities. The Australian Accounting Standards Board (AASB) mandated that AEIFRS must be introduced from 1 January 2005. For most government entities, this means that 2005-06 was the first year of reporting under these new standards.

9.32 However, the AASB required that the financial statements for 2004-05 explain how the transition to AEIFRS was being managed, the key differences in accounting policy arising from the transition, and any impact on the reporting process. In addition, to ensure that government agencies were progressing with implementation of AEIFRS, Finance required agencies to produce a range of AEIFRS compliant data, to provide comparative data for the 30 June 2006 financial year.

9.33 The ANAO was unable to comment on the full impact of AEIFRS on Australian Government financial statements, but did surmise that the new requirements would result in more volatility in the results reported on an accrual basis, particularly because AEIFRS recognises more rights and obligations in financial statements, and requires the measurement of the present value of long-term liabilities. The ANAO also noted the particular compliance difficulties that would be encountered by the Department of Defence, given the previous year's statements were subject to a 'no opinion' audit finding.[18]

Specific agency findings

9.34 The financial statements audit revealed a number of agencies with audit qualifications in the A or B categories. The Committee selected three of these agencies, with a higher number of significant findings, for closer examination.

Department of Environment and Heritage

9.35 During 2004-05 there were two significant changes to DEH – the transfer of some indigenous programs from the then Department of Immigration and Multicultural and Indigenous Affairs, following the abolition of ATSIC; and the incorporation of the Australian Greenhouse Office and the

18 ANAO Audit Report No. 21, 2005-06, p. 25.

National Oceans Office into the department. These changes, together with increased staff and superannuation expenses, resulted in an increase in DEH's expenses in 2004-05.

9.36 There were no Category A findings for DEH.

Category B findings

9.37 The ANAO identified eight Category B audit findings at its interim Audit (April 2005). Only one was resolved by DEH at the close of the financial statements period.[19] These issues were:

- deficiencies in the financial statement preparation process;
- the reconciliation of leave balances – DEH could not reconcile recreation and long service leave balances between its HR and financial systems;
- reconciliation of financial records – there were some issues in reconciling DEH's financial records to bank accounts, and to Finance records;
- reconciliation of special accounts – DEH had not been reconciling special account ledgers to the bank account and Finance records;
- access management – ANAO identified weaknesses in key systems' security controls;
- Fraud Control Plan – at March 2005 DEH did not have a current Fraud Control Plan. By August 2005 DEH was finalising a plan;
- Business Continuity Plan – DEH did not have a formally established, department-wide business continuity management plan. Some work had been completed, but testing and final endorsement was yet to occur.

9.38 A further four Category B issues were identified during the final phase of the audit:

- management of grants and suppliers – there were several instances where grants and suppliers were expensed and a liability recorded prior to the obligation arising (ie the work being undertaken);
- use of accounts – accounts used for grants, suppliers, payroll and bank transactions were not being reviewed in a timely or correct manner;

19 ANAO Audit Report No. 21, 2005-06, p. 144.

- recognition of restitution costs under international treaties – under the Antarctic Treaty, Australia must provide for restitution of the Antarctic base, under certain circumstances. Under current accounting standards, these 'make good' costs must be reflected as a provision in the accounts. DEH was unable to provide an estimate of these costs for 2004-05;
- non-financial assets management – the Australian Antarctic Division manages a significant balance of DEH's non-financial assets, using a separate asset register. The department did not provide complete information to the independent valuer engaged to value these assets, and also had some problems with some of the independent valuer's findings. The ANAO recommended that DEH closely monitor the information provided to valuers.

9.39 In July 2006 the Committee wrote to DEH asking for an update on the status of the above audit issues. The department replied that it was hopeful, subject to ANAO auditing, of achieving a 'clean sheet' against each of the 2004-05 audit issues in the 2005-06 financial statements. The department's financial management team had been bolstered by new recruitment, and other audit issues were being managed via detailed project plans and use of greater resources where needed.[20] The Committee notes that DEH resolved all these issues in the 2005-06 financial statements.[21]

Legislative breach

9.40 The Committee notes that although the ANAO report identified that DEH had overdrawn on a number of its bank accounts, the DEH submission argued that this had now been identified as erroneous.[22]

9.41 The ANAO argued that the agreements in place still did not provide for an overdraft. However, given improvements in controls over cash management, and the fact that the level and number of instances of overdraft had significantly reduced, the breach was no longer reported in subsequent audit reports.[23]

20 DEH, submission No. 7 [letter dated 27 July 06].
21 ANAO Audit Report No. 15, 2005-06, p. 140.
22 DEH, submission No. 7, p. 1.
23 Correspondence from the ANAO, 20 September 2006, p. 1.

Department of Family and Community Services[24]

9.42 The ANAO identified 12 Category B audit findings in its interim review (March 2005). By the end of the audit, the ANAO was satisfied that six of these issues had been fully addressed, and reasonable progress had been made against the remaining, which were:

- review of audit trail logs and privileged accounts;
- shortcomings in accounts payable process;
- adequate monitoring of expenditure per outcome;
- correct classification of departmental/administered payments;
- currency of financial policies and procedures; and
- unrecorded prior employment service.

9.43 However, a further eight new audit issues were identified in the final phase of the financial statements audit, outlined below. [25]

Problems with the Financial Management Information System (FMIS)

9.44 The ANAO identified significant control weaknesses in the FMIS. ANAO acknowledged that FaCS was undertaking follow-up action, which would reduce the risks.

- FMIS system account passwords – a specific problem with the FMIS was that there were four default privileged user accounts with commonly known passwords. These accounts had powerful access rights and could allow unauthorised access to the system. FaCS was in the process of changing the passwords.
- Monitoring of privileged system access – there was a lack of monitoring of privileged system access to the FMIS, increasing risk of unauthorised or inappropriate system access.
- Security access – an audit of access to the FMIS revealed that some users had inappropriate access, excessive access or access not required to perform their duties. This increases the risk of unauthorised access, resulting in changes to the system that cannot be detected.

24 Following the changes announced by the Prime Minister on 24 January 2006, the Family and Community Services (FaCS) portfolio was expanded to form the new Families, Community Services and Indigenous Affairs portfolio (FaCSIA). FaCS will continue to be used in this section as that was the departmental name at the time of the audit.

25 ANAO Audit Report No. 21, 2005-06, p. 154.

Reporting of commitments

9.45 Commitments are undertakings or future payments under a contract that will result in liabilities in future periods. The FaCS reporting system at the time of the audit not fully identify and report on future commitments, exposing FaCS to the risk of incomplete and inaccurate year-end figures.

IT security

9.46 The ANAO found that there was a lack of formal definition of roles within FaCS, increasing the risk that critical IT security activities may not performed, or will be duplicated. Ownership of different business and application systems needed to be formally allocated to business managers, to ensure accountability and responsibility.

9.47 The ANAO also found that FaCS did not regularly review the effectiveness of IT controls in place in an outsourcer's environment. There had been no independent audit of the IT control framework. FaCS was in the process of developing a compliance and audit program for its own and outside IT operations.

Business/disaster planning

9.48 The ANAO found that there could be improvements in the linkages between the FaCS Business Continuity Plan and its risk assessment/management strategy. There was no Disaster Recovery Plan in place, although one was under development.

Legislative breaches

9.49 Under Section 8 of the FMA Act, an entity must enter into an agreement for an overdraft on its official accounts, if the overdraft is for more than 30 days. One FaCS account was in overdraft from 1 July 2004 to 31 January 2005, for amounts ranging from $910,779 to $8,235,372.

9.50 The ANAO found that FaCS had breached Section 31 of the FMA Act, and accordingly Section 83 of the Constitution, by holding an ineffective Section 31 Agreement (Net Appropriation Agreement). The agreement was ineffective because either the Finance or FaCS official who signed the agreement did not have an express authorisation or delegation from their Minister to do so. A separate ANAO performance audit has identified this as a common problem across a number of agencies (reviewed at a separate public hearing).

Australian Taxation Office

9.51 The ANAO reported that the ATO had initiated a number of projects to clear the audit qualifications raised in the 2003-04 financial statements audit. The ANAO was satisfied that this progress provided reasonable assurance that the 2004-05 financial statement balances were materially correct.

9.52 However, the 2004-05 audit highlighted key issues relating to the need for improved accounting over processing of significant financial transactions. This resulted in four Category A and 15 Category B audit findings for the 2004-05 financial statements. These are outlined below.

Category A Findings

Preparation of the administered financial statements

9.53 The ANAO noted that the financial statements preparation process was streamlined for the 2004-05 statements. As a result of the new processes, adjustments of some $6.79 billion were made to the ATO financial statements, in response to ANAO representations. $3 billion of these adjustments occurred very late in the preparation process. The ANAO commented that this raises governance issues in regard to the ATO being able to deliver a complete set of financial statements within the required timeframe:

> The level of adjustments highlighted the need for a complete understanding by the preparers together with active involvement by management over quality assurance and analysis in the financial statement preparation process. There is also scope to improve the timing, quality and level of supporting documentation.[26]

9.54 The Committee followed up on this issue at the public hearing, asking the ATO to explain why nearly $7 billion in adjustments were made late in the preparation process. The ATO explained that as part of the new process, realised that it had to produce full accrual estimates on a number of administered expenses, such as the diesel fuel rebate, the baby bonus and the super co-contribution, in the financial statements. The 2004-05 statements were the first in which these items were reported as full accrual estimates. The ATO told the Committee that the adjustments, in particular the $3 billion in late adjustments, were a result of the complexities in

26 ANAO Audit Report No. 21, 2005-06, p. 224.

implementing the new accounting treatment, and the time pressures involved in meeting the financial statements deadlines:

> We were preparing numbers and the auditors were auditing them at the same time, so we did not have time to put in some of the quality control processes that we would have liked. All of those things came together and…[the auditors] identified that, in changing the accounting treatment, we had not necessarily got all of that right.[27]

9.55 The Committee sought reassurance that the ATO now has systems in place to cope with the accounting changes. The ATO replied that as there were no new accounting practices for the 2005-06 financial statements they expected more stability in producing the reports. The ATO also reported that they have worked on estimation and preparation processes to have 'better clarity about what the numbers are, how they are being produced and what they mean.'[28]

9.56 While the Committee understands that the implementation of a new accounting system or preparation process causes difficulties, it is worrisome that the ANAO picked up such large discrepancies in the ATO's calculations for 2004-05.

9.57 The Committee observed the Auditor-General's assessment of the ATO 2005-06 financial statements to satisfy concerns that similar major accounting flaws were not repeated in the 2005-06 financial year's statements. The Committee noted that the preparation of financial statements issue had not been resolved in the 2005-06 financial statements, but had been reclassified as a moderate risk matter. However, the Committee is concerned that the ANAO found two new significant risk issues in the 2005-06 financial statements.[29]

Calculation and posting of the General Interest Charge to client accounts

9.58 In the 2003-04 financial statement audit the ANAO identified a problem with the General Interest Charge (GIC) not being applied to all taxpayer accounts for companies and superannuation funds, in respect of outstanding annual income tax payments. The ATO provided an estimate of the revenue impact of this omission, however the ANAO found that it was unable to form an opinion on the estimated GIC revenue and therefore issued a qualification on that line in the accounts.

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27 Ms Madonna Moody, Australian Taxation Office, *Transcript of Evidence* 2 June 2006, p. 3.

28 Ms Madonna Moody, Australian Taxation Office, *Transcript of Evidence* 2 June 2006, p. 4.

29 ANAO Audit Report No. 15, 2005-06, p.216.

9.59 The ANAO noted that for the 2004-05 financial statements the ATO had made system changes to rectify the problem, and a reliable calculation could be determined for the 2004-05 financial statements.[30] The ATO has reported to the Committee that at 30 June 2006 that the following percentages of taxpayer accounts had been reviewed and GIC (and remission if appropriate, see below) had been posted to their accounts:

- 98.8 percent of companies and superannuation funds;
- 99.9 percent of individual and trust accounts; and
- 99.4 percent of Fringe Benefits Tax (FBT) accounts.[31]

9.60 The Committee asked if, once the error in calculating and charging the GIC was discovered, the GIC had been applied to taxpayer accounts retrospectively. The ATO replied that the GIC had been applied retrospectively to such accounts. However, the charge was remitted for accounts that had accrued over a substantial period of time, where the taxpayer had paid off their account balance but had not been notified of the accruing GIC liability.[32]

Supporting documentation

9.61 The ANAO found that the documentation of key elements of the ATO's financial reporting needed improvement, particularly in relation to the adequacy, validity and completeness of supporting documentation and to demonstrate that quality assurance checks have been performed. In particular, the ANAO was concerned about the parameters used to extract information from a data warehouse, and also the trail used to identify the data source which was supporting the financial statement balances, which was only provided at the ANAO's request.[33]

9.62 The Committee asked for an update on the ATO's steps to improve supporting documentation for the financial statements process. The ATO replied that improvements included the development of a template and procedures, agreed to by the ANAO, in advance of the financial statements 2005-06 process; and that the department had implemented a four-way management review and sign-off process.[34]

30 ANAO Audit Report No. 21, 2004-05, p. 224.

31 ATO, submission No. 4.2, p. 2.

32 ATO, submission No. 4.2, p. 2.

33 ANAO Audit report No. 21, 2004-05, p. 224.

34 ATO, submission No. 4.2, p. 3.

Management analysis of the estimation process

9.63 The ATO financial statements are prepared using estimates of the revenues to be accrued each year. The ANAO found that the estimation of accrued revenues is based on various economic models. However, there was no evidence of management review of the analysis by the ATO specialists over the economic models and the supporting documentation. An ANAO review of the approach used by the ATO led to the development of more robust disciplines for estimating a number of balances, such as fuel subsidies, family tax benefits and super co-contribution.[35]

9.64 The ATO reported that it has strengthened its management review processes. The economic models are developed by the ATO's review analysis area, and the corporate finance area is responsible for the preparation of the financial statements. The estimates methodology is now signed off by: a senior executive in the review analysis area; a senior executive in the corporate finance area; the Deputy Commissioner responsible for the revenue or expense product; and the Chief Finance Officer.[36]

Category B Findings

9.65 At the end of the financial statement period the ATO attracted a number of Category B findings. The new findings were in relation to:

- the superannuation surcharge;
- the Superannuation Guarantee Charge;
- the control self assessment framework;
- the Certificate of Compliance – Payment of public money; and
- SAP security.

9.66 The Committee sought an update on each of these findings and was satisfied with the ATO's progress towards resolving these issues (see ATO submission 4.2 for further detail).

9.67 Outstanding Category B findings from the audit included:

- agreements for the provision and receipt of services between the ATO and other Australian Government entities;
- costing of internally developed software;

35 ANAO Audit report No. 21, 2004-05, p. 224.

36 ATO, submission No. 4.2, p. 3.

- user access to payroll and recruitment functions;
- system for making emergency fixes during processing of transactions;
- finalising Business Continuity Plans;
- consolidating reconciliations for superannuation and FBT;
- management of special accounts; and
- the Certificate of Compliance process relating to Excise, Superannuation business systems, Higher Education Contribution Scheme, Legacy systems and third party refunds.

9.68 The ATO reported that at the time of the Committee's review (August 2006), the ANAO was still completing its audit of the 2005-06 financial statements and therefore the status of these audit findings was yet to be finalised. In the ensuing 2005-06 report, the ANAO found that the ATO had only resolved half of the 2004-05 Category B findings prior to August 2006. The 2005-06 financial statements audit also identified four new Category B findings, which included the downgrading of two 2004-05 Category A findings the ANAO had assessed the ATO to have significantly addressed but not rectified.[37]

Committee comment

9.69 The Consolidated Financial Statements, audited by the ANAO, provide an important accountability mechanism. This ANAO report on its audit of Government entities' financial statements for 2004-05 notes that a number of agencies have appeared to struggle to meet the financial reporting timeframes and to adjust to the new reporting requirements under the Australian Equivalent of the International Finance Reporting Standards. These issues were noted by the Committee in its review of equipment acquisition and financial management at the Department of Defence.

9.70 Some common themes emerged in the audits of the three agencies under specific review by this Committee:

- business planning – better management of financial statements process; a lack of current or integrated fraud control plans, business continuity plans;

37 ANAO Audit Report No. 15, 2005-06, p. 220.

- IT Security/governance; and
- legislative compliance – special accounts (ATO); overdrawn accounts (DEH and FaCSIA).