Guidance

supporting the Standing Directions of the Minister for Finance 2016

June 2016

(Updated July 2018)

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State Government

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ISBN 978-1-922222-75-6 (pdf/online)
Published August 2016

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dtf.vic.gov.au

Guidance

This Guidance is issued by the Department of Treasury and Finance to provide further information to support Agencies to implement the Standing Directions of the Minister for Finance (Directions) and Instructions.

Guidance is **not mandatory** and is for reference only.

The numbering of the Guidance corresponds with the associated Directions.

Queries may be directed to Standing.Directions@dtf.vic.gov.au. .

The Guidance is as follows:

Guidance 1.5 – Exemptions

Objective	To assist Agencies in applying for exemptions from the Directions
Effective Date	1 July 2016
Relevant Direction	1.5 Exemptions
Last Reviewed	1 February 2016

Summary

Section 8(d) of the FMA, and Direction 1.5, provide that the Minister for Finance may exempt an Agency from specific or all requirements in the Directions and Instructions.[1]

Direction 1.5 sets out the minimum requirements for an exemption request: that it be in writing, state the reasons for the exemption, and specify proposed alternative action or procedures.

The Directions and Instructions are intended to set down the minimum financial management standards for the Victorian Public Sector (VPS). Accordingly, exemptions will only be granted in exceptional circumstances. Agencies should only seek an exemption as a last resort.

Preparing to apply

Before applying for an exemption, an Agency should closely consider whether the exemption is required. It may be that the relevant Direction can be achieved without the need for an exemption. It should be kept in mind that the Directions are intended to be applied in a manner consistent with the size and risk profile of Agencies: see Direction 1.1(b).

If an exemption is required, the Agency should identify the minimum exemption necessary.

Agencies should consult with their Portfolio Department and DTF as soon as possible before making a formal exemption request. This may save time and effort later, and provide a chance to ensure that the application is tailored appropriately.

Agencies should dedicate sufficient time and resources to preparing a strong case for an exemption.

How to apply

An Agency should apply for an exemption by letter from their Accountable Officer or Responsible Minister to the Minister for Finance. The application should also be copied to DTF.

An Agency should include the following information in the application:

- the Directions and/or Instructions from which the exemption is sought;
- the reasons for seeking the exemption (see discussion below);
- relevant information about the Agency, including size and risk profile if relevant;
- details of any previous or existing exemptions of the Agency;
- alternative action or procedures to ensure that the objectives of the relevant Directions are achieved; and
- the duration of the exemption: for a specified period, or ongoing.

Reasons for an exemption

An Agency seeking an exemption needs to provide reasons that demonstrate to the Minister for Finance that it has a compelling case for an exemption.

[1] Note that the Directions provide that the DTF Deputy Secretary, may grant exemptions from Instructions. See discussion under 'Exemptions from Instructions' below.

An Agency may provide the following information to support its case for an exemption:

- an explanation of how the exemption sought and alternative arrangements proposed would not undermine the integrity of the Agency's financial management systems and the objectives of the Direction;
- a description of the effects on the Agency of (a) being granted, and (b) being denied, the exemption;
- a cost-benefit analysis, or other analysis, of the exemption; and
- relevant supporting material.

Demonstrating that the exemption will result in a **clear net benefit** to the Victorian community may be persuasive. A 'net benefit' is an overall positive impact on the community. It takes into account the costs and benefits related to economic impact, financial risks and other matters. Assessment of the benefit to the community will be informed by the nature of the Agency's operation and services. A potential cost of any exemption is the risk associated with an Agency being subject to a different standard of financial management to the rest of the VPS.

Evaluation and response

DTF evaluates exemption applications on a case-by-case basis, and makes a recommendation to the Minister for Finance. Careful consideration will be given to the application, the costs and benefits to the Victorian community, risks, and the impact on the Agency of granting or denying the exemption. DTF will also have regard to the purpose of the Direction and the impact that granting the exemption would have on the integrity of the financial management framework.

DTF may contact an Agency to clarify aspects of the exemption application. This is more likely if the Agency has not consulted with DTF prior to lodging the application.

The Minister for Finance makes the ultimate decision about whether to grant or reject a request for exemption. The Minister will respond by letter to the Agency.

After an exemption

An exemption may be provided for a specified time period or on an ongoing basis. It will relate to specific Directions and/or Instructions, or to the Directions and/or Instructions as a whole.

The exemption may be subject to conditions. Usually, implementation of the proposed alternative action or procedures will be a condition of the exemption. In some cases, the Agency may also be required to provide an annual assurance that there has not been any significant change to the Agency's risk profile and functions, or a relevant adverse key audit finding. If such a condition is not complied with, the exemption may lapse.

Under Direction 3.2.1.2, where an Agency is exempt from the requirement to maintain an Audit Committee, the Responsible Body must actively assume the responsibilities of an Audit Committee, and take appropriate steps to ensure these responsibilities are fully discharged.

After receiving an exemption, the Agency should implement the proposed alternative action or procedures immediately.

Direction 1.5 provides that the Accountable Officer must maintain a register of exemptions (including any conditions) granted by the Minister, and must make the register available for inspection by the Auditor-General.

DTF also maintains a register of exemptions.

Exemptions from Instructions

The Directions provide that the DTF Deputy Secretary may make and issue Instructions, and may grant exemptions from Instructions. If an Agency intends to seek an exemption from an Instruction, without seeking to be exempt from any Directions, it may do so by writing to the DTF Deputy Secretary. In doing so, the Guidance above should be considered.

The Minister may also give exemptions from Instructions.

Exemptions in relation to 2003 Directions

Exemptions from the previous 2003 Standing Directions do not carry over into the 2016 Directions. Any agency that had an exemption in place in relation to the 2015-16 financial year, which wishes to continue to receive an exemption for 2016-17, needs to re-apply in accordance with the 2016 Directions and this Guidance.

Guidance 1.6 – Glossary of terms

Objective	Provides definitions as guidance in interpreting the Directions and Instructions.
Effective date	1 July 2016
Relevant Direction	1.6 Definitions and interpretation
Last reviewed	1 February 2016

The following glossary of terms is provided as guidance to help interpret the Directions.

* An asterisk indicates that the relevant term is defined in the Directions.

Term	Description
Accountable Officer*	Has the same meaning as para (a) of the definition of *accountable officer* in section 3 of the FMA.
Agency*	Means any Public Body or Department.
Annual Report*	Means the report of operations and financial statements prepared under section 45 of the FMA, except in relation to an Agency to which section 53A(1) of the FMA applies, in which case it means the annual report, including audited financial statements, required to be submitted under section 53A(4) of the FMA.
Audit Committee*	Means an audit committee established in accordance with Direction 3.2.1.
Authorised Deposit Taking Institutions (ADIs)*	Corporations that are authorised under the *Banking Act 1959* and are prudentially supervised by the Australian Prudential Regulation Authority (APRA). ADIs include banks, building societies and credit unions.
Authority*	Has the same meaning as *authority* in section 3 of the FMA.
Borrowing/financial accommodation	Has the same meaning as in the *Borrowing and Investment Powers Act 1987.*
CFO and Chief Finance Officer*	Have the same meaning as *chief finance and accounting officer* in section 3 of the FMA.
Controlled Entities*	Means those entities in the 'Controlled Entities' list in the notes to the most recent annual financial report for the State of Victoria.
Commercial based acquisitions	Includes a range of acquisition activities such as procuring goods, services (including commissioning), and investing in assets and infrastructure.
Compliance Deficiency*	Attribute, condition, action or omission that is not fully compliant with an applicable requirement in the FMA, Directions and/or Instructions.
Compliant	A Public Sector Agency which is compliant with the Directions and Instructions.
Commodity risks	Risks arising from future changes in the price and/or availability of commodities.
Corruption*	Has the same meaning as in the latest Australian Standard on *Fraud and Corruption Control* (AS 8001). [Dishonest activity in which an employee of an entity acts contrary to the interests of the entity and abuses his/her position of trust in order to achieve some personal gain or advantage for him/herself or for another person or entity.]
CSV*	Means Court Services Victoria established under the *Court Services Act 2014*.
Department*	Has the same meaning same as in section 3 of the FMA.

Term	Description
Departmental funding model	The model used by the Government to fund the general government sector (comprising the department and the portfolio general government sector Agencies), where the Government determines the outputs to be delivered by a Portfolio Department and the price for each of the outputs for a given level of quantity, quality and timeliness. The output price is derived from unit pricing, where revenues need to be sufficient to cover all expenses incurred in the delivery of an output, including depreciation (in the form of depreciation equivalent revenue).
Directions*	Standing Directions issued by the Minister for Finance under section 8 of the FMA.
Discretionary financial benefits	A financial benefit given to a person or body for a specified purpose directed at achieving outcomes sought by government policy (e.g. grants, sponsorships and donations).
Donations	Gifts given by the Public Sector Agency, typically for charitable purposes and/or to benefit a cause. They impose no obligations on the recipient and offer little or no rights or benefits to the provider.
DTF*	Means the Department of Treasury and Finance in its capacity as a central agency supporting the Minister in administration of the FMA.
DTF Deputy Secretary*	Means the Deputy Secretary of DTF's Budget and Finance Division, or anyone who occupies that office temporarily or any DTF officer who becomes responsible for the functions of that office from time to time.
Employee	A person employed by a Public Sector Agency and paid an annual salary. This includes persons employed on a 'fixed term' basis who are on the Agency's payroll and performs a public service function. On-hire workers are the employees of the master vendors, not the Department. For differences between employees, contractors and consultants, refer to Financial Reporting Direction 22D and Guidance, and the Victorian Public Sector Commission's Guidance for Managers Engaging Contractors and Consultants to Perform a Public Sector function[2].
Exempt trust money	Money, other than money held on trust for the State or a Public Body, invested pursuant to a statutory function to hold it on trust for a known beneficiary. Consequently these funds should be sourced from an entity or person external to the State of Victoria, and must be returnable to this source. These funds should be held in a separate trust account.
Financial arrangement/derivative	Has the same meaning as in the *Borrowing and Investment Powers Act 1987.*
Financial Reporting Direction*	Means the Financial Reporting Directions issued under section 8 of the FMA.
FMA*	Means the *Financial Management Act 1994*.
Fraud*	Has the same meaning as in the Australian Standard on *Fraud and Corruption Control standard* (AS 8001).
General government sector Agencies	Comprises all government Departments, offices and other government Agencies engaged in providing public services free of charge or at prices significantly below the cost of production. Some of these entities may also earn revenue from commercial activities; however such revenue represents less than half of their total revenue.
Government objectives and/or priorities*	Means: (a) in relation to all Agencies apart from Independent Offices and CSV, the stated objectives and priorities of the government of the day; and (b) in relation to Independent Offices and CSV, the functions and/or objectives for which they were established as specified in their governing legislation.

[2] http://vpsc.vic.gov.au/html-resources/guidance-for-managers-engaging-contractors-and-consultants/

Term	Description
Grant	Money given to organisations or individuals for a specified purpose directed at achieving goals and objectives consistent with government policy, where the recipient is selected on merit against a set of criteria.
High Value High Risk (HVHR)	Projects that have a total estimated investment (TEI) of $100 million or more (regardless of funding source), and/or are projects identified as high risk under the Gateway Project Profile Model (PPM), and/or are projects nominated by Government as HVHR.
Incorporated committee of management	Has the same meaning as incorporated committee in section 14B of the *Crown Land (Reserves) Act 1978*.
Independent Office*	Means: (a) the Victorian Auditor General's Office; or (b) the Office of the Victorian Ombudsman; or (c) the Victorian Electoral Commission; or (d) the Independent Broad-based Anti-corruption Commission; or (e) the Victorian Inspectorate.
Instructions*	Means the mandatory instructions made by the DTF Secretary under delegation of the Minister for Finance.
Intangible assets	Identifiable non-monetary assets without physical substance (AASB 138 *Intangible Assets*). They are the long-term resources of an entity and derive their value from intellectual or legal rights, and from the value they add to the other assets.
Investment	A financial asset, as defined in Australian Accounting Standard AASB 132 *Financial Instruments: Presentation,* which is not a trade receivable, a loan receivable and an advance receivable.
JCV*	Judicial College of Victoria established under the *Judicial College of Victoria Act 2001.*
Material Compliance Deficiency*	Means a Compliance Deficiency that a reasonable person would consider has a material impact on the Agency or the State's reputation, financial position or financial management.
Other Loss*	A loss caused by any intentional or negligent act or omission, including theft, vandalism and arson and excluding acts of God.
Portfolio Agency*	In relation to a Portfolio Department, an Agency (apart from Independent Offices and CSV) which shares the same Responsible Minister as that Portfolio Department.
Portfolio Department*	Has the same meaning as defined in part (a) of *department* in section 3 of the FMA.
Prepaid debit card (also known as stored value card)	Means a card which has money 'stored' via prepaid deposits made by a Public Sector Agency for use by the Agency and their employees for official business, or in the case of cards issued to the public for the benefit of the recipient of the card. The card must not link directly to a bank account or credit facility.
Public body*	Has the same meaning as *public body* in section 3 of the FMA.
Public financial corporations (PFCs)	Agencies engaged primarily in the provision of financial intermediation services or auxiliary financial services.
Public non-financial corporations (PNFCs)	Agencies engaged in the production and sale of goods and services within a competitive market that is non-regulatory or non-financial in nature.
Public resources	All financial resources the Agency is responsible for directly or indirectly (e.g. resources managed on behalf of the State), including budgeted expenditure, revenue and administered items.
Purchasing card	Means any type of purchasing card used for the purchase of generic goods and services for use by Public Sector Agencies and their employees for official business (i.e. general government purchasing card, corporate card, credit card, purchasing card facility). It includes a purchasing card issued by an Agency to the employee in the name of the Agency.

Term	Description
Responsible Minister*	Means: (a) In relation to a Department (other than an Independent Office), the Minister or Ministers for the time being responsible for any part of that Department; (b) in relation to an Independent Office, the Responsible Body; (c) in relation to all other Agencies, the Minister or Ministers for the time being administering the legislation or enactment under which the Agency is established or as otherwise declared by way of that establishing legislation or instrument.
Responsible Body*	Means (a) In relation to an Agency with a statutory board or equivalent governing body established by or under statute, that board or governing body; and (b) in relation to an Agency without a statutory board or equivalent governing body established by or under statute, that Agency's Accountable Officer.
Significant or Systemic*	Means an incident, or a pattern or recurrence of incidences, that a reasonable person would consider has a significant impact on the Agency or the State's reputation, financial position or financial management.
Sponsorship	Purchase or receipt of rights or benefits, including naming rights, delivered through association with an organisation's products, services or activities. The rights or benefits typically relate to the sponsor's reputation management or communication objectives. Sponsorship includes partnership arrangements, except where the arrangement is governed by the *Partnerships Victoria Requirements 2010* or otherwise involves the development or management of infrastructure. It does not include grants, donations/bequests, sale of advertising space, editorial comment, or advertorials.

Guidance 2.3.4 – Portfolio relationship

Objective	Provides Portfolio Departments and Portfolio Agencies with guidance on their roles and responsibilities in relation to one another, including: • advice to the Minister from Portfolio Departments on matters relating to Portfolio Agencies; • Portfolio Departments support for their Portfolio Agencies; • Portfolio Agencies responsibility to inform their Portfolio Departments; and • how the relationship can contribute to managing the Government's whole of state financial management performance.
Effective date	1 July 2016
Relevant Directions	2.3 Accountable Officer 2.4.4 Responsibilities of Portfolio Department CFO 5.1.7 Portfolio Departments' reporting to DTF 5.3 External reporting and information provision
Last reviewed	1 February 2016

Ministers are accountable to the Parliament and public for the performance of their Agencies. They have constitutional and legislative governance responsibility for the Agencies in their portfolio. To carry out these responsibilities, Ministers require support from portfolio Departments to provide advice on the operations and performance of Portfolio Agencies. Portfolio Departments and Portfolio Agencies also have responsibilities in relation to one another.

These relationships are described in section 13A of the *Public Administration Act 2004* (PAA), which provides that[3]:

- the Accountable Officer of a portfolio Department must advise the relevant Minister on matters relating to a Portfolio Agency, including the discharge by the Agency of its responsibilities;
- the Accountable Officer of a portfolio Department must work with, and provide guidance to, their Portfolio Agencies to assist them on matters relating to public administration and governance;
- a Portfolio Agency must provide to the Accountable Officer of a portfolio Department any information required to enable the Accountable Officer to advise the Minister on matters related to the Agency (this requirement applies unless the Agency is prohibited from doing so under law); and
- the Accountable Officer of a portfolio Department must **not** direct or control a Portfolio Agency in the performance of the functions conferred on the Agency under law.

The Treasurer and the Minister for Finance are accountable to Parliament for the financial management performance of the State of Victoria and their obligations under the FMA.

Portfolio Departments have a role to help:

- safeguard the State's resources;
- manage financial risks;
- support the government's financial management and performance accountability to Parliament at Agency, portfolio and whole of State levels;
- support the portfolio Ministers in their oversight of the portfolio as a whole, and of Agencies individually;
- support the Treasurer and Minister for Finance by providing DTF with quality information about the portfolio; and
- facilitate portfolio outcomes and their contribution to achieving the State's fiscal objectives and strategy.

The Directions include specific requirements for Portfolio Departments, Portfolio Agencies and DTF in relation to the portfolio relationship, including in Directions 2.3.3, 2.3.4, 2.3.5, 2.4.3, 2.4.4, 5.1.7 and 5.3.

[3] This is a summary of section 13A of the PAA. See the PAA for the full details.

The focus for Portfolio Departments is on working with, and providing guidance to, their Portfolio Agencies. A Portfolio Department cannot direct or control a Portfolio Agency in relation to the performance of its statutory functions.

The Directions seek to improve the relationship between Portfolio Departments and Portfolio Agencies in relation to financial management, performance and sustainability. This will improve the information available to Portfolio Departments to support:

- their portfolio Ministers, on individual Agency and portfolio financial performance matters; and
- government, on whole of state financial performance.

These expectations aim to ensure portfolio and whole of government issues and risks are managed effectively and to improve government outcomes.

Portfolio Department responsibilities

Key functions

The Victorian Public Sector Commission (VPSC) articulates the role of the departmental Secretary as the principal portfolio adviser to government on policy matters and to assist Ministers maintain an awareness of operations within their portfolios. The Departmental Secretary often acts as the interface between Ministers, portfolio Agencies and stakeholders.

Consistent with these expectations, portfolio Departments advise and support their portfolio Ministers on financial management by:

- monitoring Portfolio Agencies to the extent required to appropriately advise the Minister;
- advising the Ministers on matters relating to portfolio Agencies;
- working with, and providing guidance to, their portfolio Agencies;
- facilitating and coordinating portfolio delivery of intended government policies and priorities including efficiency and effectiveness; and
- facilitating liaison and information sharing between Agencies and their Ministers, and with DTF on whole of government financial management and performance matters.

Appropriately advising the Minister of matters relating to portfolio Agencies will usually require a Portfolio Department to monitor its Portfolio Agencies to some extent. In doing so, Portfolio Departments should maintain an up-to-date record of portfolio Agencies and be aware of the portfolio Agencies' roles and responsibilities, risks and issues, and planned and actual performance.

The requirement to advise Ministers will assist to provide Ministers with early warning of portfolio issues. This advice should focus on governance, risk and organisational profile matters, assessing the financial and related performance of Agencies, and advising Ministers of issues to avoid surprises and mitigate risks.

Major Portfolio Agency risks/issues may include:

- outstanding legal action or potential legal exposure;
- performance audits/investigations scheduled or underway;
- current media issues and attention;
- governance and management issues such as Fraud, financial performance and sustainability; and
- any other reputational risks.

This is not an exhaustive list of risks, but is intended to prompt Agencies to identify key risks.

Working with, and providing guidance to, Portfolio Agencies is required to assist agencies and to improve the advice available to the Minister.

Facilitating and coordinating portfolio delivery will help to ensure that Agencies' plans align with the delivery of government policy and priorities, and can consider establishing more effective and efficient governance and operational inter-agency arrangements across the portfolio (e.g. shared services, co-location).

Facilitating liaison and information from and between portfolio Agencies builds on the portfolio coordination function to ensure timely and accurate information is provided to government Ministers and DTF, to effectively manage whole of government matters.

Nature and extent of portfolio relationship

The nature and extent of portfolio relationship will vary according to the level of financial management risk and performance of the individual Portfolio Agency in question. For example, incorporated committees of management are likely to require a different nature and extent of relationship with the Portfolio Department than a large statutory corporation.

The requirement for a relationship applies, at some level, to all portfolio Agencies, regardless of the form of establishment and whether they are legally required to fully apply the FMA (e.g. government controlled companies).

An alternative to a 'one size fits all' approach to managing the relationship between Portfolio Departments and Portfolio Agencies is for Departments to tailor their approach to meet the relevant materiality, complexity, capability, risk and performance of individual Agencies and/or groups of Agencies, and to complement any existing relationship frameworks (which may be outlined in specific establishing legislation). The approach may consider specific monitoring based on whether portfolio Agencies are funded through general revenue sources or their own revenue sources, and the specific governance and accountability arrangements in place.

The 'fit for purpose' approach could be enhanced by considering, for example, an 'earned autonomy' model. The model recognises and grants greater autonomy to portfolio Agencies when they have 'earned' this privilege by demonstrating consistently high standards in discharging their financial management responsibilities. Such a model could be based on specifying minimum requirements/controls across all portfolio Agencies and further tailored requirements.

Whatever model(s) is chosen, Portfolio Departments need to be satisfied that the level of assurance will meet their portfolio responsibilities. Common key features for any model chosen include:

- periodic risk assessment in which the portfolio Department regularly assesses the risk of portfolio Agencies and when necessary, adjusts the monitoring and reporting requirements appropriate to the change in the risk environment;
- monitoring and reporting capability requirements of the Portfolio Department to critically analyse Agency information, performance and compliance and identify necessary improvements; and
- effective accountability mechanisms for management at both the portfolio Department and Agency levels.

Portfolio Departments may consider establishing a portfolio board or a portfolio level audit and risk committee (including members external to government) to support their Departmental Secretary in effectively undertaking this portfolio role.

Mechanisms to improve support

To provide the necessary support to Ministers and Agencies, Portfolio Departments may:

- review Portfolio Agencies' planning documents to ensure they align with government priorities and intended objectives for the Agencies and to advise the Minister on the suitability of the plans, including financial sustainability. In the case of general government sector Agencies, this provides the ability to discuss and shape key strategies as part of corporate and long term planning for the portfolio and in the development of objectives, indicators and performance measures;
- facilitate Portfolio Agencies' understanding and interpretation of government policy objectives and priorities and provide greater clarity in the definition of Agencies' purpose, direction and objectives to ensure government's intended purpose for establishing the Agency is achieved. This could be achieved through the relationship between government, portfolio Departments and Agencies, including through regular communication of expectations;
- review Portfolio Agencies' periodic performance reports and advise on progress towards achieving targets;
- review portfolio Agencies' annual report to Parliament for alignment with government policies and priorities and review annual reports for smaller Agencies not required to table in Parliament;
- monitor overall compliance with financial management requirements (including the FMA, Directions, Instructions and Compliance Framework), identify Significant or Systemic risk issues and remedial actions, and provide advice to the Minister; and
- provide timely, relevant and quality advice and information to government and DTF on Departmental and Portfolio Agency performance, and ensure effective relationships with DTF to enable the management of whole of government financial risks and reporting on the State's finances.

Portfolio roles, responsibilities and relationships

For Portfolio Departments to be well placed to provide timely advice to their Ministers and DTF, it is important that Departments:

- have strong working relationships with portfolio Agencies, in particular between the departmental Secretary and Agency Accountable Officer; and
- maintain effective communication channels.

Provision of information that is appropriate and of sufficient quality by the Agencies will assist Departments to develop policy, advise Ministers and provide information to DTF.

In supporting their Minister(s)' responsibilities, Departments should not interfere with the statutory independence of portfolio Agencies.

By providing the required support to Ministers, Portfolio Departments will have the business intelligence and relationships necessary to better support DTF in their whole of State advice to government. Departments contribute to managing whole of State outcomes by actively monitoring and advising on the overall portfolio performance, in addition to individual Agency performance and facilitating information flows.

Portfolio Agency responsibilities

Under the Directions, Portfolio Agencies are required to:

- notify their Portfolio Department's Accountable Officer of any significant issue of which the they are aware that may affect or have affected the Agency's or State's financial management, performance, sustainability or reputation (Direction 2.3.3); and
- in the case of their CFO, provide quality and timely information to the relevant Portfolio Department CFO to meet portfolio reporting obligations, and establish and maintain an effective relationship with the relevant Portfolio Department CFO (Direction 2.4.3);
- notify the Portfolio Department of any Material Compliance Deficiency, and of planned and completed remedial actions, as soon as practicable (Direction 5.1.6);
- for Portfolio Agencies that are Controlled Entities, comply with additional reporting requirements (Direction 5.3.2).

These Directions are intended to be broadly consistent with section 13A of the PAA. The focus is on providing reliable and timely information to the Portfolio Department, which can then support the Department to advise the Minister on matters affecting the Portfolio Agency. There is also a focus on fostering a positive relationship.

Further information

- Victorian Public Sector Commission: Serving Victoria: A Guide for Public Sector CEOs[4].

[4] http://vpsc.vic.gov.au/resources/serving-victoria/

Guidance 2.3.5 – Responsibility to establish requirements for excluded entities

Objective	Provides information to assist relevant Agencies to implement the responsibility to establish financial management requirements for certain excluded entities.
Effective date	1 July 2016
Relevant Directions	1.2 Application 2.3.5 Responsibility to establish requirements for excluded entities
Last reviewed	1 February 2016

Application of Directions

Direction 1.2 provides that the Directions and Instructions apply to all Agencies, except for: school councils; incorporated committees of management; class B cemetery trusts; VicSES registered units; and Country Fire Authority volunteer brigades (note, however, that these Agencies remain subject to the requirements of the FMA).

Direction 2.3.5 then provides that appropriate financial management requirements must be established for these excluded Agencies.

This means that:[5]

- the Department of Education and Training must establish requirements for school councils;
- the Department of Land, Environment, Water and Planning (DELWP) must establish requirements for incorporated committees of management;
- the Department of Health and Human Services must establish requirements for class B cemetery trusts;
- VicSES must establish requirements for their registered units; and
- the Country Fire Authority must establish requirements for their volunteer brigades.

Entities such as school councils and volunteer brigades are excluded from the Directions because in most cases their size and risk profile is such that many of the requirements would be inappropriate for them. These entities usually have low financial risk, and unique staffing arrangements (such as the extensive use of volunteers) that require tailored financial management requirements. Further, these entities have a closer relationship with their Portfolio Department or (in the case of volunteer brigades) with their Agency than most other Agencies, including shared financial arrangements. Accordingly, it is more appropriate for their Portfolio Department or Agency to establish appropriate financial management requirements for them.

Establishing appropriate financial management requirements

'Appropriate financial management requirements' means a set of requirements that impose an appropriate level of financial management accountability, governance and compliance, having regard to the nature of the entities in question, including size, risk profile, and the financial risk that they pose to the State, both individually and as a class.

The requirements should be proportionate to the financial management needs and responsibilities of the relevant entities. For example, because school councils collectively manage state assets of significant value, it would be appropriate for them to be subject to sophisticated asset management requirements proportionate to the collective value of the assets they manage. By contrast, the requirements for other entities and classes of entities that do not manage significant assets would be focused on other aspects of financial management.

[5] The following is the relevant Portfolio Departments as at the date of issue of this Guidance. Note that actual responsibility within the Agency falls on the Accountable Officer.

The meaning of 'appropriate financial management requirements' is given more detail in Direction 2.3.5(c), which provides that the requirements must:

- be established having regard to the requirements in the Directions and Instructions;
- include appropriate accountability arrangements and monitoring by the relevant Portfolio Department/Agency to ensure entities' compliance with the requirements; and
- be consistent with relevant Agencies' governing legislation.

Having regard to the requirements in the Directions and Instructions

The requirements must be established having regard to the Directions and Instructions. However, the requirements do not need to replicate the documents. In establishing requirements, relevant Portfolio Departments and Agencies are encouraged to use the Directions and Instructions as a starting point. A Direction or Instruction should only be excluded from the requirements if there is a strong case to do so in the entity's circumstances.

Compliance requirements

The requirements must also include appropriate accountability and monitoring to ensure compliance.

Specific compliance accountabilities should be placed on key staff in the Portfolio Department/Agency, and on the excluded entities. For example, it may be appropriate to make the Accountable Officer of the entity accountable for annually reporting to the Portfolio Department on compliance. Similarly, the Accountable Officer of the Portfolio Department may have a specific accountability to provide advice and support to the entities on compliance.

The requirements also must include monitoring by the relevant Portfolio Departments and Agencies of the relevant entities' compliance with the requirements. A risk based annual process to monitor compliance, with reporting from the relevant entities, is encouraged.

Consistency with governing legislation

The requirements must have regard to, and be consistent with, the relevant entities' governing legislation.

Other requirements

In most circumstances, the requirements should also at least include:

- general accountabilities for key staff, volunteers and/or members;[6]
- effective governance and oversight;
- appropriate internal controls, such as those set out in Instruction 3.4;
- appropriate risk management, informed by the Victorian Government Risk Management Framework[7]; and
- where the entity manages assets, requirements to manage the assets informed by the Victorian Government's Asset Management Accountability Framework.

Preparation and implementation of requirements

As at the commencement of the Directions, some Portfolio Departments/Agencies may already have established financial management requirements for their excluded entities. These requirements should be reviewed by reference to Direction 2.3.5.

Relevant Portfolio Departments and Agencies are encouraged to consult with DTF in establishing financial management requirements for their entities.

The requirements may differ within a class of entities. For example, it would be open to DELWP to establish a number of sets of requirements that apply to different classes of incorporated committees of management.

The requirements should be written clearly, distributed widely, accessible online and updated as necessary. The Portfolio Department or Agency should support the entities to implement the requirements.

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[6] In addition to the compliance accountabilities required under Direction 2.3.5(c).

[7] http://www.dtf.vic.gov.au/Publications/Victoria-Economy-publications/Victorian-risk-management-framework-and-insurance-management-policy

Accountability

Direction 5.1 imposes compliance requirements on relevant Portfolio Departments and Agencies. The requirement to establish appropriate requirements for relevant entities under Direction 2.3.5 is subject to this compliance, which includes:

- an annual assessment of compliance with the requirement;
- a detailed period review by the internal audit function of compliance with the requirement;
- remedying a Compliance Deficiency in relation to the requirement;
- reporting of a Material Compliance Deficiency in relation to the requirement to the Responsible Minister and Portfolio Department; and
- attestation in the Annual Report to compliance with the requirement.

Further, the Auditor-General may audit against this requirement.

As for the accountability placed on excluded entities, the requirements that are set down should include accountability for key financial management roles in the entities. Further, Portfolio Departments and Agencies are required to include appropriate accountability and monitoring to ensure compliance.

Transition

Direction 2.3.5 is subject to a transitional arrangement in Direction 1.4.2, as follows:

- for those Agencies that are already compliant as at 1 July 2016, Direction 2.3.5 is in force from that date; and
- for those Agencies that are not compliant as at 1 July 2016, Direction 2.3.5 comes into force on 1 July 2017.

This transition recognises that it may take some time for Agencies to establish appropriate financial management requirements. However, if those requirements are already in place at the commencement of the Directions on 1 July 2016, the transition does not apply.

Guidance 2.4 – Chief Finance Officer

Objective	Provides guidance on the role, responsibilities and qualifications of the CFO
Effective Date	1 July 2016
Relevant Direction	2.4 Chief Finance Officer
Last Reviewed	1 February 2016

The role of CFO

Section 43 of the FMA requires the Accountable Officer to appoint a 'Chief Finance and Accounting Officer' (CFO) to be responsible for ensuring that proper accounting records/systems and other records are maintained in accordance with the regulations and Directions.

The Directions describe the CFO's role. The requirements include those traditionally associated with the role, such as preparing accurate financial information. The Directions also encourage a strategic role for CFOs, such as the requirement to provide strategic advice to management on matters such as future financial sustainability.

Access to executive

To support this more strategic role, CFOs must have access to the Responsible Body and Accountable Officer. Access may include a direct reporting line, regular formal access (for example, through attendance at board meetings) and/or more informal access as required (such as meetings). In larger Agencies and Departments, it may be more appropriate for the CFO to directly report to the Accountable Officer.

Job title

Section 43 of the FMA requires the Accountable Officer to appoint a 'Chief Finance and Accounting Officer'. However, it is not necessary for the holder of this position to be referred to in this way. The Directions use the more modern title of 'Chief Finance Officer' to refer to the person appointed as Chief Finance and Accounting Officer under the FMA.

Other examples of alternative titles include 'General Manager, Finance' or 'Deputy Secretary, Financial Management'. Alternative titles are appropriate, provided that the person appointed under the Act exercises the functions and has the responsibilities assigned to the role in the FMA and the Directions.

In some organisations, the person with the job title of 'Chief Finance Officer' may not be the person appointed as CFO under the FMA. To avoid confusion, this situation is discouraged.

Portfolio responsibilities

The Directions provide certain portfolio responsibilities for CFOs. The CFO of a Portfolio Agency needs to form a strong relationship with the CFO of the Portfolio Department, including by providing quality and timely information. The CFO of a Portfolio Department needs to help their Accountable Officer and DTF to support their Portfolio Agencies.

Outsourcing a CFO

For most Agencies and all Departments, outsourcing a CFO is unlikely to be consistent with the Directions. A strong, internal, full time CFO role is central to proper financial management. For example, in such Agencies, it would be difficult to adequately fulfil the requirements in Direction 2.4 with an outsourced CFO.

However, the Act and Directions do not expressly prohibit the role of the CFO from being undertaken by a person who is not an employee. Accordingly, in a small Agency, which may not have the size or risk profile to require an internal CFO, the CFO may be outsourced. A key consideration when outsourcing a CFO is ensuring there is an appropriate separation of duties of the collection and processing of information from the preparation of the financial statements.

Agencies considering an outsourced CFO should have regard to:

- Direction 2.4.1, which requires the CFO to have access to the Accountable Officer and the Responsible Body in carrying out the CFO's responsibilities;
- Direction 2.4.2, which requires the CFO to sign a declaration in the Agency's financial statements;
- Direction 3.3, which requires financial authorisations be given to employees not contractors or consultants;
- Instruction 4.2.1, which requires appropriate contract management and performance. These requirements would apply to a contract to engage an outsourced CFO. Relevant requirements include that the Accountable Officer:
  - establish an effective performance management framework for the contract;
  - include appropriate contract specification;
  - regularly monitor and manage performance; and
  - regularly report to the Responsible Body on the contractor's performance;
- Departments and some Agencies are subject to the policies issued by the Victorian Government Procurement Board. These policies will apply to the proposed engagement of an outsourced CFO.

Joint Accountable Officer/CFO

The Act and Directions do not prohibit the role of the CFO from being undertaken by the Accountable Officer. This may be appropriate in some very small Agencies, where resources are limited and financial risk is low.

However, in most Agencies, it is unlikely that a joint Accountable Officer/CFO role would be workable or appropriate. A person in such a joint role would be subject to significant and diverging responsibilities under both the Directions are other legislation, standards and policies. Further, the separation of the roles is important in most Agencies to ensure sufficient focus on financial management.

CFO expertise and qualifications

The Directions provide that the CFO must be suitably experienced and hold a graduate or post graduate qualification in accounting or a relevant discipline granted by a tertiary education provider. What constitutes a 'relevant discipline' will depend on the judgement of the Accountable Officer having regard to the circumstances of the Agency. It may include a qualification in finance, business or economics, particularly if the qualification is supported by relevant prior experience.

Professional designation (such as membership of Chartered Accountants Australia New Zealand (CA ANZ)or CPA Australia) is not a mandatory requirement for CFOs. However, it is a relevant qualification and will help to ensure that a CFO complies with the requirement to keep their knowledge and expertise up to date with developments in financial management.

Guidance 2.4.6 – CFO whole of government responsibilities

Objective	Provides guidance on setting down accountabilities for public sector CFOs to support ministerial and whole of government financial objectives and to provide information to portfolio departments or DTF.
Effective Date	1 February 2017
Relevant Directions	2.4 Chief Finance Officer 2.4.6 CFO whole of government responsibilities 5.1 Financial management compliance
Last Reviewed	23 January 2017

Background

Direction 2.4.6 sets down accountabilities for public sector Chief Finance Officers (CFOs) to support ministerial and whole of government financial objectives and to provide information to portfolio departments or DTF.

Link to Standing Directions

The Standing Directions of the Minister for Finance 2016 (Standing Directions) set the standard for financial management by Victorian Government agencies. The Standing Directions include requirements for CFOs, most of which are focused on management of internal agency finances.

Direction 2.4.6 provides additional requirements with a whole of government focus. Direction 2.4.6 reflects Government's broader priorities to increase the accountability and transparency of departments' and agencies' finances.

Direction 2.4.6 is subject to the compliance and reporting requirements in the Standing Directions. This is discussed further below.

Application

Direction 2.4.6 applies to 'relevant Departments' and to 'Agencies', depending on the direction in question.

At the time of publication the relevant Departments were:

- Department of Economic Development, Jobs, Transport and Resources (DEDJTR);
- Department of Education and Training (DET);
- Department of Environment, Land, Water and Planning (DELWP);
- Department of Health and Human Services (DHHS);
- Department of Justice and Regulation (DJR);
- Department of Premier and Cabinet (DPC); and
- Department of Treasury and Finance (DTF).

The definition of 'Agencies' captures public bodies as defined by the FMA, and bodies specified in section 16(1) of *Public Administration Act 2004*. It excludes those agencies that are already excluded from the Standing Directions, such as school councils. It also excludes Court Services Victoria, the Judicial College of Victoria, the Judicial Commission of Victoria, and independent offices as defined in the Standing Directions, such as the Victorian Auditor-General's Office.

Direction 2.4.6.1: Whole of government financial accountability of CFOs

Direction 2.4.6.1 sets down whole of government, and portfolio-wide, accountability for CFOs. It requires CFOs to support the principles of sound financial management set down in section 23D of the FMA.

The concept of 'whole of government financial objectives' in Direction 2.4.6.1(a) refers to the stated financial objectives of the Government of the day. It includes the financial policy objectives and strategies statement in the most recent Budget and Budget Update.

The ways in which a CFO might comply with this Direction will vary widely in practice. For example, it might be achieved through advice to a minister or the Government on an issue affecting the agency that has regard to factors such as the financial risks faced by the State; the prevailing economic circumstances; financial effects on future generations; financial sustainability and/or whole of government financial implications. This advice would be provided in various contexts, such as advising on policy decisions, budget bids, services or assets. The advice is only required to be provided in relation to matters relevant to the department or agency.

Directions 2.4.6.2 and 2.4.6.3: Accountability of CFOs to inform DTF/Portfolio Departments

Direction 2.4.6.2 requires CFOs of relevant departments to provide information to DTF in certain circumstances. Similarly, Direction 2.4.6.3 requires agency CFOs to provide information to their portfolio departments.

Notification of issues and risks

Directions 2.4.6.2(a) and 2.4.6.3(a) impose a requirement for CFOs to inform DTF or their portfolio department of issues and risks that may have an impact on the financial performance and position of the State. This requirement is ongoing, and arises at any time that the CFO identifies such an issue or risk. Preferably, the information is to be provided in written form (e.g. an email or letter). If in verbal form (e.g. a phone call or in person), a dated file note evidencing the conversation should be maintained.

The requirement placed on departmental CFOs in Direction 2.4.6.2(a) includes informing DTF of issues and risks identified in their portfolio agencies. This would include both issues identified by the departmental CFO, and issues notified to the departmental CFO by an agency. Accordingly, when a departmental CFO receives a notification from an agency under Direction 2.4.6.3(a), they should consider whether this needs to be passed on to DTF.

The provision of information under Directions 2.4.6.2(a) and 2.4.6.3(a) may be subject to the internal approval processes of the department or agency. For example, it may be that the department requires secretarial approval for the content of the notification.

There is an expectation that a CFO would exercise sufficient judgement to determine a significant issue or risk impacting on the State's financial performance and position, including reputation. For example, if the CFO thought it a significant enough impact to raise it with their departmental Secretary, they should use the same judgement to determine whether to inform DTF.

A CFO can also apply the same ‘reasonableness test’ used in the Standing Directions definition of ‘significant’ more broadly.

The AASB definition of ‘materiality’ is also a useful guide in a broader financial management context, not just in relation to financial reporting. It is material if 'in relation to information, that information which **if omitted, misstated or not disclosed** has the potential to adversely affect decisions about the allocation of scarce resources made by users of the financial report' (this definition can be applied to broader information on financial management issues and risks).

An issue or risk is likely to be of significant impact in relation to the financial position and performance of the State if it extends beyond the capacity of a department to manage within its annual appropriation and other resources. For example, if seeking additional resources from government and/or unused surpluses, there is a need to inform DTF. Risks can also relate to the reputation of the State as an exemplary manager of public monies.

Examples, both at a departmental or portfolio agency level, that may have significant financial management implications include:

- a human or natural event/disaster resulting in a need for additional services;
- a change or reduction in Commonwealth funding arrangements;
- output or asset overspend/underspend;
- changes in ministerial or government priorities which impact on funding;
- issues with outsourced service providers (e.g. financial difficulties or poor service delivery);
- workforce issues (e.g. Enterprise Bargaining Agreement increases or industrial action);
- unexpected need for major asset replacement (e.g. fire or flood);
- losses or fraud which has severely compromised the financial governance and internal control framework or resulted in a significant financial cost;

- issues with or the loss of IT financial systems and/or information which may impact on data feeds and data quality to DTF;
- outstanding legal issues or potential legal exposure or claims;
- insurance and indemnity claims;
- audit findings of serious financial mis-management or adverse audit opinions on financial statements; and
- concerns relating to the current or future financial sustainability of a portfolio agency.

This is not an exhaustive list of all the financial management issues or risks facing a portfolio department and/or agencies, but it illustrates some of the key risks that may impact upon government decision-making.

Responding to information requests

Directions 2.4.6.2(b) and 2.4.6.3(b) require CFOs to directly provide to DTF or their portfolio department factual financial information requested to facilitate reporting and Government decision making, within the time provided in the request.

Relevant financial information may include:

- strategic planning information (e.g. risks, challenges, options);
- the past, present and future allocations of resources;
- the outputs and outcomes resulting, or expected to result, from allocations;
- economic and financial analysis of policy proposals;
- program/service delivery information;
- business cases for outputs and assets; and
- savings information.

Factual financial information could include things like the quantum of spend on a particular program or sub-program. It does not include policy advice or recommendations.

By contrast to Directions 2.4.6.2(a) and 2.4.6.3(a), the requirement in Directions 2.4.6.2(b) and 2.4.6.3(b) is for the direct provision of information from the CFO to DTF or their portfolio department in response to a request.

Direction 2.4.6.4: Employment arrangements of departmental CFOs

Direction 2.4.6.4 requires aspects of departmental CFOs' employment arrangements to reflect a whole of government focus.

Direction 2.4.6.4 clarifies that the requirements do not limit the exercise of secretaries' employment powers under the *Public Administration Act 2004*. Secretaries retain ultimate decision-making power in relation to the employment of their CFOs, and are not subject to direction by DTF.

Changes to position description, employment contract and performance plan

Direction 2.4.6.4(a) requires secretaries to ensure that the position description, employment contract and performance plan of the department's CFO includes accountability to achieve Directions 2.4.6.1 and 2.4.6.2. This can be achieved by amending these documents by agreement between the secretary and the CFO. The documents should replicate the wording in Directions 2.4.6.1 and 2.4.6.2, clarifying that whole of government financial accountability, and accountability to inform DTF, form a key part of the employment arrangement. For the purpose of the employment contract, amending or adding a schedule would be sufficient.

For example, the position description, employment contract and performance plan could include wording as follows:

The CFO will comply with Direction 2.4.6 issued by the Minister for Finance, by:

- supporting whole of government financial objectives and the principles of sound financial management;
- supporting their portfolio Ministers in relation to the financial management of the department, the relevant Minister's portfolio and whole of government;
- informing the Secretary of DTF of issues and risks of the department and the department's portfolio agencies that may have an impact on the financial performance and position of the State; and
- directly providing to DTF factual financial information requested by DTF to facilitate reporting and Government decision making, within the time provided in the request.

Consultation with DTF on CFO employment

Direction 2.4.6.4(b) requires secretaries to consult the Secretary of DTF on the appointment, removal, remuneration level and performance assessment of their CFO, including by ensuring that a representative of DTF is included on any CFO recruitment panel. This consultation may be delegated by the respective secretaries to other departmental executives or officers.

A department may negotiate with DTF to determine the nature of the consultation in a given case, and DTF intends to take a practical approach. It is expected that such consultation would usually involve:

- **Appointment**: The department seeks DTF's input on the advertisement; a representative of DTF is included on the recruitment panel; and a discussion is held between the departments on the preferred candidate/s.
- **Removal**: A discussion is held between the departments on the considerations and consequences of removal.
- **Remuneration**: At the time of appointment and any renegotiation of remuneration, the department seeks DTF's input on the appropriate remuneration range commensurate with the responsibilities of the role (DTF would not need to be involved in the specific pay negotiations between the department and the CFO).
- **Performance assessment**: The department involves DTF in the CFO's performance assessment, providing an opportunity to provide feedback directly to the CFO, their manager and/or the secretary. This feedback will be focused on the achievement of whole of government accountabilities, as set down in Directions 2.4.6.1 and 2.4.6.2. DTF will also have the opportunity to make a recommendation to the department in relation to any salary increase.

The consultation undertaken should be documented by the department.

In circumstances where the CFO is absent for a period of time and an acting CFO arrangement is proposed, the department should consult with DTF on whether anything is required under Direction 2.4.6.4(b). Acting departmental CFOs would otherwise still be subject to Directions 2.4.6.1 and 2.4.6.2, and acting agency CFOs would still be subject to Directions 2.4.6.1 and 2.4.6.3.

Direction 2.4.6.5: Compliance and reporting

Directions 2.4.6.5 clarifies that the Direction 2.4.6 is subject to the compliance and reporting requirements set out in the Standing Directions and the Instructions supporting the Standing Directions, including public attestation to compliance.

Amongst other requirements, this means that the Direction 2.4.6 is subject to:

- an annual assessment of compliance with the requirements;
- a detailed periodic review by the internal audit function;
- remedying any compliance deficiencies;
- reporting any material compliance deficiencies to the responsible Minister and DTF/Portfolio Department; and
- attestation in the Annual Report to compliance with the requirements.

Further, the Auditor General may audit against the requirements.

Further information on the compliance requirements in the Standing Directions is available in Standing Direction 5.1, Instruction 5.1 and Guidance 5.1 .

Guidance 3.2.1– Audit Committee

Objective	Provides further guidance on the role of the Audit Committee, including a description of what should be included in an Audit Committee charter, a definition of appropriate skills and experience of an Audit Committee member, and what constitutes an independent member.
Effective Date	1 July 2016
Relevant Directions	3.2.1 Audit Committee 3.2.2 Internal audit 3.4 Internal control system 3.7 Managing risk 5.1 Financial management compliance
Last Reviewed	1 February 2016

Assess the effectiveness of the financial reporting control framework

Safeguarding the integrity of Agency financial reporting includes two important and interrelated roles for the Audit Committee. These are to independently assess the financial statements for completeness, consistency and conformity with Accounting Standards, and to regularly review the related financial policies, systems and processes.

The internal audit strategic plan and annual work program should include reviews of the effectiveness and efficiency of Agency financial systems and processes.

Such reviews, together with ongoing management and internal or external audit advice of significant issues that may affect the financial statements should enable the Audit Committee to assess whether the internal control systems are working, issues are adequately resolved, and the financial statements can be produced to present a true and fair view of the Agency's financial position and performance.

Management is responsible for the production of Agency financial statements/reports. The CFO is to provide a declaration to the Audit Committee that the Agency's:

- financial reports (estimates and actuals) present fairly, and in accordance with applicable Australian Accounting Standards and the FMA, the Agency's financial position and operating results;
- financial reports (estimates and actuals) are founded on a sound system of risk management and internal compliance and control that implements the policies adopted by the Agency; and
- systems and controls for financial management, performance and sustainability are operating efficiently and effectively in all material respects.

The Audit Committee reviews the financial statements using its knowledge of the entity, skills in financial accounting, outcomes of internal and external audits of financial management policies, systems and processes and the explanations from the CFO. This enables the Audit Committee to advise the Responsible Body whether the financial statements presents fairly, in all material aspects, the Agency's financial position and performance.

Review and assess the effectiveness of systems and controls

A key role for the Audit Committee is to review and assess the effectiveness of a range of systems, processes and controls under Direction 3.2.1.1.

Further information and checklists on Audit Committee considerations in its review and assessment can be found in The Australian National Audit Office, Public Sector Audit Committees: Independent assurance and advice for Accountable Authorities[8].

[8] https://www.anao.gov.au/work/better-practice-guide/public-sector-audit-committees-independent-assurance-and-advice

Oversee internal audit activities

The Audit Committee's oversight of internal audit activities should include the following:

- review of the internal audit charter, resources and budget to determine whether these maintain internal audit's independence from management, and the function is adequately resourced;
- address all issues of independence and objectivity with the Internal Audit function;
- provide counsel to the agency as part of the agency's appointment process of the internal auditors;
- regular reviews of the adequacy and appropriateness of the rolling strategic internal audit plan and annual internal audit program based on Agency size, complexity and risks;
- review of the performance (effectiveness and efficiency) of internal audit, including:
  - internal audit's self-assessment of its performance;
  - the quality of internal audit services and reports delivered;
  - progress of the internal audit program; and
  - how internal audit has acquitted against its charter;
- reviewing internal audit's participation in non-assurance roles to assess potential impairment of independence and alignment with the internal audit program;
- review all audit reports and provide advice to the Accountable Officer/Responsible Body on significant issues identified and action to be taken on issues raised that are relevant to the Agency;
- reviewing management's implementation of internal audit's findings and recommendations; and
- having an open and transparent relationship with the internal audit function and to meet periodically without management.

The Institute of Internal Auditors' Audit Committee Oversight Brochure [9], provides guidance on internal audit oversight considerations, including quality of performance.

When the internal audit function is co-sourced or outsourced, it is expected that the Committee would provide input to the statement of requirements developed as part of an appointment or tender process. In particular, the Audit Committee needs to ensure the independence of the function is not compromised and consider potential relationships with the external provider that may impair the independence of the assurance process internal audit provides.

Considering audit recommendations and agency management actions

While the FMA and Directions require Audit Committees to consider audit recommendations relating to or impacting on financial management, performance and sustainability, it is recommended that Agency Audit Committees consider all audit recommendations made by either internal or external audit, even if they may fall outside this scope.

Audit Committees should establish effective processes for monitoring the implementation of all Agency management actions relating to audit recommendations, and a risk based approach for assessing whether completed management actions have effectively addressed the underlying risks or issues raised by audit.

The Victorian Auditor-General recommended this approach in his report on Audit Committee Governance (August 2016).[10] The report made a number of recommendations regarding best practice governance arrangements for Agency Audit Committees to ensure they operate in a fully effective manner.

Review annual financial statements

As the Audit Committee independently reviews the Agency's annual financial statements and makes a recommendation to the Accountable Officer/Responsible Body, it is important for Audit Committee members to have a sound understanding of the Agency's financial reporting requirements and the significant policies and principles that underpin these reports.

[9] https://na.theiia.org/services/quality/Public_Documents/Forms/AllItems.aspx
[10] http://www.audit.vic.gov.au/reports_and_publications/latest_reports/2016-17/20160831-audit-committees.aspx

In general, the Audit Committee should consider the following more specific responsibilities in relation to the annual financial statements of the Agency:

- obtain assurance from the CFO that the financial statements comply with all prescribed accounting requirements and are materially correct before recommending the financial statements for certification by the Accountable Officer or Responsible Body;
- assess the appropriateness of Agency accounting policies;
- assess the process used by management to make material estimates and judgements in financial statements;
- identify and actively assess any unusual financial or operational trends or variations from forecasts;
- review the impact of any materially adverse audit findings on the integrity of the Agency's financial statements;
- assess whether the information contained in the financial statements is consistent with the Audit Committee's knowledge of the Agency's 'business' and the significant issues raised throughout the year that may affect the financial statements;
- perform other due care and diligence processes, including whether the statements are complete and operationally accurate and 'present fairly' the Agency's activities for the period under review and the state of its affairs at balance date. Of particular relevance are the various notes and other disclosures that complement the statements, including any performance indicators; and
- enquire of management and external audit that the financial statements have been prepared in accordance with the timeframes agreed with the external auditors and whether there are any unresolved issues with external audit.

The judgement in the 2011 Federal Court case of *ASIC v Healy* (the Centro Case) highlighted the directors' responsibilities in relation to a company's financial statements. The judgement outlined that directors cannot simply rely on specialist advice (e.g. from external auditors) or advice from others (e.g. management) in discharging their duties. The general principles covered by the judgement could be applied to Agencies when the Accountable Officer and, in addition for Public Bodies, a member of the Responsible Body, are responsible for certifying the Agency's financial statements.

Review of annual report of operations

The Directions require the Audit Committee to review the report of operations before it is finalised. The Audit Committee review should be limited to checking the consistency of financial information in the report with the audited financial statements.

The Audit Committee review should only focus on relevant financial related information in the report of operations that impacts the Agency's financial management, financial performance and financial sustainability, not all the information in the report of operations.

For example, this may include financial related performance indicators, historical financial position summaries and any other information containing financial outcomes or data in the report of operations.

In considering the financial related information the committee should be satisfied that the messages conveyed from such information are not inconsistent with the view presented by the audited financial statements.

Review and monitor compliance

A key responsibility of an Agency's Audit committee is to review and monitor compliance with relevant risk and financial management laws and standards and the Directions. This will enable the Committee to provide assurance and make recommendations to the Responsible Body on the level of compliance attained, issues to be resolved and proposed mitigation plans.

Reviewing the effectiveness of how an Agency is monitoring its financial management compliance with relevant legislation, regulations and associated government policies is generally an established function of Audit committees.

However, in larger Agencies, with significant operational risks, the Responsible Body may establish a separate Risk Committee to undertake overall Agency risk oversight.

Agencies must comply with a considerable volume and complexity of legislation and policy, including the Directions. Therefore, it would be expected the Audit Committee will focus on those aspects that pose the highest risk to the Agency, and on how the Agency manages its compliance responsibilities.

Similarly, in reviewing an Agency's compliance with the FMA, Directions and Instructions, it is expected that Audit Committees will take a practical, risk-based approach to the evidence required to demonstrate compliance. This is

particularly relevant to those Directions that require Agencies to achieve broad principles of good financial management. An example is Direction 2.2(a), which requires the Responsible Body to ensure that the Agency furthers government objectives and priorities. Reasonable evidence for compliance with such a requirement could include a brief summary of significant Government priorities that the Agency has pursued in the relevant year. It would usually be unreasonable to require that the Agency undertake a detailed analysis of all actions taken under such requirements.

An Audit Committee should, at least annually, in relation to financial management, performance and sustainability, undertake the following:

- review management processes to ensure the Agency is kept up to date with new legislation and/or changes to existing legislation relevant to the Agency;
- review the effectiveness of internal control and other systems for monitoring the Agency's compliance with the relevant legislation and associated government policies;
- monitor remedial actions for significant and systemic breaches of compliance;
- determine whether management has appropriately considered legal and compliance risks as part of the Agency wide risk management plan;
- regularly review the adequacy of the strategic internal audit plan and annual internal audit program based on the size, complexity and risks of the Agency;
- provide advice and assurance to the Responsible Body/Accountable Officer regarding the Agency's annual compliance assessment report; and
- provide advice (including mitigation strategies) to the Responsible Body/Accountable Officer regarding the Agency's responsibilities in relation to any Fraud, Corruption and Other Losses, and Material Compliance Deficiencies (see Directions 3.5 and 5.1.6).

Audit Committee performance and membership review

Under Direction 3.2.1.4, the Responsible Body must formally review the Audit Committee's performance and membership at least once every three years. The membership aspect of the review will help to ensure the individual members and the overall composition of the Audit Committee continue to meet performance expectations and the membership requirements of Direction 3.2.1.3.

Annual self-assessment

In assessing its own performance under Direction 3.2.1.3(g), the Audit Committee should consider at least the following:

- the effectiveness of the Audit Committee as a whole;
- the performance of individual Audit Committee members (for external members, performance criteria may be included in their letter/contract of engagement, and for Agency staff, performance criteria may be included in their performance plans);
- identifying the process for implementing action plans that respond to areas identified for improvement; and
- compliance with the Audit Committee's charter.

The Audit Committee might assess its performance collectively and individually against criteria such as:

- a good understanding of, and commitment to, the Audit Committee's role and responsibilities;
- objectivity and independence;
- an ability and willingness to take difficult but constructive positions at meetings when necessary;
- a good understanding of the Agency's business;
- a good understanding of the Agency's risk management and internal control processes;
- participation in activities to maintain current knowledge of their business, industry, financial and regulatory environment; and
- preparation for, and participation in, Audit Committee meetings.

Audit committees can use tools such as self-assessment questionnaires to assist with the evaluation of a member's performance and contribution to the Audit Committee. The Audit Committee may also seek input from non-member attendees and separately assess the information received.

The self-assessment approach adopted by the Audit Committee should cover areas in the Committee's charter such as authority, membership, meetings, organisation and responsibilities.

The results of the self-assessment should be used by the Audit Committee for discussion to identify areas for improvement and be provided to the chair of the Responsible Body.

Audit Committee Charter

The Audit Committee charter should be consistent with the requirements of the Audit Committee as specified in the Directions and specify at a minimum, the following:

- authority, role, operations and membership requirements (including declarations of interests) of the Committee;
- frequency of meetings, quorum, how and when the minutes and recommendations of the Audit Committee are forwarded to the Responsible Body;
- the process and authority for the Committee to access staff and information held by the Agency relevant to the Committee's responsibilities;
- authorisation for the Chair to have direct access to the Responsible Body to discuss any matters deemed necessary; and
- authorisation for the Committee to seek independent professional advice, as and when required to enhance its independence and capacity to obtain a full appreciation of relevant issues.

Sample Audit Committee charters are available on the Victorian Public Sector Commission[11] or the Australian National Audit Office[12] websites.

Appropriate skills and experience

The appropriate skills and experience for the Audit Committee include:

- integrity, objectivity, accountability, honesty and openness;
- an understanding of the Agency, its products, its services, risks and controls (it is noted that new audit committee members may not have a full understanding of the Agency when joining and should be given sufficient time to understand the business);
- the ability to read or understand basic financial statements, ask relevant questions about them and interpret and evaluate the answers;
- the ability to enquire, evaluate and make independent judgement;
- the ability to offer different perspectives to management and constructive suggestions; and
- an understanding of Audit Committee functions.

In addition, Audit Committee members should have the capacity to dedicate sufficient time and energy to the role.

Appropriate expertise in financial accounting or auditing

Appropriate expertise includes any of the following:

- a thorough knowledge of Australian accounting standards and financial statements;
- experience in applying the Australian accounting standards in connection with financial reporting and public financial statements;
- experience in preparing or auditing general purpose financial statements;
- an understanding of the accounting issues within the specific industry;
- a thorough knowledge of Australian auditing standards; or
- experience with internal controls and procedures for financial reporting.

[11] http://vpsc.vic.gov.au/
[12] http://www.anao.gov.au/

A Responsible Body may look beyond their own Board to appoint an external Audit Committee member should no member of their Board be able to provide the appropriate expertise in financial accounting or auditing, or to meet the requirement for a majority of independent members.

Independent members

An independent member of an Audit Committee is not involved in the day-to-day management of the Agency. This seeks to ensure that the independent Audit Committee member acts in an objective, impartial manner, is free from conflict of interest, inherent bias or undue external influence.

For Departments, independent members must be external to the Department. Where Departments have an even number of independent (external) and non-independent members (management) on the Committee, the independent chair will have the casting vote in any decisions requiring a vote. In this situation a Department will be compliant with the Direction.

For Agencies in which the Responsible Body is the board, at least three members must be non-executive directors of the board. At least two of those three members must be independent.

Relationships that may be seen to impair an Audit Committee member's independence include:

- current or previous employment by the Agency or having been a non-executive Board director after ceasing to hold such employment;
- receipt of material consulting, advisory or contractual relationship with the Agency other than as a Board or committee member of the Agency; or
- any interest and any business or other relationship which could, or could reasonably be perceived to, materially interfere with the person's ability to act in the best interests of the Agency.

A non-executive director is a member of the Board of directors of an Agency who does not form part of the executive management team. For example, they are not the Chief Executive Officer or Chief Finance and Accounting Officer.

Generally speaking, Audit Committee members are sourced from non-executive directors on the Board. As such, a non-executive board member (director) can also be an independent member of the Audit Committee. The concepts of 'non-executive director' (i.e. member of the Board) and 'independent Audit Committee member' are therefore not mutually exclusive.

An employee of the Agency can be a member of the Audit Committee, however they are not considered an 'independent' member.

While under the Directions an Audit Committee may have internal management representatives, these should not include executive members of the board. For Departments members of the executive team may be members of the Audit Committee (except those excluded in the Direction). However, while these members can participate in discussions they should not vote on issues related to their functional area due to conflict of interest.

Whether a non-executive director's independence is affected for the purposes of them serving as an independent member of an Audit Committee should be judged on whether the member's service on the board or committee has been for a period which could, or could reasonably be perceived to, materially interfere with the person's ability to act in the best interests of the public sector Agency.

Members of an Audit Committee should be appointed for an initial term of up to three years and, subject to a formal review of performance and independence, may be appointed for further terms of up to three years but no more than nine years in total.

Smaller Agencies

To reduce the burden on smaller Agencies, for example a one member Responsible Body such as a Commissioner, they may consider sharing an appropriately constituted Audit Committee with other similar Agencies.

Alternatively, any smaller low risk Agency may seek an exemption from this requirement. In this case, the Responsible Body takes on the role.

Further information

The Australian National Audit Office (ANAO) Better Practice Guide March 2015, Public Sector Audit Committees: Independent Assurance and Advice for Accountable Authorities[13] – sets out comprehensive guidance including a discussion on: a range of functions and responsibilities that may be undertaken by the Audit Committee of a Commonwealth entity; shared committee arrangements; and sharing resources between entities. The Guide also includes a number of checklists and other material for use by committees and entity management.

ASX Corporate Governance Principles and Recommendations 3rd Edition[14] – sets out recommended corporate governance practices for entities listed on ASX. As they reflect a contemporary view of appropriate corporate governance standards public sector Agencies may find them helpful in formulating their governance rules and practices.

[13] http://www.anao.gov.au/Publications/Better-Practice-Guides/2014-2015/Public-Sector-Audit-Committees
[14] http://www.asx.com.au/documents/asx-compliance/cgc-principles-and-recommendations-3rd-edn.pdf

The Institute of Internal Auditors Audit Committees: A guide to good practice[15] – is a joint publication from the Auditing and Assurance Standards Board, Australian Institute of Company Directors and The Institute of Internal Auditors – Australia. It provides a practical introduction to the role and responsibilities of an Audit Committee. Although the guide is written largely for directors and Audit Committees of Australian listed companies, Directors, boards of management and Audit Committees of public sector entities may also find this guide a useful reference. The guide can be purchased from the IIA website.

Victorian Auditor-General's Report – Water Entities Results of 2013-14 (February 2015)[16] – provides a useful list of key elements (good practices) for an effective Audit Committee framework.

Victorian Auditor-General's Report – Audit Committee Governance (August 2016)[17] – makes a number of recommendations regarding best practice governance arrangement for Audit Committees to ensure they are fully effective.

[15] http://www.iia.org.au/announcements/12-08-28/AUDIT_COMMITTEES_A_guide_to_good_practice.aspx
[16] http://www.audit.vic.gov.au/reports_and_publications/latest_reports/2014-15/20150212-water-entities.aspx
[17] http://www.audit.vic.gov.au/reports_and_publications/latest_reports/2016-17/20160831-audit-committees.aspx

Guidance 3.2.2 – Internal audit

Objective	To guide consideration of an internal audit charter, a rolling strategic internal audit plan and an annual audit work program.
Relevant Directions	3.2.1 Audit Committee 3.2.2 Internal Audit 3.4 Internal control system 5.1 Financial management compliance
Effective date	1 July 2016
Last reviewed	1 February 2016

Internal audit

Internal audit is an important part of an Agency's governance framework, providing an independent and objective assessment of the efficiency and effectiveness of an Agency's controls, and practical recommendations for improvement.

To ensure independence of the internal audit function, it should functionally report to the Audit Committee, and administratively to management.

The internal audit charter provides the framework for the conduct of the Agency internal audit function.

The Internal Audit function is intended to provide the Audit Committee and Responsible Body with a level of assurance that key risks to the achievement of an Agency's objectives are appropriately addressed.

Independent of management

Internal auditors must be independent of management in carrying out their functions. Independence includes that they must not:

- have operational duties; and
- be subject to direction from management in how they undertake their functions.

In relation to functional matters, the internal audit function is accountable to the Responsible Body generally through its Audit Committee. In relation to administrative matters such as human resource administration and budgets, the internal audit function reports to management (e.g. Accountable Officer or its delegate).

Suitably experienced and qualified

Internal auditors must be suitably experienced and qualified. What constitutes this will depend on the judgement of the Responsible Body having regard to the circumstances of the Agency. A relevant tertiary qualification would usually be required. A professional designation (such as membership of the Institute of Internal Auditors) is not a mandatory requirement. However, it is a relevant qualification and will help to ensure that internal auditors are suitably qualified and keep their knowledge and expertise up to date with developments in internal auditing.

Conflicts of interest

The internal audit function can be in-sourced, co-sourced or outsourced. Whichever resourcing model the Agency adopts, the split between functional and administrative reporting still applies. For example, the contract administration of an outsourced function can remain with management, but contract performance remains with the Audit Committee.

When the Internal Audit role is to be filled by an external service provider, relationships that may be seen to impair Internal Audit member's independence could include:

- current or previous employment by the Agency, or having been a non-executive director after ceasing to hold such employment;
- receipt of a material consulting, advisory or contractual relationship with the Agency, other than as an internal auditor of the Agency; or
- any interest or business or other relationship that could, or could reasonably be perceived to, materially interfere with the internal auditors ability to act in a capacity independent of management and in the best interests of the Agency.

Charter

The internal audit charter defines the purpose, responsibilities and accountability of the internal audit function. It should be consistent with the internal audit requirements in the Directions and specify at a minimum, the following:

(a) purpose;

(b) role;

(c) authority and accountability, including access to records and personnel;

(d) independence and objectivity;

(e) responsibilities (some of the key responsibilities can be further expanded as separate topics e.g. planning, review of internal audit activity);

(f) outsourcing/co-sourcing arrangements (if applicable);

(g) reporting and monitoring;

(h) annual review of the charter by the Audit Committee; and

(i) standards of audit practice, reflecting Australian and international auditing and professional standards relating to internal audit.

Helpful guidance on the contents of an internal audit charter can be found at:

- Institute of Internal Auditors (Australia) – Internal Audit Charter checklist[18];
- Australian National Audit Office – Model Internal Audit Charter[19].

Strategic internal audit plan and an annual audit work program

Internal audit planning needs to be appropriate for the Agency's size, complexity of functions and risk profile. It should consider the key risks and areas outlined in the Agency's Corporate plan. Potential areas for internal audit coverage include:

- compliance with legislation, standards, policies and procedures;
- operational/financial processes and controls and review of transactions;
- information and communication technology including IT systems and controls on information quality, integrity and reliability;
- evaluation of the efficiency and effectiveness of the Agency's performance, including specific areas of Agency functions;
- governance arrangements and planning;
- the risk management framework;
- project/program management; and
- special investigations and ad hoc reviews.

The strategic internal audit plan and annual audit work program need to be of sufficient detail to assure the Audit Committee and Responsible Body that the proposed audit coverage will address the business needs and key risks.

[18] http://www.iia.org.au/sf_docs/default-source/quality/internal-audit-charter-review-checklist8E790F548D4A.pdf?sfvrsn=2
[19] https://www.anao.gov.au/work/better-practice-guide/public-sector-internal-audit-investment-assurance-and-business

Strategic internal audit plan

The strategic internal audit plan must cover a period of three to four years. It supports the Direction requirement of reviewing all financial management obligations over a medium term cycle.

For Portfolio Departments, this timeframe also aligns with the rolling four year corporate planning process which considers how a Department will respond to challenges and expectations in the medium term.

The strategic internal audit plan should be reviewed and updated annually and describe the role of internal audit in the Agency's overall assurance processes, and provide an important link between the internal audit charter and the internal audit annual work program.

Good practice internal audit planning involves a risk assessment of the areas of strategic and operational significance to the achievement of an Agency's objectives to determine appropriate timing and frequency of coverage for these areas over the planning period. Key risk areas may be reviewed more frequently, even yearly, whereas lower risk areas may only be reviewed in detail every three to four years.

The strategic internal audit plan provides a comprehensive view of an Agency's governance, risk and control activities and helps to focus the internal audit effort. The plan communicates the medium term internal audit direction in supporting the achievement of the Agency's objectives and the mitigation of risks. Senior management provides an important input into this planning process.

Annual audit work program

The annual internal audit work program sets out in detail the key areas for internal audit review for the upcoming year.

Evidence required for compliance

In conducting audits under the strategic internal audit plan, it is expected that Internal Audit will take a practical, risk-based approach to the evidence required to demonstrate compliance. This is particularly relevant to those directions that require Agencies to achieve broad principles of good financial management. An example is Direction 2.2(a), which requires the Responsible Body to ensure that the Agency furthers government objectives and priorities. Reasonable evidence for compliance with such a requirement could include a brief summary of significant Government priorities that the Agency has pursued in the relevant year. It would usually be unreasonable to require that the Agency undertake a detailed analysis of all actions taken under such requirements.

Further information

Planning reference material

Further guidance on the contents of the strategic internal audit plan and annual internal audit program can be obtained from the following:

- Institute of Internal Auditors (Australia), Practice Guide – Developing the Internal Audit Strategic Plan[20];
- Australian National Audit Office, Better Practice Guide, Public Sector Internal Audit (September 2012)[21];
- Australian National Audit Office – Planning Internal Audit Activities[22]; and
- Australian National Audit Office – Templates and guidance on internal audit strategy and work plan[23].

[20] http://www.iia.org.au/technicalResources/practiceGuides.aspx
[21] https://www.anao.gov.au/work/better-practice-guide/public-sector-internal-audit-investment-assurance-and-business
[22] https://www.anao.gov.au/work/better-practice-guide/public-sector-internal-audit-investment-assurance-and-business
[23] https://www.anao.gov.au/work/better-practice-guide/public-sector-internal-audit-investment-assurance-and-business

Professional standards

The Institute of Internal Auditors (IIA Australia) website provides a number of best practice guides and training, including:

- International Standards for the Professional Practice of Internal Auditing[24];
- International Professional Practices Framework[25];
- Assisting Small Internal Audit Activities in Implementing the 'International Standards for the Professional Practice of Internal Auditing[26]; and
- Best practice and updated skills training for Audit Committee members.

Measuring and assessing effectiveness

- The IIA Practice Guide – Measuring Internal Audit Effectiveness and Efficiency[26] will help Internal Audit measure, monitor and report the results of its effectiveness and efficiency to the Audit Committee.
- The IIA Practice Guide – Assessing the Adequacy of Risk Management[26] using ISO 31000 will help Internal Audit assess any risk management process established by the Agency.

Victorian Auditor-General's Office

Audit reports with internal audit recommendations for Agencies to consider:

- Public Hospitals: Results of the 2011–12 Audits[27] – opportunity to improve the use of internal audit to review capital project arrangements.
- Local Government: Results of the 2010-11 Audits[28] – results of VAGO's examinations of council internal audit frameworks against better practice.
- Tertiary Education and Other Entities: Results of the 2011 Audits[29] – results of VAGO's annual audit of 106 entities from tertiary education, sustainability and environment, health, planning and community development and local government sectors.

[24] http://www.iia.org.au/technicalResources/standards.aspx
[25] http://www.iia.org.au/technicalResources/professionalGuidance.aspx
[26] http://www.iia.org.au/technicalResources/practiceGuides.aspx
[27] http://www.audit.vic.gov.au/reports_and_publications/latest_reports/2012-13/20121114-public-hospitals.aspx
[28] http://www.audit.vic.gov.au/reports_and_publications/latest_reports/2011-12/20111123-local-govt.aspx
[29] http://www.audit.vic.gov.au/reports_and_publications/latest_reports/2011-12/20120523-tertiary-ed.aspx

Guidance 3.3 – Financial authorisations

Objective	This guidance provides information to support Public Sector Agencies in following Direction 3.3, including how to ensure authorisations are properly exercised, reviewed and recorded.
Effective date	1 July 2016
Relevant Directions	2.2 Responsible Body 2.3 Accountable Officer 3.3 Financial Authorisations
Last reviewed	1 February 2016

Authorisation is appropriate

Authorisations may be used when:

- it is required for the effective conduct of the business; and/or
- a formal separation of duties is required; and/or
- there is a need to mitigate financial risk, including Fraud.

Formal separation of duties is a key internal control element designed to reduce errors and the risk of Fraud. Authorisations for the spending and receipt of public monies should be allocated in such a way that no one authorised position has control or authority over the end to end process.

Authorised persons should have:

- an understanding of the scope of their authorisation (e.g. the type of activity);
- an understanding of any limits applying to their authorisation (e.g. financial limits);
- knowledge of processes for exercising an authorisation;
- knowledge of mechanisms for managing any conflicts of interest (actual or perceived) related to an authorisation; and
- awareness and understanding of all relevant policies, procedures and guidelines in the Agency's internal control system as well as external legislative requirements.

Central record of financial authorisations

A central record of financial authorisations should contain the following details:

- the transaction type, for example financing, investing and operational types;
- a list of positions holding financial authorisations for each transaction type;
- financial and operational limitations for each transaction or authorisation type;
- a list of staff names holding positions; and
- specimen signatures and/or electronic approval processes for each holder of an authorisation.

Authorisations are current and reviewed

A review of authorisations should occur regularly to ensure they are appropriate for the efficient and effective conduct of the business of the Agency.

The following could be considered as a part of the review:

- Is there any evidence of non-compliance with authorisations?
- Are there instances of authorisations not operating effectively?
- Is there any evidence of Fraud?

- Are there any concerns about conflicting authorisations?
- Have there been any significant changes to the structure, objectives and roles of the Agency and positions?
- Has an authorisation never or very rarely been used?

Mechanisms should be in place to enable continuous and efficient running of the Agency in the absence of the holders of an authorised position. In the event of a major restructure of an Agency (e.g. a restructure affecting 50 per cent or more of the positions in the Agency), financial authorisations should be reassessed and reapproved within one calendar month.

Financial authorisation following machinery of government changes

Following the announcement of machinery of government changes, Portfolio Departments should endeavour to facilitate the making of new financial authorisations to ensure they are in place from the effective date of the proposed changes.

For Portfolio Departments, the Responsible Body is the Minister or the Ministers jointly if there is more than one Minister for that Portfolio Department. Accordingly, in a Portfolio Department with multiple portfolio Ministers, a financial authorisation should be conferred 'jointly' by all of its respective Ministers .

A financial authorisation may be conferred 'jointly' by having each Minister sign the one instrument of authorisation (i.e. the same document). Alternatively, each Minister could provide separate written authorisation by signing a counterpart copy of the instrument of delegation.

Equally, when remaking financial authorisations, each relevant Minister could sign the one instrument of delegation or provide separate written authorisations by signing a counterpart copy of the instrument of delegation.

If an instrument of authorisation is being signed in counterpart, it should expressly state that it is to be (or can be) signed in counterpart by the relevant Ministers. Departments should also advise their Ministers that each portfolio Minister has been provided with a counterpart copy for signature.

Employees of the Public Sector Agency

Authorised persons are to be employees of the Agency. For differences between employee, contractors and consultants, refer to Victorian Public Sector Commission's Guidance for Managers Engaging Contractors and Consultants to Perform a Public Sector Function[30].

Further information

For more information on financial authorisations, please visit the Victorian Public Sector Commission's website[31].

[30] http://vpsc.vic.gov.au/html-resources/guidance-for-managers-engaging-contractors-and-consultants/
[31] http://vpsc.vic.gov.au/governance/governance-structure-and-roles/governance-structure/

Guidance 3.4 – Internal control system

Objective	Describes the five key components of the Committee of Sponsoring Organisations of the Treadway Commission (COSO) Framework, and provide further information on maintaining and implementing policies and procedures.
Effective date	1 July 2016
Relevant Directions	3.3 Financial Authorisations 3.4 Internal control system 3.5 Fraud, Corruption and Other Losses 3.6 Purchasing and prepaid debit cards 3.7 Managing risk 3.9 Managing financial information 4.2 Using and managing public resources 5.3 External reporting and information provision
Last reviewed	1 February 2016

Internal control system

An internal control system is a range of processes established by an Agency's Responsible Body, management, and other personnel, to provide reasonable assurance regarding:

- effectiveness and efficiency of operations, including financial and operational performance goals and safeguarding assets against loss;
- reliability of reporting, including internal and external financial and non-financial reporting; and
- compliance with applicable laws and regulations to which the Agency is subject.

An Agency's internal control system should clearly articulate expectations and internal accountabilities for the management of the Agency's activities and key risks.

COSO Framework

The Committee of Sponsoring Organisations of the Treadway Commission (COSO) *Internal Control – Integrated Framework* [32] provides approaches and examples of how Agencies can apply key principles in designing, implementing, or conducting control over the Agency's operations.

The framework sets out five components of internal control. It also sets out seventeen principles representing the fundamental concepts associated with each component. The principles can apply to any size or type of Agency. However, the extent to which these principles are implemented by Agencies may vary depending on risk profile and complexity of operations. For example, government Departments and Agencies with more complex risk profiles and operations may include additional principles (such as Prudential Requirements and Insurance Requirements for Public Finance Corporations). Application of the principles will also evolve as circumstances change over time.

The five components of the COSO Framework and associated principles are described below.

[32] http://www.coso.org/ic.htm

Control environment

The control environment is the foundation for all other components of internal control. The Accountable Officer and senior management should set the tone for the organisation in relation to the importance of internal control and expected standards of conduct. The control environment provides discipline, process and structure.

The five principles relating to the control environment are:

- the Agency demonstrates a commitment to integrity and ethical values;
- the Responsible Body demonstrates independence of management and exercises oversight for the development and performance of internal control;
- the Responsible Body establishes structures, reporting lines and appropriate authorities and responsibilities in the pursuit of objectives;
- the Agency demonstrates a commitment to attract, develop and retain competent individuals in alignment with objectives; and
- the Agency holds individuals accountable for their internal control responsibilities in the pursuit of objectives.

Risk assessment

Risk assessment involves a dynamic and iterative process for identifying and analysing risks to achieving the Agency's objectives and forming a basis for determining how risks should be managed. Management should consider possible changes in the external environment and within its own business model that may impede its ability to achieve its objectives. See Direction 3.7.1 for specific requirements in the VPS.

The four principles relating to risk assessment are:

- the Agency specifies objectives with sufficient clarity to enable the identification and assessment of risks relating to objectives;
- the Agency identifies risks to the achievement of its objectives across the Agency and analyses risks as a basis for determining how the risks should be managed;
- the Agency considers the potential for fraud in assessing risks to the achievement of objectives; and
- the Agency identifies and assesses changes that could significantly impact the system of internal control.

Control activities

Control activities are the actions established by policies and procedures to help ensure management's directives to mitigate risks are carried out. Control activities are performed at all levels of the Agency and at various stages in business processes, and over the technology environment.

The three principles relating to the control activities are:

- the Agency selects and develops control activities that contribute to the mitigation of risks to the achievement of objectives to acceptable levels;
- the Agency selects and develops general control activities over technology to support the achievement of objectives; and
- the Agency deploys control activities as manifested in policies that establish what is expected and in relevant procedures to affect the policies.

Information and communication

Sharing information is necessary to achieve organisational objectives. Communication occurs both internally and externally and provides the Agency with the information needed to carry out day-to-day internal control activities. Communication enables all personnel to understand responsibilities in relation to internal controls and their importance in achieving objectives. See Direction 3.9 for specific requirements in the VPS.

The three principles relating to information and communication are:

- the Agency obtains or generates and uses relevant, quality information to support the functioning of other components of internal control;
- the Agency internally communicates information, including objectives and responsibilities for internal control necessary to support the functioning of other components of internal control; and
- the Agency communicates with external parties regarding matters affecting the functioning of the components of internal control.

Monitoring activities

Ongoing evaluations, one-off evaluations, or some combination of the two are used to ascertain whether each of the five components of internal control, including controls to affect the principles within each component, are functioning effectively. Findings are evaluated and deficiencies are communicated in a timely manner, with serious matters reported to senior management and to the Responsible Body.

The two principles relating to monitoring activities are:

- the Agency selects, develops, and performs ongoing and/or separate evaluations to ascertain whether the components of internal control are present and functioning; and
- the Agency evaluates and communicates internal control deficiencies in a timely manner to those parties responsible for taking corrective action, including senior management and the Responsible Body, as appropriate.

Policies and procedures

In maintaining and implementing policies and procedures, the Accountable Officer may wish to consider:

- defining and documenting roles and responsibilities for positions in the financial management team structure to ensure the most effective and efficient allocation of tasks and resources (prerequisite skills, qualifications and experience for each position should also be defined and documented);
- implementing procedures relating to the completion, review and monitoring of reconciliations;
- ensuring internal control procedures are not compromised when more than one financial delegation is assigned to a particular position;
- accessing whether financial management systems and data is not commensurate with roles and responsibilities; and
- reviewing all policies and procedures over a three to four year period.

The following circumstances could trigger a review of policies and procedures to ensure they are in line with requirements and the Agency's direction:

- significant change in the underlying business of the Agency, e.g. organisational restructure, merging or alteration of finance structure, changes to staff numbers or the finance team;
- legislation or regulation introduction/amendment with financial management impact (these changes often impact procedures rather than policies);
- new accounting standards or policies;
- the benefits of periodic review;
- whole of government or departmental change to financial management, e.g. implementation of shared services; and
- machinery of government changes.

Separation of roles (segregation of duties)

Separation of roles aims to prevent fraud and errors. This objective is achieved by disseminating the tasks and associated privileges for a specific business process among multiple individuals. In the event that this cannot be achieved due to limited resources or staff, compensating safeguards are to be established to manage the risks.

Conflicting roles and responsibilities relating to authorisation, record keeping, asset custody and relevant management functions should be identified and appropriately segregated. The Accountable Officer may wish to consider:

- enhancing the separation of roles by implementing proper controls over access to systems, programs, data, important documents or physical assets (access should be restricted to authorised staff commensurate with the duties assigned to them);
- ensuring physical controls restrict physical access to negotiable assets such as cash or for items that might easily be converted to cash or personal use;
- ensuring controls are documented and subject to periodic review by an independent function (that is, a business unit or person not associated with the internal control); and
- ensuring segregation of duties and restricted access controls are established in light of factors such as:
  - volume, complexity and financial significance of different types of transactions;
  - sequence of steps necessary to process transactions;
  - technology and application system(s) used to process transactions;
  - opportunities or motives for individuals to commit fraud or perpetuate errors;
  - risk of loss or financial misstatement due to errors or fraud; and
  - existence of alternative or compensating controls.

Financial authorisations

The Accountable Officer should establish and maintain financial authorisations to ensure that the financial obligations are undertaken by delegates with appropriate levels of authority.

Direction 3.3 outlines further requirements, including for financial authorisations. The associated guidance material provides details on how to ensure financial authorisations are properly exercised.

Monitoring and assessment activities and control representations

Internal control systems need to be monitored to assess the quality of the system's performance over time.

When the Agency determines a deficiency, management should assess the impact of that deficiency on the effectiveness of the Agency's internal control system. The responsibility of identifying and assessing deficiencies rests with the Agency in the normal course of performing its functions.

The controls representation should include:

- the system of internal control across the Agency mitigates risk to an appropriate, acceptable level;
- the control objectives and performance expectations are communicated to all relevant staff and used to design efficient controls to mitigate identified risks;
- decisions are made by those authorised to make them;
- resources are safeguarded against material loss due to waste, abuse, mismanagement, errors, fraud, omissions and other irregularities;
- relevant laws, regulations, policies, directives and standards regarding financial management and internal controls are adhered to;
- decision-makers receive relevant, reliable and timely financial and related non-financial information to monitor performance and effectiveness of the internal control system;
- appropriate actions are taken to correct suboptimal performance of internal controls; and
- adequate, objective and independent assurance has been sought over the design and operational effectiveness of the internal control system, which is generally undertaken by Internal Audit and the Audit Committee.

Managing revenue

Cost Recovery Guidelines

The Directions require Agencies to apply the *Cost Recovery Guidelines*.

The Cost Recovery Guidelines provide a rigorous framework for use by government agencies when considering, developing and reviewing user charges and regulatory fees.

They ensure that cost recovery arrangements in Victoria are transparent, efficient, effective and consistent with legislative requirements and government policy.

The 'annual rate' fixed by the Treasurer for the annual automatic indexation of fees and penalties (fines) can be found on DTF's website.

Receipt of money by payment card (credit/debit card)

Agencies should refer to the Payment Card Industry – Data Security Standards [33](PCI-DSS) when money is received via payment card.

Managing cash

Borrowing and investing cash

For the general government sector, the borrowing and investing of cash is managed through established cash management policies and processes between the Portfolio Departments, DTF and the Treasury Corporation of Victoria.

For those Agencies who are able to borrow or invest cash, refer to Direction 3.7.2 for obligations and guidance.

Managing expenditure

Whole of government policies

Gifts, Benefits and Hospitality: Gifts, Benefits and Hospitality Policy Framework[34], issued by the Victorian Public Sector Commission.

Travel: Victorian Public Sector Travel Principles[35] which is available from DPC.

Advertising and Communications: Victorian Government Communication Guidelines 2012[36] issued by DPC.

Remuneration of Boards, Statutory Bodies and Advisory Committees: Appointment and Remuneration Guidelines for Victorian Government Boards, Statutory Bodies and Advisory Committees[37] issued by DPC.

Managing taxes

Taxation obligations and concession requirements applicable to an Agency

Depending on an Agency's individual circumstances, various Commonwealth taxation obligations and concessions may apply. These obligations are administered by the Australian Taxation Office[38] (ATO).

Commonwealth taxation obligations that may apply to an Agency include:

- Goods and Services Tax (GST);
- Pay As You Go (PAYG);
- Fringe Benefits Tax (FBT);
- Superannuation Guarantee Charge (SGC);
- Excise and customs duty;

[33] https://www.pcisecuritystandards.org/pci_security/
[34] http://vpsc.vic.gov.au/resources/gifts-benefits-and-hospitality-policy-framework/
[35] http://www.procurement.vic.gov.au/files/3629ef59-3e55-478e-8905-a40600ba5ee9/VPS-Travel-Principles-March-2010.pdf
[36] http://www.dpc.vic.gov.au/index.php/18-resources/communication
[37] http://www.dpc.vic.gov.au/index.php/policies/governance/appointment-and-remuneration-guidelines
[38] http://www.ato.gov.au/

- *Taxation Administration Act 1953*;
- National Tax Equivalent Regime (NTER); and
- ATO publications including, but not limited to, GST Rulings, FBT Rulings, Interpretative Decisions, and Determinations.
- Commonwealth taxation concessions may be available to an Agency, including:
  - Deductible gift recipient status;
  - Public benevolent institution status; and
  - Fuel tax credits.

Conduct of Commonwealth taxation obligations and concessions reviews

Consistent with Direction 5.1.2, an Agency is to conduct an annual review on a range of obligations. Whether the annual review of compliance includes Commonwealth taxation obligations and concessions is to be determined based on an assessment of tax risks.

Consistent with Direction 5.1.3, internal audit is to review in detail the Agency's compliance with all Commonwealth taxation obligations and concessions over a three or four year cycle.

When conducting a tax compliance review, the Agency should refer to the Australian Taxation Office's[39] website and its available supporting material.

Other relevant taxation compliance information

A better practice guide for the management of GST[40] – this guide has been published by the ATO to assist Agencies establish appropriate internal control frameworks for the effective management of goods and services tax (GST) administration.

Better practice for the administration of FBT[41] is also published by the ATO to help Agencies better administer their fringe benefits tax (FBT) obligations.

Agencies may also refer to DTF's website[42] or the Australian Taxation Office's[39] website for further information.

Managing shared services and outsourcing

Outsourcing is a process by which an Agency contracts with a third party to provide a specific service or group of services. Services are typically outsourced to achieve cost savings, improve quality, and access specialised skills or other efficiencies. Some examples of commonly outsourced services include payroll, investment consulting, debt collection and the maintenance of financial systems.

[39] http://www.ato.gov.au/

[40] http://www.ato.gov.au/Business/GST/In-detail/Non-profit-and-government-organisations/Government-organisations/A-better-practice-guide-for-the-management-of-GST/

[41] https://www.ato.gov.au/general/fringe-benefits-tax-(fbt)/in-detail/government-organisations/better-practices-for-managing-specific-fringe-benefit-types/

[42] http://www.dtf.vic.gov.au/Home

Outsourcing – models of service delivery

There is a broad spectrum of models to deliver services. The following table provides an overview of the spectrum of service delivery models.

Internal delivery	Delivery of the service is managed and resourced internally. Third parties may provide discrete products or services.
Full outsourcing	Where a single contract with a single supplier covers a broad scope of services and needs. This model is typically implemented as a strategic partnership between management and the service provider and is usually put in place for the long term.
Co-sourcing	Responsibility for delivery of service is split between an outsourcer and internal delivery. This model often involves an internal delivery team working with the outsourcer as a single group.
Insourcing/shared services	Insourcing or shared services disconnect a service from the organisation via a separate business unit. The business unit is usually set up with its own profit/loss statement. An agreement such as a Service Level Agreement (SLA) is commonly in place to govern the provision of the service and payment levels. The underlying concept is to run the separate unit like a business and emulate outsourcing services and pricing. The benefits of this type of arrangement are that organisations can achieve consolidation, integration, and standardisation while maintaining direct control of the service provider and openness to changing market options.
Selective sourcing	Where multiple contracts are set up with multiple suppliers. This type of arrangement is common in the public sector. This model is often implemented when the sourcing strategy is undefined and there is a variety of service delivery options. Benefits of this type of outsourcing model include the ability to leverage the markets' best capabilities in a very competitive environment. Innovation is available and the cost associated with the change is typically minimal. When managed effectively, agility, flexibility, and scalability are readily available.

The following should be considered in complying with Instruction 3.4.10 *Managing shared or outsourced services*:

Before engaging a service - cost-benefit analysis

Prior to engaging an outsourced service provider, Agencies should undertake a cost-benefit analysis. The cost benefit analysis should include:

- the costs and basis for estimating the cost;
- the benefits and basis for estimating the benefits;
- an assessment of planned non-financial benefits;
- potential risks associated with outsourcing the function and how they will be mitigated; and
- a recommendation for future proposed action.

Management of outsourced services

Direction 3.1 requires that the Responsible Body ensure effective management and oversight of shared services arrangements and private sector providers of financial management activities and obligations (outsourcing).

The Responsible Body should be aware that entering into shared services arrangements does not diminish the responsibilities of the Chief Finance Officer (CFO) and the Accountable Officer for the outsourced function – a service can be outsourced, but the risk and responsibilities cannot.

An outsourced financial service will impact on the financial management, financial processing or financial statements of an Agency. Accordingly, specific assurance on the control procedures of the outsourced service provider is needed to ensure the:

- Agency's responsibilities and accountabilities for good governance and sound financial management are not negatively impacted by the outsourced activities;
- provider is complying with the agreed terms and conditions (e.g. performance measures as outlined in the contract or Service Level Agreement);
- controls for activities and processes are effective and result in accurate reporting of financial and other relevant information;
- control environment surrounding the outsourced services facilitates complete and accurate processing of underlying transactions and/or data; and
- Accountable Officer and CFO can sign off on their formal annual statements that the:
  - financial reports are presented fairly;
  - risk management, internal compliance and control framework is sound; and
  - internal control framework is operating effectively and efficiently.

In addition, to ensure all legislative requirements are being met, the outsourced or shared services should operate within the requirements of the FMA, the Directions, Instructions and other relevant legislation applicable to the Agency. For example, if the payroll function is being outsourced, the Accountable Officer and the CFO need to ascertain that the service is being delivered in compliance with the relevant requirements in the Directions.

Obtaining assurance from an outsourced service provider

Before engaging an outsourced service provider, an Agency should consider the Assurance or Auditing Standard requirements[43], and liaise with its internal and/or external auditors to discuss the best approach to obtain assurance. This will ensure the Agency receives assurance reports that are fit for purpose and provide an accurate reflection of the control environment in the outsourced provider.

The type and level of assurance required should be determined in the context of an Agency's individual risk profile (e.g. complexity of operations and size) and be factored in as part of the initial contract negotiation. The service contract should also provide access to the service provider's information by an Agency's internal and external auditors.

Note: If an Agency is aware that several Agencies are using the same outsourced service provider, it may initiate discussions with those Agencies and the provider to obtain a combined assurance report. However, such a report should meet the individual assurance needs of each Agency.

[43] Australian Standard on Assurance Engagements ASAE 3402 Assurance Reports on Controls at a Service Organisation or Auditing Standard AUS 810 Special purpose reports on the effectiveness of control procedures.

The following options for obtaining assurance may be considered:

Option 1: **Assurance from the outsourced service provider**	This may be either: • A **publicly available opinion** on internal control (usually this is an opinion in accordance with Australian Auditing Standards that is made available to all customers of the outsourced service provider); or • An **opinion or report specifically designed** (e.g. letter of comfort) for the use of the Agency. In these instances, a tailored scope of work will typically be **requested by the Agency**, but the work is performed and report provided by the outsourced service provider's internal or external auditors.

Option 2:
 	
Assurance provided by an independent auditor
	An Agency may arrange for an **independent auditor** (e.g. the Agency's internal auditor or a third party) to visit the outsourced service provider to obtain assurance.
	
	In these instances, the Agency will determine the scope of work and results will be reported in a format the Agency is familiar with.
	
	Factors that need to be considered in interpreting the results include, but are not necessarily limited to:
	
	• What type of opinion or report has been issued?
	  – Is there a reference to an auditing standard? If so, is there an expression of the level of assurance provided and are there any limitations on scope referred to?
	• What period of time is covered by the opinion or report?
	  – Is this consistent with the period of interest to the Agency?
	• What locations, specific business processes and/or transactions have been reviewed and reported on?
	  – Do these cover the full scope of the Agency's activities or transactions provided by the outsourced service provider? If not, are the activities or transactions not covered material or significant to the Agency?
	• What issues or concerns have been identified? What is their impact?
	• What resolution plans has the provider put in place?

Agencies are encouraged to closely consider, and act on, the findings in assurance reports.

Financial information

Direction 3.9 requires the Accountable Officer to ensure that the Agency applies relevant legislation, standards and policies in relation to the management of financial information, including financial information systems.

Appropriately managing financial information (including IT systems) is a key internal control of Agencies. For example, it may not be possible to have confidence in financial statements that have not been kept on adequate IT systems.

Guidance 3.9 provides more guidance on managing financial information.

Guidance 3.5 – Fraud, Corruption and Other Losses

Objective	Provides further information to assist Agencies in establishing a Fraud, Corruption and Other Losses prevention and management policy and establishing a sound control environment and assessing risks of Fraud, Corruption and Other Losses.
Effective date	1 July 2016
Relevant Directions	3.2.1 Audit Committee 3.4 Internal control system 3.5 Fraud, Corruption and Other Losses 5.1.5 Dealing with Compliance Deficiencies
Last Reviewed	1 February 2016

Fraud and Corruption

The AS 8001 -2008 *Fraud and Corruption Control Standard* defines Fraud and Corruption as follows:

Fraud is dishonest activity causing actual or potential financial loss including theft of monies or other property by employees or persons external to the entity and where deception is used at the time, immediately before or immediately flowing from the activity. This includes:

- the deliberate falsification, concealment, destruction or use of falsified documentation used or intended for use for a normal business purpose; or
- the improper use of information or position for personal financial benefit.

Corruption is a dishonest activity in which an employee of an entity acts contrary to the interests of the entity and abuses his/her position of trust in order to achieve some personal gain or advantage for him/herself or for another person or entity.

Fraud, Corruption and Other Losses prevention and management policy

The Agency's Fraud, Corruption and Other Losses prevention and management policy should document the Agency's approach to controlling Fraud and Corruption exposure at strategic, tactical and operational levels. It should also detail the Agency's intended action in implementing and monitoring the policy.

The policy drives the development and operation of the control framework. Both the policy and control framework should be consistent with the latest AS 8001 -2008 Fraud and Corruption Control Standard (the Standard). The extent to which the Standard should be applied will differ depending on the size of the Agency and the outcome of the Fraud and Corruption risk assessment.

There are a number of internal and external Corruption risks associated with financial management including procurement, contract management and collecting and/or distributing funds and other property. As such, the policy and internal control framework should place high importance on prevention and detection, as well as recovery of any funds defrauded from the Agency. In these Agencies, the AS8001 standard should be applied in its entirety.

For Agencies with lower Fraud or Corruption risk, the Responsible Body should apply those elements of the Standard applicable to the Agency's circumstances.

The policy should include:

(a) responsibilities for Fraud and Corruption management in the Agency;

(b) processes for managing employee awareness;

(c) thresholds that define significant Fraud;

(d) processes for managing the safety and security of assets (refer to Direction 4.2.3 for more details);

(e) Fraud and Corruption detection and reporting processes;

(f) fraud risk profile development and assessment processes;

(g) protected disclosure systems and contacts;

(h) investigation procedures;

(i) recovery systems and processes; and

(j) disciplinary procedures.

Establishing a sound control environment

The Agency's control environment should include the safeguard and security of property and money. It also includes the systems, rules, delegations and accountabilities to minimise the prospect of Fraud or Corruption occurring. In the event that the Agency's preventative control systems fail, Agencies should implement systems aimed at detecting Fraud and Corruption as soon as possible after it has occurred. Recommended elements of Fraud and Corruption policy and sound control environment are outlined below.

Culture

Implementing and maintaining a sound ethical culture is a key strategy in managing the risk of Fraud and Corruption in an Agency. An Agency should aim to ensure that it has a healthy and sustainable ethical culture underpinned by example setting by senior management. Refer to the Victorian Public Sector Code of Conduct[44] for more details.

Line management accountability

Agencies should ensure that line managers are aware of their accountabilities for the prevention and detection of Fraud and Corruption. The management of Fraud and Corruption should be incorporated into the performance measurement system and each line manager's performance should be measured against relevant benchmarks.

Separation of roles and delegations

Agencies should ensure appropriate separation of roles exist in their internal processes. Separation of roles is the concept of having more than one person to complete a task. Official delegations are required for the spending and receipt of public monies and should be allocated in such a way that no one delegate has control or authority over the end to end process. Such separation of roles provides for checks and balances to be the responsibility of different employees. Such separation of roles and delegations is important in transactions involving the receipt or payment of moneys, entering into or administering contracts and in the employment or remuneration of staff. Refer to Directions 3.3 and 3.4 for more details.

Risk consciousness

A high level of risk consciousness for the risks of Fraud and Corruption should be present across the senior management group. Agencies exhibiting 'best practice' in the control of Fraud and Corruption invariably have a senior management group that recognises the need for Fraud and Corruption prevention and detection even in the absence of recently detected incidents.

Process controls

Agencies should ensure that all business processes, particularly those assessed as having a higher predisposition to the risks of Fraud and Corruption, are subject to a rigorous system of internal controls that are well documented, updated regularly and understood by all personnel.

Protected disclosure program

Agencies should be aware of their obligations under the *Protected Disclosure Act 2012*. Processes designed to comply with the Act are one component of a sound internal control system for Fraud and Corruption prevention and assessment.

[44] http://vpsc.vic.gov.au/resources/codes-of-conduct/

Employment screening

Employment screening should be conducted within the confines of relevant legislation and with the informed and express consent of the employee. Agencies should have regard to the Victorian Public Service Commission's Integrity in Recruitment Guidance Note[45]. Employment screening is contemplated for all new employees joining the organisation (including contractors) and all personnel being transferred to a senior executive position or to a position considered by the Agency to be 'higher risk' in terms of the potential exposure to Fraud or Corruption associated with those positions. Levels of vetting will vary depending on the risk associated with the Agency and with the specific position.

Supplier vetting

Agencies should take steps to ensure the bona fides of new suppliers and periodically confirm the bona fides of continuing suppliers. The Agency should consider its ongoing commercial relationship with the other party if inquiry finds a heightened risk of Fraud or Corruption in continuing to deal with that party.

Investigation

An investigation into apparent or suspected Fraud, Corruption and Other Losses should be conducted as soon as possible after Agency management becomes aware of it. Any investigation should be managed and conducted by people who:

- have appropriate skill and experience;
- are independent of the business unit in which the alleged fraudulent or corrupt conduct occurred; and
- do not have a conflict of interest.

The investigator(s) does not need to be a staff member of the Agency. Suspicions of Fraud or Corruption may also be referred to more appropriate Agencies for investigation including:

- the Victorian Auditor-General – for mismanagement of public funds and services or where funds have not been properly raised, protected from loss, or spent with maximum efficiency and effectiveness; or
- Victoria Police – where the matter constitutes a criminal offence and where an indictment is likely; or
- the Independent Broad-based Anti-corruption Commission – for identifying, investigating and preventing corrupt conduct across the whole public sector.

An Agency should include in its internal discipline policy how disciplinary proceedings should be conducted against employees found to be involved in Fraud, Corruption or Other Losses.

Recovery systems and processes

As Fraud, Corruption and Other Losses involve the loss of public monies, assets or property, all reasonable attempts should be made to recover those losses. The resources applied to recover such losses should be commensurate with:

- the size of the loss;
- the reputation issue for Government; and
- the likelihood of successful recovery.

Section 57 of the FMA provides for the investigation and recovery of loss or damage by an officer.

Where an Agency wishes to use external skills for recovery of losses, only reputable Agencies or individuals should be used.

Assessing risks of Fraud, Corruption and Other Losses

Agencies should adopt a policy and processes for the systematic identification, analysis and evaluation of Fraud, Corruption and Other Losses risk and should periodically conduct a comprehensive assessment of the risks of Fraud, Corruption and Other Losses in their business operations.

[45] http://vpsc.vic.gov.au/html-resources/integrity-in-recruitment-guidance-note/

The frequency with which the Agency should conduct an assessment of these risks will be dependent upon factors such as the Agency's size, complexity of business operations, and the extent to which the Agency is monitored by other Agencies. Typically an assessment should be conducted at least every two years. The risk assessment should be conducted in accordance with AS/NZS ISO 31000:2009, *Risk management - Principles and guidelines*.

Agencies should ensure that adequate means for reporting suspicious or known illegal or unethical conduct are available to all personnel. The Agency should consider a policy of mandatory reporting of known or suspected Fraud, Corruption or Other Losses through one or more alternative reporting lines.

Systems should be in place for confidential reporting of suspicious conduct and for the reporter to suffer no repercussions.

Audit of business processes or units

Directions 3.2.2.2 (b) and (c) requires a strategic audit plan and annual work program to be developed. These must include audits to identify business processes likely to be vulnerable to Fraud or Corruption, and targeted reviews for potential or actual Fraud, Corruption and Other Losses in those business areas or processes identified as vulnerable to Fraud or Corruption.

Audits should:

- involve senior management;
- be documented; and
- include areas for detailed review.

Targeted reviews should include:

- assessment of controls to prevent Fraud, Corruption and Other Losses in that business area or business process;
- suitable treatment plans and remedial actions; and
- accountabilities assigned for administering the treatment plans.

Guidance 3.6 – Purchasing and prepaid debit cards

Objective	Provides guidance to establish an efficient and effective process for achieving the objectives of the Instruction and outcomes of the Direction.
Effective Date	1 July 2016
Relevant Directions	3.3 Financial Authorisations 3.5 Fraud, Corruption and Other Losses 3.6 Purchasing and prepaid debit cards 5.1 Financial management compliance
Last reviewed	1 February 2016

Roles and responsibilities

Accountable Officer

Accountable Officers are responsible for establishing the purchasing and/or prepaid debit card program in their Agency in accordance with the requirements in the Instruction. They have the ability to delegate these responsibilities in accordance with Direction 3.3.

Accountable Officers and program administrators are responsible for having effective administrative policies and procedures for the use and administration of these cards, thereby providing the Responsible Minister with assurance that rigorous controls are in place.

Accountable Officers are to review all instances of unauthorised use and non-compliance with the Instruction reported by the program administrator. They are to report any Significant or Systemic non-compliance to the Audit Committee and as soon as practicable of the non-compliance occurring, to the Responsible Minister, Portfolio Department and the Auditor-General (refer Direction 3.5.3). If necessary, the non-compliance should be referred to the police for investigation and action, or in the case of **corruption**, to the Independent Broad-based Anti-corruption Commission. Otherwise it should be referred for disciplinary action unless the Accountable Officer considers the unauthorised use was accidental or was not part of a pattern of unauthorised use (accidental or not).

Program administrator

Program administrators provide operational support to Accountable Officers in administering the purchasing and/or prepaid debit card program for their Agency. They are the main contact for the card providers, cardholders and authorised signatories (approver of expenditure).

A program administrator should be nominated when the Agency provides administrative support to Responsible Ministers for the management of purchasing and/or prepaid debit cards to relevant statutory office holders.

Program administrators should consider applying the following procedures for each authorised signatory appointed by the Accountable Officer:

- confirm that the authorised signatories hold a financial authorisation (this does not have to be of a particular quantum); and
- the authorised signatories understand their responsibilities, what constitutes purchases for official purposes and how to report unauthorised use.

Program administrators should when issuing cards to cardholders:

- confirm the employee has the appropriate financial authorisation at least equivalent in value to the transaction limit agreed by the authorised signatory, and in instances when the employee does not have financial authorisation for the prepaid debit card, the authorised signatory has the appropriate financial authorisation;
- ensure the employee reads the card provider's terms and conditions provided with the card;

- ensure the employee reads and signs an 'Undertaking by the cardholder' which sets out the policies and procedures of the Agency (Attachment A provides a sample of an agreement) and any restrictions on the types of goods or services for which the cardholder may use the card (e.g. restrictions on domestic and overseas travel, hospitality and entertainment);
- ensure the employee is appropriately trained on the operation and use of the cards;
- ensure the employee signs the purchasing card immediately;
- circulate any revised obligations or Agency policies to the cardholder in a timely manner;
- record information about cardholders; and
- assess the requirement for ongoing issue of the card to the current cardholder including limits and types of expenses, when the cardholder changes position in an Agency.

Program administrators are to refer promptly all cases of unauthorised use or non-compliance with the Instruction to their Accountable Officer.

Authorised signatory (approving expenditure)

Authorised signatories should generally be employees who are senior to the cardholders they are responsible for. For Accountable Officers who are cardholders, the chair of the relevant Audit Committee should be the authorised signatory. For statutory office holders and Agencies exempted from having an Audit Committee, the authorised signatory should be the chair of the relevant Portfolio Department's Audit Committee.

An authorised signatory must hold a financial authorisation, and have undertaken training and developed an understanding of all responsibilities and requirements of holding a financial authorisation.

The purpose of the authorised signatory's approval is to serve as a review of the transaction. When approving purchases, authorised signatories should scrutinise the purchases as if they were made through the mainstream procurement and payment systems. For example, are they for official purposes, appropriate for business use, have goods and services been received and is there sufficient supporting documentation. The approved statement is forwarded to the program administrator for processing. Any non-accidental unauthorised use should be reported to the program administrator.

Cardholders

Cardholders must be employees of an Agency. Ministers and their staff are not eligible to be cardholders as they are not employees of an Agency. Statutory office holders (e.g. the Auditor-General, Electoral Commissioner and Ombudsman) may require access to purchasing and prepaid debit card services. Although not technically employees of the Agencies, the Minister has authorised the provision of these cards to persons occupying these offices, subject to the cardholders adhering to a control regime which is at least equivalent in its standards to that applying to employees of Agencies. The Minister may provide advice from time to time to assist the Responsible Minister's or Parliamentary officer's oversight of the use and administration of purchasing cards outside the direct control of Accountable Officers in their portfolio.

Cardholders should acknowledge their responsibilities regarding the security and use of the cards as specified in the Instruction and read the card provider's terms and conditions. They should safeguard the card and its details at all times, especially when purchasing online or making payments, no different to how they would protect their personal credit or debit cards.

Cardholders should only use the card for official purposes. In determining whether a purchase is of a private or official nature, cardholders need to consider whether the purchase can legitimately be paid as if the transaction were being managed through mainstream procurement and payment systems. When it is unclear, for example the purchase of gifts or flowers for staff who are leaving the organisation or are ill, they should take advice from their authorised signatory before incurring the expenditure. Purchasing and prepaid debit cards are a purchasing facility and should not be used as a convenient alternative to seek reimbursement for minor work-related expenses. Cardholders should not purchase items using a 'stringing' arrangement, which is, splitting one transaction into many to avoid exceeding card limits.

Cardholders should review and sign their card statement/transaction report and provide this to their authorised signatory to approve. They should follow up any discrepancies on the statement with the card provider and promptly advise the program administrator.

Mitigate risk

The objective of card use policies and procedures is to assist in the management of risk. As a consequence, Agencies should consider the following as part of a broader risk management strategy overseen by its Audit Committee and internal audit program. Adherence to the Purchasing and Prepaid Debit Card Instruction is, therefore, more than a compliance exercise.

Agencies can perform a number of roles to mitigate risks in administering purchasing and prepaid debit card programs, including:

- appointing relevant administrative personnel (e.g. authorised signatories, program administrator) to ensure the efficient and effective administration of the facility account in that Agency. Persons appointed to such positions are to be at a level appropriate to the responsibilities of that position;
- assessing the costs and benefits of using purchasing and prepaid debit cards;
- developing adequate internal controls, security measures and reporting procedures to implement and control the operation of the purchasing and prepaid debit cards;
- determining their own internal rules or policies for the use and administration of the purchasing and prepaid debit cards, particularly regarding electronic commerce;
- administering and monitoring the operation of purchasing cards in compliance with the Department of Treasury and Finance (DTF) Instructions and any Agency policies or procedures. Service issues should first be raised with the card provider;
- authorising and processing the relevant documentation for the operation of purchasing cards;
- maintaining all documents, statements and reconciliations required to be kept in relation to the use and administration in accordance with the Instruction; and
- providing administrative support to Responsible Ministers for the management of purchasing cards as it applies to relevant statutory office holders. This function includes nominating a program administrator regarding these cardholders.

Internal controls

It is important that an Agency has appropriate internal controls to ensure the integrity and security of the card program, including:

- providing appropriate training to employees on their obligations under the Directions before they are issued with a purchasing and/or prepaid debit card;
- limiting the number of credit cards issued per employee to a maximum of one credit card and when necessary, to only one card per facility account (e.g. one Visa credit card and an American Express credit card);
- appropriate card limits (facility and transaction limits) are set and reviewed in line with the cardholder's actual usage;
- sufficient documentation is obtained and maintained covering the authorisation and identification of transactions, including merchant records and approved and reconciled statements;
- the allocation of transactions to expenditure types is made in the same manner as other Agency expenditure;
- a policy where cards are withdrawn and/or immediately cancelled:
  - on the termination, or notification of resignation of the cardholder's employment in an Agency;
  - when the card has been lost, stolen or misused;
  - when the card is no longer relevant to the performance of the cardholder's functions and duties in an Agency;
  - if the cardholder's account is inactive; or
  - when the cardholder incurs a number of separate instances of unauthorised use; and
- monthly reports are monitored by the program administrator.

Card linked directly to a bank account are covered by Direction 3.4 and Instruction 3.4 and not by Direction 3.6 and Instruction 3.6.

Sufficient supporting documentation

Instruction 3.6 *Purchasing and prepaid debit cards* (Requirement 5.1) requires a cardholder to obtain and retain sufficient supporting documentation for every transaction made using a purchasing or prepaid debit card.

Supporting documentation substantiates that transactions are made for valid business purposes and meet taxation requirements.

The requirement for sufficient supporting documentation applies irrespective of whether the transaction is:

- made directly with a merchant; or
- made by telephone, mail or electronic means.

Each transaction should be supported by the invoice, receipt or receipt reference the cardholder receives at the time of purchase or requested to be sent at the time of making the order.

Such documentation consists of, but is not limited to, receipts, tax invoices and merchant records (e.g. an airplane boarding pass).

When original supporting documentation is not obtainable, copies of such documentation can be provided with a cardholder-signed statement of why the original documentation was not available.

In exceptional circumstances when appropriate supporting documentation cannot be obtained, alternate certification may be acceptable. In these cases, the advice of the authorised signatory and/or appropriate Agency personnel (e.g. card program administrator) is best sought before a monthly statement is verified.

All supporting documentation is to be sufficiently detailed to adequately support the payment processes.

To avoid any doubt as to the level of documentation required regarding various transactions, Agencies may wish to determine transaction thresholds and matching substantiation requirements.

Review and approve the monthly statements or transaction report

A cardholder's expenses are to be authorised by the authorised signatory, who is senior to the cardholder. In the case of expenses incurred by Accountable Officers who are cardholders, arrangements are to be made for cardholder statements to be authorised by the chairman of the relevant Audit Committee. In the case of statutory office holders and those operating in an environment where there is no Audit Committee, arrangements are to be made through the relevant departmental Audit Committee to gain authorisation.

Good practice procedures for reviewing monthly statements

On a monthly basis, the cardholder is required to acquit and verify the transactions on the card to substantiate that they are valid and ensure no unauthorised use of the card by the cardholder or by a third party.

Good practice procedures include:

- reconciliations on a timely basis upon receipt of the monthly statement;
- discrepancies on the statement are to be followed up with the card provider and promptly advised to the program administrator;
- goods or services paid for using the card are actually delivered or provided;
- credits on the card are raised when, for example, a good or service is not delivered or not provided in accordance with original expectations;
- each transaction appearing on the card provider's statement is appropriately coded for accounting purposes; and
- sufficient supporting documentation for each transaction is attached to the card provider's statement when statements are provided by the cardholder to the authorised signatory for approval.

Reporting of significant or systemic instances of purchasing and prepaid debit card non-compliance

Unauthorised use should be reported by the cardholder and/or authorised signatory to the program administrator. The program administrator needs to promptly review each instance of unauthorised use or non-compliance and refer all cases of unauthorised use or non-compliance to the Accountable Officer.

The Accountable Officer is responsible for investigating Significant or Systemic instances of unauthorised use or non-compliance and reporting these to the Agency's Audit Committee, Responsible Minister, Portfolio Department and the Auditor General as required under Direction 3.5.

The *Australian Standards on Fraud and Corruption Control* (AS 8001) provides information on investigative, reporting and disciplinary considerations. When the Accountable Officer has determined that a significant non-compliance has occurred but does not warrant police involvement, the Accountable Officer should refer the matter for disciplinary action. Disciplinary action should conform with the Agency's disciplinary or misconduct policy.

Instruction 3.6 states that the purchasing or prepaid debit card must be withdrawn if any unauthorised transaction involves an amount greater than the limit deemed appropriate by the Accountable Officer or $1 000, whichever is the lower, or is part of a pattern of unauthorised use. In addition to referral for disciplinary action, when three separate instances of unauthorised use occur with the same cardholder, irrespective of the dollar amount, consideration should be given to withdrawing the purchasing or prepaid debit card immediately to minimise risk of future unauthorised use or non-compliance.

Role of Portfolio Departments

Direction 5.1.6 requires public sector Agencies to inform their Responsible Ministers and Portfolio Departments of any Material Compliance Deficiency. Direction 2.3.4 requires the Accountable Officer of a Portfolio Department to oversee the discharge of financial responsibilities and to provide information to the Responsible Minister on key assurance and risk matters.

For purchasing and prepaid debit cards, Portfolio Departments are expected to:

- monitor portfolio compliance with the Instruction on Purchasing card and prepaid debit cards;
- provide briefings to the Responsible Minister on non-compliance reported by the Portfolio Agencies; and
- review reports of non-compliance and implement strategies to promote compliance throughout portfolios.

DTF role

Direction 2.3.6 requires DTF to undertake the role of adviser to the Minister for Finance regarding the use and administration of purchasing cards policies as part of the financial management framework in the Victorian public sector.

Attachment A: Undertaking by the cardholder

Purchasing card cardholder agreement

Cardholder name:
Position:
Branch:
Division:
Agency:
Accountable Officer:
Authorised signatory:
Program administrator:

I understand and agree that the Purchasing Card is issued to me on the express understanding that I will, at all times, comply with the following conditions:

Use

1. The purchasing card is the property of (specify provider) and is in my possession and under my strict control.
2. I will not permit the purchasing card to be used by any person other than myself.
3. I will only use the purchasing card for official purposes.
4. I will immediately report any suspected or known unauthorised use of the purchasing card to the card provider and the program administrator.
5. I will not use the purchasing card to pay for expenses that have already been claimed (or will be claimed) by any form of allowance.
6. I will not use the purchasing card to pay for tips or gratuities, except in countries other than Australia, to the minimum extent expected in accordance with common practice in the country.
7. I will not use the purchasing card to obtain cash, except for prepaid debit cards, where cash may only be obtained if the Accountable Officer has authorised the use of the card for this purpose.
8. I can use the purchasing card to a maximum limit of $ in any one transaction and to a maximum monthly limit of $. My use of the purchasing card is subject to the following restrictions on transaction types (specify):
9. I will not split transactions on the purchasing card to avoid exceeding purchasing card transaction limits.
10. I hold a financial authorisation that is at least equivalent in value to the transaction limit in 8 above.
11. In the case of general government purchasing cards, I understand that purchasing information may be periodically reviewed by the Department of Treasury and Finance.

Transaction/monthly reconciliation

12. I will be issued with a monthly statement by the card provider. I will ensure that all transactions that appear on the monthly statement are verified by me and that sufficient supporting documentation is attached to the monthly statement when it is submitted for approval. I will ensure that goods or services paid for using the purchasing card are actually delivered or provided. I will ensure that each transaction appearing on the card provider's statement is appropriately coded for accounting purposes.

13. I will sign the monthly statement provided by the card provider to indicate that the transactions being paid by the State have been made only for official purposes.
14. I will ensure that credits are requested in relation to transactions made using the purchasing card as soon as I become aware of the need for a credit, for example, where a good or service is not delivered or not provided in accordance with original expectations.

Change in cardholder details

15. I will immediately advise the program administrator of any change in my name or contact details.

Upon resignation or transfer

16. I will immediately return my purchasing card to the program administrator if I resign or retire, or if my services as an employee of the Agency or statutory office holder are otherwise terminated, or if I take up a position in another Agency, or if I am instructed to do so by the Accountable Officer or the program administrator.

Lost or stolen cards

17. I will immediately report the loss or theft of my purchasing card to the card provider (24 hour ☎ service) and the program administrator.

Declaration

18. I confirm that I have access to only one purchasing card.
19. I acknowledge receipt of Instruction 3.6 (Purchasing and prepaid debit cards).
20. I have been briefed on all aspects of the operation and use of the purchasing card.

Signature of cardholder	Signature of Agency program administrator
Name of cardholder	Name of Agency program administrator
Date	Date

Guidance 3.7– Managing specific risks – business continuity planning, indemnities and immunities

Objective	Provides guidance on managing risks, business continuity planning, insurance, indemnity and immunity considerations.
Effective date	1 July 2016
Relevant Directions	3.2 Oversight and assurance 3.4 Internal control system 3.7 Managing risk
Last reviewed	1 February 2016

Business continuity management

Business continuity management aims to support continuous operations before, during and after a significant business disruption. AS/NZS 5050:2010 Business continuity – Managing disruption related risk explains how to apply AS/NZS ISO 31000:2009 Risk management – Principles and guidelines to disruption-related risks.

Further guidance on business continuity management is available:

- Australian National Audit Office – Business Continuity Management – building resilience in public sector entities: Better Practice Guide June 2009. [46]

Treasurer's indemnity and statutory immunity

An indemnity is an agreement to be responsible for the financial liability for all, or a part, of the loss or damage that another party may suffer. An indemnity creates a potential financial risk or liability that may be realised at a later date due to the occurrence or non-occurrence of a specified event. Indemnities may be provided by the Government whereby it accepts responsibility for the liability that its employees or agents, or occasionally, another entity or person, may incur.

An immunity is a legislative provision that prevents action being taken against a person and confers protection from all forms of civil liability.

[46] http://www.anao.gov.au/uploads/documents/Business_Continuity_Management_.pdf

Guidance 3.7.2.2 – Treasury and investment risk management policies

Objective	Provides information to assist with the preparation of Financial Market Risk Management Polices, in particular Treasury and Investment policies and in complying with the requirements.
Effective date	1 July 2016
Relevant Directions	3.7.2 Treasury and investment risk management
Last reviewed	1 February 2016

Treasury Policy

Treasury policies set parameters for Treasury risk management and should be consistent with the Agency's overall corporate policies, objectives and risk culture.

The Treasury Policy document for the Agency should include sufficient information to detail all aspects relevant to achieving the primary objectives of the Treasury operation. Although the policy will vary across Agencies in its specific detail, there is similarity in the general content to be included. The proposed content of the policy is described below. An example of a Treasury Policy is available in Attachment A.

Introduction and overview

This section covers:

- purpose of the Treasury Policy;
- scope of the Treasury Policy;
- reference to other documents relevant to the treasury management function; and
- description of the position responsible for maintaining and approving the Treasury Policy, the process for review and amending the policy and the frequency of review of policy.

Treasury objectives and strategies

This section provides a brief outline of the objectives of the Treasury operation, including strategies developed to achieve those objectives. The Responsible Body's risk tolerance can be reflected in the Treasury's objectives and strategies.

Roles and responsibilities

This section covers information regarding the roles and responsibilities of the parties involved in the management, control and reporting of the organisation's financial risks. Typically, the involved parties will be some or all of the following:

- Responsible Body;
- Accountable Officer;
- Chief Finance Officer;
- Treasury Committee; and
- Treasury Manager.

Delegation of authority

This section covers the delegation of authority, from the Responsible Body down through the Agency to the Treasury, and delegation in the Treasury. Delegations form a vital part of both the Agency's governance structure and the Treasury Policy.

A listing of delegated authorities and discretionary limits (often held as an attachment to the policy), details what transactions are delegated to whom, who should authorise them and what limits apply. It can be comprehensive in capturing all types of transactions that are subject to delegation. Refer to Direction 3.3 for requirements.

Treasury risk recognition and management

This section should include clear definition of risks, details of recognition, measurement, timing and objectives of risk management.

Further information on risks can be found in a later section of the guidance on 'Treasury risks'.

The following factors should be considered in developing strategies to manage risk:

- Agency projected cash flows over the short to medium-term;
- the life cycle of assets and the strategies for their replacement;
- the nature and structure of existing liabilities;
- the sensitivity of the Agency's cash flows to movements in economic variables, commodity prices and financial market variables (e.g. interest rates, inflation rates and exchange rates); and
- the risk tolerance of the Responsible Body.

Approved financial instruments

This section specifies the financial instruments approved by the Treasurer of Victoria. The Responsible Body may wish to provide further limits on the approved instruments.

For each category of approved financial instrument, it is recommended the policy document covers:

- maximum maturity for which instruments may be entered into;
- maximum amount per transaction; and
- that they should be with TCV/VFMC or as otherwise approved by the Treasurer.

Use of financial arrangements (derivatives)

This section includes information on financial arrangements entered into. In developing, maintaining and complying with guidelines for the use of financial arrangements (derivatives) as per Instruction 3.7.2.2 *Treasury and investment risk management policies*, particular attention should be given to:

- items which expose the Agency to risk and need to be hedged;
- approved instruments that are effective in reducing the exposures; and
- management reports to measure, monitor, and control derivative activity including mark-to-market information on all open positions by instrument category.

Internal control systems

This section documents the internal control systems. The policy should contain procedures regarding:

- the role of internal audit, frequency of audits and to whom the results are conveyed;
- adequate operational policies that reasonably ensure:
  - Directions, Instructions and the Treasury Policy are not breached;
  - computer systems are appropriate and error free;
  - risks are being regularly identified, measured and evaluated;

- appropriate segregation of duties;
- management policies and directives are being adhered to; and
- reporting of breaches, including defining levels of significant breach, procedures to ensure that breaches are reported appropriately and internal controls amended if required.

The policy should also record the requirement of compliance reporting when significant and systemic breaches of the policy occur, see Direction 5.1.

Reporting and monitoring process

This section includes the frequency and contents of reports to management and the Responsible Body including the reporting of Treasury activities and adherence to dealing limits.

Treasury risks

The following provides further description on the various risks.

Interest rate risk

Interest rate risk is the risk to earnings or capital arising from movements in interest rates. Agency interest rate risk can arise from:

- differences between the timing of interest rate changes and the timing of cash flows;
- resetting of interest rates on Agency's loans or bank deposits; and
- when interest costs fluctuate according to interest rate movements during the life of a loan.

Agencies that borrow should determine their funding and cash flow requirements and also the type of borrowing, its term to maturity and interest rate risk management strategies. Interest rate risk may be mitigated by including a mix of fixed and floating rate debt with a range of maturities in the liability portfolio, and ensuring that new or replacement debt is added in a way that minimises any concentration of maturities or repricing dates.

The limits (shown below) may be a useful guide to Agencies with significant ongoing borrowings in the development of their policies.

Term to maturity	Target (%)	Limits (%)
0 – 1 year*	20	10–30
1 – 4 years	35	20–50
4 – 8 years	35	20–50
8 years and over	10	0–20

* Loans maturing within 12 months and term loans with floating rate resets should be included in the 0 to 1 year period.

Setting of interest rate risk limits may not be appropriate for all Agencies. For example, Agencies that undertake one-off project borrowings may opt to use a TCV 'crédit foncier' style loan, with a term broadly matching the life of the underlying asset and with a rate of interest fixed for the life of the loan.

Some Agencies may hold minimal short-term borrowing facilities for the purposes of liquidity management only, and would therefore not need to adopt the portfolio approach described above.

TCV is available to provide advice and financial products in relation to interest rate risk management.

Liquidity risk

Liquidity risk is the risk that an Agency does not have sufficient funds available to meet cash outflow commitments or faces a liquidity crisis brought on by unforeseen events. Liquidity risk consists of two main elements:

- funds risk; and
- transaction risk.

Funds risk is the risk that the Agency will not be able to meet its obligations as they fall due. This is a cash flow risk and it is managed by ensuring that adequate funds of the correct currency are available in the right places at the right time. Regular forecasts of future cash flows should be prepared to monitor future funding requirements.

Transaction risk is the risk that losses will arise from being exposed to an illiquid market. This ties very closely to market risk. If market rates become more volatile, transaction risk increases for the Agency if it tries to sell or buy in the market.

Under the Government's centralised Treasury model, Agencies that borrow are responsible for managing the funds risk. TCV is responsible for managing the transaction risk and ensuring that funding lines are always available to borrowers. Agencies should focus on managing liquidity risk through careful cash flow forecasting and developing an appropriate maturity profile to manage refinancing. Agencies are ultimately responsible for the management of liquidity risk.

Foreign exchange risk

Foreign exchange risk is a risk to operating result and or capital due to a change in foreign exchange rates. For Agencies, foreign exchange risk mainly arises:

- when a cash payment or receipt is denominated in a foreign currency; or
- an Australian dollar cash payment or receipt is determined by a foreign currency amount converted to Australian dollars at an exchange rate prevailing at some future date.

Exposure to changing foreign exchange rates often arises indirectly in the normal course of business. It may occur when purchasing products from a foreign supplier and a fall in the value of the Australian dollar may reduce the operating margin. In some instances the foreign currency exposure may be embedded in the terms of a contract, such as an agreement to purchase goods from an offshore supplier. To assist Agencies to determine exposures, it is important to consider the likely amount and timing and the degree of certainty attached to both.

Foreign exchange hedging is the process of 'locking in today' the exchange rate for a transaction that will take place at some future date. Hedging is a means of protecting against exchange rate uncertainty. An Agency will be able to buy or sell at an agreed price, regardless of how the actual exchange rate changes. Hedging protects against adverse exchange rate changes but also excludes any benefit arising from favourable movements. The most common instrument used to hedge foreign exchange currency exposures is a forward foreign exchange contract (see example below). With a forward foreign exchange contract a foreign exchange rate for any future date can be set today. When the future date arrives, the foreign exchange transaction is settled based on the agreed exchange rate regardless of where the actual exchange rate is on settlement day. These contracts and other foreign exchange risk management products can be provided by TCV.

Foreign exchange example

On 30 August, an Agency signs a contract to buy some medical equipment from a supplier in Germany for EUR 1 million, with an agreed payment date of September 30. If the current one month forward exchange rate is 0.75, the cost of the equipment in Australian dollars is $1.3 million. In this example the exposure is in excess of AUD $1 million and the amount and timing are certain, consequently the exposure is required to be hedged with TCV. If the Agency does not hedge and the exchange rate on September 30 is 0.71, it will cost the Agency AUD $1.4 million to purchase the equipment.

The most significant currency exposures faced by Agencies are cash flow exposures. TCV offers a variety of specific market instruments to manage these exposures, including forward foreign exchange, currency swaps, currency futures and options, which lend themselves readily to transaction exposures.

The Responsible Body should ensure policies and procedures in relation to foreign exchange risk have been developed which identify the foreign exchange exposure and recognise the requirement that these exposures be fully hedged when material. Policies should therefore specifically address how any exposure arising from trade transactions (payables/receivables) is to be managed so as to eliminate foreign exchange risk.

When an Agency purchases goods and services using fixed price state purchase contracts they are reducing their foreign currency and commodity price exposure. This is because the prices are fixed for a period of time, sometimes 3 or more years, and generally should not fluctuate. This includes items purchased under Health Purchasing Victoria contracts and whole of Victorian Government contracts.

There could be a higher exposure to foreign exchange or commodity price risk when an Agency negotiates pricing directly for goods and services with the supplier, for example when an Agency purchases directly from an overseas supplier in an overseas currency.

Commodity price risk

Commodity risk is a risk to operating result or capital due to a change in the price of a commodity that is a key input or output. For example an Agency may be required to purchase fuel. A commodity price risk may arise because the future price of fuel is uncertain. If fuel prices are rising the Agency will have to pay more for fuel and this might reduce the operating margins if the increased prices cannot be recovered.

A Commodity[47] is defined as a tradable item that can generally be further processed and sold; includes industrial (metals such as aluminium), agricultural (wool, wheat, sugar, etc.), and bulk (coal, iron ore) goods. Commodities are important to the Australian economy as they account for the majority of our exports.

Examples of a definition of commodity price risk that could be included in a policy are:

- commodity price risk is the risk that a change in the price of a commodity that is a key input or output of a business will adversely affect its financial performance; and
- commodity price risk is defined as the risk that changes in commodity prices will have an impact on the cost of purchased raw materials and the proceeds received for commodities sold.

Hedging is the process of reducing or removing the price risk associated with a particular exposure. Hedging is a means of protecting against price uncertainty. The most common hedging strategy is to set a future price of a commodity today by using a forward rate contract. These contracts can be provided by TCV along with other risk management products. By using this type of contract an Agency can have certainty today what price it will pay in the future for a commodity. Regardless of how the actual commodity price changes, an Agency will be able to buy at an agreed price. The forward contract protects against price rises but also excludes any benefit arising from falling prices.

Agencies should be aware that many commodities have a foreign exchange component in their AUD pricing.

Credit risk

Credit risk is the risk that another party in a transaction will fail to meet its financial obligations. Credit risk may include:

- counterparty risk, which is the risk that the other party to a transaction will not meet its obligations as to timing or amount of settlement;
- country/political/sovereign risk associated with government directives and policies that may affect the contractual performance of either party to the transaction, and that are generally beyond the direct control of the counterparty; and
- settlement or delivery risk that may exist if there is a default in a single settlement or delivery, in which case all other exposures or positions with that counterparty will be closed out, thus establishing claims for transaction costs.

Credit risk is mitigated if investments are through TCV and VFMC as they are responsible for monitoring and managing counterparty risk. TCV and VFMC are also prudentially supervised by DTF. Policies in relation to credit risk should therefore be focused on non-TCV investments and non-financial market transactions.

Treasury operational risk

Treasury operational risk is the risk of losing money as a result of failures in systems, people or procedures in a given market. The focus of operational risk management in a Treasury Policy relates to the roles and responsibilities of staff employed in the Treasury function and the related systems. Financial loss can occur in the Treasury function due to mismanagement, error, fraud, omission, theft, unauthorised use of techniques and/or financial products, or inadequate information systems. Operational risks are managed by having an adequate control framework in place which limits authority, establishes supervision and separates sensitive duties. The management approach to operational risk should be to clearly define the roles and responsibilities of staff employed in the Treasury section. The management of operational risk in the Treasury function should be consistent with overall operational risk management and policies.

[47] From Australian dictionary of investment terms.

Investment risk

Investment risk is a risk to the operating result or capital from an adverse movement in the value of investment assets. A primary consideration for Agencies that invest is capital preservation. All amounts invested through TCV are guaranteed by the State. Should an Agency be holding surplus investments for a period of time pending future capital works or projects are encouraged to invest funds to match future cash flows. A specific investment policy is required for Agencies investing with VFMC or in long-term or other high-risk assets such as equities and managed funds.

Investment policy statement

An Investment policy statement sets out the framework for managing the Agency's long-term or other high-risk investments. This is only applicable to Agencies with ongoing surplus investments.

The statement should document the Agency's investment policy and the approach taken in managing its investments. Although the statement will vary across Agencies in its detail, there is similarity in the general content to be included. The proposed content of the statement is described below. An example of an Investment Policy Statement is available in Attachment B.

Introduction and overview

This section covers:

- purpose of the Investment Policy Statement;
- scope of the Investment Policy Statement;
- reference to policies or documents relevant to the investment management function, such as investment powers in legislation and policies concerning prudent investment and financial risk management practices; and
- description of the position responsible for maintaining and approving the Investment Policy Statement, the process for review and amending the policy and the frequency of review of policy.

Investment objectives and strategies

This section outlines the investment objectives established by the Responsible Body for returns and risk that form the basis of its investment strategy and support the Agency maintaining long-term investments.

Investment objectives should be set by the Responsible Body in consultation with VFMC and be consistent with the objectives of the Agency's corporate plan.

An investment strategy refers to the types of investments permitted in a portfolio and the conditions under which those investments can be varied.

Roles and responsibilities

The Statement commonly contains information regarding the roles and responsibilities of the parties involved in the management, control and reporting of the investment function. The parties may be some or all of the following:

- Responsible Body;
- Accountable Officer;
- Chief Finance Officer;
- Investment Committee;
- Investment Manager; and
- external consultants.

Delegation of authority

It should include details of what transactions and functions are delegated, to whom, who should authorise various transactions or functions, and what financial or other limits should apply. Refer to Direction 3.3 for requirements.

Investment risks

For each investment risk, it is important to provide details of the risk, recognition, measurement, timing and objectives of risk management. Below are some of the key investment risks:

- **liquidity risk:** The risk that the Agency cannot satisfy its day to day cash flow commitments;
- **inflation risk:** The risk that investment values fail to match inflation in the long-run;
- **interest rate risk:** The risk that falling rates lower the earnings on cash or fixed interest securities; and
- **operational risk:** The risk of an investment loss resulting from management error or fraud.

Where an Agency invests through VFMC, VFMC will take measures to manage some investment risks on their behalf. These investment risks include:

- **market risk:** The risk that prices and yields across many markets fall in response to expectations of declining general economic conditions;
- **credit risk:** The risk that a security issuer or other counterparty may fail to repay some or all of an investment;
- **selection risk:** The risk of poor portfolio performance due to poor asset selection; and
- **concentration risk:** The risk that there is insufficient diversification between investments, investment issuers, fund managers or other characteristics which may lead to an Agency being exposed to a single economic event.

Other risks

This section documents additional risks a long-term investor may be subject to, such as those listed in 'Treasury risks' above, and are not listed in the previous section. When these risks arise, they should be addressed in either a separate Treasury Policy or be included in the Investment Policy Statement.

External investment advisors and fund managers

Government policy is for investments to be directed through VFMC as VFMC will take measures to manage some investment risk and is prudentially supervised by DTF. When the Agency chooses to invest outside VFMC, this section documents the policies regarding the engagement, performance management and retention of external investment advisors/managers.

Some criteria against which to assess potential fund managers should include:

- expertise, skills and knowledge of the personnel in the organisation;
- risk profile adopted by the manager and the investment products offered;
- investment style of the manager including the personnel involved in the decision making process;
- fee structure;
- corporate strength;
- past performance; and
- the level of funds under management.

The Agency is responsible for ensuring that investments managed by an external manager on its behalf are invested consistent with its investment powers, objectives and strategies.

Internal control systems

The nature and extent of the control environment is driven by the type and value of the investments. The statement should prescribe an appropriate internal control environment that includes the following features:

- a clear definition of the role of Internal Audit, the frequency of audits and to whom the results are conveyed;
- adequate operational policies that reasonably ensure that:
  - *Directions*, *Instructions* and the *Investment Policy Statement* are not breached and that DTF should be contacted verbally and in writing of any breaches;
  - risks are being identified, measured and evaluated regularly;
  - adequate segregation of duties to ensure that the risk of error or fraud in the investment management process is minimised, and there is an enhanced probability for the discovery of error or fraud; and
  - management policies and Directions are being adhered to;
- robust investment processes and compliance structures are in place; and
- accounting and information systems are appropriate to task and error free.

Permitted investment list

The Responsible Body may wish to provide further limits on approved investments when prudent. The aim of including such a list in the Statement is to ensure that employees are explicitly aware of the investment products and arrangements that may be undertaken, and those not permitted.

Reporting and monitoring process

It is common for the Responsible Body to receive a detailed investment report on a quarterly basis and summary investment data on a monthly basis. Agencies investing through VFMC will receive comprehensive reporting on a monthly, quarterly, and annual basis. More frequent investment reporting may be necessary when the investment environment or operational circumstances dictate that this would be prudent. Reporting requirements could include a comparison of investment performance against relevant benchmarks.

Definition

A **credit foncier loan** is a medium to long-term loan with fixed regular payments of principal and interest. TCV is able to structure these loans whereby the repayment arrangements match the specific cash flow requirements of clients. The repayment frequency for credit foncier loans can be monthly, quarterly or semi-annual.

Other relevant information

Queries in relation to this material, should be directed to:

Director, Financial Assets and Liabilities
Department of Treasury and Finance
Level 5, 1 Treasury Place
EAST MELBOURNE VIC 3002
Tel: 03 9651 5305
Fax: 03 9651 2321

Attachment A: Treasury Policy example

1. Sample Treasury Policy

This sample policy is based on a Public Sector Agency involved in borrowing, investing and financial arrangement activities. This sample can be modified for use by any Public Sector Agency by deleting areas not applicable to their operations and adding based on their specific treasury functions.

Public Sector Agency [ABC]
Treasury Policy
June 2015

1.1 Purpose

The purpose of this treasury policy is to provide a framework for the management of the treasury operation of [ABC]. Specifically this involves the relationship between [ABC], TCV, DTF , Portfolio Department and private financial institutions.

The purpose of this treasury policy is to ensure a prudent and efficient approach to financial risk management. This will be achieved through the monitoring, reporting and management of the following:

- interest rate risk associated with borrowing and investment activities;
- counterparty risk attached to transacting with financial markets;
- liquidity risk associated with maintaining an adequate cash flow position to meet ongoing funding requirements;
- any material foreign exchange risk as and when it arises; and
- operational risk within the treasury operation itself.

1.2 Scope

This policy covers the use and maintenance of borrowings, financial arrangements, and cash and interest-earning investments held by [ABC].

This treasury policy will apply to all:

- borrowings;
- financial arrangements for managing interest rate and foreign exchange risk; and
- cash holdings including transactional bank accounts and at call/11am funds plus interest-earning investments generally such as term deposits.

1.3 Other relevant documents

This document should be read in conjunction with the following legislation as it applies to the operations of [insert Public Sector Agency name]:

- *Borrowing and Investment Powers Act 1987;*
- *Treasury Corporation of Victoria Act 1992;*
- *Audit Act 1994*; and
- governing legislation (if any).

Other State government policy material relevant to the operation of the treasury function of [ABC] include the following:

- borrowing, investments and financial arrangement Direction, Instruction and Guidance; and
- …

Other internal policy materials relevant to the operation of the treasury function of [ABC] include the following:

- ...; and
- …

1.4 Maintenance of the treasury policy

[insert responsible person's name] is responsible for maintaining and supervising compliance with this treasury policy. The policy and all amendments must be approved by the Board. The policy is reviewed annually.

2. Financial objectives and strategies

2.1 Financial objectives

The financial and treasury management objectives of [ABC] are as follows:

- to manage liquidity needs on a daily and longer term basis and meet cash flow commitments when they fall due;
- to practice efficient cash management and maintain the minimum required cash balances in transactional bank accounts;
- to determine accurate annual borrowing requirements for inclusion in the budget feeds based on corporate plans and forecast capital expenditure;
- to ensure financial risks and treasury management exposures are identified, quantified, planned and managed; and
- to safeguard financial resources by allocating appropriate resources, internal controls and oversight of the corporate treasury function.

2.2 Financial strategy

The financial strategies employed to achieve these treasury management strategies are as follows:

- to undertake regular cash flow forecasts and to meet all cash flow commitments when they fall due;
- where there are borrowings outstanding, to use any surplus funds to retire debt as a first priority;
- to maintain any surplus cash balances not required to retire debt in an at call facility with TCV;
- to maintain an actuarially determined percentage of surplus cash balances in term deposit products with TCV;
- to keep floating rate debt to a minimum, unless there are offsetting sensitivities in revenue;
- to maintain the following debt portfolio composition in consultation with TCV:

Term to maturity	Target (%)	Limits (%)
0 – 1 year*	20	10–30
1 – 4 years	35	20–50
4 – 8 years	35	20–50
8 years and over	10	0–20

* Loans maturing within 12 months and term loans with floating rate resets should be included in the 0 to 1 year period.

- to actively manage refinancing risk for large fixed rate loans through obtaining appropriate financial arrangements through TCV;
- preparing regular cash forecasts to effectively monitor future funding requirements and minimise liquidity risk;
- to liaise with TCV to ensure that access to credit lines is available to meet any unexpected funding requirements;
- to prohibit speculative position taking, and only enter into financial arrangements for hedging/risk management purposes;

- to undertake all borrowings, financial arrangements and cash investments through TCV to mitigate any foreign currency or credit/counterparty risk;
- to undertake an annual internal audit of the treasury management function, and undertake treasury management operations predominantly through TCV to manage operational risk;
- to operate at all times within the Board approved treasury policy; and
- maintain the highest standards of professional conduct and ethical dealing in the management of the treasury function.

3. Roles and responsibilities

Responsibility for the management and control of financial risks faced by [insert Public Sector Agency name] rests with the Accountable Officer and involves the following parties:

- the Responsible Body (Board);
- Audit Committee;
- the Chief Finance Officer (CFO); and
- Treasury Manager/Financial Accountant.

3.1 The Board

The Board must:

- approve this treasury policy and all amendments and ensure the policy is complied with;
- approve all borrowings, investments and risk management products;
- receive at least quarterly treasury reports from management concerning borrowings, financial arrangements and cash investments. The Board may request more regular reporting if this would be prudent or otherwise desirable; and
- approve all relevant delegations and dealer limits in operation within the Treasury function.

3.2 Audit Committee

The Audit committee:

- is responsible for endorsing the overall financial risk management strategy of [insert Public Sector Agency name].
- should receive regular internal audit reports concerning Treasury operations and providing the results to the Board on at least an annual basis.
- may direct the internal auditor to investigate the Treasury operation of [insert Public Sector Agency name] on a more regular basis if it has reason to believe there has been a significant breach of this treasury policy.

3.3 Chief Finance Officer

The CFO:

- is responsible for overseeing and monitoring the management of the treasury function in accordance with this treasury policy and related legislation.
- must make available the approved policy to [Portfolio Department X] and DTF upon request.
- must make recommendations to the Board concerning delegations and responsibilities within the treasury function.
- may recommend amendments to the treasury policy for Board approval.
- has authority to liaise with TCV concerning any investment or borrowing within the restrictions of any dealer limit of delegation prescribed by this treasury policy.
- is responsible for reviewing and signing off on all treasury reports before they are presented to the Board.

3.4 Financial Accountant/Treasury Manager

The Financial Accountant will act as Treasury Manager and is delegated responsibility to liaise with TCV concerning the execution of the treasury strategies contained in the treasury policy.

The Treasury Manager:

- is responsible for operating and administering the treasury function including relevant forecasting, correspondence, accounting and reporting functions.
- is responsible for identifying any emerging financial risks and developing appropriate financial risk management strategies for approval by the CFO and Board.
- may liaise with TCV in relation to cash investment or borrowings within restrictions of any dealer limits or delegations provided in this document.
- is not authorised to liaise with TCV concerning entering into or performing financial arrangements.
- is responsible for providing quarterly treasury reports to the CFO and the Board.
- is responsible for assisting the CFO concerning any amendments to this treasury policy.

4. Delegations (these may also be attached to the policy in a table)

- All borrowings, financial arrangements or investments of greater than $xx million must be authorised by the Board and transacted by the CFO.
- The CFO is approved to authorise financial arrangements on behalf of [ABC]. This delegation is granted up to the value of $xx million, and must be transacted by the Treasury Manager.
- The CFO is approved to authorise cash investments with TCV on behalf of [insert Public Sector Agency name] in amounts greater than $x million but less than $xx million. These investments must be transacted by the Treasury Manager.
- The CFO is approved to authorise financial accommodation from TCV on behalf of [insert Public Sector Agency name] in amounts greater than $x million but less than $xx million. These borrowings must be transacted by the Treasury Manager.
- The Treasury Manager may place investments with TCV on behalf of [insert Public Sector Agency name] up to a limit of $x million. These investments must be transacted by an accountant within the treasury function reporting directly to the Treasury Manager.
- The Treasury Manager may obtain financial accommodation on behalf of [insert Public Sector Agency name] from TCV in amounts less than $x million. These borrowings must be transacted by an accountant within the treasury function reporting directly to the Treasury Manager.

5. Financial risk recognition and management

5.1 Interest rate risk

Interest rate risk is the risk that the organisation will suffer a financial or economic loss due to adverse movements in interest rates.

Interest rate risk will arise where:

- there is a cash surplus or deficit that needs to be managed;
- borrowing or investments mature;
- an interest repricing occurs on a borrowing, investment or financial arrangement;
- there are new borrowings; or

[insert Public Sector Agency name] predominantly manages interest rate risk by:

- keeping floating rate debt to a minimum and adhering to the debt portfolio maturity profile contained in the financial strategy section (2.2) of this policy;
- performing extensive corporate planning activity that monitors future capital expenditure requirements and how this will affect the portfolio structure; and
- where a large fixed interest rate loan is due to be refinanced, contacting TCV to arrange for appropriate risk management products to be put in place before this event occurs.

5.2 Liquidity risk

Liquidity risk is the risk that an unforseen event or miscalculation in the required funding level will result in insufficient funds when commitments fall due., This could result in excessive borrowing costs or lower interest income.

Liquidity risk is managed by performing regular cash forecasts, monitoring the life cycle and replacement time of plant and equipment, liability profile, business sensitivities to macroeconomic variables and maintaining access to credit lines through TCV. Liquidity risk is also managed by ensuring accurate estimates are provided for the annual borrowing approval process.

Short-term liquidity management is ensured through a combination of effective daily bank account and cash management to ensure funds are available on demand.

Long-term liquidity management is managed through ensuring appropriate funding facilities are in place with TCV to meet all long-term funding requirements. Long-term liquidity management is achieved through monitoring the maturity profile of borrowings, and through TCV ensuring access to financial markets.

Investments are limited to highly liquid cash investments provided by TCV to ensure funding flexibility.

5.3 Foreign exchange risk

Foreign exchange risk is the risk that [ABC] will suffer financial loss due to adverse movements in foreign exchange rates.

A material foreign currency exposure to [ABC] is a financial exposure in excess of $100 000. [ABC] is exposed to forex risk when purchasing equipment from foreign suppliers. Where a material foreign currency risk arises these must be fully hedged using an appropriate risk management product obtained from TCV.

5.4 Commodity price risk

Commodity risk is a risk to operating result or capital due to a change in the price of a commodity that is a key input or output. Public Sector Agency x is not exposed to commodity price risk.

5.5 Credit risk

Credit risk is the risk that [ABC] will suffer financial loss due to the inability of a customer or counterparty to meet its financial obligations in full and on time. [ABC] faces credit risk in the following areas:

- investments;
- performance guarantees;
- supplier contracts; and
- customer ability to meet contractual commitments.

Credit risk is reduced by maintaining all borrowings, financial arrangements and cash investments in excess of $2 million with TCV and through using the Westpac government banking contract for all other banking needs.

[ABC] only accepts performance guarantees from issuers with a minimum credit rating of A- and avoids concentration risk through maintaining a register of issuers.

The Supply Manager maintains a list of all counterparties which is reviewed annually. The Supply Manager monitors the ability of all suppliers and customers to meet their contractual obligations when they fall due.

5.6 Treasury operational risk

Operational risk is the risk that [ABC] will suffer loss due to the mismanagement of the treasury function. These may include risks of financial loss due to error, fraud or unauthorised dealing or use of financial products.

- Operational risk is monitored and controlled through the following risk management practices:
- regular performance of internal and external audit;
- the execution of treasury management operations and financial strategy through TCV;
- abiding by the treasury management procedures and policies outlined in this treasury policy;
- appropriate organisational structure and resourcing within the treasury function;
- ongoing training and staff development opportunities;
- fully documented dealing and authorisation limits;
- effective reporting of treasury operations and any breaches to management and the Board; and
- measures to protect the integrity of information systems including security, backup and disaster recovery of treasury and information systems.

5.7 Investment risk

[ABC] is not normally exposed to investment interest rate risk as it uses all surplus funds to reduce borrowings.

From time to time [ABC] may have excess cash pending future capital works. These funds are invested with TCV for a period matching the timing of the project expenditure. [ABC] obtains forecast interest rates from TCV and these rates are used in forecasts and budgets to reduce investment interest rate risk exposure.

6. Approved financial instruments

6.1 Approved borrowing products

Management and staff are permitted to use the following TCV borrowing products:

- short term loans including 11:00am loans;
- term floating rate loans;
- fixed rate loans; and
- forward settlement loans.

6.2 Approved investment products

Management and staff are permitted to use the following TCV and Westpac investment products

- 11:00am cash deposits;
- term deposits;
- fixed interest deposits;
- floating rate deposits; and
- guaranteed bill index deposits.

6.3 Approved financial arrangement products

Management and staff are permitted to use the following TCV investment products

- forward settlement loans; and
- spot foreign exchange rate contracts.

6.4 Maximum amount per transaction

Delegations in section 4 provide details concerning the maximum value of borrowings allowed according to role.

6.5 Approved counterparties

TCV is the only approved counterparty for borrowings and financial arrangements. Investments products are provided by TCV and Authorised Deposit Taking Institutions (ADIs) in accordance with the Standing Directions of the Minister for Finance. If TCV cannot provide the required financial product then approval is required from the Board, the relevant Minister and Treasurer to operate outside the centralised framework.

7. Use of financial arrangements (derivatives)

To manage refinancing risk for large fixed rate loans as they approach maturity TCV may be engaged to provide financial arrangements. In this case, TCV should be requested to provide appropriate financial arrangements (derivatives) to manage refinancing risk.

In the event of a material foreign exchange exposure, TCV may be approached to provide risk management products to mitigate this risk.

Financial arrangements may be requested by the CFO where the exposure in question is less than $xx million. For exposures of $xx million or greater the Board must approve the granting of any financial arrangement/risk management product from TCV.

Any financial arrangement entered into by [ABC]:

- must be designated as a hedge at the time of entering into the arrangement;
- the risk exposure must not already be effectively hedged by an off-setting risk;
- must contribute to the reduction of exposure to financial risk;
- must not be entered for the purposes of leveraging a transaction; and
- trading activities in the context of transacting to create new or additional exposures are not permitted.

Treasurer's approval must be sought prior to entering into financial arrangements.

Where financial arrangements are in use, management must report to the Board concerning measurement, monitoring and control of derivative activity including mark-to-market information on all open positions by instrument category.

8. Internal controls and systems

8.1 Internal audit

Internal audit will be carried out by [Accounting Firm X] in accordance with the Internal Audit Direction 3.2.2 and internal audit plan. Internal audit reports for the Treasury function will be conducted on at least an annual basis, and more regularly at the request of the Audit Committee. The internal audit report will be provided to the Audit Committee for their consideration. The Audit Committee reserves the right to perform engage additional audit activity at any time should it be required.

8.2 Operational policies

Management and staff must comply with the requirements of the Direction and relevant Instructions and other materials at all times.

Management and staff must comply with the terms of this treasury policy in the conduct of the treasury function of [ABC].

Management and staff must ensure that computer systems, including accounting software and communications systems are capable of supporting the treasury management function at all times.

Management, including the Accountable Officer and the CFO are responsible for ensuring systems are in place to identify, measure and evaluate potential financial risks as and when they eventuate. Management should frequently review the risk environment of the Public Sector Agency, and update the treasury policy as required.

The Board is responsible for ensuring that management policies and directions, including this treasury policy, are being adhered to by management and staff.

8.3 Breach reporting

Management should ensure that the Board become aware of any breach or potential breach of this policy, if and when this breach becomes apparent.

All breaches of this policy should be recorded in an attachment to this Treasury Policy to ensure that breaches are reviewed and not repeated. Significant and or Systemic breaches are reported in accordance with the Standing Directions of the Minister for Finance – Compliance and Reporting Direction.

9. Reporting to Board and management

Management must report to the Board on monthly basis concerning the treasury operations and financial risks of [ABC].

Treasury reports provided to the Board should detail the following information:

- borrowing levels and how these are tracking against annual borrowing limits approved by the Treasurer and planned capital expenditure detailed in the corporate plan and annual budget feeds;
- the status of financial risks faced by [ABC] and any material changes to these risks along with proposed mitigation strategies;
- any likely unplanned capital expenditure requirements and whether these will require increasing the Treasurer's approved borrowing limit for the financial year;
- cash forecasts concerning the timing of upcoming cash flows, a detailed consideration of the application of any surplus cash, and details concerning the required composition of cash balances in transactional, at call and term deposit products;
- the report should also cover adherence to dealer limits and delegations as set out in this treasury policy document;
- general details of treasury transactional activities;
- details of portfolio composition and position;
- strategic planning issues;
- a record of performance against measures;
- exceptions or breaches to Board approved policy;
- operational issues; and
- a report concerning the measurement, monitoring and control financial arrangements outstanding including mark-to-market information concerning all open positions.

Internal audit reports provided to the Audit Committee should include:

- a summary of financial risk management activity;
- an overview of portfolio composition and position;
- strategic action plans;
- performance overview of treasury function; and
- any exceptions or breaches to the Board approved Treasury Policy.

Attachment B: Investment Policy Statement example

Sample Investment Policy statement

Public Sector Agency [ABC]

Investment Policy statement

June 2015

In this example, the entity [ABC] maintains cash and short term deposits with TCV and a longer term investment portfolio with VFMC via one or more of its three funds.

1. Introduction and overview

1.1 Purpose

The purpose of this Investment Policy Statement is to provide a framework for the investment management function of [ABC]. This includes the relationship between [ABC], VFMC, TCV, DTF and approved private financial institutions and advisers specified in this document.

1.2 Scope

This Investment Policy Statement and the guidelines within it apply to all:

- investments held with VFMC and TCV; and
- any other investments approved by the relevant Minister and the Treasurer as suitable for use by [ABC].

1.3 Other relevant documents

This document should be read in conjunction with the following legislation as it applies to the operations of [insert Public Body name]:

- *Borrowing and Investment Powers Act 1987* and Orders in Council re approved manner of investments;
- establishing legislation;
- *Treasury Corporation of Victoria Act 1992*;
- *Victorian Funds Management Corporation Act 1994*; and
- *Audit Act 1994*.

Other State government policy material relevant to the operation of the treasury and investment function of [ABC] including the following:

- borrowing, investments and financial arrangement Direction, Instruction and Guidance; and
- Treasury and investment risk management Direction, Instruction and Guidance.

1.4 Maintenance of the Investment Policy Statement

The Chief Finance Officer (CFO) is responsible for maintaining and supervising compliance with this Investment Policy Statement. The Policy and any amendments must be approved by the Board. Following Board approval of this Investment Policy Statement, it must be available to the [Portfolio Department X] and DTF for review upon request. The Policy will be reviewed by [ABC] at least annually.

2. Investment objectives

The investment objectives of [ABC] are as follows:

- **return**: To maintain a return objective of [e.g. CPI +3.0%] for surplus funds over a [e.g. rolling five-year] period; and
- **risk**: e.g. to limit the likelihood of a negative return to no more than one year in every seven years.

3. Investment strategy

The investment strategy to achieve the objectives is to:

- invest with VFMC in its Balanced, Growth, and/or Capital Stable funds ;
- invest with TCV in term deposits to cover medium term cash flow requirements; and
- hold cash with TCV to cover short-term liquidity requirements.

4. Roles and responsibilities

Responsibility for the management and control of investment related financial risks faced by [insert Public Sector Agency name] rests with the Accountable Officer and involves the following parties:

Responsibility for the management and control of investment related financial risks of [ABC] resides with the following officers:

- The Responsible Body (Board);
- The Chief Finance Officer; and
- Finance/Investment Manager.

4.1 The Board

The Board is responsible for overseeing the management of the investments. The specific roles and responsibilities of the Board with respect to investment management are to:

- ensure that [ABC] has an Investment Policy Statement which is being complied with;
- set the investment objectives for [ABC];
- approve the investment strategy and its execution;
- approve the use of any financial arrangements to manage investment related financial risks;
- approve any delegations of responsibility within the investment management function;
- receive and consider investment reports prepared by TCV and VFMC, management and any external advisors at least quarterly; and
- review the investment objectives, strategies and Investment Policy Statement at least annually.

4.2 Chief Finance Officer

The Chief Finance Officer (CFO) is responsible for overseeing (on behalf of the Accountable Officer/CEO) the management of the investment function in accordance with this Investment Policy Statement and related legislation. Specific responsibilities of the CFO are to:

- monitor the activities of, and take responsibility for the operation of the investment management function;
- make recommendations to the Board concerning delegations and responsibilities within the investment function;
- recommend amendments to the Investment Policy Statement for Board approval;
- liaise with TCV and VFMC concerning the execution of the investment strategy within the limits and delegations prescribed by this Investment Policy Statement;
- liaise with TCV and VFMC to enter into and perform any financial arrangements that are authorised by the Board within the limits and delegations prescribed by this Investment Policy Statement; and
- review and sign off on regular investment reports before they are presented to the Board.

4.3 Finance Manager/Investment Manager

The Finance Manager will act as Investment Manager and is responsible for operating and administering the investment function including relevant forecasting, correspondence, accounting and reporting duties.

The Investment Manager:

- is responsible for implementing the financial risk management strategy of the investment function in coordination with the CFO and authorising transactions within Board approved dealer limits and delegations.
- is not authorised to liaise with VFMC or TCV concerning entering into or performing financial arrangements.
- in coordination with VFMC, is responsible for providing investment reports to the CFO and the Board.

5. Delegations

These include:

- The Board must approve of any change in the investment objectives or strategy of [ABC].
- All investments of greater than $XX million must be authorised by the Board and transacted by the CFO. All portfolio investment services must be provided by VFMC or TCV.
- The CFO is approved to authorise investments with VFMC or TCV on behalf of [insert Public Body name] in amounts greater than $xx million but less than $xx million. These investments must be transacted by the Investment Manager.
- The Investment Manager may place investments with VFMC or TCV on behalf of [ABC] up to a limit of $xx million.

6. Investment risks

In seeking to achieve the investment objectives in this Investment Policy Statement the Board acknowledges that risks are being taken in order to achieve investment returns above the risk free rate of return. Risks accepted in order to achieve the investment objective include the following:

6.1 Liquidity risk

Liquidity risk is the risk that [ABC] cannot satisfy its day to day cash flow commitments when they fall due. Liquidity risk has been managed by investing a proportion of funds in highly liquid asset classes through TCV, and/or maintaining a proportion of liquid investments with VFMC.

6.2 Credit risk

Credit risk is the risk that a Public Body will suffer financial loss due to the inability of a counterparty to meet its financial obligations in full and on time. Credit risk is reduced by maintaining all investments with TCV and VFMC.

6.3 Inflation risk

Inflation risk is the risk that investment performance fails to match long-term inflation. This risk has been managed by maintaining a strategic allocation toward long-term growth assets in the form of the [VFMC X Fund].

6.4 Interest rate risk

Interest rate risk is the risk that falling rates lower the earnings on cash or fixed interest securities. This risk has been managed by maintaining allocation in long-term growth assets in the form of the [VFMC X Fund].

6.5 Market risk

Market risk is the financial risk associated with macroeconomic factors impacting upon portfolio performance. VFMC is responsible for managing market risk on behalf of [ABC] through investing in a balanced portfolio of financial assets.

6.6 Selection risk

Selection risk is the risk associated with poor portfolio performance due to poor asset selection. VFMC is charged with managing selection risk on behalf of [ABC]

6.7 Concentration risk

Concentration risk is the risk of inadequate portfolio diversification and disproportionate exposure to a specific financial risk or adverse economic event. Concentration risk is managed by maintaining a highly liquid investment portfolio, including a balanced growth component allocated between growth and defensive assets. VFMC manages concentration risk on behalf of [ABC].

6.8 Foreign exchange risk

Foreign exchange risk is the risk that [ABC] will suffer financial loss due to adverse movements in foreign exchange rates.

A material foreign currency exposure is a financial exposure in excess of $xx. All investments are undertaken through VFMC which maintains hedging arrangements for foreign exchange exposures. All fixed income products obtained from TCV are denominated in Australian dollars and do not expose the organisation to foreign exchange risk.

6.9 Operational risk

Operational risk is the risk that a Public Body will suffer loss owing to the mismanagement of the investment function. These may include risks of financial loss due to error, fraud or unauthorised dealing or use of financial products.

Operational risk is monitored and controlled through the following risk management practices:

- oversight by management and the board of directors;
- regular internal and external audits;
- the execution of investment strategy through VFMC and TCV;
- adherence to the investment management policies and procedures outlined in this Investment Policy Statement, including fully documented dealing and authorisation limits;
- appropriate organisational structure and resourcing within the investment function;
- effective reporting of investment operations to management and the Board; and
- measures to protect the integrity of information systems including security, backup, and disaster recovery of treasury and information systems.

7. Permitted investment list

7.1 Approved financial products

[Insert Public Body name] is permitted to invest in the following investment products offered by TCV and VFMC subject to the dealer limits and delegations provided by this Investment Policy Statement:

- VFMC balanced, growth and stable funds;
- TCV 11 am cash deposits;
- TCV term deposits;
- TCV structured deposits;
- TCV guarantee bill index deposits;
- TCV term floating rate deposits;
- TCV fixed interest deposits; and
- TCV protected bill index deposits.

8. Internal controls and systems

8.1 Internal audit

Internal audit will be carried out by [Accounting Firm X] on an annual basis. The internal audit function will be reviewed by the Board and re-tendered on a triennial basis. Internal audit reports will be conducted on at least an annual basis, and more regularly at the request of the Board. The internal audit report will be provided to the Board for their consideration. The Board reserves the right to engage additional audit activity at any time should it be required.

8.2 Operational policies

Management and staff must comply with the requirements of the relevant Directions and Instructions.

Management and staff must comply with the terms of this Investment Policy Statement in the conduct of the investment function of [insert Public Body name].

Management, including the Accountable Officer and the CFO are responsible for ensuring systems are in place to identify, measure and evaluate potential financial risks as and when they eventuate. Management should frequently review the risk environment of the Public Body, and update the Investment Policy Statement as required.

Management and the Board must ensure adequate segregation of duties to minimise the risk of error or fraud in the investment management process and enhance the probability of discovering error or fraud.

The Board is responsible for ensuring that management policies and directions, including this Investment Policy Statement, are being adhered to by management and staff.

8.3 Information systems

Management and staff must ensure that computer systems, including accounting software and communications systems are capable of supporting the investment function at all times.

8.4 Breach reporting

Management must ensure a process is in place to report breaches to the Board of any requirements in this Investment Policy Statement requirement, including procedures to ensure that breaches are appropriately addressed and internal controls amended if required.

All breaches of this policy should be recorded in an attachment to this policy to ensure that the breaches are recorded and not repeated. Significant breaches are reported in accordance with the Compliance and Reporting Direction.

9. Reporting to Board and management

Management should ensure that it reports to the Board on at least a quarterly basis concerning the investment operations and performance of [insert Public Body name].

VFMC will provide comprehensive investment reporting on a monthly, quarterly, and annual basis. More frequent reporting may be prudent in periods of high market volatility.

Quarterly investment reports from management to the Board should contain the following features:

- a regular reporting of portfolio values using the mark-to-market methodology;
- a breakdown of investment performance for each asset class or product including a comparison of performance against relevant benchmarks; and
- a note verifying compliance with the Investment Policy Statement, and all relevant legislation, subordinate legislation, Ministerial Directions and Instructions including the provision of a detailed explanation where any of the above requirements are breached.

Guidance 3.7.2.3 – Borrowings, investments and financial arrangements

Objective	Provides information on: • automatic exceptions contained in Direction 3.7.2.3; • applying for an exemption; • the Treasury Corporation of Victoria and Victorian Funds Management Corporation; • the policy and process for borrowing; and • the Centralised Treasury and Investment Policy.
Effective date	1 July 2016
Relevant Direction	3.7.2.3 Borrowings, investments and financial arrangements
Last reviewed	1 February 2016

Automatic exceptions

Cash on hand

Agencies are automatically able to maintain transactional banking facilities with an Authorised Deposit-Taking Institution (ADI) for operational purposes. There is no limit attached to the funds that an Agency may hold in a transactional banking account. It is in the best interest of Agencies to adopt efficient cash management practices and maintain operational balances to the minimum required level. Transactional bank accounts do not include cash management accounts, 11am deposits, or at call deposits.

Bank overdrafts

Neither TCV or VFMC offer bank overdrafts. However, with the Treasurer's and Responsible Minister's approval, an Agency with a genuine business requirement to operate a bank overdraft may do so with an ADI. Agencies that are part of the annual borrowing cycle may receive a bank overdraft approval based on the previous year's approval as part of the annual borrowing process. Once the Treasurer has approved a bank overdraft, it is automatically exempt from the requirements of Direction 3.7.2.3.

DTF recommends only using overdraft facilities to provide additional working capital to meet unexpected temporary cash requirements during periods of uneven cash flow. It can be an expensive option to use overdraft facilities for medium or long-term financing.

While TCV does not offer a traditional overdraft facility attached to a bank account, it is able to provide a variety of inexpensive short-term funding facilities. Agencies considering entering into an overdraft facility should approach TCV to determine whether it is able to offer a facility that meets the liquidity management needs at a lower cost.

Written requests for obtaining overdraft facilities from ADIs should be forwarded to:

Director, Financial Assets and Liabilities
Department of Treasury and Finance
Level 5, 1 Treasury Place
EAST MELBOURNE VIC 3002

DTF recommends that Agencies who are part of the annual borrowing approval cycle with a need for a different overdraft amount from the previous year should contact DTF by the end of April.

Total investment does not exceed $2 million

Agencies are automatically permitted to maintain investments with an ADI not exceeding $2 million in aggregate. This is in addition to cash on hand in a transactional bank account. These investments include any cash management accounts, 11am deposits, at call deposits, and term deposits.

Exempt trust money

'Exempt trust money' is money held on trust for a known beneficiary (other than for the State or an Agency) pursuant to a statutory function. Consequently, these funds should be sourced from an entity or person external to the State of Victoria, and must be returnable to this source. These funds should be held in a separate trust account.

Examples include:

- funds held in Lawyers' General Trust Accounts and Statutory Deposit Accounts as required by Part 3.3, and 6.7.4 of the *Legal Profession Act 2004*;
- aged care accommodation bonds held by Health Service Providers pursuant to Part 3A.3 of the *Aged Care Act 1997* (Cth); and
- private funds held with State Trustees as executor or trustee as governed by sections 5-9 of the *State Trustees* (State Owned Company) *Act 1994*.

This automatic exemption will not cover funds used in the operating business of the Agency. Donations, gifts and bequests are not automatically classed as exempt trust money. Funds of this nature used in the operating business of the Agency and consolidated into the Whole of State balance sheet are not considered exempt trust money.

Transfer Negotiation Authority and Similar Payroll Arrangements

A Transfer Negotiation Authority (TNA), also known as a Transactional Negotiation Agreement, is an arrangement which guarantees that a client's bank will honour all payroll related instructions from a specialist third party payroll company. TNAs are used by a number of public sector agencies such as hospitals. DTF does not consider a TNA to be a borrowing/overdraft, and therefore no exemption request is necessary if an agency uses a TNA.

Applying for exemption

There is no requirement to apply for an exemption for the exceptions listed above as they are automatic. Further advice on the above exceptions and when seeking an exemption can be obtained from DTF using the following contact details:

Director, Financial Assets and Liabilities
Department of Treasury and Finance
Level 5, 1 Treasury Place
EAST MELBOURNE VIC 3002
Tel: 03 9651 2319
Fax: 03 9651 2321

Information on Treasury Corporation of Victoria and Victorian Funds Management Corporation

Making arrangements with the TCV

Treasury Corporation of Victoria (TCV) was established in 1993 as the centralised treasury for the State. Part of its role is to ensure the State sources funds at the lowest possible cost and to manage associated financial risks. TCV provides borrowings, short-term deposit facilitates and financial arrangements to hedge, protect or manage the value of assets and liabilities. TCV does not offer bank overdrafts or leases.

Under the centralised framework all borrowings, short-term investments, and financial arrangements should be dealt with through TCV. TCV can advise on appropriate funding, hedging and investing structures, taking into account the financial requirements and risk appetite of the Agency. TCV is also able to offer advice in the development of treasury policies and the outsourcing of treasury operations.

Requests for further information concerning TCV's products and services, should be directed to:

Treasury Client Services
Treasury Corporation of Victoria
Level 12, 1 Collins Street
MELBOURNE VIC 3000
Tel: 9911 3636
Email: treasuryclientservices@tcv.vic.gov.au

Making arrangements with the VFMC

The Victorian Funds Management Corporation (VFMC) was established in 1994 as the centralised long-term investment arm for State Agencies. VFMC manages long-term investments, advises and/or implements diversified investment strategies, and executes the associated transactions. When it is clear that an Agency has a long-term investment need, the Agency should approach VFMC directly. Refer to Instruction 3.7.2.2 for requirements to develop an Investment Policy Statement.

Requests for further information concerning VFMC's products and services in relation to the management and execution of investments should be directed to:

Head of Client Services
Victorian Funds Management Corporation
Level 13, 101 Collins Street
MELBOURNE VIC 3000
Tel: 03 9207 2900
Fax: 03 9207 2999

Borrowing approval process

The majority of regular borrowers are public non-financial corporations such as water corporations. They have borrowing powers under the *Borrowing and Investment Powers Act 1987*. Other Agencies also have borrowing powers under their establishing or governing legislation. Agencies can obtain borrowings subject to obtaining the Treasurer's approval of a borrowing limit. TCV will be authorised to lend up to this limit.

Annual borrowing cycle

The borrowing approval framework operates on an annual cycle. The Treasurer approves the borrowing requirements for each Agency for the following financial year. This approval is based on data submitted to DTF via the annual budget process. The Agency borrowing requirements for the forthcoming year should be reflected in its annual budget feeds. Once approved, the Agency is provided with written confirmation of its annual borrowing limits and these limits are provided to TCV.

Borrowing approval process outside of annual cycle

There may be occasions when an Agency borrows on a 'once-off' or project basis outside the annual borrowing cycle, or requires additional borrowings (over and above the borrowing limit approved in the annual cycle). Public Sector Agencies should submit a written request to DTF detailing the amount of additional borrowings with an accompanying explanation or business case if project related.

Written requests for borrowing limits outside of the annual approval cycle should be forwarded to:

Director, Financial Assets and Liabilities
Department of Treasury and Finance
Level 5, 1 Treasury Place
MELBOURNE VIC 3002

Approvals for general government agencies

General government Agencies are not normally given approval to borrow as they are subject to the Expenditure Review Sub-Committee (ERSC) process and funded by Budget Appropriations. General government public sector Agencies permitted to borrow by exception include:

Hospitals

As a result of a previous BERC decision, hospitals may request borrowings for new car park developments when a commercially viable business case has been submitted to DTF for approval. Such borrowings are outside the scope of the annual borrowing cycle, and will require the approval of the Minister for Health, the Minister for Finance and the Treasurer.

School cooperatives

School cooperatives may borrow from TCV to finance school building projects. A business case is required along with support from the Department of Education and Early Childhood Development (DEECD). Further information (only accessible to schools) is contained on the DET intranet.

Finance leases

The *Borrowing and Investment Powers Act 1987* includes finance leases in the definition of financial accommodation or borrowing (see Instruction 3.7.2.3). This Act and most other Victorian legislation require a Public Sector Agency to obtain the Treasurer's approval before obtaining financial accommodation (including finance leases). TCV or VFMC do not offer finance leases. Therefore, when an Agency requests approval from the Treasurer to enter into a finance lease, an exemption to the Direction should also be sought. Agencies entering into finance leases as part of Public Private Partnership (PV) arrangements should also consider obtaining an exemption along with all other relevant approvals as part of the PV framework.

Investments

Investments are defined in the Instruction 3.7.2.3 and include:

- cash and term deposits;
- equity instruments;
- debt securities;
- derivatives;
- certificates of deposit;
- bills of exchange; and
- trust or managed investment scheme funds containing a combination of the above.

Centralised Treasury and Investment Policy

A Centralised Treasury and Investment Policy [48] has been issued by the Treasurer.

The centralised treasury and investment policy creates significant benefits as it:

- provides the capacity to net the State's borrowings and investments prior to approaching financial markets, thus reducing its overall borrowing program;
- creates economies of scale, which reduces execution and administration costs;
- enables the State's overall counterparty risk to be monitored and managed;
- improves prudential oversight of the State's overall borrowings and investments; and
- allows the concentration of appropriate financing and investment expertise, rather than being spread thinly across a range of Agencies.

[48] http://www.dtf.vic.gov.au/Publications/Victoria-Economy-publications/Centralised-treasury-and-investment-policy

Guidance 3.9 – Managing financial information

Objective	Brings together key information and resources for managing financial information.
Effective date	1 July 2016
Relevant Directions	3.4 Internal control system 3.7 Managing risk 3.9 Managing financial information
Last reviewed date	1 February 2016

Direction 3.9 provides that the Agency must apply relevant legislation, standards and policies in relation to its management of financial information, including financial information systems. This captures all forms of financial information and information systems, including documents, digital records and information technology systems.

There is a range of existing frameworks in place in relation to information management by the VPS. Where a framework applies to an Agency, it should be applied to all relevant information, financial and non-financial. However, the Directions emphasise that the proper management of financial information is particularly important.

Significant legislation, standards and policies include those for information management, recordkeeping, privacy and data protection, intellectual property, data sharing and information systems. Each is described in more detail below.

Agencies should note that Direction 3.9 only applies to the extent that particular legislation, standards or policies already apply to an Agency. For example, the *Privacy and Data Protection Act 2014* specifies the Agencies and bodies to which the Act applies. Only Agencies subject to the Act would apply it under Direction 3.9.

Information management

Information management is the way in which an organisation plans, identifies, creates, receives, collects, organises, governs, secures, uses, controls, disseminates, exchanges, maintains, preserves and disposes of its information. It is also the means through which the organisation ensures that the value of that information is identified and exploited.

The Whole of Victorian Government Information Management Principles[49] support the long-term vision for information management in the Victorian Government. They describe expected behaviours and best practice and provide high-level guidance on how information should be managed. They are supported by Standards and Guidelines.

Agencies subject to the Principles must ensure that they are applied in relation to financial information.

More information, and copies of the Principles, are available from www.enterprisesolutions.vic.gov.au/business-systems/information-management/.

Recordkeeping

The *Public Records Act 1973* establishes a framework for the preservation, management and utilisation of public records. The Public Record Office Victoria (PROV) issues and manages more detailed standards for the efficient management of public records under section 12 of the Act. The standards apply to all records created by the Victorian Government and detail requirements for the creation, maintenance and use of these records.

Agencies subject to PROV's standards must ensure that they are applied in relation to financial records. Financial records may include minutes of meetings held by the CFO, documents prepared to discharge financial reporting obligations, accounting records, spreadsheets and emails. PROV's standards impact on access, capture, control, disposal, operations management, storage, and strategic management of financial records.

More information, and copies of the standards, are available from prov.vic.gov.au/government/standards-and-policy.

[49] http://www.enterprisesolutions.vic.gov.au/business-systems/information-management/

Privacy and data protection

The *Privacy and Data Protection Act 2014* (PDPA) regulates three areas of activity:

- Part 3 - Information privacy;
- Part 4 - Protective data security; and
- Part 5 - Law enforcement data security.

The PDPA sets out obligations for the responsible collection and handling of personal information in the Victorian public sector, the establishment of a protective data security regime for the protection of Victorian public sector data, and obligations relating to law enforcement data security. Parts 3, 4 and 5 of the PDPA identify the respective Agencies or bodies to which each part of the Act applies.

The PDPA contains measures that address the protection of financial information, regardless of media or format (for example, soft or hard copy).

Part 3 of the PDPA sets out privacy measures for the protection of personal information held by Agencies or bodies. These privacy protections are embodied in ten Information Privacy Principles (IPPs) set out in the Act, which govern the collection, holding, management, use, disclosure or transfer of personal information by Victorian public sector organisations. Any projects or programs that involve personal information (including personal financial information) should have a Privacy Impact Assessment undertaken to evaluate compliance with the IPPs to identify potential privacy risks and mitigation strategies.

Under Part 4 of the PDPA, the Commissioner for Privacy and Data Protection must develop the Victorian Protective Data Security Framework (VPDSF) for monitoring and assuring the security of public sector data. Public sector data includes all official information (including financial information) that is captured, collected, recorded or generated by an Agency or body. The VPDSF, due for release in 2016, establishes data protection obligations for Agencies or bodies, as well as contracted service providers with direct, or indirect, access to public sector data. The framework sets out mandatory data protection requirements and provides supporting guidance material with respect to Governance, and the protective security domains of information, personnel, information communications technology (ICT), and physical security.

Under the VPDSF, Agencies or bodies will be provided resources to assess the value of information (including financial information) against potential compromise to the confidentiality, integrity or availability of public sector data. The output of this assessment will identify the appropriate security measures to protect that information.

Part 5 of the PDPA establishes law enforcement data security standards for the security and integrity of law enforcement data systems and crime statistics data systems. This extends to the protection of financial information by Victoria Police and the Crime Statistics Agency.

Agencies subject to the PDPA must ensure that the Act, and relevant Standards and Principles, are applied in relation to financial information. The Act and Standards will particularly impact on the confidentiality, integrity and availability of financial information to protect data security.

More information is available from www.cpdp.vic.gov.au.

Intellectual property

The *Whole of Victorian Government Intellectual Property Policy*[50] (IP Policy) is the State's framework for the ownership and management of its intellectual property (IP), and for its use of IP belonging to other parties.

Agencies subject to the IP Policy must ensure that it is applied in relation to financial IP. Financial IP will usually be confined to the copyright in financial works, such as spreadsheets, reports, advices and submissions. The IP Policy impacts on granting rights for re-use, managing IP, moral rights of creators, licensing IP and commercialisation of IP in financial information.

More information, and a copy of the IP Policy, is available from www.dtf.vic.gov.au/intellectual-property.

50 http://www.dtf.vic.gov.au/Victorias-Economy/Victorian-Government-intellectual-property-and-data-policies/Intellectual-Property-Policy

Data sharing

The *DataVic Access Policy*[51] enables the sharing of government data to support research and education, promote innovation, support improvements in productivity and stimulate growth in the Victorian economy.

Agencies subject to the DataVic Access Policy must ensure that it is applied in relation to financial data. Many Agencies hold extensive financial data in various forms. The Policy encourages Agencies to publicly release appropriate data online in re-usable formats.

More information, and a copy of the DataVic Access Policy, is available from www.dtf.vic.gov.au/Victorias-Economy/Victorian-Government-intellectual-property-and-data-policies/DataVic-Access-Policy-and-Guidelines.

Information systems

The Department of Premier and Cabinet's Enterprise Solutions Branch provides strategic guidance, including standards, policies and templates, in relation to VPS management of information systems. Enterprise Solutions defines standards for the procurement of new business systems, plus whole of government policies for ICT and business systems. It develops policies and standards for information management and technology. More information is available from www.enterprisesolutions.vic.gov.au.

Agencies should consider the guidance issued by Enterprise Solutions in relation to their financial information systems.

51 http://www.dtf.vic.gov.au/Victorias-Economy/Victorian-Government-intellectual-property-and-data-policies/DataVic-Access-Policy-and-Guidelines

Guidance 4.1.1 – Planning and managing performance

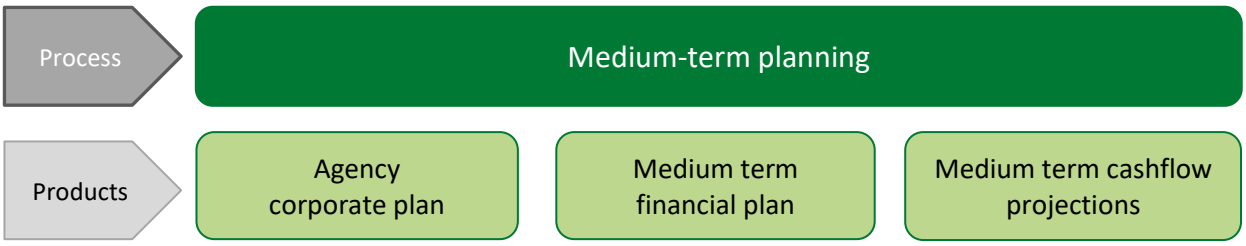
Objective	Provides guidance to all Agencies to support effective planning and performance management practices.
Effective date	1 July 2016
Relevant Directions	2.3 Accountable Officer 4.1 Planning and managing performance 5.3 External reporting and information provision
Last reviewed date	1 February 2016

Analyse and plan: Planning

Analysis and planning are integral components of an Agency's performance management framework and can occur at all levels in the Agency. These processes lead to the documentation of various types of plans ranging from strategic and corporate plans through to operational plans for business units. Refer to guidance in the Strategic Management Framework[52] for the key activities and questions addressed in these elements.

Planning is about creating a vision, making choices to shape the future, and operating in a financially sustainable way. Strategic planning focuses on establishing and continuously reviewing the Agency's purpose, vision and business objectives to ensure these align with the Government's objectives and priorities and the objectives for which the Agency was established. It should drive the Agency's priorities for each budget cycle.

Medium-term planning typically covers a four year horizon. It focuses on the strategies, activities and administrative responses to the vision and objectives to meet agreed service levels, asset delivery and corporate priorities, within available resources and at lowest cost, and in addition, a return on investment for public corporations. A planning horizon greater than four years may be appropriate for significant government programs and for capital planning. The Accountable Officer is responsible for ensuring the proper use and management of the public resources for which the Agency is responsible. General government sector Agencies contribute to the service delivery measures and targets published in the *Departmental Performance Statement* in the State budget papers to support the State's annual appropriation. Some Agencies may consider this as their plan, but medium-term planning should be more comprehensive.

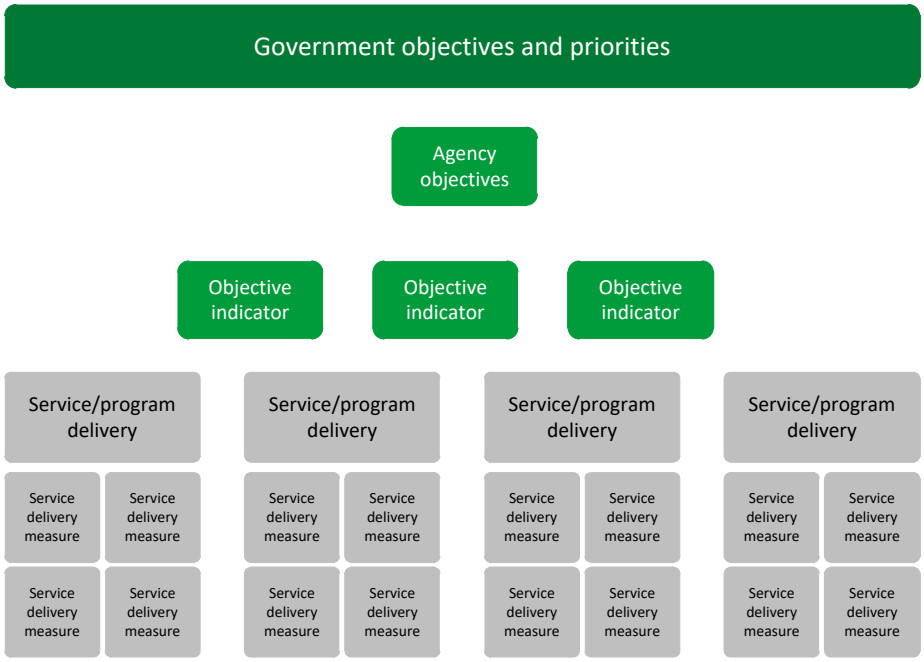


Performance management is central to the effective and efficient delivery of quality services to Victorians. In planning for and managing performance, Agencies describe what they intend to achieve for the community and how the mix of services and/or programs to be delivered is intended to contribute to the achievement of these objectives.

A framework against which Agency performance can be monitored is represented below. It consists of:

- business (Agency) objectives, associated indicators and targets, and
- service delivery, associated measures and targets.

[52] http://www.dtf.vic.gov.au/Publications/Government-Financial-Management-publications/Strategic-Management-Framework



The majority of Agencies are lines of business used by Government to deliver its objectives and priorities. Hence, the Agency's business direction should contribute to the Government's objectives and priorities.

Corporate Plan

The Corporate Plan provides a clear statement of strategic priority of the Agency and forms the basis for managing and reporting performance. Some Agencies already prepare similar plans through their establishing legislation or under a policy requirement.[53] Others may prepare corporate plans to assist in clarifying business goals.

A brief description of the requirements for the Corporate Plan and associated planning activities follows.

(a) Purpose, vision, and desired Agency objectives

In setting the Agency's business direction, it first needs to describe its purpose, vision, objectives and strategies to deliver on these objectives.

Purpose (Mission) specifies the overall aim of the Agency.

Vision indicates what the Agency aspires to be.

Agency objectives describe the effects or impacts an Agency seeks to have on its clients and the community in contributing to Government's objectives and priorities and any legislated business objectives and directions. Objectives help the Agency focus on achievable goals and attain the best possible results from its capabilities. Objectives are typically achieved progressively over a number of years.

Agency objectives should be:

- clear, concise and specific;
- strategic;
- results or impact focused;
- standard focused i.e. what the Agency wants to achieve;
- attributable to the Agency or more broadly to Government; and
- measurable/verifiable and achievable in the medium-term.

[53] Government Business Enterprises are subject to corporate planning requirements contained in the *Corporate planning and performance reporting requirements Government Business Enterprises, October 2009.*

(b) Future challenges and opportunities from analysis of both external and internal environments

Analysing the external and internal factors that may affect the Agency objectives will inform planning choices.

External factors can include:

- forecasts of economic conditions;
- sector-specific inflationary pressures;
- longer-term changes to the drivers of demand;
- inconsistent/variable demand for services provided;
- demographic changes;
- anticipated technological developments;
- actions by other governments; and
- the regulatory environment.

Internal factors can include:

- the Agency's culture and structure;
- capacity to deliver;
- resources, including the available technology and condition of assets;
- physical location of service delivery providers;
- performance data; and
- clients/community, service, asset and operation plans.

This type of information will allow an Agency to conduct risk and SWOT (strength, weakness, opportunities and threats) assessments.

(c) Strategies to meet service demands and objectives in the corporate plan period including strategies to deliver high quality/better services to Victorians at minimum cost. For Government Business Enterprises[54], these are to include measures to improve return on investment

The next phase of planning is formulating strategies and developing implementation plans to deliver high quality/better services at minimum cost and meet Agency objectives over the medium-term. Government Business Enterprises are to consider measures to improve return on investment. This should involve the whole business to ensure planning addresses key performance drivers, emerging risks, challenges and opportunities.

Some areas for consideration include:

- restructuring activities and products/deliverables;
- addressing demand and supply factors;
- technology and innovation (e.g. market-based solutions);
- minimising operating costs and achieving operational efficiency;
- workforce planning and improving capability;
- asset planning to manage and achieve optimal value from the Agency's asset base;
- engaging the market in maximising the value from procurement and external service providers; and
- addressing government policies, targets and commitments.

Resource planning (assets, finance, workforce) is an integral part of the corporate planning process through the inclusion of targets for planning purposes.

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54 Bodies that are subject to the *Corporate planning and performance reporting requirements Government Business Enterprises, October 2009* are: those GBEs that are accountable to the portfolio Minister and/or the Treasurer where the Treasurer has a legislated role to receive corporate planning or other financial documents.

(d) Planned services and infrastructure delivery

Following the analysis and strategy formulation phases, an Agency should identify and/or confirm the strategies, priorities, services, infrastructure and activities to be delivered over the medium-term. These should cover all critical aspects of the business.

(e) Estimates of revenue and expenditure over the corporate plan period

Planning includes confirming the financial resources available to meet the Agency's planned services and infrastructure delivery, strategies and priorities, and business objectives usually over the next three to four years. The estimated financial statements are supported by the medium-term financial plans and strategic medium-term cash flow projections (see below for further guidance on these plans).

(f) financial and non-financial key performance indicators/measures (KPIs) and associated targets covering, at a minimum, the Agency's operations, assets, the achievement of organisational objectives and the delivery of services

Planning involves identifying relevant KPIs and setting appropriate targets. This will assist in managing performance and for accountability reporting of actual performance against planned.

Setting targets

Agencies may use a combination of methods to set targets. Commonly used approaches in setting targets include:

- current performance;
- current performance plus/minus a percentage improvement change;
- averaged performance (national, state, or industry);
- best practice (benchmarking);
- technical targets (external targets established by professional associations); and
- management decisions (calculated decisions given resource and staffing parameters).

To ensure targets are not unrealistic or create perverse incentives:

- targets should be set through Agency planning processes;
- proposed targets should be trialled in parallel with existing targets; and
- targets should be presented in the context of the service being delivered and government funding models used.

Performance indicators and service delivery performance measures

Performance indicators demonstrate the impact services and projects have on clients and the community. They are indicators of efficiency and effectiveness and provide evidence in measuring progress towards achieving Agency objectives in the medium-term. When dealing with impacts, direct measures are often difficult and measures can often only 'indicate' the outcome. Therefore, an indicator may be supported by multiple data series.

Performance indicators are results focused. They should:

- have a logical and consistent relationship to the Agency objectives;
- provide links between the objectives and deliverables; and
- be set at a level to support performance analysis.

Service delivery performance measures enable the examination of Agency performance in delivering services and projects. They demonstrate the efficiency and effectiveness of delivery and should not encourage unwanted or wasteful behaviour. Measures should be stretching to reflect the Government's expectations for improved standards of public services, but be achievable within the Agency's available resources. Performance measures should have the capacity to measure the extent and standard of service and project delivery. They should seek to measure different attributes of service delivery such as:

- quantity;
- quality;
- timeliness; and
- cost.

Effective performance reporting requires consideration of the following factors when developing performance indicators and measures:

- comprehensive – there should be indicators to cover all critical aspects of the Agency objectives and measures to cover services and/or projects and/or activities;
- fit for purpose – indicators and measures should reflect what the Agency is trying to achieve;
- balanced –a balanced set of indicators and measures should be developed;
- attributable – indicators should be attributable to the Agency objectives, and measures to services, projects and activities delivered by the Agency;
- clear – the definition of the indicator and measure should be clear so that data collected is easy to understand and documentation of measurement processes should be maintained;
- measurable – indicators and measures should be able to be measured consistently and be responsive to change. There should be a clear and transparent standard of success and data should be available;
- comparable – indicators and measures should remain relevant over the medium-term, allowing comparisons over time and between target groups and across jurisdictions;
- interpretable – indicators and measures are able to be reported with appropriate context (e.g. trends, targets) to enable meaningful conclusions to be drawn;
- cost-effective – cost of data collection and processing does not outweigh the benefits the indicators and measures provide;
- credible – indicators and measures are supported by stakeholders and when appropriate, supported by research and/or established industry standards; and
- timely – performance data should be produced regularly enough to track progress and, quickly enough for the data to still be of value for decision-making.

Financial performance indicators in assessing financial sustainability

The Directions require the Responsible Body to oversee the Agency's financial sustainability performance and the Accountable Officer to promote financial sustainability and ensure the availability of performance indicators and targets.

Relevant financial information and key financial performance indicators help to provide insight into Agency financial sustainability. Although the medium-term corporate plan should contain financial information, this information, when appropriate, should be based on long-term planning (refer to section on financial sustainability expectations).

In developing suitable indicators and targets, Agencies should consider regulatory, governance, funding and operating arrangements. The same set of indicators will not be appropriate for assessing financial sustainability for all Agencies due to the varied nature of these arrangements across the VPS.

Indicators to assess financial sustainability may include a combination of:

- reported net profit;
- net cash flows from operations;
- capital structure and gearing ratios, which show the relative proportion of the assets of the business that are being financed by the owner and external financiers;
- liquidity (current ratio), which expresses, as a ratio, the value of cash and other assets that could reasonably be expected to be monetised during the current financial year relative to the value of liabilities that are due and payable during the current financial year;
- debt servicing capacity, interest coverage on earnings before interest and tax (EBIT), earnings before depreciation, interest and tax (EBITDA) (both on a cash and accrual basis) and total debt to EBITDA (on a cash and accrual basis); and
- profitability – return on assets, return on equity, and sales margin, which express earnings as a percentage of assets, equity and sales.

Monitoring reports should cover both the current year and medium to longer-term period. It is important to consider historical and projected trend data in decision-making and in reviewing financial performance. Medium to longer-term reporting is to address the impact of short-term decisions and/or activities (e.g. 'lumpy' nature of capital expenditure) on financial sustainability. All indicators need to be interpreted in context, such as:

- the commercial focus of entities;
- revenue sources;
- capital allocation and cash management models used and price determinations by regulators;
- asset valuations;
- dividend requirements; and
- industry and/or sector features such as volatility.

Financial sustainability expectations

Balancing the delivery of government objectives and priorities with finite financial resources is an important responsibility of the Accountable Officer and Responsible Body.

Financial sustainability is the ability of an Agency to deliver required services in the medium and longer term, and within its regulatory, governance, funding and operating environment and proposed strategies. To be financially sustainable, an Agency needs to have a sustainable capacity to meet its current and future financial obligations. Effective medium to longer term planning and budgeting (financial projections) is therefore a key consideration for the continued provision of services.

In summary, a financially sustainable Agency should be able to:

- deliver agreed services and service levels within available financial resources and at minimum cost;
- maintain operational viability;
- ensure fees and charges are set in accordance with the Victorian Government's Cost Recovery Guidelines;
- ensure assets are looked after and maintained;
- meet any relevant government policies, targets and commitments; and
- when relevant, deliver a return on investment for public corporations.

Financial sustainability evaluation involves the assessment of both corporate and financial performance. Corporate performance is about the efficiency and effectiveness of service delivery within financial capacity and cost minimisation. It is assessed by key performance indicators and measures, reviews and audits. Financial performance is the financial result of corporate performance and is measured by financial performance indicators.

Financial sustainability is the capacity to fund all operating expenditures from operating revenue. In addition, for most public corporations, it includes the capacity to meet capital replacement requirements. Hence, the management of capital and long-term assets and liabilities is an important component of financial sustainability, which includes:

- the maintenance of existing assets to ensure required service levels are achieved and their expected economic life is maximised unless there is a substantive reason not to; and
- timely submissions, consistent with the Agency's long term plan and strategy, to the appropriate budget funding authority for new or replacement assets to sustain or expand services.

In certain circumstances, the expected economic life of assets cannot be maximised. For example, when the Agency is restructuring and/or its role and functions are changing. Further, for some Agencies with cultural activities or significant community service type obligations, government policy decisions may also limit their ability to fund capital replacement requirements from operating revenues.

Agencies need to consider a range of policy options to attain the optimum revenue and expenditure balance, such as adjusting fees and charges, containing costs, increasing productivity and reshaping product and/or service offerings.

All Agencies have the ability to minimise cost. Some suggested strategies such as using market-based solutions are included in the 'Corporate Plan' section of this guidance.

In addition, DTF conducts Cost control and efficiency reviews designed to deliver practical options for improving value for money in the delivery of services, which can further assist Agencies in this area.

Different government sectors

Agencies across the different sectors of Government have differing accountability and funding models, depending on their institutional classification and overall objectives. There are three institutional sectors of Government recognised in relation to financial reporting by Agencies under Australian Accounting Standards: public non-financial corporations (PNFC), public financial corporations (PFC), and general government sector agencies.[55]

Given the different functions, objectives and funding arrangements of Agencies in each of the abovementioned sectors, different governance arrangements and accountability models apply. The Government has an arm's length relationship with public corporations, has expectations for them to operate on a commercial basis, and appoints boards of governance (independent from management) to oversee these Agencies. The Government has a relatively close relationship with general government sector Agencies due to its provision of funding, departmental-portfolio support, and their contribution to the State's fiscal objectives.

General government sector Agencies

General government sector Agencies (refer to glossary for definition) are listed in the Controlled Entities Note in the State's Annual Financial Report.

A financially sustainable general government sector Agency is able to:

- in the short-term, finance its operating expenditure obligations; and
- for the medium to longer term, maintain the existing capital base to a level that ensures their economic life is maximised unless there is substantive or policy reason not to.

For the replacement of capital and the expansion of the capital base, the Accountable Officer provides support to the Portfolio Department to undertake portfolio budgeting and planning based on the capital allocation model, including advice to the Responsible Minister and the Portfolio Department about portfolio specific risks, particularly when they will likely lead to future funding requests.

[55] Australian System of Government Finance Statistics: Concepts, Sources and Methods. Australian Bureau of Statistics Cat 5514.0. See glossary for definitions.

General government sector Agencies derive the majority of their funding from the Consolidated Fund. The Government approves general government sector asset investment decisions. Funding for these decisions is typically provided through depreciation equivalent revenue (a balance sheet receivable to a Portfolio Department), or through appropriations as a capital contribution to increase its net asset base. Only in exceptional circumstances, for example finance lease arrangements, are general government sector Agencies expected to carry long term borrowings on their balance sheets. In such instances, Agencies are expected to cover ongoing loan repayments and financing costs as part of their budget funding.

Financial sustainability does not necessarily require a general government sector Agency to set and maintain revenues at a level to cover its non-cash annual depreciation charge (and thereby accumulate capacity to replace non-financial assets), particularly given the high value of many public service delivery assets. A general government sector Agency is expected to manage and maintain its existing assets to deliver the agreed service levels and to maximise their economic life.

The departmental funding model governs the setting and management of Portfolio Departments' global appropriations and the circumstances under which Portfolio Departments can potentially receive additional funding. Under the departmental funding model, the Government determines the outputs to be delivered by a Department and portfolio general government sector Agencies and the price for each of the outputs for a given level of quantity, quality and timeliness. Portfolio Departments are responsible for ensuring the delivery of these agreed outputs within the Government's desired parameters and managing all associated costs.

In the context of the departmental funding model and supporting the Portfolio Department to undertake portfolio planning and budgeting, expectations of the Accountable Officer of general government sector Agencies include:

- input to corporate and long-term portfolio plans;
- submissions to the relevant Cabinet Committee for budget funding, and for reporting on the use of budget funding; and
- advice to the Responsible Minister and the Portfolio Department about portfolio specific risks, particularly when they are likely to lead to future funding requests.

The Responsible Minister, or the Government more broadly, may make a decision to not fund an Agency to the level requested, and at this time, the Accountable Officer of the general government sector Agency should advise the Minister as to the consequences of this decision.

Public corporations (i.e. public non-financial and public financial corporations)

A financially sustainable public corporation is able to:

- in the short-term, finance its operating and financing expenditure obligations; and
- for the medium to longer term:
  - maintain the existing capital base to a level that ensures their economic life is maximised unless there is substantive or policy reason not to; and
  - replace the existing capital base, when this is the agreed governance and capital arrangements with Government.

To expand the existing capital base, the Accountable Officer advises Government through its corporate and strategic planning process of the proposed expansion, financing options and a request for government investment.

Public corporations are typically funded through own-sourced revenue, and the boards of these Agencies are responsible for overseeing the Agency's delivery of services within the available funds. For a PNFC, long term financial sustainability is the capacity to fund all operating expenditures and capital replacement requirements from operating revenues. In the short term, financial sustainability focuses on the capacity to fund operating expenditures and to achieve an appropriate return on investment.

In the absence of contrary government policy decisions such as regulated pricing or mechanisms that limit an Agency's ability to raise sufficient revenue, long term financial sustainability includes the *maintenance and replacement* of the existing capital base.

Regarding the *expansion* of the existing capital base, the Responsible Body should advise Government through its corporate and strategic plans how this expansion will be financed, along with a request for additional government investment (including equity injection). The Government, as owner of the business, should decide if further investment in the business should be pursued in line with government objectives and priorities. In many cases, additional borrowings are sufficient to allow for an expanded capital base.

Rolling medium-term financial plans

The medium-term financial plan sets out the Agency's approach to managing its finances to meet the agreed business objectives and priorities. The plan is an internal document developed as part of the Agency's medium-term planning process and aligns with the Corporate Plan. In developing the plan, Agencies should consider governance, regulatory and funding arrangements.

The main objectives of the medium-term financial plan are to:

- explain the financial context in which the Agency is to work over the medium-term;
- identify the financial resources needed to deliver the Agency's medium to longer term business objectives and priorities;
- provide a medium-term forecast of resources and expenditure; and
- achieve a stable and sustainable financial position capable of withstanding financial pressures and avoiding deficit spending.

The plan attempts to match future predicted resources and expenditure to meet the Agency's business objectives and priorities, identifies potential gaps, outlines the financing requirements including borrowing limits and whether borrowings are new or refinanced and other financial goals (e.g. capital repayments, dividends), and provides the financial framework for the next three to four years.

Depending on the nature of the Agency's business and/or change in function or service delivery, the Agency may need to develop longer-term financial plans (e.g. if it has long-lived assets or its service delivery model is changing).

The plan is a tool through which an Agency can monitor, manage and resolve issues affecting its financial sustainability. Monitoring the plan requires matching reality against assumptions, evaluating the impact of changes to risk status, and making necessary amendments as more information becomes available or circumstances change.

For Portfolio Departments and Agencies funded by the State Budget, the plan should reflect the budget and forward estimates articulated in the Budget (i.e. the same assumptions regarding wages, inflation).

The governance, regulatory and funding arrangements will dictate the levers available to each Agency in managing its finances. This then determines the scope of the plan. For example, some Agencies may have greater scope to raise revenue than others. The following are suggested areas for inclusion in the plan:

- **Funding Strategy** – this sets out where funding will come from, when it comes from a specific source, and its use.
- **Capital Strategy** – this sets out the strategic direction for the Agency's capital management and investment plans, and is integral to the medium-long term planning and budget setting process. It sets the principles for prioritising capital investment. Capital expenditure is defined as the purchase or enhancement of assets when the benefits last longer than the year of expenditure. The capital budget should support the overall objectives of the Agency and Government.
- **Treasury Management and Investment Management Strategy** – this covers the financing and investment strategy for the forthcoming financial years (refer to Direction 3.7.2).
- **Risk Management Strategy** – this identifies the key risks relating to the financial plan to support the delivery of organisational priorities and objectives (refer to Direction 3.7).

Rolling strategic medium-term cash flow projections

Cash flow projections indicate the likely future movement of cash in and out of an Agency and provide information on upcoming cash surpluses or shortages. For general government sector Agencies, these projections should align with the cash flows in the State Budget.

Strategic cash flow projections are used to plan for significant cash flows and any contingencies. For example, new capital acquisitions or to identify the need to secure additional investment. Cash flow projections need to align and complement the medium-term financial plan.

Strategic cash flow projections are different to short term tactical forecasts. Short term tactical forecasts are usually prepared monthly to provide detailed estimates of the cash flows expected or weekly operational forecasts to meet cash flow requirements.

Depending on the nature of the Agency's business and/or change in function or service delivery, the Agency may need to develop longer-term cash flow projections (e.g. if it has long-lived assets or its service delivery model is changing).

Allocate resources

The Responsible Body, Accountable Officer and the CFO have individual responsibilities to ensure public money is safeguarded and appropriately allocated to deliver the Agency's plans and strategies efficiently and effectively.

The Australian National Audit Office (ANAO) **Developing and Managing Internal Budgets, June 2008**[56] provides guidance to assist organisations better manage internal budgeting activities. It discusses a range of principles and techniques to embed internal budgeting in an organisation's planning, control and accountability systems.

Effective internal budgeting processes that underpin effective resource allocation should assist the Agency achieve its goals and objectives when embedded into corporate planning and aligned to the external budget.

The ANAO guide identifies:

- better practice organisations embed internal budget processes into organisational planning and management by:
  - integrating the internal budget into organisational planning;
  - aligning the internal budget with organisational roles and responsibilities;
  - integrating operational and capital budgets;
  - aligning internal and external budgets;
  - harmonising budgeting and reporting; and
  - engaging stakeholders in the internal budget;
- developing and implementing an internal budget requires effective:
  - planning and coordination, including clearly defined expectations and assumptions, a coordinated calendar of activity and well-documented and communicated policies and procedures;
  - budget construction through implementing established and agreed budget methodologies and automating budget processes; and
  - oversight, review and communication through active senior management involvement, rigorous quality assurance processes and structured communication.

[56] https://www.anao.gov.au/work/better-practice-guide/developing-and-managing-internal-budgets

Monitor and evaluate

Performance monitoring

Performance management requires measuring and monitoring actual results or performance achieved against plans. Evidence from performance measurement enables Government and management to focus on improving the results and impact by supporting decision-making and managing risk. Performance data can be used to:

- inform strategic planning and ongoing development and implementation of policy, strategies and plans;
- inform capability and service development;
- report consistently and concisely on achievements; and
- hold managers accountable for performance.

Performance monitoring should:

- be conducted for all levels and types of plans including strategic, corporate, operational and financial plans;
- identify performance trends, gaps and risks;
- enable the implementation of mitigation strategies and corrective actions, if required;
- cover both the financials and non-financials and the interrelationships between them to enable integrated performance information to be reported; and
- span across multiple years.

Non-financial performance monitoring should cover the delivery of services and activities at the operational level, and the progress towards achieving Agency objectives and outcomes at the strategic level.

Financial and budget monitoring should cover the current year and the medium-term. This will enable monitoring of the budget for the current year as well as assessing financial sustainability over the medium-term and the impact on service delivery and results.

Under Direction 2.3.2, Agencies are required to inform the Responsible Minister of significant risks. Agencies should consider informing the Responsible Minister when they become aware of:

- significant variations to strategies compared to plan;
- significant variations to the total estimated investment (TEI) or timing of capital investments compared to plan;
- material variation in forecast full year profit or cash flow from operating activities compared to plan;
- significant variations to KPIs compared to plan; and
- any financial or non-financial (including reputational) developments which may materially impact the Agency or the Government.

Evaluating policy and programs

The DTF Guide to Evaluation 2005[57] provides a practical framework and some key principles for planning and implementing effective policy and program evaluations. It also includes references that may be useful for more detailed information and examples of effective evaluation.

Report

Performance reporting provides relevant information to stakeholders and decision-makers, and supports government transparency and accountability.

There are two main streams of performance reporting:

- accountability reporting – measuring and reporting performance against targets/plans; and
- internal (organisation) performance management reporting – providing information to help management, stakeholders, and decision-makers better understand the business and respond tactically or strategically to mitigate risks.

[57] http://www.dtf.vic.gov.au/Publications/Government-Financial-Management-publications/Policy-and-program-evaluation

Performance information on past results also informs planning and budgeting activities.

Internal performance management reporting should assist with:

- early identification of potential problems through performance measures, trend analysis, forecasting, benchmarks;
- data driven decision-making (i.e. information and measures to assist management decision making);
- quality improvement programs, based on clear identification of areas for improvement that align with business plans across the Agency; and
- allocation of responsibilities and accountabilities.

Good performance reporting depends on reliable performance information for both external requirements and internal management and review. Some strategies to improve performance reporting include:

- establishing a robust performance culture based on public sector values;
- maintaining strong links between reporting, planning and management; and
- ensuring strong links between external and internal reporting.

Internal management reporting requirements depend on the nature of the Agency's business, the operational and strategic drivers, and expectations of management and the Responsible Body. It should consistently reflect and align with strategic objectives and only provide key information that drives an Agency's performance in achieving business objectives. An effective suite of management reports require a balance of financial, operating, risk and control indicators.

Some good practice internal management reporting principles include reports that:

- fulfil business needs;
- are clear and relevant;
- are accurate, reliable and timely;
- are complete and consistent; and
- comment, evaluate and compare.

Refer to Direction 3.9 and Direction 5.3 for further information on information collection and management and reporting requirements of Agencies and Portfolio Departments.

Guidance 4.2.1 – Acquisition of assets, goods and services

Objective	Provides guidance for contract management and performance (in accordance with Instruction 4.2.1) and information on whole of state polices and guidance for procuring goods and services and infrastructure investments.
Effective date	1 July 2016
Relevant Direction	4.2.1 Acquisition of assets, goods and services
Last reviewed date	1 February 2016

Contract management and performance (in accordance with Instruction 4.2.1)

Managing contracts effectively is an important aspect of good governance. It provides assurance to the responsible Agency that the contractor is delivering the agreed services at the required standard, and there is efficient and effective use of public resources.

As more services and projects are delivered outside the public sector robust contract management is becoming increasingly important. Establishing a sound governance framework for effectively managing projects and contracts may include a review of risk management plans and consideration of risk sharing. In many cases ensuring appropriate contract design and management will require appointing an effective contract manager. One of the critical roles the contract manager will play is establishing effective performance management monitoring and evaluation and managing effective commercial relationships to ensure appropriate performance and value for money is obtained from the contract.

Performance management is an important part of contract design and specification. Without it, not all parties subject to the contract or agreement will have the same expectations. As such, appropriate effort needs to be devoted to this important task. The contract development phase is critical to achieving the outcomes sought by the Agency and sets the basis for the effective management of the contract.

Performance expectations typically articulated in the contract or service level agreements may include:

- key personnel within an Agency and the provider who will be responsible for delivery;
- what will be delivered using quality, quantity and timeliness criteria;
- key performance indicators and related targets and standards (including quality standards) or goals used to measure delivery. These should be linked to the purpose or objective of the infrastructure or service requirements and be clear, relevant, achievable and readily measurable;
- the type and frequency of performance monitoring and verification arrangements which will be implemented. These arrangements are designed to provide Agencies with comfort that performance is in accordance with the contract and payment should proceed;
- the frequency and method of payment when performance measures or targets are met. For example, upon delivery or at agreed intervals;
- the penalties or other consequences to be applied for any performance shortfall. For example, part of the payment may be withheld until the required performance or delivery standard is met;
- the process for resolving disputes when there is a disagreement about performance;
- arrangements for monitoring performance and access to documentation, whether by the Agency, its delegate or the Auditor-General;
- parameters around the ownership and, sharing of data and records, and protocols for communication and dispute resolution;
- arrangements for ongoing communication, including dispute resolution protocols; and
- the timing of evaluation and reporting expectations.

This list is not exhaustive and there may be some specific performance expectations an Agency will seek to articulate.

An Agency's Responsible Body is ultimately responsible for the delivery of all infrastructure and services within its control. Therefore, the responsibility of the Accountable Officer needs to ensure the Agency has appropriate performance management arrangements, particularly for those services or infrastructure being delivered by providers external to the Agency. This is particularly important when the Accountable Officer or delegate is not involved in the day-to-day management or delivery of the service or infrastructure.

Monitoring

Regular ongoing monitoring and assessment of contract performance throughout the life of the contract is important, as it:

- enables the early identification and resolution of any issues before they become a significant problem;
- encourages performance measures and targets and helps ensure relevant timelines are met;
- identifies any variation to specification that may be required to address identified issues; and
- puts the onus on the provider to ensure that delivery occurs to specification.

The Accountable Officer is accountable for monitoring contract performance and delivery. The Responsible Body (supported by the Audit Committee through independent assurance and advice) is responsible for overseeing performance of the Agency, in particular contracts which it has specifically made decisions on.

Individuals involved in the specification phase of the contract or those responsible for the service or asset post-delivery may be best placed to be involved in monitoring the provider. However, from time to time, the Accountable Officer may require someone independent of the contract to monitor performance. Internal audit or a specialist advisor may be engaged to provide advice to the Accountable Officer and/or Responsible Body. In order to effectively monitor and assess contract performance, a number of things are required:

- monitoring arrangements the provider will be subject to should be agreed to, documented and actioned;
- ongoing access to relevant, reliable and timely data/information from the provider relating to performance is necessary and should extend to other relevant parties in Government who may perform a monitoring or review role, such as Portfolio Departments;
- for longer-term service delivery contracts, regular independent reviews of performance data prepared by the contractor will provide the Agency with a level of assurance on the accuracy and reliability of data for performance management and payment; and
- communication protocols should be agreed and documented, including dispute resolution arrangements.

Record retention and information access or sharing arrangements enable an Agency to monitor and verify performance. Such arrangements may need to continue for a period of time after the contract has concluded to allow for independent verification of required delivery standards.

Communication is a key component of any monitoring arrangement. Open communication between an Agency's management and the provider is important to ensure that all parties are aware of any issues before they impact on the service or infrastructure.

Reporting of contractor performance assessment and any shortcomings is provided to the Audit Committee (on behalf of the Responsible Body) to review performance on a regular basis.

Evaluate and report

At the conclusion of the contract engagement, an evaluation should be conducted. This is to review and evaluate the success of the contract against stated goals, and government objectives and priorities, and to recommend appropriate actions. To a large extent, the evaluation should use the success measures established during the business or service need phase and the performance measures outlined in the contract.

Evaluations are useful to all parties involved in the contract as they can identify successes and lessons learnt. An honest assessment of the contract should provide information that can be used in future contracts or to make recommendations to resolve any outstanding issues with the contract.

Similar to monitoring arrangements, evaluations can be conducted internally by the Agency or by an external provider such as a specialist advisor. In addition, the Portfolio Department may choose to separately evaluate the contract to identify systemic issues or as part of their ongoing assurance program. Such evaluations would be separate to an internal evaluation undertaken by the Agency. It is important that appropriate access and record retention arrangements are established to ensure such evaluations can be undertaken.

As it may take time for an evaluation to be conducted or for the full benefits of the contract to be realised, the contract should adequately provide for record retention and information access or sharing arrangements for a period of time after the conclusion of the contract. Access to such information should be provided to the Responsible Body/Accountable Officer or their delegate, internal audit, or the Portfolio Department.

The findings from the evaluation should be documented, considered, actioned and formally endorsed by the Accountable Officer and provided to the Audit Committee (Responsible Body). Further, the evaluation results should be referenced and used by the Accountable Officer in future contracts. It is also useful to provide summarised findings to other Agencies or the Portfolio Department which may be undertaking similar contracts, to enable them to leverage off any lessons learnt.

Infrastructure investment

Investment lifecycle and High Value/High Risk guidelines [Department of Treasury and Finance]

The guidelines provide guidance on processes, documents and other requirements to support robust development and delivery of all investment proposals. At each stage of the investment lifecycle, this guidance helps Agencies to shape, monitor, control and evaluate an investment. The following stages of the Investment Lifecycle are relevant to the contracting of services:

- **Stage 1: The Conceptualise stage** confirms the need, defines likely benefits and explores strategic interventions.
- **Stage 2: The Prove stage** confirms that the recommended project solution offers value-for-money and can achieve the benefits sought, and indicates the likely costs and risks to the State. The key deliverable for this stage is a business case.
- **Stage 3: The Procure stage** processes should align with the procurement strategy developed in the business case. Tendering is a phase of the procurement process in which Agencies seek and select offers from suitable suppliers. The key deliverable for this stage is the awarding of the contract.
- **Stage 4: The Implement stage** focuses on managing project delivery. The Agency needs to be monitoring not only the schedules and budgets but whether the solution is and remains robust, the effectiveness of contract management arrangements and whether there is a basis for evaluating ongoing performance.
- **Stage 5: The Realise stage** measures the success of the investment.

High Value/High Risk (HV/HR) projects [Department of Treasury and Finance]

For general government Agencies, infrastructure and ICT projects identified as being high value and/or high risk will be subject to more rigorous scrutiny and approval processes.

The process applies to all infrastructure and ICT investments that:

- have a total estimated investment (TEI) greater than $100 million (regardless of funding source);
- are identified as high risk using an approved risk assessment tool; or
- are determined by the Government as warranting the rigour of increased oversight.

The Government may also nominate projects to be part of this process.

Gateway reviews [Department of Treasury and Finance]

For general government Agencies, Gateway reviews are mandatory for infrastructure and ICT projects identified as being high value and/or high risk.

The Gateway review process examines projects and programs at key decision points throughout their lifecycle regarding progress and likelihood of delivery success.

- **Gate 1: Concept and feasibility** – investigates the strategic direction and concept development.
- **Gate 2: Business case** – confirms the business is robust, i.e. it meets the business need, is affordable, achievable and is likely to obtain value for money.
- **Gate 3: Readiness for market** – confirms the business case once the project is fully defined, confirms the objectives and desired outputs remain aligned and ensures the procurement approach is robust, appropriate and approved.
- **Gate 4: Tender decision** – confirms the business case including benefits plan once the bid information is confirmed and checks the required statutory and procedural requirements were followed and that the recommended contract decision is likely to deliver the specified outcomes on time, within budget and provide value for money.
- **Gate 5: Readiness for service** – tests the projects readiness to provide the required service by confirming the current phase of the contract is complete and documented, the contract management arrangements are in place and current, and the business case remains valid.
- **Gate 6: Benefits realisation** – examines whether the benefits as defined in the business case are being delivered, typically occurs 6-18 months after project completion.

Investment Management Standard [Department of Treasury and Finance]

The Investment Management Standard (IMS) is a collection of simple ideas and practices to help organisations direct resources to deliver the best outcomes. Investment Management can be used to undertake the following seven practices:

- shape a new investment;
- prioritise investment proposals;
- develop new policy;
- monitor and measure the delivery of benefits;
- evaluate a program of investment;
- refocus an organisation to improve its effectiveness; and
- monitor an organisation's outcomes.

Procurement

Victorian Government Purchasing Board (VGPB) policies

The VGPB policies are mandatory for all Departments (FMA section 54L) in procuring goods and services for the Agency's own use. It is recommended that other Agencies apply similar procurement policies.

There are five policies covering the end-to-end procurement activities, together with supporting guides, tools and templates:

- Governance policy[58] specifies the requirements for your procurement governance framework, assessment to manage procurement activity and complaints management.
- Complexity and capability assessment policy[59] specifies the requirements to conduct an assessment of the complexity of the procurement and the capability required to carry out the procurement successfully.
- Market analysis and review policy[60] specifies requirements for market analysis, aggregated purchasing and disposal of assets.
- Market approach policy[61] specifies the requirements for market approach, critical incidents, and evaluation, negotiation and selection.
- Contract management and contract disclosure policy[62] specifies requirements for managing and disclosing contracts.

[58] http://www.procurement.vic.gov.au/Buyers/Policies-Guides-and-Tools/Governance-Policy
[59] http://www.procurement.vic.gov.au/Buyers/Policies-Guides-and-Tools/Complexity-and-Capability-Assessment-Policy
[60] http://www.procurement.vic.gov.au/Buyers/Policies-Guides-and-Tools/Market-Analysis-and-Review-Policy
[61] http://www.procurement.vic.gov.au/Buyers/Policies-Guides-and-Tools/Market-Approach-Policy
[62] http://www.procurement.vic.gov.au/Buyers/Policies-Guides-and-Tools/Contract-Management-and-Contract-Disclosure-Policy

State Purchase Contracts[63] (SPC) are standing offer agreements for Victorian government common use goods and services. They are established when value for money in procurement can best be achieved through aggregating demand. SPCs are established for use by Departments and are mandatory, however these contracts can be used by other public bodies.

Public Private Partnerships Policy [Department of Treasury and Finance]

The *Partnerships Victoria* policy provides the framework for a whole-of-government approach to the provision of public infrastructure and related ancillary services through long term public-private partnership contracts.

The *Partnerships Victoria* Framework requires compliance with both the National Public Private Partnerships Policy and Guidelines and the *Partnerships Victoria* requirements and annexures.

Alliance Contracting Policy [Department of Treasury and Finance]

Alliancing is a method of procuring, and sometimes managing, major capital assets. Under an alliance contract, a state Agency contractually works collaboratively with private sector parties to deliver the project.

The Victorian Government policy and guidance material are aimed at Departments and Agencies undertaking alliancing contracts and other collaborative contracting models such as Early Contractor Involvement (ECI). The National Alliance Contracting: Policy Principles[64] sets out the Victorian Government's minimum requirements for alliance contracting and other collaborative contracting models.

Normally, alliancing is used to deliver the larger, more complex and high-risk infrastructure projects (with capital costs exceeding $50 million) and where the owner has particular capability to contribute its skills and expertise to deliver the project.

Public construction policy (Ministerial Directions) and guide [Department of Treasury and Finance]

The policy prescribes procurement, tendering and contracting procedures and practices for public construction in Victoria (*Project Development and Construction Management Act 1994* and Ministerial Directions).

Victorian Industry Participation Policy [Department of Economic Development, Jobs, Transport and Resources]

The policy requires government Departments and Agencies to consider competitive local suppliers, including SMEs, when awarding contracts valued at:

- $1 million or more in regional Victoria, or
- $3 million or more in metropolitan Melbourne or for state-wide activities.

Procurements that have a total project value of $50 million or more are considered Strategic Projects under the policy and will have minimum local content requirements set to help drive additional economic activity and jobs.

The Department of Economic Development, Jobs, Transport and Resources website provides helpful information.

ICT Procurement Policy and Standards (Department of Premier and Cabinet)

Enterprise Solutions produces standards, policies and governance frameworks for whole of Victorian government shared services and information and communications technology.

Traditional Contracting of infrastructure [Department of Treasury and Finance]

The National framework for traditional contracting of infrastructure documents best practice to promote productivity improvements in the planning and contracting phase of major projects.

In the context of the framework, traditional contracting refers to those contracts that to varying degrees allocate construction and design risk to the suppliers (but are not alliances or PPPs).

[63] http://www.procurement.vic.gov.au/state-purchase-contracts
[64] http://www.dtf.vic.gov.au/Infrastructure-Delivery/Alliance-and-traditional-contracting

The two primary categories of traditional contracting are:

- construct only (CO): the design has been undertaken by the client, and the supplier is responsible for constructing the works to the client's design; and
- design and construct (D&C): generally a limited design has been undertaken by the client who then invites potential suppliers to tender on the basis of completing the client's design and constructing to that design.

Market-led Proposals Interim Guideline [Department of Treasury and Finance]

The Market-led Proposal Interim Guideline[65] documents a transparent and consistent process where private parties can directly approach Government seeking support and approval to provide a project or service.

The Guideline does not apply to the routine procurement of goods and services as covered under Part 7A of the FMA (i.e. goods and services covered by VGPB policies). Further information can be found on DTF's website – Market-led proposals[66].

Other guidance

The following provides further information on each of the policies and guidance. Guidance material is generally accessible via the following websites:

- Department of Treasury and Finance[67]
- Enterprise Solutions[68]
- Victorian Auditor-General's Office[69]
- Australian National Audit Office[70]
- Department of Economic Development, Jobs, Transport and Resources[71]
- Victorian Government Purchasing Board[72]

Investing smarter in public sector ICT: Turning principles into practice [Victorian Auditor-General's Office]

The guidance is designed to assist public sector chief executive officers and senior responsible officers to question and assess whether their investments are delivering their intended benefits, resulting in better business and financial value for government and the public.

Developing and Managing Contracts [Australian National Audit Office]

Getting the right outcome, Achieving value for money[73] (2012) covers the phases of the procurement cycle commencing from the selection of a preferred tenderer or contractor through to managing and ending the contract.

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65 http://www.dtf.vic.gov.au/Publications/Infrastructure-Delivery-publications/Market-led-Proposals-Interim-Guideline/Market-led-Proposals-Interim-Guideline

66 http://www.dtf.vic.gov.au/Infrastructure-Delivery/Market-led-proposals

67 http://www.dtf.vic.gov.au/Home

68 http://www.enterprisesolutions.vic.gov.au/

69 http://www.audit.vic.gov.au/

70 http://www.anao.gov.au/

71 http://economicdevelopment.vic.gov.au/

72 http://www.procurement.vic.gov.au/Home

73 https://www.anao.gov.au/work/better-practice-guide/developing-and-managing-contracts-getting-right-outcome-achieving-value

Guidance 4.2.2 – Discretionary financial benefits – grants, sponsorships and donations

Objective	Provides guidance on financial management control considerations in administering discretionary grants, sponsorships and donations.
Effective date	1 July 2016
Relevant Direction	4.2 Using and managing public resources 4.2.2 Discretionary financial benefits – grants, sponsorships and donations
Last reviewed	1 February 2016

Discretionary financial benefits – grants, sponsorships and donations

Discretionary financial benefits include discretionary grants, sponsorships and donations. These forms of discretionary financial benefits are given to a person or body (including community groups, statutory bodies or commercial enterprises) to achieve results sought by government policy. Such discretionary financial benefits do not include financial benefits as consideration for goods or services provided under a commercial agreement (e.g. contracts), or transfer of funds to a government entity for funding non-contestable output delivery.

Discretionary financial benefits typically have the following characteristics:

- a transfer to a recipient which may be in return for compliance with certain terms and conditions;
- a transfer which may not directly give approximately equal value in return to the Government (that is, there is a non-exchange transaction or subsidisation so there may not be exact dollar for dollar value); and
- a recipient may have been selected on merit against a set of program-specific criteria.

Discretionary grants

A discretionary grant is money given to organisations or individuals for a specified purpose directed at achieving goals and objectives consistent with government policy. The portfolio minister or paying Agency has discretion in determining whether or not an applicant receives funding and may or may not impose conditions in return for the grant. Funds transferred to a government entity for non-contestable output delivery is not considered a discretionary grant.

Investment principles for discretionary grants

The following investment principles[74] have been endorsed by the Victorian Government to guide the development of discretionary grants programs:

- grants should only be used when they secure a government policy outcome;
- discretionary grants should not be used without first considering alternative policy mechanisms or existing grant programs;
- grants should not be used with the principal objective of transferring revenue to local government;
- care should be taken to ensure grants do not lead to State Government overreach into Local Government's areas of responsibility, nor create an ongoing need for funding;
- grants programs should be designed to minimise administration costs;
- when small grants are used, they should be administered by the organisation that is able to do so most efficiently;

74 http://www.dtf.vic.gov.au/Publications/Government-Financial-Management-publications/Financial-Management-Compliance-Framework/Investment-principles-for-discretionary-grants

- accountability requirements imposed on grant recipients should be proportionate to risk;
- grants can be disbursed by competitive, negotiated or allocated mechanisms; and
- Better Grants by Design[75] should be used to provide further guidance when designing and developing new grant programs.

Better Grants by Design[75] may also assist in considering, making and managing other discretionary financial benefits to achieve program objectives.

Sponsorships

Sponsorship is the purchase or receipt of rights or benefits, including naming rights, delivered through association with an organisation's products, services or activities. The rights or benefits typically relate to the sponsor's reputation management or communication objectives.

Sponsorship includes partnership arrangements, except when the arrangement is governed by the Partnerships Victoria Requirements 2013[76] or otherwise involves the development or management of infrastructure.

Departments are required to develop their own Agency-specific sponsorship procedures based on, and consistent with, the principles identified in the Victorian Government Sponsorship Policy[77].

Donations

Donations or bequests are gifts given, typically for charitable purposes and/or to benefit a cause. They impose no obligations on the recipient and offer little or no rights or benefits to the provider. Most Agencies will rarely give or receive a donation.

Under Direction 4.2.2(b), donations must be subject to effective and efficient administrative controls. More broadly, donations must be subject to proper financial management, such as Direction 3.2, requiring an effective internal control system to ensure efficient operations and safeguard resources. Due to the nature of donations, giving or receiving a donation would normally require a strong rationale and a high level of approval within an Agency. Agencies that more regularly deal with donations, such as some arts agencies, should have more detailed policies and procedures in place.

Gifts, benefits and hospitality

Gifts, benefits and hospitality are not forms of discretionary financial benefits. The Gifts, Benefits and Hospitality Policy Framework[78] sets out the State's framework for gifts, benefits and hospitality given or received by Agencies and their staff.

[75] https://www.intranet.vic.gov.au/connect/better-grants-design

[76] http://www.dtf.vic.gov.au/Publications/Infrastructure-Delivery-publications/Partnerships-Victoria/Partnerships-Victoria-Requirements

[77] http://www.dpc.vic.gov.au/index.php/communication/policies-and-guidelines/sponsorship-policy-introduction-application-and-definitions

[78] http://vpsc.vic.gov.au/resources/gifts-benefits-and-hospitality-policy-framework/

Guidance 5.1 – Financial management compliance

Objective	Provides guidance on the financial management compliance framework requirements and the review and reporting of compliance including transitional arrangements
Effective date	1 July 2016
Relevant Direction	5.1 Financial management compliance
Last reviewed date	1 February 2016

Financial management compliance framework

Australian standard on compliance

Agencies are encouraged to adopt Australian Standard ISO 19600:2015 *Compliance Management Systems – Guidelines* (the Standard) in establishing a financial management compliance framework.

The objective of the Standard is to provide guidance for establishing, developing, implementing, evaluating, maintaining and improving an effective and responsive compliance management system within an Agency.

The Standard does not specify requirements, and is intended to be adaptable. Its use may differ depending on the size and level of maturity of an Agency's compliance managements system and on the context, nature and complexity of the Agency's activities, including its compliance policy and objectives.

ISO 19600:2015 references seven key themes:

- context of the organisation;
- leadership;
- planning;
- support;
- operation;
- performance evaluation; and
- improvement.

Detailed review of all obligations

Many Agencies have historically involved their Internal Audit function in reviewing financial management compliance. Direction 5.1.3 makes this a mandatory requirement.

A detailed review of individual obligations is required, at minimum, once every three or four years. A detailed review involves an in depth analysis and testing of sample documents, transactions and the gathering of evidence and substantiation to support conclusions on compliance levels.

The internal auditor is to prepare and maintain a strategic internal audit plan and an annual audit work program based on the risks and controls of the Agency (refer to Guidance 3.2.2 *Internal Audit* on information about the strategic internal audit plan). This provides for an independent objective assessment of compliance.

From 2016-17, as part of the strategic internal audit plan, Internal Audit is to develop a detailed financial management requirement review schedule based on a high level assessment of compliance gaps and risks. The detailed review schedule is to be reviewed and refined during each subsequent year based on a reassessment of any compliance gaps and/or risks.

A risk-based approach to prioritising and planning the detailed review of compliance should occur when preparing and refreshing the strategic internal audit plan and annual audit work program (refer to Direction 3.2.2 *Internal Audit*). The resulting plan and program should outline the type and frequency of detailed reviews and any targeted assessments. High compliance risk areas for the Agency should be given higher priority for audits including greater frequency. For example, areas assessed as high compliance risk require more frequent reviews than areas of lower compliance risk, which should be reviewed at least once every three to four years. By adopting risk-based audits covering multiple obligations from a single audit event can further remove duplicating effort.

Reports from detailed reviews should be provided to the Audit Committee for review and monitoring of agreed rectification and remedial actions. For further information on the role, refer to Direction 3.2.1 *Audit Committee*. The findings of detailed reviews should be used to inform the annual assessment of compliance (further information provided below).

Agencies are to submit a summary of their internal audit detailed financial management requirement review plan to their Portfolio Department and Audit Committee.

Annual assessment and attestation of compliance

Under the 2003 Directions, Agencies prepared an internal attestation of compliance within Government. A key change is that all Agencies will be required to make a public attestation in their annual report on compliance with the financial management obligations. This new requirement will be introduced over a two year period to ensure Agencies have systems in place to support public attestation in 2018 for the 2017-18 financial year.

What is a Compliance Deficiency?

The Directions and Instructions include two concepts in relation to a failure to fully comply with a requirement in the FMA, Directions or Instructions:

Concept	Definition	Requirements
Compliance Deficiency	An attribute, condition, action or omission that is not fully compliant with a requirement in the FMA, Directions and/or Instructions (Direction 1.6).	• Must be addressed (Direction 5.1.5). • Must be reported to Portfolio Department in compliance report (Instruction 5.1, clause 1.2). • Key areas of Compliance Deficiency must be reported by Portfolio Department to DTF in portfolio compliance summary (Instruction 5.1, clause 1.4).
Material Compliance Deficiency	A Compliance Deficiency that a reasonable person would consider has a material impact on the Agency or the State's reputation, financial position or financial management (Direction 1.6).	All requirements in relation to compliance deficiencies set out above apply, and additionally: • Must be notified to Responsible Minister and Portfolio Department. Independent Offices must discuss with DTF (Direction 5.1.6). • Must be included in financial management compliance attestation in Annual Report (Direction 5.1.4).

In preparing their Annual Report attestation, an Agency must identify which of its Compliance Deficiencies are 'Material Compliance Deficiencies'. The definition, set out in the table above, involves an objective 'reasonable person' test. The question is whether a reasonable person would consider the deficiency to be material to the State or Agency's reputation, financial position or financial management. For example, a very small number of missing taxi receipts in the course of a year is unlikely to constitute a Material Compliance Deficiency. But the absence or failure of a system or control, or a systemic failure in relation to a certain system, is likely to be material.

Annual assessment and attestation processes and timelines

The annual assessment of compliance with the Directions takes into consideration information from various sources. These could include:

- current and previous detailed reviews of obligations conducted and actions taken since to rectify any failure or deficiency, when appropriate;
- any targeted assessments which may be conducted as a result of:
  - changes to requirements or operating environment considered high risk to complement previous detailed reviews (for example, a change to GST legislation on appropriations or an organisation change of the finance function), and
  - Material Compliance Deficiencies identified during the year;

- outcomes from monitoring and analysing planned and unexpected changes to the business and operating environments and the impact on compliance with obligations since last annual assessment;
- any compliance deficiencies reported during the year;
- information from regular reviews of risk during the year (refer to Direction 3.7.1, dealing with risk management); and
- issues, queries and feedback from the Audit Committee throughout the year.

It is expected that Agencies will take a practical, risk-based approach to demonstrating compliance. This is particularly relevant to those Directions that require Agencies to achieve broad principles of good financial management. An example is Direction 2.2(a), which requires the Responsible Body to ensure that the Agency furthers government objectives and priorities. Reasonable evidence for compliance with such a requirement could include a brief summary of significant Government priorities that the Agency has pursued in the relevant year. It would usually be unnecessary to undertake a detailed analysis of all actions taken under such requirements.

The annual assessment is then provided to the Audit Committee whose responsibility is to review and monitor agency compliance. Information on compliance levels will support analysis to be contained in the assessment report and submitted to the Accountable Officer of Portfolio Departments by **15 September** for agencies for with an annual reporting period ending 30 June (**15 March** for agencies with an annual reporting period ending 31 December).

In preparing their assessment, Agencies should document a summary of the:

- the levels of compliance achieved;
- Compliance Deficiencies;
- action to be taken to remedy compliance deficiencies and timeframes;
- an assessment of the most significant compliance risks for the Agency; and
- proposed plan/schedule of internal audit detailed financial management requirement reviews over the next three to four years.

The Committee then recommends to the Responsible Body the proposed compliance levels and mitigation strategies. Further information on the role of the Audit Committee is provided in Direction 3.2.1.

Direction 1.4.5 and Instruction 5.1 set out transitional arrangements for attestation in relation to 2015-16, 2016-17 and onwards.

For the 2016-17 transitional year, a separate risk management and insurance attestation is required to continue in the Annual Report under Direction 3.7.1 and clause 3.2 of the *Victorian Government Risk Management Framework* (VGRMF). A template attestation is included at pages 64 and 65 of the *2016-17 Model Report for Victorian Government Departments*.

The requirements are summarised in the tables below for Agencies with 30 June balance dates and 31 December balance dates.

Agencies with 30 June Balance Dates			
Compliance Year	**2015-16**	**2016-17**	**2017-18 onwards**
Compliance Assessment	Assessment conducted for the year ended **30 June 2016**	Assessment conducted for the year ended **30 June 2017.**	Assessment conducted for the compliance year ending **30 June**.
Compliance Report	Report provided to the Responsible Minister in accordance with the 2005 FMCF (by **30 September 2016**).	Report provided to the Portfolio Department by **15 September 2017**, including: (a) a trial attestation in the form set out under Instruction 5.1, Clause 5.2; and (b) a progress update on actions taken by the Agency to prepare for commencement of transitional Directions under Direction 1.4.	Report provided to the Portfolio Department by **15 September** after end of compliance year.
Public Attestation	No public attestation in annual report except for risk management as set out in 2003 Direction 4.5.5.	No public attestation in annual report except for risk management as set out in 2016 Direction 3.7.1 (a template attestation is provided in the *2016-17 Model Report for Victorian Government Departments*).	Agencies must complete a full public attestation in relation to all applicable 2016 Directions and Instructions in the annual report (by Instruction 5.1, clause 2). The above annual assessment process and detailed reviews by internal audit will continue to support this public attestation. Note: The previous risk management and insurance attestation (Direction 3.7.1) will cease in 2017-18 and become part of the overarching public attestation with the Directions.

Agencies with 31 December Balance Dates			
Compliance Year	**2016**	**2017**	**2018 onwards**
Compliance Assessment	2003 Directions: Assessment conducted for the period ended 30 June 2016. 2016 Directions: Conducted early in 2017 for the period 1 July 2016 to 31 December 2016.	Assessment conducted for the year ended **31 December 2017** in early 2018.	Conducted for the compliance year ending **31 December** early in the following year.
Compliance Report	2003 Directions: Report provided to the Responsible Minister in accordance with the 2005 FMCF (by **30 September 2016**). 2016 Directions: Report provided to Portfolio Department by **15 March 2017** (in relation to the **six** month period ending 31 December 2016), including: (a) a trial attestation in the form set out under Instruction 5.1, Clause 5.2; and (b) a progress update on actions taken by the Agency to prepare for commencement of transitional Directions under Direction 1.4.	Report provided to the Portfolio Department by **15 March 2018**.	Report provided to the Portfolio Department by **15 March** after end of compliance year.
Public Attestation	No public attestation in annual report except for risk management as set out in 2003 Direction 4.5.5.	For the period **1 January 2017 to 30 June 2017** – public attestation in annual report for risk management as set out in 2016 Direction 3.7.1 (a template attestation is provided in the *2016-17 Model Report for Victorian Government Departments*). For the period **1 July 2017 to 31 December 2017** – public attestation in annual report as required by Instruction 5.1, clause 2. Accordingly, the 2017 annual report will include two separate attestations, one for each period.	Agencies must complete a full public attestation in relation to all applicable 2016 Directions and Instructions in the annual report (by Instruction 5.1, clause 2). The above annual assessment process and detailed reviews by internal audit will continue to support this public attestation. Note: The previous risk management and insurance attestation (Direction 3.7.1) will cease in 2018 and become part of the overarching public attestation with the Directions.

In the event an agency has an annual reporting balance date other than 30 June or 31 December, compliance assessment and reporting obligations must occur within **75 days** of the balance date, under Instruction 5.1, clause 1.1 (c). For example, for an agency with a **31 October** annual reporting date the following timeframes apply for the 2016 Directions:

- **2016** - initial compliance assessment conducted for period 1 July 2016 to 31 October 2016 with compliance report provided to portfolio department by **14 January 2017**. A risk management attestation for the whole year, under 2003 Direction 4.5.5, must be completed;
- **2017** - compliance assessment conducted for period 1 November 2016 to 31 October 2017 with compliance report to portfolio department by **14 January 2018**. The 2017 annual report will include two attestations, one for risk management, under 2016 Direction 3.7.1, for the period **1 November 2016 to 30 June 2017** and one for compliance with all 2016 Directions for the period **1 July 2017 to 31 October 2017**; and

- **2018 and onwards** - compliance assessment conducted for the period 1 November to 31 October each year with a compliance report provided to the portfolio department by 14 January in the following year. One attestation will be completed in the annual report for all compliance obligations.

The Victorian Management Insurance Authority[79] (VMIA) has developed a number of overarching principles and a range of guidance material in support of risk attestation processes for Agencies. Some of these key principles also apply to compliance attestation and include:

- attestation is intended to provide 'assurance' or demonstrate 'performance' – it should not be merely a box-ticking exercise;
- keep the attestation framework and process as pragmatic and relevant as possible; and
- the Agency's risk maturity, size, complexity and risk appetite needs to be considered, because 'attestation is relative to maturity.'

Portfolio Department compliance role

As is currently the case, Portfolio Departments have a significant role in supporting the portfolio Ministers in their oversight of the portfolio as a whole, and of Agencies individually (see Directions 2.3.4 and 2.4.4, and Instruction 2.3.4 for more details on this role). This role is consistent with the Responsibility of Department Heads (Accountable Officer) in section 13A of the *Public Administration Act 2004*, introduced in 2014.

As a key part of this role, Portfolio Departments are to monitor the compliance of their Portfolio Agencies and provide advice on the level of assurance with financial management requirements (including the FMA, Directions and Instructions) to their Ministers and DTF including the identification of key portfolio Compliance Deficiency risk issues and remedial actions proposed (see Instruction 5.1, clause 1.4). This may also involve a departmental review of portfolio Agencies' internal audit detailed financial management requirement review plans/schedules to ensure appropriate coverage and to identify areas of potential compliance risk, particularly during the transition period.

A Portfolio Department is to review annual Agency compliance assessment reports and to work with Agencies to improve compliance performance and manage Compliance Deficiency risks. This process will help inform the portfolio summary compliance report to Minsters and DTF.

For 2016-17 onwards annual portfolio summary reports are to be provided to DTF **by 31 October** following the year reviewed (including the 2016-17 transitional year). The contents, as per Instruction 5.1, should, at a minimum, include:

- the levels of compliance achieved across the portfolio (including within the Portfolio Department as an Agency, and all Portfolio Agencies);
- key areas of Compliance Deficiency across the portfolio, including planned and completed remedial actions and timeframes of the Agencies and Portfolio Department; and
- an assessment of the significant compliance risks facing the portfolio, including key strategies of the Agencies and the Portfolio Department to mitigate these risks.

For 2017-18 onwards, Portfolio Departments should also review the annual attestation statement in Agencies' annual reports to ascertain whether they are an accurate assessment of their level of compliance.

Department of Treasury and Finance whole of State role

From 2016-17, DTF will establish oversight arrangements including:

- face to face meetings with Portfolio Departments;
- reviewing of whole of state compliance and identify strategies to improve levels of compliance;
- an assurance program, either on site or desktop based;
- analysing portfolio compliance summary reports and other data to identify improvements;
- working with Portfolio Departments to improve compliance performance and the management of risks in the lead up to Agency public attestation in 2017-18;

[79] https://www.vmia.vic.gov.au/

- reporting to the Minister for Finance on whole of state progress on achieving compliance with the new Directions by **15 December** each year;
- publishing a summary whole of state compliance report on the DTF website subsequent to the Minister's review for 2015-16 and 2016-17 (and further years as requested by the Minister); and
- proposing changes to the Directions, Instructions and Guidance to the Minister for Finance when required from improved practices identified, mitigating risks or improving Agency understanding of requirements.

Transitional compliance expectations for all Agencies

The following table guides Agencies in transitioning to some of the key requirements in relation to compliance with the Directions and Instructions.

Compliance elements	**2016-17 compliance year – Year 1** **Internal compliance attestation**	**2017-18 compliance year – Year 2** **External compliance attestation**
Establish compliance framework	Develop internal compliance framework and commence implementation.	Embed internal compliance framework.
Initial assessment of compliance gaps and risks	Initial high level assessment of compliance to: • identify compliance gaps and actions required; and • inform internal audit detailed compliance review schedule.	
Internal audit detailed financial management requirement review schedule (Audit Committee approval)	Develop internal audit detailed review plan/schedule based on high level assessment of compliance gaps and risks.	Review and refine internal audit detailed review schedule.
Annual Assessment of compliance	Determine approach for assessment. Complete first annual assessment of compliance.	Review and refine approach for assessment (including Portfolio Department feedback).
Internal Audit detailed reviews of compliance	Commence detailed review of financial management requirements as per internal audit plan and schedule.	Ongoing detailed compliance reviews.
Audit Committee review, monitoring and assurance of compliance	Enhance Audit Committee's involvement in compliance.	Audit Committee to provide assurance as to level of compliance for attestation.
Annual Agency compliance assessment report to Portfolio Department by 15 September (15 March for 31 December Balance date agencies)	Compliance assessment report to Portfolio Department (and Responsible Minister).	Review effectiveness of compliance assessment report to Portfolio Department (and Responsible Minister) and refine (including Portfolio Department feedback).
Annual public attestation in annual report	**Internal to government** Trial attestation statement. Additional information on compliance issues/risks and assessment of implementation progress, including target compliance level by Year 2.	**First year of public attestation** Public attestation statement in annual report.
Education and information dissemination of Directions across Agency	Communication and training across the Agency including specific roles (e.g. Audit Committee, Internal Audit, Accountable Officer).	Ongoing communications and training.

Transitional compliance expectations for Portfolio Departments

The following table guides Portfolio Departments in transitioning to some of the key requirements in relation to compliance with the Directions and Instructions.

Compliance elements	2016-17 compliance year – Year 1 Internal compliance attestation	2017-18 compliance year – Year 2 External compliance attestation
Financial management compliance of portfolio Agencies	Enhance compliance model/arrangements with Agencies.	Review effectiveness and refine compliance model/ arrangements with Agencies.
	Review summary of Agency's internal audit detailed financial management requirement review plan/schedule for appropriate coverage and identify areas of compliance risk (in Responsible Minister's brief).	Review Agency's summary of internal audit detailed financial management requirement review plan/schedule for appropriate coverage and identify areas of compliance risk (in Responsible Minister's brief).
	Enhance reporting mechanism to Responsible Minister's on individual/ portfolio issues/compliance report.	Review effectiveness of reporting mechanisms on individual/ portfolio issues/compliance report (including public attestation) to the Responsible Minister and refine.
Annual Agency compliance assessment report	Review annual Agency compliance assessment reports. Work with Agencies to improve compliance performance and manage non-compliance risk.	Review effectiveness of annual Agency compliance assessment reports. Work with Agencies to improve compliance performance and manage non-compliance risk.
Annual Portfolio summary report to DTF by 31 October	Enhance current Portfolio compliance summary report to meet requirements.	Review effectiveness of portfolio summary report and refine (including DTF feedback).

Transitional compliance expectations for DTF

The following table provides guidance as to how DTF intends to transition to some of the key requirements in relation to compliance with the Directions and Instructions.

Compliance elements	**2016-17 compliance year – Year 1 Internal compliance attestation**	**2017-18 compliance year – Year 2 External compliance attestation**
Compliance oversight	Enhance compliance oversight model/arrangements with Portfolio Departments.	Review effectiveness and refine compliance oversight model/arrangements with Portfolio Departments.
	Work with Portfolio Departments and review portfolio oversight/ assurance arrangements.	Review with Portfolio Departments the effectiveness portfolio oversight/ assurance arrangements and refinements.
	Review identified portfolio Compliance Deficiency risk issues and remedial actions proposed.	Review identified material portfolio Compliance Deficiency risk issues and remedial actions proposed.
	Establish reporting mechanism to Minister for Finance on compliance.	Refine reporting mechanism to Minister for Finance on compliance.
DTF Assurance program	Reassess approach, objectives and risks. Refine current process.	Review effectiveness of approach etc. and refine program.
Annual assessment of Portfolio compliance summary report	Analyse Portfolio compliance summary report and identify improvements. Work with Portfolio Departments to improve portfolio/agency compliance performance for public attestation and management of risks.	Analyse Portfolio compliance summary report and identify improvements. Work with Portfolio Departments to improve portfolio/Agency compliance performance for public attestation and management of risks.
Annual assessment of compliance across VPS and currency of framework (including Directions, Instructions and Guidance)	Advise Minister on compliance levels, issues, risks, proposed amendments to Directions, progress on implementation and strategies.	Advise Minister on compliance performance, public attestation outcomes, strategies and amendments to Directions.
	Amend/refine and reissue Directions, Instructions and Guidance as required.	Amend/refine and reissue Directions, Instructions and Guidance as required. Implement agreed strategies.

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