

# 2013-14 Results of the Victorian Public Hospital Audits

25 February 2015

The Victorian Auditor-General's Office (VAGO) has today released the results of the financial audits of Victoria's public hospital sector, made up of 87 public hospitals and 23 associated entities. This bulletin is a summary of the key findings. The full report and associated material can be accessed via [http://www.audit.vic.gov.au/reports\\_and\\_publications/latest\\_reports/2014-15/20150225-public-hospitals.aspx](http://www.audit.vic.gov.au/reports_and_publications/latest_reports/2014-15/20150225-public-hospitals.aspx).

Ordinarily these reports would be tabled in November of each year, but this was deferred to February 2015 for the 2014 report due to the state election.

## Quality of Reporting

VAGO commented that financial reporting by Victorian public hospitals was more timely and accurate in 2013-14 compared to the previous audit.

## General Internal Controls

Internal controls of the public hospital sector were assessed by VAGO as appropriate for ensuring accuracy for external reporting. Any identified internal control weaknesses of individual organisations have been formally communicated from VAGO. The common internal weaknesses identified across all organisations were lack of timely review of key reconciliations, and lack of appropriate authorisation of supplier payments. Of the 358 internal control weaknesses identified during the audit process in 2012-13, 30 per cent were yet to be resolved.

## Financial Sustainability Risks

In total, over the 2013-14 period, the public hospital sector managed a total expenditure budget of \$12.6 billion, and delivered a surplus of \$235 million.

VAGO has assessed the financial sustainability of the sector as "medium", which is consistent with the assessment of the previous audit period but reflects VAGO's concerns about financial sustainability risks. In particular, an increased number of organisations within the sector (32 compared to 28 in 2012-13) are at risk of not being able to meet their financial obligations over the coming 12 months. In order to mitigate this risk, the Department of Health provided letters of financial support to these organisations, committing the Department of Health and Human Services (as it is now known) to provide financial support to these organisations should this be required, until September 2015. It is important to note that this does not constitute additional funding, but is considered financial assistance in the case of financial difficulties.

The future challenges for the public hospital sector are recognised by VAGO, which acknowledges the need for financial sustainability to meet expenditure requirements, and to replace and maintain assets as necessary. VAGO identifies that many public hospitals operate with significant financial sustainability risks, which, is primarily a result of tight cash positions. For example, 12 of the 87 public hospitals hold only enough cash reserves to operate for a maximum of seven days if planned cash income is delayed. Furthermore, if within this seven day period such organisations did not receive a grant payment, they would be required to seek alternative sources of funding (including recallable grants from the Department of Health and Human Services).

The VAGO report shows that the majority of public hospital services (70 per cent) are not renewing fixed assets as they are being used, as measured through depreciation. This leads to a poor capital replacement risk result, and is especially true in rural areas. With asset valuations occurring every five years, and last conducted in 2013-14, it is expected that public hospitals will need to meet increased depreciation costs by 30 June 2015. However, the funding model does not provide progressive funds for public hospitals to match asset depreciation.

Notably, VAGO comments that the “mismatch between the governance and funding models blurs accountability for the financial performance of individual hospitals” (p. 19), particularly in regards to capital management.

### Internal Audit

Public hospitals were shown to spend \$4 million on internal audit functions, which equates to 0.03 per cent of total sector expenditure. However, two hospitals were noted to lack an internal audit function, and have been informed of this issue.

VAGO notes areas that require improvement across all organisations:

- Management of potential and actual conflicts of interest, which could affect the independence of internal auditors,
- Collaboration with internal auditors to develop audit plans that provide assurance that all key risks for each organisation are addressed,
- Alignment of audit plans with organisational risk registers,
- Controls over cash management,
- Controls over asset management,
- Data security, and
- Data quality.

### Asset Maintenance

During 2013-14, VAGO found that the public hospital sector operated \$11.9 billion of assets, and spent \$232 million maintaining these assets. Maintenance costs increased from \$212 million in 2012-13. Forty eight public hospitals did not have an asset maintenance policy or strategy, and most of these 48 did not have adequate internal reporting to assess maintenance spending, risk management, funding plans or life cycle maintenance and costing. Rural hospitals were noted to spend a significantly smaller proportion of their net asset base on asset maintenance compared to their metropolitan and regional counterparts.

## Audit Recommendations

### **That public hospital boards and management:**

1. Review their financial reporting processes to address the better practice report preparation elements, including the timely preparation of shell financial statements
2. Address all issues raised in audit management letters on a timely basis, including ongoing concerns regarding the need to improve controls around key account reconciliations, the authorisation of supplier payments, and the regular review of financial and information technology policies
3. Through audit committees, implement appropriate monitoring mechanisms to ensure audit findings are resolved by management on a timely basis
4. Maintain good cash management processes to ensure that they are able to meet their financial obligations as they fall due, particularly for those public hospitals assessed as having a high liquidity risk
5. Work with the Department of Health and Human Services to ensure they are able to renew ageing assets as required to prevent any loss of services provided to the public.

### **That Dunmunkle Health Service and Casterton Memorial Hospital:**

6. Establish and maintain an internal audit function.

### **That public hospital boards and management:**

7. Have in place stand-alone internal audit charters that provide a clear framework for the selection, operation and oversight of the internal audit function.
8. Establish a process for the identification, communication, assessment and mitigation of conflicts of interest between internal audit and the public hospital
9. Work with their internal audit function to develop and implement a three-year audit plan that is approved by the audit committee, and which aligns with the risks identified in the hospital's risk register
10. Review their internal audit plan to ensure that the internal audit function is providing the level of assurance required
11. Undertake annual performance reviews of the internal audit function to ensure it continues to operate in line with the internal audit charter
12. Implement better practice asset management strategies to provide a framework for asset maintenance decisions
13. Undertake comprehensive asset condition assessments to enable individual asset maintenance plans to be created and actioned
14. Maintain comprehensive and appropriate information regarding asset maintenance requirements to assist in strategic asset management planning.