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|  | Paper No.: 5412T1426 I                                    |  |
|   | Date: 31/10/12  |  |
|   | Member: <i>M. Palazzo</i>                                 |  |
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CABINET BUDGET REVIEW COMMITTEE

DECISION

Brisbane, 29 August 2011

Decision No.: 3279, (Submission No.: 4242)

TITLE: Impact of salary overpayments on Queensland Health 2010-2011 Annual Financial Statements

COMMITTEE decided:

To note Queensland Health's preferred option (Option 1) to retain the 2010-2011 Financial Statements in their current form i.e. to record an employee overpayment receivable of \$69.048 million, associated impairment of \$17.372 million and show an overall surplus of \$2.285 million for the 2010-2011 financial year.

CIRCULATION: Implementation Responsibility  
 Department of Health and copy to the Minister for Health  
Departmental Records  
 Department of the Premier and Cabinet  
 Treasury Department  
Perusal and Return  
 All other Committee Members

*ASL*  
Cabinet Secretary



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**SECURITY CLASSIFICATION "C"****SUBMISSION TO CABINET BUDGET REVIEW COM****COVERSHEET****TITLE**

Impact of salary overpayments on Queensland Health 2010-2011 Annual Financial Statements.

**MINISTER**

Minister for Health

**OBJECTIVE**

To seek Cabinet Budget Review Committee endorsement of Queensland Health's preferred option with respect to the accounting treatment of salary overpayments in the 2010-2011 Financial Statements and the consequential audit opinion.

To advise Cabinet Budget Review Committee that even if the salary overpayment accounting treatment is resolved to the satisfaction of the Auditor-General, there remains a likelihood that Queensland Health's Financial Statements may be qualified due to the valuations of Queensland Health facilities. This was raised for the first time on the afternoon of 24 August 2011.

**SUMMARY**

Queensland Health has previously advised the Government of the \$69.048 million salary overpayments for the financial year ending 30 June 2011. With respect to salary overpayments, Queensland Health has currently recorded an impairment provision of \$17.372 million for potential unrecoverable overpayments. The impairment provision is not a write-off of employee overpayments, but recognition that a proportion of the salary overpayments may not be recovered.

Ongoing dialogue with Queensland Audit Office (QAO) has indicated that total overpayments and the associated impairment cannot be verified and therefore a qualification will be included in the audit opinion if left unadjusted.

QAO has indicated that it has concerns regarding the recognition of the salary overpayments recorded as a receivable on the Balance Sheet. QAO proposes that approximately \$52 million of the salary overpayment balances should be derecognised as an asset until acknowledged by employees as a debt and therefore recorded as a salaries and wages expense (in the Profit and Loss Statement) (refer **Attachment 1**). The impairment provision should be reduced by approximately \$16 million. These proposed adjustments would have a net impact of approximately \$36 million to the Profit and Loss Statement and would result in an overall budget deficit of approximately \$34 million for 2010-2011.

Although not formally advised, other issues that the Auditor-General had raised as potential reasons of audit qualification around payroll, including failure to locate supporting documentation and the inability to successfully perform a high level analytical review, have since been resolved. In addition, the Auditor-General has noted a significant improvement in the fortnightly payroll outcome.

On the afternoon of the 24 August 2011, Queensland Audit Office (QAO) staff raised the issue that the Financial Statements may be qualified due to the approach undertaken for the valuation of Queensland Health facilities. There have been progressive discussions with QAO staff since this issue was first raised in April 2011. In addition, the approach to valuation had previously been agreed with QAO staff, however, it is understood that the Auditor-General has the capacity to form a view that is inconsistent with that of QAO staff.

### OPTIONS

Option 1 – Retain Financial Statements in their current form as outlined in paragraphs 37 to 38 below.

Option 2 – Adjust the Financial Statements as outlined in paragraphs 39 to 50 below.

### RESULTS OF CONSULTATION

- **Is there agreement? YES.** See paragraphs 47 to 50 of body of submission.

### RECOMMENDATIONS

That Cabinet Budget Review Committee note Queensland Health's preferred option (Option 1) to retain the 2010-2011 Financial Statements in their current form (i.e. to record an employee overpayment receivable of \$69.048 million, associated impairment of \$17.372 million and show an overall surplus of \$2.285 million for the 2010-2011 financial year).



**GEOFF WILSON MP**  
**Minister for Health**

26/08/2011

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**BODY OF SUBMISSION**

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**OBJECTIVE**

1. To inform Cabinet Budget Review Committee (CBRC) of the options with respect to the accounting treatment of salary overpayments in the 2010-2011 Financial Statements and the consequential audit opinion.

**BACKGROUND**

- **Context**

2. The issues arising from the implementation of the Queensland Health payroll system in March 2010 have required a concerted effort to address short, medium and long term issues.
3. A significant portion of the effort to date has been directed at seeking to resolve the technology issues to bring about stability and improve the quality of the pay outcomes. This focus has been reinforced through the recommendations contained in Queensland Audit Office (QAO) and Ernst & Young (EY) reports.
4. In June 2010, Queensland Health ceased the automatic recovery of overpayments, following union requests and a recommendation by the Queensland Industrial Relations Commission (QIRC), until the payroll system was stabilised.
5. In February 2011, consultation with unions regarding a recovery process of overpayments commenced.
6. In March 2011, an Employee Overpayments Program (EOP) was established to recover approximately \$62 million from around 38,000 staff (as at 30 June this totalled \$69.048 million). This included developing business processes, establishing analysis and recovery teams, implementing call centre systems and issues management systems.
7. Approximately 38,000 staff members were sent a notification letter in June 2011, outlining the overpayments and interim cash payments they had received prior to 16 May 2011. A call centre was provided to staff to answer questions around the calculation of overpayments.
8. On 9 July 2011, the Government announced a moratorium on the recovery of overpayments and made a commitment to strengthen the focus on processes to reimburse underpaid staff.
9. Queensland Health has prepared the 2010-2011 Financial Statements which were endorsed by the Audit and Risk Management Committee on 5 August 2011. QAO is comfortable with the evidence in support of the \$69.048 million salary overpayments

- in 2010-2011, however QAO is concerned around the accounting treatment of recording these as a receivable. There are also QAO concerns in respect of the potential recoverability of these overpayments.
10. Currently, the Financial Statements include an employee overpayment receivable of \$69.048 million and an impairment provision of \$17.372 million representing approximately 25% of overpayment receivables outstanding.
  11. QAO has indicated that the Auditor-General will qualify the Financial Statements if a significant proportion of the current receivables as recorded on the balance sheet are not recorded as salary and wages expense.
  12. It is understood that to avoid qualification, the Auditor-General expects approximately \$52 million (refer **Attachment 1**) to be written back against salaries and wages expense (i.e. increase the salaries and wages expense by approximately \$52 million) and record this as a contingent asset within the notes to the Financial Statements.
  13. The Auditor-General believes the receipt of salary overpayments is contingent on the employee agreeing with the value of the overpayment and contingent on the Government lifting the moratorium.
  14. In addition, it is understood that the Auditor-General expects the impairment provision should be reduced from \$17.372 million to \$1.521 million. The net amount of \$15.726 million represents interim cash payments of \$9.559 million and those employees who have agreed to repay \$6.167 million. Therefore, the net impact on the financial statements would be approximately \$36 million, leading to an overall budget deficit of approximately \$34 million, versus the current budget surplus of \$2.285 million.
  15. As outlined in **Attachment 1**, adopting the QAO preferred approach will necessitate an increase to the salaries and wages expense (in the Profit and Loss Statement) of approximately \$52 million. In addition, the impairment provision would decrease by approximately \$16 million. The net impact of these adjustments is approximately \$36 million to the Profit and Loss Statement.
  16. Queensland Health has examined the criteria within the relevant Accounting Standards and does not consider the employee overpayment receivables to be a contingent asset.
  17. A contingent asset is a 'possible asset' that arises from past events and whose existence will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the Department. A contingent asset is not recognised within the balance sheet or profit and loss statement, it is disclosed in the notes to the financial statements.

18. Employee overpayments are monies owing by employees to Queensland Health resulting from salary and wages overpayments and therefore are not considered to be contingent (possible) assets. Up until the moratorium was announced, these amounts were considered recoverable and a dedicated Team was in place to validate overpayment amounts for accuracy.
19. Although the moratorium has been announced, Queensland Health has an obligation to tax payers to recover amounts owed to the Department by employees and intends on pursuing recovery of these amounts. The recovery process will commence once underpayment strategies have been implemented. Therefore, Queensland Health does not consider employee overpayments to be contingent assets and as such the Financial Statements should remain in their current form (Option 1).

#### **Other Issues**

20. The Auditor-General is expected to provide a modified audit opinion on the Financial Statements that the Department has failed to satisfy the prescribed requirements to maintain an appropriate system of internal controls in relation to the payroll process. This is consistent with the 2009-2010 financial year.
21. The Auditor-General as a consequence of a recent review raised the issue that the accounts may have to be qualified due to:
  - the inability to locate the documentation (e.g. time sheets) to support employees' pay variations; and
  - an analytical review of employee costs in 2010-2011 resulted in QAO being unable to arrive at the amount shown in the financial statements.
22. Although not formally confirmed by the Auditor-General, the QAO has indicated that these issues have been addressed.
23. Payroll specific issues that were highlighted in the 2009-2010 audit and those highlighted in 2010-2011 are being progressively addressed by the Payroll Foundation Program.
24. In addition the Auditor-General has found a significant improvement in fortnightly payroll outcomes during the 2<sup>nd</sup> and 3<sup>rd</sup> reviews of the payroll, for the financial year.
  - **Previous Consideration by Cabinet**
25. In May 2011, Cabinet Budget Review Committee (Decision No. 03204) noted a waiver of Queensland Health salary overpayments for a cumulative amount up to and including \$200 between 1 July 2010 and 30 June 2011 which would benefit at least 22,000 employees at a cost of about \$1.7 million. This waiver was in addition to a similar waiver for the period 8 March to 30 June 2010.

- **Facility Valuations**

26. In March / April 2011, Queensland Health and Queensland Audit Office (QAO) discussed QAO's expectations with respect to the valuation of Queensland Health facilities. Queensland Health's approach has been to comprehensively revalue all facilities every 5 years. This requirement has now changed to every 1-2 years.
27. Because it was impossible at that date, to undertake market revaluations of all Queensland Health facilities, an approach was agreed between QAO staff and Queensland Health Finance. No issues have been raised with this approach and the valuations until the afternoon of the 24 August 2011 as part of the Auditor-General's review (as opposed to QAO's review) of the Financial Statements.
28. The results of the Auditor-General's review will not be known until 26 August 2011, although QAO staff have raised this as a potential qualification to the Financial Statements.

- **Date for Signing**

29. The Queensland Audit Office has confirmed that the Department must sign the Financial Statements by 31 August 2011. If the Financial Statements are signed after this date, an emphasis of matter may be included in the audit opinion.
30. The Queensland Audit Office has indicated that if the Auditor-General approves the Financial Statements he may also sign on the same day, or at a later date.

**URGENCY**

31. With respect to the 2010-2011 Annual Financial Statements, the Auditor-General proposes to provide his audit certificate on 19 August 2011.

**ISSUES**

- **Proposed Audit Opinion**

32. QAO has indicated that the Auditor-General will include a qualified audit opinion (outlining inherent uncertainty) with the current accounting treatment around the \$69.048 million salary overpayment receivables and the \$17.372 million provision for impairment currently recorded in the QH financial systems. This is due to the fact that the Auditor-General has indicated that a significant proportion (approximately \$52 million) of the overpayment receivable should be recorded as salaries and wages expenditure in the 2010-2011 financial statements.
33. In addition, the Auditor-General believes that the current economic and political climate leads him to have significant uncertainty regarding the Department's ability to recover the outstanding overpayments.
34. Any write back of the employee overpayment receivables could result in a public perception that these debts will not be pursued.

35. Of the approximate 38,000 staff who received an overpayment notification letter in June 2011, approximately 17,400 responses have been received by the Employee Overpayment Program (EOP). Of these, 25% of respondents (totalling \$6.167 million of overpayments) have agreed to repay. The remainder wish to query the quantum or do not accept that they have been overpaid.

### OPTIONS

36. There are two options for the employee overpayment receivables and associated impairment:

#### **Option 1 – No change to the 2010-2011 Financial Statements**

37. Retain the \$69.048 million employee overpayment receivable and the \$17.372 million impairment provision. This will result in no changes being made to the Financial Statements and Queensland Health reporting an overall budget surplus of \$2.285 million for 2010-2011.
38. Retaining the 2010-2011 Financial Statements in their current form will result in a qualified audit opinion. QAO has indicated that the qualification will outline the inherent uncertainty of the employee overpayment receivables and associated impairment balances.

#### **Option 2 – QAO Proposed Option – Including write back of Employee Overpayment Receivables to Salaries and Wages Expense and Reporting a Contingent Asset in the Financial Statements**

39. This option will result in a write back of approximately \$52 million in employee overpayment receivables against salaries and wages expense (or an increase in the salaries and wages expense) and a decrease in impairment expense of approximately \$16 million. This will result in a net impact to the Statement of Comprehensive Income (Profit and Loss Statement) of approximately \$36 million and will lead to a Queensland Health budget deficit of approximately \$34 million for 2010-2011.
40. Queensland Health believes the write back proposed by QAO to be excessive as the net receivable would be the absolute worst case scenario. The Department's view is that the current provisioning is appropriate.
41. The Notes to the Financial Statements will then record a contingent asset of approximately \$52 million, as the Auditor-General believes these amounts are 'contingent' on the employee accepting the value of the overpayment and the Government lifting the moratorium.
42. This option will result in an employee overpayment receivable of approximately \$17 million, an associated impairment provision of \$1.5 million and a contingent asset of approximately \$52 million. In addition, an overall budget deficit will be recorded totalling approximately \$34 million.



43. These figures are an indication based on discussions held between the Deputy Director-General Finance, Procurement and Legal Services Division and the Assistant Auditor-General and are not a firm QAO recommendation.
44. Reducing the receivable by writing back the overpayment receivables against salaries and wages could send a signal to overpaid employees that the Department is not expecting recovery.
45. Such a write back will be undertaken at a Departmental level as opposed to an employee level (i.e. significant work would need to be undertaken to determine those employee overpayments not expected to be recovered).
46. The current level of overpayments have not been subject to any income tax as Queensland Health has informed employees that they have been overpaid. This approach was agreed with the Australian Taxation Office (ATO).
47. Subsequent write-off of amounts have the potential to be subject to Fringe Benefits Tax that Queensland Health will be obliged to pay. Consequential write-back of amounts may give rise to a consequential Fringe Benefit outcome, or at the very least raise concerns with the ATO.
48. It is anticipated that this option will not result in a qualified audit opinion.
49. QAO has indicated that increasing the impairment provision alone will not remove the audit qualification.
50. Queensland Health considers Option 1 to be the most appropriate. This decision has been supported by Queensland Treasury.

#### CONSULTATION

- **Community**
51. Not applicable
- **Government**
- *Department of the Premier and Cabinet*
52. The Department of the Premier and Cabinet has been consulted.
- *Treasury Department*
53. Queensland Treasury has been consulted.
- *Other Departments*
54. Not applicable.

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**RESULTS OF CONSULTATION**

- 55. The Department of the Premier and Cabinet have no objections to the submission proceeding.
- 56. Queensland Treasury has indicated that it supports Option 1.

**RURAL/REGIONAL IMPACT STATEMENT**

- 57. Not applicable.

**EMPLOYMENT AND SKILLS DEVELOPMENT IMPACT STATEMENT**

- 58. Not applicable.

**CLIMATE CHANGE IMPACT STATEMENT**

- 59. Not applicable.

**FINANCIAL CONSIDERATIONS**

- 60. Refer to paragraphs 15 and 16 which highlight the impact on the Queensland Health 2010-2011 reported operating result in the Financial Statements, should the QAO proposal be adopted.

**IMPLEMENTATION**

- 61. Once the Cabinet Budget Review Committee has made a decision, Queensland Health Finance Branch will make the required amendments to the Financial Statements if required.

**PUBLIC PRESENTATION**

- 62. The Queensland Health 2010-2011 Financial Statements are due for publication in September 2011.
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**ADDENDUM**

**CONSULTATION DETAILS**

**Title of CBRC Submission:** Impact of salary overpayments on Queensland Health  
2010-2011 Annual Financial Statements.

| <b>DEPARTMENT</b>                     | <b>OFFICER</b>                    | <b>DATE</b> |
|---------------------------------------|-----------------------------------|-------------|
| Queensland Treasury                   | Janelle Thurlby & Jeanette Miller | 15.8.2011   |
| Department of the Premier and Cabinet | Justin Murphy                     | 16.8.2011   |

**LIST OF ATTACHMENTS**

**ATTACHMENT 1:** Estimated Employee Overpayment Receivables Spreadsheet

Queensland Health  
**QAO Preferred Adjustment - Employee Overpayments/Impairment**  
**For the year ending 30 June 2011**

|   | \$<br>`000             |  |
|---|------------------------|--|
| Interim Cash Payments                                   | 9.559                  |  |
| Agreed to Repay   | 6.167                  |  |
| Waiver  | 1.521                  |  |
| <b>TOTAL OVERPAYMENTS RECEIVABLE</b>                    | <u><u>17.247</u></u>   |  |
| Current Overpayments Receivable                         | 69.048                 | Per current Financial Statements   |
| Adjustment Required                                     | <u><u>51.801</u></u>   | Decrease Overpayment Receivables/<br>Increase Salaries and Wages Expense |
| <b>Provision for Impairment - Employee Overpayments</b> |                        |  |
| Waiver  | 1.521                  |  |
| <b>TOTAL IMPAIRMENT PROVISION</b>                       | <u><u>1.521</u></u>    |  |
| Current Impairment Provision                            | 17.372                 | Per current Financial Statements   |
| Adjustment Required                                     | <u><u>15.851</u></u>   | Decrease in Impairment Provision   |
| <b>QAO Proposed Adjustment</b>                          |                        |  |
| Receivables Adjustment                                  | <u><u>(51.801)</u></u> | Decrease Overpayment Receivables   |
| Impairment Adjustment                                   | 15.851                 | Decrease in Impairment Provision   |
| <b>Net Adjustment Proposed by QAO</b>                   | <u><u>(35.950)</u></u> | Net P & L Impact   |
| Current Surplus   | 2.285                  |  |
| <b>Estimated Deficit</b>                                | <u><u>(33.665)</u></u> |  |
| <b><u>Summary of Proposed QAO Changes</u></b>           |                        |  |
| Proposed Contingent Asset                               | 51.801                 |  |
| Proposed Overpayments Receivable                        | 17.247                 |  |
| Proposed Impairment                                     | 1.521                  |  |
| Proposed Overall Budget Deficit                         | (33.665)               |  |

