

**Department of Human Services
Funding and Financial Policy Branch
Metropolitan Health & Aged Care Services
Division**

***Guidelines for the
identification and
establishment of
Specific Purpose Funds***

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1. INTRODUCTION

Specific Purpose Fund (SPF) balances, as reported in the 1999/2000 annual accounts of Health Care Networks, contributed approximately \$230 million to the equity of metropolitan hospitals, the equivalent of almost 60 percent of the available liquid assets of those agencies.

The Ministerial Review of Health Care Networks, March 2000, identified a number of unsatisfactory aspects of hospital/health service management of SPFs, including:

- failure to distinguish between the types of funds in consolidated management reports and in financial statements;
- inappropriate accounting practices which have not matched revenue to expenditure across the three funds¹ over a number of years;
- inadequate recognition of the ‘trust’ nature of a number of SPFs;
- reliance on SPF revenues to support operations over a period of years, with the result that [liquid] asset backing for a number of SPF balances had been substantially eroded in many cases;
- failure to differentiate between the types of SPFs and accumulated impacts of inappropriate accounting practices meaning it is not possible to readily determine the implications of the nominal shortfall in liquid assets in meeting SPF obligations; and
- the impact on hospital/health service management of arbitrary restraints in the expenditure of SPF balances to assist in entity cash management not being adequately understood by agencies and the Department of Human Services (DHS).

In response, the Government’s Economic Review Committee determined that ‘*DHS issue guidelines on the management and usage of SPF cash flows to ensure hospitals meet SPF liabilities as and when they fall due*’. This requirement triggered the Review of SPFs undertaken by BDO Consulting Pty Ltd., which was completed in September 2001. A working group comprising a representative group of Chief Finance Officers from Metropolitan Health Services (MHSs), was established to provide guidance to the consultants in their Review.

The consultant’s Report on the Review of SPFs was used in developing these Guidelines. Sessions were also convened with MHSs and rural hospitals and health services to discuss and refine the draft Guidelines and review their practical application.

These guidelines have been prepared to assist agencies to:

- identify and categorise SPFs;
- develop business rules to manage SPFs such as recording, matching of revenue and expenses and reporting;
- formulate accounting policy, recording and reporting frameworks relevant to SPF accounts;
- monitor the asset backing and liquidity of SPFs to ensure that they are able to meet their obligations on their SPFs as and when they fall due; and
- “clean up” existing SPFs;

Hospitals/Health Services will be expected to fully implement these Guidelines by 30 June 2002.

¹ The three funds are the Operating Fund, Capital Fund and Specific Purpose Fund. These funds are more fully described in Attachment 1.

2. FUNDS

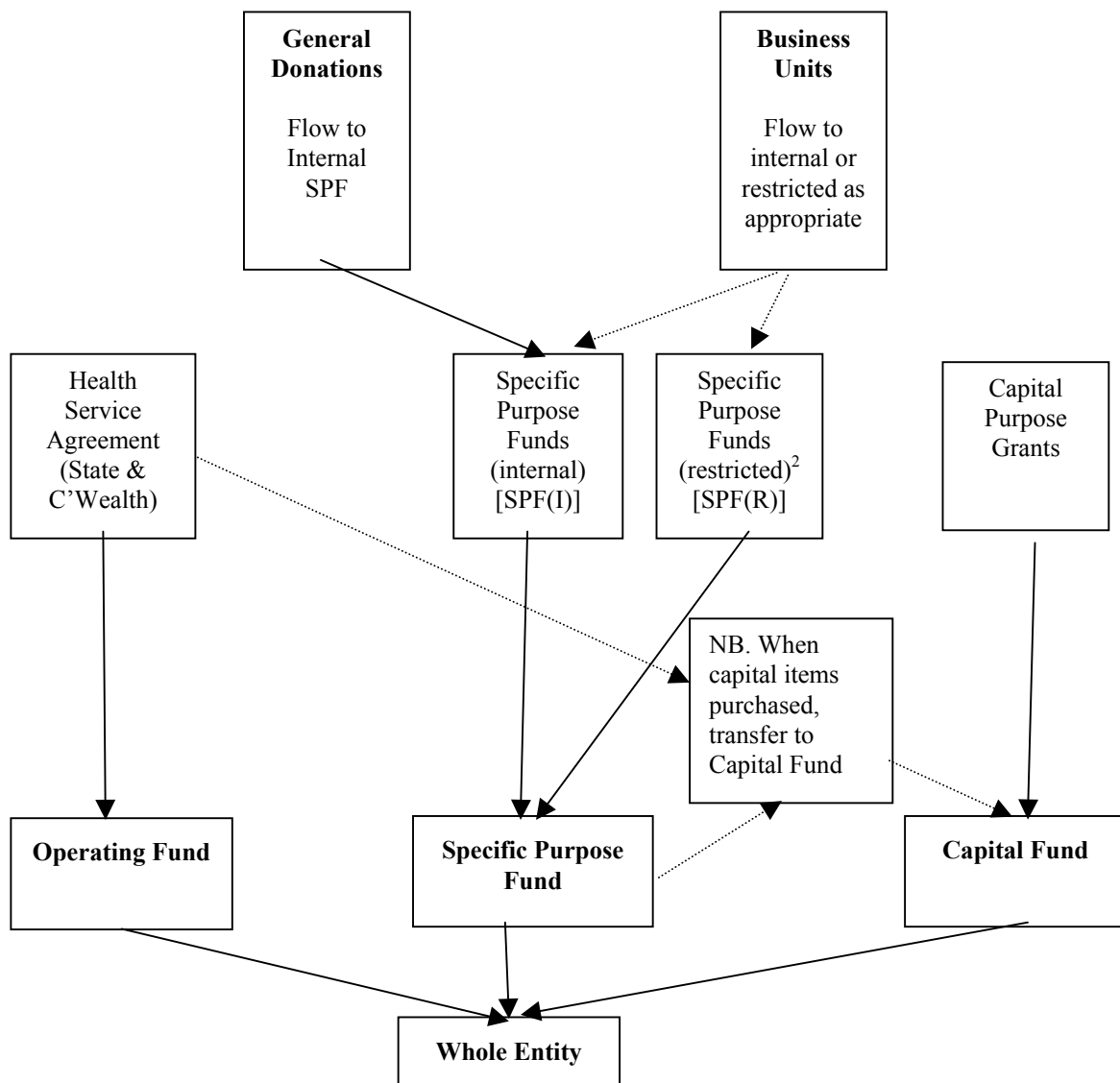
2.1 Background

All funding received by hospitals/health services is allocated to one of the following funds:

- (a) the Operating Fund;
- (b) the Capital Fund; or
- (c) the Specific Purpose Fund.

This distinction is set down in the DHS Finance and Accounting Manual for Public Hospitals –1996. Reporting to DHS using the Agency Information Reporting System (AIMS) is to include information drawn from the fund classification system as required by the Finance and Accounting Manual. This is depicted below:

2.2 Classification of Transactions by Fund



² The SPF(R) is more fully described in Attachment 2.

The entity result encompasses the activities of all three Funds. Information to be disclosed in the Equity section of the Statement of Financial Position should include the following:

- Contributed Capital.
- Retained Surplus or Accumulated Deficits.
- Revaluation Reserve.
- SPFs (Restricted).
- Other Reserves.

3. IDENTIFYING AND CATEGORISING SPECIFIC PURPOSE FUNDS

3.1 Introduction

SPFs fall into two broad categories namely internally managed funds [SPF(I)] and restricted funds [SPF(R)]. In the case of SPFs(R) hospitals have the responsibility to clearly document and record these funds and to provide resources and liquidity to meet the obligations of these funds as and when these are fall due. SPFs(I) refers to those funds over which the hospitals have management control as well as the discretion on the ultimate disposition of these funds. As the documentation / recording, reporting and liquidity requirements for these two categories of funds differ, it is essential that restricted SPFs are clearly identified and categorised.

3.2 Test of Type

The most satisfactory means of determining the type of fund and the final legal ownership of fund assets (and responsibility for liabilities) is to apply three tests:

1. How was the fund established?
2. Who has usual daily control over the fund's activities and has the authority to spend these funds?
3. Who ultimately owns the assets of the fund in the event of either winding up the hospital/health service or altering of its legal status?

These tests are further explained below with examples provided to assist understanding. A flowchart is also provided to help visualise the sequence of tests.

The answers to the above questions will determine in which SPF the transaction is recorded and whether the balance of the funds at the end of an accounting period is a liability or equity.

3.2.1 Establishment

How was the fund established? Was it:

- A form of legal instrument (including a commitment to a third party)?
- A decision to establish a commercial arrangement?
- A decision by the Board of Management (BoM) to allocate operational funds?
- The creation of a trust?
- A donation for a specific purpose?
- A general donation?
- A staff activity resulting in income (e.g. lecturing, a ward raffle, etc)?

The diagram in Section 3.3 shows how the answers to these questions influence the fund classification of the relevant transaction.

3.2.2 Management

On a day-to-day basis, who normally makes decisions on the activities of the fund? Is it:

- A separate board, committee or trustee?
- The committee of an auxiliary or fund-raising group?
- A head of a department or ward?
- A researcher or research group?
- The hospital/health service's Executive Group?
- The BoM?

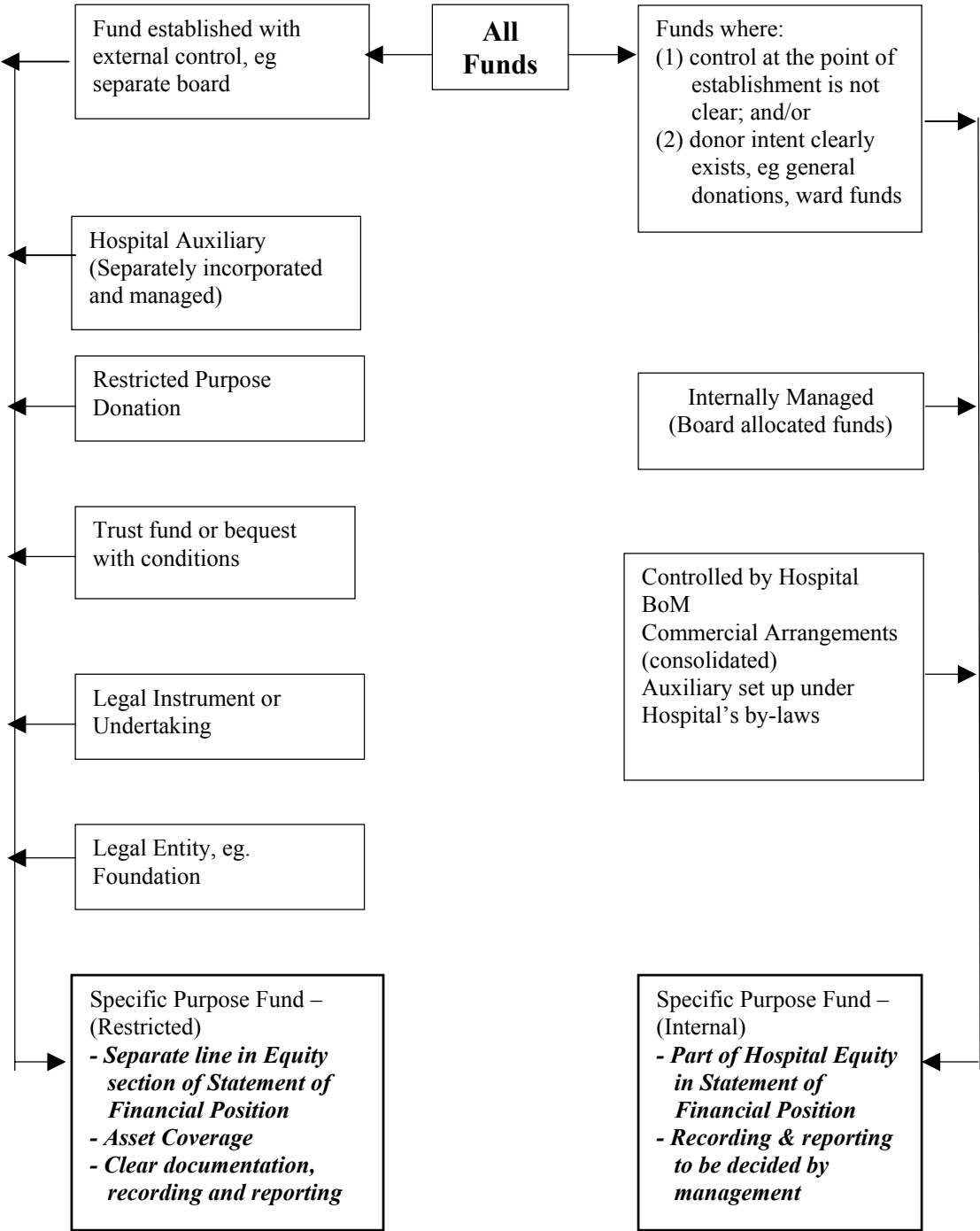
3.2.3 Control

Ultimately, who has the final legal ownership of the balances in the fund in the event of a winding up or reorganisation? Is it:

- A separate board, committee or trustee?
- The committee of an auxiliary or fund-raising group?
- A legal entity with a degree of external stake-holding?
- Any third party with a valid legal claim over part or all of the assets of the Fund?
- The BoM?

3.3 “Test of Type” Flowchart

This flowchart read in conjunction with Section 3.1 provides explanation and examples on the three key tests, namely establishment, management and control, in determining the type of fund. The flowchart illustrates in the 1st column the distinction where agencies have possession or title to the funds but has no discretion to amend the restriction and/or condition underlying the funds. The 3rd column relates to situations where agencies have management control as well as the discretion on disposition of the funds. Further categorisation of these two broad groupings is discussed in Section 3.5.



3.4 Examples

The series of tests (Section 3.2) are illustrated systematically below, with examples to illustrate the decision-making process:

1. The Smithtown Sports Club Auxiliary was formed to support Smithtown Hospital after the CEO addressed the Club's annual meeting. The Smithtown Sports Club formed an incorporated association (Sports Club Auxiliary Inc.) and invited its members to join and raise funds for capital works at the Smithtown Hospital. The Directors of the Association meet regularly with the Hospital CEO and focus their fundraising on what the Hospital wants most. A cheque is handed over at an annual ceremony. The bookkeeping and administration of the Association is carried out at the Hospital by the Accountant, but the cheque signatories are the Directors of the Association.

Unless the Association makes a donation, the funds raised are outside the control of the Hospital and are not recorded in the Hospital's books. The cheques are received by the Hospital as general donations or specified donations, according to the facts of the case from time to time.

2. As for (1.) above, except that the members of the Hospital Board are, as of right, Directors of the Association and the Association's Articles of Association require funds raised to be spent solely for the benefit of the Hospital. The Auxiliary is consolidated with the Hospital accounts each year.

This passes the test of 'Establishment' and 'Control' criteria above and is a SPF(R).

3. The Hospital forms a 'Recycling Club' with Hospital executives on its Committee together with the local Scout and Guide leaders who have an equal voice. The Club collects bottles, cans and cardboard and the Hospital Engineer arranges sales. At the request of community members, the proceeds go into a special bank account for spending on development of a gymnasium in the Children's Ward. Management control clearly lies with the committee, which is not controlled by the Hospital.

This passes the 'Management' test above and is a SPF(R).

4. In example 3 above, if the Scout and Guide leaders were simply observers, 'Control' would be with the BoM and the proceeds would form part of hospital/health service's equity, as for general donations.
5. It is common to have an auxiliary established under the hospital's by-laws to provide voluntary services for the general benefit of the hospital. For example a hospital sets up a retail shop or kiosk within the hospital's premises. The business is run by volunteers from an unincorporated auxiliary group formed under the hospital's by-laws. It is clear that the retail business is established and controlled by the BoM. The surplus or deficit derived from the business would form part of hospital/health service's equity, ie. a SPF(I).

6. There is a legal view that a doctor's private practice fund if not formally donated to the hospital by the doctor, remains under the control of the doctor who established the fund pursuant to an agreement with the hospital or health service. The management of the private practice fund is governed by the terms of the agreement. In this scenario, the fund would be considered to be a SPF(R)
7. It is common for general donations to be provided without any clear restriction. However, if there is a general inference or latent donor intent that these donations should not be applied to defray recurring operating expenses then there is a moral obligation on the part of hospital to recognise the existence of donor intent and to treat these donations as SPF(I).

3.5 Categorisation of Funds

The application of the tests of type put the funds into two broad categories namely SPF(R) and SPF(I). The diagram in Section 3.3 illustrates that SPF(R) should be reported separately in the Equity section of the Statement of Financial Position whereas SPF(I) should be reported as part of the health service's equity. Further guidelines on record keeping and asset backing are provided in Sections 5 and 6.

To allow for meaningful reporting of SPF(R) and SPF(I) to both hospital/health service Executive Management and BoM, these funds should be disaggregated into further categories. While each agency should decide on its own categories, an example of the classes in which funds may be placed is as follows:

- SPF(R):
 - Trust funds.
 - Funds held in perpetuity.
 - Auspiced agencies.
 - Funds controlled jointly with third parties.
 - Foundations.
 - Other.
- SPF(I):
 - Fund raising activities.
 - Commercial ventures.
 - Departmental fund.
 - Specific project.
 - Other.

4. BUSINESS RULES

4.1 Present Practices and Issues

Practices vary between hospitals/health services at present to the point where consistent reporting of SPFs across the Victorian public health sector cannot be guaranteed. Not only are funds not consistently clarified into internal or restricted, other variations exist as well. For example:

- costs are not always matched with SPF revenues;
- revenues are not always allocated to SPFs on a consistent basis between hospitals/health services;
- the Capital Fund and the SPF are used in different ways by hospitals/health services, for example, differences exist in the treatment of donations and interest;
- the above three inconsistencies may obscure cross-subsidies being passed between funds to meet deficits;
- liquidity ratios generally calculated by including cash and investments that may be required for particular 'restricted' purposes in legally enforceable arrangements or in funding agreements. The liquidity ratios being calculated may mask serious liquidity shortfalls; and
- the Operating Fund tends to be a repository for expenses, assets and liabilities not allocated to another Fund.

There is also a need to re-state the basis of the DHS fund accounting system and its key features.

4.2 Fund Accounting

By classifying financial transactions between 'funds', the purpose of the transaction is recorded in the general ledger, thereby facilitating accountability for those transactions to the organisation or group providing the related funds and eliminating cross-subsidies.

Fund accounting is an important feature of public sector accountability and is seen in the classification of Public Account transactions between the Consolidated Fund and the Trust Fund. DHS applies a similar accountability model to hospitals/health services through the conditions of funding in its Health Service Agreements.

4.3 Accounts and Record-Keeping

4.3.1 Accounts

At regular intervals, at least annually at the same time as the annual accounts of the health service are prepared, all individual SPFs should be scrutinised and properly reconciled and if necessary adjustments made, so that their correct position may be understood. This is best achieved by producing statements of financial position and performance for each component of the SPF(R) and SPF(I). Where the fund relates to an auspiced agency or a separate legal entity, a statement of financial position and statement of financial performance should be prepared on an accrual basis. Auspiced agencies should always have a statement of Financial Position and Statement of Financial Performance prepared to report their transactions.

4.3.2 Record Keeping

All SPF(R) and SPF(I) should have readily available data on:

- the purpose of the fund;
- the proposed classification of the fund (SPF(R) or SPF(I));
- details of the stakeholders;
- copy of any trust deed, instrument, deed of gift, will or other means by which the fund was established;
- details of decision-makers over the fund and an exact statement of the circumstances in which material decisions may or must be made;
- details of the financial history of the fund;
- details of the history of activity of the fund; and
- details of the way the fund may be terminated and the manner in which any final disbursement of remaining assets may be made.

This applies to all funds making up the SPFs and all legal entities which are subsequently consolidated. A specimen record layout is provided in Attachment 3.

4.4 Treatment of Certain Transactions

This section is applicable to all three Funds (see Attachment 2) which include SPFs(R) and SPFs(I).

4.4.1 Interest

Generally, interest earned on monies held in any particular fund should be credited to that fund. Similarly, borrowing expenses, interest paid, or imputed interest earned or charged should be attributed to the fund to which it relates. Certain capital grants are provided ahead of their expenditure and the funds are held until needed. The interest earned on these funds properly belongs to the Capital Fund.

4.4.2 Inter-fund Interest Charges

Accounts within the Capital Fund and SPF with a positive monetary balance may be credited with interest unless there is a particular circumstance related to that account which precludes it. This situation will usually arise when some funds (including the Operating Fund) may be in deficit and others are in credit. Interest may be charged to the deficit fund and credited to the fund in surplus. Charging interest, between funds, should only occur on the basis of a clear policy that is applied consistently between funds and over time. The cost of administration should be considered when formulating such a policy. If specific investments are held for a particular fund, the interest should be attributed to that fund.

4.4.3 Administration Fees

Administration fees may be charged to any individual fund account such as a fundraising foundation or a research trust, to offset the costs associated with the administration of that account, provided this is not forbidden by the instrument (if any) which established it. The amount of the fee is a matter for management to decide; in practice it is frequently related to the amount of interest (actual or allocated) earned by the fund. The amount should not exceed a reasonable approximation of the actual costs associated with the administration of the fund, including the absorption of a share of fixed administrative overhead.

4.4.4 Costs of Services Supplied Externally

When a fund, either a SPF(R) or a SPF(I), earns material revenue from supplying services or goods outside the health service, for example pathology fees charged to a private hospital, and the revenue is credited to the fund, it is important for the costs associated with that revenue to be recognised in the fund. While the most desirable outcome is an exact matching of the costs, it may be impractical to do so because of the nature of the service sold or the limitations of the costing system (if any). In these circumstances, it is acceptable to estimate the costs involved, provided the estimate has a logical basis and is applied consistently. In the case of a service where there is readily available data on commercial equivalents, an allocation of cost as a percentage of selling price may be acceptable. In any case, the cost should not be ignored, as this would overstate the costs carried in the Operating Fund.

4.5 Auspiced agencies

The assets and liabilities of auspiced agencies should be included in SPF(R). Where the agreement allows for an administration fee or similar, that fee should be transferred to the Operating Fund at appropriate intervals. Reporting should be in the manner laid down in the auspiced agency agreement or in the manner described in these guidelines for SPF(R).

4.6 Consolidation

All controlled entities, regardless of the status of their equity as between SPF(R) and SPF(I), must be consolidated with the accounts of the health service for the purpose of annual reporting in accordance with Australian Accounting Standards.

5. ASSET BACKING AND LIQUIDITY

5.1 Asset Backing

Section 3 requires SPF(R) to be reported as separate item in the equity section of the Statement of Financial Position. Other SPF(I) are to be reported as part of hospital/health service equity. In all cases these SPF(R) if not technically a ‘trust’, are of a trust nature. As such there should be adequate assets backing these funds.

Whether or not a particular SPF(R), or SPF(R) as a class, need be represented by liquid assets is a question of fact based on their establishment and prudent management. Some funds are created by the donation of non-liquid assets, such as investment property or fixed securities, while an auspicing entity may place fixed assets under the long-term control of the agency. Although the current practice of most agencies is to convert donated assets to cash or tradeable securities, this may be prevented by the terms of the donation or other practical issues.

SPF(R) may contain non-current, and non-liquid, assets and liabilities according to the circumstances and nature of the fund. Where the agency wishes to treat the assets of the fund globally with the other assets of the agency for cash management or similar purposes, the interests of the fund must be protected by recognising the rights of the fund in internal management reporting and making the treatment clear in reporting fund and liquidity balances to the BoM. It is most important that the BoM is fully aware that the liquid assets of the SPF(R) have been fully or partly used to calculate liquidity ratios. If there is a situation where the Trustees or other responsible parties for a SPF(R) intend to withdraw the assets of their fund for any lawful purpose, the BoM must be advised forthwith, together with detailed information of the effect of the withdrawal on liquidity ratios.

It is recommended that adequacy of assets supporting the SPF(R) be presented to BoM and DHS in the following format.

Report of Cash Holdings, Trust Liabilities and SPF(R)

		Month	
		<u>Current</u>	<u>Previous</u>
	Cash Holdings	\$	\$
	Investments (current and non current)	\$	\$
(A)	Sub total	<u>\$</u>	<u>\$</u>
	Less SPF(R)	\$	\$
	Less Employee Trust Accounts	\$	\$
(B)	Sub total	<u>\$</u>	<u>\$</u>
(C)	Less Pre funded capital works	<u>\$</u>	<u>\$</u>
[1]	Amount Available for Operating Activities (A-B-C)	\$	\$
[2]	Less minimum working capital requirement	\$	\$
	Excess (Deficiency) [1-2]	<u><u>\$</u></u>	<u><u>\$</u></u>

5.2 Management of Investments

Where the fund entity has separate legal status, those responsible for the management of the fund account may choose to allow the investments to be included with the hospital/health service investments globally. However, if the enabling instrument allows it, management of the fund entity may choose to manage its investments separately. The legal facts should be observed at all times. If separating the investments of an entity which is entitled to such separation causes, or would cause, an untenable operating situation in the hospital/health service, that situation must be reported immediately to the BoM and DHS.

5.3 Management Strategies for Insufficient Liquidity

Attachment 4 sets out the strategies available to agencies for managing their financial viability generally. These strategies are equally applicable to an agency with issues of insufficient liquidity in SPFs especially SPF(R). The attached list includes key elements of management strategies but is not an exhaustive list of all possibilities for every situation.

6. Board Reporting

The principal issues, which must always be brought to the attention of the BoM of the hospital/health service, are those where legal rights and obligations of the hospital/health service are involved. The legal ownership of assets and liabilities and associated liquidity ratios must be reported to the BoM on a regular basis. This means that the separate reporting of the financial position of the SPF(R) is necessary at least annually, because of their third party obligations (see Attachment 3).

The liquidity ratios and asset backing for SPF(R) (see Section 5) should be advised to the BoM at least monthly. The extent to which supplementary reporting of the practical issues of management control and influence over these assets and liabilities is necessary, is a matter for the BoM and the hospital/health service's executive. These issues may be complex and should not be allowed to disguise the true legal position.

The financial position of all material auspiced agencies of the hospital/health service should also be reported to the BoM regularly, at least on an annual basis.

The extent of reporting to the BoM of the financial position of SPFs generally is a matter for the BoM and the hospital/health service's executive to decide. A pro forma reporting format is set out in Attachment 5.

The nature and detail of reporting to BoM is a matter for each agency, but it is important to recognise that there is a minimum amount of information which a BoM must have in order to be able to perform its review and monitoring functions. Equally, the provision of masses of detail obscures the important matters which require board consideration. For these reasons, it is suggested that regular reports to BoM should include the following details and indicators with regard to SPFs(R) and SPFs(I):

- SPFs(R):
 - The overall number of funds and the total value of these funds.
 - The number and value of funds by classification. For example:
 - Trust funds.
 - Funds held in perpetuity.
 - Auspiced agencies.
 - Funds held in conjunction with third parties.
 - Foundations.
 - Other.
 - Overall movement in SPF(R) by category as follows:
 - Opening balance
 - Add Revenue
 - Less Expense
 - Other movements
 - Closing balance
 - Any fund which is 'overdrawn' (that is, having a debit balance) with a brief explanatory note.
 - A brief note of any significant or abnormal activity which has occurred in any fund.
 - A brief note of the accounting policies applied.

- SPFs(I):
 - The overall number of funds and the total value of these funds.
 - The number and value of funds by classification. For example:
 - Fund-raising activities.
 - Commercial ventures.
 - Departmental funds.
 - Specific projects.
 - Other.
 - Overall movement in SPF(I) by category as follows:
 - Opening balance
 - Add Revenue
 - Less Expense
 - Other movements
 - Closing balance
 - Any fund which is materially ‘overdrawn’ (that is, having a debit balance) with a brief explanatory note;
 - A brief note of any significant or abnormal activity which has occurred in any fund.
 - A brief note of the accounting policies applied.

7. MANAGEMENT OF FUNDS

7.1 Transitional Issues

The process of changing to a more prescriptive situation for the reporting and managing of SPFs(R) and SPFs(I) will inevitably crystallise problems in individual funds which have previously been masked. The following strategies are suggested for dealing with a number of possible problems in both SPFs(R) and SPFs(I).

7.1.1 Unexpended Balances

Where the original purpose of the fund has been achieved or has become redundant and there is a balance in the fund of \$1,000 or less, the balance should be 'written off'. The write off is accomplished through a transfer of the amount written off from the SPF reserve to retained earnings (accumulated deficit). If the staff member or other interested person who had input to the management of the fund is available, it may be prudent to discuss the possible transfer of the fund balance to another more active fund. Where the fund balance is larger and the purpose of the fund is restricted, a new purpose should be devised for the fund rather than writing off the fund balance. If this option is not feasible, it is recommended that for the closure of SPF(R) with balance above \$1,000 the concurrence of the interested third parties should first be obtained. If it is not practicable to do so or the parties concerned are no longer contactable, a Board resolution authorising the closure of the SPF(R) should be obtained to formalise the write off.

7.1.2 Lost Records

In the event that there are no clear records as to the purpose or disposition of the assets of a particular fund, it should be written off as described in section 7.1.1 above. The amount of effort devoted to attempting to reconstruct or trace details should relate to the value of the assets, but any such fund valued at \$1,000 or less should be transferred to the Operating Fund.

7.1.3 Amalgamation, Disaggregation and Change of Purpose

If the original purpose of a fund has become impractical due to a change of circumstances and the intentions of the donor, and the effects of the change are neither clear nor capable of being reinterpreted, the only options are to write the balance off to the Operating Fund or to create a new purpose for the assets. This decision should take into account the balance remaining in the fund, together with the nature of the original fund and the general intention of the provider. If the balance is less than \$1,000, writing off to the Operating Fund is an obvious option, but care should be exercised to ensure that legal obligations, such as trust deeds or the wishes of executors are complied with. If the assets are significant, the opinions of interested parties, particularly trustees, executors and actively interested relatives of otherwise incapable donors, should be sought.

It should be noted that returning assets to a donor or an estate when there is no clear legal obligation to do so, is inappropriate. In resolving this type of issue, attention should be directed to the agency's ability to identify the specific provider(s) of the funds and practical options for the use of those funds.

7.1.4 Small and/or Inactive SPF Accounts

Because of the extremely diverse nature of transactions which may be considered to be included as either SPFs(R) or SPFs (I), there has been a tendency by agencies to create a very large number of small funds. This has usually occurred because many donors equate the high degree of difficulty in raising relatively small amounts, with the value which should be placed on the resultant fund, agencies tend to hold large numbers of small and relatively inactive accounts in their systems.

These factors have contributed to the difficulties in both managing and reporting the funds in a meaningful way.

In addition, few agencies have in place a policy for dealing with small residual balances to be found in funds which have ceased to be useful, or which have arisen from mis-postings.

It is suggested that a policy be developed or adopted by each agency having specific purpose funds which includes the following points:

- each individual fund should have a named staff person responsible for making decisions about the fund and with the authority to do so;
- both debit and credit transactions should be shown in each fund so that a net balance is available;
- on an annual basis, any fund which has a net balance of less than \$1,000 and that has had no transactions for the year, other than bank charges or allocated interest, should be closed and the balance written off as described in Section 7.1.1; and
- any fund which remains constantly overdrawn should be closed.

Each fund should be classified into a category for BoM reporting purposes, see Section 3.5.

7.1.5 Closure of Funds

In the course of reviewing SPFs, some funds may need to be closed. Attachment 6 provides draft paragraphs for use in corresponding with interested third parties on closing an unwanted or inappropriate fund.

7.1.6 Funds with Negative Balances

In some instances it will be noted that a fund or funds is showing a negative (“overdraft”) balance. If this is due to an accounting error it should be corrected, however there are two other common causes. Firstly, the fund may have been deliberately or inadvertently over-spent, leaving aside appropriate management remedies. In this case the funds should be returned to a nil balance by transfer from the operating account. This has no effect on the operating results, but corrects the reported values of the Operating, Specific Purpose and Capital Funds. Secondly, in some hospitals there is a practice of raising two funds for a single purpose, with income in one and expenditure in another. This is intended to make the financial activity on those funds more apparent over multiple accounting periods. There is no effect on the reported operating results or statement of financial position, but there is a risk of confusion in reporting fund activities. This is not be the most effective way of accounting, and these two records should be merged

8. DRAFT ACCOUNTING POLICY

1. The general accounting policies applied to the agency as a whole, are applied to SPFs(R) and SPFs(I).
2. Both SPFs(R) and SPFs(I) are subject to accrual accounting principles.
3. Receipts relating to SPFs(R) and SPFs(I) are treated as revenue. If a breach of purpose has occurred with respect to a SPF(R), a liability may be created for the return of certain assets to the provider of funds.
4. The net balance of SPFs(R) as a group is represented by assets and are designated as SPFs(R) in the Equity section of the Statement of Financial Position. The balance of other SPFs(I) is included in assets and equity.
5. A set of financial reports for both SPFs(R) and SPFs(I) by category is prepared at least annually.

GLOSSARY

AIMS	Agency Information Management System
BoM	Board of Management
DHAC	Commonwealth Department of Health and Aged Care
DHS	Department of Human Services
MHS	Metropolitan Health Services
SPF	Specific Purpose Fund
SPF(I)	Internally managed Specific Purpose Fund
SPF(R)	Restricted Specific Purpose Fund

FUND ACCOUNTING

Operating Fund

The Operating Fund records all activities and transactions that are supported wholly or partly by DHS, apart from capital transactions. Funding from the Commonwealth Department of Health and Aged Care (DHAC), or from any other State or Commonwealth source, which is primarily intended to support day-to-day operations of the agency is also included in the Operating Fund. The Operating Fund includes all general donations, that is, donations which have not been made for a particular purpose, either as specified by the donor or where the publicly stated reason for collecting the funds had no clear purpose which precludes this treatment. However, if there is a general inference or latent donor intent that these donations should not be applied to defray recurring operating expenses then there is a moral obligation on the part of hospital to recognise the existence of donor intent and to treat these donations as SPFs. Interest earned on the invested balance of the Operating Fund stays in this Fund.

Capital Fund

The Capital Fund includes all purchase and sale transactions which relate to land, buildings, equipment, furniture, vehicles and investments, whether funded by DHS or from other sources. All depreciation is charged to this Fund. Repairs and maintenance of an operating nature are charged to the Operating Fund or the appropriate SPF, but major refurbishment or replacements are charged to the Capital Fund. Property taxes, such as land tax and stamp duty on transfers are charged to the Capital Fund, while municipal rates and similar service charges are treated in the same way as repairs.

Specific Purpose Fund

This Fund includes all transactions where there is some form of restriction placed on the use of the funds. The Fund may be divided further into SPF(R) and SPF(I). SPF(I) may be divided further to separate large commercial undertakings as discussed below. Funds provided by DHS or DHAC for aged care residents' fees are not included in the SPF. Where monies are supplied from a non-DHS source for a capital purpose, after the capital project commences the monies and subsequent assets belong in the Capital Fund.

SPECIFIC PURPOSE FUNDS (RESTRICTED)

A clear distinction of conditions, restrictions and obligations is essential to the identification and categorisation of SPF. The distinction drawn is also helpful in understanding the typology used to identify and classify SPF (see Section 3).

It should be emphasised that regardless of the nature of the restriction, the recognition of any transfer of funds from an external source as revenue at the time of the transfer is not affected by the existence of a **restriction** on the use of the funds. This transfer immediately creates revenue and a liability arises only when a **condition** is breached.

This approach is supported by the Australian Accounting Standards.

Stipulations

Stipulations are the terms attached to a transfer into a fund which specify certain responsibilities of the recipient regarding the transferred resource. For example, a **restriction** imposed by the transferor to limit or direct the use of contributed funds to (say) constructing a building. This does not necessarily create a liability or financial **obligation** because, depending on the nature of the condition, if the condition is breached, the asset may not need to be returned to the provider of funds.

To fully understand an entity's financial performance and position, users should be aware of the full amounts of resources provided to the entity. This is particularly important in the not-for-profit sector, as the gross level of funding earned is crucial information to enable assessment of performance. Information concerning such stipulations should be disclosed, both in the accounts and in AIMS reporting, since the service potential embodied in an asset (especially cash and investments) can be affected by the existence of restrictions.

The treatment of funds which come with stipulations will vary according to the level of seriousness of the stipulation. In the least serious case, all that is stipulated is an obligation to acknowledge the intent of the provider in some way such that the agency is seen, in general terms, to be following the intent of the giver.

More serious is a restriction, since this places the agency in a position where the use of funds is clearly specified. It does not go so far however as to require the return of the funds should the purpose not be complied with. In the event of a breach of a restriction, the worst outcome might be a civil action to enforce specific performance. Unless that occurred, there is no requirement under the Australian Accounting Standards to create a liability.

The most serious stipulation is that which requires the gift to be used as intended or it must be returned to the provider. In that case an accounting liability may be created.

These degrees of stipulation are discussed below.

Conditions, Restrictions and Obligations

It is important to examine each gift, donation or similar transfer and make a distinction between the following categories of stipulations:

- a condition;
- a restriction; and
- an obligation.

This will lead to the correct accounting treatment.

A **condition** specifies an uncertain future event that must occur, or fail to occur, before a recipient has an unconditional right to retain a contributed asset in cash or other form. Conversely, the occurrence or failure of that event may trigger the requirement for the return of the asset and require the creation of a liability in the accounts which recognises the need for returning the asset. An asset received in these circumstances always gives rise to a SPF(R).

A **restriction**, while still being more specific than the broad limits resulting from the nature of the organisation or the environment in which it operates (and thus not applying to general donations) is a stipulation which does not require the return of the asset in any circumstances. Although fiduciary duties are imposed to use the asset for its stipulated purpose, a restriction does not have the ability to create a liability, in the manner of a condition. That fiduciary responsibility does not, of itself, create a liability in an accounting or legal sense.

Restrictions may be narrow or broad, short-term or long-term, or temporary or permanent (e.g. in perpetuity). Restrictions usually lead to a SPF(R). Restrictions do not apply to reserves created, for example, to designate a surplus to meet certain purposes, unless those reserves are alienated in a legally enforceable way, such as by the creation of a trust. Reserves created to earmark or 'quarantine' unrestricted accumulations do not take on the characteristics of a SPF(R) but remain as a SPF(I).

An **obligation**, which is neither a condition nor a restriction, always arises when an entity receives resources in the nature of a gift, donation, bequest or something similar, i.e. where a provider passes over value when not obliged to do so or without receiving consideration amounting to fair value in exchange for the amount transferred. An obligation is created by the general intent of the donor or provider and requires the entity to act with that general intent in mind. It carries no ties or sanctions, other than the likely withholding of future sums if the entity does not honour the intent of the gift. Unless an obligation creates a liability as defined in *Statement of Accounting Concepts* SAC4 there is no particular accounting treatment for an obligation in this context, because it is a non-monetary requirement to apply the funds in accordance with the wishes of the provider.

Conditions and restrictions are dealt with above, and the special case of the **general donation**, i.e. a donation which is free of conditions or restrictions and has no implied specific purpose, is dealt with by taking the donation to the Operating Fund (see Attachment 1).

All other receipts of such assets should be recognised as being SPF(I), albeit not as SPF(R), in acknowledgment of the obligation to respond to the wishes of the provider of funds. This action does not place an obligation to report a liability, except as discussed above, but does emphasise the need to disclose SPF(I) as acknowledgment of those wishes.

RECORD LAYOUT

A record in the following suggested format should be maintained for each Specific Purpose Fund established by the hospital/health service.

Establishing a Specific Purpose Fund				
<u>Basic Information required</u>				
Department: _____				
Responsible Manager: _____				
Delegation Limit: \$ _____				
(NOTE. This person will have the authority to make entries in the fund and to authorise transfers, including closure for fund balance not exceeding \$1,000.)				
Proposed Name of Fund: _____				
Type of Fund¹:		Specific Purpose Fund (Restricted)	<input type="checkbox"/>	
		OR		
		Specific Purpose Fund (Internal)	<input type="checkbox"/>	
CATEGORY OF FUND (Tick appropriate box)				
Specific Purpose Fund (Restricted)	Trust Fund	<input type="checkbox"/>	Foundation	<input type="checkbox"/>
	Fund Held in Perpetuity	<input type="checkbox"/>	Fund Held With Third Party	<input type="checkbox"/>
	Auspiced Agency	<input type="checkbox"/>	* Other (Describe below)	<input type="checkbox"/>
Name of Third Party (e.g. Company sponsoring drug trial): _____				
* Other SPF(R) _____				
Specific Purpose Fund (Internal)	Fund Raising Activity	<input type="checkbox"/>	Specific Project	<input type="checkbox"/>
	Commercial Venture	<input type="checkbox"/>	** Other (Describe below)	<input type="checkbox"/>
	Departmental or Ward Fund	<input type="checkbox"/>		
** Other SPF(I): _____				
Purpose for Which Fund Will be Used: _____				
Source(s) of Revenue: _____				
Reporting Requirements: _____				
Audit Requirements: _____				
Authorised by: _____				

¹ **Note.** For guidance on the type of fund, see Section 3 of the Guidelines for the identification and establishment of Specific Purpose Funds.

MANAGEMENT STRATEGIES REFERENCE GUIDE

Strategy	Effects on Viability	Management Tools
1. Improved debt collection.	Reducing accounts receivable; Reducing working capital needs; Releasing cash funds; Earlier recognition of bad debts.	Monthly cash flow projections; Budget v. actual output performance; Earlier wrap-up by DHS; Monthly casemix acquittal; Prompt invoicing by agencies; Account analysis and reconciliation; Aged debtors' analysis; Continuing collection follow-up; Monthly performance reporting.
2. Leave management	Reducing current liabilities; Reducing working capital needs.	Monthly cash flow projections; Projections v. actual performance; Leave rosters; Staff replacement options; Monthly performance reporting.
3. Extending credit terms from suppliers	Reducing working capital needs.	Monthly cash flow projections; Competitive bidding; Contract negotiation; Regular payment on due dates;
4. Disposing of excess property and equipment	Releasing working capital; Improving operating results; Funding new capital projects; Increasing equity.	Asset utilisation data; Financial management strategy; Capital expenditure forecasts; Capital grant projections; Three-year cash flow projections.
5. Lower inventory levels	Reducing working capital needs; Reducing space needs; Reducing inventory management resources; Reducing inventory write-offs.	Minimum re-order levels; Just-in-time ordering; Perpetual inventory systems; Monthly performance reporting.
6. Planned timing of building and equipment maintenance	Trade-off between maintenance and replacement; Reducing working capital needs.	Fixed asset registers; Scheduled maintenance planning Risk-based priority-setting; Budget v. actual financial performance; Outsourcing maintenance management.
7. Asset replacement	Lower maintenance costs; Cash accumulation from appropriations for depreciation increases working capital; Ongoing operating costs draw working capital; Ongoing operating costs reduce surpluses and equity.	Fixed asset registers; Financial management strategy; Three-year cash flow projections; Risk-based priority-setting; Outsourcing capital-intensive activities; Monthly financial activity reports.

Strategy	Effects on Viability	Management Tools
8. Sale and leaseback of assets	Releases working capital; Increases financing costs;	Financial management strategy; Operating v. finance leases. Reassessment of equipment needs.
9. Borrowing from DHS to fund asset acquisition or refinance liabilities	Creates capital for infrastructure or current needs; Increases financing costs; May reduce longer term flexibility and stability; Need to match borrowing and investment maturity profiles.	Financial management strategy; Three-year cash flow projections; Budget v. actual financial performance; Monthly cost of capital monitoring.
10. Rostering and work practices	Reducing operating costs; Increasing surplus and equity; Reducing working capital needs.	Budget v. actual financial performance; Staff rosters; Absenteeism statistics and trends; Overtime and penalty statistics and trends; Award negotiations; Benchmarking; Market testing; Incentive arrangements.
11. Market testing and outsourcing	Reducing operating costs; Increasing operating surplus; Reducing working capital needs; Reducing capital investment; Increasing return on property assets; Significant transitional costs; Future quality and control issues; Contract management costs; May reduce equity.	Strategic plans; Output specifications; Employee agreements; Financial management strategy; Budget v. actual financial performance; Baseline costing of outputs specified; Market testing processes; Competitively neutral pricing; Incentive payments; Redundancy funding; Analysis of leave liabilities; Quality and volume monitoring; Contract management methodology; Monthly performance reporting.
12. Redeeming or selling investments	Releasing working capital; Improving solvency margin; Reducing investment revenue.	Investment register; Financial management strategy; Monthly cash flow projections; Risk and cost-benefit analysis of alternative sources of finance; Specialist external financial management advice.
13. Earning market rents for non-core properties	Commercial return on investment properties, including consulting rooms, laboratories, nursing homes, allied and community health premises; Increasing working capital;	Property investment register; Financial management strategy; Monthly cash flow projections; Risk and cost-benefit analysis of alternative uses of funds; Specialist external financial management advice.

Strategy	Effects on Viability	Management Tools
14. Profitability of business units	Earning a target, commercial return on assets and equity; Increasing working capital; Generating funds for asset replacement;	Financial management strategy; Output pricing policy; Target return on assets and equity; Three-year cash flow projections; Monthly cash flow budgets; Budget v. actual profit outcomes; Debt collection statistics; Statistics for demand for outputs;

BOARD REPORTING TEMPLATE

DRAFT for Guidance only

Specific Purpose Funds (Restricted)

OVERALL STATISTICS

	Trusts	Funds held in Perpetuity	Auspiced Agencies	Held involving third parties	Foundations	Other	Total
Number							
Value							

Movements for Month

	Trusts	Funds held in Perpetuity	Auspiced Agencies	Held involving third parties	Foundations	Other	Total
Opening Balance							
Add Revenue							
Less Expense							
Other Movement							
Closing Balance							

Commentary

1. Overdrawn Funds

2. Significant Activity

3. Accounting policies

BOARD REPORTING TEMPLATE

DRAFT for Guidance only

Specific Purpose Funds (Internal)

OVERALL STATISTICS

	Fund Raising	Commercial Ventures	Departmental funds	Specific Projects	Other	Total
Number						
Value						

Movements for Month

	Fund Raising	Commercial Ventures	Departmental Funds	Specific projects	Other	Total
Opening Balance						
Add Revenue						
Less Expense						
Other Movement						
Closing Balance						

Commentary.

4. Overdrawn Funds

5. Significant Activity

6. Accounting policies

**SPECIMEN PARAGRAPHS FOR INCLUSION IN
CORRESPONDENCE TO TRUSTEES ON CLOSURE OF FUNDS**

1. Closure of Fund – Purpose Achieved

We wish to advise that the purpose of the fund has been achieved as laid out in _____ (eg. the trust deed, etc).

There is a balance of \$_____ remaining in the fund and since that balance is relatively small, we propose to transfer these funds to a (new) fund which has a similar purpose. The fund will then be closed.

OR

We wish to advise that the purpose of the fund has been achieved as laid out in _____ (eg. the trust deed, etc).

There is a balance of \$_____ remaining in the fund and since that balance is significant, we would value your advice as to a proper purpose to which that sum could be put. Because the original fund has achieved its purpose, it will be closed and a new fund created for the new purpose.

2. Closure of Fund – Inability to Continue

As you will be aware, the original purpose of the fund can no longer be achieved, owing to (closure of campus etc). We are of the view however, that (such and such) is of a sufficiently similar character to fulfil the spirit of the original (bequest etc) and accordingly the fund should be renamed and the balance of (dollars) be applied to that purpose.

3. Closure of Fund – Loss of Purpose

As you will be aware, the original purpose of the fund is no longer appropriate, owing to (funding by Government etc). We are of the view however, that (such and such) is sufficiently important to be the beneficiary of the unexpended balance and accordingly we are seeking your permission to rename the fund and apply the balance of (dollars) to that purpose.

Specific Purpose Funds (Internal)

Because SPF(I) are ultimately under the control of the BoM, permission from the creator of the fund is not strictly necessary. It should be noted however, that many such funds are created by the goodwill and efforts of staff and others acting in a voluntary capacity. For this reason, consultation and communication should be always made with the appropriate person before radical changes are made to such funds.