In accordance with section 38E of the Public Finance and Audit Act 1983, I present a report titled Purchasing Hospital Supplies: Follow-up of 2002 Performance Audit.
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**Performance Audits by the Audit Office of New South Wales**

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**Contact officer**  
Sean Crumlin, Director Performance Audit  
Tel (02) 9275 7286  
email: sean.crumlin@audit.nsw.gov.au
Foreword

Periodically we review the extent to which agencies have changed their practices as a result of our audits. This gives Parliament and the public an update on the extent of progress made.

In this follow-up audit, we examine changes following our September 2002 report, to assess whether NSW Health has improved its buying of hospital supplies using electronic systems.

NSW Health spends over $1.3 billion on hospital supplies. It is the largest expenditure area after employee costs. Reform of this area has the potential to make significant savings that could be redirected to frontline services.

As part of our series of audits in the area of e-government, our previous audit looked closely at the extent to which technology was being used to deliver potentially major savings in purchasing hospital supplies. This is a key area of so-called "process re-engineering" in the "e" field, and NSW Health provided an ideal case study.

Whilst implementing large-scale e-procurement has many technical aspects, it is not chiefly a technical issue. The key requirements for success reside in effective change management, in particular being clear as to who has the authority to make change decisions and be held accountable.

This audit looks at NSW Health’s successes to date, and its frustrations and challenges in making further progress in this field. Many of the issues raised in this report may provide lessons for any agency that is seeking to drive a significant change program.

Bob Sendt
Auditor-General

November 2005
Executive summary
Executive summary

The 250 public hospitals in NSW spend over $1.3 billion annually on goods and services including medicine, food, asset maintenance and general purchases.

The 2002 audit

In 2002 we conducted an audit on buying hospital supplies, as part of our series of audits on e-government. We studied the health sector as a case study for a significant aspect of harnessing value from technology, namely electronic procurement.

NSW Health was already implementing a Supply Chain Reform Strategy (SCRS) at that time. The strategy was to be completed by late 2003, and deliver between $60 million and $80 million in savings.

The 2002 audit found that with less than two years to meet the SCRS targets, the health sector had made only limited progress. Our report identified a range of issues and impediments, and made a considerable number of specific recommendations to assist NSW Health in its endeavours.

This report, three years later and two years after the SCRS target, provides an update on progress\(^1\). In particular we reviewed:

- whether the accepted recommendations from the original audit were implemented
- what changes have been made to buy hospital supplies more efficiently and economically
- what benefits this has generated.

Audit Opinion

The health sector in NSW has made some progress in reforming its purchasing practices. Since it began its Supply Chain Reform Strategy in 2000, NSW Health estimates that it has saved $60 million with increased efficiency and economy.

To date, major improvements made to the way the NSW health sector purchases hospital supplies include:

- increasing the proportion of purchases made with state contracts from 48% to 50%
- reducing the number of warehouses from 74 to 26, and also reducing the inventory levels held in the warehouses by about one third
- creating three groups of Area Health Services (Areas) that could act collectively to implement their own procurement initiatives.

\(^{1}\) Our practice is not to make new recommendations in follow-up audit reports. We find lessons and issues.
Good as this is, the savings are at the lower end of the estimated savings range, and significantly short of the $80 million upper estimate. And it has taken considerably longer than the 2003 time target.

Encouragingly, there appears to be considerable potential for a great deal more to be achieved in this area. To that end, priority needs to be maintained on delivering results in this key area of reform.

In our view, issues that have impeded progress, or which require priority attention, include:

- finding successful models and processes for IT governance and change-management across the breadth of the health sector
- finalising an electronic catalogue, which has been a persistent issue of difficulty now spanning 15 years
- achieving consistency in implementing procurement business processes and systems
- implementing a viable electronic marketplace system
- extracting vital performance information, including whether the timeliness of receiving goods and services has improved
- routinely paying all suppliers on time. This is another persistent issue for most Areas, causing lost discounts, and reducing the reliability of supply and the ability to negotiate better deals.

Progressing the electronic procurement strategy is proving more complex than NSW Health originally anticipated. Most reforms of this type experience this. But at essence, this is not a technical issue. The key focus is procurement and governance reform.

The key requirements for success reside in achieving a consistent procurement business model, effective change-management, and developing clarity of accountability and decision-making for progressing change. In the IT profession this is referred to as harmonising IT governance with business governance, and aligning IT strategy with the needs of the business. Our report highlights areas in which these key factors for success can be addressed.

2005 audit findings

In mid-2004, NSW Health restructured the 17 Area Health Services into eight, which included plans to establish a shared corporate services group. In 2005 it disbanded the Health Peak Purchasing Council. The Areas are now directly accountable to the NSW Health Director-General. However, this has not been fully implemented in practice, and the Areas still largely operate as 17 separate entities.

Performance indicators have only recently been developed, and Areas have been required to report on them quarterly since the start of 2005. However, Areas cannot always provide the needed information. Also, because the Areas still use different systems, the information provided is not always comparable.
Executive summary

Information is not currently available on whether the time to receive ordered goods and services, including those that are life critical, has improved with the changes made.

Health advises that it will implement a shared services group over the next six years. This group will take over all the corporate support functions of all Areas and hospitals. This will allow the hospitals and Areas to concentrate on their main business of delivering patient care.

Chapter 2 - What changes have been made to purchasing practices?

Since our 2002 audit, improvements have been made in a number of areas of Health’s supply chain process. Health estimates that to mid-2005, approximately $60 million has been saved.

NSW Health has increased the amount bought on contracts to cover approximately 50% of its annual spend, and is trialling guaranteed large-volume contracts. This is expected to result in significant savings.

A standard contract document template has been developed and there is a single contract database that allows all Areas to use already negotiated contracts.

The number of warehouses has reduced. Some Areas have suppliers send requested items direct to hospitals rather than store them in warehouses. Most hospitals and Areas now use barcoding to monitor supply levels.

There is still no standardised procurement process encompassing IT systems, guidelines, ordering and purchasing methods, prices, contracts, payment methods, KPIs and communication processes.

Health still cannot pay suppliers on time in all cases. This impacts on price, reliability of supply and its ability to negotiate better deals.

After 15 years, Health is still trying to develop an electronic catalogue that can be used by all Areas to make purchases and track items. Likewise, a single corporate services IT system has not been implemented across the state. This makes data collection, information sharing and performance management difficult.

Some Areas have worked together to establish a common payment method and system to deal with suppliers. Some have also established their own catalogues for commonly purchased and used items.
Response from NSW Health

Thank you for the copy of the follow-up Performance Audit Report, Buying Hospital Supplies.

The report highlights the breadth and complexity of procurement within the health system and the steps being taken to reduce costs and improve performance. Overall the report provides a sound assessment of our progress. The recommendations are consistent with our reform agenda with the issues already addressed, or in the process of being addressed through either the supply Chain Reform Strategy, or the e-Marketplace initiative.

A number of issues have been encountered in the change process, particularly in relation to the implementation of electronic procurement. There was a need to restart the e-marketplace project due to the inability of Smartbuy to address the specific needs of Health. Regardless of the challenges encountered, Health has made substantial advances in reforming and improving the procurement outcomes.

It is worth noting that procurement savings of $65 million were achieved in the supply chain reform strategy, over three years to June 2005 and an additional $45.3 million in savings is targeted during the 2005/06 financial year through the procurement budget conversion strategy.

In summary, the report recognises the difficulties in reforming supply chains in the NSW Public Health system and makes a useful contribution to the process. It is a pity the report does not reflect that many of the progress delays have been caused by external factors, but I am pleased that it recognises the extent of the task being progressed by so many in the Health system to bring about these important reforms.

I appreciate the level of co-operation that existed between NSW Health and the Audit Office during the preparation of the report, and thank the staff of both agencies for their professionalism.

(signed)

Robyn Kruk
Director-General

Dated: 8 November 2005
Has managing procurement change across the health sector been successful?
The original audit

In 2002 we conducted an audit on buying hospital supplies, as part of our series of audits on e-government. We studied the health sector as a case study for a significant aspect of harnessing value from technology, namely electronic procurement.

Our recommendations covered three main areas:
- improving contract management
  - establishing best value for money contracts
  - collecting better information to enable NSW Health to achieve better prices and availability
  - paying early to get supplier discounts
- implementing electronic procurement
  - implementing standard IT systems
  - standardising buying processes across the whole of NSW Health
  - tracking goods and services from request to supply and payment
- managing and monitoring performance of Areas, hospitals and suppliers
  - establishing key performance indicators (KPIs)
  - measuring hospital performance against the KPIs.

The two main groups that make up NSW Health (called NSW Health in this report) referred to in this report are the Department of Health (called Health), and the Area Health Services (called Areas).

NSW Health agreed to implement all the recommendations. It had already started to implement a Supply Chain Reform Strategy (SCRS), which it stated would address the problems we identified. This Strategy, implemented in 2000, covered purchasing practices, electronic commerce, electronic catalogue, support functions and basic infrastructure.

At the time, NSW Health said this would lead to the introduction of electronic procurement by the end of 2003 with total savings of $60 million to $80 million. It also advised that it would increase its purchases on health-specific state based contracts from 35% to 60%.

In 2003, NSW Health re-estimated the Supply Chain Reform Strategy projected savings to $56 million over three years to June 2005.

The current change program is a continuation of the Supply Chain Reform Strategy, as expanded through the 2003-05 Supply Chain Reform Business Plan. NSW Health advised this Plan refocussed the program around consistency in procurement business practices in the new Areas, and the proposed shared corporate services group.
Has managing procurement change across the health sector been successful?

NSW Health advised that, as other committees and structures covered a lot of the issues in the recommendations, the Health Audit Committee did not separately monitor the implementation of the recommendations. We were advised that the Strategic Procurement Committee is monitoring the entire reform process.

The original audit and its recommendations were not specifically addressed in any Annual Reports since the original audit, although the SCRS has been discussed.

The future of purchasing

A supply chain covers all the goods and services required to support the operations of an Area Health Service. It includes the people, process and technology to plan supply needs, place orders, receive goods and services, pay suppliers, and manage the performance of Areas, hospitals and suppliers. Effective supply chain management can generate savings from improved management of inventory and payments.

NSW Health expects the Supply Chain Reform Strategy to change the way it purchases and manages its goods and services. Its 2004-05 Procurement Plan reports that:

The major benefits to procurement will be the streamlining of procurement processes and costs, to further aggregate spending and improve the ability to use the buying power of NSW Health to control the cost of goods and services entering the NSW Health system.

NSW Health anticipates that once all its planned changes are made, hospital staff will be able to order supplies on-line from a terminal at the hospital ward. Staff will electronically pick items from a catalogue, and get all approval delegations to make purchases. Centralised purchasing units will aggregate the hospital orders, get a price based on the volume ordered, and send one order to the supplier. The supplier will deliver goods to the hospital, either directly or via a warehouse, whichever is more efficient. Health will also be able to receipt and make payments through the system.

Financial information on NSW Health

NSW Health has 250 hospitals servicing over 1.3 million in-patients annually. The annual budget is $10 billion and employs around 100,000 staff.

NSW Health spends more than $1.3 billion annually on goods and services covering pharmacy, food services, asset management and general purchases. Exhibit 1 shows the major expenditure areas for NSW Health.
Has managing procurement change across the health sector been successful?

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Employee expenses</td>
<td>4,431</td>
<td>4,543</td>
<td>4,822</td>
<td>5,339</td>
<td>5,893</td>
</tr>
<tr>
<td>Food</td>
<td>64</td>
<td>64</td>
<td>69</td>
<td>73</td>
<td>76</td>
</tr>
<tr>
<td>Drugs, medical and surgical supplies</td>
<td>540</td>
<td>569</td>
<td>623</td>
<td>699</td>
<td>766</td>
</tr>
<tr>
<td>Fuel, light, power</td>
<td>52</td>
<td>54</td>
<td>56</td>
<td>59</td>
<td>61</td>
</tr>
<tr>
<td>Visiting medical staff</td>
<td>291</td>
<td>292</td>
<td>320</td>
<td>361</td>
<td>381</td>
</tr>
</tbody>
</table>

Source: 2003-04 Annual Report, p58

We have been advised that approximately 30% of hospital purchases are made through warehouses based at hospitals or the Area Health Services. The remainder is sent directly from suppliers to hospitals.

Thirty per cent of an Area’s expenditure is on asset management, pharmaceuticals and food, all purchased through its own specialised electronic systems. The remainder is mostly on medical and surgical needs and is monitored locally.

**Health Peak Purchasing Council**

The Health Peak Purchasing Council (PPC) was responsible for managing the total cost of the healthcare supply chain for NSW Health, and to provide advice and support to the Areas on procurement, contracting and logistics. NSW Health advises it disbanded the PPC in July 2005.

During the PPC’s existence, some of the changes it implemented included:

- negotiating some state-wide contracts for medicines at cheaper prices
- developing a standard evaluation process for medical equipment and consumables
- trialling a new contract based on committed volume levels
- agreeing new guidelines for managing health-specific state contracts with the Department of Commerce
- convening the Strategic Procurement Committee
- developing a standard tendering and contract document used by all Areas
- monitoring the progress of the Supply Chain Reform Strategy in Areas
- establishing key performance indicators and collating the Areas’ results against these
- reporting annually to Health on the changes achieved in procurement practices and the plans for future years
- assessing the value in including purchases on state contracts.
Has managing procurement change across the health sector been successful?

However, whilst it had the responsibility for the SCRS, the PPC did not have the power to enforce the needed changes in the Areas. This governance model was unable to bring the changes in NSW Health at the desired speed.

Reforming NSW Health

There are two main aspects of reforming the procurement and supply chain - amalgamations of the Area Health Services and the Shared Corporate Services Management Program.

In order to improve governance and achieve savings, a restructure of NSW Health was announced by the Government in July 2004, to take effect from 1 January 2005. It was the first major change for 18 years.

The main part of the restructure was combining 17 Area Health Services to make eight. This is intended to minimise administrative duplication, with any savings to be kept by the Area and redirected to patient care. All Area Boards were dissolved, and Areas are now directly accountable to the NSW Health Director-General. The new geographic break-up of the Areas is shown in Exhibit 2.

Exhibit 2: new Area Health Services

![Exhibit 2: new Area Health Services](source: Planning Better Health, p13)

Change management

NSW Health is moving to a more coordinated centre-led procurement and supply chain management approach. At present it is fragmented, with different models and systems used within and between the Areas. This restricts sharing information and adopting best practices.

NSW Health advises it has a group that will review and coordinate procurement reform and its outcomes to ensure information is shared and the Areas adopt best practices.
NSW Health plans to establish a unit to implement the shared services program. This unit will be responsible for consolidating and managing shared corporate and business services across NSW Health.

With shared services, NSW Health expects:
- a more streamlined system and process
- clearer separation of roles, responsibilities and accountabilities
- greater control of expenditure and better contract management
- information on spending that is more comprehensive and accessible
- greater confidence that what people report is actually happening
- better prices and ‘per unit’ cost
- improved turnover of inventory and reduced storage.

Shared services will be implemented in two stages:
- implement a transitional common procurement business model across the eight Areas, supported by statewide procurement guidelines. This will involve greater centralisation of functions, services, staff and systems at Area level rather than hospital level
- move shared services into three hubs for North, West and South NSW. Non-clinical supplies will be moved first, then clinical supplies. Electronic purchasing will be implemented at the same time.

Health initially planned for shared services to be introduced through 2004 and 2005. With the Area amalgamations, it was delayed to 1 July 2005, with complete implementation over the following 2-3 years. It estimated savings of $100 million through this streamlining to be redirected to patient care. At the time of the audit however, it was still not implemented. Health now plans to introduce shared services over a six-year period.

Health acknowledges the shared services program will require significant changes to established business policies, processes, work practices, IT systems, and the interactions between service providers and their customers - but it has not yet determined what they will be.

NSW Health advises it has developed a shared corporate services strategy, including a corporate services program, to integrate with their clinical care systems.

Progressing the electronic procurement strategy is proving more complex than Health originally anticipated. Health advises it has not yet secured the funding for implementing electronic procurement.

Most IT reforms experience the problems created by this complexity. But at essence, this is not a technical issue. The key focus is procurement and governance reform.

The key requirements for success reside in achieving a consistent procurement business model, effective change-management, and developing clarity of accountability and decision-making for progressing change. In the IT profession this is referred to as harmonising IT governance with business governance, and aligning IT strategy with the needs of the business.
Managing and monitoring Area, hospital and supplier performance

There are problems with comparing Area Health Service performance against targets because the collection and provision of information is done differently in each Area. Some Areas acknowledge that they cannot always provide data. This makes monitoring the progress of both the Supply Chain Reform Program and overall performance doubtful.

Areas have to report every three months against business key performance indicators (KPIs) that were established in January 2005. Reporting against these KPIs is difficult because data has to be taken from different systems, and there are no guidelines on the data to be provided.

Health advises it expects KPI reporting to improve when the planned common IT system and standard Chart of Accounts are implemented.

The Strategic Procurement Committee monitors the progress on KPIs. The following table shows initial Area Health Service performance against these KPIs for the three months ending 31 March 2005. Some Areas have not submitted any reports, or incomplete reports, for the first two quarters of this year because of the Area amalgamations, and their different IT systems.

Exhibit 3: AHS supply chain key performance indicators (March 2005)

<table>
<thead>
<tr>
<th></th>
<th>Greater Western</th>
<th>Hunter/ New England</th>
<th>North Coast</th>
<th>North Sydney/ Central Coast</th>
<th>South East Sydney/ Illawarra</th>
<th>Sydney West</th>
</tr>
</thead>
<tbody>
<tr>
<td>Order processing done in 2 days of request</td>
<td>NDP</td>
<td>94.5%</td>
<td>99%</td>
<td>99%</td>
<td>92.4%</td>
<td>100%</td>
</tr>
<tr>
<td>On time delivery</td>
<td>NDP</td>
<td>81%</td>
<td>90%</td>
<td>NDP</td>
<td>NDP</td>
<td>NDP</td>
</tr>
<tr>
<td>Stock received on first request</td>
<td>94.9%</td>
<td>99.1%</td>
<td>99.2%</td>
<td>98.3%</td>
<td>98.1%</td>
<td>99.9%</td>
</tr>
<tr>
<td>Cost of supply as a percentage of the spend on goods and services</td>
<td>NDP</td>
<td>NDP</td>
<td>45.8%</td>
<td>NDP</td>
<td>NDP</td>
<td>NDP</td>
</tr>
<tr>
<td>Average number of days to turn over warehouse items</td>
<td>46.8</td>
<td>23</td>
<td>39.5</td>
<td>25</td>
<td>24</td>
<td>26</td>
</tr>
<tr>
<td>Average number of days from receipt of invoice to payment</td>
<td>NDP</td>
<td>39</td>
<td>37.5</td>
<td>65</td>
<td>35</td>
<td>45</td>
</tr>
<tr>
<td>Savings made by contracts</td>
<td>NDP</td>
<td>438,000</td>
<td>160,000</td>
<td>515,000</td>
<td>150,000</td>
<td>968,000</td>
</tr>
</tbody>
</table>

No report provided for Greater Southern or Sydney South West AHS.
NDP = no data provided by AHS on this KPI.
Source: KPI reports from AHS for quarter ending March 2005
Has managing procurement change across the health sector been successful?

Health cannot advise, and we cannot tell, if the time taken from purchase to delivery of a good has improved since our last audit.

Supply Chain Reform Strategy performance

As well as reporting on business performance, Areas have had to complete quarterly Health Service Progress Reports on the Supply Chain Reform Strategy since January 2005. The 49 operational KPIs cover warehouses, stock, ordering, sourcing, contracts, electronic purchasing, record keeping, and expenditure.

Reporting against these KPIs should enable cross-Area Health Service benchmarking to occur. However, little data is provided, and there is no auditing to confirm the accuracy of the information that is given. For the June 2005 report, the Areas were variable in providing information, giving data for between none and 12 items.

The following table shows the progress in implementing the Strategy as at 31 March 2005.

<table>
<thead>
<tr>
<th>SCRS stage</th>
<th>Number of milestones</th>
<th>Due date for completion</th>
<th>Percentage completed</th>
</tr>
</thead>
<tbody>
<tr>
<td>Stage 1</td>
<td>19</td>
<td>June 2003 - June 2004</td>
<td>70%</td>
</tr>
<tr>
<td>Stage 2</td>
<td>8</td>
<td>July - December 2004</td>
<td>50%</td>
</tr>
<tr>
<td>Stage 3</td>
<td>13</td>
<td>January - December 2005</td>
<td>58%</td>
</tr>
</tbody>
</table>

Providing feedback on performance

There is only limited feedback by Health to the Areas on their performance.

In mid-2005, Area CEOs were briefed about their performance against the strategic procurement KPIs. They were also given a comparison of the Areas’ progress on milestones for the SCRS against overall Health performance for the prior quarter, and any identified strengths and weaknesses.

However, despite the strategic importance of this information, this is not a regularly scheduled briefing. Health advises it plans to start more regular and coordinated reporting to the Areas.

Monitoring supplier performance has improved

As well as monitoring business and supply chain reform performance as discussed above, Health also monitors the performance of suppliers.

Health implemented the Health Quality Reporting System (HQRS) in early 2004. This records product and supplier information when problems are identified with a product, and the subsequent outcome. It provides a framework for the management of product and service quality issues, and tracks supplier performance across all of Health. All Areas have access to update and review this system.
Health has found that with the HQRS, the response time for fixing product quality problems has substantially improved. The information is used to manage supplier performance at a statewide level. It will also be used during contract renewals, as it provides information on supplier’s service performance and their responsiveness to any issues.

**Priority issue requiring attention**

In our view, to assess the effectiveness of all the changes being made, there would be value in Health establishing clearly defined indicators and starting to collect information against these now. Indicators might include:

- turnaround times for ward staff ordering
- cost of hospital supplies vs total expenditure
- cost per unit of a representative group of supplies
- staff and resources involved in purchasing
- cost of providing a good (includes storage and movement) as part of total cost
- length of time to wait for an ordered good
- payment of suppliers within their payment terms.

NSW Health advises it will work to develop more meaningful KPIs.
What changes have been made to purchasing practices?
Overall position of NSW Health purchasing

Overall, NSW Health has not made as much progress on improving purchasing as it initially planned.

NSW Health advises this has been largely due to problems with using the Department of Commerce’s SmartBuy. It needed to restart its own implementation of e-marketplace using its own resources, but also advises that any progress on this will depend on further funding.

There is still no standardised procurement process encompassing IT systems, guidelines, ordering and purchasing methods, prices, contracts, payment methods, KPIs and communication processes.

However Health has made progress in implementing the Supply Chain Reform Strategy (SCRS). Its report on action taken against our specific recommendations is at Appendix 2.

Total estimated savings to 30 June 2005, since the procurement and supply chain reform agenda was introduced in 2000, is $60.6 million.

<table>
<thead>
<tr>
<th>Year</th>
<th>2000-01</th>
<th>2001-02</th>
<th>2002-03</th>
<th>2003-04</th>
<th>2004-05</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total savings</td>
<td>introduced</td>
<td>14</td>
<td>27</td>
<td>12</td>
<td>7 (estimated)</td>
</tr>
</tbody>
</table>

Sources: NSW Health Procurement Plans 2004-05, 2003-04, 2002-03; PPC meeting 27 July 2005

NSW Health’s reported achievements in 2002-03 included:
- increased spending under health-specific state contracts from $235 million to $320 million
- increased spending under general state contracts from $240 million to $300 million, giving savings of approximately $8 million
- approximately 48% of total spend is on contract
- established groups of Areas to aggregate purchasing power, gain greater discounts, and share best available practice
- established KPIs for: service, risk, supply overheads, inventory, creditor days, cost, contract savings, contract performance, customer satisfaction
- new contract established covering almost all pharmaceutical products
- closure of 42 warehouses with estimated recurrent savings of $13.4 million and $8.4 million as a one-off saving.

Reported achievements in 2003-04 included:
- introducing e-tendering systems
- value of goods and services purchased on health-specific state contracts increased from $320 million to $360 million
- $84 million spent on state contracts
- purchases made on all state contracts increased to 50% of expenditure
- 37.5% of Area spending is controlled through local formal contracts or agreements
- introduced Health Quality Reporting System
- new guidelines for managing health-specific state contracts.
What changes have been made to purchasing practices?

Improvements in warehousing

The number of warehouses reduced from 74 in 1998 to 26 in 2004. NSW Health has developed a statewide plan for warehousing and distribution. It is progressively consolidating existing warehouses as part of the Area mergers. Following is a table of changes in warehouse numbers since the last audit.

<table>
<thead>
<tr>
<th>New AHS</th>
<th>Old AHS</th>
<th>Number in 2000</th>
<th>Number in 2005</th>
<th>Proposed</th>
</tr>
</thead>
<tbody>
<tr>
<td>Northern Sydney Central Coast</td>
<td>Central Coast</td>
<td>1</td>
<td>1</td>
<td>1</td>
</tr>
<tr>
<td></td>
<td>Northern Sydney</td>
<td>5</td>
<td>1</td>
<td></td>
</tr>
<tr>
<td>North Coast</td>
<td>Northern Rivers</td>
<td>6</td>
<td>3</td>
<td>1</td>
</tr>
<tr>
<td></td>
<td>Mid North Coast</td>
<td>3</td>
<td>2</td>
<td></td>
</tr>
<tr>
<td>Hunter New England</td>
<td>Hunter</td>
<td>8</td>
<td>1</td>
<td>1</td>
</tr>
<tr>
<td></td>
<td>New England</td>
<td>3</td>
<td>1</td>
<td>1</td>
</tr>
<tr>
<td>Sydney South West</td>
<td>Central Sydney</td>
<td>2</td>
<td>1</td>
<td>1</td>
</tr>
<tr>
<td></td>
<td>South Western Sydney</td>
<td>6</td>
<td>3</td>
<td></td>
</tr>
<tr>
<td>South Eastern Sydney</td>
<td>South Eastern Sydney</td>
<td>2</td>
<td>1</td>
<td>1</td>
</tr>
<tr>
<td>Illawarra</td>
<td>Illawarra</td>
<td>1</td>
<td>1</td>
<td></td>
</tr>
<tr>
<td>Greater Western</td>
<td>Macquarie</td>
<td>1</td>
<td>1</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Far West</td>
<td>3</td>
<td>3</td>
<td>1</td>
</tr>
<tr>
<td></td>
<td>Mid Western</td>
<td>8</td>
<td>1</td>
<td>1</td>
</tr>
<tr>
<td>Sydney West</td>
<td>Wentworth</td>
<td>2</td>
<td>2</td>
<td>1</td>
</tr>
<tr>
<td></td>
<td>Western Sydney</td>
<td>7</td>
<td>2</td>
<td></td>
</tr>
<tr>
<td>Greater Southern</td>
<td>Greater Murray</td>
<td>7</td>
<td>1</td>
<td>1</td>
</tr>
<tr>
<td></td>
<td>Southern</td>
<td>2</td>
<td>1</td>
<td></td>
</tr>
<tr>
<td>Total</td>
<td></td>
<td>67</td>
<td>26</td>
<td>10</td>
</tr>
</tbody>
</table>

Source: NSW Health Warehouse Survey

During 2003-04 Areas reduced their inventory holdings by about a third compared to 2001-02. The average value of inventory across NSW Health was $58.3 million ($86.4 million in 2001-02). Also, the reduced warehouse numbers saved approximately $1.6 million in operational costs.

NSW Health advises it is piloting two third-party logistics providers that it expects will improve its stock management models.

One Area consolidated its purchasing, and reports that it makes about 80% savings on delivery. It achieved this by having one delivery day on one truck from one centrally coordinated supplier.
What changes have been made to purchasing practices?

**Improving contracts**

In our 2002 audit, we recommended that NSW Health improve its contract management. NSW Health has progressed this issue but there have been a number of significant problems and obstacles.

NSW Health advises that it is working on developing improved contracting processes by removing duplication in the current state contract system, simplifying the contracting process and reducing Area staff resources, in conjunction with the Department of Commerce.

The following table shows spending on health-specific state contracts over the last three years.

<table>
<thead>
<tr>
<th>Exhibit 7: health-specific state contracts since the last audit</th>
</tr>
</thead>
<tbody>
<tr>
<td>2002-03</td>
</tr>
<tr>
<td>$ spend</td>
</tr>
<tr>
<td>% spend on all contracts</td>
</tr>
<tr>
<td>Number of contracts</td>
</tr>
</tbody>
</table>

NYC = not yet calculated

*Source: Procurement Plans 2003-04 and 2004-05*

However, NSW Health does not have the systems to identify its purchase volumes. This hinders its ability to identify and negotiate the best prices to purchase items.

Despite this system problem, Areas have taken action to negotiate better value-for-money contracts.

**Case study**

One Area Health Service has done an orthopaedic whole-of-Area tender. To gain the support of the medical staff the Area had to offer more than only cost savings. It negotiated for suppliers to give a rebate based on agreed expenditure targets that could be used to purchase equipment needed by hospitals.

**Problems in monitoring expenditure**

Another problem with contracts is that NSW Health completely relies on the Department of Commerce to advise on its contract expenditure. The Department of Commerce can advise on health-specific contract expenditure, but cannot report on general expenditure, as it does not separate this expenditure between agencies.

In 2004-05, NSW Health expenditure through all state contracts was conservatively estimated at $450 million. NSW Health reports making $5.8 million in new savings from all contracts.

In 2003-04, 40-50% of health system suppliers were on state contract. Another 37.5% of Area spending was controlled through formal contracts or agreements at Area/hospital level. Three-quarters of the expenditure not made through state contracts, was controlled through local contractual agreements.
What changes have been made to purchasing practices?

Difficulties in using state contracts

All Areas are required to use state contracts, but not all do, for three reasons. The first is that if an Area already has a contract in place, it can continue to use the contract until it expires.

Second, some Areas consider there is little value added by state contracts. This is because the state system cannot handle the large information required to support Area needs, for instance, variations to pricing structures. Also, most state contracts do not commit volume sales to suppliers. Some staff would like to see NSW Health negotiate its own contracts.

Third, a lot of medical consumables are specific to a type of equipment, which can restrict the opportunities for negotiating deals. However, NSW Health advised it is now reviewing how medical equipment and consumables are purchased.

Case study

NSW Health, with the Department of Commerce, negotiated a sole supplier for needles and syringes, but not all hospitals could use the chosen type because they were not always compatible with existing equipment.

Also, the needle exchange clinics in one Area could not accept the contract, because the users did not like the needle and syringe type chosen by NSW Health. This led to confrontations with clinical staff, and potential problems with threats of reusing their preferred needle and syringe. The Area considered that it had no option but to decline to use the sole supplier.

NSW Health considers that state contracts do deliver value. It admits that in some cases, large well-resourced metropolitan Areas could negotiate better contract prices for products that meet their needs, as there is currently some cross-subsidisation of rural locations. However, state contracts give administrative savings, eliminate probity concerns, and can generate savings in the cost of implementation and from volume purchasing.

New contracting practices

NSW Health is currently implementing a new strategy for Areas on state contracts with annual committed volumes, and it expects to make significant savings. The strategy is being used for renewing the contract on caps, gowns, masks and overshoes, as discussed in the next case study. This new contract type is designed to stop Areas entering into price negotiations with contractors after a contract is awarded.
What changes have been made to purchasing practices?

Case study

NSW Health is renewing its contract on caps, gowns, masks and overshoes based on a commitment to purchase a minimum volume.

Tenderers offered a range of prices based on different quantities, as well as a discount for dollar-value commitments by the Areas. All Areas were requested to make a volume purchase commitment from six selected suppliers over the following year. The Area’s purchase commitments will be aggregated, and contracts entered with all the different suppliers. This is a modification to the usual state contracts whereby the volume discount is only available to NSW Health as a whole.

New guidelines are also being developed for the management of health-specific contracts, to ensure the best outcome for NSW Health, which may not necessarily be the best for individual Area Health Services. Targets to be achieved and detailed roles and responsibilities, by both Department of Commerce and groups within NSW Health, will be agreed in a Performance Partnership Agreement.

Improvements through contract standardisation

Another improvement by NSW Health in managing contracts is the implementation of a contract and tenders database, which is used by all Areas to record all their contracts and tenders. The database has reduced administrative costs and the time taken to evaluate tender submissions. It also allows the Areas to monitor when contracts need to be reviewed before they expire.

NSW Health has also developed a standard tendering and contract document. Areas use this to negotiate their own contracts for items not on state contract. A clause allowing other Areas to use the contract is included. This is used especially by rural Area Health Services to gain the benefits of cheaper metropolitan-negotiated contracts.

However, there are complications to be managed when an Area tries to introduce its own contracts.

Case study

One Area negotiates contracts for individual hospitals as necessary, rather than across the Area. This is because each hospital operates independently, and there is no one clinical officer responsible for each clinical area across the Area.

The Area’s purchasing section does tenders, supply agreements and contact management for the Area. It stated that it does not provide as much value-add as it could for non-tender orders, where it only processes requests.

Involvement of clinical staff

It is important to have clinical staff agree to any major contractual changes on medical items. If staff disagree with the changes, Areas and hospitals could find changes difficult to implement.
What changes have been made to purchasing practices?

Case study
Pharmaceutical contracts need careful monitoring. For instance, a contract for one drug, which has a restricted choice in the strengths available, is for mental health patients. The risk is that giving them additional tablets, or tablets that look different from what they are used to, the person may refuse to take them. One Area Health Service, on the advice of clinical staff, refused to change over because of safety concerns for their patients.

One reason that clinicians may not agree to contractual changes, is that suppliers sometimes sponsor medical services or provide in-kind funding for medical positions. We have been advised the NSW Health Code of Conduct does not allow this practice. No records are kept of additional funding and support given by suppliers. If a supplier lost a contract and stopped their sponsorship, the services might have to cease.

NSW Health advise that it is involving relevant medical practitioners through clinical networks to assess new clinical contracts before including or changing any products.

Lessons
In our opinion the main lessons for implementing more effective contracts are:

- need for senior clinicians to have some ownership in the decision making process
- need to have a partnership approach between the Areas and suppliers when an Area introduces changes
- need to consider any implications a major contract change may have for changing the marketplace, eg creating a monopoly.

Paying suppliers on time
NSW Health still does not always pay its suppliers promptly, because not all Areas have the necessary funds. A lot of Area resources are used to manage suppliers’ complaints about this problem.

NSW Health advises it expects this problem to be eliminated when it implements the shared corporate services with a central payment system.

Health does not collect data on, monitor, or enforce the timeliness of paying suppliers. It is seen as an Area responsibility.

If suppliers remain unpaid, the worst case scenario is that they will stop supply. Not paying in a timely manner also impacts on price, reliability of supply and ability to negotiate better deals in the long-term.

Some Areas argue that NSW Health will have trouble negotiating better contracts while this situation continues. They consider that NSW Health needs to improve funding processes to Areas. For instance, one Area Health Service advised it was given $10 million to spend in the last two weeks of last financial year. It stated that this was not the first time this had happened.
Electronic procurement

NSW Health advises that progressing the electronic procurement strategy is proving more complex than originally anticipated, and availability of funding will decide if it is progressed.

The e-marketplace will manage purchasing through a standardised electronic procurement system, single e-catalogue, standard health vendor file, streamlined transaction procure-to-pay process, and a single Chart of Accounts, all on a single integrated IT system.

This integrated system does not exist at present. This makes data collection, information sharing and performance management difficult because the Areas use different systems. NSW Health anticipates having this integrated system in place within the next three years.

NSW Health advises there were delays in implementing e-procurement because:
- it needed to gain Area and hospital buy-in to the right model
- Areas currently use different IT systems
- it needs suppliers to support the change
- there is no standard catalogue
- there were problems with the initially proposed model, and NSW Health needed to recommence the implementation process
- resources are inadequate.

Nevertheless, NSW Health has made some significant progress on this issue. Most Areas have online requisition and ordering within their financial systems, and are moving to automated inventory requisition systems. Items are now barcoded in most Areas. Some Areas are trying to have suppliers send ordered goods directly to hospitals rather than the warehouses.

Case study

One hospital uses an imprest order for clinical goods. Items are barcoded, and there is frequent scanning of storage bins for items that are constantly used, to top up supplies to meet the imprest amount.

If items are not in stock at the Area warehouse, the hospital units will put in non-stock requisitions approved by the delegated authority.

It uses planned or standing orders for items not on imprest but needed regularly, eg clean gowns, oncology drugs.

The main changes made since the original audit in this hospital is the improvements in the imprest system, barcoding which makes monitoring much easier, less staff time is wasted and storerooms now have locks.
What changes have been made to purchasing practices?

Catalogue still to be implemented

NSW Health started developing its own e-catalogue about 15 years ago, but to this point it is still not implemented.

Every Area Health Service wants a catalogue so they can collect accurate data on what they buy and what it costs, and to develop contract specifications. It is also difficult to quantify savings generated from changes if they do not know what is already bought or needed.

At the time of the original audit, the government had advised that all agencies would have to use SmartBuy to purchase all their goods. This would include an e-catalogue to cover all items needed by all agencies. It would be available by the end of 2002. NSW Health was later advised that the Department of Commerce could not create a catalogue that contained all the information fields NSW Health needed. NSW Health then started again to develop its own e-catalogue. All Areas agreed in late 2003 to the e-catalogue project, which involved implementing electronic systems and establishing the right coding.

A single health catalogue is being developed by a contracted company. Health has also been preparing health vendor guidelines for a single health catalogue since 2002. It expects it to be completed during 2005-06, but it will only initially include the top 40 Health-nominated vendors.

When introduced, the e-catalogue will be used as a management tool for monitoring supplies used, needed and in stock. To have one catalogue with a uniform set of product codes by the end 2006, all Areas will have to change stock numbers.

Areas have initiated their own changes

Because of the problems discussed above, some Areas have initiated their own changes in practice.

NSW Health advises that a number of Areas have taken the initiative and developed their own catalogue for major spend items. The catalogue is for items regularly purchased, with a pre-approval amount limit, so the lengthy normal purchase order process does not have to be followed.

Case study

One Area reduced the amount of paper it receives from suppliers by cutting down on the invoices received. It now gets an electronic file from large suppliers to upload direct to the general ledger.

It gave suppliers a standard format for the invoice, so it receives only one invoice for a large dollar amount, rather than hundreds of small dollar amount invoices. The Area Health Service needs to have confidence in the supplier as it receives only one invoice at infrequent intervals.

This change has reduced the number of accounts payable clerks from a staff of 20 by three or four through ‘natural attrition’.
What changes have been made to purchasing practices?

**Joint Area Health Service initiatives**

Some Areas joined together during 2003 to implement their own procurement initiatives. One was to combine product volumes to achieve additional savings on those available through state or individual Area-level contracts. This concept was concluded when the restructure was announced in 2004. However, the Areas still saved $4.5 million in 2003-04, and some Areas still actively collaborate when necessary.

**Case study**

One Area has centralised the management of the IT system for three Area Health Services, which gives a standardised system for the west of NSW. The other Areas changed their financial systems and chart of accounts to enable the lead Area to act on their behalf.

These Areas are trying to achieve savings in accounts payable by having all invoices scanned and sent to relevant people for sign-off for non-purchase-order based purchases.

At the moment, each Area still purchases items for itself, with the lead Area doing only some joint payment work. The Areas want to centralise procurement services, but they still need to uniformly name each product.

This model is aimed at gaining maximum efficiency from staff employed in all the Areas. For example, one Area will print cheques and process payments, but other Areas will specialise in other parts of procurement, for instance talking to suppliers. The Areas share their services, but run like a single business unit.

**Piloting the e-marketplace**

NSW Health has also continued to develop its own e-marketplace, which it plans to implement across the state over 12-18 months from March 2006.

One Area Health Service will pilot the e-marketplace from 1 November 2005, which will be evaluated after three months. This will include the central health catalogue, procurement intelligence, financial management system and integration of Smartbuy. The trial will have only 40 suppliers, and be run in parallel with the current system.

The following diagram shows the design of the new NSW Health e-marketplace.
What changes have been made to purchasing practices?

Exhibit 8: NSW Health e-marketplace

Savings from the e-marketplace

Expected e-marketplace savings and benefits include streamlined processes, reduced IT infrastructure and hosting costs, reduced purchasing costs, reduced transaction time, decreased transaction and staff costs, limits on the selection of products available, control over non-contract/catalogue purchases and improved contract prices with known usage commitments. However, the Areas have not seen any savings yet.

Different reports and business cases supplied by NSW Health give different anticipated savings amounts from the e-marketplace. One report advises estimated savings of 5-10% of their costs. A second advises between $24 million and $46 million will be saved annually. Another reports anticipated savings of $109 million over five years to 2009-10, with $46 million saved after 2009-10.

These reported variations in planned savings from the e-marketplace, along with the delays in implementing both the e-marketplace and the Supply Chain Reform Strategy, highlight that NSW Health does not yet have the full capability to implement, quantify and monitor the supply chain reform program.

NSW Health advises that all these problems will be addressed with its e-marketplace pilot program, standard IT system and Chart of Accounts, and shared corporate services program.
What changes have been made to purchasing practices?

**Alternative systems provided by suppliers**

Even though NSW Health is implementing the pilot as described above, some companies are already offering an alternate supply system that allows Areas to make purchases by ordering from the supplier’s own online models.

**Case study**

All metropolitan Area Health Services use an online electronic ordering system for buying stationary, printers, etc from selected suppliers. One Area advised that using this approach, it has been able to control and reduce costs, and orders are delivered the next day. It also advised it has seen a decrease in expenditure and against budget.

**Priority issues requiring attention**

Problems that could arise when implementing the e-marketplace include:

- few suppliers will be on the e-marketplace initially so there will be different ways to order and process goods and services
- any electronic catalogue suppliers currently use will not be linked to NSW Health’s system
- an interface between all the systems is not in place yet
- there always will be a lot of paper invoices, because some small rural businesses will never be able to implement electronic systems
- sites will not know if there is a problem or delay when they place orders through Smartbuy
- timing of clinical supplies is vital, so hospital staff might be tempted to place overorders and hoard purchases
- there is still user confusion about what is meant to be happening and when
- the trial date of 1 November 2005 deadline appears to be ambitious.
Appendix 1: About the audit

Audit objective, criteria, scope and focus

In 2002 we conducted a performance audit titled *electronic procurement of hospital supplies* in NSW Health. Our report identified a range of issues and impediments, and made a considerable number of specific recommendations to assist NSW Health.

This follow-up performance audit provides an update on progress by NSW Health in purchasing hospital supplies. In particular we reviewed:

- whether the accepted recommendations from the original audit were implemented
- what changes have been made to purchase hospital supplies more efficiently and economically
- what benefits this has generated.

Audit approach

We obtained sufficient evidence to show what NSW Health did to progress accepted recommendations, and what changes had occurred as a result of implementation.

We also obtained specific evidence to show what changes they had implemented to their procurement practices.

Findings were based on the evidence collected through document analysis, interviews with NSW Health and Area Health Service staff, and NSW Health’s formal response to the recommendations.

Cost of the audit

The estimated cost was $126,000, which includes printing and overheads.

Acknowledgement

The Audit Office gratefully acknowledges the cooperation and assistance provided by representatives of NSW Health including Health head office, and SouthEastern Sydney/Illawarra, Hunter/New England and Sydney West Area Health Services.

Audit Team

Our team leader for this performance audit was Sandra Tomasi. Sean Crumlin provided direction and quality assurance.
## Appendix 2: Schedule of actions on 2002 recommendations

<table>
<thead>
<tr>
<th>Audit recommendation</th>
<th>2002 response</th>
<th>2005 response</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Use connected computers across the state, and establish standard business processes</td>
<td>Implement an e-Marketplace or the Supply Chain Reform Strategy.</td>
<td>Implementing e-marketplace, including developing a whole-of-Health product catalogue. Standardised some processes. Developing a single financial management system.</td>
</tr>
<tr>
<td>2. Track products from purchase to use</td>
<td>Create an e-catalogue. Introduce barcodes and scanning.</td>
<td>Selected a standardised product identification system that is being incorporated into the e-marketplace.</td>
</tr>
<tr>
<td>3. Determine and collect information needed across NSW Health</td>
<td>Establish KPIs (under Supply Chain Reform Strategy). Develop a system to record costs.</td>
<td>AHS report against KPIs quarterly. Health Quality Reporting System (HQRS) collects product quality and supplier information.</td>
</tr>
<tr>
<td>5. Assess AHS capability to implement e-procurement</td>
<td>Multiple teams established to assess AHS readiness.</td>
<td>AHS ability to implement e-marketplace assessed in 2004. First implementation of e-marketplace in one AHS.</td>
</tr>
<tr>
<td>6. Improve collaboration, sharing of information and better practices across the state</td>
<td>Health Peak Purchasing Council website includes information on suppliers and products and purchasing policies. Will include benchmark data on AHS’.</td>
<td>AHS can view and take advantage of other AHS-negotiated contracts. Networking groups facilitated by Strategic Procurement Committee. Supply Chain Reform project managers meet quarterly. AHS performance benchmarked against state average and best performing AHS, and reported to all AHS Chief Executives.</td>
</tr>
<tr>
<td>Audit recommendation</td>
<td>2002 response</td>
<td>2005 response</td>
</tr>
<tr>
<td>----------------------</td>
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<td>---------------</td>
</tr>
<tr>
<td>7. AHS' to have greater responsibility and accountability for their e-procurement reforms</td>
<td>Health-specific state contracts provide flexibility for AHS to gain better prices. PPC Strategic Planning Committee exploring alternatives.</td>
<td>Health-specific state contracts now negotiated at 'best level', i.e. whole-of-state, groups of AHS or individual AHS.</td>
</tr>
<tr>
<td>8. Consider purchasing based on clinical/procedural needs</td>
<td>Increase purchases though state contracts to 60% in two years. AHS-negotiated contracts to be offered to all AHS. PPC assessing clinical procedure-based contracts.</td>
<td>Strategic Procurement Committee looking at strategic procurement (high-value/high-risk items). Trialling new purchasing arrangements. Approximately $450 million purchased on State Contracts.</td>
</tr>
<tr>
<td>9. Improve management of Health-specific State Contracts, and assess their value (monetary and benefits)</td>
<td>Reviewing state contracts, introduce KPIs and a common catalogue. Review performance agreement between NSW Supply and PPC.</td>
<td>Renegotiated with Department of Commerce the partnership arrangement for state purchases, including a performance agreement. New guidelines for managing state contracts developed in 2004. Spend on state contracts collected quarterly. Supplier performance reported through HQRS.</td>
</tr>
<tr>
<td>10. Pay creditors to get settlement discounts</td>
<td>Monitor performance in paying creditors, assess the existing system and maximise prompt payment discounts.</td>
<td>AHS financial performance, including payment cycle, monitored by Health Chief Financial Officer.</td>
</tr>
</tbody>
</table>
Appendix 3: Glossary

<table>
<thead>
<tr>
<th>Term</th>
<th>Definition</th>
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</thead>
<tbody>
<tr>
<td>Area Health Service (Areas or AHS)</td>
<td>Eight Areas in NSW. Role is to promote, protect and maintain public health and to provide health services in NSW.</td>
</tr>
<tr>
<td>electronic catalogue (e-catalogue)</td>
<td>An electronic list of material, products or service information, to support the business processes. In Health, this will include a product code, product description, price, supplier details and code.</td>
</tr>
<tr>
<td>electronic commerce (e-commerce)</td>
<td>The transacting of business electronically over the internet, rather than on paper. It can be between two businesses transmitting funds, goods, services and/or data, or between a business and a customer.</td>
</tr>
<tr>
<td>electronic procurement (e-procurement)</td>
<td>Use web-based technologies and communication to connect buyers and sellers. Facilitates the process from requisition and approval of purchases through to receipt and settlement.</td>
</tr>
<tr>
<td>e-marketplace</td>
<td>An on-line environment where accredited buyers and suppliers can conduct business, including identification and selection of goods and services, and the placement and tracking of orders, invoices and payments.</td>
</tr>
<tr>
<td>Health Peak Purchasing Council (PPC)</td>
<td>Responsible for managing the total cost of the healthcare supply chain for NSW Health, and to provide advice and support to the Areas on procurement, contracting and logistics. It was disbanded in July 2005.</td>
</tr>
<tr>
<td>Health Quality Reporting System (HQRS)</td>
<td>Electronic recording of product and supplier information by NSW Health when problems are identified with a product, and the resolution of the problem.</td>
</tr>
<tr>
<td>imprest</td>
<td>Cost centre managers pre-set the maximum stock level to be maintained in a hospital ward. This level is checked and replenished regularly by the supply section in each AHS.</td>
</tr>
<tr>
<td>NSW Health</td>
<td>NSW Health is made up of the Department of Health, Area Health Services, Health Administration Corporation and Ambulance Service. The Department is responsible for providing advice to government, strategic planning and policy development, performance management and strategic financial and asset management. Area Health Services are responsible for the planning, delivery and coordination of local health services in the areas they cover.</td>
</tr>
<tr>
<td>procurement</td>
<td>A process involving all activities, following the decision that a good, an asset, facilities or service is required.</td>
</tr>
<tr>
<td>SmartBuy</td>
<td>The product ordering system that was to be implemented across all state agencies by the government.</td>
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<tr>
<td>Strategic Procurement Committee</td>
<td>The internal Health committee responsible for monitoring the implementation of the supply chain reform process.</td>
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<tr>
<td>Supply Chain Reform Strategy (SCRS)</td>
<td>The strategic framework for reforming NSW Health’s supply chain.</td>
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<td>------------------------------------</td>
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<tr>
<td>supply chain</td>
<td>Covers all goods and services required to support the operations of an AHS, including medical, surgical and pharmaceutical supplies, support services, maintenance services and capital equipment.</td>
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</table>
Performance Audits by the Audit Office of New South Wales
Performance Auditing

What are performance audits?
Performance audits are reviews designed to determine how efficiently and effectively an agency is carrying out its functions.

Performance audits may review a government program, all or part of a government agency or consider particular issues which affect the whole public sector.

Where appropriate, performance audits make recommendations for improvements relating to those functions.

Why do we conduct performance audits?
Performance audits provide independent assurance to Parliament and the public that government funds are being spent efficiently and effectively, and in accordance with the law.

They seek to improve the efficiency and effectiveness of government agencies and ensure that the community receives value for money from government services.

Performance audits also assist the accountability process by holding agencies accountable for their performance.

What is the legislative basis for Performance Audits?
The legislative basis for performance audits is contained within the Public Finance and Audit Act 1983, Part 3 Division 2A, (the Act) which differentiates such work from the Office’s financial statements audit function.

Performance audits are not entitled to question the merits of policy objectives of the Government.

Who conducts performance audits?
Performance audits are conducted by specialist performance auditors who are drawn from a wide range of professional disciplines.

How do we choose our topics?
Topics for performance audits are chosen from a variety of sources including:

- our own research on emerging issues
- suggestions from Parliamentarians, agency Chief Executive Officers (CEO) and members of the public
- complaints about waste of public money
- referrals from Parliament.

Each potential audit topic is considered and evaluated in terms of possible benefits including cost savings, impact and improvements in public administration.

The Audit Office has no jurisdiction over local government and cannot review issues relating to council activities.

If you wish to find out what performance audits are currently in progress just visit our website at www.audit.nsw.gov.au.

How do we conduct performance audits?
Performance audits are conducted in compliance with relevant Australian standards for performance auditing and operate under a quality management system certified under international quality standard ISO 9001.

Our policy is to conduct these audits on a "no surprise" basis.

Operational managers, and where necessary executive officers, are informed of the progress with the audit on a continuous basis.
What are the phases in performance auditing?

Performance audits have three key phases: planning, fieldwork and report writing.

During the planning phase, the audit team will develop audit criteria and define the audit field work.

At the completion of field work an exit interview is held with agency management to discuss all significant matters arising out of the audit. The basis for the exit interview is generally a draft performance audit report.

The exit interview serves to ensure that facts presented in the report are accurate and that recommendations are appropriate. Following the exit interview, a formal draft report is provided to the CEO for comment. The relevant Minister is also provided with a copy of the draft report. The final report, which is tabled in Parliament, includes any comment made by the CEO on the conclusion and the recommendations of the audit.

Depending on the scope of an audit, performance audits can take from several months to a year to complete.

Copies of our performance audit reports can be obtained from our website or by contacting our Office Services Manager.

How do we measure an agency’s performance?

During the planning stage of an audit the team develops the audit criteria. These are standards of performance against which an agency is assessed. Criteria may be based on government targets or benchmarks, comparative data, published guidelines, agencies corporate objectives or examples of best practice.

Performance audits look at:

- processes
- results
- costs
- due process and accountability.

Do we check to see if recommendations have been implemented?

Every few years we conduct a follow-up audit of past performance audit reports. These follow-up audits look at the extent to which recommendations have been implemented and whether problems have been addressed.

The Public Accounts Committee (PAC) may also conduct reviews or hold inquiries into matters raised in performance audit reports. Agencies are also required to report actions taken against each recommendation in their annual report.

To assist agencies to monitor and report on the implementation of recommendations, the Audit Office has prepared a Guide for that purpose. The Guide, Monitoring and Reporting on Performance Audits Recommendations, is on the Internet at www.audit.nsw.gov.au/guides-bp/bpglist.htm

Who audits the auditors?

Our performance audits are subject to internal and external quality reviews against relevant Australian and international standards. This includes ongoing independent certification of our ISO 9001 quality management system.

The PAC is also responsible for overseeing the activities of the Audit Office and conducts reviews of our operations every three years.

Who pays for performance audits?

No fee is charged for performance audits. Our performance audit services are funded by the NSW Parliament and from internal sources.

For further information relating to performance auditing contact:

Stephen Horne
Assistant Auditor-General,
Performance Audit
(02) 9275 7278
email: stephen.horne@audit.nsw.gov.au
# Performance Audit Reports

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