



Management of School Funds



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Auditor-General

Management of School Funds

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Victorian Auditor-General's Office
Auditing in the Public Interest

The Hon. Robert Smith MLC
President
Legislative Council
Parliament House
Melbourne

The Hon. Jenny Lindell MP
Speaker
Legislative Assembly
Parliament House
Melbourne

Dear Presiding Officers

Under the provisions of section 16AB of the *Audit Act 1994*, I transmit my performance report on *Management of School Funds*.

Yours faithfully



D D R PEARSON
Auditor-General

6 May 2009

Foreword

Provision of quality education depends greatly on the effective and efficient management of the resources available to schools.

Schools seek to supplement their resources through a variety of means, for example fund raising events and voluntary financial contributions from parents. Another way is through a school cooperative which, once formed and approved, provides the school with access to borrowed funds.

School councils must have appropriate policies, guidelines and accounting systems to effectively manage these funds. It is also important they assure parents and the school community, through timely financial reporting, that these funds are being used to optimise student's learning experiences.

It is pleasing to note the initiatives of DEECD in recent years to assist schools in the management of their funds through the introduction of the school administration and finance system – CASES21, and the professional development programs available to school administrators. These initiatives have contributed to the effective management of funds by schools.

Clarifying the legal implication for schools of borrowings by cooperatives and the issue of insurance cover of jointly funded school facilities will serve to strengthen funds management.



D D R PEARSON
Auditor-General

6 May 2009

Contents

Foreword	v
1. Audit summary	1
1.1 Introduction	1
1.2 Overall conclusion	1
1.3 Key findings	2
1.4 Recommendations	2
2. Audit Act 1994 section 16—submissions and comments	3
2.1 Introduction	3
2.2 Submissions and comments received	3
3. Background	5
3.1 Introduction	5
3.2 Framework for managing school funds	5
3.3 Audit objective and scope	6
4. School compliance with fund management requirements	9
4.1 Policies and procedures	10
4.2 DEECD support and monitoring	11
4.3 Conclusion	12
5. Operation and monitoring of school cooperatives	13
5.1 Introduction	14
5.2 Compliance with legislation and other requirements	15
5.3 Legality of borrowings by school cooperatives	17
5.4 Insurance cover over school facilities partly funded through cooperative loans	18
5.5 Conclusion	19

1

Audit summary

1.1 Introduction

Effectively managing school funds is critical to the ongoing financial viability of Victoria's government schools, and in turn contributes to the provision of better quality education.

The management of school funds is governed primarily by the *Education and Training Reform Act 2006*, and guidelines issued by the Department of Education and Early Childhood Development (DEECD). The Act requires schools to establish a school council to take responsibility for the governance and financial management of the school, and for DEECD to monitor the activities of school councils. Although the Act does not permit schools to borrow funds, under the *Co-operatives Act 1996* a school community can establish a cooperative for this purpose.

At 30 June 2008 funds held by Victoria's 1 595 government schools were around \$705 million.

This audit assessed whether government schools were managing their funds appropriately, and the adequacy of the role played by DEECD in supporting and monitoring schools in performing this function. The audit also examined whether using school cooperatives to borrow funds was consistent with legislation, adequately managed and disclosed by the school, and adequately monitored by DEECD.

Twenty-one schools were examined in the audit that held funds and investments totalling \$37.3 million at 30 June 2008. Seven of these schools had cooperatives.

1.2 Overall conclusion

With minor exceptions, which are being addressed by the respective schools, most were managing their funds in accordance with applicable legislation, policies, and guidelines, including sound investment management practices. In this regard DEECD was adequately supporting and monitoring schools with an effective quality assurance regime.

All school cooperatives examined were legally established. They complied with the various requirements governing their operation, except for some legislative financial reporting requirements. This non-compliance has weakened the accountability of schools for these entities. DEECD needs to address both these financial reporting

issues and the existing legislative anomaly that allows cooperatives to borrow funds for use by the school but does not permit a school to borrow in its own right.

DEECD also needs to provide clear guidance to schools about the insurance implications where school facilities are jointly funded by the school and DEECD. At one school examined this uncertainty has resulted in the school having a financial exposure of \$500 000, including an associated \$150 000 cooperative loan liability, if the facility was completely destroyed.

1.3 Key findings

- Only three of the 21 schools examined failed to comply with some of the policies and procedures governing the management of school funds. Instances of non-compliance were investing in shares, which is no longer permitted, an overdrawn bank account and incorrect information in financial reports.
- DEECD provides an adequate range of support and guidance to assist schools in managing their funds and this work contributes to an effective quality assurance regime.
- Monitoring by DEECD of schools' management of funds is facilitated by reviews of school financial reporting and independent audits.
- Cooperatives did not fully comply with their annual reporting requirements, including failing to prepare, having audited and table annual financial statements.
- Although legal, in substance the establishment of school cooperatives enables schools to enter into loan agreements, which may contravene the *Education and Training Reform Act 2006*.
- While school facilities are fully covered under DEECD's insurance policy, in the event that a jointly funded asset is fully destroyed, DEECD may choose to pay only to the school's entitlement, creating a financial exposure for the school for that component funded through donations or fund raising activities.

1.4 Recommendations

DEECD should:

- Reinforce to schools the importance of school cooperatives fulfilling all of their legislative annual reporting requirements in a timely manner
(Recommendation 5.1).
 - Address the legislative anomaly regarding school borrowings
(Recommendation 5.2).
 - Provide guidance to schools regarding the insurance implications where new school facilities are jointly funded by DEECD and the school. This should include clarification of their respective financial obligations in the event the facility is fully destroyed or only partly damaged and the availability of school level insurance.
(Recommendation 5.3).
-

2 Audit Act 1994 section 16— submissions and comments

2.1 Introduction

In accordance with section 16(3) of the *Audit Act 1994* a copy of this report, or relevant extracts from the report, was provided to the Department of Education and Early Childhood Development (DEECD) and the Department of Justice with a request for comments or submissions.

The comments and submissions provided are not subject to audit nor the evidentiary standards required to reach an audit conclusion. Responsibility for the accuracy, fairness and balance of those comments rests solely with the agency head.

2.2 Submissions and comments received

RESPONSE provided by the Secretary, Department of Justice

The Department of Justice welcomes the report.

Consumer Affairs Victoria (CAV) has historically attempted to support the efforts of cooperatives to become compliant with the requirements of the Cooperatives Act 1996. CAV is currently undertaking a major project, which may provide additional options for CAV to deal with non-compliant cooperatives.

CAV will engage with the Department of Education and Early Childhood Development to seek assistance with improving the compliance of these particular school cooperatives.

RESPONSE provided by the Secretary, Department of Education and Early Childhood Development

The Department of Education and Early Childhood Development (DEECD) welcomes the Auditor-General's report and supports its recognition that effective management of schools funds is important to the ongoing financial viability of Victoria's government schools.

The results of this audit will contribute to DEECD's pursuit of the effective quality assurance over the financial activities of schools and in this context the Department accepts all recommendations contained in the report, recognising that implementation of recommendation 5.1 will require the prior address of recommendation 5.2.

RESPONSE provided by the Secretary, Department of Education and Early Childhood Development – continued

Response to specific recommendations:

Recommendation 5.1 DEECD should reinforce to schools the importance of school cooperatives fulfilling all of their legislative annual reporting requirements in a timely manner.

DEECD accepts this recommendation which is partly dependant on the outcome of recommendation 5.2. DEECD will leverage the Auditor-General's recommendation to ensure resources made available to schools, such as the School Finance Manual and the Victorian Government School Reference Guide, includes relevant information on the financial reporting requirements of school cooperatives.

Recommendation 5.2 Address the legislation anomaly regarding school borrowings

DEECD accepts this recommendation and will seek legal opinion to ensure the issue is managed appropriately and any perceived breach of the Education and Training Reform Act (2006) is addressed.

Recommendation 5.3 Provide guidance to schools regarding the insurance implications where new school facilities are jointly funded by DEECD and the school. This should include clarification of their respective financial obligations in the event the facility is fully destroyed or only partly damaged and the availability of school level insurance.

DEECD accepts this recommendation. The Department will continue to provide advice to schools on the insurance implications for jointly funded facilities to ensure clear and consistent information is conveyed across all Victorian Government schools.



3 Background

3.1 Introduction

Effectively managing school funds is critical to the ongoing financial viability of Victoria's government schools, and in turn contributes to the provision of quality education. The majority of funding received by the 1 595 government schools is through the Department of Education and Early Childhood Development (DEECD). Fundraising events and voluntary financial contributions from parents are the other main sources of school funding.

The Commonwealth Government and local councils also provide funds to schools. Local councils may also provide other resources such as in-kind support.

At June 2008 funds held by these schools were around \$705 million compared with \$642 million at June 2007 and \$409 million at June 2006.

3.2 Framework for managing school funds

Victorian government schools operate under the *Education and Training Reform Act 2006* and its regulations. In terms of financial management, the Act requires a school to establish a school council to take responsibility for the governance and financial management of the school. The Act also requires DEECD to establish an effective quality assurance regime for the financial and operational activities of school councils.

School councils are subject to the accountability and auditing provisions of the *Financial Management Act 1994* and the *Audit Act 1994*. Although schools are not required to table an annual report in Parliament, financial statements are prepared, audited and presented in the school's annual report which in turn is provided to the school community. The statements are also consolidated into DEECD's annual financial statements.

The school principal is responsible for managing the school's financial systems, ensuring that information about its financial activities is made available to the council and that the annual budget process and budget management are fully documented. The principal is supported by the school business manager and finance subcommittee.

In addition to the legislative requirements, statewide guidelines have been issued by DEECD. For example, the School Finance Manual provides comprehensive guidance for managing funds, and the School Compliance Checklist is designed to assist schools to comply with their key management, legislative and regulatory responsibilities.

Since the 1980s, government primary and secondary schools have been provided with standard computer systems and equipment to assist with managing their main administrative and finance functions. The current system, CASES21, is also used by schools to report on their financial position and to meet DEECD's reporting and legislative requirements.

3.3 Audit objective and scope

The objective of this audit was to assess whether government schools manage the funds under their control appropriately, and to assess the adequacy of DEECD's role in supporting and monitoring this school function.

Specifically the audit assessed whether:

- schools had established adequate policies over the management of funds and were managing them in accordance with relevant legislation, DEECD policies and guidelines, and sound investment management practices
- DEECD adequately supports and monitors schools in managing school funds
- the use of school cooperatives to borrow funds was consistent with legislation, adequately monitored by DEECD, and adequately managed and disclosed by the school.

VAGO examined a sample of 21 government schools. Schools were selected based on factors such as size, risk profile, value of funds held at 30 June 2008, involvement with a school cooperative and previous audit coverage (Figure 3A).

Figure 3A
Government schools selected for audit examination

School	Region	Size	Funds held and invested at 30 June 2008 \$'000
Sunshine College ¹	Western Metro	L	6 316
Forest Hill College	Eastern Metro	L	5 229
Bendigo Senior Secondary College	Loddon Mallee	L	4 434
Berwick Secondary College *	Southern Metropolitan	L	3 266
Leongatha Secondary College	Gippsland	L	3 100
Brauer Secondary College	Barwon	L	3 090
Glen Waverley Secondary College	Eastern Metropolitan	L	2 347
Glenroy Specialist	Northern Metropolitan	M	1 175
Northcote High *	Northern Metropolitan	L	1 170
Brentwood Secondary College *	Eastern Metropolitan	L	1 151
Glenferrie Primary	Eastern Metropolitan	M	1 019
Wanganui Park Secondary *	Hume	L	1 018
Ripponlea Primary	Southern Metropolitan	M	904
Bellbridge primary	Western Metropolitan	M	853
Cheltenham Secondary College *	Southern Metropolitan	L	776
Somerville Primary	Southern Metropolitan	M	397
Gladstone Views Primary *	Northern Metropolitan	M	268
Rockbank Primary	Western Metropolitan	S	264
Footscray City Primary	Western Metropolitan	M	249
Alvie Consolidated	Barwon	S	136
Sebastapol College *	Grampians	L	134
Total			37 296

Note: *School cooperative established.

Source: Victorian Auditor-General's Office, based on DEECD data.

The audit was performed in accordance with the Australian Auditing Standards applicable for performance audits, and included tests and procedures to enable audit conclusions to be reached.

The total cost of this audit, including staff time, overheads and the preparation and printing of this report, was \$320 000.

¹ Included in this balance is federal funding for the building and operation of the Australian Technical College Sunshine. A total of \$6.305 million was received during 2007–08.

4 School compliance with fund management requirements

At a glance

Background

The management of school funds is governed by legislation and various policies and procedures established by the Department of Education and Early Childhood Development (DEECD). DEECD is also required to put in place an effective quality assurance regime for the financial activities of schools.

Findings

- Only three of the 21 schools examined failed to comply with some of the policies and procedures governing the management of school funds. Instances of non-compliance were investing in shares, which is no longer permitted, an overdrawn bank account and incorrect information in financial reports.
- DEECD provides an adequate range of support and guidance to assist schools in managing their funds and this work contributes to an effective quality assurance regime.
- Effective monitoring by DEECD of schools' management of funds is facilitated by reviews of school financial reporting and independent audits.

4.1 Policies and procedures

Figure 4A summarises the results of our examination of the extent to which school councils complied with the various policies and procedures governing the management of school funds established under legislation and by the Department of Education and Early Childhood Development (DEECD).

Figure 4A
Roles and responsibilities of school councils
in managing school funds

Audit criteria	Audit observations		
	Met	Not met	Partly met
Funds management policies			
<ul style="list-style-type: none"> School policies and procedures were clearly documented, comprehensive, appropriate and consistent with relevant legislation and DEECD policies and guidelines. 	21	–	–
Budget process and allocation of available funds			
<ul style="list-style-type: none"> Annual budgets prioritised the allocation of available funds. 	21	–	–
<ul style="list-style-type: none"> Annual budgets were scrutinised by the school finance committee. 	21	–	–
<ul style="list-style-type: none"> Annual budgets were formally approved by the school council. 	21	–	–
Management of funds			
<ul style="list-style-type: none"> Funds were managed in accordance with relevant legislation, DEECD policies and guidelines, and school policy requirements. 	20	–	1
<ul style="list-style-type: none"> Funds raised for a specific purpose were correctly applied for that purpose. 	21	–	–
Investment of funds not immediately required			
<ul style="list-style-type: none"> An investment policy consistent with DEECD's policy and guidelines had been adopted and is reviewed annually. 	18	3	–
<ul style="list-style-type: none"> Cash flow budgets were prepared to determine cash requirements for any given period and to maximise funds available for investment. 	21	–	–
<ul style="list-style-type: none"> Surplus funds were invested in accordance with DEECD's policy and sound investment management practices. 	21	–	–
<ul style="list-style-type: none"> Returns on investments were optimised with regard to prudent investment principles and restrictions on investment types. 	21	–	–
Reporting responsibilities			
<ul style="list-style-type: none"> Information on the management of school funds required by DEECD was provided within the required time frames. 	21	–	–
<ul style="list-style-type: none"> The school council adequately discharged its financial reporting obligations. 	21	–	–
<ul style="list-style-type: none"> The school council adequately discharged its accountability obligation for the management of school funds through preparation of an annual report. 	20	–	1
<ul style="list-style-type: none"> Annual financial reports provided adequate disclosure of school funds, revenue and expenditure. 	21	–	–

Source: Victorian Auditor-General's Office.

Figure 4A shows that, apart from some minor exceptions, the schools complied with the various requirements governing the management of school funds.

Instances of non-compliance related to:

- **Shares:** Two schools held investments in shares. When they were acquired DEECD's investment policy was not clear as to whether share investments were permitted. Under DEECD's revised policy, effective from August 2008, schools are not permitted to invest in shares. DEECD has recently identified 18 schools—including one identified by VAGO—with share investments totalling around \$1.8 million, which had been acquired before the policy revision. DEECD has recently requested that these schools dispose of their shares.
- **Investment policy:** Although investment decisions were ratified by the school council at three schools, these schools had not formally minuted an investment policy as required under the School Finance Manual.
- **Overdrawn banks accounts:** DEECD's School Finance Manual stipulates that under no circumstances should the schools' official bank account become overdrawn. At one school the official bank account was in overdraft at various times during the past two years (for a total of five weeks) ranging from \$1 000 to \$43 000. The school acknowledged that it was not complying with DEECD's policy and that it needed to improve its cash management practices.
- **Financial reports:** The 2006 and 2007 annual reports of one school contained material errors in its statement of financial position.

4.2 DEECD support and monitoring

DEECD's role in the management of school funds includes the provision of training, technical and general support, and the development of guidelines and policies. DEECD also has a legislative responsibility to monitor schools' financial management practices.

We reviewed whether DEECD adequately supports and monitors how well schools manage their funds.

4.2.1 Support and guidance

DEECD's support and guidance for schools includes:

- financial management policy advice
- development and delivery of professional development programs
- advice and guidance on best practice
- monitoring and advice on financial management issues
- provision of computer systems and equipment—currently CASES21.

We found that schools are significantly reliant on DEECD for guidance, training and advice on various aspects of financial management and implementation of DEECD's financial management policies. All the schools visited were very satisfied with the effectiveness of DEECD's support and guidance.

4.2.2 Monitoring

Monitoring by DEECD is facilitated mainly through the following:

- **CASES21 finance module:** Schools are required to use the CASES21 finance module to manage and report on their funds. DEECD can access the financial information recorded in CASES21 at any time. DEECD has established an ongoing CASES21 review program that includes analysis of monthly school bank balances and general ledger information, compliance by schools with investment policy, and review of schools' financial commitments.
- **Internal audit:** DEECD regularly undertakes reviews of various aspects of funds management. During 2008 DEECD completed a number of reviews relating to funds management, including the management of finances in schools, payments to parents and the operation of school cooperatives. These reviews have resulted in recommendations for improvement, which DEECD has either implemented or are considering. Ad hoc reviews are also undertaken in response to emerging financial management concerns.
- **External audit:** Schools' annual financial results are audited by DEECD-appointed auditors. External audits conducted for the calendar year ended 31 December 2007 did not identify any major fund management issues.

The findings of DEECD's monitoring are consistent with the results of this audit.

4.3 Conclusion

Apart from minor exceptions, most of the schools examined were managing their funds in accordance with applicable legislation, policies and guidelines, including sound investment management practices. DEECD is adequately supporting and monitoring schools in their management of school funds and this work contributes to an effective quality assurance regime.

5 Operation and monitoring of school cooperatives

At a glance

Background

Under the *Co-operatives Act 1996*, a school community may establish a cooperative for the purpose of borrowing funds to construct or improve facilities on school grounds. The school has primary responsibility for repaying these loans although the borrowings are guaranteed by the Treasurer of Victoria.

At 30 June 2008, there were 157 government school cooperatives with loan guarantees totalling \$16.1 million. The audit examined seven cooperatives.

Findings

- All cooperatives did not fully comply with their annual reporting requirements, including failing to prepare, have audited and table annual financial statements.
- Although legal, in substance the establishment of school cooperatives enables schools to enter into loan agreements, which may contravene the *Education and Training Reform Act 2006*.
- Unless schools fully insure new facilities jointly funded by DEECD and the school, insurance cover only extends to the value of DEECD's contribution creating a financial exposure for the school.

Recommendations

DEECD should:

- Reinforce to schools the importance of school cooperatives fulfilling all of their legislative annual reporting requirements in a timely manner
(Recommendation 5.1).
- Address the legislative anomaly regarding school borrowings
(Recommendation 5.2).
- Provide guidance to schools regarding the insurance implications where new school facilities are jointly funded by DEECD and the school. This should include clarification of their respective financial obligations in the event the facility is fully destroyed or only partly damaged and the availability of school level insurance.
(Recommendation 5.3).

5.1 Introduction

Under the *Education and Training Reform Act 2006* (formerly the *Education Act 1958*), school councils are not permitted to obtain loans or credit facilities. However, a school community may establish a cooperative for the purpose of borrowing funds to construct or improve facilities on school grounds.

Government school cooperatives are established under the *Co-operatives Act 1996* (the Act) as 'non-trading' incorporated entities with limited liability. Membership is voluntary and open to any person (parent, staff and/or supporter who has a link with the school). Members are allocated non-trading shares. School councils have primary responsibility for repaying loans obtained by the school cooperative, which they must fund from their 'own-sourced' income. Under the Act, the Treasurer of Victoria may provide a guarantee for the repayment of any loan obtained by the cooperative. In practice guarantees are provided for all loans.

At 30 June 2008, there were 157 government school cooperatives for which the Victorian Treasurer has provided guarantees totalling \$16.1 million. Loans obtained by school cooperatives range from \$21 000 to \$800 000, with the average loan being around \$185 000.

Seven of the twenty-one schools covered in this audit had established cooperatives to obtain finance to partially fund the construction of facilities at the school, predominately gymnasium and basketball courts.



Sports stadium at a school, partly funded by the school cooperative loan.

5.2 Compliance with legislation and other requirements

The establishment and operation of school cooperatives is governed by the Act and guidelines issued by the Department of Treasury and Finance (DTF) and Consumer Affairs Victoria (CAV).

Figure 5A summarises the results of our examination reflecting the extent to which the seven cooperatives were complying with the legislation and other requirements governing their establishment and operation.

Figure 5A
Key requirements to establish and operate a school cooperative

Audit criteria	Audit observations		
	Met	Not met	Partially met
Establishing the cooperative			
• Governing rules established and approved by the Registrar of Cooperatives (Consumer Affairs Victoria).	7	–	–
• Formation meeting of members held.	7	–	–
• Board of Directors appointed – at least 2 directors.	7	–	–
• Register of members maintained – at least 25 members.	7	–	–
Financial obligations			
• Members paid up at least 10 per cent of the nominal value of their shares – total value not to exceed \$1 500.	–	–	6
• Level of uncalled capital was equal to the amount of the loan.	6	–	–
• The rate of interest applicable to the loan was the indicative borrowing rate for borrowings by general cooperatives.	6	–	–
• The term of the loan does not exceed 15 years (generally coinciding with the useful life of the asset).	6	–	–
• The Victorian Treasurer's guarantee was provided.	6	–	–
• Repayments of principal and payments of interest were being made in accordance with the repayment schedule in the loan agreement.	6	–	–
Annual reporting requirements			
• Annual general meetings were held.	5	–	2
• Financial statements prepared, audited and tabled at the annual general meeting.	2	–	4
• Annual returns submitted in a timely manner to the Registrar of Cooperatives.	2	–	5

Note: One cooperative did not take out a loan.

Source: Victorian Auditor-General's Office.

Figure 5A shows that apart from a financial obligation and the annual reporting requirements, the schools complied with the various requirements governing the establishment and operation of school cooperatives. At the six cooperatives with a loan, the related schools funded the members contribution.

5.2.1 Annual reporting requirements

The Act stipulates that a cooperative must lodge an annual report with the Registrar of Cooperatives within 28 days of the annual general meeting being held, or such further time as the Registrar may allow.

The report must contain:

- a list of directors and principal executive officers
- the annual financial statements, including the directors' report and the auditor's report.

There were instances of non-compliance, to varying degrees at all cooperatives, with the annual legislative reporting requirements and guidelines of CAV. For example:

- Thirteen annual returns were not submitted to CAV on time and in ten cases, not at all. At four of the seven cooperatives we sighted letters from CAV advising they were in breach of the Act for not submitting annual returns. In response to the letter, three schools submitted their outstanding returns. At the date of our audit the fourth school had not responded to CAV.
- Audited financial statements were not tabled at annual general meetings in three instances. This did not occur because the annual financial statements had not been completed and audited in time for presentation at the meeting.
- At two cooperatives annual general meetings were not held, for two years and three years respectively. No explanation was provided as to why these meetings did not occur.
- Minutes of annual general meetings could not be produced for audit review in 25 instances across four cooperatives.

The cooperatives failure to fully comply with the legislative and other reporting requirements has implications for school councils' monitoring of the financial activities of cooperatives.

Schools require their cooperatives to prepare a report on their financial activities for tabling at each school council meeting, usually held about eight to nine times each year. The fact that five cooperatives had not tabled audited annual financial statements at their annual general meeting, demonstrates that these school councils had not been adequately monitoring the financial activities of their cooperatives.

We also found that record keeping was poor at all the cooperatives we visited.

Records and documents were contained in manila folders and arch lever files and none of these files were indexed. Similarly, key documents were not filed in any logical order. Consequently, schools found it difficult to locate records and documents for audit examination, in particular, minutes of meetings, copies of financial statements and annual returns to CAV. Accordingly, four schools were unable to advise whether annual general meetings or board meetings of cooperative directors had been held.

DEECD support and oversight

We found that the Department of Education and Early Childhood Development (DEECD) did not provide any direct assistance or guidance to schools about establishing a cooperative or its ongoing operation, neither, until recently, did it monitor the operations of school cooperatives. DEECD advised that, as school cooperatives have their own legal identity under the *Co-operatives Act 1996* the Department has no legislative responsibility for the establishment or operation of cooperatives.

DEECD has recently acted to oversee the financial transactions of school cooperatives. Following DEECD's assessment of the financial reporting implications of school cooperatives in June 2007, the Department directed schools to record all transactions relating to cooperative bank accounts and loans in CASES21 and in the schools' annual financial statements.

5.3 Legality of borrowings by school cooperatives

In December 2006 a report on government school cooperatives was prepared by a consultant for the then Department of Education (now DEECD). The report concluded that school cooperatives appear to be controlled entities of schools and this potentially gave rise to a breach of the then *Education Act 1958* as the schools had effectively borrowed money.

The report indicated that, among other things:

- schools generally bear all the risks and benefits of ownership of the assets created
- schools control the administration of the cooperatives
- schools bear the risk in relation to meeting the financial obligations of the loans
- the sole purpose for the existence of the cooperative is to benefit the school
- the cooperative is economically dependent on the school.

The report recommended that DEECD investigate the legality of borrowings by school cooperatives. Although DEECD subsequently obtained legal advice, it considered that the opinion was not clear. DEECD sought advice from VAGO concerning the implications from an accounting disclosure perspective and subsequently directed schools to prepare their annual financial statements inclusive of cooperatives. However, the issue of the legality of schools borrowing through cooperatives remains unresolved.

Under Australian Accounting Standards, and as reported by the consultant engaged by DEECD, a school cooperative is a controlled entity of the school that established the cooperative. While it is clear that the school cooperative has legally entered into the loan agreement, as a controlled entity of the school, in substance the school has borrowed the funds.

5.4 Insurance cover over school facilities partly funded through cooperative loans

DEECD insures all buildings on government school grounds under an Industrial Special Risks policy with the Victorian Managed Insurance Authority but carries a deductible of \$3 million dollars per event, which means DEECD is responsible for repairing the majority of damage to school buildings.

Where construction of a school building has been jointly funded by DEECD and the school through, for example, a cooperative loan, DEECD may not fully replace the facility if it is destroyed as it will only supply facilities up to the funding entitlement level for the school. Where the cost of full insurance is prohibitive or part insurance impractical, the school is exposed to financial risk. This is illustrated by the following situation at a primary school audited (Figure 5B).

Figure 5B
Example of financial risk in schools

In November 2008 the school completed construction of a new 'full sized' gymnasium. DEECD contributed \$1.5 million, which equated to the school's capital funding entitlement based on student enrolments, and the school contributed \$500 000, comprising \$350 000 from its operating budget and \$150 000 from a cooperative loan. The current replacement value is \$2.0 million. In the event that the new gymnasium was destroyed, DEECD would only provide \$1.5 million towards its replacement.

Currently, the school gymnasium is not insured for the balance of its replacement value of \$500 000 exposing the school to financial risk up to this value if the school facility was fully destroyed. The school council sought quotes from private sector insurers to cover the balance of the replacement value but was advised that this was not possible because of the practicalities of determining which portion of the gym was uninsured. DEECD advised that the school council may not have been aware that at least one broker is capable of sourcing such cover.

Source: Victorian Auditor-General's Office.

DEECD's funding entitlement policy is also unclear in situations where a jointly funded facility is only partly damaged. It is not clear if DEECD will bear the full cost of repairs, and this will to some extent depend on the configuration of the building.

DEECD advised that schools are fully aware of their funding entitlements in relation to school facilities although they may not be aware of the availability of school level insurance. Where schools choose to invest in facilities over and above entitlement, school councils have a responsibility to make sure they have the financial resources to meet operating costs, including cleaning, maintenance and insurance cover. Before committing to these projects, schools should formulate a detailed business case that would identify the financial implications of investing in school facilities over and above entitlement.

5.5 Conclusion

The seven school cooperatives were established in accordance with the legislative requirements and legally, the shareholders are liable in the event of a default. However, from an accounting perspective they are a controlled entity of the school and in practice, schools are ultimately responsible for repaying the funds borrowed.

Notwithstanding that exposure, cooperative debt is low across the education sector and for individual schools, their establishment effectively allows schools to enter into loan agreements. This may contravene the *Education and Training Reform Act 2006*. It also means that legislative responsibility for establishing and overseeing the financial activities of cooperatives rests with CAV rather than DEECD.

The failure of some cooperatives to comply with some of their legislative reporting obligations has weakened the accountability by schools for these entities. Of particular concern is the failure to prepare, have audited and table financial statements at the cooperatives' annual general meeting. DEECD's recent directive requiring schools to record cooperative financial information in CASES21 should contribute to improved accountability.

While we acknowledge the principle of 'self insurance' is an acceptable risk management practice, DEECD should remind schools of the insurance implications where school buildings are jointly funded. At one school this uncertainty has resulted in the school having a financial exposure of \$500 000 if the facility was fully destroyed.

Recommendations

DEECD should:

- 5.1 Reinforce to schools the importance of school cooperatives fulfilling all of their legislative annual reporting requirements in a timely manner.
- 5.2 Address the legislative anomaly regarding school borrowings.
- 5.3 Provide guidance to schools regarding the insurance implications where new school facilities are jointly funded by DEECD and the school. This should include clarification of their respective financial obligations in the event the facility is fully destroyed or only partly damaged and the availability of school level insurance.

Auditor-General's reports

Reports tabled during 2008–09

Report title	Date tabled
Managing Complaints Against Ticket Inspectors (2008–09:1)	July 2008
Records Management Checklist: A Tool to Improve Records Management (2008–09:2)	July 2008
Investing Smarter in Public Sector ICT: Turning Principles into Practice (2008–09:3)	July 2008
Private Practice Arrangements in Health Services (2008–09:4)	October 2008
Working with Children Check (2008–09:5)	October 2008
CASES21 (2008–09:6)	October 2008
School Buildings: Planning, Maintenance and Renewal (2008–09:7)	November 2008
Managing Acute Patient Flows (2008–09:8)	November 2008
Biosecurity Incidents: Planning and Risk Management for Livestock Diseases (2008–09:9)	November 2008
Enforcement of Planning Permits (2008-09:10)	November 2008
Auditor-General's Report on the Annual Financial Report of the State of Victoria, 2007–08 (2008–09:11)	November 2008
Local Government: Results of the 2007–08 Audits (2008–09:12)	November 2008
Management of the Multi-Purpose Taxi Program (2008–09:13)	December 2008
Results of Audits for Entities with 30 June 2008 Balance Dates (2008–09:14)	December 2008
Preparedness to Respond to Terrorism Incidents: Essential services and critical infrastructure (2008–09:15)	January 2009
Literacy and Numeracy Achievement (2008–09:16)	February 2009
Administration of the <i>Flora and Fauna Guarantee Act 1988</i> (2008–09:17)	April 2009
Access to Public Hospitals: Measuring Performance (2008–09:18)	April 2009

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