1 Report Summary

1.1 Background

Each financial year, three reports are presented to Parliament containing the results of financial audits completed during the year.

This is the third and final report for 2008–09. Principally it deals with the audit of public sector entities with financial statement balance dates other than 30 June 2008. The other results reported are for entities with 30 June 2008 balance dates (2008–09:14) and Local Government: Results of 2007–08 audits (2008–09:12).

This report covers 123 entities from the Higher Education, Vocational Training, Alpine Resorts, Health, and Community Development sectors. These entities are outlined in Figure 1A.

Figure 1A
Entities with balance dates other than 30 June 2008

			2008–09			
Sector	**Type of entity**	**2007**	**30 Sept**	**31 Oct**	**31 Dec**	**31 Mar**
Higher education and vocational training	Universities	8	–	–	**8**	–
	Associated companies, trusts and joint ventures	76	–	–	**71**	–
	TAFEs (stand-alone)	14	–	–	**14**	–
	Associated companies and trusts	11	–	–	**12**	–
	Other training entities	7	–	–	**6**	–
	Associated companies and trusts	2	–	–	**2**	–
Sustainability and environment	Alpine resorts	5	–	**5**	–	–
Health	Boards and a charity	3	**1**	–	**2**	–
Community development	A company and a trust	2	**1**	–	–	**1**
Total		**128**	**2**	**5**	**115**	**1**

Source: Victorian Auditor-General's Office.

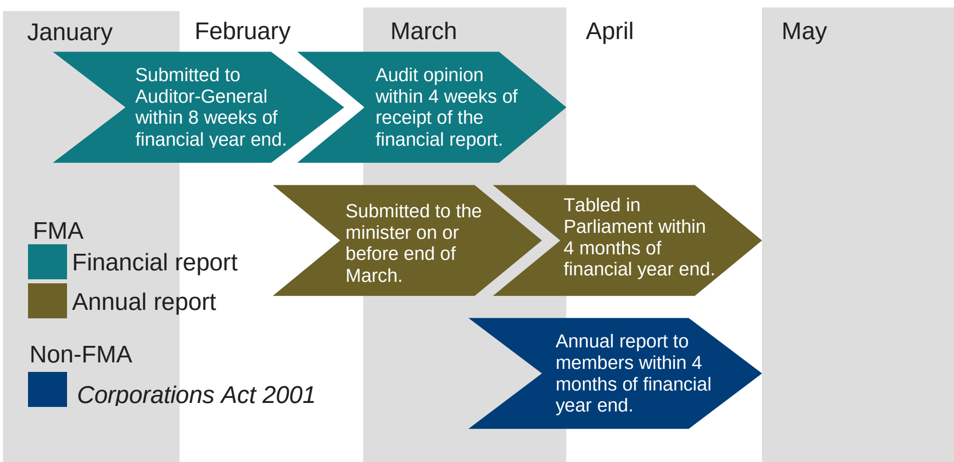
The majority are from the Higher Education and Vocational Training sectors, which accounts for 113 entities.

There are also 11 entities included, whose financial statements were submitted for audit after our close off for reporting on entities with 30 June balance dates. This meant they were not included in the audit report tabled on 3 December 2008 (2008–09:14).

1.1.1 Reporting framework

The public sector must comply with a range of legislative and accounting requirements when preparing its financial statements to be tabled in Parliament, as shown in Figure 1B.

Figure 1B
Victorian financial reporting time frames



Source: Victorian Auditor-General's Office.

The *Financial Management Act 1994* requires entities to submit annual reports for tabling in the Parliament, within four months of the end of the financial year, including financial statements which must be prepared and audited within 12 weeks. These FMA requirements also apply to the majority of entities owned or controlled by the universities and TAFEs, who are required to finalise their financial statements, including the consolidation of their subsidiaries, within 12 weeks.

For companies owned or controlled by public sector entities, the governing legislation is the *Corporations Act 2001*. This Act requires them to report to their members within four months after the end of their financial year.

Financial statements are required to be prepared in accordance with Australian accounting standards.

In October 2007, DIIRD issued an executive memorandum to the TAFEs, universities with TAFE divisions, and two training entities, requesting they disclose the approved key performance indicators in a concise performance statement. This statement was to be audited and included in their annual reports.

In addition there was an increased focus on internal controls and financial sustainability during the audits, as part of the audit planning process.

1.2 Key findings

1.2.1 Results of audits

At 15 April 2009, 115 of the 123 financial statements had been finalised (94 per cent). Of the 115 opinions issued 111 were clear and four required qualification, compared to 126 audit opinions at 30 April 2008, of which four were qualified.

The entities qualified and reasons why are summarised in Figure 1C.

Figure 1C
Qualified audit opinions issued

Entity	Status	Type	Reason for qualification
Deakin University	Continuing	Exception	Certain grants received were deferred and recognised as a liability, rather than as income when received, contrary to the requirements of AASB 1004 *'Contributions'*.
The University of Melbourne	Continuing	Exception	
The Meanjin Company Limited	Continuing	Exception	
Anti-Cancer Council of Victoria	Continuing	Exception	We were unable to assess the completeness of cash donations, due to the inherent risk involved in the collection of this revenue which cannot be mitigated by further internal controls.

Source: Victorian Auditor-General's Office.

The independent audit opinion adds credibility to the financial report by providing reasonable assurance that the information in the statements is reliable.

A qualified audit opinion means that a statement has not been prepared in accordance with the relevant reporting framework and, therefore, is less reliable and useful as an accountability document.

Deakin University and **The University of Melbourne** have again had their financial statements qualified. This is because their accounting policies for recording non-reciprocal research grants do not accord with current Australian accounting standards.

These universities are not recording this revenue when received, which is when they gain control, consistent with *Australian Accounting Standards Board AASB 1004 'Contributions'*. Rather they are recording grant receipts as a liability until they spend the grants.

The AASB has not issued any amendments to the applicable accounting standards, so the qualifications remain.

The type of qualification issued to the **Anti-Cancer Council of Victoria** is one generally attached to the financial statements for entities that have significant 'public appeal' based fundraising activities, where it is particularly difficult to meet the evidentiary standards for revenue verification.

Clear audit opinions were issued on the 19 performance statements submitted for audit. An audit opinion was not issued on the performance statement of **Holmesglen Institute of TAFE** as it was not certified by the governing body and was not submitted for audit.

As reported last year, the requirement for TAFEs to prepare audited performance statements is not mandatory.

Holmesglen Institute of TAFE is a significant entity in the sector with the result that consistent credible performance information is not universally reported for the $1.2 billion sector.

With the current government reforms to improve choice and contestability by supporting a broader range of providers in the vocational training market, there is now further argument for a robust monitoring framework to operate across this sector.

1.2.2 Quality of reporting

An important attribute of the quality of financial reporting is its timeliness and accuracy. It is important that public sector entities prepare and publish timely financial information. The later the reports are produced and published after year-end, the less useful they become.

Overall, 28 of the 34 entities or 82 per cent reporting under the FMA finalised their statements within the 12-week statutory timeframe (76 per cent in 2007). Of the 89 non-FMA entities, 82 entities or 92 per cent finalised their statements within the required four months (98 per cent in 2007). At 15 April 2009, there are seven entities that are yet to finalise their financial statements, which are detailed in Figure 2B.

Higher education and vocational training entities generally performed well with 89 of the 113 entities or 79 per cent completing their financial statements within the required 12 weeks (81 per cent in 2007). However, four TAFEs and one training entity have not met the timetable (one TAFE in 2007).

Alpine resorts significantly improved their timeliness of reporting in 2008, with all five entities completing their financial statements within 12 weeks (all resorts were late in 2007).

Another measure of report quality is the number and size of adjustments required to finalise the financial statements. When the audit process reveals errors in the draft financial statements, they are raised with the entity. If the errors are considered material, adjustments are requested.

The 2008 results are comparable to the previous year, however the quality control over reporting in most TAFEs and ARMBs could improve.

1.2.3 Financial performance

Universities as a group generated a total operating surplus of $27 million. This is a decrease of $337 million or 93 per cent from 2007.

The significant reduction in the result is due mainly to $356 million of impairment losses on investment assets.

TAFEs generated a collective operating surplus of $53 million, which was a reduction from 2007 of $26 million or 33 per cent. Generally, operating expenses grew faster than revenues in 2008. TAFEs were also affected by the global financial crisis where impairment losses on investments accounted for $15 million of the decline in the operating surplus.

Alpine resorts collectively generated a combined operating surplus of $533,000, a decrease of $3.3 million or 86 per cent from 2007. All the alpine resorts recorded an operating deficit, except Falls Creek, which recorded an operating surplus.

1.2.4 Impact of global financial crisis

The current global financial crisis has significantly reduced the values of equities traded on share markets during 2008. Some Victorian universities and TAFE institutions hold substantial investment portfolios of Australian and international equities.

A significant issue this year was the impairment losses on investment assets. In total, $371 million of impairment losses were expensed by the higher education and vocational training sector. The following entities recorded impairment losses:

- four universities – **The University of Melbourne, Monash University, Swinburne University of Technology** and **University of Ballarat**
- three university controlled entities – **Melbourne Business School Ltd, Monash University Foundation** and **RMIT Foundation**
- two TAFEs – **Holmesglen TAFE** and **East Gippsland TAFE**.

Consistent with accounting standards, these losses have been recognised as expenses in their income statements, and severely affected their operating results. The impairment losses are due to the general deterioration in equities invested in the sharemarket, and are broadly consistent with the market's decline in 2008.

1.2.5 Increase in international student fees

The trend for the past three years for universities and TAFEs shows a steady growth in international student fees. The growing contribution from international student fees increases the exposure for both universities and TAFEs to the increasingly competitive market for international students.

1.2.6 Financial sustainability

Financial sustainability information is gained from the analysis of five selected indicators – the underlying result, level of liquidity, debt to equity ratio, self-financing capability and the level of capital replacement.

For higher education and vocational training entities, the findings are similar to 2007. Most universities and TAFEs are in a healthy condition.

While based on only three years data, the 'self-financing ratio' shows the weakest results of the indicators, with the entities having limited ability to fund new assets from operating cash flows. While TAFEs are generating small operating surpluses, they do not generate sufficient own-source revenues to be able to build up enough retained earnings to finance future asset replacement. Under the current government funding approach, depreciation expenses are generally not funded until capital requirements are established. However, the TAFE boards are held fully accountable for financial management and performance.

In respect of the Alpine resorts, financial sustainability findings are similar to 2007 with **Lake Mountain** and **Mt Baw Baw** in the weakest condition. These ARMBs are heavily reliant on snow-related revenue and do not have enough capacity to replace assets and fund new assets.

Bush Fires

The future operating results of **Lake Mountain** and **Mt Baw Baw** will be affected by the recent bush fire events. As the areas surrounding the smaller Alpine resorts have suffered significant fire damage, this may affect their ability to generate revenue from visitor fees.

In addition, **Lake Mountain** has lost assets from the bush fires and will need to acquire replacement assets in time for the 2009 snow season. The ARMB has yet to fully quantify the value of these assets.

1.2.7 Effectiveness of internal controls

Internal controls should provide reliable, accurate and timely reporting. The audit of financial reports includes an examination of the internal control framework that relates to financial reporting. Where significant control weaknesses or breakdowns are identified these matters are reported to the entity's management.

This year our audits confirmed that entities' systems of internal control were overall sufficient to produce reliable financial reports. The most significant commonly identified control weaknesses were inadequacies in:

- preparation and review of reconciliations
- financial policy and procedure manuals
- management of information system (IS) access controls.

1.2.8 Investment management

This year as part of our cyclical approach to reviewing significant aspects of financial management, we carried out a review of investment management at universities and TAFEs. The higher education and vocational training sector had $2.5 billion in investments at 31 December 2008.

Best practice guidelines on investment policies have been published in Queensland[1] and Western Australia[2]. These guidelines have been used to develop criteria for assessing investment management practices in Victorian universities and TAFEs.

Our review found elements of the best practice guidelines were not included in the majority of investment policies reviewed, including:

- requirements for the governing body to actively monitor the performance of their investments
- criteria that would trigger liquidation of their investments
- criteria for the selection and removal of external investment managers.

1.3 Key recommendations

These recommendations follow from the key findings outlined above.

1.3.1 Higher education and vocational training

- **Holmesglen TAFE** should prepare and publish their audited performance statement in their annual report. **(Recommendation: 2.1)**
- Entities with material errors in their draft financial statements, and those unable to achieve the legislated timeframes, should adopt better practice initiatives for financial reporting. **(Recommendation: 2.2)**

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[1] Queensland Treasury 2007, Investment Policy Guidelines, Queensland Government

[2] Department of Local Government and Regional Development 2008, Investment *Policy – Local Government Operational Guidelines*, No. 19, Government of Western Australia.

- Entities should assess their policies and procedures against the commonly identified weaknesses within internal and information system control environments and implement any required changes so that their controls are operating in a reliable and cost-effective manner. **(Recommendation: 2.3)**
- Universities and TAFEs should have a current investment management policy, which is approved by the governing body, and reviewed at least annually against the best practice guidelines. **(Recommendation 2.4)**
- Governing bodies should at least annually review the quality of reports received. **(Recommendation 2.5)**
- Investment policies should state the role, function and controls in relation to the engagement of external investment managers. **(Recommendation 2.6)**

1.3.2 Alpine resorts

- Each board should determine and monitor the long term implications of financial sustainability, as there are significant challenges for the smaller ARMBs. **(Recommendation 3.1)**
- Each board should monitor the sustainability of its revenue and expenditure policies, and model the affect of proposed changes to these policies. **(Recommendation 3.2)**
- The **Lake Mountain** and **Mt Baw Baw** ARMBs should make further contributions to the legislatively required ‘snow drought’ and ‘capital’ funds. **(Recommendation 3.3)**

1.4 General

The total cost of preparing and printing this was $185 000.