Queensland Audit Office

Results of audit: Education sector entities 2015

Report 18: 2015–16

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QUEENSLAND

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QAO
Queensland Audit Office

Your ref:
Our ref: 11477

May 2016

The Honourable P Wellington MP
Speaker of the Legislative Assembly
Parliament House
BRISBANE QLD 4000

Dear Mr Speaker

Report to Parliament

This report is prepared under Part 3 Division 3 of the *Auditor-General Act 2009*, and is titled Results of audit: Education sector entities 2015.

In accordance with s.67 of the Act, would you please arrange for the report to be tabled in the Legislative Assembly.

Yours sincerely

Andrew Greaves
Auditor-General

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Summary

Who this report covers

This report summarises the results of our financial audits of the seven Queensland public universities and their controlled entities; the eight Queensland grammar schools; and a small number of other education specific entities that have 31 December 2015 financial year end dates. The universities and grammar schools are statutory bodies while the controlled entities mainly comprise public companies.

The universities provide tertiary education including undergraduate and postgraduate studies, while the grammar schools all provide years 7–12 high schooling, with some students starting at prep year.

To enable better like-for-like comparisons, we benchmark universities' results both across the Queensland sector and against national data, broken down where possible between regional and metropolitan locations, and also against the Group of Eight (Go8) universities. The Go8 is a coalition of research-intensive Australian universities, which includes the University of Queensland and some of the largest and oldest universities in Australia.

Figure A
University classification

Metropolitan	Regional
University of Queensland* Queensland University of Technology Griffith University	James Cook University Central Queensland University University of Southern Queensland University of Sunshine Coast

* Member of the Go8

Source: Queensland Audit Office

What this report covers

This report deals with the financial audit results for the 2015 calendar year of above entities. It provides a snapshot of their finances at 31 December 2015 and expands on the significant financial accounting issues that arose during the audits.

This year we also report on our in-depth review of risk management practices operating at the seven universities and on the key income and cost drivers across the university sector.

Audit results

We issued unqualified audit opinions for all entities included in this report. This is consistent with 2014 and confirms their financial reports were prepared according to requirements of legislation and relevant accounting standards.

While all entities received unqualified audit opinions, we included an emphasis of matter paragraph in our opinion for twelve entities. This serves to highlight issues that help users better understand the financial report. In all cases, the emphasis of matter drew the users' attention to the fact the statements have been prepared for a special purpose, rather than as general purpose financial statements.

Timeliness and quality

The universities and grammar schools are required to have their financial statements certified by us within two months of the end of the financial year. All met this legislated timeframe. This is a better result than last year, where one entity was certified outside the legislative deadline.

Most of the universities' controlled-and-related-entities' certification timeframes extend beyond two months, because of their different legal status and the specific requirements of their legislation. However, most of these also needed to be certified within two months so that their results can be consolidated into their parent entity's financial statements.

The quality of draft financial statements presented for auditing continues to be good, with limited changes required to either balances, or disclosures, after they were submitted to us.

Simplification of financial statements

A number of universities have taken the opportunity in 2015 to reduce the volume of notes and simplify disclosures in their financial statements.

Of the seven universities audited, five have reduced the number of notes disclosed in their certified financial statements, with USC reducing its number of notes by 37.5 per cent and USQ by 25.6 per cent. Across the sector, the average percentage decrease in note numbers was 13.2 per cent.

Key audit matters

We identified and responded to a number of key audit matters during our 2015 audits. These matters, in our professional judgement, were of most significance in the audit of the financial statements. We communicate these matters to the governing body of the relevant entity as part of the finalisation of our financial audit. From 2017, we will include these in our audit opinions.

Valuation of property, plant and equipment

Each year, universities assess the value of property, plant and equipment. This is one of the more subjective and complex assessments undertaken, because of the assumptions and estimates applied throughout the process.

As at 31 December 2015, the net book value of property, plant and equipment for all universities, including controlled entities, was $7 411 million, an increase of $159 million (2.19 per cent) from the 31 December 2014 amount of $7 252 million. This increase in net book values is attributable mainly to buildings of $284.8 million and plant and equipment assets (including leasehold improvements) of $36.4 million offset by a decrease in infrastructure assets of $117.1 million and leased assets of $40.9 million.

Griffith University engaged an independent valuer to perform a valuation of its land, buildings and infrastructure assets for the year ended 31 December 2015. The valuation was affected by the Australian Accounting Standard Board's clarification of the definition of residual value, which necessitated an adjustment to prior year figures.

The financial impact of the valuation was a material change in the carrying value of the university’s non-current assets (downward adjustment of $480.7 million to the prior year building assets carrying value) and an increase of $22.9 million in the 2014 depreciation expense charged to the Statement of Comprehensive Income.

Land sales and acquisitions

The University of Southern Queensland (USQ) purchased the University of Queensland (UQ) Ipswich campus at a contract price of $21.5 million. USQ engaged an external valuer to assess the fair value of the assets acquired. This fair value was deemed to be $82.6 million and USQ recognised a gain on acquisition of $61 million in the 2015 financial report.

On 30 October 2015, the University of Southern Queensland (USQ) entered into a contract to sell its Fraser Coast Campus to University of the Sunshine Coast (USC) with a settlement date of 1 February 2016. The conditions of the contract were required to be finalised post balance date on 12 January 2016. The purchase price for the sale has been determined as $7 million payable in two equal instalments over two years.

Investments in controlled and other entities

In June 2015, Swiss multinational pharmaceutical company, Novartis International AG (Novartis) acquired 100 per cent of biotech company, Spinifex Pharmaceuticals Inc. (Spinifex) for a total potential consideration of US$725 million on achievement of future milestones. UniQuest Pty Ltd (UniQuest), a controlled entity of UQ, held approximately a 5.9 per cent share of Spinifex and recorded a gain on sale of AU$15.5 million for 2015.

Each Queensland University holds 10 000 $1 fully paid shares in Education Australia Limited (EA). EA in turn holds a 50 per cent share in IDP Education Ltd (IDP). IDP listed on the Australian Stock Exchange in November 2015. As at 31 December 2015, EA held 125 397 484 shares in IDP valued at $417.6 million. All universities now recognise their investment at approximately $9 million.

Financial performance

The overall financial performance of all the universities and most of the grammar schools remains sound; with all the universities meeting or exceeding key financial ratio targets. These targets are indicators of the current financial performance and position of the entities as well as their future sustainability.

Ipswich Grammar School and Rockhampton Girls Grammar School reported operating deficits in 2015 and need to review their expenditure and revenue policies to ensure future sustainable results.

Financial control

The 'control environment' is an integral component of each entity's governance framework. Management's operating philosophy, attitude and demonstrated commitment to sound financial control strongly influences the effectiveness of its system of controls.

Significant financial control issues we reported to management

Internal control over financial reporting is generally sound in the sector, but more management attention is required to improve information technology-based controls.

We reported fewer significant control issues this year than last year; however, IT security and access control breakdowns remain prevalent across both the university and grammar school sectors. IT security and access controls are important to prevent external attacks and to preserve data integrity and confidentiality. This trend concerns us, given we have raised a number of similar IT issues for two years in a row.

Some longstanding procurement approval and delegation issues are yet to be addressed, and we have recommended to the relevant entities that they be actioned as a matter of priority.

Internal audit

In general, university internal audit units and audit committees are operating effectively; although the timeliness of following up unresolved audit issues can be improved. At the time of audit, across the sector, there were 148 (2014: 94) high and moderate risk internal audit issues unresolved. Of these, two (2014: nine) high-risk issues had been outstanding for over 12 months.

The number of outstanding internal audit issues raised and the length of time they have been outstanding is something that audit committees and university councils should be monitoring closely.

Reporting underlying results

All the universities perform a calculation of an 'underlying' or 'normalised' result for their own internal management financial reporting purposes. This result differs from the audited statutory result in their published financial statements, which they prepare in accordance with various legal requirements, including Australian accounting standards.

The main difference between the two results are adjustments for one-off or infrequent items or certain non-cash transactions. We do not audit the underlying result and it is not prepared in accordance with Australian accounting standards.

During 2015, the Queensland universities, as a group, developed a framework to assist in a more consistent calculation of the underlying result, which would better inform users who seek to benchmark the various universities' results.

We assessed the universities' approach against both the Australian Securities and Investment Commissions (ASIC) regulatory guide (RG 230) for disclosing financial information not in accordance with the International Financial Reporting Standards (IFRS) and against the new university framework developed. Currently four universities publish this calculation in their annual report.

Overall, our assessment is that all universities comply with both frameworks in most instances. Areas they can improve are:

- clearly stating that the underlying result is unaudited
- including comparative information
- enhancing comparability by treating adjustments of certain transactions consistently across the sector (e.g. research grants and unrealised gains/losses on investments).

The universities have worked diligently to improve this process and we will continue to work closely with them to ensure they meet the relevant framework requirements.

Managing output costs

Managing their cost drivers and their activity and service costs are important elements of sound financial control in universities, linked directly to their financial sustainability. In this respect, we note that the extent of cost analysis and level of cost reporting varies across the sector.

One benefit of timely detailed cost identification and reporting is that council/senate members and senior management can identify whether their courses are running efficiently and whether they will remain financially viable to run.

All universities identify costs at an academic course level as part of developing the business case to undertake a new academic course, but only three regularly monitor costs at the course/subject level. The benefit of regular cost monitoring at this level is that management can assess whether the expected economic benefits outlined in the business case are being realised.

It is difficult to compare the cost of outputs delivered across universities because their methods of allocating their indirect costs, such as corporate salaries and wages and depreciation, to the universities outputs vary. Information about the full cost of outputs, that could be compared within and between universities, would allow better informed decisions about allocating resources to various functions (e.g. teaching, research); activities (e.g. student enrolment, student visa processing, asset management); and student cohort groups (e.g. course enrolled, mode of study) of the university.

In the absence of reliable, consistently measured output costs, indicators of relative cost-efficiency rely on an analysis of input costs, such as the ratio of the number of academic staff to non-academic staff. These are relatively poor proxies, but can shed some light onto relative financial performance and efficiency. In this example, the ratio of academic to non-academic staff ranges between 43 per cent and 57 per cent across Queensland universities, as well as nationally.

On average across the Queensland sector for 2014, non-academic employee expenses represented 28.3 per cent of total expenditure, as compared to 27.4 per cent nationally. Within the Queensland university sector for both 2014 and 2015, this percentage varied between universities, ranging from 25 per cent to 35 per cent.

These results are above the federal department's benchmark of 20 per cent for administrative expenses (of which non-academic staff costs is a significant portion) as a proportion of total expenditure; but we note this benchmark was last updated in 2001.

Risk management

In addition to the mandatory financial audit review of risk management, this year we conducted an in-depth review of risk management practices in Queensland universities.

The application of a structured and well-defined risk management framework strengthens a university's ability to deal with uncertainty, and to minimise potential adverse impacts on its strategic objectives. If executed properly, risk management also helps identify business opportunities and can foster innovation in service delivery and the development of new products.

We found there was strong leadership of, and recognition among, university senior management of the importance of risk management. The differences between the universities related to their articulation of risk appetite and risk tolerance levels, the extent of risk reporting, and the amount of focus on assessing risk as part of strategic planning. Of the seven universities, only three had a formally articulated risk appetite statement and none had specified risk tolerance levels, although some universities were in the process of developing them. Our model for assessing a university's maturity in risk management is in Appendix H.

With the growing national policy focus on innovation, it is likely that all universities will need to become more sophisticated in how they identify and capitalise on opportunities. However, capitalising on innovation requires an appreciation of what is an acceptable amount of risk that the university is willing to take on in pursuing opportunities. This reinforces the importance of each university having an established and well-understood risk appetite to guide these decisions, some of which are likely to involve significant investment or new and untested ways of doing business. The greatest value of a risk appetite statement lies in the discussions and process used in its development, and not just in the statement itself.

We have provided each university with a customised risk scorecard to help them improve their risk maturity so that they can better manage risk, now and into the future.

Reference to comments

In accordance with s.64 of the *Auditor-General Act 2009*, a copy of this report was provided to the Premier, the Director-General of the Department of the Premier and Cabinet, the Minister for Education and the Director-General of the Department of Education and Training as well as all universities and grammar schools named in this report, with a request for comment.

Their views are considered in reaching our audit conclusions and are represented to the extent relevant and warranted in preparing this report. The Department of Education and Training provided a formal response, which is in Appendix A.

1. Context

Scope of report

The education sector, for the purpose of this report, comprises universities, their controlled entities, grammar schools and other education entities that have a financial year-end of 31 December. The majority of controlled entities are companies that carry out various activities to further each of the university's objectives.

This report does not include the state Department of Education and Training nor TAFE Queensland, which have 30 June year-ends. We discuss these entities in the auditor-general's report to parliament on results of audit: state public sector entities with a 30 June year-end.

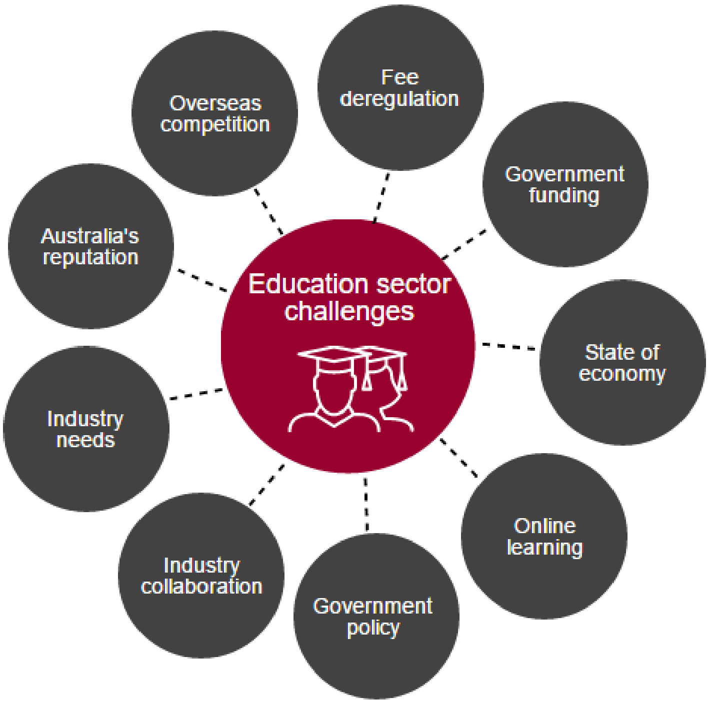
This report includes 88 entities, of which 36 prepare financial statements for audit certification. This leaves 52, which do not prepare financial statements, as they are not required to, or are exempt, by law. Of these, 20 were dormant; that is, they did not operate in 2015 (see Appendices B and C).

Influences shaping the education sector

Various stakeholders and industry groups influence the universities and grammar schools. How the universities and schools shape their business and position themselves to remain sustainable is a continual challenge.

Figure 1A identifies some of the significant challenges the sector faces.

Figure 1A
Sector challenges



Source: Queensland Audit Office

The sector as a whole face these challenges daily and our report identifies the impact these are having on their financial performance, sustainability and current financial position. These challenges will affect enrolment numbers, fee settings, Australian university's reputation and the mode of learning.

Education sector entities financial responsibilities

Legislative framework

Universities and grammar schools are required by the *Financial Accountability Act 2009* (the Act) to:

- ensure their operations are carried out efficiently, effectively and economically
- establish and keep funds and accounts that comply with legislative requirements
- ensure annual financial statements are prepared, certified and tabled in parliament in accordance with legislative requirements
- undertake planning and budgeting appropriate to their size
- establish and maintain appropriate systems of internal control and risk management.

Universities

Each of the seven universities has its own legislation. For financial reporting purposes, their Acts provide that they are statutory bodies and are subject to the requirements of the Act and the *Statutory Bodies Financial Arrangements Act 1982.*

The universities prepare general purpose financial statements in accordance with the Financial and Performance Management Standard 2009 and the Australian accounting standards. The Act requires audited financial statements to be included in the annual report of each university and tabled in parliament by the Queensland Minister for Education. Additional disclosure requirements are required by the Australian Government's Department of Education and Training in accordance with the *Higher Education Support Act 2003*.

Grammar schools

While historically associated with the public sector through the provisions of the *Grammar Schools Act 1975*, grammar schools operate on a fully commercial basis with limited financial assistance provided by the state. They are statutory bodies and are subject to the requirements of the Act and the *Statutory Bodies Financial Arrangements Act 1982*.

Controlled entities

The majority of controlled entities of universities are public companies subject to the requirements of the *Corporations Act 2001*.

The *Corporations Act 2001* requires public companies to report to members and provide the auditor's report on the financial statements. They must do this, either by 21 days before the next annual general meeting after the end of the financial year, or four months after the end of the financial year—whichever is earlier. Entities with a 31 December year-end must report by 30 April.

Other reporting requirements

As statutory bodies, universities and grammar schools are required, when preparing their annual financial statements, to have regard to the minimum reporting requirements contained in the financial reporting requirements for Queensland Government agencies. Queensland Treasury issues these reporting requirements.

The chancellor/chair and the executive responsible for financial administration at each entity must certify compliance with legislative requirements for establishing and keeping accounts. They must also certify that the financial statements present fairly the entity's transactions for the financial year and financial position.

At the first meeting after it receives the audit report on the statements, the governing body of the university or grammar school must consider the statements and the report. If the report contains comments, observations or suggestions about anything arising out of an audit, the governing body must consider these.

The Queensland Financial and Performance Management Standard 2009 requires universities and grammar schools to provide draft financial statements for audit by an agreed date. They must allow enough time to conduct the audit and complete the audit opinion by no later than two months after the end of the financial year to which the statements relate.

The university or grammar school must give the annual report to the minister in time to allow the report to be tabled in parliament within three months of the end of the financial year to which the report relates.

Audit responsibilities

Section 40 of the *Auditor-General Act 2009* requires the auditor-general to audit the annual financial statements of all public sector entities (including those of statutory bodies) and to prepare an auditor's report about the financial statements.

The auditor's report, which includes the audit opinion, assures readers of the reliability of the financial report, including compliance with legislative requirements. In accordance with Australian auditing standards, one or more of the following audit opinion types may be issued:

- An **unmodified opinion** is issued when the financial statements comply with relevant accounting standards and legal requirements.
- A **qualification** is issued when the financial statements as a whole comply with relevant accounting standards and legislative requirements, with the exceptions noted in the opinion.
- An **adverse opinion** is issued when the financial statements as a whole do not comply with relevant accounting standards and legislative requirements.
- A **disclaimer of opinion** is issued when the auditor is unable to express an opinion on the compliance of the financial statements with relevant accounting standards and legislative requirements.

An emphasis of matter may also be included with the audit opinion to highlight an issue of which the auditor believes the users of the financial statements need to be aware. The inclusion of an emphasis of matter does not modify the audit opinion. An emphasis of matter will be included for all special purpose financial statements, which are designed to meet the financial information needs of specific users. General purpose financial statements, on the other hand, are intended to meet the information needs of all users.

A copy of the certified statements and the auditor's report is provided to the chief executive officer of the entity as well as the appropriate minister.

The auditor-general prepares a report to parliament on each audit conducted. The report states if the audit has been finished and the financial statements audited. It must also include:

- details of significant deficiencies where financial management functions were not performed adequately or properly
- any actions taken to improve deficiencies reported in previous reports.

This report satisfies these requirements.

Report structure and cost

Chapter	Description
Chapter 2	▪ University sector ▪ Conclusions ▪ Audit results ▪ Key audit matters ▪ Financial performance and sustainability ▪ Infrastructure and finance ▪ Financial control ▪ Massive open online courses (MOOCs).
Chapter 3	▪ Area of controls focus: risk management ▪ Leadership ▪ People and accountability ▪ Process integration ▪ Response ▪ Monitoring ▪ Achieving outcomes and innovation ▪ Managing research risk.
Chapter 4	▪ Grammar School sector ▪ Conclusions ▪ Key audit matters ▪ Audit results ▪ Financial performance and sustainability ▪ Financial control.
Appendix A	formal response provided.
Appendix B	contains the status of the 2015 financial statements.
Appendix C	lists entities for which audit opinions will not be issued.
Appendix D	provides details of the operating results of the universities and grammar schools.
Appendix E	provides checklist for preparation of financial statements.
Appendix F	provides better practice principals for disclosing underlying results.
Appendix G	provides definitions of staff by function.
Appendix H	provides details of QAO's Risk Management Maturity model.
Appendix I	provides better practice on risk management.
Appendix J	provides a glossary of risk management terms.

The cost of the report was $130 000.

2. Universities

In brief

The seven Queensland public sector universities are located across Brisbane, Gold Coast, Rockhampton, Sunshine Coast, Toowoomba and Townsville. Some have campuses across the state, interstate and overseas. The universities conduct undergraduate and postgraduate programs of study and research programs. These seven universities control 67 entities of which 15 were also required to prepare financial statements in 2015.

Conclusions

- All universities are operating sustainably and managing their financial risks effectively.
- Internal control frameworks are operating effectively, with some improvements recommended to reduce the risk of error or fraud arising from breakdowns in controls.
- The quality and timeliness of the financial statements are satisfactory.
- All financial statements have been prepared in accordance with the legal requirements.

Findings

- We issued unmodified audit opinions for all universities and their 15 controlled entities, which were required to prepare financial statements, with nine of these controlled entities also receiving an emphasis of matter about their special purpose financial statements.
- University management and external audit certified all financial statements within the legislated period of two months.
- We were satisfied with the quality and preparation processes of financial statements by all universities, with some improvements recommended.
- We identified some control breakdowns, including IT security access to key financial systems.
- All universities made operating surpluses in 2015, as they did in 2014, and their key financial ratios are within acceptable levels.
- We have suggested improvements to the reporting of underlying results.
- We have suggested universities gain a deeper understanding of their cost drivers to enable them to monitor the costs of their key functions and activities.
- All universities continue to monitor the potential impact of low-cost, massive, open, on-line courses on their business operations.

University sector

Universities are the largest providers of higher education qualifications in Australia. Queensland's public universities are all not-for-profit institutions and are governed in accordance with state and federal legislation.

All universities are registered with the Tertiary Education Quality Standards Authority (TEQSA). TEQSA is the Australian government regulator responsible for assuring the quality of higher education providers. However, unlike other higher education providers, universities can set their own accreditation standards for graduating students.

All universities are required to teach at the tertiary level, undertake research and provide service to the community. The requirement to undertake research is the main difference between Australian universities and other higher education providers.

International education export income 2014-15	
Australia	$18.8 bil.
Queensland	$2.7 bil.

In 2014–15, international education activity generated a total export income of $18.8 billion for Australia, making it the third largest export after iron ore and coal. The higher education sector, mostly universities, contributed $12.5 billion (66.5 per cent of total education export income). In Queensland international education activity generated export income of $2.7 billion, representing 5.8 per cent of total exports. Queensland universities enrol more than 220 000 full-time and part-time students and employ 22 048 staff (full time equivalents).

Entities covered in this chapter

There are seven universities and 67 controlled entities. Due to reasons listed in Appendix C, only 15 controlled entities prepared financial reports. All entities have a 31 December balance date.

In conducting this year's analysis, we have compared the Queensland university sector and individual universities with various national averages calculated from statistics available on the Australian government Department of Education and Training website. The national average for the entire university sector has been further categorised for the Group of 8 (Go8), metropolitan (excluding Go8) and regional universities. Go8 is a distinct group of universities, including The University of Queensland, that comprises the eight most research-intensive universities, which are also the highest internationally ranked Australian universities. Metropolitan universities have been defined as those based principally in large cities including capital cities and the Gold Coast. Regional universities are those universities principally based outside of capital cities.

Conclusions

All universities are financially sound and all received unmodified audit opinions in 2015 and 2014. The financial statements were prepared in accordance with the legal reporting requirements including the Australian accounting standards.

The quality and timeliness of the financial statements were satisfactory, with all universities meeting the two-month legislated requirement for audit to certify their financial statements. Four universities adjusted their draft financial statements in 2015 by $45.01 million (2014: $13.8 million). $33 million of this year's adjustment relate to one university making a series of amendments to both assets and equity.

The internal control environment was generally sound, with some weaknesses identified and improvements recommended at six universities. The classification of audit issues changed in 2015 to align more closely with the auditing standards. There were no material deficiencies identified, two significant deficiencies, and 59 lower risk control deficiency issues raised in 2015. The two significant deficiencies related to inadequate controls over access to key financial computer systems.

All universities have produced an operating surplus in 2015 and the financial performance and sustainability ratios across the sector indicate the universities are operating effectively and are able to meet their short-term and long-term financial obligations (see Appendix D).

All universities monitor costs at an organisational unit level, with three universities regularly monitoring costs at a course/subject level. The method of allocating indirect costs across the sector differs, with the majority of universities not allocating indirect costs at a course or subject level. To better understand the costs of teaching a particular group of students, universities require a full understanding of the associated cost drivers. This detailed understanding of cost drivers will assist management and those charged with governance to make better-informed resource allocation decisions.

An influence on non-current asset valuations for 2015 was the Australian Accounting Standards Board (AASB) determination in May 2015 that a not-for-profit entity is unable to recognise a residual value for an asset where there is no monetary consideration when the asset is disposed. We asked all universities to gauge the impact that this decision would have on their asset values, more specifically their depreciation expense, and the need to incorporate the requirements of the AASB determination into their 2015 valuation process.

Audit results

We have issued unqualified audit opinions on the financial reports of all seven universities and their 15 controlled entities that were required to prepare financial statements. Appendix B shows the list of entities and the audit opinions issued.

Four of seven universities provided draft financial statements for audit by their agreed milestones. One university provided its draft financial statements almost two weeks after the agreed date. Management and audit certified the financial reports for all seven universities by their legislative deadlines.

At year-end, four universities made changes to their draft financial reports affecting their operating result or net assets. Figure 2A shows the total value of adjustments to financial statements before they have been certified by audit.

Financial reporting simplification

A number of universities have taken the opportunity in 2015 to reduce the volume of notes and simplify disclosures in their financial statements. We have worked with each university to advise and assist with this de-cluttering/simplification process. Some are yet to take full advantage of this opportunity and will look at simplifying their statements in 2016.

The focus of the de-cluttering process is on:

- including accounting policies only where necessary to help users understand how material transactions and events are recorded in the financial statements
- including only transactions and activities that are most relevant to understanding the financial statements
- grouping together items that are measured similarly, rather than simply following the order of the income statement or balance sheet
- removing notes that duplicate information or relate to immaterial financial statement balances.

Of the seven universities audited, five have reduced the number of notes disclosed in their certified financial statements, with USC reducing its number of notes by 37.5 per cent and USQ by 25.6 per cent. Across the sector, the average percentage decrease in note numbers was 13.2 per cent.

Figure 2A
Changes to financial statements before they have been certified by audit

Financial statement	2011 $ m	2012 $ m	2013 $ m	2014 $ m	2015 $ m
Income	328.08	2.35	0.36	–	0.16
Expenses	42.91	10.5	3.56	2.98	5.18
Assets	51.23	3.4	7.69	10.82	18.93
Liabilities	142.27	10.5	1.94	–	2.92
Equity	62.17	2.9	–	–	17.82
Total	**626.66**	**29.65**	**13.55**	**13.8**	**45.01**
Number of universities that made an adjustment	6	3	3	4	4

Source: Queensland Audit Office

The adjustments made this year mainly comprise one university's adjustments of $16.49 million to both assets and equity relating to an incorrect journal processed, and the reversal of an addition to capital works in progress included in the revaluation. The other adjustments relate to incorrect processing of accruals, and the misclassification of expenses and liabilities.

There were also changes made to the notes to the financial statements to comply with the Queensland Treasury requirements and the Australian Government Department of Education and Training guidelines. Some of the changes led to more precise disclosures around:

- property, plant and equipment and fair value measurement
- commitments and contingencies
- related parties disclosure
- events occurring after balance date.

We have assessed the process for universities to prepare timely and quality financial statements based on the better practice guide (refer Appendix E) for preparation of financial statements. Overall, we found the financial statements' preparation process to be satisfactory, which contributed to all university financial statements being certified within the statutory deadline.

Key audit matters

We identified a number of significant financial reporting issues throughout the university sector during 2015, as detailed below. We tested these transactions and confirmed their accuracy and completeness. We also ensured the accounting for these transactions was in accordance with relevant legislative requirements.

Valuation of property, plant and equipment

As at 31 December 2015, the net book value of property, plant and equipment for all universities, including controlled entities, was $7 411 million, an increase of $159 million (2.19 per cent) from the 31 December 2014 amount of $7 252 million. This net book value increase is mainly attributable to buildings of $284.8 million and plant and equipment assets (including leasehold improvements) of $36.4 million, offset by a decrease in infrastructure assets of $117.1 million and leased assets of $40.9 million.

Each year, universities assess the value of property, plant and equipment. This is one of the more subjective and complex assessments undertaken, because of the assumptions and estimates applied throughout the process. Valuations vary, depending on the complexity of the valuation methodologies used. This is the case whether the valuations are made by independent valuers, by in-house experts, or by the application of applicable indices. Management's overall assessment of these valuations is crucial to ensuring the values disclosed in the financial statements are materially correct.

A further influence on the 2015 valuations was the AASB determination made in May 2015 that a not-for-profit entity is unable to recognise a residual value for an asset where monetary consideration is not obtained when the asset is disposed. We requested all universities to gauge the impact that this decision would have on their asset values, more specifically their depreciation expense, and the need to incorporate the requirements of this AASB determination into their 2015 valuation process.

For 2015, as a result of these valuations, there has been an overall net increase of $54.3 million (2014: net increase of $206 million). This net valuation increase mainly comprises an increase in buildings of $183.8 million, offset by a decrease in infrastructure assets of $101.9 million and leased assets of $34.6 million.

Griffith University engaged an independent valuer to perform a valuation of its land, buildings and infrastructure assets for the year ended 31 December 2015. Because of the change in valuer, Griffith University adopted a different valuation methodology for 2015 compared to 2014. This has resulted in a significant reduction in the fair value of assets and an increase in depreciation due to the following:

- change in residual values following the Australian Accounting Standards Board (AASB) clarification that the recognition of residual value, in accordance with AASB 116 *Property, Plant and Equipment*, is limited to the value an entity expects to receive as consideration at the end of an asset's life and does not include any future savings from the re use of that asset
- the university needed an additional level for short-life component assets to avoid separate valuations being undertaken for planned maintenance
- change in the depreciation estimate from a conditional assessment 'consumption based' approach to a straight line approach
- change in some asset useful-life-estimates.

The financial impact of the valuation was a material change in the carrying value of the university's non-current assets (downward adjustment to the building assets' carrying value as at 31 December 2013 totalling $480.7 million) and an increase of $22.9 million in the 2014 depreciation expense charged to the Statement of Comprehensive Income. A prior period adjustment was made by the university, which included restatement of the comparative figures to the earliest date practicable: 1 January 2014.

Land sales and acquisitions

The University of Southern Queensland (USQ) purchased The University of Queensland (UQ) Ipswich campus at a contract price of $21.5 million. The transfer of title took place on 7 January 2015 following the receipt of a first instalment of $4 million. The balance will be paid in annual instalments over three years.

USQ engaged an external valuer to assess the fair value of the assets acquired. This fair value was deemed to be $82.6 million and USQ recognised a gain on acquisition of $61 million in the 2015 financial report.

On 30 October 2015, the University of Southern Queensland (USQ) entered into a contract to sell its Fraser Coast Campus to University of the Sunshine Coast (USC) with a settlement date of 1 February 2016. The conditions of the contract were required to be finalised post balance date on 12 January 2016. As per the Fraser Coast Campus Asset Sale Agreement (FCCASA), the purchase price for the sale has been determined as $7 million payable in two equal instalments over two years.

Investments in controlled and other entities

In June 2015, Swiss multinational pharmaceutical company, Novartis International AG (Novartis) acquired 100 per cent of biotech company, Spinifex Pharmaceuticals Inc. (Spinifex) for a total potential consideration of US$725 million on achievement of future milestones, consisting of:

- up-front cash payment of approximately US$200 million
- US$525 million (maximum value) deferred consideration subject to the successful achievement of set future milestones.

UniQuest Pty Ltd (UniQuest), a controlled entity of UQ, held approximately a 5.9 per cent share of Spinifex before the divestment and has the right to receive consideration equal to its share held. The effect of the transaction has given rise to the disposal of one financial asset, being the investment in Spinifex, and the acquisition of another financial asset in the form of cash and the right to receive future cash.

We have considered management's proposed accounting treatment for each of the following:

- de-recognising UniQuest's carrying value of the shares held in Spinifex
- determining the fair value of the consideration to be received for the share held by UniQuest in Spinifex at the transaction date, taking into account the three elements of cash, cash held in escrow (funds held for a 12 month period to cover potential claims against the sellers) and the deferred consideration. The total consideration payable to UniQuest is as follows:
  - cash AU$16 million
  - cash held in escrow AU$1.6 million
  - deferred consideration AU$4.98 million
- accounting for the net gain of AU$15.5 million on disposal
- subsequent measurement of the financial asset acquired as at balance date.

Each Queensland university holds 10 000 $1 fully paid shares in Education Australia Limited (EA). EA in turn holds a 50 per cent share in IDP Education Ltd (IDP), a provider of international student placement services and English language tests via the International English Language Testing System (IELTS).

IDP listed on the Australian Stock Exchange in November 2015. As at 31 December 2015, EA held 125 397 484 shares in IDP valued at $417.6 million.

Most universities arranged for an independent valuation of their share entitlement to value their shares for financial statement purposes. A valuation report was provided to the universities who then used this information to assess the fair value of their investment in EA, which approximated $9.2 million each.

Financial performance and sustainability

Universities must be able to meet current and future obligations, as they fall due, to be financially sustainable in the short term. In the longer term, they should be able to absorb foreseeable financial risks without adjusting their current revenue and expenditure policies.

Analysts use financial ratios to help them assess an entity's financial health. We selected financial ratios commonly used by analysts across the Australian not-for-profit sector to help us understand the short and long-term sustainability of the university sector.

These financial ratios were calculated using university parent figures from the audited financial statements to allow for comparability against various national averages. These ratio calculations are included in Appendix D of this report. The results of these ratios should be considered with other factors such as management standards, financial budgets, asset replacement strategies, cash and investment balances and capacity to generate revenue.

Results of the analysis of these ratios for universities for 2015 were positive indicating all universities:

- achieved a positive operating result
- had adequate liquidity to meet their short term liabilities as they fall due
- maintained a low level of debt compared to their revenues
- are adequately replacing existing capital with many within the sector growing their campus infrastructure
- were able to meet employee expenses
- generated sufficient revenue to repay borrowings and loans.

Operating result

Figure 2B shows all universities have produced an operating surplus for 2015.

Figure 2B
Operating results

	UQ	QUT	GU	USQ	JCU	CQU	USC	Qld sector
2015 Operating result ($'000 parent)	35 550	33 727	50 887	81 608	29 728	13 526	15 156	260 182
2015 Operating result ($'000 consolidated)	58 572	33 767	50 887	81 608	26 402	14 599	15 135	280 970

Source: Queensland Audit Office

All universities have achieved operating surpluses for the past three years, which is a good result. They will continue to be challenged by reduced government funding; the volatility of the Australian dollar affecting international student numbers; government policy on visa laws; fee deregulation uncertainty; and the increased use of technology with on-line learning.

Central Queensland University (CQU) became the first dual sector university in Queensland in 2014. The impact of the merger with the Central Queensland Institute of TAFE continues, and CQU will need to manage this transition to achieve the expected financial and operational benefits.

Underlying results reporting

Four universities report a non-statutory underlying result in their published annual report. This underlying result adjusts the audited statutory operating result for various items that managers consider abnormal or extraordinary. There is no Australian accounting standard regulating the underlying results disclosure. This disclosure is unaudited. However, the Australian Securities and Investments Commission (ASIC) have released some guidance on how to disclose an underlying operating result in ASIC RG 230 *Disclosing non-IFRS financial information.* The New Zealand Financial Markets Authority (FMA) has issued similar guidance. Last year QAO adapted these guides and provided 10 principles for better practice reporting about more subjective financial measures such as underlying operating result (refer Appendix F).

Figure 2C
Underlying results

	UQ	QUT	JCU	USC
2015 Statutory operating result ($'000 consolidated)	58 572	33 767	26 402	15 135
2015 Underlying result ($'000 consolidated)	29 917	26 811*	(3 763)*	5 100*

* Parent figure only

Source: *Queensland Audit Office*

In last year's report, where a university reported an underlying result in its annual report, we assessed this against QAO's better practice principles. Areas for improvement included that there was:

- no clear narrative explaining underlying results
- no reconciliation with the statutory result
- no explanation of adjustments made
- no disclosure of adjustments being 'one-off' in nature
- no clear statement advising that the figures were unaudited.

We also found inconsistency in the nature of the adjustments applied across the university sector to determine the underlying results. Based on our identified areas for improvement, we outlined a series of better practice principles adapted from ASIC's RG 230 to assist university CFOs when disclosing underlying results within their annual reports.

In November 2015, the Queensland Universities Chief Financial Officers Group (QUCFOG) issued the QUCFOG Financial Reporting Standard Practice Statement titled *Underlying Operating Result* to provide greater consistency across the Queensland university sector in how to calculate and disclose the underlying result. The QUCFOG statement proposed five principles for a standard approach for reporting non-statutory underlying operating results. The universities' proposal to apply consistent underlying result reporting principles is a positive step and demonstrates the Queensland sector's desire for consistency in reporting.

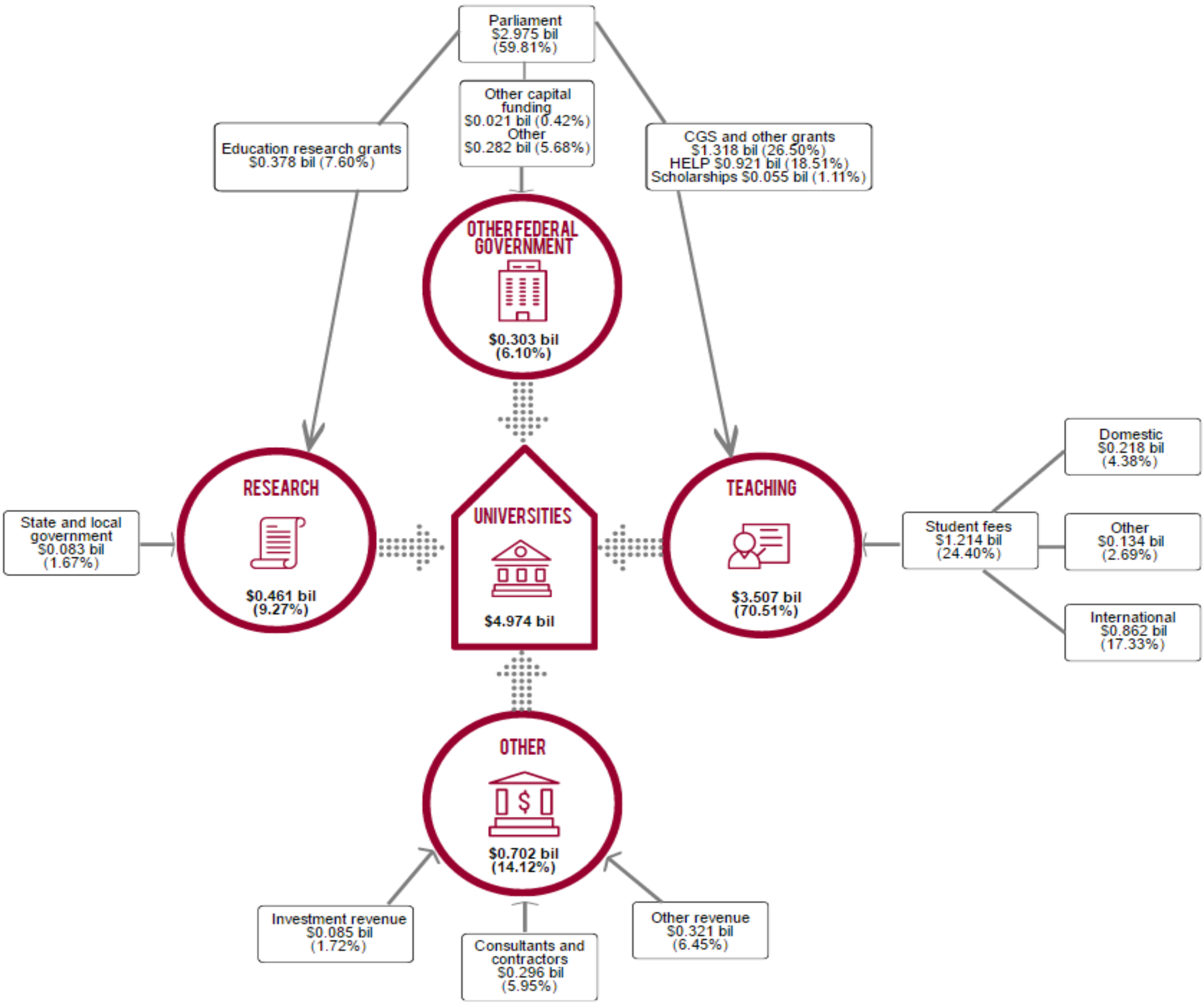
We have reviewed the 2015 underlying result against the QUCFOG principles and noted there was still some inconsistency around adjustments made relating to research grants and unrealised gains/losses on investments. We acknowledge there will be specific circumstances for each university and some differences may always occur.

This year we again assessed the underlying result disclosures against QAO's better practice principles. One university fully complied. The other three universities complied with at least eight of the 10 principles, with all three not specifying that the underlying results were unaudited. One university did not disclose comparative information.

Operating income

In 2015, Queensland universities generated total consolidated operating income of $5.087 billion, an increase of $70.99 million (1.42 per cent) compared with 2014. Figure 2D shows the standard operating revenues of the parent entities generated from the various functions of the university sector. In 2015, revenue generated from parent operations was $4.974 billion, an increase of $60.679 million (1.23 per cent) compared with 2014.

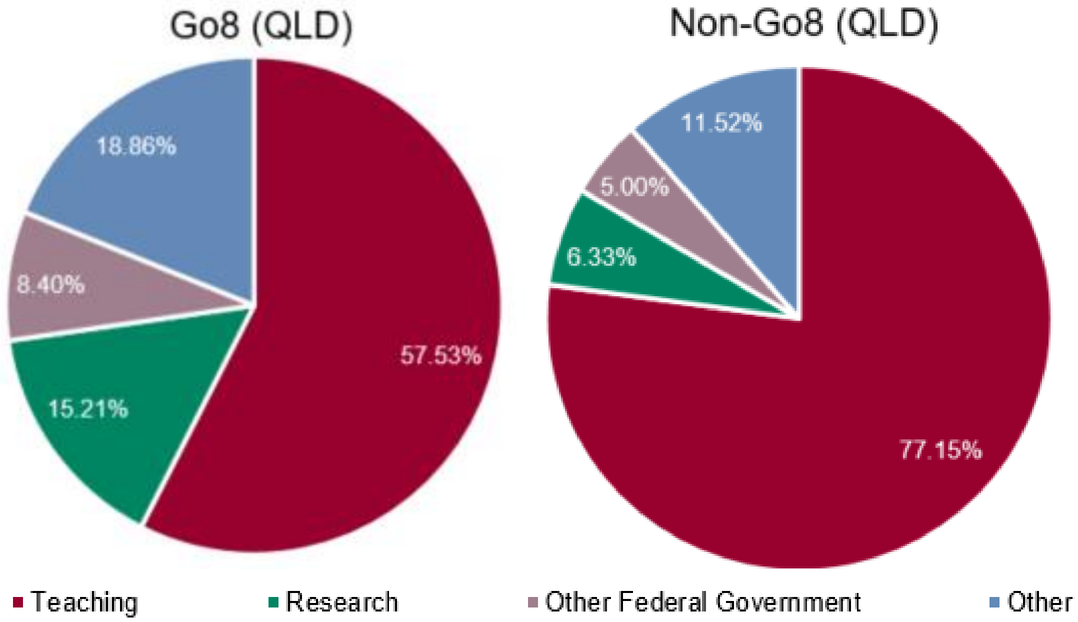
Figure 2D
2015 operating income (parent)



Source: Queensland Audit Office

The composition of revenue differs between the Go8 and non-Go8 universities. Figure 2E shows the differences between Go8 and non-Go8 universities in Queensland, with similar differences occurring nationally. Non-Go8 universities rely more heavily on teaching-related revenues, while Go8 universities generate a greater proportion of their revenues from research and other funding sources.

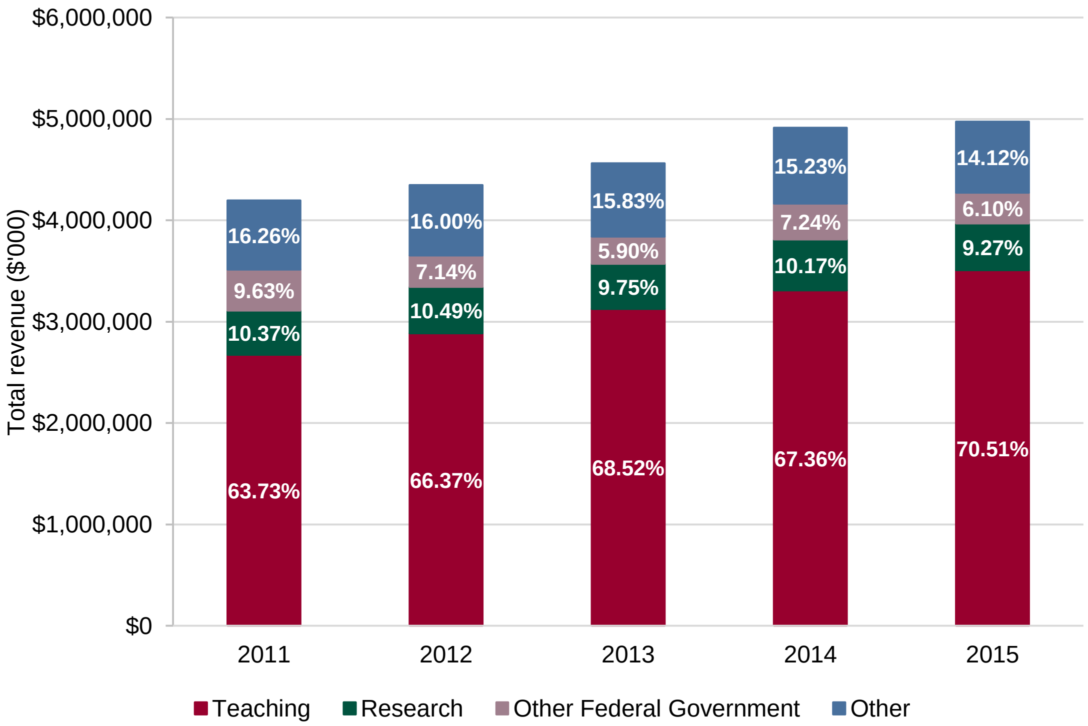
Figure 2E
Revenue composition by Go8 and non-Go8 universities 2014



Source: Queensland Audit Office

Figure 2F shows revenues across the Queensland sector have grown over the past five years by 18.52 per cent. Teaching-related revenues have significantly grown over the five-year period, representing approximately 70 per cent of total university revenues in 2015. This is consistent with the national trend.

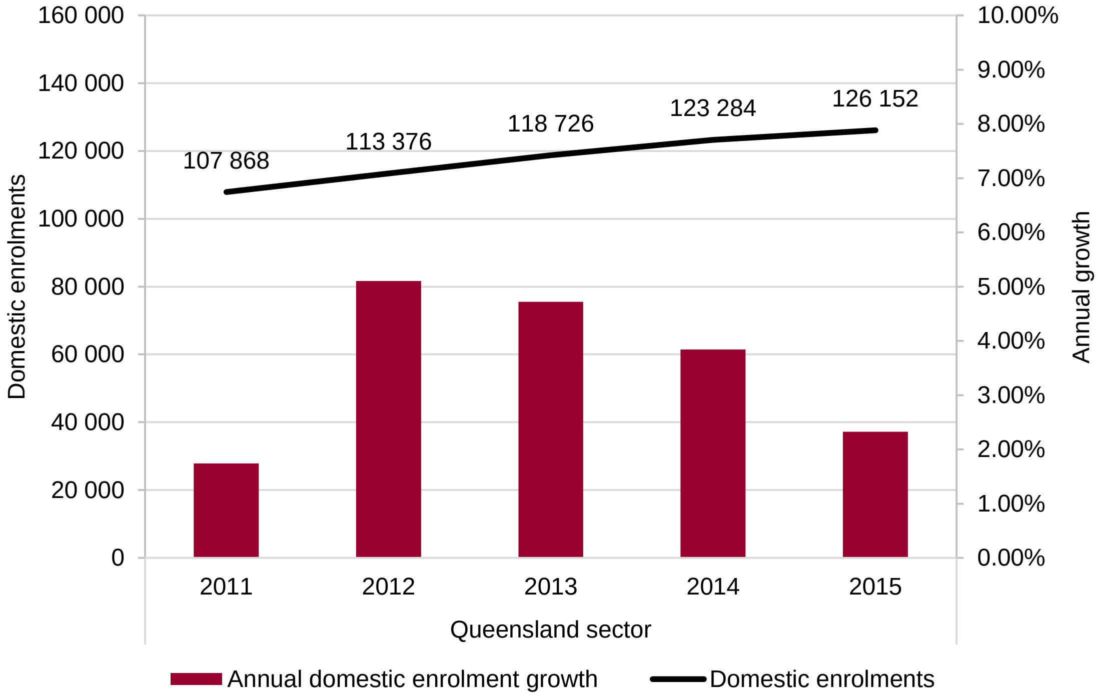
Figure 2F
Operating income composition 2011–2015



Source: Queensland Audit Office

Teaching related revenues have increased due to increases in domestic and international student revenues. Figure 2G shows Queensland domestic student enrolments have consistently increased over the 2011 to 2015 period, following the introduction of demand driven funding for undergraduate courses in 2012. However, the rate of growth has continued to soften since 2012. A similar trend has occurred nationally.

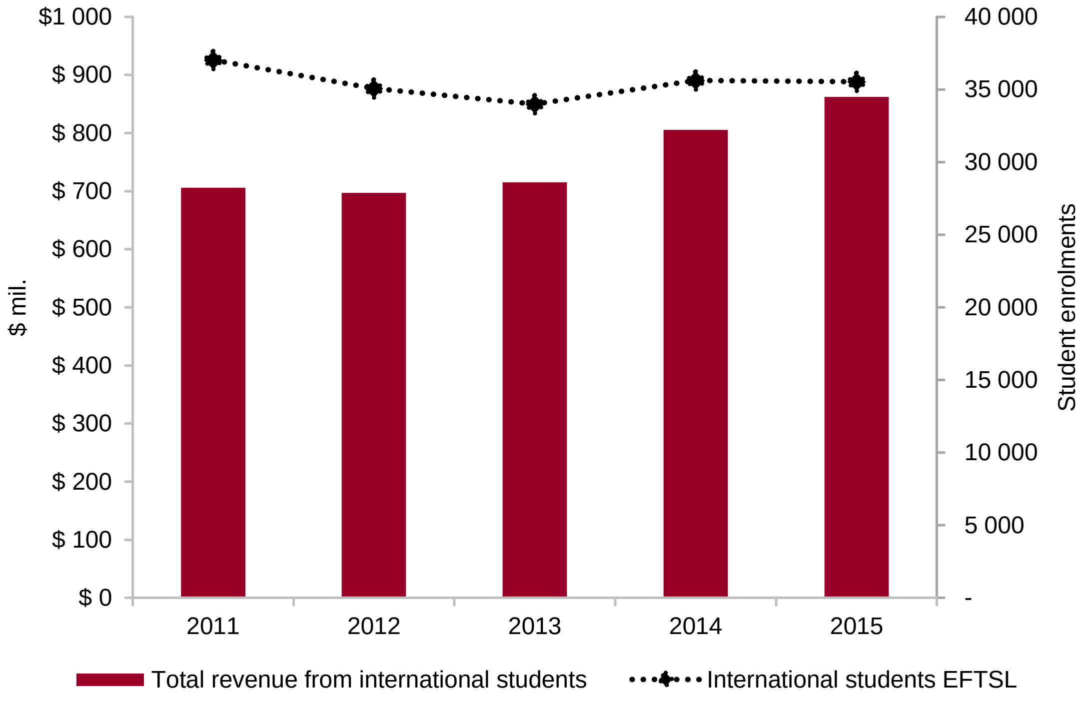
Figure 2G
Domestic student enrolment trend 2011–2015 (EFTSL)



Source: Queensland Audit Office

Figure 2H shows revenue generated from international students has been increasing over the last five years, despite the decline of international student enrolments. The increased revenue is due to increases in the average international student fees, along with the increasing proportion of international students undertaking postgraduate courses that attract higher fees than undergraduate courses. The average international student fee for Queensland universities increased from $19 068 in 2011 to $24 258 in 2015. This is an increase of 27.2 per cent.

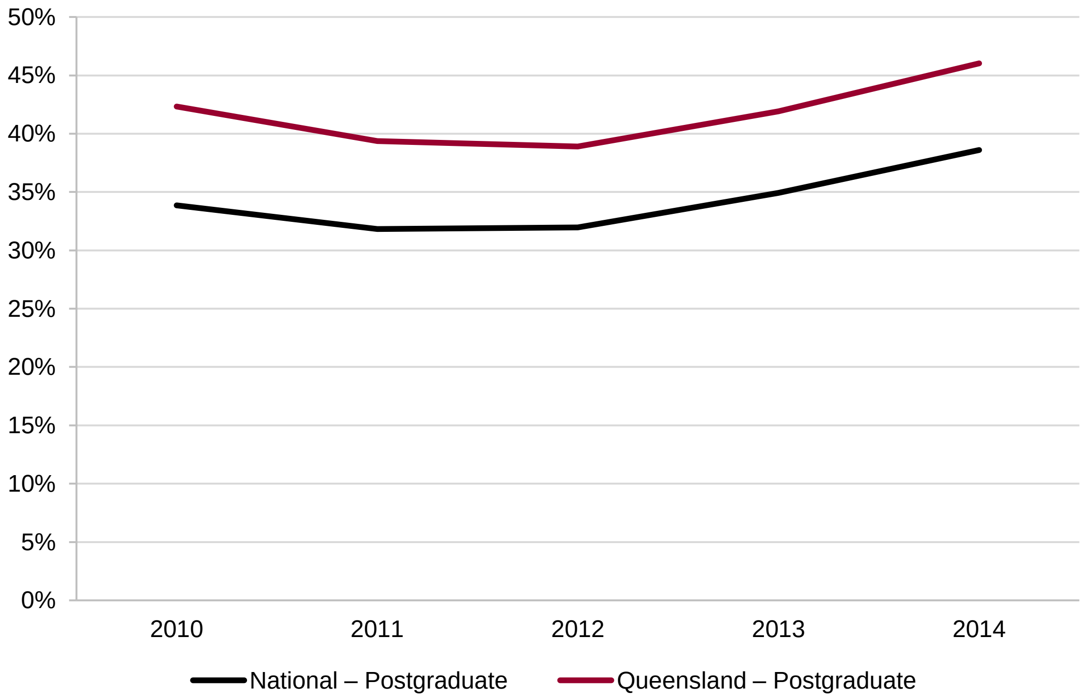
Figure 2H
International students revenue and enrolments



Source: Queensland Audit Office

Figure 2I shows the number of postgraduate students as a percentage of total international students has been growing since 2011, both within Queensland and nationally. This figure also shows that Queensland has a higher proportion of its international students undertaking postgraduate studies compared to the national average.

Figure 2I
Percentage of international students undertaking post graduate studies (EFTSL)

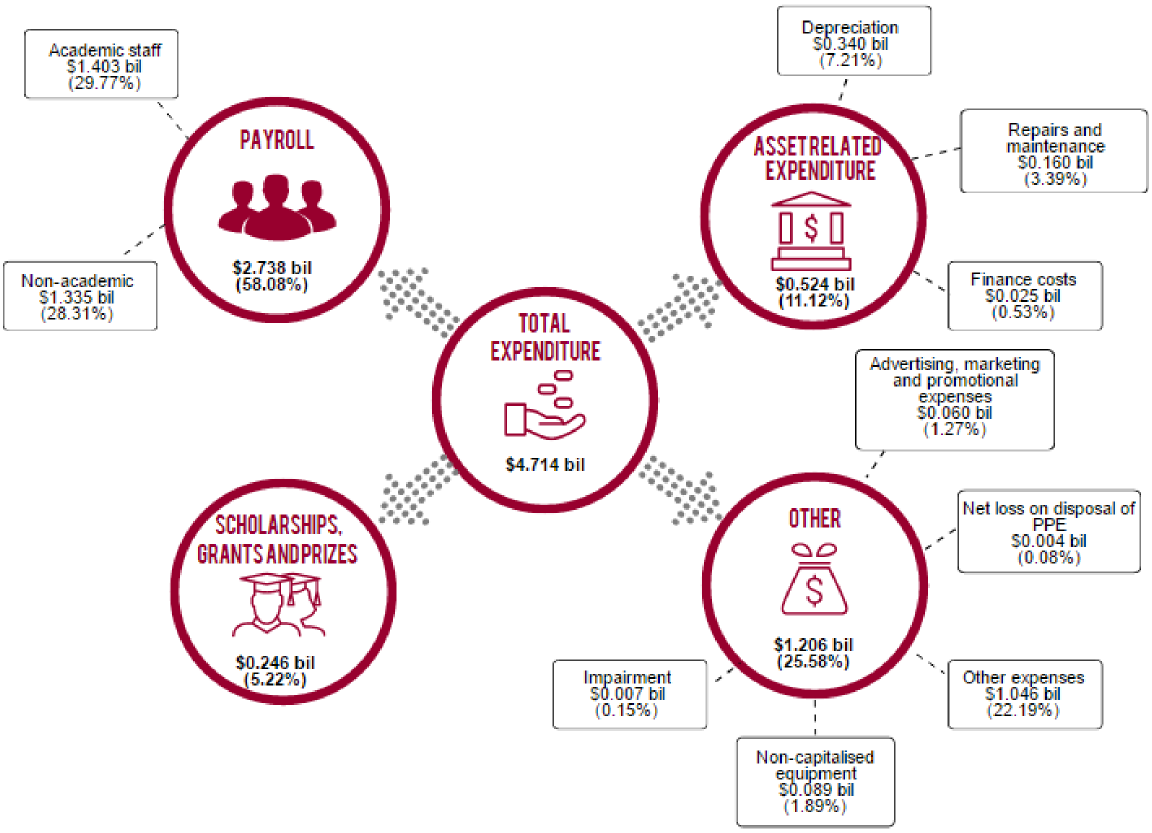


Source: Queensland Audit Office

Operating expenditure

In 2015, Queensland universities had total consolidated operating expenses of $4.806 billion, an increase of $223.49 million (4.88 per cent) compared with 2014. The graphic below (2J) shows the total operating expenses for the parent entities' standard operations. In 2015, operating expenses of parent entities totalled $4.714 billion, an increase of $228.61 million (5.10 per cent) compared with 2014. The biggest portion of the operating cost is employee expenses including academic and non-academic staff that account for about 58 per cent of the total operating expenses. About 11 per cent of the operating expenditure relates to asset finance and management.

Figure 2J
2015 expenditure (parent)

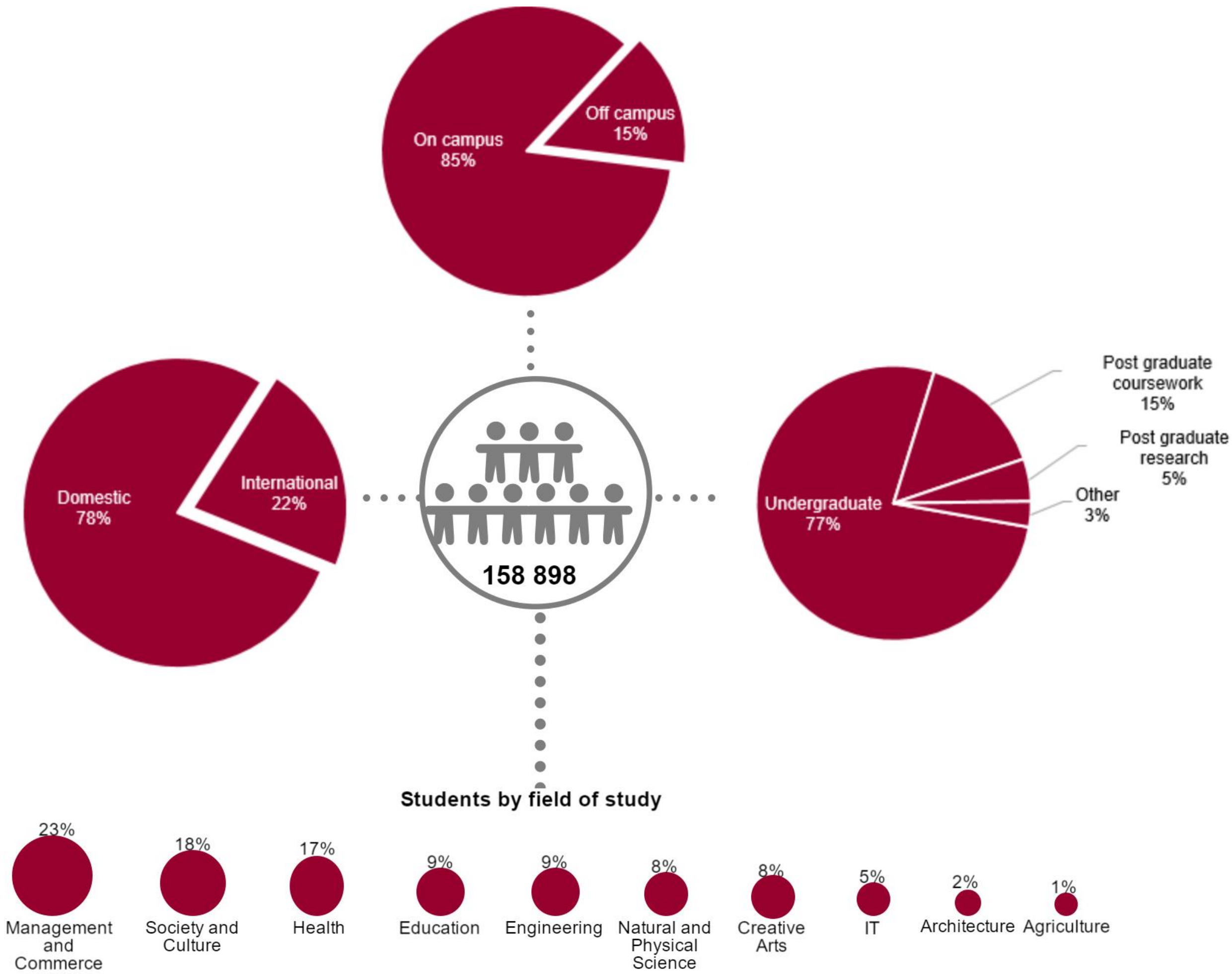


Source: Queensland Audit Office

To get a better understanding of the costs to teach a particular group of students, universities require a deep understanding of the associated cost drivers.

The enrolment composition at universities consists of various groups based on certain factors, including field of study, mode of delivery and domestic/international status. The following figure (2K) provides an overview of the 2014 student enrolment composition within Queensland universities based on the most recent publicly available information from the Australian Government Department of Education and Training.

Figure 2K
Queensland student composition 2014 (EFTSL)



Source: Queensland Audit Office

Identifying and managing teaching output costs

The enrolment composition at an individual university influences the teaching output costs of a university as the cost drivers can significantly differ between student groups. For example:

- Postgraduate courses tend to cost more to teach than undergraduate courses, due to smaller class sizes and the use of senior staff to deliver postgraduate courses. Research students also require supervision by a senior academic.
- International students cost more to enrol and teach due to agent fees to recruit international students; increased regulatory costs including student visa processing costs; and increased student support services to assist students to adjust to living in a new country.
- Off-campus/external students in general have less need for on-campus infrastructure such as lecture theatres, tutorial rooms, parking and social infrastructure. As a result, the cost to finance and maintain these assets is likely to be higher for on-campus students than students who study off-campus. However additional IT infrastructure costs are incurred to support external/off campus students to access various technology platforms.
- Costs to deliver a specific course will vary from one course to another and will be influenced by size of classes; seniority of staff in delivering the course; the extent of practical experience required (including external practical placements); and the use of specialist equipment.

The nature and extent of reporting teaching costs varies across the sector. We reviewed the cost management information provided to those charged with governance and discussed this issue with managers. All universities provide costing reports to those charged with governance at relevant organisational unit levels (i.e. division/faculty/school). All universities identify costs at an academic course level as part of developing the business case to undertake a new academic course. However, only three universities regularly monitor costs at the course/subject level. The benefit of regularly monitoring costs at the course/subject level is that it assists managers to assess whether the economic benefits outlined in the business case are being realised. It also helps managers to decide objectively which courses/subjects are operating efficiently so they can determine their viability.

We also noted the method of allocating indirect costs to the organisational unit or course level (i.e. corporate salaries and wages and depreciation) varies across universities making it difficult to compare costs for respective outputs between universities. None of the universities has identified the unique cost drivers for identifiable student groups, or reported these costs to those charged with governance. Identifying the full cost of outputs, that can be compared within and between universities, would allow better informed decisions about allocating resources to various functions (e.g. teaching, research); activities (e.g. student enrolment, student visa processing, asset management); and student cohort groups (e.g. course enrolled, mode of study) of the university. In the absence of reliable, consistently measured output costs, indicators of relative cost-efficiency rely on an analysis of input costs.

These observations are not unique to Queensland. On 31 November 2015, the Grattan Institute published a report titled '*The cash nexus: how teaching funds research in Australian universities*' which concluded Australia needs a more transparent system for reporting how universities spend their money. The report noted that, unlike the United Kingdom and the United States, Australia does not classify university spending according to its purpose. As a result, it is unclear how much is spent on each of the core functions/outputs of a university (teaching and research).

While revenue can be easily allocated to the functions of teaching and research (see Figure 2D), this is more difficult for expenses, as they are not regularly tracked and reported based on function across the sector. There are also difficulties in allocating shared costs between functions (teaching and research) and cost drivers to determine costs for a particular student cohort group. For example, buildings and staff may be used across functions and various student groups, and costs should be allocated accordingly. Most universities have their own systems to allocate costs for internal reporting purposes, but these methods vary across the sector and there is no regular national reporting of expenditure on this basis.

Employee expense

Employee expense is the largest expense incurred across the sector totalling $2.738 billion; it represents about 58 per cent of total university expenditure.

The Australian Government Department of Education and Training's *Benchmarking: A Manual for Australian Universities* provides a series of operational benchmarks, to ensure universities maintain sufficient flexibility to meet their various competing needs. These include the following indicators on what is considered good practice with respect to expense:

Figure 2L
Employment expenditure benchmarks

Benchmark analysis 2014	Employee expenses as % of revenue		Non-academic employee exp as % of total expenditure	
	2014 %	5 yr avg %	2014 %	5 yr avg %
UQ	53.49	51.48	25.36	25.62
QUT	57.18	54.72	30.70	31.06
GU	57.11	55.49	29.78	30.19
USQ	56.33	58.79	35.30	34.92
JCU	48.43	51.00	26.98	26.82
CQU	37.90	46.05	26.61	24.85
USC	50.62	53.53	32.26	32.08
Qld Sector	52.92	52.84	28.27	28.30
National	53.97	53.58	27.44	27.34
Regional (Nat)	52.19	52.93	28.58	28.27
Metro (excl. Go8) (Nat)	57.32	55.51	28.49	28.25
Go8 (Nat)	51.91	51.91	26.13	26.23

Source: Queensland Audit Office

Figure 2L shows total employee expense as a percentage of total revenue for all universities is between 50 to 70 per cent which, according to the department's manual, is good practice. National data for 2015 is not available. As a result Figure 2L provides the benchmark measures for 2014 to allow comparison with national averages.

Another relevant operational benchmark is comparing administrative expenses to total expenditure. The department's manual defines overall administrative expenses to include central administration, the costs of outsourced functions (e.g. payroll) and any administrative costs within units with devolved responsibilities. For the purposes of this report, this benchmark has been calculated using non-academic employee expenses as a percentage of total expenditure. Non-academic employees are those not employed in a teaching and/or research capacity and non academic costs are the most significant portion of administrative expenses. These costs also include staff employed on various government funded projects. Figure 2L shows from a Queensland perspective for the 2014 year, four universities exceed both the state and national averages, while UQ has the lowest ratio across the Queensland universities and is lower than the Go8 average. There is a 10 per cent difference between the highest and lowest Queensland universities' results for 2014. CQU had the lowest five-year average.

The department's current manual considers it good practice when a university's total administrative expenses do not exceed 20 per cent of total expenditure allowing a greater proportion of the total annual budget to be spent on the core functions of teaching and research. This current benchmark is dated 2001.

The above result is explained when you look at the composition of staff between academic (those employed in a teaching and/or research capacity) and non-academic within universities. Appendix G outlines the staff function definitions provided by the Australian Government Department of Education and Training. Figure 2M below details the composition of staff between academic and non-academic across the Queensland university sector and is consistent with the national trend, with non-academic staff representing 57 per cent across the sector.

Figure 2M
Academic and non-academic staff composition 2015

	QUEENSLAND	NATIONAL
Academic staff	42.70%	43.56%
Non-academic staff	57.30%	56.44%

Source: Queensland Audit Office

Universities overseas are actively seeking opportunities to share service/cost sharing arrangements with other universities to achieve cost savings as well as realise other associated benefits (e.g. greater specialisation). For example, in February 2015, Universities UK released a report titled *Efficiency, effectiveness and value for money* highlighting the economic benefits of shared service/cost sharing arrangements. This report also states work is underway to develop a model to assist institutions to maximise the benefits of sharing services.

Infrastructure and finance

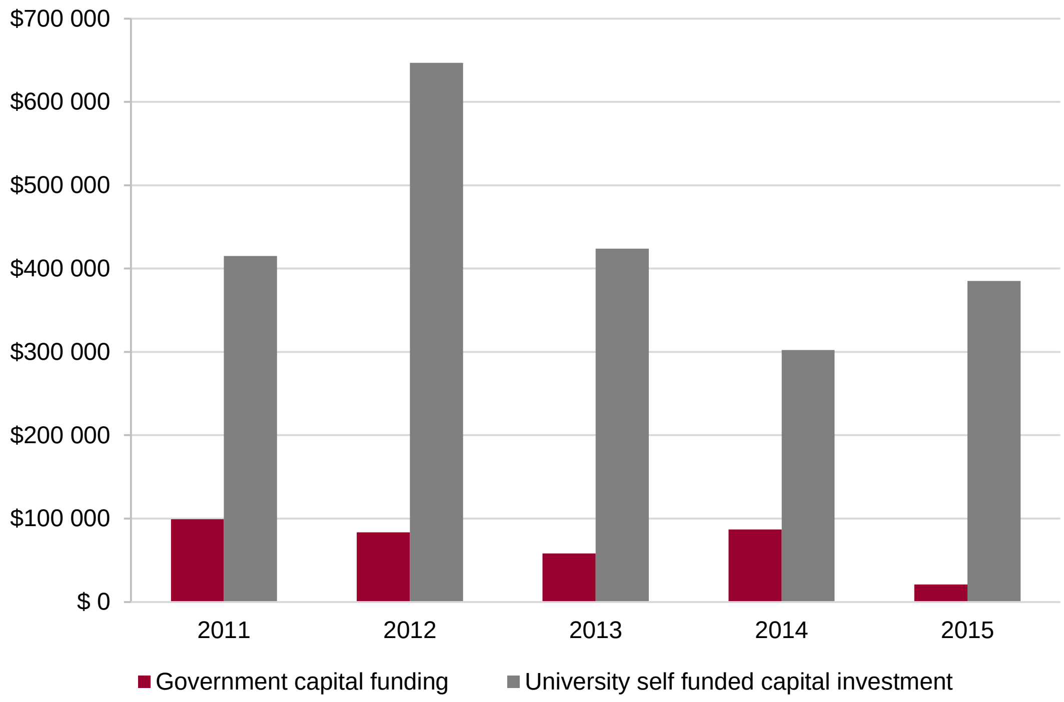
Property, plant and equipment (PPE) is the most significant item in the financial statements. It represents about 75 per cent of the total assets across the university sector in Queensland. PPE related expenditure across the sector has increased by $201.72 million in the period 2011 to 2015 and by 2.44 per cent as a proportion of total expenditure over the same period.

As with PPE in any sector, the cost of purchasing, managing and maintaining these assets is challenging. Universities have structures and processes in place to monitor costs such as capital works, repairs and maintenance, depreciation, amortisation (the process of accounting for asset usage over a period) and financing costs. Government has traditionally provided capital-funding support for the construction of new infrastructure. However, Figure 2N shows that the level of capital grant funding from government has been trending downward in recent years.

The significant spike in self-funded investment in 2012 related to a peak in the capital works programs of four universities, which included University of Southern Queensland's development of its Springfield campus and Griffith University's construction of its medicine and oral health and general teaching facilities. The increased government funding in 2014 relates to increased capital grants to assist Central Queensland University's transition to a dual sector university. In 2015, government capital grant funding supported five per cent of sector capital investment with approximately 95 per cent of capital investment self-funded by the universities. This compares with 2011 where government capital funding supported 19 per cent of sector capital investment.

Better understanding the cost drivers of key functions will allow universities to review activities affecting these cost drivers to reduce costs and provide greater capacity to self-fund capital growth and perform ongoing asset maintenance.

Figure 2N
Funding split for capital investment 2011 to 2015 ('000)



Source: Queensland Audit Office

Controls over financial reporting

All universities have appropriately designed and implemented internal controls, and our testing found them to be generally effective to enable audit to rely on them and reduce our substantive testing.

In 2015, the classification of audit risk for issues identified changed, to better align with the auditing standards. Material and significant deficiencies are audit issues that have the potential to lead to a material misstatement of the financial statements. We identified no material deficiencies, and we raised just two significant deficiency issues in 2015.

These two issues related to information technology controls, including inappropriate privileged access to a key financial system and inadequate user access reviews. These issues, if unresolved, increase the risk for unauthorised access to the financial system and potential fraudulent transactions occurring undetected.

We also reported 59 lower risk deficiency issues addressing the following areas: information technology controls such as system access; policies and procedures; expenditure and procurement approval processes; payroll controls in respect of master file changes; time recording; and excessive leave balances.

Internal audit

An effective internal audit function assures those responsible for governance that:

- appropriate internal controls exist and operate effectively
- risks are being managed
- operations are being run efficiently, economically and effectively.

An effective internal audit function will have a high percentage of its recommendations accepted by management and implemented within the recommended period. However, the acceptance of recommendations should not come unilaterally and there should be an exploration of the willingness of management to:

- assume the risk identified after consensus is reached with internal audit that a level of risk is acceptable
- propose an alternate solution which should be mutually agreed with internal audit.

The benefits of an internal audit report, regardless of quality, diminish over time where risks remain untreated. The time taken to act on internal audit recommendations can also be an indicator of the attitude of management to internal audit and their perceived value to the organisation.

Across the university sector in 2015, internal audit teams have identified 148 (2014: 94) outstanding high and moderate risk rated recommendations of which 40 (2014: 27) have been rated as high risk/priority. Two (2014: nine) of these high risk rated recommendations have been outstanding for longer than 12 months. This indicates that internal audit units across the sector have been active in recommending improvements to business practices and internal controls that were implemented by management. At one university, the internal audit unit is implementing significant changes to improve how it collates and monitors the implementation of internal audit recommendations.

The audit committee and the internal audit unit should work closely together to monitor and action internal audit issues in a timely manner. We have identified the following better practices all universities should consider:

- robust reporting to monitor the status of recommendations
- direct reporting and involvement of the vice-chancellor
- an ongoing assessment and consideration by both audit committees and management over the continued relevance of outstanding recommendations
- risk ratings that are appropriate for the level of impact on the organisation.

Massive open online courses

All universities offer the option of studying externally (distance learning) where course content is primarily delivered online. Students studying externally study the same curriculum, receive the same academic award, and generally pay the same course fees as students studying on campus. Few courses are delivered exclusively online, with students attending examinations or practical experience (where applicable) in person, either on campus or at regionally located examination centres.

In addition to the traditional on-campus and off-campus modes of study, there has been a growing international trend across the university sector in the delivery of open online courses or massive open online courses (MOOCs). MOOCs are courses aimed at large scale participation and open access via the internet. Currently, MOOCs are provided to students at no or little cost and do not result in an academic degree. MOOCs started to become popular overseas at institutes and universities in the United States and the United Kingdom from 2012. Over the past two years, Australia has been engaging in this new learning delivery channel with Queensland universities offering MOOCs from 2014.

All Queensland universities, except for the University of the Sunshine Coast, offered MOOCs during 2015. In total,42 courses were offered with total enrolments of 489 195 for the 2015 year. The University of Queensland is the most active in this work, currently offering 17 courses through their MOOC platform. It has registered more than 500 000 participants since releasing its first course in March 2014.

Most universities have arrangements to allow students to obtain academic credit toward their degree from past experience, including work experience and previous studies (which include MOOCs), reducing the number of subjects required to be completed at the university. Universities generally approve academic credit on a case-by-case basis, depending on the institution and the subject covered. UQ is also in discussions with the Australian National University (ANU) along with other international universities using the same MOOC platform on ways to enable their students who complete MOOCs offered by other universities to gain academic credit towards their degree.

All Queensland universities continue to monitor the progress, development and delivery of MOOCs globally and within Australia to assess any potential impact to their business including physical and IT infrastructure needs.

3. Area of controls focus: risk management

Overview

Managing risks is an essential part of the job for a public sector manager. The application of a structured and well-defined risk management framework helps deal with uncertainty. Managers who support well-managed risk-taking can maximise value for money in service delivery by identifying business opportunities and limiting the potential adverse consequences of risk on their organisation's objectives.

In 2013–14 we conducted a risk management review across 24 Queensland Government agencies from the general government sector (*Report 1: 2014-15 Results of audit: Internal control systems 2013–14*). We found that their risk management frameworks and their processes for identifying and assessing risks satisfied minimum requirements. However, there was no active reporting, monitoring or review of risks and risk treatments. Risk registers lacked substance and risk management was not integrated into strategic and operational planning.

This year, in addition to the mandatory financial audit review of risk management, we conducted an in-depth review of risk management practices in Queensland universities. The focus of this review on risk management was informed by our previous work in 2013–14 and on emerging risks we identified through environmental scanning. The purpose of the review was to assess whether universities were effectively managing risk to achieve their objectives.

Legislation and guidance

The *Financial Accountability Act 2009* requires all accountable officers to establish and maintain appropriate systems of risk management.

The Financial and Performance Management Standard 2009 prescribes that the entity's risk management system must provide for:

- mitigating the risk to the department or statutory body and the state from unacceptable costs or losses associated with the operations of the department or statutory body
- managing the risks that may affect the ability of the department or statutory body to continue to provide government services.

Queensland Treasury and the Department of the Premier and Cabinet have developed a reference for public sector agencies called *A Guide to Risk Management*. The guide gives an overview of the concepts of risk management and guidance on how Queensland public sector agencies can apply risk management processes. The guide also states that, while not mandated by legislation, it is expected that agencies will apply the Australian/New Zealand Standard ISO 31000:2009 Risk management—Principles and guidelines.

Our approach

As part of our annual planning for each financial audit, our auditing standards require us to:

- assess the effectiveness of each entity's risk assessment process
- examine each entity's risk registers to determine whether and how any risks identified could affect the risk of fraud or error in the financial statements.

For this review, we first developed a model to assess the maturity of risk management aspects of the internal control environment. The model was developed after extensive research into current developments in public and private sectors in Australia and overseas.

Our maturity model for assessing risk management is included at Appendix H. Our model outlines six attributes of risk management:

- leadership
- people and accountability
- process integration
- response
- monitoring
- achieving outcomes and innovation.

We conducted detailed reviews and fieldwork at four of the seven Queensland universities. These reviews included assessing their risk management framework, policies and procedures and underlying risk registers against the six key attributes of risk management within our risk management maturity model. As part of these reviews, we met with a sample of 'risk owners' and reviewed some of the risk treatments in detail. For the remaining three universities, we conducted a higher-level review of their risk management framework, policies and procedures, underlying risk registers and met with their risk managers.

We conducted a survey of the members of audit and risk committees at all seven universities. The survey obtained the views of risk committee members about the effectiveness of risk management within their university. The sector average responses to the survey are in Appendix I. We considered survey responses as part of each university's individual review.

Figure 3A below summarises the type of reviews completed across the sector.

Figure 3A
University reviews

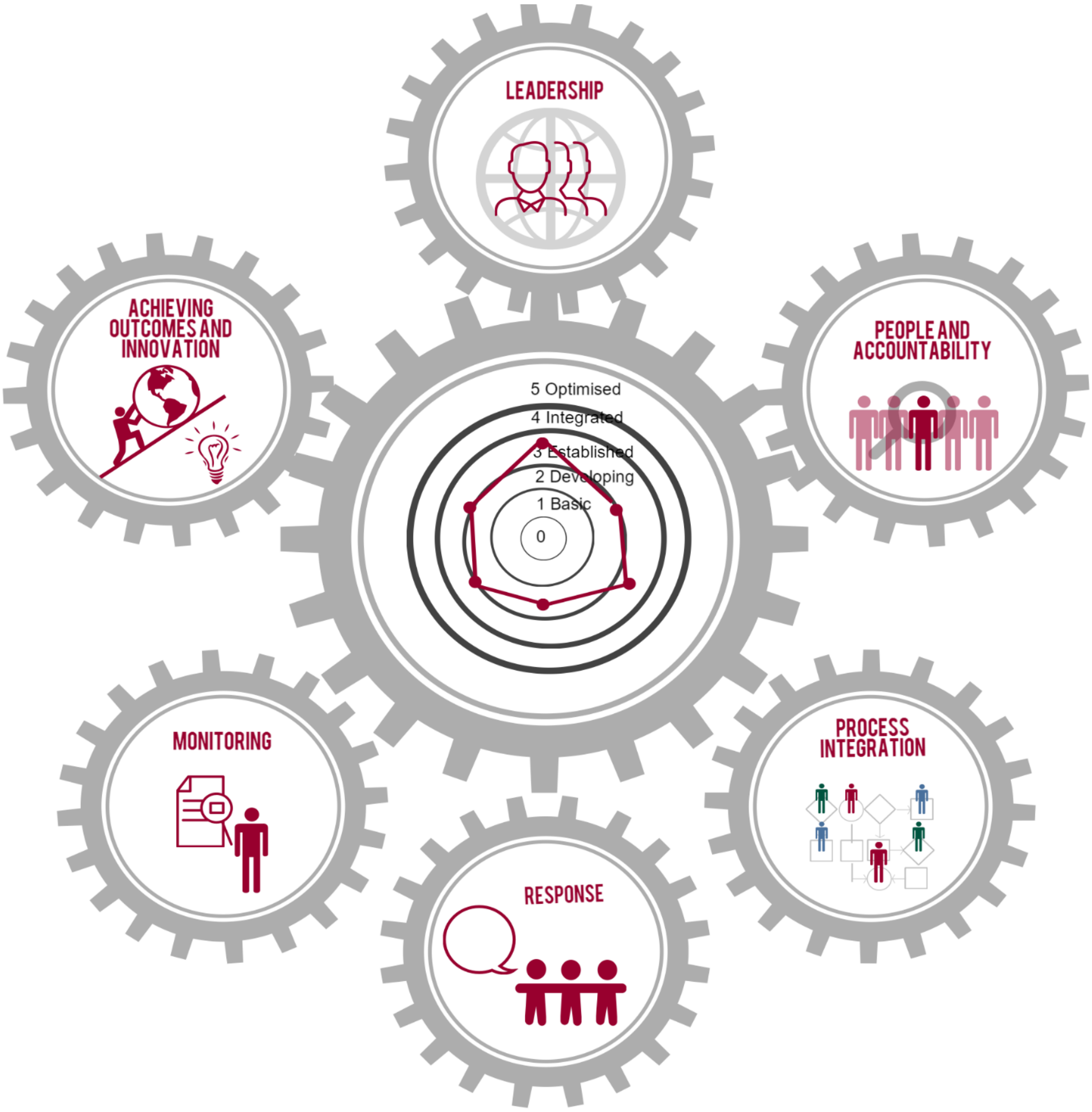
University	Audit performed
Griffith University	Detailed review
Queensland University of Technology	Detailed review
University of Sunshine Coast	Detailed review
University of Southern Queensland	Detailed review
Central Queensland University	Higher level review
James Cook University	Higher level review
University of Queensland	Higher level review

Source: Queensland Audit Office

Figure 3B provides the average sector scores across the six key risk management attributes within QAO's risk management maturity model. Scores were calculated from the in-depth reviews conducted at four universities; however, commentary provided against the attributes includes our assessments of all universities, both the detailed and high-level reviews.

We have included a summary of the suggested improvements for increased maturity we made across the sector. As this review was across seven universities of varying maturity, the findings and suggested improvements are not applicable to all universities.

Figure 3B
Sector average risk maturity scores



Source: Queensland Audit Office

Audit findings across the sector

For each of the six better practice attributes we have identified themes relating to universities' performance. A glossary of risk management terms is at Appendix J.

Leadership

Risk appetite and tolerance levels

Risk appetite is the amount of risk that the agency is prepared to accept or be exposed to at any point in time. Of the seven universities within the sector, only three had approved risk appetite statements and none had finalised risk tolerance levels. Some work on establishing tolerance levels had commenced at one university.

For the universities where risk appetite had been specified, in some instances we identified risks within the risk registers that had residual risk ratings higher than their stated risk appetite. These exceptions had not been identified as there were no mechanisms in place to monitor or report on exceptions. There was no evidence that the relationship to appetite had been considered in accepting residual risk ratings.

Two universities had not only articulated their overarching risk appetite, but also had individual risk appetite statements across the key areas of the university.

QAO guidance on risk appetite is included at Appendix I.

Management review

Across the sector, each university has an established risk committee that regularly discusses risk and reviews risk registers, reports and frameworks.

The review cycle of some universities' risk management frameworks exceeds the commonly accepted better practice of review every two to three years.

At some universities, risk is not a standing agenda item for its senior management meetings. While others not only have risk as a standing agenda item, they also receive and review regular reports, including risk heat maps, as well as presentations from risk owners. Management of these universities have committed resources and time to the regular meeting of risk champions or risk owners as part of risk forums.

Additional guidance on the use of risk champions and risk forums is included in Appendix I.

Risk and strategic planning

Risk assessments were not completed and considered as part of the strategic planning process at all universities. While attempts were made to link risks to the achievement of strategic objectives, there was no evidence that risks to the achievement of strategic objectives were specifically identified.

People and accountability

Staff training

Two universities offered no discrete risk management training for staff. Instead, reliance was placed on general risk management principles included in staff inductions and risk guidance material provided on intranets and within policy frameworks. For one university, the focus was only on the identification and management of workplace health and safety (WH&S) risks and for the other university training was on WH&S and fraud risk management, not overarching risk management.

The more mature universities not only provided staff with specialised risk training, but engaged staff from across their universities in risk workshops and dedicated time to focus on risk, for example, 'risk week'. The use of creative staff prompts to remind staff of the fundamentals of risk management in everyday operations also supported the ongoing training and awareness of employees.

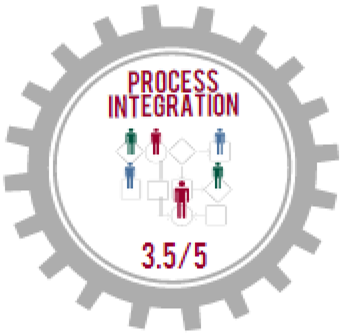
Accountability

All of the universities articulated roles and responsibilities for risk management in their risk management frameworks and supporting policies, but accountability for the discharging of these responsibilities was not included in duty statements and performance assessments of the relevant staff. No university had included responsibility for risk management in performance agreements and assessments.

In some instances, responsible risk officers were risk owners for risks that had mitigating controls listed that they would have no ability to influence or measure the effectiveness of. In these circumstances reliance is placed solely on internal audit reviews for the assessment of risk controls and mitigation strategies. No other measures or accountabilities were in place for monitoring the effectiveness of risks treatments.

Some universities ask risk owners to make regular presentations to senior management and risk committees on how strategic and operational risks are managed by the risk owner. These presentations help senior managers to see how risk is managed across the university, and give them an opportunity to challenge the application of risk management processes and treatments. These meetings hold individual risk owners accountable for risk management.

Process integration



Consistency

Each university has established risk management frameworks, including policies and procedures, but the extent to which these are applied consistently across each university differs. Some are inconsistent in how risk assessments and risk treatments are performed and recorded, particularly for operational risks.

In some universities, there is strong reporting and monitoring of risk assessment and risk management at the strategic level, but not much evidence of it in operational levels. Not all universities link risks to strategic and operational objectives. Even in those universities that do, not all objectives have risks linked to them; these universities consider risk in an ad hoc way as part of strategic and operational planning

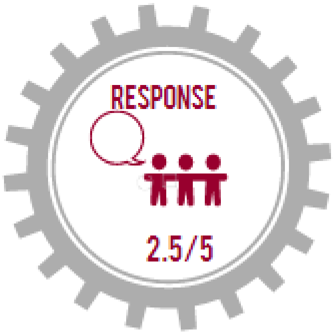
The use of planning and risk automated tools have given some universities a mechanism for guiding risk officers in the completion of risk assessments, while ensuring consistency in risk data presentation and capture.

We raised the use of risk forums as part of our review of leadership over risk management. The use of risk forums, or working groups with representation across the divisions and faculties as well as across the layers of management, demonstrates management's commitment to risk management activities. It also enables knowledge sharing and open discussion, leading to consistent application of risk management policies and practices.

QAO guidance on the use of champions and forums is included at Appendix I.

Response

Risk treatments



Assessments across the sector range from basic to integrated. Basic assessments apply to three universities that do not have risk plans; where risk information is limited to the risk register record; or where they only have treatments for some of their strategic and operational risks. An assessment of being established and integrated occurs when risk treatment plans are maintained. The level of detail recorded in these risk treatments varies across the sector. The deficiencies differed from university to university, but collectively they included:

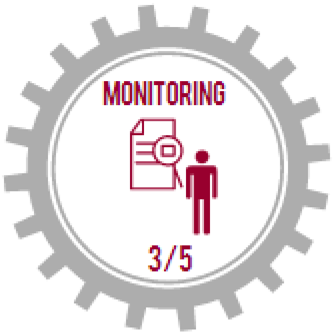
- no record of inherent risk ratings
- insufficient detail of risk triggers and controls
- no assessment of the acceptability of residual risk ratings to appetite
- no cost/benefit analysis performed
- no measures of treatment or control effectiveness or performance measures focused on achieving strategic objectives, nor the effectiveness of risk mitigation strategies
- no linkage to strategic objectives.

One university has introduced progress reporting by risk owners, where they assess the effectiveness of treatment plans, including costs and practicality. This practice demonstrates a mature risk response environment, where risk management is treated like any other management decision-making process. Effectiveness, cost and practicality are assessed in order to evaluate the likelihood of achieving the agency's objectives. This university intends to ensure this reporting is ongoing and not limited to annual review.

An example risk treatment plan checklist is included at Appendix I.

Monitoring

Level of reporting to senior management



All universities have a committee responsible for risk management. These committees all meet regularly throughout the year and review risk management information; however, the level of information provided to these committees varies across the sector.

For some universities, monitoring activities is limited to an annual review of risk registers. Survey responses received from some university risk committee members indicate that they find this information too detailed. Our review identified that these practices reflect a risk management environment where there is no formal risk reporting across senior management, and for some universities risk was not a standing agenda item for management meetings.

One university has identified indicators and performance measures; however, in most instances, these measures were yet to be incorporated into performance reporting across the university.

The universities we rated as established and integrated have established reporting and management discussion of risk across senior and operational management. The nature of these reports differs, but all enable senior managers to report to risk committees on risk management activities. The reporting is insightful and succinct, including the use of risk heat maps.

QAO examples of risk indicators are included at Appendix I.

Achieving outcomes and innovation

Opportunity assessments

Each university's risk management framework or governing risk policy outlines a commitment by management to support and encourage staff to take well-managed risks in order to seize opportunities. Some universities even articulate to staff that the greatest risk they face is to not identify and exploit these opportunities.

While this support is included in risk management frameworks and policies, some universities are unable to show how this translates into an active culture of well-managed risk taking. Their risk assessment processes remained focused on the identification and management of risks and are not used to drive innovation or identify opportunities.

The more mature universities in managing innovation actively assess their opportunities, as much as they assess risk. These universities were able to demonstrate how risk management was being used to identify and exploit opportunities across their universities. One university was able to provide examples where environmental scanning includes identifying opportunities available to the university. This intelligence then informs opportunity assessments.

Managing research risk

The university sector is a highly competitive industry and, to remain competitive and to attract and retain students, universities need to differentiate themselves from their competitors. Many opt to invest heavily in their research programs as a means to secure more funding and attract students.

In 2015, Queensland universities received $461 million in grant revenue, representing 9.27 per cent of total operating income.

With a limited number of government grants available to fund university research, there is increased pressure among researchers to compete for grant funding. The scarcity of grant funding increases the potential risk for research fraud, both in the grant application process and in the conduct of the research itself. To mitigate the risks and the potential adverse impacts research fraud may have on the organisation, particularly on its reputation, each university needs to embed effective control measures.

Research fraud or research misconduct can take many forms and may include:

- falsification — manipulating data or resources used in research
- fabrication — making up data to report as results
- plagiarism — using another person's research without giving appropriate credit or recognition.

Each of these can pose significant consequences for a university if it does not manage the risk effectively. It questions the integrity of the data, the validity of the results, and the skills of the researcher. It can also have more far-reaching impact as it jeopardises the reputation of the university and the results of past research projects.

Examples of research fraud in Australia have been reported recently, resulting in universities retracting research articles and returning grant funds to the funding bodies.

Through our area of controls focus review, we observed that Queensland universities are recognising research fraud as a risk in their risk registers and are implementing controls to mitigate this risk. Case study 1 (below) describes how one university has taken a considered approach to managing the risk.

Given the ongoing uncertainty relating to future university funding and the associated implications and pressures to continue to find revenue, we will continue to monitor how this risk is being addressed by Queensland universities.

Case study 1

Managing research risk
One of the universities we assessed in detail recognises research capacity and integrity as a risk category, and identifies its potential failure to continually improve its reputation for quality research as a corporate risk. Risk treatments focus on better engagements with industry and key international companies, as well as increased awareness for the importance of research integrity. While focusing on research conduct and quality, and research innovation in the one corporate risk, the university undertook an exercise to distinguish its appetite for both aspects of the risk. In response to a recent external review, the university established individual risk appetite statements for key activities across the university and mapped these on a Risk Appetite range to compare and contrast how the level of risk appetite can vary depending on the activity. By dividing the research risk into two distinct key activities, it was able to apply a different level of risk appetite for each activity. While taking a cautious approach towards conducting research, by separating out its appetite for research innovation, the university can take an opportunistic view and accept a higher level of risk for innovation while not letting it compromise the ethics, legality or quality of research undertaken. The university encapsulated the distinct approaches to research-related risk in its treatment plan, including treatment descriptions that mitigated against research fraud, and protecting its reputation, while also being careful not to stifle innovation. For example, treatments included building inter-disciplinary capacity, and strong relationships with industry, while also establishing an Office of Research Ethics and Integrity, and introducing education and training to better understand how to apply research integrity principles.

Audit and risk committee survey

As part of our review, we conducted a survey of audit and risk committee members across the university sector. The survey canvassed members' views as to the effectiveness of risk management within their university. We provided each university with the responses received from their members as well as general themes from across the sector. Responses to the survey are included at Appendix I and include the average scores and themes from the responses across the sector. Our audit did not include testing the accuracy of responses received.

4. Grammar schools

In brief

- The eight Queensland public grammar schools are:
  - Brisbane Grammar School (BGS)
  - Brisbane Girls Grammar School (BGGS)
  - Ipswich Grammar School (IGS)
  - Ipswich Girls' Grammar School (IGGS)
  - Rockhampton Grammar School (RGS)
  - Rockhampton Girls Grammar School (RGGS)
  - Townsville Grammar School (TVGS)
  - Toowoomba Grammar School (TWGS).
- Each grammar school provides facilities at secondary school level, and except for BGGS, all provide a limited number of primary school places. Some provide prep places.

Conclusions

- All financial statements were materially correct and complied with the relevant accounting standards.
- Schools' financial statement reporting was timely.
- The control environment across the schools appears to be improving, with fewer significant issues identified than in 2014.
- The quality of the draft financial statements provided to audit has improved.
- Financial performance of most grammar schools is sound; however, IGS and RGGS have recorded deficits in 2015 and need to monitor their revenue and expenditure policies.
- Employee expenses are stable when compared to total revenue across the schools.

Findings

- All eight grammar schools received unmodified audit opinions in 2015, as they did in 2014.
- All schools met the two-month legislated period for certifying financial statements, as they did in 2014.
- The number of significant control weaknesses reduced from nine (2014) to two (2015).
- The quality of the draft financial statements provided to audit has improved in the past three years. Changes totalling $9.11 million were made to three grammar school draft financial statements submitted to audit (2014: $4.99 million across seven grammar schools). While the total changes made to the financial statements have increased, only three schools needed adjustments to the draft financial statements before finalisation (2014: seven schools). Of these adjustments, one school recorded $8.4 and the other two schools' changes were not significant.
- IGS improved its financial performance in 2015 when compared to 2014, but it still recorded an operating deficit of $0.46 million for 2015 ($1.15 million deficit for 2014). From 2013, IGS's financial performance has continued to improve.
- RGGS recorded an operating deficit of $0.04 million in 2015. In 2014, RGGS recorded an operating surplus of $1.16 million.
- The total operating revenue of the grammar schools has increased by eight per cent and the main driver is the transition of year seven to secondary school in Queensland in 2015.
- The total expenditure for grammar schools increased by nine per cent, mainly due to increases in employee costs and other expenses to meet the additional costs for the year seven transition to high school.
- While employee expenses still represent over 60 per cent of total costs in most schools, the employee expense as a percentage of operating revenue has decreased in 2015 and 2014.

Grammar School sector

The grammar schools were created under the *Grammar Schools Act 1860*. The current *Grammar Schools Act 1975* replaced this Act.

Grammar schools operate on a fully commercial basis with some financial assistance provided by the state. They are statutory bodies and are subject to the requirements of the Grammar School Act and the *Statutory Bodies Financial Arrangements Act 1982*.

Conclusions

Most schools are financially sound and all received unmodified opinions in 2015, as they did in 2014 and 2013. The financial statements were prepared in accordance with the legal reporting requirements, including the Australian accounting standards.

The quality and timeliness of the financial statements were satisfactory, with all schools meeting the two-month legislated requirement for audit to certify their financial statements. The draft financial statements provided to audit were of an acceptable standard with only three schools making adjustments before the statements were finalised.

The internal control environment was generally sound, with some weaknesses identified and improvements recommended at six schools. The total number of significant issues raised across all schools reduced to two in 2015 (from nine in 2014).

IGS has shown continuous improvement in its operating results since 2013. The 2015 operating result at IGS was a $0.46 million deficit, an improvement of $0.69 million on 2014. IGS had net assets of $54.6 million at year end. The school should continue its efforts to improve its financial performance with close monitoring of revenue and expense policies.

RGGS recorded an operating deficit of $0.04 million for the year (2014 operating surplus was $1.16 million). RGGS is a small school with an equivalent full time student load (EFTSL) of 321 in 2015 (2014 the EFTSL was 331). The reduction of EFTSL for 2015 and additional expenses incurred in the process of appointing an acting principal, including the salary expense, as well as the damage caused by Cyclone Marcia in February 2015 all had an impact on the operating result. In 2014, the school also received a state capital grant of $0.6 million and did not receive a similar capital grant in 2015.

Reduced capital spending by BGS, IGS and IGGS, as identified by the capital replacement ratio five year average (Appendix D), may lead to increased capital expenditure requirements in the future.

Employee expenses appear to have stabilised for most schools over the past two years when considered as a percentage of total revenue (see Figure 4F).

Audit results

We have issued unqualified audit opinions to the financial reports of all eight grammar schools. Appendix B provides the dates that management and audit signed the financial statements and the type of audit opinions issued for the grammar schools.

Six of eight grammar schools provided draft financial statements for audit by their agreed milestones. The other two grammar schools provided the draft statements one week late, due to delays in finalising the land and building valuation reports. Management and audit certified financial reports for all eight grammar schools by their required legislative deadline.

At year-end, three grammar schools made changes to their draft financial statements affecting their operating result or net assets. The total value of adjustments to financial statements prior to audit certification in 2015 was $9.11 million as detailed in Figure 4A below.

The adjustments made this year mainly include TWGS's adjustments of $3.8 million to assets and equity that relate to late revaluation adjustments and other audit adjustments.

Overall, the financial statements process was satisfactory and contributed to meeting the statutory deadline for financial statement certification.

In addition to quantitative changes, six schools adjusted the disclosure notes. Overall, the adjustments were minimal and related to policy note changes including deletion of irrelevant policy notes, and changes to valuation, borrowings and superannuation disclosures.

Figure 4A
Changes to financial statements before audit certification*

Financial statement area	2012 $ m	2013 $ m	2014 $ m	2015 $ m
Income	0.28	1.65	0.01	0.00
Expenses	4.03	1.52	0.88	0.29
Assets	2.31	1.35	1.69	4.41
Liabilities	1.43	0.58	2.15	0.40
Equity	1.29	0.00	0.26	4.01
Total	**9.34**	**5.10**	**4.99**	**9.11**
Number of grammar schools that processed a change	5	4	7	3

* The extent of changes made within financial statements for each grammar school based on materiality to the financial statements.

Source: Queensland Audit Office

Key audit matters

Reduced disclosure for financial statements

Australian Accounting Standard 1053 *Application of Tiers of Australian Accounting Standards* applied to annual reporting periods beginning on or after 1 July 2013, and consists of two tiers of reporting requirements for preparing general purpose financial statements:

- Tier 1: Australian Accounting Standards
- Tier 2: Australian Accounting Standards — Reduced Disclosure Requirements (RDR).

Grammar schools have the option of applying Tier 2 reporting, which would reduce the amount of disclosure in the financial statements, while still complying with the legal reporting requirements. By preparing the financial reports under reduced disclosure requirements, the schools could simplify the financial statements and reduce the cost of financial reporting. Seven grammar schools prepared financial statements in compliance with the Australian Accounting Standards — Reduced Disclosure Requirements in 2015. The other school will apply RDR in 2016.

Valuation of property, plant and equipment

As at 31 December 2015, the net book value of property, plant and equipment for all schools was $597.4 million, an increase of $18.3 million (3.2 per cent) from the 31 December 2014 amount of $579.1 million.

Each year, schools assess the value of property, plant and equipment. This is one of the more subjective and complex assessments undertaken, because of the assumptions and estimates applied throughout the process. Valuations vary depending on the complexity of the valuation methodologies used. This is the case whether independent valuers or in-house experts performed the valuation, or assets were valued through application of a suitable index. Management's overall assessment of these valuations is crucial to ensuring the values disclosed in the financial statements are materially correct.

We reviewed the independent valuations and application of indices undertaken during 2015 for the schools' assets. We assessed whether the assumptions and estimates relating to these valuations (including impairment, residual values and useful life assessments) and depreciation calculations were in accordance with applicable accounting standards.

For 2015, across the sector, there has been an overall net increase in value of $8.8 million (in 2014 there was a net increase of $0.6 million) specifically due to valuation processes.

Financial performance and sustainability

The financial objective for grammar schools is to generate sufficient revenue to meet their financial obligations and to fund asset replacement and new asset acquisitions. The ability of grammar schools to achieve this depends on their management of expenditure and revenue.

The operating result — the difference between the revenue inflows and expenditure outflows, measures the schools' financial performances. Their financial position is measured by net assets — the difference between what they own (total assets) and what they owe (total liabilities).

The Queensland Department of Education and Training monitors the financial and business performance of grammar schools across Queensland.

We have referred to the department’s benchmarks as well as additional benchmarks to determine the sustainability of the grammar schools. We have selected financial ratios that are commonly used by analysts across Australian not-for-profit sectors to help us understand the short and long-term sustainability of the grammar schools.

We have calculated the ratios from information contained in the audited financial statements. The results of these ratios should be considered in conjunction with other factors such as management standards, financial budgets, asset replacement strategies, cash and investment balances, and capacity to generate revenue.

Results of the analysis of ratios for the eight grammar schools (refer Appendix D) indicate the following:

- Operating ratios calculated indicate that six out of eight grammar schools have adequate revenue to meet expenditure. IGS's ratio is below zero, but shows improvement when comparing the 2015 operating ratio to the five-year average. IGS will need to continue to monitor its future income and expenditure policies and implement strategies to ensure its long-term sustainability. We have noted that in the last three years the operating ratio of IGS has improved when compared to the previous year. The RGGS operating ratio dropped significantly in 2015 to below zero. RGGS’s negative ratio is due to recording an operating deficit of $0.04 million for 2015. This operating deficit is partly due to the additional principal costs of $0.2 million incurred in 2015. These costs included acting principal salary, recruitment, legal and consultancy fees.

- Current ratio shows that all grammar schools have adequate liquidity to meet their short-term liabilities as they fall due. IGS and RGS had current ratios close to one and need to monitor their liquidity position closely to ensure that their current liabilities do not exceed current assets. IGS and IGGS current ratios have improved when compared with 2014 and are now more than one. RGGS and RGS showed a downward movement and the ratio has moved closer to one.
- Net financial liabilities ratio calculated by comparing the total liabilities less current assets to total revenue indicates whether the schools are carrying excess debt levels. IGGS is still above the benchmark of 60 per cent in 2015 but has been improving over the last five years. IGGS has honoured its debt commitments for 2015 and reduced overall borrowings by $2 million. IGGS borrowed funds to meet significant capital expenditure undertaken in 2008 and 2009.
- Debt to revenue ratio calculated by comparing total borrowings at year-end to revenue generated shows that all grammar schools had a ratio of less than 100 per cent in 2015 which is acceptable. Schools need to ensure that they generate enough revenue to meet their debt, expenditure and investment obligations. A low ratio indicates that schools have capacity to meet these obligations as they fall due.
- Capital replacement ratio calculated based on comparing capital expenditure with depreciation shows that BGS, IGS and IGGS spent less on capital replacement than the annual depreciation expense on average for the last five years. This could lead to higher replacement or maintenance costs in the future.

Operating results for the sector

Six of the eight grammar schools had a positive operating result for 2015. In total, the grammar schools achieved an operating result in 2015 of $16.5 million (2014: $18.1 million), which represented a nine per cent decrease. Five schools recorded reduced operating results from 2014. Of these, four maintained positive results while RGGS recorded a negative result (deficit) of $0.04 million.

The total income from continuing operations has increased by $19.8 million. Increases in fee revenue of $13.1 million and other revenue of $7.0 million explain this. Six schools showed increased fee revenue while two schools (IGS and RGGS) showed decreased fee revenue. In 2015, year seven became part of secondary schools and the fee revenue for grammar schools increased due to this. Additionally there were annual fee increases across all schools. In some schools, decreased student numbers offset these increases. Other revenue increases related mainly to three schools. Of these, two received $4.7 million as insurance payments for storm damages. Other increases related to revenue from study tours and more extra-curricular activities offered as a fee for service.

Total expenditure increased by $21.4 million. This was attributed mainly to employee related expenses $8.5 million, supplies and services $8.7 million and other expenses $2.2 million. Employee expenses increased in six schools, mainly due to meeting the requirements of year seven moving to secondary school.

The supplies and services expense for 2015 has increased by 16.5 per cent to $61.4 million.(2014: $52.7 million) This $8.7 million increase is due mainly to increases in supplies and services at: BGS $5.8 million, RGS $1.4 million and TWGS $1.0 million. BGS had increased costs due to year seven moving to high school and repairs for storm damage amounting to $4.1million. RGS had higher repairs and maintenance costs ($0.5 million) due to storm damages as did RGGS. The increase at TWGS is due to higher repairs and maintenance undertaken during the year.

Of the increase in other expenses, BGGS accounted for $0.9 million, which included a $0.3 million loss on disposal of property, plant and equipment.

Figure 4B shows the 2015 operating results of the grammar schools.

Figure 4B
Operating results

	BGS	BGGS	IGS	IGGS	RGS	RGGS	TVGS	TWGS
2015 Operating result ($'000)	4 239	2 566	-464	1 270	2 939	-38	2 168	3 800

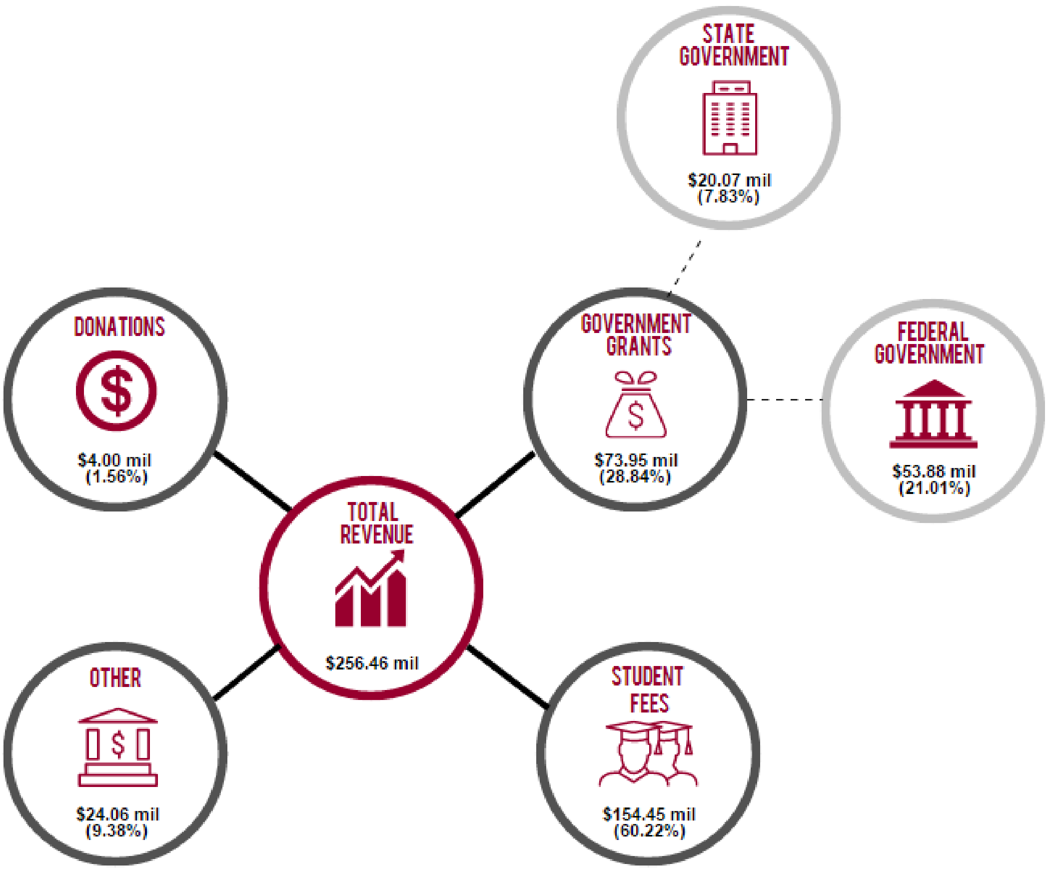
Source: Queensland Audit Office

Operating income

Figure 4C shows the composition of operating income for the year. Total operating revenue has increased from 2014 by eight per cent.

Overall, the components of operating income have not significantly shifted over the past five years, as no significant change has affected the sector. Student fees continue to contribute approximately 60 per cent of operating income while approximately 30 per cent comes through government grants.

Figure 4C
Total revenue 2015

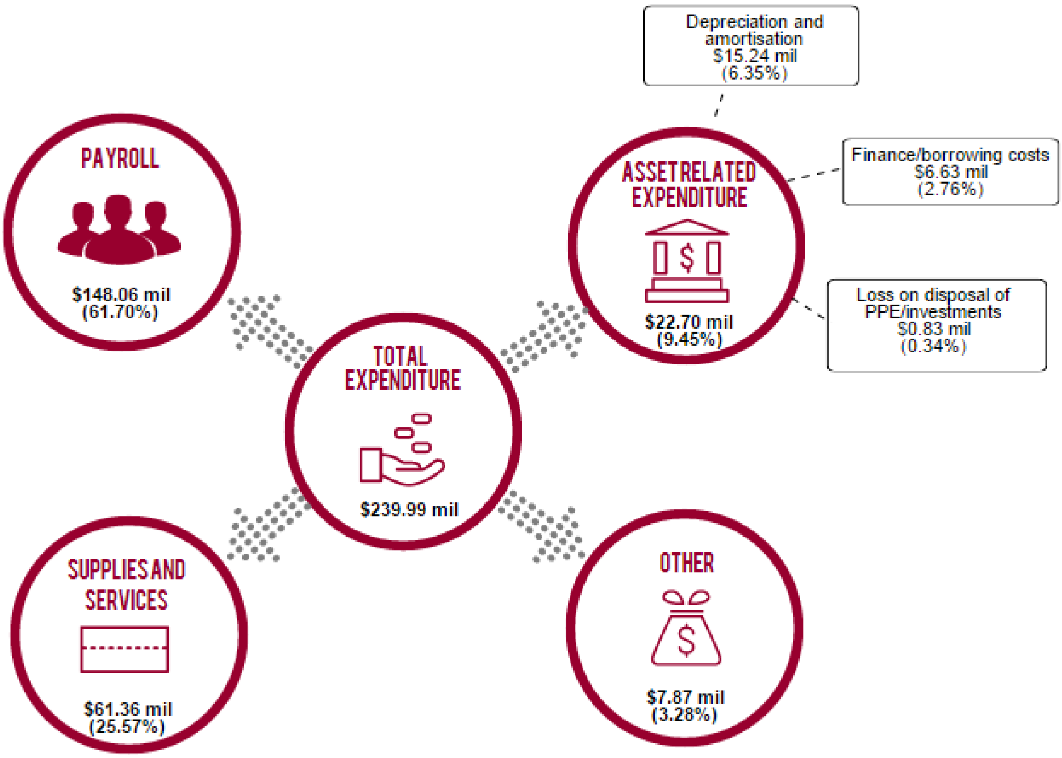


Source: Queensland Audit Office

Operating expenditure

Figure 4D shows the operating expenditure components. The percentages of major operating expenditure components are employee related expenses, supplies and services, depreciation, amortisation, finance, and borrowing costs. The percentages of these components to total operating expenditure has not changed significantly in the past five years.

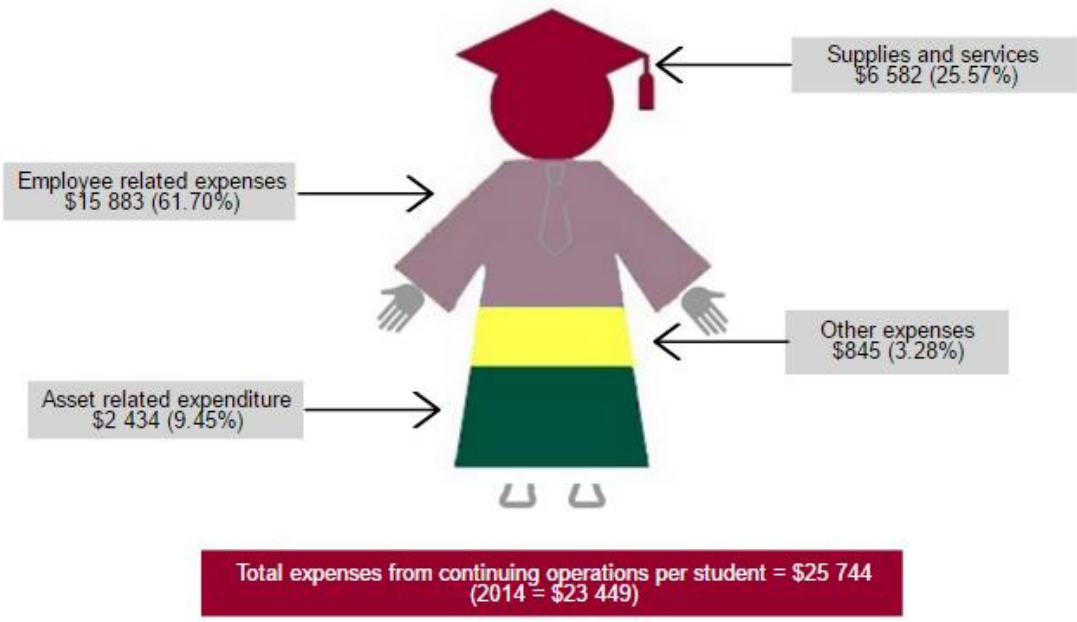
Figure 4D
Total expenditure 2015



Source: Queensland Audit Office

By dividing the total operating expenses for the grammar school sector by the Equivalent Full Time Student Load (EFTSL), cost per student for the sector is calculated. While this is a high-level benchmark, relevant cost drivers should be identified at a lower level e.g. course/school level to assist in managing the schools financial operations effectively. See Figure 4E below.

Figure 4E
Cost per student



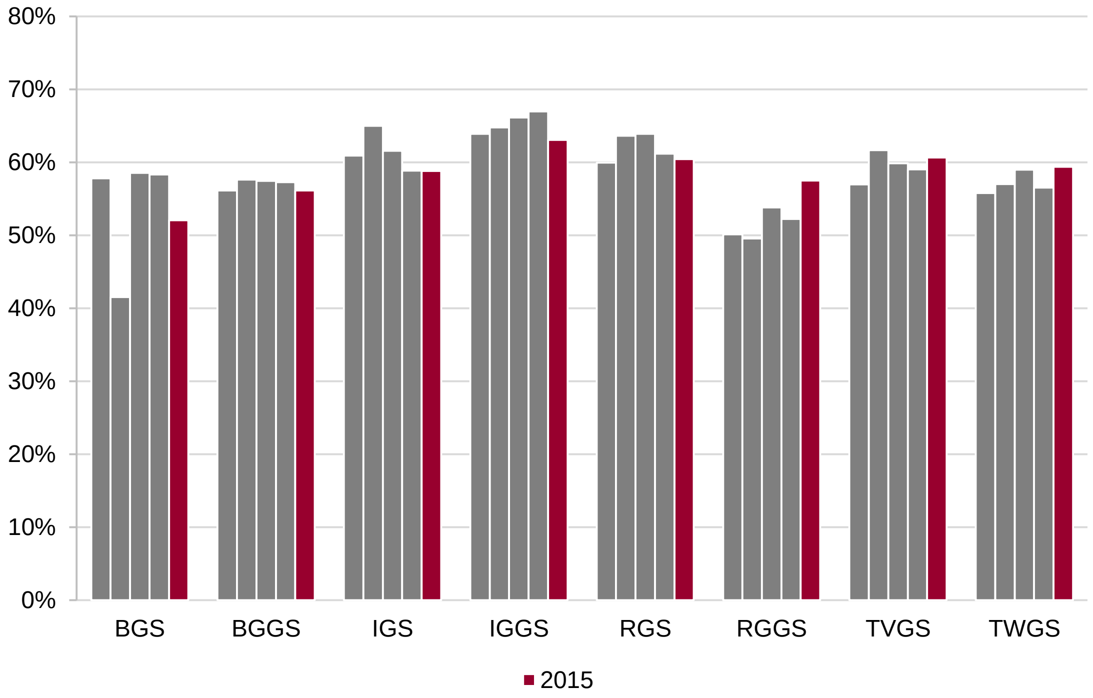
Source: Queensland Audit Office

Employee expenditure

The most significant expense incurred by the grammar schools has consistently been employee expenses. Employee expenses for 2015 increased by 6.1 per cent to $148.1 million (in 2014 it was $139.6 million), driven mainly by a 5.9 per cent increase in full time equivalent employees (FTEs) and agreed salary increases across the sector ranging from 2.4 to 4.2 per cent.

Figure 4F shows employee expenses as a percentage of total revenue. A large percentage of operating revenue used for employee expenditure may indicate that the school has less revenue available to meet its obligations. The university sector considers a benchmark between 50 to 70 per cent to be acceptable. All schools were within this acceptable benchmark.

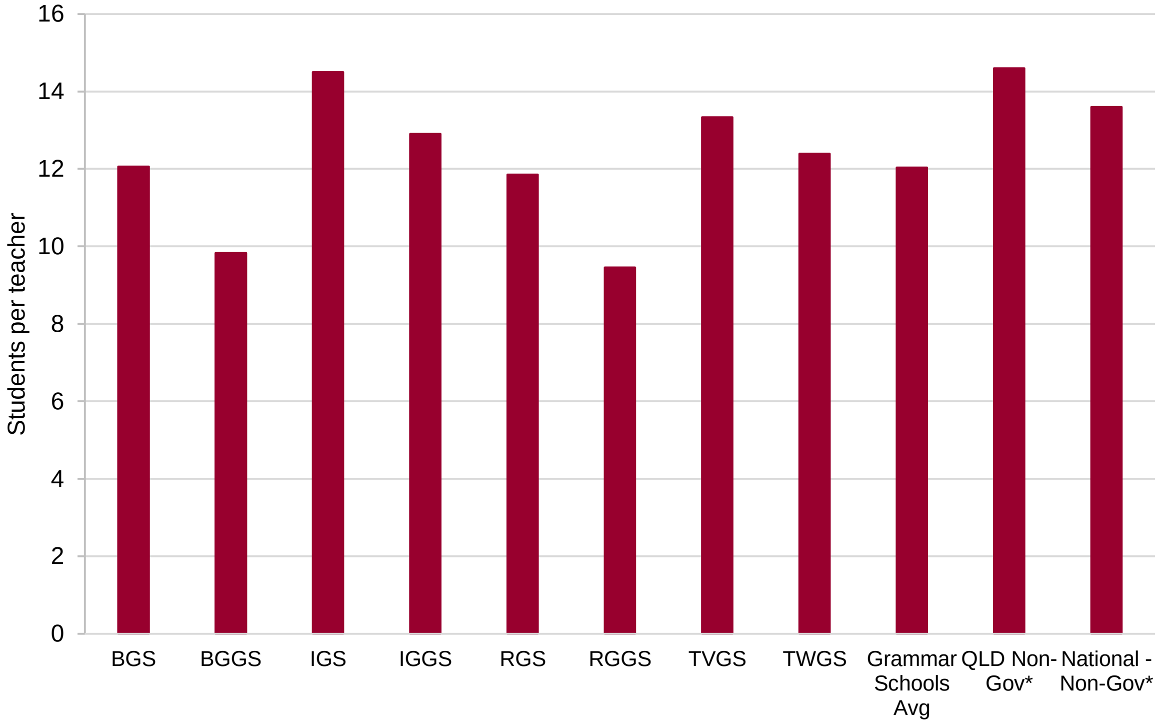
Figure 4F
Employee expenses and on-costs as a percentage of total revenue 2011–2015



Source: Queensland Audit Office

Figure 4G shows the EFTSL/Staff Full time Equivalent (FTE) ratio for Grammar schools, and Queensland and national non-government schools for 2014. Monitoring the proportion of teachers to students assists schools to achieve optimal outputs. Most grammar schools had a lower student per teacher ratio when compared with the Queensland and national non-government sector averages. IGS's ratio of 14.5 was the highest and is comparable to the Queensland non-government and national non-government ratios of 14.6 and 13.6 respectively.

Figure 4G
Student EFTSL/staff FTE ratio 2014



Source: Australian Bureau of Statistics and Queensland Audit Office

Finance cost per student

Figure 4H shows that the average finance cost per student across Queensland grammar schools is just above $700. Finance costs include mainly the annual interest payments for borrowings. Increased borrowings would result in higher finance costs that would affect the schools operating results. IGGS and BGGS have the highest finance cost per student as at the end of 2015 at over $1 200 and $1 000 per student respectively.

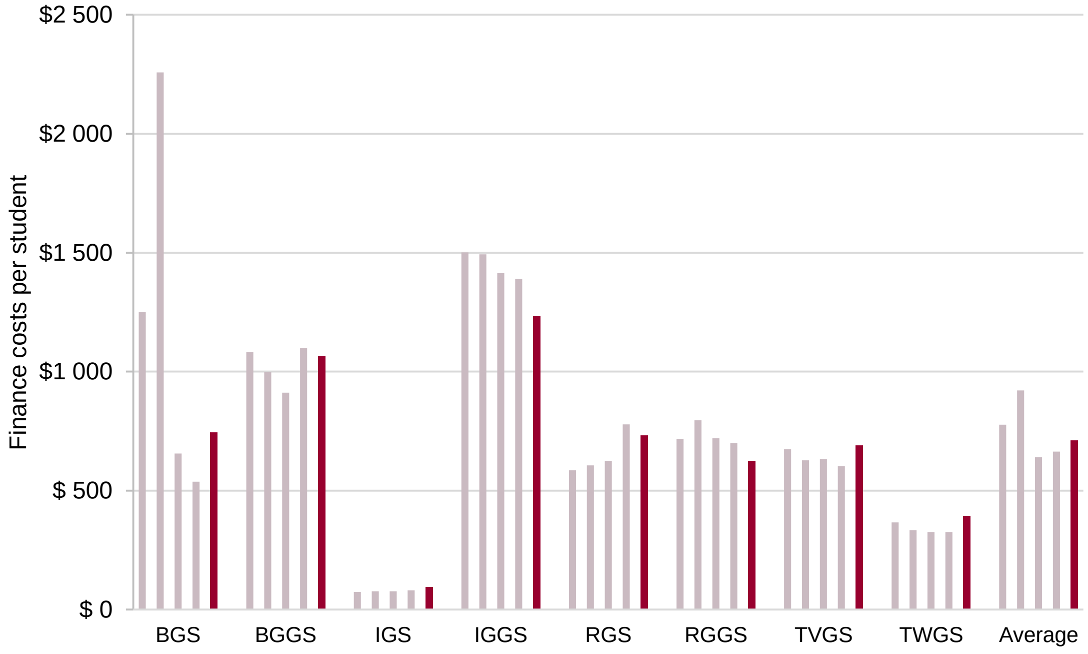
IGGS's finance costs, amounting to $1.2 million, were 5.7 per cent of total operating expenditure while the average for all grammar schools was 2.8 percent. IGGS borrowed $20.8 million in 2008 and 2009 to construct new buildings and in 2015 the balance outstanding was $18.8 million. This high loan balance has contributed to the higher finance cost.

BGGS's finance costs, amounting to $1.4 million, were 3.7 percent of total operating expenditure and additional borrowings in 2014 of $13.5 million have increased the finance cost per student in 2014 and 2015.

BGS shows increased finance costs per student in 2012 and 2015, while its total borrowings were reducing annually from 2012. In 2012 and 2015, BGS reduced its loan balances by more than its minimum annual payment requirement. In 2012, the loan payment requirement was $2.9 million but BGS paid $12.6 million. In 2015, the annual payment requirement was $2.3 million and BGS paid $4.7 million. In 2015 because of accelerated loan payments, BGS paid an additional $0.5 million as a market realisation charge to the lender and was included in the finance costs. Similarly, in 2012, BGS incurred additional finance costs for accelerating its loan repayments.

IGS has no borrowings and has minimal finance costs relating to lease liabilities.

Figure 4H
Finance costs per student



Source: Queensland Audit Office

Controls over financial reporting

Grammar schools must maintain good internal control processes to assure their boards of trustees that they have effective business and financial operations and reliable financial reporting.

In 2015, the classification of audit issues changed from *high*, *moderate* and *low risk* and *business improvement opportunity* to *material deficiency*, *significant deficiency*, *deficiency*, and *other matters* to better align with the auditing standards. Material deficiency and significant deficiency are the equivalent to the old high and moderate risk issues. There were two significant deficiency issues raised in 2015, compared with nine high and moderate risk issues in 2014.

IT data back up and retention processes, and policies and procedures relating to awarding scholarships and bursaries in a grammar school were the two significant issues reported.

In addition, we have reported 16 deficiency and other matter issues that included the following:

- no supporting documents including employee contracts, tender evaluations and details of persons making changes to master data (such as vendor details)
- inadequate segregation of duties. One person can raise and approve purchase orders
- access to post journals not restricted
- payment processes not followed
- asset register not agreed to the general ledger balances.

Grammar schools need to continue to monitor their control environments closely to prevent control breakdowns.

Appendices

Appendix A—Comments

In accordance with s.64 of the *Auditor-General Act 2009*, a copy of this report was provided to the Premier, the Director-General of the Department of the Premier and Cabinet, the Minister for Education and the Director-General of the Department of Education and Training as well as all universities and grammar schools named in this report, with a request for comment.

Views expressed by relevant parties during the preparation of this report have been considered in reaching our audit conclusions and are represented to the extent relevant and warranted.

Comments received from Director-General, Department of Education and Training

RECEIVED
20 MAY 2016
QUEENSLAND AUDIT OFFICE

Queensland Government

Office of the
Director-General

Department of
Education and Training

18 MAY 2016

Mr Andrew Greaves
Auditor-General
Queensland Audit Office
PO Box 15396
CITY EAST QLD 4002

Dear Mr Greaves

Thank you for your letter dated 28 April 2016 providing a draft report on the results of the 2015 education sector audits.

I appreciate the opportunity to review the report and thank you and your team led by Mr John Welsh for your collaborative approach.

Should your officers wish to discuss this matter further, I invite them to contact Mr Adam Black, Assistant Director-General and Chief Financial Officer, Department of Education and Training, on telephone 3513 6601.

Yours sincerely

DR JIM WATTERSTON
Director-General

Ref: 16/197499
Your ref: 11477

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Appendix B—Status of financial statements

Figure B1 — Status of financial statements

Entity type	Unfinished audits	Unmodified opinions issued	Unmodified but with an emphasis of matter	Total
Universities and controlled entities	—	13	9	22
Grammar schools	—	8	—	8
Other statutory bodies	—	1	—	1
Jointly controlled entities	—	2	2	4
Audited by arrangement	—	—	1	1
Total	**—**	**24**	**12**	**36**

Source: Queensland Audit Office

Figure B2 — Status of financial statements

Audit	Date statements signed	Date opinion issued	Opinion	Timeliness (since 31 December)		
				<2 mths	2–3 mths	>3 mths
Universities and their controlled entities						
Central Queensland University	22.02.16	23.02.16	U	✓		
▪ Australian International Campuses Pty Ltd	22.02.16	23.02.16	U	✓		
▪ Australian International Campuses Trust	22.02.16	23.02.16	U	✓		
▪ C Management Services Pty Ltd	19.02.16	23.02.16	U	✓		
▪ CQU Travel Centre Pty Ltd	19.02.16	23.02.16	U	✓		
▪ Health Train Education Services Pty Ltd	19.02.16	23.02.16	U	✓		
Griffith University	24.02.16	25.02.16	U	✓		
▪ Gold Coast Innovation Centre Limited	31.03.16	07.04.16	E			✓
James Cook University	26.02.16	29.02.16	U	✓		
Queensland University of Technology	26.02.16	26.02.16	U	✓		
▪ Creative Industries Precinct Pty Ltd	16.02.16	18.02.16	E	✓		
▪ QUT Enterprise Holdings Trust	15.02.16	18.02.16	E	✓		

Audit	Date statements signed	Date opinion issued	Opinion	Timeliness (since 31 December)		
				<2 mths	2–3 mths	>3 mths
▪ QUTbluebox Pty Ltd	16.02.16	16.02.16	E	✓		
▪ QUTbluebox Trust	16.02.16	16.02.16	E	✓		
The University of Queensland	25.02.16	27.02.16	U	✓		
▪ University of Queensland Foundation Trust	19.02.16	24.02.16	E	✓		
▪ UQH Finance Pty Ltd	19.02.16	24.02.16	E	✓		
▪ UQ Holdings Pty Ltd	19.02.16	24.02.16	U	✓		
▪ UQ Investment Trust	19.02.16	24.02.16	E	✓		
University of Southern Queensland	22.02.16	23.02.16	U	✓		
University of the Sunshine Coast	23.02.16	25.02.16	U	✓		
▪ Innovation Centre Sunshine Coast Pty Ltd	15.02.16	19.02.16	E	✓		
Grammar schools						
Board of Trustees of the Brisbane Girls' Grammar School	22.02.16	24.02.16	U	✓		
Board of Trustees of the Brisbane Grammar School	25.02.16	25.02.16	U	✓		
Board of Trustees of the Ipswich Girls' Grammar School	25.02.16	29.02.16	U	✓		
Board of Trustees of the Ipswich Grammar School	23.02.16	24.02.16	U	✓		
Board of Trustees of the Rockhampton Girls' Grammar School	25.02.16	29.02.16	U	✓		
Board of Trustees of the Rockhampton Grammar School	24.02.16	29.02.16	U	✓		
Board of Trustees of the Toowoomba Grammar School	25.02.16	29.02.16	U	✓		
Board of Trustees of the Townsville Grammar School	23.02.16	26.02.16	U	✓		
Statutory body						
Queensland College of Teachers	19.02.16	24.02.16	U	✓		

Audit	Date statements signed	Date opinion issued	Opinion	Timeliness (since 31 December)		
				<2 mths	2–3 mths	>3 mths
Jointly controlled entities						
International WaterCentre Joint Venture	18.03.16	23.03.16	U		✓	
Queensland College of Wine Tourism	25.02.16	26.02.16	E	✓		
Queensland Cyber Infrastructure Foundation Ltd	29.03.16	31.03.16	U		✓	
The Grammar Schools of Queensland Association Inc.	02.02.16	12.02.16	E	✓		
Audited by arrangement						
Translational Research Institute Trust	18.03.16	21.03.16	E		✓	

* An emphasis of matter was issued to alert users of the financial statements to the fact that special purpose financial statements had been prepared.

Opinion key: U = unqualified Q = qualified A = adverse E = unqualified with emphasis of matter D = disclaimer

Source: Queensland Audit Office

Appendix C—Entities for which audit opinions will not be issued

Figure C1

Entity	Controlled by	Reason
Applied Resource Economics Pty Ltd	The University of Queensland	Dormant
Ausonex Pty Ltd (deregistered 30 September 2015)	The University of Queensland	No separate financial statements
Bilexys Pty Ltd (deregistered 7 January 2015)	The University of Queensland	No separate financial statements
Brisbane Business School Pty Ltd	Queensland University of Technology	Dormant
CCA Therapeutics Pty Ltd	The University of Queensland	Dormant
Ceramipore Pty Ltd (deregistered 14 January 2015	The University of Queensland	No separate financial statements
CQU Institute of Higher Learning Pte Ltd	Central Queensland University	Dormant
Cloevis Pty Ltd	The University of Queensland	No separate financial statements
Cyclagen Pty Ltd	The University of Queensland	Dormant
Dendright Pty Ltd	The University of Queensland	No separate financial statements
GeneCo Pty Ltd (deregistered 13 January 2016)	Queensland University of Technology	Dormant
Global Change Institute Pty Ltd	The University of Queensland	Dormant
IMBcom Asset Management Company Pty Ltd	The University of Queensland	Dormant
IMBcom Asset Trust	The University of Queensland	No separate financial statements
IMBcom Pty Ltd	The University of Queensland	No separate financial statements
International WaterCentre Pty Ltd	The University of Queensland and Griffith University	Dormant
James Cook Holdings Pte Ltd	James Cook University	Exempt audit

Entity	Controlled by	Reason
James Cook Australia Institute of Higher Learning Pte Ltd	James Cook University	Exempt audit
JCU CPB Pty Ltd	James Cook University	Dormant
JCU Early Learnings Centres Pty Ltd	James Cook University	No separate financial statements
JCU Enterprises Pty Ltd	James Cook University	No separate financial statements
JCU Health Pty Ltd	James Cook University	No separate financial statements
JCU Univet Pty Ltd	James Cook University	No separate financial statements
JCU Pathways Pty Ltd	James Cook University	No separate financial statements
JK Africa Mining Solutions Pty Ltd	The University of Queensland	No separate financial statements
JKTech Pty Ltd	The University of Queensland	No separate financial statements
JKTech South America Spa	The University of Queensland	No separate financial statements
Kalthera Pty Ltd	The University of Queensland	Dormant
Leximancer Pty Ltd	The University of Queensland	No separate financial statements
Lucia Publishing Systems Pty Ltd	The University of Queensland	Dormant
Mask-Ed International Pty Ltd	Central Queensland University	Dormant
Metallotek Pty Ltd	The University of Queensland	No separate financial statements
Neo-Rehab Pty Ltd	The University of Queensland	No separate financial statements
North Queensland Commercialisation Company Pty Ltd	James Cook University	Dormant
Pepfactants Pty Ltd	The University of Queensland	No separate financial statements
QUT Enterprise Holdings Pty Ltd	Queensland University of Technology	No separate financial statements
Rapisure Pty Ltd (deregistered 15 July 2015)	The University of Queensland	No separate financial statements

Entity	Controlled by	Reason
Sarv Pty Ltd (deregistered 13 May 2015)	The University of Queensland	No separate financial statements
Snoresounds Pty Ltd (deregistered 14 January 2015)	The University of Queensland	No separate financial statements
SUSOP Pty Ltd	The University of Queensland	No separate financial statements
Symbiosis Pty Ltd	The University of Queensland	No separate financial statements
Tropical Queensland Centre for Oral Health Pty Ltd	James Cook University	No separate financial statements
UATC Pty Ltd (Deregistered 17 June 2015)	The University of Queensland	Dormant
UniQuest Pty Limited	The University of Queensland	No separate financial statements
UQ College Limited	The University of Queensland	No separate financial statements
UQ Health Care Limited	The University of Queensland	No separate financial statements
UQ Jakarta Office Pty Ltd	The University of Queensland	Dormant
UQ Sport Ltd	The University of Queensland	No separate financial statements
University of Southern QLD (South Africa) Pty	University of Southern Queensland	Dormant
UTASAT Pty Ltd (deregistered 25 January 2015)	The University of Queensland	Dormant
UTSAT Pty Ltd (deregistered 7 September 2015)	The University of Queensland	Dormant
UWAT Pty Ltd	The University of Queensland	Dormant

Source: Queensland Audit Office

Appendix D—Financial information

Figure D1
Universities and Grammar Schools
Operating results before income tax (consolidated)

Entity	2011 $ m	2012 $ m	2013 $ m	2014 $ m	2015 $ m	Five-year average $ m
Universities						
University of Queensland	192.78	58.18	108.11	42.77	58.57	92.08
Queensland University of Technology	63.84	100.66	56.32	33.58	33.77	57.64
Griffith	90.03	87.04	73.44	54.53	50.89	71.18
Southern Queensland	14.52	38.09	27.22	47.53	81.61	41.79
James Cook	44.40	37.99	18.94	62.85	26.40	38.12
Central Queensland	-2.97	-26.46	24.54	149.70	14.60	31.88
University of the Sunshine Coast	8.59	25.36	20.45	38.58	15.14	21.62
Grammar Schools						
Brisbane Grammar School	-0.04	16.28	1.97	2.83	4.24	5.06
Brisbane Girls Grammar School	2.95	1.69	2.77	2.85	2.57	2.57
Ipswich Grammar School	-2.21	-2.38	-1.49	-1.15	-0.46	-1.63
Ipswich Girls Grammar School	-1.55	0.04	0.17	0.36	1.27	0.06
Rockhampton Grammar School	1.41	0.15	1.21	3.45	2.94	1.83
Rockhampton Girls Grammar School	0.34	0.80	0.65	1.16	-0.04	0.58
Townsville Grammar School	3.76	2.80	2.42	2.66	2.17	2.63
Toowoomba Grammar School	2.87	2.02	3.51	5.92	3.80	3.62

* Prior year amounts may have been adjusted due to changes identified in individual university financial statements.

Source: Queensland Audit Office

Figure D2 — 2015 Financial data (consolidated) and ratios (parent)

Entity	Revenue $'000	Operating result before tax $'000	Total Assets $'000	Borrowings $'000	Operating result ratio		Current ratio		Net financial liabilities ratio		Debt to revenue ratio		Capital replacement ratio	
					2015	5 yr avg	2015	5 yr avg	2015 %	5 yr avg %	2015 %	5 yr avg %	2015	5 yr avg
University														
UQ	1 736 591	58 572	3 434 044	120 836	2.08	5.62	1.94	1.91	3.35	4.13	0.00	4.33	0.70	1.52
QUT	951 689	33 767	1 682 072	73 141	3.53	6.69	4.76	4.20	-22.19	-20.95	7.65	7.98	1.04	1.75
GU	881 151	50 887	2 146 641	142 443	5.78	8.79	4.33	3.50	-26.24	-21.56	16.17	10.71	1.08	3.49
USQ	369 675	81 608	626 067	9 191	22.08	13.58	4.02	4.17	-20.31	-21.95	2.49	4.96	3.30	3.50
JCU	524 645	26 402	1 103 957	84 807	6.17	7.43	4.08	3.55	-25.07	-12.48	16.45	14.29	0.89	1.50
CQU	359 129	14 599	704 455	2 911	3.79	7.08	2.13	2.11	-6.49	-5.25	0.81	0.29	2.86	1.68
USC	216 400	15 135	378 280	10 626	7.02	11.77	3.24	4.07	-11.94	-16.92	4.92	8.55	4.60	2.96
Qld Sector*	N/A	N/A	N/A	N/A	5.23	7.69	3.32	3.02	-12.68	-10.06	6.38	7.10	1.19	1.92
National*	N/A	N/A	N/A	N/A	6.80	7.56	1.61	1.65	40.65	36.71	12.35	11.12	1.79	2.22
Regional*	N/A	N/A	N/A	N/A	10.63	8.35	2.00	2.08	33.62	31.47	8.57	7.57	1.78	2.20
Metro (excl. Go8)*	N/A	N/A	N/A	N/A	5.07	6.01	1.92	1.62	24.74	20.28	11.60	9.13	1.76	1.97
Go8*	N/A	N/A	N/A	N/A	6.93	7.31	1.15	1.18	51.71	46.92	12.09	11.19	1.53	1.96

Entity	Revenue $'000	Operating result before tax $'000	Total Assets $'000	Borrowings $'000	Operating result ratio		Current ratio		Net financial liabilities ratio		Debt to revenue ratio		Capital replacement ratio	
					2015	5 yr avg	2015	5 yr avg	2015 %	5 yr avg %	2015 %	5 yr avg %	2015	5 yr avg
Grammar Schools														
BGS	56 930	4 239	147 499	5 704	7.45	9.42	1.52	1.54	4.50	23.99	10.02	23.93	0.72	0.91
BGGS	41 492	2 566	112 873	26 228	6.18	7.50	2.57	3.54	35.91	25.54	63.21	62.20	1.47	2.53
IGS	23 406	-464	59 160	955	-1.98	-7.11	1.07	0.64	9.43	14.80	4.08	7.60	0.34	0.32
IGGS	21 774	1 270	62 486	18 792	5.83	0.04	1.43	0.75	87.62	106.88	86.30	104.19	0.78	0.51
RGS	38 209	2 939	82 310	16 566	7.69	5.40	1.08	1.61	43.88	42.67	43.35	51.76	2.59	3.08
RGGS	10 108	-38	31 926	3 744	-0.37	5.97	1.11	1.64	36.41	34.26	37.04	41.31	1.33	1.84
TVGS	30 653	2 168	73 907	19 008	7.07	9.16	4.97	3.12	23.92	31.61	62.01	51.92	1.14	2.49
TWGS	33 896	3 800	108 581	11 543	11.21	11.87	8.40	7.41	-15.81	-19.44	34.05	25.41	4.80	2.60
Qld Avg.	N/A	N/A	N/A	N/A	6.43	6.43	2.56	2.31	23.85	28.40	39.98	43.60	1.70	1.79

* National Averages are 2014, 5 Year Average is for the 2010 to 2014 period. (National 2015 numbers not available)

Operating result ratio measures the percentage of operating result to operating revenue, a ratio above zero is deemed satisfactory. Interest expense is included.

Current ratio is the relationship between current assets and current liabilities, a ratio of greater than one is acceptable. Current liabilities only includes provisions expected to be settled within the next 12 months.

Net financial liabilities ratio is used to compare the total liabilities less current assets to revenue. A percentage under 60 percentage is considered a reasonable benchmark.

Debt to revenue ratio compares all current and non-current borrowings to total operating revenue and income - this provides an indicator of the affordability and sustainability of debt levels. A lower percentage indicates a greater ability to repay debt.

Capital replacement ratio indicates whether universities are replacing their property plant and equipment (PPE) assets as they reach the end of their useful lives. Ratio higher than one indicates that annual capital expenditure exceeds the annual amount of depreciation, and the entity is likely to be sufficiently maintaining, replacing or renewing existing PPE assets. Due to the nature of capital replacement expenditure this ratio can fluctuate year to year as a result the five year average ratio is more relevant.

Source: Queensland Audit Office

Appendix E—Checklist for preparation of financial statements

Figure E1

Checklist for preparation of financial statements	
1	Is a plan established that outlines the processes, resources, milestones, oversight and quality assurance practices required in preparing the financial report?
2	Is a pro forma financial report prepared and provided to the auditors before 31 October to enable early identification of amendments, minimising the need for significant disclosure changes at year end?
3	Is materiality including quantitative and qualitative thresholds assessed at the planning phase in consultation with the audit committee?
4	Is full accrual monthly reporting adopted to assist in preparing the annual financial report?
5	Is the supporting documentation, data and the financial report itself prepared to a high standard and reviewed by an appropriately experienced and independent officer prior to providing to the auditors?
6	Is rigorous and objective analytical review undertaken during the financial report preparation process to help to improve the accuracy of the report?
7	Are robust quality control and assurance processes established sufficiently to provide assurance to the audit committee on the accuracy and completeness of the financial report?
8	Do the preparers of the financial report have a good understanding and experience in applying relevant accounting standards and legislation, and have project management and interpersonal skills?
9	Are periodic compliance reviews undertaken to identify areas of non-compliance or changes to legislation that affect the financial report?
10	Is sensitive information protected and safeguarded throughout the process to prevent inappropriate public disclosure?

Source: Queensland Audit Office

Appendix F—Better practice principles for disclosing underlying results

Figure F1

Better practice principles
1. There should be a clear and understandable statement in the IMFR or annual report disclosing the reason that the Members believe the alternative profit measures provide useful information.
2. The operating result in the financial statements be disclosed more prominently than the underlying result.
3. The underlying result be clearly labelled in a way that distinguishes it from the operating result in the financial statements. Any term or label used to describe the underlying result must not cause confusion with the operating result in the financial statements.
4. There should be a clear narrative explanation as to how the underlying result is calculated.
5. There should be a reconciliation explaining the calculation of the underlying result and how it relates to the operating result in the financial statements.
6. The approach used to determine the underlying result should be consistent with the prior period. If there has been a change in approach, there should be an explanation about the nature of the change, reasons for the change and financial impact of the change.
7. For each adjustment made to the operating result in the financial statements, corresponding items be adjusted in any comparative information.
8. Underlying results should be unbiased and not used to avoid presenting ‘bad news' to the market.
9. Items that have occurred in the past or are likely to occur in a future period not be described as ‘one-off’ or ‘non-recurring’.
10. A clear statement be made about whether the underlying result has been audited or reviewed in accordance with Australian Auditing Standards.

Source: Queensland Audit Office, adapted from Deloitte financial reporting survey June 2014, and ASIC RG 230 Disclosing non-IFRS financial information.

Appendix G—Definitions — staff by function

Teaching only function

The work involves only teaching and associated activities (including lecturing, group or individual tutoring, preparation of teaching materials, supervision of students, marking, and preparation for the foregoing activities), or the management and leadership of teaching staff and of staff who support teaching staff. There is no formal requirement that research be undertaken.

Research only function

The work involves undertaking only research work or providing technical or professional research assistance, or the management and leadership of research staff and of staff who support research staff. There may be limited other work (eg participation in the development of postgraduate courses and supervision of postgraduate students).

Teaching-and-research function

A formal requirement is that both a teaching function and a research function will be undertaken, or the work requires the management and leadership of teaching staff and research staff and persons who support such staff.

Other function

Functions other than a teaching only function or a research only function or a teaching-and-research function. People with such functions may be located within academic organisational units as well as other types of organisational units.

Source: Australian Government - Department of Education and Training.

Appendix H—QAO risk management maturity model

Leadership — Senior management's commitment and approach to risk management as a key governance mechanism				
Basic	Developing	Established	Integrated	Optimised
Senior management demonstrates awareness of the need to appropriately manage risk, however does not commit dedicated resources to risk management. There is no relationship between risk management activities and senior management's decision making. Senior management approaches risk management reactively, with limited proactive risk assessments.	Senior management reviews the entity's risk management framework on an ad hoc basis, and provides input into the approaches adopted for managing risks. Senior management commits some resources to risk management. Risk management activities are aimed at the entity's compliance with laws and regulations, but are not linked to strategic and operational decision-making. Senior management focusses on risk avoidance, not managing new opportunities. When managing risk, there is limited emphasis on long term business and planning objectives.	Senior management promotes the entity's risk management framework across the entity. Senior management makes explicit its risk appetite, tolerance to risk and capacity for risk taking. Ownership of risk management is vested in a senior person and is appropriately resourced. Risk management processes include the identification of opportunities. There is some evidence of risk management being factored into senior management's decision-making processes, but risk management is not formally embedded.	Senior management demonstrates ongoing commitment to risk management activities and their ongoing development across the entity. Senior management is proactive in ensuring that risk management is adequately resourced. Senior management encourages managed risk taking associated with innovative approaches to the entity's activities and to new business opportunities. Senior management considers risk as part of its strategic planning process.	Senior management drives the integration of risk management at both strategic and operational levels. Risk is incorporated into all senior management decision making and when setting objectives for the entity. Senior management commits to continual improvement in its approach to risk management and has adopted relevant leading practice.

People and accountability — How well the entity's responsibility structures support risk management				
Basic	Developing	Established	Integrated	Optimised
Some staff are aware of the need to assess and manage risk. These staff have basic knowledge of risk management principles. There is no central coordination of risk management for the entity.	Key staff are provided training and guidance material to assist in the management of risk. A central person/team leads risk management, but there is little input from across the entity more broadly.	Key staff have the skills and knowledge to manage risk effectively. Staff are given clear responsibility for managing risk, but there is no formal accountability mechanisms to monitor how risk management is being applied. Staff are engaged from across the entity in risk management activities and there is representation from all major business units.	Most staff have relevant skills and knowledge to manage risk effectively. Regular training is available to staff to enhance their risk management skills. Staff are accountable for managing risk and their roles in risk management have been clearly articulated to them. There is ongoing specialist risk management support available for staff. A central risk management team has formal risk management responsibilities.	All staff have responsibility for risk management and see it as a part of all the entity's processes. Responsibility for risk management is incorporated into duty statements, performance agreements and annual performance assessments. A central risk management team has been established and has developed leading practice methodologies to support ongoing risk management activity.

Process integration — The depth of integration of risk management in key business processes, practices and systems				
Basic	Developing	Established	Integrated	Optimised
Risk assessment processes are stand-alone activities and are not supported by established policy or procedures. Risk management activities are managed manually or in simple tools that are developed in isolation of the entity's operational context.	Risk management processes are being developed but they are applied inconsistently across the entity and are not integrated into key business processes and planning.	Risk management processes have been implemented in key areas. Specific risk assessments have been undertaken in areas of potential high exposure (e.g. fraud risk assessments).	Standardised risk management processes are an integral part of the entity's core operations. The entity's systems have the capacity to meet the ever-changing business and risk environment.	Risk management strategies and processes are integrated as part of all business processes. Risk management activities are managed within sophisticated systems that highlight exceptions, report risk events and prompt staff for remedial action when required.

Response — The processes in place to ensure treatments are effective				
Basic	Developing	Established	Integrated	Optimised
Risk treatments have been identified for some risks but there is no formal mechanism for assessing their effectiveness.	Risk treatments are assessed to ensure that risks are managed in accordance with the entity's risk appetite and risk framework.	Risk treatment plans include alternative courses of action and cost/benefit analyses of treatments. There is a formal process of monitoring treatments.	Responses to risks are commensurate to the level of risk, including risk appetite and tolerances to risk defined across the entity (risks are not under or over controlled). Responses address the root cause of risks. Treatments are assigned to a specific risk owner.	Exception reports highlight instances where risks fall outside the maximum tolerances. There is an independent review of all risks and treatment plans to ensure consistent treatment. The results of an assessment of treatment effectiveness are shared across the entity.

Monitoring — The extent of ongoing activity to monitor the entity's risk profile				
Basic	Developing	Established	Integrated	Optimised
Risk policies and basic risk registers are provided to senior management for review on an ad hoc basis, but no risk performance monitoring reports are provided to senior management. Risk is a standing agenda item for the risk management committee.	Senior management review and discuss risk as part of management meetings on a regular basis. Risk performance monitoring reports are provided to senior management.	Risk is a standing agenda item for executive management meetings. Concise reports (backed up by more detailed information as required) highlighting exceptions are provided to allow senior management to focus on issues that require attention.	Senior management routinely reviews and discusses the risks that could cause the greatest impact on the entity and on achieving its strategic objectives. These discussions are supported by integrated risk, performance and financial information linked to the entity's objectives. There is a process for monitoring changes to the external environment that may impact the entity's risk profile, but the process is not systematized.	Systems are in place to support the ongoing review of the entity's risk management strategies, including key risk performance indicators that allow management to monitor the effectiveness of risk management activities. The entity's risk management framework is regularly benchmarked to external best practice. There is ongoing environmental scanning to identify trends and external factors that may impact the entity.

Achieving outcomes and innovation — The entity's culture supports well-managed risk taking to foster improvements and innovation				
Basic	Developing	Established	Integrated	Optimised
Focus is only on achievement of business objectives. There is minimal or no focus on the benefits of effective risk management and no recognition of its linkage to innovation.	The risk assessment process is used to identify new opportunities and improve business practices, but this happens in an ad hoc manner.	The entity's culture supports open discussion of lessons learnt and supports managed risk taking to foster improvements and innovation.	Proactive procedures and approaches are in place to maximise identification of opportunities in line with the entity's risk appetite and tolerance levels. Risk management contributes to improved and innovative service delivery and outcomes.	The entity has a record of maximising opportunities and innovation through effective and well managed risk taking. Risk management drives improved service delivery and outcomes.

Research material

COSO Integrated Framework, Framework and Appendices May 2013
ISO 31000:2009
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Auditor General Victoria, Good Practice Guide, Managing risk across the public sector, 2004
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Appendix I—Risk management better practice material

Figure I1
Risk appetite

Risk appetite
What is risk appetite? Risk appetite is the amount of risk that the entity is prepared to accept at any point in time to achieve its objectives. It reflects the entity's risk management philosophy, and in turn influences the entity's culture and operating style. Risk appetite guides resource allocation, assists in aligning the organisation, people and processes necessary to effectively respond to and monitor risks. * **Why make a risk appetite statement?** Articulating an entity's risk appetite makes explicit the entity's attitude to risk. This in turn guides strategic and operational planning about the nature and extent of activities or objectives the agency is willing to be involved in and therefore makes the agency more likely to achieve its stated objectives. The absence of a defined risk appetite can lead to confusion over the levels of acceptable risk and shortcomings in response to risk. **What makes a risk appetite statement effective?** ▪ Aligned – is linked to the entity's mid and long term strategies. ▪ Complete – covers all fundamental risks in the entity's risk profile. ▪ Measurable – contains a small number of succinct quantitative and qualitative statements used to define the risk that will or will not be assumed. ▪ Realistic – establishes a sufficient buffer between risk appetite and the entity's capacity to absorb risks/shocks and sets real boundaries that account for serve stress. ** **Articulating risk appetite statement** There is no one universal risk appetite statement applicable to all agencies. At the highest level an agency states an overall risk appetite that is broad enough yet descriptive enough for the lines of business to manage their risks consistently within it. This statement is supported by articulating appetite for each major class of organisational objective and then for different categories of risk. *** **Example risk appetite statement** The entity operates within a low overall risk range. The entity has a low risk appetite for the safety of its staff and for non-compliance with laws and regulations. The entity has a moderate risk appetite for developing new lines of business and identifying new customers. The entity has a low risk appetite for any risk not related to the achievement of its strategic objectives. *** **What is risk tolerance?** Risk tolerance is the variation from the pre-determined risk appetite an agency is prepared to accept. Risk tolerance is an expression in absolute terms the level of risk an agency can accept. **Examples of risk tolerance statements** We will not enter into contracts with certain types of clients. We accept no more than X workplace health and safety instances per year. We will not invest more than X% in new lines of business. We expect zero decrease in research output.***

** Source: COSO Enterprise Risk Management – Integrated Framework, p 19.*
*** Source: Adapted from 'Enabling more effective risk appetite frameworks', Bank Governance Leadership Network, Viewpoints, 26 September, 2013.*
**** Source: Adapted from COSO Enterprise Risk Management – Understanding and Communicating Risk Appetite, Thought Leadership in ERM.*

Figure I2
Risk champions and using forums

Risk champions and using risk forums
Risk champions A risk champion provides leadership within their team/division on the management of risk. They drive the day to day implementation of risk management processes. They can assist in changing an attitude of risk management being a compliance activity to it being seen as integral to the achievement of an agency's objectives. **Risk forums** Having risk champions meet on a regular basis as part of a dedicated risk forum encourages collaboration, joint commitment and an increased awareness of risks impacting individual divisions, groups or activities that may prove common across an agency. This approach also broadens environmental scanning, ensures a consistent approach to risk identification and assessment is adopted across an agency and across strategic and operational risks, and further enhances existing risk responsibility structures. Risk champions provide the most benefit to an agency where they represent varying levels of management and operational activities. Risk champions do not need to be a risk owner.

Source: Queensland Audit Office

Figure I3
Risk treatment plan checklist

Risk treatment plan checklist
From our review of the universities and through our wider work across government agencies who have strong risk treatment plans we have identified the following elements that are essential for a risk treatment plan to be effective: ▪ Detailed nature of the risk ▪ Inherent risk rating ▪ Risk triggers ▪ Mitigating controls ▪ Linkage to strategic or operational objectives ▪ Cost benefit analysis of treatment options ▪ Assessment of residual risk rating to appetite ▪ Performance measures to help monitor risk ratings and mitigation strategies ▪ Risk owner clearly identified

Source: Queensland Audit Office

Figure I4
Examples of risk indicators

Risk	Risk key performance indicator
Budget – cost efficiencies not achieved	Cost to income ratio
Legal and regulatory risk	Number of regulatory compliance breaches
Investment risk	Investment performance compared to benchmark
Workplace, health and safety (WH&S) risks	Number of WH&S incidents compared to industry benchmark or prior year

Source: Queensland Audit Office

Audit and Risk Committee survey

Questions 1–7

Questions 1-7 requested respondents provide a rating of 1-5 as follows:

1 Very dissatisfied

2 Somewhat dissatisfied

3 Neither satisfied or dissatisfied

4 Mostly satisfied

5 Very satisfied

Figure I5
Rating questions

Questions	Sector average rating
1. How satisfied are you that your university:	
▪ Clearly defines strategic objectives to enable the identification and assessment of risks relating to these objectives?	4.6
▪ Identifies the most significant risks to achieving the university's objectives?	4.6
▪ Implements appropriate controls to manage the most significant risks?	4.4
▪ Considers the potential for fraud in assessing the achievement of objectives?	4.4
▪ Assesses changes that could significantly impact the system of internal control?	4.3
2. How satisfied are you with the quality of the information you receive about each of the following aspects of risk management:	
▪ Uncertainty and volatility in the sector (economic, political, social)	4.4
▪ Growth and innovation	4.3
▪ Operational risk and the internal control environment	4.4
▪ IT security (including data privacy and protection of intellectual property)	4.0
▪ Legal and regulatory compliance	4.6
▪ Funding pressures and revenue challenges	4.4
▪ Emerging strategic risks affecting the sector	4.4
3. How satisfied are you about the amount of time the university devotes to considering and discussing risk management?	4.4
4. How satisfied are you about the internal audit function's coverage of key risk areas in its work plan?	4.3
5. How satisfied are you about the level of visibility and management of the risks associated with your university's operations outside Queensland (national and/or international)?	4.2
6. How satisfied are you that the notion of risk appetite is well understood by those involved in risk management at your university?	4.1

Questions		Sector average rating
7.	Overall, on a maturity scale of 1-5, with 1 being basic and 5 being equivalent to leading practice, how would you rate the maturity of the following:	
	▪ the leadership's (executive management) commitment and approach to risk management	3.9
	▪ the responsibility structures (people and accountability) in place to support risk management activity at an operational level	4.1
	▪ the level of integration of risk management in key processes	3.9
	▪ the extent of ongoing activity to monitor the university's overarching risk profile	4.2
	▪ the university's ability to identify opportunities and maximise the benefits of well managed risk (e.g. to innovate)	3.7
	▪ the university's ability to readily identify and address risks posed as a result of partnerships and collaboration with other entities	3.6

Source: Queensland Audit Office

Questions 8–12

These questions provided an opportunity for survey respondents to provide a direct response outlining their views on key aspects of risk management. The table below provides a summary of the themes of these responses from audit and risk committee members across the sector.

Figure I6
Direct responses

Other questions	Sector themes
8. Is there a particular aspect of your university's current operations / service provision that you consider to pose a significant risk that requires more effective management?	Responses across the sector focused on ongoing financial viability given uncertainty around government funding and management of student load, particularly retention of international students as the risks that require more effective management.
9. What single risk do you consider to be the most potentially damaging for your university (if different from your answer to 8 above) and do you consider this risk is being effectively managed?	Common responses across the sector identified government funding, maintaining university reputation and technology risks as the most potentially damaging risks facing universities.
10. What do you consider to be the main emerging risk areas over the next 5 years and do you consider the university is taking appropriate action to adequately respond to these emerging risks?	Emerging risks consistently identified across the sector included fee deregulation and maintaining competitive and funded research. Survey respondents were largely satisfied that appropriate action addressing these risks is being taken.
11. What do you consider to be the emerging opportunities for your university over the next 5 years and do you consider the university is taking appropriate action to take advantage of the emerging opportunities?	Emerging opportunities consistently identified across the sector included the advancement of on-line education enabling increasing diverse student populations and education offerings in diverse geographic locations. Survey respondents were mostly satisfied that action was being taken to take advantage of these emerging opportunities.
12. In your experience, what are the critical components to an effective risk management system?	Commonly identified components of effective risk management included: Clearly articulating risk appetite and tolerance levels. Defining responsibility and ensuring accountability for risk management activities. Robust risk assessment processes that enable the identification of emerging and changing risks. Consideration of innovation and opportunities. Integration with strategic planning and decision-making processes.

Source: Queensland Audit Office

Appendix J—Risk management glossary

Figure J1
Glossary

Term	Definition
Operational risk	Those risks that arise in day to day operations, and which require specific and detailed response and monitoring regimes. If not treated and monitored, operational risks could potentially result in major adverse consequences of the agency.
Residual risk	Risk remaining after new controls or treatments are taken into account.
Risk	The chance of something happening that will have an impact on the achievement of the agency's objectives. Risk is measured in terms of consequences and likelihood, and covers threats and opportunities.
Risk appetite	The amount of risk that the agency is prepared to accept or be exposed to at any point in time.
Risk management committee	A standing committee responsible for providing oversight of the agency's management of risk.
Risk management framework	The agency's policies, procedures, systems and processes concerned with managing risk.
Risk management process	The systematic application of management policies, procedures and practices to the tasks of establishing the context, identifying, analysing, evaluating, treating, monitoring and communicating risks.
Risk profile	The documented and prioritised overall assessment of a range of specific risks faced by the agency.
Risk retention	Intentionally or unintentionally retaining the responsibility for loss, for financial burden of loss within an agency.
Risk sharing	Sharing with another party the burden of loss, or benefit of gain from a particular risk.
Risk tolerance	The variation from the pre-determined risk appetite an agency is prepared to accept.
Risk transfer	Shifting the responsibility or burden for loss to another party through legislation, contract, insurance or other means.
Strategic risk	Risks that may affect the agency's ability to meet its strategic objectives and require oversight by senior executives.

Source: Queensland government: A guide to risk management, July 2011

Auditor-General Reports to Parliament

Reports tabled in 2015–16

Number	Title	Date tabled in Legislative Assembly
1	Results of audit: Internal control systems 2014–15	July 2015
2	Road safety – traffic cameras	October 2015
3	Agricultural research, development and extension programs and projects	November 2015
4	Royalties for the regions	December 2015
5	Hospital and Health Services: 2014–15 financial statements	December 2015
6	State public sector entities: 2014–15 financial statements	December 2015
7	Public non-financial corporations: 2014–15 financial statements	December 2015
8	Transport infrastructure projects	December 2015
9	Provision of court recording and transcription services	December 2015
10	Queensland state government: 2014–15 financial statements	December 2015
11	Management of privately operated prisons	February 2016
12	Follow up Report 12: 2012–13 Community Benefits Funds: Grant Management	February 2016
13	Cloud computing	February 2016
14	Financial risk management practices at Energex	April 2016
15	Queensland public hospital operating theatre efficiency	April 2016
16	Flood resilience of river catchments	April 2016
17	Results of audit: Local government entities 2014–15	May 2016
18	Results of audit: Education sector entities 2015	May 2016