



Examination of Auditor- General Reports on the water sector

Report No. 38, 57th Parliament
State Development and Regional Industries Committee
February 2023

State Development and Regional Industries Committee

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Acknowledgements

The committee acknowledges the comprehensive work of the Auditor-General and Queensland Audit Office in preparing the following reports:

- **Water 2021** (Report No. 3: 2021-22)
- **Water 2020** (Report No. 9: 2020-21)
- **2021 status of Auditor-General's recommendations** (Report 4: 2021-22)

The committee also acknowledges Seqwater, Sunwater, Urban Utilities, Unitywater, Gladstone Area Water Board and Mount Isa Water Board and their responses to the committee's enquiries.

Contents

Chair's foreword	ii
Recommendations	iii
1 Strengthening the security of information systems in the water sector	1
1.1 Key findings and recommendations of the Auditor-General	1
1.2 What steps are water entities taking to strengthen information security	1
1.3 Committee comment	2
Appendix A – Inquiry conduct	3
Appendix B – Water 2021 (Report 3: 2021-22) – Summary	4
Appendix C – Water 2020 (Report 9: 2020-21) – Summary	7
Appendix D – 2021 status of Auditor-General's recommendations (Report 4: 2021-22) – Summary	11

Chair's foreword

This report presents a summary of the committee's examination of 2 financial audits conducted by the Auditor-General relating to Queensland's water sector, *Water 2020* and *Water 2021*. Six entities in Queensland's water sector were audited: Seqwater, Sunwater, Urban Utilities, Unitywater, the Gladstone Area Water Board and the Mount Isa Water Board.

This report focusses on findings of the Auditor-General relating to water entities strengthening their information security. A more detailed overview of the findings of each audit can be found in the appendices.

Water entities rely on information technology systems to operate and strong controls are needed over who has access to systems and information. Weaknesses in information technology controls increase the risk of errors going undetected or financial loss, such as fraud.

Over several years, the water entities have received recommendations from the Queensland Audit Office (QAO) regarding the security of their information security. One of those reports, *Report 19: Security of critical water infrastructure*, dates back to June 2017, yet in 2021 the QAO continues to find improvements are necessary.

The committee fully supports the recommendation of the QAO, that water entities must take steps to strengthen the security of their information systems.

After considering QAO reports on the Queensland water sector and taking evidence from the Auditor-General, the committee strongly recommends that the Department of Regional Development, Manufacturing and Water consider requiring that all water entities establish their own independent audit and risk management committees, and that these committees be required to consider cyber security and information management risks on a regular basis.

Thank you also to my committee colleagues for their collaborative approach and the Parliamentary Service staff who have supported this inquiry.

I commend this report to the House.



Chris Whiting MP

Chair

Recommendations

Recommendation 1

6

That the Department of Regional Development, Manufacturing and Water takes steps to ensure that all water entities establish their own independent audit and risk management committees, and that these committees be required to consider information management system and cyber security risks.

1 Strengthening the security of information systems in the water sector

Water entities rely on information technology systems to operate and strong controls are needed over who has access to systems and information. The Auditor-General states that weaknesses in information technology controls increase the risk of undetected errors or potential financial loss, including fraud.¹

1.1 Key findings and recommendations of the Auditor-General

Over several years, the water entities have received recommendations from the Queensland Audit Office (QAO) regarding the security of their information security. One of those reports dates back to June 2017, *Security of critical water infrastructure*, yet in 2021, the QAO continues to find improvements are necessary.

Key findings include:

- Water entities rely heavily on information systems and technology and as such must be prepared for cyber attacks.
- A cyber breach was exposed where malicious actors accessed an entity's web server. Fortunately, no customer or financial data was lost. The entity implemented measures to address the breach, such as updating software, stronger passwords and monitoring web traffic.
- All entities must have strong security practices to protect information, respond to changes and safeguard against external threats. Not all entities have fully addressed this recommendation.
- Timely monitoring of access to systems is essential. Entities should only grant employees the minimum access they need to carry out their work. User access, especially privileged access, must be regularly reviewed and monitored.²

In 2021, the Auditor-General recommended that immediate action needs to be taken to address ongoing security weaknesses in information systems.

1.2 What steps are water entities taking to strengthen information security

The committee sought responses from each of the water entities in terms of their progress against the recommendations. In summary, the committee found entities were implementing a mix of the below measures:³

- Incorporating external standards and recommendations into corporate plans and systems, such as the ISO27001 (Data Protection), Queensland Government Standard IS18 (Information Security Policy) and the QAO's *Managing Cyber Security Risks* report.
- Regular audits of access, with reviews and monitoring of privileged access and increased identity protection for key risk employees.
- Regular cyber security training and refreshers for staff.
- Application of "least privilege basis" (i.e. giving someone the least amount of access they need to perform their work) with segregation of duties to ensure access is appropriate.
- Use of strong password practices in line with Queensland Government Chief Information Officer recommendations and addition of multi-factor authentication.

¹ Queensland Audit Office, Water 2020, p 6; Queensland Audit Office, Water 2021, p 6.

² Queensland Audit Office, Water 2020, p 6; Queensland Audit Office, Water 2021, p 6.

³ The committee has not specified which entities are carrying out which specific steps so as to not indicate their cyber security capabilities.

- Access controls and encryption for sensitive data.
- Network and firewall upgrades, timely patching of security vulnerabilities and software updates in accordance with vendor patching cycles.
- Self-assessing their systems against the audit and assessing risks to their systems, penetration testing of network security, technology risk registers and round-the-clock security monitoring and response services.
- Partnering with the Australian Cyber Security Centre (ACSC) and implementing the ACSC's Essential Eight Mitigation Strategies.

1.3 Committee comment

Information security is critical to the delivery of services and protection of customer information. The committee notes that the Auditor-General regards cyber security as the biggest risk threat to state and local government public sector entities, with cyber security risks growing during the pandemic when many businesses moved operations online.⁴

The committee strongly supports the QAO's recommendations that water entities address the security of their information systems. We also recommend that water entities, regardless of size, establish independent audit and risk committees, and that these committees be required to consider risks to cyber security and information management systems on a regular basis.

Recommendation 1

That the Department of Regional Development, Manufacturing and Water consider requiring all water entities to establish their own independent audit and risk management committees, with these committees required to consider risks to cyber security and information management systems.

⁴ Private briefing transcript, Brisbane, 14 March 2022, p 1.

Appendix A – Inquiry conduct

8 March 2021 – Public briefing

Queensland Audit Office

- Brendan Worrall, Auditor-General
- Patrick Flemming, Assistant Auditor-General
- Vaughan Stemmett, Senior Director

14 March 2022 – Private briefing

Queensland Audit Office

- Brendan Worrall, Auditor-General
- Patrick Flemming, Assistant Auditor-General
- Vaughan Stemmett, Senior Director

Department of Communities, Housing and Digital Economy

- Robert Champion, Queensland Government Chief Information Security Officer

Responses from water entities

The committee wrote to all six entities in April 2021 requesting updates on their implementation of *the Water 2020* recommendations. All entities responded by May 2021.

As the information received relates to information security, these responses will remain confidential to the committee.

Appendix B – Water 2021 (Report 3: 2021-22) – Summary

About the report	
<p>Water 2021 summarises the audit results of 6 entities in Queensland’s water sector: Seqwater, Sunwater, Urban Utilities, Unitywater, Gladstone Area Water Board, and Mount Isa Water Board. To read the report see: https://www.qao.qld.gov.au/sites/default/files/2021-11/Water%202021%20%28Report%203%E2%80%942021%E2%80%9322%29.pdf</p>	
Headline results⁵	
<ul style="list-style-type: none"> • Seqwater was no longer liable for damages from the 2011 South East Queensland floods class action. • Financial statements were reliable, complied with relevant laws and standards, prepared in a timely manner and of good quality. • Weaknesses in information systems continued. • Profits and shareholder returns increased. • Drought, the sustainable supply of water, and dam improvement programs remained issues. 	
Recommendations to all entities⁶	
Rec 1	Water entities address the security of their information systems.
Audit opinion results⁷	
<ul style="list-style-type: none"> • Unmodified audit opinions were issued to all 6 entities. • Five entities met their legislative deadline of 31 August 2021. Seqwater’s financial statements were certified on 21 September 2021. • Most entities self-assessed their financial statement preparation as ‘integrated’ or ‘optimised’—the highest levels in the QAO’s financial statement preparation maturity model. This means entities believed their processes for preparing financial statements were efficient and provided high-quality information in a regular, timely manner. The results of the QAO’s audits supported their assessments. 	
Internal controls were generally effective⁸	
<ul style="list-style-type: none"> • Internal controls were generally effective but could be improved. • One entity’s control environment was assessed as ‘ineffective’ due to 3 significant deficiencies. These deficiencies related to security of, and access to, information systems. There were an additional 21 deficiencies in internal controls across the sector.⁹ 	

⁵ Queensland Audit Office, Water 2021, p 1.

⁶ Queensland Audit Office, Water 2021, p 2.

⁷ Queensland Audit Office, Water 2021, p 4.

⁸ Queensland Audit Office, Water 2021, pp 5-7.

⁹ Of the 21 deficiencies identified, 8 related to security of/access to information systems; 6 related to the recognition of donated assets; 4 related to procurement processes; one related to the separate categories

- The QAO was satisfied with the responses received from each entity on planned corrective action for the internal control issues raised.

Immediate action needs to be taken to address ongoing security weaknesses in information systems

- Not all entities had fully addressed the recommendation made in *Water 2020* to strengthen the security of their information systems. Control weaknesses in information system security were identified at 3 entities.
- For one entity, there were 3 significant deficiencies relating to management of user access across multiple systems (financial, invoicing, and payroll). The QAO stated entities should only assign employees the minimum access required to perform their jobs.
- A cyber breach (between August 2020 and May 2021) resulted in unauthorised access to an entity’s web server. No customer or financial information was lost. The entity took steps to remedy the breach.
- The QAO stated cyber risk vulnerabilities and exposures must be continuously assessed and that entities must ensure their users know their responsibilities in managing cyber risks.

Timely recognition of donated assets

- Distributor-retailers collect developer contributions from developers, which are cash contributions or donated assets (such as water and sewerage infrastructure). In 2019–20, the QAO reported on control weaknesses affecting the timely recognition of donated assets.
- Distributor-retailers undertook an independent review to amend data inconsistencies. As a result, weekly compliance checks of all donated assets were implemented to ensure completeness and accuracy of data.

Assessment tools for internal controls¹⁰

- The QAO was developing new assessment tools for internal controls relevant to public sector entities to provide them with greater insight into the rigour of their internal control processes.
- The tools focussed on asset management, change management, culture, governance, grants management, information systems, monitoring, procure-to-pay (the whole procurement process), record keeping, and risk management.
- The QAO consulted on the tools with clients and intended to use them in its 2021-22 audits.

The sector’s profits and shareholder returns rose¹¹

- Profits increased by \$234.7 million (106.6 per cent) in 2020–21. The largest impact was an adjustment to Sunwater’s profit in relation to the 2011 South East Queensland floods class action. The settlement between Sunwater and group members of the class action was \$80 million less than originally estimated in 2019–20.
- In September 2021, the New South Wales (NSW) Court of Appeal overturned the Supreme Court of NSW’s November 2019 decision that found Seqwater was negligent in relation to the

of security of/access to electronic funds transfers payment information; one related to security of supplier and employee information; and one related to the review of useful lives of property, plant and equipment.

¹⁰ Queensland Audit Office, *Water 2021*, p 7.

¹¹ Queensland Audit Office, *Water 2021*, pp 5, 8.

<p>2011 South East Queensland floods. As a result, Seqwater was no longer liable to pay damages. This decision did not impact Seqwater’s 2020–21 results.</p> <ul style="list-style-type: none"> • Seqwater did not pay a dividend in 2020–21 despite reporting a profit. • Shareholder returns increased due to the sector’s increased profits.
<p>Bulk and irrigation water pricing¹²</p>
<ul style="list-style-type: none"> • In response to COVID-19, the Queensland Government deferred the Queensland Competition Authority’s review of the South East Queensland bulk water prices to 2021–22. This resulted in the bulk water price for 2020–21 being rolled forward for an extra year (2021–22), with the government recently directing the same 3.5 per cent increase that was applied in 2020–21. • The government continued to pay community service obligation payments (\$19.7 million) to compensate Sunwater and Seqwater where the government set irrigation prices below cost.
<p>Drought and sustainable water supply¹³</p>
<ul style="list-style-type: none"> • Queensland continued to experience extreme weather conditions, with 34 councils fully drought-declared. Prolonged drought led to reduced water storage levels, increased operational costs, and the need for increased capital investment in water security projects. • Projects were underway to improve water supply in drought-declared areas, including water restrictions and longer-term solutions such as the Rookwood Weir Project, the Granite Belt Irrigation Project and the Toowoomba to Warwick Water Pipeline Project.
<p>Dam improvement programs¹⁴</p>
<ul style="list-style-type: none"> • The QAO was undertaking a performance audit on the Department of Regional Development, Manufacturing and Water’s framework for ensuring dams are managed safely. • The cost of dam improvement programs continued to be a challenge, as was uncertainty over the cost of works. • Future shareholder returns were likely to be impacted by asset improvements costs.

¹² Queensland Audit Office, Water 2021, p 9.

¹³ Queensland Audit Office, Water 2021, pp 10-11.

¹⁴ Queensland Audit Office, Water 2021, pp 11-12.

Appendix C – Water 2020 (Report 9: 2020-21) – Summary

About the report	
<p>Water 2020 summarises the audit results of 6 entities in Queensland’s water sector: Seqwater, Sunwater, Urban Utilities, Unitywater, Gladstone Area Water Board, and Mount Isa Water Board. To read the report see: https://www.qao.qld.gov.au/reports-resources/reports-parliament/water-2020</p>	
Headline results ¹⁵	
<ul style="list-style-type: none"> • Seqwater’s financial statements should have included a liability and expense as a result of an unfavourable court judgement relating to the 2011 South East Queensland floods class action. • Financial statements were reliable, complied with relevant laws and standards, prepared in a timely manner and of good quality. • Information security continued to be a challenge. • Profits and shareholder returns declined. • Drought, and the need to provide a sustainable supply of water, posed challenges. 	
Recommendations to all entities ¹⁶	
Rec	<p>We recommend all entities strengthen the security of their information systems. They rely heavily on technology, and increasingly, they have to be prepared for cyber attacks. Any unauthorised access could result in fraud or error, and significant reputational damage.</p> <p>Their workplace culture, through their people and processes, must emphasise strong security practices to provide a foundation for the security of information systems.</p> <p>Entities should:</p> <ul style="list-style-type: none"> • provide security training for employees so they understand the importance of maintaining strong information systems, and their roles in keeping them secure • assign employees only the minimum access required to perform their job, and ensure important stages of each process are not performed by the same person • regularly review user access to ensure it remains appropriate • monitor activities performed by employees with privileged access (allowing them to access sensitive data and create and configure within the system) to ensure they are appropriately approved • implement strong password practices and multifactor authentication (for example, a username and password, plus a code sent to a mobile), particularly for systems that record sensitive information • encrypt sensitive information to protect it • patch vulnerabilities in systems in a timely manner, as upgrades and solutions are made available by software providers to address known security weaknesses that

¹⁵ Queensland Audit Office, Water 2020, p 1.

¹⁶ Queensland Audit Office, Water 2020, p 2.

	could be exploited by external parties. Entities should also self-assess against all of the recommendations in our report— <i>Managing cyber security risks</i> (Report 3: 2019–20)—to ensure their systems are appropriately secured.
Rec	As part of the negotiation process for enterprise agreements, entities should ensure they understand how these arrangements interact with employee contracts.
Recommendation to distributor-retailers (Urban Utilities and Unitywater)¹⁷	
Rec	Distributor-retailers (Urban Utilities and Unitywater) need to: <ul style="list-style-type: none"> • engage more closely with developers to determine whether assets are complete (ready to use) • obtain engineering drawings and other information in a timely manner • closely monitor development application registers for completeness of recorded assets • identify and address causes of delays in processing engineering drawings.
Audit opinion results¹⁸	
	<ul style="list-style-type: none"> • Five entities received unmodified opinions. Seqwater received a qualified opinion¹⁹ for not recording a liability and matching expense due to the unfavourable court judgement relating to the 2011 South East Queensland floods class action, meaning its profit was overstated.
Mature financial statement preparation processes are in place²⁰	
	<ul style="list-style-type: none"> • The QAO worked with the entities as they undertook a self-assessment of their financial statement preparation processes using the QAO’s maturity model. The entities assessed most of their processes as ‘integrated’ or ‘optimised’—the highest levels of maturity. This means the entities assessed that their processes supporting the preparation of financial statements were efficient and provided high-quality information in a regular, timely manner.
Internal controls are generally effective²¹	
	<ul style="list-style-type: none"> • Internal controls were generally effective but could be improved. • The QAO found 25 deficiencies in internal controls across the sector. Of these, 4 were rated as significant deficiencies²² (those of higher risk that require immediate action by management) with the remaining 21²³ considered to be of lower risk that can be corrected over time.

¹⁷ Queensland Audit Office, *Water 2020*, pp 4-5.

¹⁸ Queensland Audit Office, *Water 2020*, p 4.

¹⁹ The QAO expresses a qualified opinion when financial statements are fairly presented, with the exception of a specified area. Source: Queensland Audit Office, *Water 2020*, p 4.

²⁰ Queensland Audit Office, *Water 2020*, p 5.

²¹ Queensland Audit Office, *Water 2020*, pp 5-7.

²² Of the 4 significant deficiencies identified, 3 related to information systems security and access and one related to timely recognition of donated assets.

²³ Of the 21 deficiencies identified, 9 related to information systems security and access; 3 related to electronic funds transfer payments security and access; 3 related to supplier and employee information security;

- The QAO had received responses from each entity on their planned corrective action to the internal control issues raised and was satisfied with the responses.
- The QAO recommended 4 entities strengthen the security of their information systems.

Timely recognition of donated assets

- Distributor-retailers collect developer contributions from developers, which are cash contributions or donated assets (such as water and sewerage infrastructure). Distributor-retailers report these contributions as revenue. Recognition of revenue from donated assets is affected if developers submit engineer-certified drawings late or when values are wrong.
- Three control weaknesses impacted the timely recognition of donated assets:
 - unrecorded assets that had been constructed but were waiting for a connection certificate
 - missing engineering drawings for issued connection certificates
 - delays in processing the engineering drawings.

There is a need to better understand complex employee arrangements²⁴

- In 2019–20, Sunwater and Seqwater became aware that some employee entitlements (e.g. salaries, superannuation, and overtime) may have been covered by both individual employment contracts and enterprise agreements. Due to the legal complexity of the interactions between the relevant enterprise agreements and the employee contracts, some employee entitlements may have been underpaid.
- As at 30 June 2020, Sunwater and Seqwater increased employee entitlements by \$5.3 million and \$1.6 million respectively, covering current and past employees (including other associated costs, e.g. payroll tax). For Seqwater, those additional employee entitlements did not include the interaction between the relevant enterprise agreements and employment contracts because it was still assessing the arrangements. It expected to resolve the matter in 2020–21.

The sector's profits and returns to the Queensland Government fell

- Profits fell by 48.9 per cent. The largest impact on profits was the \$330 million expense and matching liability recognised by Sunwater arising from the class action. By Seqwater not recognising its share of the expense (and associated liability), reported profits for 2019–20 were higher than they should have been.
- Returns to the Queensland Government were lower than in previous financial years due to the sector's reduced profit.

Water pricing and asset maintenance costs²⁵

- In response to COVID-19, the Queensland Government decided in May 2020 to set rural irrigation water prices for 2020–21 at 2019–20 levels, or to pass on any price reductions recommended by the Queensland Competition Authority.

2 related to the timely recognition of donated assets; 2 related to improvement of procurement processes; and 2 were classified as 'other'.

²⁴ Queensland Audit Office, Water 2020, p 8.

²⁵ Queensland Audit Office, Water 2020, p 10.

- The Queensland Government also confirmed it would continue to absorb irrigators' share of dam safety costs, rather than recover these costs through irrigation prices.
- The 2020–21 Queensland Budget committed \$81.6 million over 3 years to support irrigators where it sets the prices for water provided by Sunwater and Seqwater. From 1 July 2021, this funding included a 50 per cent discount on irrigation prices for fruit and vegetable growers and a 15 per cent discount for all other irrigators.

Drought and sustainable water supply²⁶

- Queensland experienced extreme weather conditions, with 41 councils drought declared. Prolonged drought led to reduced water storage levels, increased operational costs, and the need for increased capital investment in water security projects.
- Seqwater's drought response was triggered in November 2019, when dam levels fell to 60 per cent. In 2019–20, the Gold Coast Desalination Plant doubled water production to 13,804 megalitres (28.4 per cent of capacity) to the South East Queensland water grid.
- Seqwater, in consultation with the Queensland Government, deferred the decision to fully restart the Western Corridor Recycled Water Scheme until after the 2020–21 summer. This was due to rain in February 2020 and a forecast of increased rainfall over the summer.
- In May 2020, work started to lower the Paradise Dam wall by 5.8 metres to improve its stability while a long-term solution was developed.
- Projects were underway to address the issue of water supply in drought areas, ranging from interim solutions such as water restrictions to long-term projects such as the Rookwood Weir, Haughton Pipeline Duplication and Granite Belt Irrigation Projects.
- Future shareholder returns were likely to be impacted by asset improvements costs.

²⁶ Queensland Audit Office, Water 2020, p 10.

Appendix D – 2021 status of Auditor-General’s recommendations (Report 4: 2021–22) – Summary

About the report
<p>2021 status of Auditor-General’s recommendations summarises entities’ self-assessments of their progress in implementing performance audit recommendations the QAO made in its 2015–16, 2016–17, and 2017–18 reports. To read the report see: https://www.qao.qld.gov.au/sites/default/files/2021-11/2021%20status%20of%20Auditor-General%27s%20recommendations%20%28Report%204%E2%80%942021%E2%80%9322%29_0.pdf</p>
Progress in implementing recommendations²⁷
<ul style="list-style-type: none"> • The QAO asked 50 entities to report on the implementation of 447 recommendations in 32 reports. The QAO did not assess the accuracy of entities’ responses. • Of the 447 recommendations: <ul style="list-style-type: none"> • 72 per cent were fully implemented • 19 per cent were partially implemented • 6 per cent had not been implemented • 3 per cent were no longer applicable.
Recommendation categories most commonly not implemented²⁸
<ul style="list-style-type: none"> • The 4 categories with the highest number of outstanding recommendations²⁹ were: <ul style="list-style-type: none"> • performance monitoring and reporting – this category required the most improvement across the 50 entities audited. 34 per cent of 101 recommendations had not been implemented. Ten recommendations had been outstanding for more than 5 years. • governance – 81 per cent of governance recommendations had been implemented. However, one entity had not implemented recommendations from more than 5 years ago. • strategic planning – 45 per cent of the 58 recommendations were in progress or not started. • interagency coordination and information sharing – 55 per cent of the 49 recommendations had been implemented. Some entities reported difficulty in implementing recommendations in collaboration with other entities. Entities’ governance structures were often not well suited to deliver whole-of-government services.

²⁷ Queensland Audit Office, 2021 status of Auditor-General’s recommendations, p 2.

²⁸ Queensland Audit Office, 2021 status of Auditor-General’s recommendations, pp 4-5.

²⁹ ‘Outstanding recommendations’ includes partially implemented recommendations and recommendations not implemented.

Insights from entities' responses³⁰
<ul style="list-style-type: none"> • Some entities lacked the systems and processes for recording and monitoring whether they had implemented the QAO's recommendations. • Other entities reported they had implemented recommendations made to them, but it was unclear whether intended results had been achieved and evaluated. • The QAO repeated its past recommendation that entities establish audit committees with independent committee members.
Status of outstanding recommendations^{31,32}
<ul style="list-style-type: none"> • There were outstanding recommendations from reports going as far back as tabled in 2015-16. Findings from these past reports include: <ul style="list-style-type: none"> • entities not possessing adequate controls for protecting their systems and information • some entities could be better prepared for cyber security threats • entities possess valuable data sources, but data is not always easily accessible, well understood or analysed to provide insights for strategy and policy decisions • a lack of integration across systems, which can create a barrier to having a complete view of performance. Some entities could better integrate their systems to share information. • There was an instance of entities reporting differing outcomes with respect to implementing a recommendation that required their collaboration.
Council-specific issues³³
<ul style="list-style-type: none"> • The QAO has consistently highlighted that financial sustainability is one of the biggest risks to the sector. • Some councils reported difficulties in implementing recommendations due to a lack of resources. • The QAO referred to a report that made 6 recommendations to 5 councils. The council with the most outstanding recommendations was the one without an audit and risk committee.

³⁰ Queensland Audit Office, 2021 status of Auditor-General's recommendations, p 6.

³¹ Queensland Audit Office, 2021 status of Auditor-General's recommendations, pp 9-13.

³² Queensland Audit Office, 2021 status of Auditor-General's recommendations, pp 13-18.

³³ Queensland Audit Office, 2021 status of Auditor-General's recommendations, pp 17-18.