EDUCATION AND INNOVATION COMMITTEE

Members present:

Mrs RN Menkens MP (Chair)
Mr SA Bennett MP
Mr MA Boothman MP
Mrs YM D'Ath MP
Mr RG Hopper MP
Mr MR Latter MP
Mr NA Symes MP

Staff present:

Ms B Watson (Research Director)
Ms M Salisbury (Principal Research Officer)

PUBLIC BRIEFING—AUDITOR-GENERAL'S REPORT NO. 16 FOR 2013-14—RESULTS OF AUDIT: EDUCATION SECTOR ENTITIES 2013

TRANSCRIPT OF PROCEEDINGS

WEDNESDAY, 21 MAY 2014

Brisbane

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Committee met at 9.35 am

BRAHMAN, Mr P, Assistant Auditor-General, Queensland Audit Office

GREAVES, Mr Andrew, Auditor-General, Queensland Audit Office

CHAIR: Welcome. Before we begin this morning I ask everybody present to turn off their mobile phones or set them to silent. Any media recording today's proceedings are asked to adhere to the committee's endorsed media guidelines. If you require another copy of the guidelines, please ask secretariat staff. This morning's public briefing relates to the Auditor-General's report No. 16 for 2013-14, entitled *Results of audit: Education sector entities 2013*. The Queensland parliament has referred this report to the Education and Innovation Committee for consideration, and we intend to report back to the parliament once our consideration is completed.

We have invited the Auditor-General and Queensland Audit Office staff to brief us on the report's findings from the education sector entity audits. Education sector entities included in the report are the seven universities and eight grammar schools in Queensland, as well as the entities they control.

I remind everyone that today's briefing is a formal process of the parliament and parliamentary privilege applies to all evidence presented. Any person intentionally misleading the committee is committing a serious offence. I also advise that this briefing is being broadcast live via the Queensland parliament website. It will also be recorded and transcribed by Hansard. Once available, the transcript will be published on the committee's webpage.

I will now introduce the members of the Education and Innovation Committee. I am Rosemary Menkens, the member for Burdekin and the chair of this committee. With me are Mr Ray Hopper, deputy chair and member for Condamine; Mrs Yvette D'Ath, the member for Redcliffe; Mr Michael Latter, the member for Waterford; Mr Steve Bennett, the member for Burnett; Mr Mark Boothman, the member for Albert; and Mr Neil Symes, the member for Lytton.

Briefing us today are Mr Andrew Greaves, who is the Auditor-General, and Mr P Brahman, the Assistant Auditor-General. Mr Brahman, I understand your full name is easily mispronounced and it is your preference that we just call you Brahman. Although this hearing is public, you are able to request through me as chair that any material or information you provide be kept private. You can also object to particular questions. Additionally, you may wish to take questions on notice if you do not have that information at hand.

If it is okay with you both, we might leave any questions we have to the end of your briefing. If there is anything particularly sensitive, we could meet further on that. Gentlemen, I will now hand over to you.

Mr Greaves: Thank you very much, Chair. Thanks for the opportunity to present the results of our audits of the financial statements of education sector entities today. I will just give some brief contextual opening remarks and then hand over to Brahman to give you a summary of the findings of the report. Then, as you have suggested, we are then happy to take any questions the committee may have.

In terms of the context for this report, you are no doubt aware that all public sector entities prepare financial statements and have them audited each year by the Auditor-General, including universities and grammar schools. The universities and grammar schools do not have the standard 30 June year ended; they have 31 December year ended. So that is why the report is being tabled at this time.

We issue an audit opinion on the financial statements, and the audit opinion accompanying those financial statements is included in the annual reports of those entities that are then tabled in the parliament. As we do our financial audit and form our opinion on the financial statements, we have to consider a range of risks relating to whether or not there is fraud or error in those financial statements, and in considering those risks of fraud or error we also review and analyse aspects of the internal controls that these entities have established to prevent fraud or error or to detect it and correct it should it occur. So our financial audit is more than simply the opinion you see expressed and attached to the financial statements. It is also a review of internal control. As a part of our review, we also have to understand whether or not the entities we are auditing are what we call 'going concerns'—in other words, can they continue to meet their debts as and when they fall due, at least until the next time we express an audit opinion? So we have regard then to the financial state of affairs of the entities as we are undertaking our audit of the financial statements.

Any matters we find, we are obliged under our auditing standards to represent to those who are charged with governance of these entities—so the boards of the entities. We provide what we call management letters to them on the results of our reviews of their internal controls and any other significant financial reporting or accounting matters that we detect throughout our financial audits. So they have all been provided with essentially private reports from us to them which are not made public unless they, of course, wish to make those reports public.

In terms of discharging accountability to the parliament though, under the Audit Act, not only do we provide reports to each entity but the parliament requires that at least once each year I provide a report to it on the results of these financial audits, and the report we are talking about today is me discharging that accountability to the parliament. All we really are required to do under the act is talk about whether or not we issued an audit opinion and what the audit opinion was and any serious deficiencies that we may find in financial administration. The report that is before you today expands on that, and we actually do talk about the internal control issues that we have found to the extent that they would be systemic or systematic across the sector. We also report on what we term the financial sustainability of the entities within these sectors.

So that is the context of the report that we have tabled today. I will now ask Brahman to give you a high-level overview of the findings under each of those headings.

Mr Brahman: Firstly, I will cover universities followed by grammar schools. Overall, the financial performance of universities was sound, with clear audit opinions provided for the seven universities and their 20 controlled entities. This means they have prepared their financial statements in accordance with all their legislated requirements. All universities produced timely financial statements, with all entities being audit certified within the two-month legislated time frame. The quality of the draft financial statements they submit to us to be audited improved also, with the dollar value of errors identified by both audit and management in 2013 being significantly less than the previous year. This indicates that the quality assurance processes put in place by universities for the preparation of their financial statements are operating effectively.

The number of significant internal control weaknesses we identified this year increased from 24 issues in 2012 to 42 in 2013. The increase in control issues identified by us arose mainly from our in-depth reviews of controls over procurement and delegation, although IT access and security control weaknesses continue to be of concern.

In relation to procurement controls, we developed a checklist of better practice for supplier engagement, which is included in our report in appendix E, and we assessed universities against this better practice checklist. We found all universities could increase their use of preferred suppliers for significant purchases as well as increase their use of corporate cards for the purchase of low-risk lower value items. Both these practices could reduce time and cost for universities. In relation to delegation controls, we identified that all universities appropriately delegated expenditure approvals with more significant and higher value transactions delegated appropriately to more senior management.

In relation to the financial performance of universities, we calculated a number of key ratios each year, which helps us to make a financial risk assessment of each university and also allows us to comment on their future sustainability. All universities have been assessed as low-risk based on their historic performance and are in a sound financial position with relatively strong balance sheets and are able to pay their short term debts and obligations.

The grammar schools also received clean audit opinions and the timeliness and quality of their financial statements were generally satisfactory. However, Ipswich Grammar School did not meet the two-month legislative time frame, mainly due to problems identified by audit late in the financial statement preparation process. The number of internal control weaknesses identified across the eight schools had reduced in 2013—from 17 in the prior year to 12, which indicates signs of improvement.

In relation to their overall financial performance, most schools are in a sound position, but Ipswich Grammar School and, to a lesser extent, Ipswich Girls Grammar, need to continue to closely monitor their revenue and expenditure policies to ensure future sustainability. Ipswich Grammar recorded a loss of $1.4 million—the sixth year of losses in succession. It is also acknowledged that, in 2013, the result is a $1 million improvement on the prior year.

A long-running issue, which has been finally resolved in 2013, is the disclosure of key management personnel information in the school's financial statements. The Queensland Treasury and Trade policy requires all statutory bodies to disclose the position titles of all key management personnel as well as their remuneration details at the individual level. We have previously qualified all the grammar schools for the nondisclosure of this information, but we are now satisfied that full disclosure has been made in accordance with the policy requirement.

Mr Greaves: Thanks, chair. We are now happy to take any questions that the committee may have.

CHAIR: Thank you so much for that. That is certainly very positive for many of those entities. Brahman, I would just like to ask you a very broad-ranging question, but focusing on the grammar schools. Many of those grammar schools service rural areas. As we know, the rural areas have been going through severe drought and adverse economic circumstances. Would you have noticed that that could have any impact on any of the grammar schools, probably more so the regional grammar schools, from the perspective of maybe their numbers? Their revenue comes from the number of students. So it would be to do with the number of students and possibly even unpaid accounts?

Mr Greaves: Chair, I am happy to start answering that and Brahman may come in. In terms of student fee revenue at page 52 of the report, we have analysed at a macro sense the fee revenue for grammar schools, which is student fee revenue, which has accounted for about 60 per cent of their total revenues. What we have observed in the report is that all schools reported only marginal increase or decrease in student numbers. So we did not see any patterns of decline in any location, be it metro, regional or rural, in terms of student numbers. Therefore, the student revenue as an average across the sector has stayed fairly stable. You will see, of course, that the different schools have made a different fist then of the revenue versus their expenditure in terms of how they fared on their operating results. You can see at figure 3G on page 55 where we simply relate the operating result to the revenues. Some of them have had kind of a downward trend in their operating result, which means that their expenditure is effectively growing faster than their revenue is growing. The Brisbane Girls Grammar is the first one there in figure 3G where you can see that the trend is downwards, but more out in the regional it is a bit mixed. You can see these flat kind of trends and then downward trends. So it is fairly variable. But it does not seem from our higher-level analysis that revenue has been the major concern. We have not disaggregated it in the report by grammar school, but we are happy to do that and provide that information to the committee. The alternative, of course, is that this would be available in their annual reports—publicly available, anyway.

CHAIR: Thank you for that. As I say, it was a rather broad-ranging question. But it is possible it may have an impact. Do we have any further questions from the committee, which I am sure we do?

Ms D'ATH: Thank you. Mr Greaves, I am just interested in relation to Central Queensland University and its return to surplus this year. You talked about the early payment in relation to funding for the development of the dual sector entity. I am interested in your observations as to whether you believe that that surplus is a direct result of that early payment. Is the Central Queensland University at risk of falling back to a deficit once that has been expended?

Mr Greaves: Thanks very much. There are a range of answers to that seemingly simple question. I might start by first referring to what seems to be an issue for the university sector, which is that they do not like the way they have to record grants. You will see in a number of the universities' annual reports that they will not talk about their operating result; they will talk about an underlying result. So this is an artefact of the accounting standards, which requires you to record as revenue the year you get the grant, not the year you are going to spend the grant. So we do not try to match revenue with expenditure, as we did 20 or so years ago. That has moved on significantly. When you get control of the money and it is yours, it is then treated as revenue. This is why you will see some fluctuations in the financial statements of all public sector entities, because of the timing and flow of the grants. What we observed in this report is that that grant came in this year, or last year—2013—but, of course, most of the expenditure is going to be in subsequent years. So all we simply observe is that, if you took that grant out, then, obviously, the result would be less. From our perspective, that is not of a concern, because when we are looking at sustainability of these organisations we are more concerned about the longer-term trends and averages. So we would rather focus on what has the result been like over the last five years or the last 10 years.

So that then takes us to the analysis of their financial ratios that we have in the report. If you look at CQU in particular and some of the analysis I draw your attention to in the report, CQU was heavily involved in international student placements but had significant expenditure. They have changed their model. So their international student revenue has dropped dramatically at figure 2P as a percentage of their total operating revenues by design.

Ms D'ATH: Sorry, Mr Greaves. Can I just ask what page you are on?

Mr Greaves: On page 33 of my report, figure 2P. But if you then look at their expenditures, their expenditures are within the target range. Say, for example, of employee benefits, which makes up most of their expenditure—figure 2R on page 35—you will see that they were having a trending increase in salary expenditure as a percentage of total expenditure. They have now been able to bring that back.

The figure that tells us most about them, though, is their operating ratio, which is whether or not they make a surplus or a deficit and how that relates to their total revenue. At figure 2T on page 37 you can see that, for the last five years, it was deteriorating significantly. It has now increased for 2013, but a lot of that increase was that grant.

So if you then average that, you will see that there is still some work to be done, I would suggest, at CQU in getting their finances under control. However, the most recent signs are all improving. So the trends are improving—the current ratios. They do not have any debt on their balance sheet, which I think puts them in a sound position there. But, of course, not having any debt—and that debt figure is shown in figure 2V on page 39—they also are not replacing their assets as fast as they are depreciating, which is at figure 2X on page 41.

So as I said, it is a fairly complex answer to what seems to be a simple question. You have to look across a range of indicators to understand their total financial performance. That is why we analyse these different ratios, which are also analysed by the Australian government and by the state government. They are not ratios that we have invented; they are ratios that are looked at to understand and examine the financial sustainability of the sector.

I am not sure that there is a simple yes or no or right or wrong answer to your question. The trends in the most recent historic data that we have look positive. But, of course, as to the future risks, as auditors we are auditing historic data. We do not speculate or comment on future data, or forecasts.

CHAIR: That is interesting. Thank you for that. Of course, they have taken the proactive move of aligning with TAFE. Any more questions?

Mr BENNETT: If I could just ask in relation to procurement policies and practices that were obviously part of the review. With the changes that came out in 2013 to the State Purchasing Policy—and I notice some assessment in your report—do we see some conflict with the university policies and the State Purchasing Policy in trying to get some efficiencies of perhaps this outsourcing or contestable market issues that we use, particularly around, for example, the corporate credit cards? I notice that they are used for small-value transactions. I am just wondering if you see any conflict with the university's internal policies and the State Purchasing Policy?

Mr Greaves: There was none that were evident to me in conflict. There are basic procurement policies that they must comply with, as other state entities must comply with. Each year we would look at procurement generally to make sure that the goods and services that they are purchasing are legitimate and valid and that they pay the right amount for them. But every few years we will go into much more depth. But the focus of our in-depth review is more about what we term good practice, or better practice, not minimum or mandatory practice. So it is quite appropriate and compliant to use a credit card to purchase. We are not saying that they are not complying. But in the context of the credit card observation, our experience and our analysis tells us that you can extract more efficiencies in the cost of processing by procuring low-value, high-volume goods through credit card than going through a traditional procurement process. So we are simply saying that universities—and, in fact, other public sector entities—could be more efficient in the way they buy things and lower the transaction costs of procurement if they analysed their supplier base from a couple of perspectives: one, work out the strategic, important stuff that they buy and establish preferred supplier arrangements, and that is totally consistent with the direction of the procurement policy and the changes that are happening at the state level; but, two, leverage the use of credit cards for the low value, which would therefore be effectively what we call low-risk items and try to use that more and more to reduce that transaction costs.

So that is the flavour of the observations that we have in the report around procurement. We have basically said, 'Generally sound.' They were not always documenting plans, which were a requirement, for strategic procurement. The issue there is that they therefore cannot demonstrate transparently and accountably that they have considered all of these issues that had to be considered when they were going through a procurement. If you cannot demonstrate what you have done, it is hard then to defend that if it turns out not to be a value-for-money decision in the future. So we made some observations around needing to better document and be more transparent in the documentation of their procurement plans.

CHAIR: Any further questions? I am rather interested to know if you had any comments on the growing trend for open online courses, which probably do not bring a great deal of revenue back into the universities and whether, in the long term, from an auditor's perspective what effect this may have on the viability of those universities.

Mr Greaves: Thanks, chair. You have alluded to one type of online learning, which is generally described these days as massive open online courses—or MOOCs to give it the acronym. The advent of MOOCs is certainly a recent phenomenon, but a growing phenomenon, a worldwide phenomenon. We examine things like MOOCs and online learning through a financial audit lens, basically, in terms of future financial risk. What is happening is that a lot of universities have been providing online courses for a number of years to their students, but this now becomes kind of a competition risk, because these MOOCs, in particular by very prestigious universities around the world, are being offered and at this stage they are being offered for free largely, although you can now start paying a small fee to get a diploma issued. So we are in very early days of MOOCs and we are simply saying to universities, 'That presents a long-term financial risk, because, one, you will be investing in infrastructure if you want to be in the MOOC game, or, in fact, in your online learning area without necessarily a revenue return, a revenue stream. So you may have to, in fact, make some strategic investment decisions in something like MOOCs that do not return you a dollar, but cost you money and, whether it is going to return you a dollar, I guess the case is still out.' So we are not really sure where this is going. So we are simply, as part of our review of the financial sustainability of the education sector, trying to understand what these key future financial risks are. Because each university is required under the financial management act to manage their financial risks, including their emerging financial risks, this is something that we then look at.

As we say in the report, the approach to MOOCs has been variable within the Queensland context. Some of them are starting to and have signed up to some of these broad international partnerships. Others have not really started approaching the issue as much. So I think that would be certainly something that the committee, if it was interested, in talking to the actual vice-chancellors and to the universities themselves about how they see this as a future risk for them and where they might be going with MOOCs.

CHAIR: I understand in some cases that those courses may be lower-level courses, perhaps designed to be the hook to encourage students to go further. But I am not sure exactly how that is working at this stage.

Mr Greaves: I am not an expert in it either. I am not sure that anyone is an expert at the moment. I think it is really a new and emerging area. As I said, it is developing. I have seen it represented as a way to hook potential students and then get them to enrol in actual courses delivered by the university. You can see that there is a blurring between the online offering to the actual students enrolled in that university and the MOOC offering. So it could go that way. It is really at this stage fairly early. It is simply something that we will track with the universities over time and if something crystallises as a significant risk then we will pay much more attention to it as auditors from that point forward.

CHAIR: Thank you for that. Did we have any further questions? Thank you so much. You seem to have satisfied all of the committee very much. I thank you so much for your time and for also for this very interesting briefing. This brings to a close this public briefing on the Auditor-General's report No. 16 for 2013-14, *Results of audit: education sector entities 2013.* I thank you both very much for your time this morning. The information you have provided will greatly assist our deliberations. Subscribers to the work of this committee will automatically be emailed updates about the committee's consideration of the Auditor-General's report and, of course, the outcome. Subscribers will also be advised if the committee decides to seek public comments on the issues raised in the report. I therefore urge those who have not already done so to subscribe to the committee's email subscription list via the Queensland parliament's website. Could I thank you both, Mr Greaves and Mr Brahman. I now declare this briefing closed. Thank you.

Committee adjourned at 10.04 am