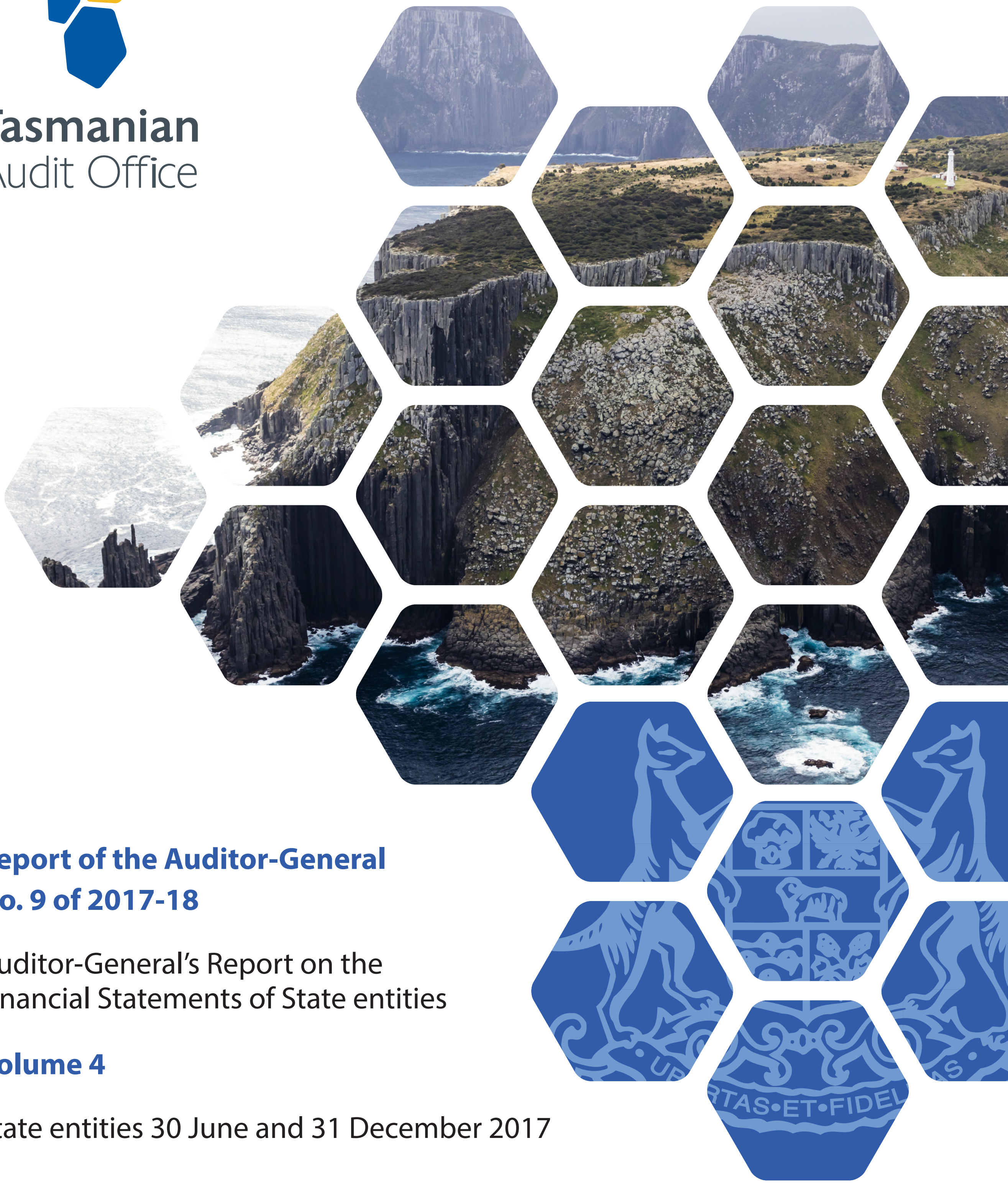
Tasmanian
Audit Office



Report of the Auditor-General
No. 9 of 2017-18

Auditor-General's Report on the
Financial Statements of State entities

Volume 4

State entities 30 June and 31 December 2017

June 2018

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THE ROLE OF THE AUDITOR-GENERAL

The Auditor-General's roles and responsibilities, and therefore of the Tasmanian Audit Office, are set out in the *Audit Act 2008 (Audit Act).*

Our primary responsibility is to conduct financial or 'attest' audits of the annual financial reports of State entities. State entities are defined in the Interpretation section of the Audit Act. We also audit those elements of the Treasurer's Annual Financial Report reporting on financial transactions in the Public Account, the General Government Sector and the Total State Sector.

Audits of financial reports are designed to add credibility to assertions made by accountable authorities in preparing their financial reports, enhancing their value to end users.

Following financial audits, we issue a variety of reports to State entities and we report periodically to the Parliament.

We also conduct performance audits and compliance audits. Performance audits examine whether a State entity is carrying out its activities effectively and doing so economically and efficiently. Audits may cover all or part of a State entity's operations, or consider particular issues across a number of State entities.

Compliance audits are aimed at ensuring compliance by State entities with directives, regulations and appropriate internal control procedures. Audits focus on selected systems (including information technology systems), account balances or projects.

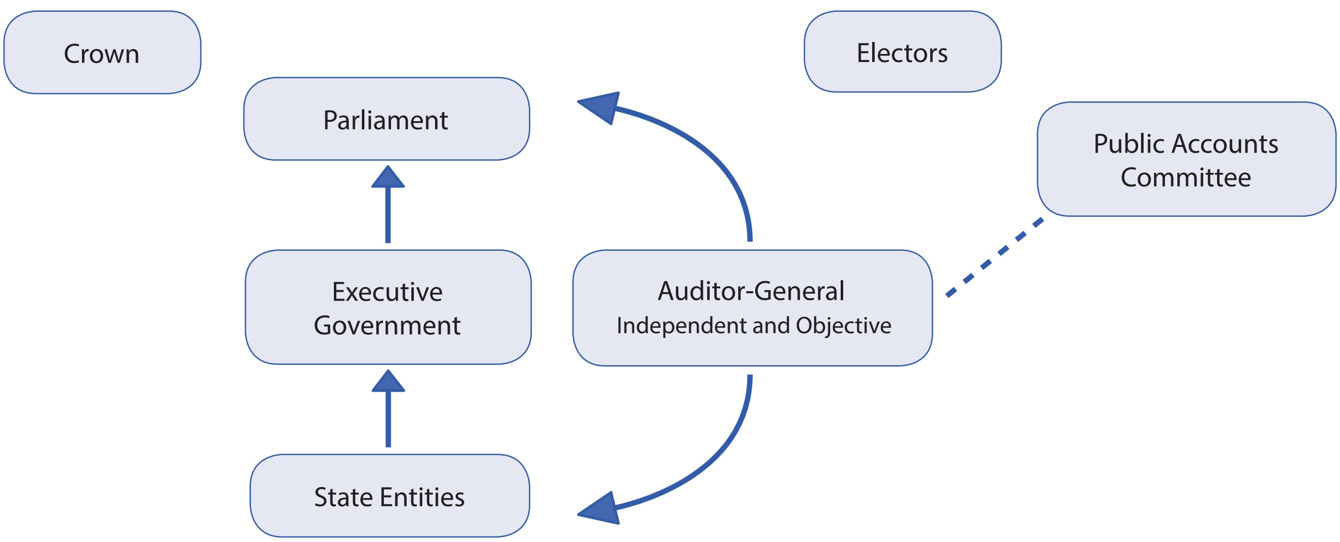
We can also carry out investigations but only relating to public money or to public property. In addition, the Auditor-General is now responsible for state service employer investigations.

Performance and compliance audits are reported separately and at different times of the year, whereas outcomes from financial statement audits are included in one of the regular volumes of the Auditor-General's reports to the Parliament normally tabled in May and November each year.

Where relevant, the Treasurer, a Minister or Ministers, other interested parties and accountable authorities are provided with opportunity to comment on any matters reported. Where they choose to do so, their responses, or summaries thereof, are detailed within the reports.

The Auditor-General's Relationship with the Parliament and State Entities

The Auditor-General's role as Parliament's auditor is unique.



2018 (No. 2)

2018
PARLIAMENT OF TASMANIA

Report of the Auditor-General
No. 9 of 2017-18

Volume 4
State entities 30 June and 31 December 2017

June 2018

Presented to both Houses of Parliament in accordance with the requirements of Section 29 of the *Audit Act 2008*

Auditor-General's reports and other reports published by the Office can be accessed via the Office's website. For further information please contact:

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12 June 2018

President
Legislative Council
HOBART

Speaker
House of Assembly
HOBART

Dear President
Dear Speaker

Report of the Auditor-General No. 9 of 2017-18, Auditor-General's Report on the Financial Statements of State entities, Volume 4 – State entities 30 June and 31 December 2017

In accordance with the requirements of Section 29 of the *Audit Act 2008*, I have pleasure in presenting my Report on the audit of the Financial Statements of State entities, Volume 4 - State entities 30 June and 31 December 2017.

Yours sincerely

Rod Whitehead
Auditor-General

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EXECUTIVE SUMMARY

INTRODUCTION

This Report is the fourth and final volume in our series advising Parliament on the outcome of our financial audits for 2016-17 and the 2017 calendar year and it includes summaries relating to:

- the timeliness of financial reporting
- audit opinions on financial statements
- audit findings
- audits dispensed with
- setting audit fees for financial audits.

This Report also includes Chapters on:

- developments in financial reporting and auditing
- public sector readiness for developments in financial reporting
- an assessment of Agency audit committees.

STATE ENTITIES COVERED BY THE REPORT

This Report contains a Chapter for the University of Tasmania (University) and its controlled entities; University of Tasmania Foundation Inc (University Foundation), AMC Search Limited (AMC Search) and the Tasmanian University Union Inc (TUU). It also includes a summary Chapter for other 31 December 2017 State entities; ANZAC Day Trust, the Solicitors' Trust and the Theatre Royal Management Board.

The University and the other 31 December 2017 entities included in this Report submitted their financial reports within the statutory deadline apart from the Solicitors' Trust. The audits were completed satisfactorily and unqualified opinions issued in all instances.

The Report also covers the 30 June 2017 audit of River Clyde Trust. River Clyde Trust failed to meet the statutory deadline for the submission of its 30 June 2017 financial statements. This was the third consecutive year it failed to meet this deadline.

SUBMISSION OF FINANCIAL STATEMENTS AND TIMELINESS OF AUDIT OPINION

Compliance with the 45 days statutory deadline for submission of financial statements declined in the 2017 audit cycle compared to the 2016 audit cycle. Seven State entities failed to comply with the requirement compared to two entities the year before.

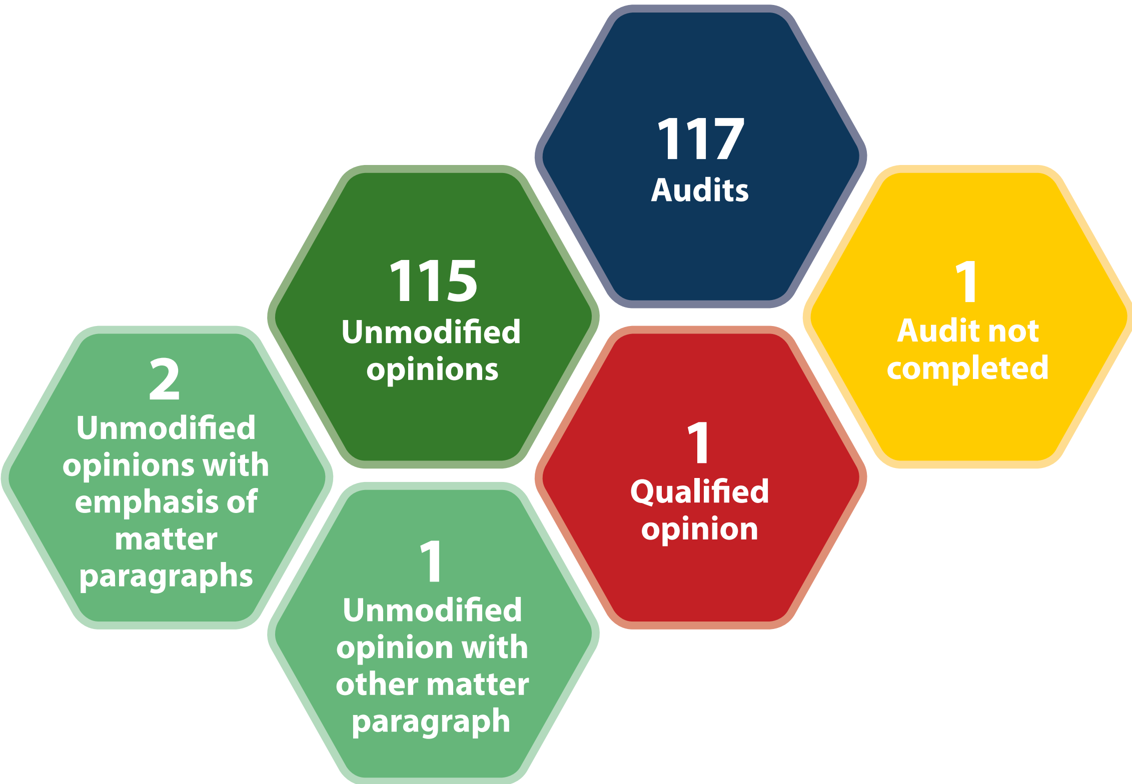
Our compliance with the requirement to complete audits of financial statements within 45 days of their receipt also declined from 2016. Seven audits were completed outside the time required, compared to one audit in the 2016 audit cycle.

Copping Refuse Disposal Site Joint Authority (Copping) submitted financial statements on 8 August 2017. A disagreement with Copping as to whether it was a for-profit or not-for-profit entity and whether it had control of the C Cell Unit Trust resulted in the audit not being completed within 45 days from the date of submission of the statements. On 15 February 2018, Copping withdrew the financial statements originally submitted, with revised financial statements submitted on 9 May 2018. As at the date of this Report the audit had not been completed.

The disagreement with Copping contributed to delays in finalising the audits of the four owner councils of Copping within the 45 day deadline.

Financial statement audits of all State entities, excluding Copping, for the years ended 30 June 2017 and 31 December 2017 have been completed.

AUDIT OPINIONS ON FINANCIAL STATEMENTS



We issued unmodified audit opinions on all financial statement audits completed during the 2017 audit cycle, except for the National Trust Australia (Tasmania).

National Trust of Australia (Tasmania)	The Trust possesses certain heritage collections, but not all of these assets were recognised. Due to the nature of the assets, we were unable to quantify the financial effect.

Two of the unmodified audit opinions contained an emphasis of matter paragraph.

Forestry	Emphasis of matter paragraph drew attention to a note which described Forestry's application of Treasurer's Instruction GBE-08-52-08P in respect of an exemption from application of the requirements of Australian Accounting Standard AASB 5 *Non-current Assets Held for Sale and Discontinued Operations*.
Tascorp	Emphasis of matter paragraph drew attention to a note which described Tascorp's application of Treasurer's Instruction GBE-08-051-08P in respect of $730.40m received from the Tasmanian Government on 29 June 2017 for the establishment of the Mersey Community Hospital Fund.

One unmodified audit opinion contained another matter paragraph.

West Coast Council	The other matter paragraph drew attention to West Coast Council failing to disclose overnight recreational vehicle parking and camping services as a significant business activity as required by the *Local Government Act 1993*. The disclosure was not made on the basis that Council disagreed with the findings of the Regulator and disputed that it provided any services at all.

FINDINGS FROM 30 JUNE 2017 AND 31 DECEMBER 2017 AUDITS

2017		2016	
187	**119**	**209**	**85**
Audit matters raised	Audit matters raised in prior periods assessed as unresolved	Audit matters raised	Audit matters raised in prior periods assessed as unresolved

We report deficiencies in internal controls, matters of governance interest and unresolved issues identified during our audits to management and those charged with governance of State entities. We do this through management letters, which include our observations, related implications, recommendations and risk ratings. For the 2016-17 audit cycle:

- 187 matters were raised
- there were 16 high risk findings, 91 moderate risk findings and 80 low risk findings
- the majority of matters raised related to the valuation of non-current physical assets, corporate governance and information systems
- 40% of issues previously reported remained unresolved in 2017, which included two high risk issues that were over 12 months old.

AUDIT DISPENSED WITH

The Auditor-General has the authority to dispense with the audits of State entities, but must consult with the Treasurer prior to exercising such dispensation. Audits are dispensed with on the condition the entity demonstrated appropriate financial reporting or the entity was controlled by a State entity and the financial transactions and balances of the controlled entity were subject to audit procedures as part of the group audit of the controlling entity.

In 2016-17, 47 (2015-16, 39) audits were dispensed.

BASIS FOR SETTING AUDIT FEES

Fees for financial audits are determined by the Auditor-General pursuant to Section 27 of the Audit Act. Fees are set for each State entity commensurate with the size, complexity and risks of the engagement. Charge rates for Tasmanian Audit Office (TAO) audit staff are based on the principle of the Office being able to recover its costs of operation. Charge rates comprise of two parts, direct salary cost and overhead recovery.

Where circumstances surrounding an audit engagement have materially changed, additional audit fees may be sought from the State entity.

For 2017-18 financial year audits, the adjustment to fees was:

- 2.5% – 4.0% for General Government Sector entities
- 6.0% for Local Government Authorities
- 4.0% for Government Businesses.

This increase was primarily based on salary increases in the *2016-2018 Public Sector Union Wages Agreement* and as such reflects that employee costs are the main driver of our costs. The higher increase for local government audits was caused by the need for the Office to mitigate losses incurred across all audits within this sector.

DEVELOPMENTS IN FINANCIAL REPORTING AND AUDITING

This Report includes a Chapter summarising developments in financial reporting and audit requirements. Topics covered include:

- financial reporting in the public sector
- financial reporting developments for 2017-18
- financial reporting developments for financial years after 2017-18
- financial audit developments.

PUBLIC SECTOR READINESS

All entities will need to understand and report how and to what extent they will be impacted by ever changing accounting standards. We looked at the three key upcoming changes in accounting standards that included:

- Revenue (AASB 15 and AASB 1058)
- Financial instruments (AASB 9)
- Leases (AASB 16).

As part of the review we assessed selected entities' disclosures in two parts, the understanding of the nature of change and discussion of the impact on the financial statements.

We found that while a few entities presented disclosure of future accounting standard impacts well, there were quite a number of instances where there appeared to be a lack of understanding of future accounting standard impacts, a level of non-engagement by clients in assessing the impacts and a lack of adequate detail in some of the disclosures with short inadequate comments. This was evident in some disclosures where the accounting standards quoted were incorrect, did not apply to that entity type, had already been applied or didn't actually need to be included.

All entities need to be cognisant that disclosure requirements for pending accounting standards requires more than just a listing those that are relevant. In order to comply with these requirements, entities need to ensure they are fully informed and understand the effects of each new standard.

An observation that is evident from this review is that many entities need to revisit and complete a revised assessment of the potential impacts of pending accounting standards.

AGENCY AUDIT COMMITTEES

Audit Committees play a key accountability role in the governance framework of Tasmanian public sector agencies. While management retains ultimate accountability for operations, the Audit Committee should independently review and assess the effectiveness of key aspects of an Agency's operations.

Our review assessed the Audit Committees' composition, operational arrangements and the roles and responsibilities of the Committee in the Agency, as documented in the Audit Committee's current charter. The review was performed against the requirements of Treasurer's Instruction TI 108 *Internal Audit* (the Treasurer's Instruction) and better practice guidance, specifically, the Australian National Audit Office's *Public Sector Audit Committees: Independent assurance and advice for Accountable Authorities* (the ANAO better practice guide).

The review found there is significant room for improvement in the governance arrangements of the Audit Committees of the Agencies reviewed. Audit composition is the most critical area that should be addressed to ensure independence as it was found that Audit Committees generally do not have a majority of independent members, an independent Chair and several instances where members held management positions in the Agency that create potential conflicts of interest.

As a result of this review several recommendations have been made that include both amendments to the Treasurer's Instruction and improvements to the Agencies' Audit Committee charters.

Recommendations

Recommendation 1

The Treasurer's Instruction is amended to ensure the composition of the Audit Committee supports an adequate level of independence to meet the required functions. The required composition should include:

- the appointment of an external chair
- the majority of members are independent/external
- regular rotation of Audit Committee membership.

Recommendation 2

The Treasurer's Instruction is amended to include the following requirements:

- Audit Committee Charters are reviewed and, where necessary, updated on an annual basis
- Audit Committee's commission an annual assurance map.

Recommendation 3

Audit Committee Charters are amended to include the following roles and responsibilities in relation to engagement with external audit:

- have a members-only meeting with the TAO at least once per year so that the committee can obtain the views of the TAO without internal audit or management being present
- periodically review the performance of external audit, and report the results to the Accountable Authority.

Recommendation 4

The Treasurer's Instruction is amended to include reviewing financial reporting responsibilities and the financial report as a role in the Audit Committee's oversight function.

Audit Committee Charters are more specific on the role of the Audit Committee in reviewing financial reporting responsibilities and the financial report.

Recommendation 5

The Treasurer's Instruction is amended to include reviewing performance reporting responsibilities as a role in the Audit Committee's oversight function.

Audit Committee Charters include oversight of performance reporting as part of their roles and responsibilities.

Recommendation 6

The Treasurer's Instruction is amended to include oversight of the Agency's risk management function as a responsibility and as a role of the Audit Committee.

Recommendation 7

Audit Committee Charters include oversight of the Agency's responsibility to manage the exposure to fraud risk in order to ensure that the Audit Committee complies with the Treasurer's Instruction.

Recommendation 8

It is recommended that the Treasurer's Instruction expands the oversight functions of the Audit Committee around the system of internal control to include:

- oversight of the Agency's system of internal control in order to ensure that the Audit Committee complies with the Treasurer's Instruction
- oversight of the Agency's systems for monitoring legislative and policy compliance
- promotion of ethical and lawful conduct
- obtaining an annual report from Internal Audit on the overall controls of the Agency
- business continuity management
- delegations
- ethical and lawful conduct.

UNIVERSITY OF TASMANIA

INTRODUCTION

The University was established in 1890 and is the fourth oldest university in Australia. It has campuses within the three main regions of the State: Hobart in the south, Launceston in the north and Burnie in the north-west. The University is organised into five Colleges: College of Arts, Law and Education, College of Health and Medicine, College of Sciences and Engineering, Tasmanian School of Business and Economics and University College.

KEY RESULTS AND DEVELOPMENTS

$679m	$620m	($7m)	$59m
Total income	Total expenses	Underlying result	Net result

The University incurred an Underlying deficit of $6.58m for 2017 compared to an Underlying deficit of $17.57m in 2016. The lower Underlying deficit was mainly attributed to an increase in user charges and fees of $31.56m, partially offset by higher employee related expenses of $10.85m and consultancy and advisory services and other expenses of $11.00m

Australian Government operating grant funding of $425.49m was 46.0% of total revenue compared to 50.0% for the prior year.

For 2017, expense categories as a percentage of total operating expenses were relatively consistent (within 1.0%) with last year's percentages.

Employee costs were the largest component of expenditure in 2017 at $361.12m, which was $6.91m (excluding restructure costs) higher compared to 2016. Academic salary costs were $187.96m (30.0% of operating expenses) and non-academic salary costs were $173.16m (28.0% of operating expenses).

Other significant operating expenses included scholarships and prizes, $27.90m, consultancy and advisory services, $31.87m, research sub-contractors, $19.49m, travel and staff development, $18.70m and consumables, $13.17m.

The University's Net result for the year was a surplus of $58.93m compared to a surplus of $14.93m in 2016.

Net investment returns from the University's investment portfolio were $33.51m (2016, $18.34m) with the net return on the average investment portfolio for the year being higher in 2017 at 8.3% (2016 at 5.2%).

The Tasmanian and Australian Government provided capital funding of $10.00m towards the Northern Transformation project and $13.00m for the Hedberg Centre.

3.4	:	1	1.3	:	1
Domestic student load		International student load	Academic staff		Non-academic staff

Total student EFTSL (equivalent full time student load) increased by 689 students in 2017, or 3.3%, which was a lower growth than in 2016 (1 160 students or 5.9%). Domestic students decreased by 20 EFTSL to 16 767 EFTSL, a decrease of 0.1% from the previous year (2016, 5.1%). Fee paying overseas and off-shore student numbers increased by 708 EFTSL to 4 970 EFTSL, an increase of 16.6% from the previous year (2016, 9.1%).

Fees and charges increased by $26.97m, mainly due to the higher onshore fee paying overseas students which increased 27% from the prior year. The main growth was recognised in Tasmanian School of Business and Economics enrolments, up 62%, College of Health and Medicine, up 25% and College of Sciences and Engineering, up 10%.

Full Time Equivalent (FTE) staff numbers over the past four years remained consistent, marginally increasing from 2 410 at the end of 2013 to 2 426 at 31 December 2017. Academic staff numbers decreased by 17 to 1 056 FTEs in twelve months to 31 December 2017. Non-academic numbers decreased by 8 FTEs to 1 370 over the same period.

$478m	$462m	$94m	$90m
Land and buildings	Cash and investments	Borrowings	Employee provisions

The University's Net assets increased by $0.75m reflecting the Net result for the year of $58.93m less the net decrement on revaluation of assets, $58.13m.

Property, plant and equipment represented 46.3% of total assets and were valued at $603.65m at 31 December 2017. Significant changes in the value of Property, plant and equipment from 31 December 2016 were:

- additions totalling $59.77m
- revaluation decrements of $58.13m primarily related to the revaluation of the Newnham and Burnie campuses
- the transfer of $143.51m from land and buildings to the service concession purpose built student accomodation asset
- $9.56m carrying value of assets disposed, which included the Conservatorium of Music and surrounding properties
- Depreciation charges of $28.80m.

Capital expenditure during 2017 totalled $59.77m and included $20.07m for the student accommodation development in Melville Street, Hobart, which was commissioned in February 2017 and $10.94m for the Hedberg Centre.

Capital projects totalling $106.90m were completed during the year and capitalised as buildings and plant and equipment. Significant completed projects included:

- student accommodation facility at Melville Street, Hobart, $86.35m
- purchase of the Red Cross land and building at 40-42 Melville Street, $8.00m
- an innovative new autonomous underwater vehicle at Australian Maritime College, $5.16m.

Capital projects in progress at 31 December 2017 totalled $30.44m with the most significant project being the Hedberg Centre, $21.41m.

Cash, short and long-term investments totalling $461.62m represented 35.4% of total assets at 31 December 2017. Cash and cash equivalents and Investments increased by $24.55m and $131.26m respectively as at 31 December 2017, primarily due to $132.61m received as part of the Purpose Built Student Accommodation transaction. Investments also increased due to unrealised gains of $17.52m.
The University had a deficiency in working capital of $60.02m at the end of 2017, (2016, $91.01m). This was not considered a concern as investments (classified as non-current assets) could be redeemed to cover any potential working capital deficiency.
Funding was received from the Australian Government based on estimated student enrolments and associated courses, with actual enrolments confirmed post year-end. It was estimated that $13.80m (2016, $22.48m) was repayable due to differences in estimated and actual student enrolments. The amount payable included funding received in 2017 and prior years.
Borrowings obtained from the Tascorp under a Master Loan Facility Agreement were $93.60m at 31 December 2017, a reduction of $9.50m from the prior year. Borrowings related to the construction of student accommodation facilities.
Employee related provisions totalled $89.91m at 31 December 2017, which was consistent with prior year, with an increase of only $2.08m.
The Building sustantiability ratio has declined to 33% in 2017. This is the result of the University investing in new buildings to replace existing buildings. As a result the capital maintenance spending has reduced on existing buildings that will not be required in the future.

AUDIT FINDINGS

In performing our audit we did not identify any significant deficiencies in internal control and no high risk audit findings were identified during the course of the audit. We identified one moderate risk finding related to the University's depreciation policy for buildings.

BACKGROUND

The University is governed by the University Council (the Council) established under the *University of Tasmania Act 1992*. The Council has responsibility for high-level strategic direction, major financial planning, monitoring management performance and compliance, staff appointments and the allocation of funds.

The Council delegates broad powers to the Vice-Chancellor (the managerial and academic leader) to manage the operations of the University in conformity with agreed plans, principles and policies. The Vice-Chancellor, in turn, empowers other members of the Senior Management Team.

The financial report comprises the financial statements of the University, being the parent entity, and the following entities that were controlled by the University during the year and made up the consolidated entity:

- University Foundation
- AMC Search
- TUU
- UTAS Holdings Pty Ltd (UTAS Holdings)
- Sense-Co Tasmania Pty Ltd (Sense-Co)

The results reported in this section of the Chapter related to the University's consolidated financial performance and position. The University Controlled Entities section of the Chapter includes financial results of the controlled entities.

The University reports on a calendar year basis and therefore the financial results related to the year ended 31 December 2017.

The University operated in an environment influenced by the following:

Purpose Built Student Accommodation

The University executed a market transaction with the Spark Living Consortium in relation to its Purpose Built Student Accommodation (PBSA) during 2017. This was part of the University's strategy to monetise PBSA assets to provide the capacity to pay down debt and fund future infrastructure investments. The arrangement represents a public service as student accommodation contributes to the University's primary objective of providing an education.

The University has recognised a service concession asset of $143.51m for the buildings and in exchange for the receipt of an up-front amount of $132.61m, a grant of right to operate (GORTO) liability of $132.61m. The liability will be amortised over the 30 year life of the agreement, where, upon completion, the University will retain all PBSA assets.

Major capital projects

The National Rental Affordability Scheme (NRAS) project at Melville Street in Hobart was completed in early 2018 and an amount of $85.56m was commissioned.

The University commenced the construction of its new performing arts centre, the Hedberg Centre, in late 2016. The development is a partnership between the University, the Tasmanian Government and the Theatre Royal Management Board and will house the Tasmanian Conservatorium of Music and the Creative Exchange Institute, which will focus research on performance, design and creativity. The new facility is expected to be completed during 2019 and is estimated to cost $90.00m. A total of $21.41m has been spent on the Hedberg Centre as at 31 December 2017.

University transformation projects

The University has secured $300.00m to deliver new campuses in Launceston and Burnie, with $150.00m support from the Commonwealth Government and a further $75.00m from the State Government. The planning for the new campuses at Inveresk and West Park is underway, with construction activities expected to commence in 2018.

Future of higher education reform

In December 2017, the Federal Government made a number of announcements in the 2017-18 Mid-Year Economic and Fiscal Outlook which will impact funding arrangements for universities. From 2018 the Government will cap the amount of funding it pays for bachelor courses. In 2018 and 2019 the cap will be set at a level of funding provided in 2017. From 2020 onwards, Government funding will grow in line with national 18 of 64 year old population growth if certain performance requirements are achieved. The performance indicators will be subject to consultation with the sector in 2018 and may relate to improvements in student attrition, low socioeconomic status participation and workforce preparedness of graduates.

AUDIT RESULTS

Key matters considered during the audit

Land and buildings

The University's land and buildings are recognised at fair value based on an independent market valuation performed by external experts. The valuation is impacted by the specialised nature of some of the buildings. In addition, the University carried a significant capital work in progress balance at balance date.

The calculation of depreciation includes estimation of useful lives which involves a high degree of subjectivity. Changes in useful lives can significantly impact the depreciation charged.

The University has targeted a number of land and building for disposal at its Sandy Bay Campus. Some of these buildings have been leased back by the University.

To address identified audit risks we performed the following audit procedures:

- testing, on a sample basis, additions and disposals throughout the year
- assessing depreciation expense
- challenging management's assessment of useful lives of buildings
- reviewing recent valuations for the Newnham and Burnie campuses
- following up on the matter concerning ownership of land at Burnie campus
- assessing the adequacy of relevant disclosures in the financial report
- ensuring the accounting treatment for the purpose built student accommodation transaction complied with AASB 1059 *Service Concession Arrangements: Grantors*
- confirmed with the Australian Government Department of Education and Training that the early adoption of AASB 1059 was permitted.

Capital expenditure program

The University continued to undertake significant strategic infrastructure investment and maintenance expenditure. Significant building projects under construction during the year included the NRAS project at Melville Street, Hobart, the Hedberg project, and the campus relocation projects in Launceston and Burnie.

The capital expenditure for 2017 amounted to $59.77m.

To address identified audit risks we performed the following audit procedures:

- testing the appropriateness of capitalisation of costs
- verifying capital work-in-progress during the year and at year end
- reviewing allocation between interest capitalised and expensed
- testing the appropriateness of the timing of capital project conversion to depreciable assets
- reviewing the disclosure of future capital commitments.

Investment portfolio

At 31 December 2017 the University held $403.46m in investments with a large portion of this balance managed by an investment manager. Investments were held in 21 unlisted managed funds (80.9%), 2 direct equity portfolios (9.2%) and cash deposits with banks (9.9%). The majority of unlisted funds were invested in Australian and international listed equities or listed equity derivatives, with some investments in Australian and international fixed interest/hybrid funds.

All managed funds prepared audited financial statements at 30 June 2017, and the majority of funds provided auditor reports on the design, implementation and operating effectiveness of controls around investment management services for the year ended on that date. As the University has a calendar year balance date, additional audit procedures were undertaken to cover the period from 30 June 2017 to 31 December 2017.

In addition, the University held a direct investment in an unlisted public company, Education Australia Limited which was valued at $16.17m at 31 December 2017.

To address audit risks associated with investment balances we completed the following audit procedures:

- reviewing the contract between the University and Pitcher Partner Investment Services Pty Ltd (PPIS) so as to understand the rights and obligations of each party
- reviewing and evaluating the monitoring controls exercised by the University over the performance of PPIS
- obtaining a confirmation from PPIS as to their controls over the existence, completeness and valuation of assets under their management

- obtaining direct from the managed funds:
  - audited financial statements for the managed fund for the latest financial year
  - confirmation of units held by the University at 31 December 2017 and unit valuation at that date
  - Auditor Control Reports on the design, implementation and operating effectiveness of controls at the managed fund
  - confirmation that existing (and any new) controls are still operating effectively from the date of the last Auditor Control Report to the date of the confirmation
- assessing the University's methodology for calculating the value of the direct investment held with Education Australia Limited
- assessing the adequacy of disclosures relating to investments.

FINANCIAL ANALYSIS

Financial snapshot 2017

Figure 1 provides a snapshot of the University's financial results for 2017 in comparison to prior years.

Figure 1: University of Tasmania Financial Snapshot 2017

	2017		2016		2015		2014	
	$'000s	Ind	$'000s	Ind	$'000s	Ind	$'000s	Ind
Financial Performance								
Total Australian Government financial assistance	425 489	●	420 249	●	406 726	●	393 525	▲
Employee related expenses	371 593	●	360 747	▼	336 727	●	324 912	▼
Reconciliation from underlying result to net result								
Underlying result	(6 575)	▲	(17 573)	▼	(11 981)	▲	(24 663)	▼
Net investment revenue	33 511	▲	18 342	▼	24 668	▲	19 720	▼
Capital income	13 959	▲	10 831	▲	5 776	▼	6 672	▼
Capital grants received	13 116	▲	6 672	▼	10 550	▲	0	●
Net movement in unspent research grants	4 918	▲	4 013	▼	6 532	▲	4 272	▲
Commonwealth grant scheme and HECS adjustments	0	▼	2 776	▲	(7 109)	▼	(1 862)	▼
Impairment expense and loss on disposal	0	▲	(10 127)	●	(10 268)	▼	(446)	▼
Gain(Loss) on disposal of assets	0	●	0	▲	(9 250)	▼	0	●
Net result for the year	58 929	▲	14 934	▲	8 918	▲	3 693	▼
Total comprehensive income	753	▼	11 736	▼	17 520	▲	3 351	▼
Financial position[1]								
Investments	419 633	▲	288 375	●	279 864	●	276 471	▲
Property, plant and equipment	603 651	▼	783 869	▲	745 636	▲	688 066	▲
Service concession asset	143 512	▲	0	●	0	●	0	●
Borrowings	(93 600)	▲	(103 100)	▲	(118 600)	▼	(95 601)	●
GORTO liability	(132 608)	▼	0		0	●	0	●
Employee provisions	(89 913)	●	(87 833)	▼	(79 308)	●	(80 095)	●
Net assets	912 318	●	911 565	●	899 829	●	882 309	●

	2017		2016		2015		2014	
	$'000s	Ind	$'000s	Ind	$'000s	Ind	$'000s	Ind
Key financial ratios								
Operating margin	0.99	●	0.96	●	0.98	●	0.96	●
Own source revenue	43.7%	▲	39.7%	●	39.8%	●	40.3%	▼
Liquidity ratio	1.70	▲	0.76	▼	1.13	▼	1.69	▼
Self-financing ratio	5.5%	▼	7.1%	▲	4.5%	▼	5.7%	▲
Debt to equity	10.3%	●	11.3%	▲	13.2%	▼	10.8%	●
Building sustainability	33.8%	▼	62.9%	▼	106.0%	▲	100.0%	▼

Indicators: ▲ *improvement from prior year* ▼ *deterioration from prior year* ● *no material change from prior year*

[1]Assets are positive, liabilities are negative

UNIVERSITY CONTROLLED ENTITIES

Entities included in this section are:

- The University Foundation is an incorporated association which acts as trustee for the University of Tasmania Foundation Trust. It raises money to endow scholarships, support research and build resources, while developing links between the University, industry and the community.
- AMC Search Ltd is a company limited by guarantee which provides maritime training and consulting services.
- The TUU is an incorporated association established in 1899 and is the body of student representation for tertiary students attending the University. Under AASB 10 *Consolidated Financial Statements*, the University satisfies the definition of control and has consolidated the TUU since 2014.
- UTAS Holdings is a company limited by shares. The company was registered 15 August 2014 and established to act as a holding company for commercialisation activities of the University. The company did not trade during the year ended 31 December 2017.
- Sense-Co is a company limited by shares. The company was registered 19 August 2014 and established to focus on the commercialisation opportunities of sensing technology. The company is a wholly owned subsidiary of UTAS Holdings Pty Ltd. The company did not trade during the year ended 31 December 2017.

KEY RESULTS AND DEVELOPMENTS

University Foundation
The University Foundation recorded a Net surplus of $5.01m in 2017 (2016, $6.34m).
Total revenue in 2017 was $10.70m (2016, $12.09m), which mainly comprised donations, bequests and a University transfer of $4.85m (2016, $8.29m), and investment income of $4.34m (2016, $2.63m). The decrease in the revenue is mainly due to donation of $2.60m received from Warren Endowed Chair in 2016.
Total expenditure in 2017 was $5.69m (2016, $5.75m). The Foundation's main expenses were scholarships, bursary and other payments $4.16m (2016, $4.49m) which fluctuate from year to year depending upon fund availability or decisions when to offer scholarships and grants, and other expenses of $1.53m (2016, $1.26m) which remain consistent.
Net assets were $58.75m at 31 December 2017 (2016, $53.75m).

AMC Search
AMC Search recorded a Net Loss of $0.49m in 2017 (2016, $1.66m Net Surplus).
Net assets were $4.74m at 31 December 2017, down from $5.24m in 2016.
Total revenue in 2017 was $8.90m, down from $10.08m in 2016, and total expenditure was $9.39m, up from $8.42 in 2016.
The Pacific Patrol Boat Contract with the Department of Defence was extended until July 2019 for the second of three possible contract extension periods.
AMC Search purchased a total of $3.17m in goods and services from UTAS compared to $2.10m in 2016. This was due to the inclusion of a management fee payable to UTAS by AMC Search.
TUU
TUU recorded a Net surplus of $0.32m in 2017 (2016, $0.51m).
Total revenue in 2016 was $2.29m (2016, $2.58m), which mainly comprised student services and amenities fee (SSAF) funding of $0.90m (2016, $1.23m), and baseline funding of $0.48m (2016, $0.47m), both of which were received from the University in accordance with an annual baseline funding and student services and amenities fee allocation agreement.
Total expenditure in 2017 was $1.97m (2016, $2.06m), of which $1.33m (2016, $1.19m) was spent by the Board of Management to fund the administration of the TUU including employment of relevant staff, and management of the organisation's annual budget. In 2017, the Student Representative and Student Council spent $0.26m (2016, $0.47m) on education and welfare advocacy initiatives as well as student events and activities.
Net assets were $9.33m at 31 December 2017 (2016, $9.01m).

Audit Findings

In performing our audit of the three subsidiaries we did not identify any significant deficiencies in internal control and no new audit findings were reported.

FINANCIAL ANALYSIS

Figure 2 summarises the financial results and position of University controlled entities for 2017.

Figure 2: Financial Results

	Underlying surplus (deficit) $'000s	Net surplus (deficit) $'000s	Comprehensive surplus (deficit) $'000s	Net Assets 2017 $'000s	Net Assets 2016 $'000s
University Foundation	5 008	5 008	5 008	58 754	53 746
AMC Search	(494)	(494)	(494)	4 743	5 237
TUU	324	324	324	9 333	9 010

OTHER STATE ENTITIES 31 DECEMBER 2017

INTRODUCTION

This part of the Report provides information on the following State entities who reported on a calendar year basis:

- ANZAC Day Trust
- Theatre Royal Management Board
- The Solicitors' Trust.

Information on UTAS and its controlled entities is included in the previous Chapter.

KEY RESULTS AND DEVELOPMENTS

ANZAC Day Trust

Anzac Day Trust recorded a Net deficit of $0.001m (2016, $0.002m surplus). The Trust only completed a statement of receipts and payments and therefore did not produce a balance sheet.

Theatre Royal Management Board

$2.45m	$2.29m	$0.25m	$0.16m
Total income	Total expenses	Underlying surplus	Net surplus

As at 31 December 2017, the Theatre Royal Management Board reported an Underlying surplus of $0.26m (2016, deficit $0.05m), an improvement of $0.30m, predominately due to a $0.29m increase in program, bar and box office income.

The Theatre Royal Management Board entered into a development agreement with the University and the Tasmanian Government for the construction of a performing arts centre adjacent to the Theatre Royal building which will be called the Hedberg Centre. During the year, the Theatre Royal Management Board expensed costs of $0.09m in relation to the Hedberg Centre. These costs were excluded from the calculation of the Underlying result.

The construction of the Hedberg Centre will require the theatre to be closed for a minimum of six months from October 2018. The Theatre Royal Management Board believes it has sufficient reserves to operate through this period.

2017		2016	
182	**$1.20m**	**197**	**$1.05m**
Number of performances	Program income (excluding grants)	Number of performances	Program income (excluding grants)

The number of performances in 2017 decreased from the previous year but program income was $1.37m (2016, 1.23m), an increase of $0.14m. The higher revenue reflected the popularity of a number of shows in the 2017 season.

Net assets were $1.53m at 31 December 2017, up from $1.37m in 2016. Operating cash and cash held in term deposits totalled $2.50m, of which $1.17m was cash from advanced ticket sales, deposits received and gift vouchers sold.

The Solicitors' Trust

$3.06m	**$0.12m**	**$0.00m**	**$3.04m**
Total Trust income	Total expenses	Total Guarantee fund income	Total grant distributions to grantees and Legal Professional Board funding

As at 31 December 2017, the Trust reported a Net deficit of $0.10m, (2016, $1.39m), a decrease of $1.29m from prior year, predominately due to higher interest received $0.28m and a decrease in distributions to grantees of $1.20m.

The Trust's Income of $3.06m was primarily derived from interest on Statutory Deposits, trust accounts operated by legal practitioners and trust investment funds.

The Trust made $1.96m in grant distributions to grantees pursuant to section 361(6) of the *Legal Profession Act 1997* for 2017, and paid $1.08m to fund the Legal Profession Board pursuant to section 359(3)(b) of the *Legal Profession Act 2017.*

Net assets at the end of 2017 totalled $10.85m, largely comprised of cash assets of $13.06m, partially offset by the accrual of grant distributions and Legal Profession Board funding of $2.16m.

The Trust disclosed $63.61m in Statutory deposits as at 31 December 2017. These funds are administered by the Trust under Section 352 of the *Legal Professional Act 2007,* and as such are only reflected in the notes to the financial statements.

AUDIT FINDINGS

The Solicitors' Trust submitted financial statements one day after the statutory deadline. The other entities included in this Chapter submitted their financial statements within the statutory deadline. Unqualified audit reports were issued in all cases.

In performing the audits we did not identify any significant deficiencies in internal control and no high risk audit findings were identified during the course of these audits.

FINANCIAL ANALYSIS

Financial snapshot 2017

Figure 3: Other Entities Financial Snapshot 2017

	Underlying surplus (deficit) 2017 $'000s	Net surplus (deficit) 2017 $'000s	Net Assets 2017 $'000s	Net Assets 2016 $'000s
ANZAC Day Trust	(1)	(1)	2	3
Theatre Royal Management Board	260	161	1 535	1 374
The Solicitors' Trust	(99)	(99)	10 849	10 948

RIVER CLYDE TRUST 30 JUNE AUDITS

INTRODUCTION

The River Clyde Trust (the Trust) was established in 1898 and operates under the *Water Management Act 1999*. It owns assets which include control gates at Lake Sorell and Lake Crescent and a pump station at Lake Meadowbank. These assets allow farmers along the Clyde River to access water for irrigation.

KEY DEVELOPMENTS

Completion of audits

The Trust failed to meet its statutory reporting deadline in each of the past three financial years. As a result, the Trust breached section 17 of the Audit Act, which requires accountable authorities to submit financial statements to the Auditor-General within 45 days after the end of the financial year.

The Trust submitted signed financial report for 30 June 2015 on 21 January 2016, 30 June 2016 on 14 December 2016 and 30 June 2017 on 22 November 2017.

The audit of the financial reports for the 2014-15, 2015-16 and 2016-17 financial years have been completed, with independent audit opinions issued on 6 July 2017, 18 August 2017 and 20 December 2017, respectively.

We have recommended the Trust review year-end financial statement preparation procedures to ensure it can meet the statutory deadline requirements from 30 June 2018.

FINANCIAL ANALYSIS

Financial snapshot 2017

Figure 4: River Clyde Trust Financial Snapshot 2017

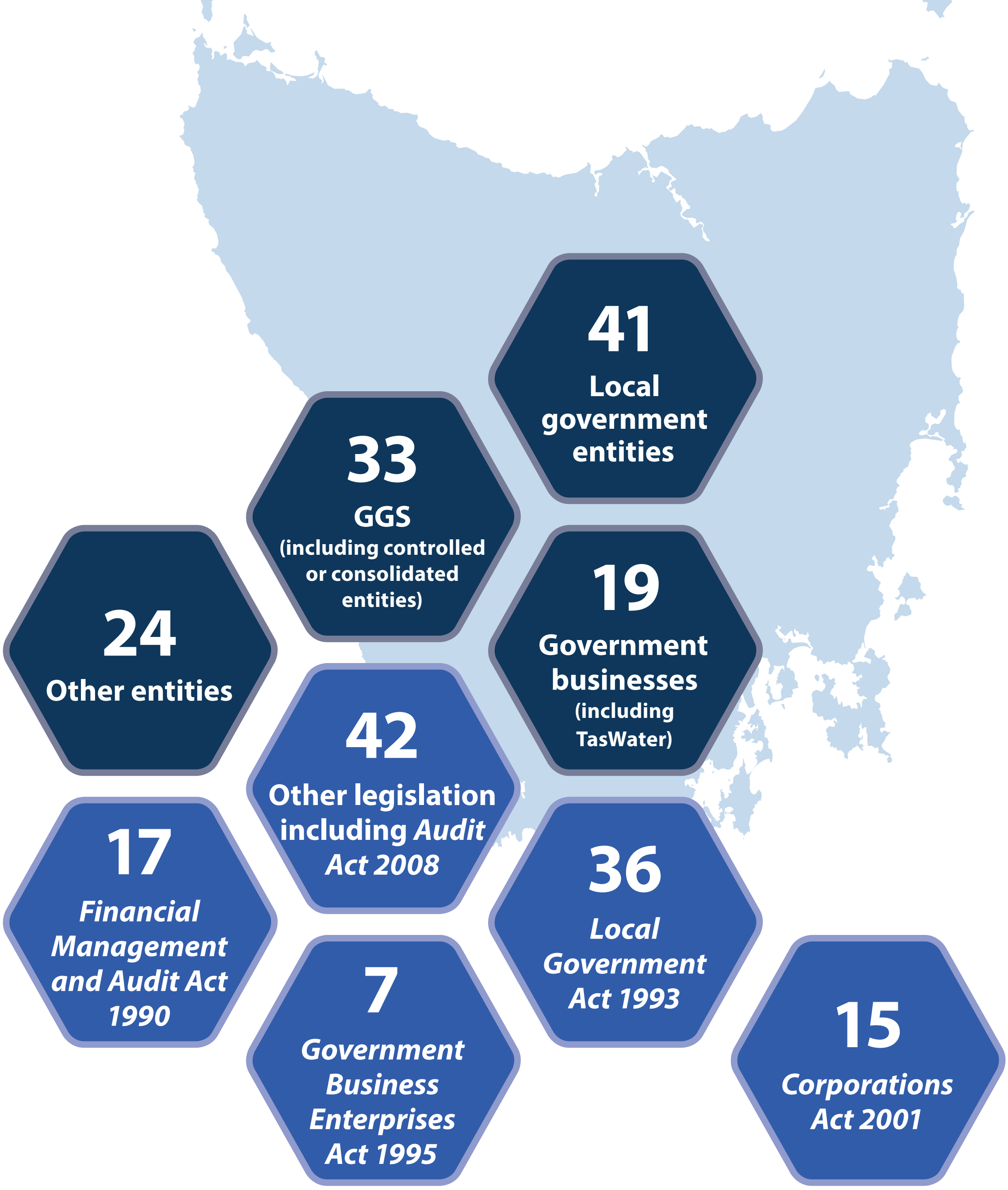
	Underlying surplus (deficit)		Net surplus (deficit)		Comprehensive surplus (deficit)		Net Assets	
	$	Ind	$	Ind	$	Ind	$	Ind
Other State entities								
River Clyde Trust	(61)	▼	(61)	▼	(61)	▼	1 464 414	●

Indicators: ▲ *improvement from prior year* ▼ *deterioration from prior year* ● *no material change from prior year*

FINANCIAL STATEMENT AUDITS

The Auditor-General has the mandate to carry out audits of the financial statements of the Treasurer and of all Tasmanian State entities. The aim of an audit is to enhance the degree of confidence in the financial statements by expressing an opinion on whether they are presented fairly, or give a true and fair view, in accordance with the applicable financial reporting framework. We carried out 117 financial statement audits across four main sectors in the 2017 audit cycle.

The information provided in this Chapter summarises the financial audits we undertook under sections 16 and 18 of the *Audit Act 2008* (the Audit Act). Audits we undertook by arrangement under section 28 of the Audit Act are not included in this Chapter.



AUDIT PROCESS AND METHODOLOGY

Financial audits are performed in accordance with Australian Auditing and Assurance Standards issued by the Australian Auditing and Assurance Standards Board. Whilst not a legislative requirement, when conducting annual financial audits, we give regard to probity considerations related to the management or use of public resources.

In conducting financial audits, we use an electronic financial audit toolset known as IPSAM (Integrated Public Sector Audit Methodology). IPSAM was specifically designed for the conduct of audits in the public sector environment and includes:

- consideration of the probity of matters associated with the management or use of public resources
- assessing compliance with relevant acts, regulations, Government policies and other prescribed requirements
- reporting to Parliament on matters arising from audits or relating to the Auditor-General's other activities in accordance with relevant legislation.

The audit process employed by us is adaptable to a wide range of government activities. Figure 5 below illustrates the major factors that govern the three elements of the audit process, the Accountability Framework, Audit Client Assertions and Audit Framework.

Figure 5: Elements of the Audit Process

At the heart of the equation is the *Acceptable Audit Risk*. This is established by first analysing two inter-linked elements know as *Inherent Risk* and *Control Risk* as they apply to the organisation concerned. We are then able to assess the level of *Audit Detection Risk*, which is crucial in determining the most appropriate procedures.

SUBMISSION AND AUDIT OF FINANCIAL STATEMENTS

All State entities are required to submit their financial statements to the Auditor-General within 45 days after the end of each financial year. In the 2017 audit cycle, the 45 day deadline fell on Monday 14 August 2017 for June balance date reporting and 14 February 2018 for December balance date reporting.

The Auditor-General must then audit the financial statements and issue an audit report outlining compliance with relevant legislation and accounting standards within 45 days of their submission. Where financial statements are received prior to the 45 day deadline, the 45 days audit completion obligation commences from the submission date.

Volumes 1 - 3

Detailing results of 30 June financial statements audits tabled in Parliament before 31 December 2017

30 June 2017
Balance Date

109* Financial statements submitted for audit	**94%** Financial statements submitted on time	**92%** Audits completed on time

31 October 2017
Deadline for tabling of
Treasurer's Annual Financial Report (TAFR)

26 October 2017
Unqualified audit opinions issued
on the audited components of TAFR

**Only relates to financial statements that were audited, does not include those that were dispensed with.*

Volume 4

Detailing results of 31 December financial statement audits tabled in Parliament

31 December 2017
Balance Date

7* Financial statements submitted for audit	**86%** Financial statements submitted on time	**100%** Audits completed on time

**Only relates to financial statements that were audited, does not include those that were dispensed with.*

Compliance with the 45 days statutory deadline for submission of financial statements declined in the 2017 audit cycle compared to the 2016 audit cycle. Seven State entities failed to comply with the requirement compared to two entities the year before.

Our compliance with the requirement to complete audits of financial statements within 45 days of their receipt also declined from 2016. Seven audits were completed outside the time required, compared to one audit in the 2016 audit cycle.

Copping submitted their financial statements on 8 August 2017. A disagreement with Copping as to whether thet were a for-profit or not-for-profit entity and whether it had control of the C Cell Unit Trust resulted in the audit for Copping not being completed within 45 days from the date of submission of the statements. On 15 February 2018, Copping withdrew the financial statements originally submitted, with revised financial statements submitted on 9 May 2018. As at the date of this report the audit had not been completed.

The disagreement with Copping contributed to delays in finalising the audits of the four owner councils of Copping within the 45 day deadline.

Financial statement audits of all State entities, excluding Copping, for the years ended 30 June 2017 and 31 December 2017 have been completed.

Section 17 of the Audit Act, requires State entities to submit financial statements to the Auditor-General within 45 days after the end of the financial year. Prior to 2016-17, we required State entities to submit statements certified by the accountable authority. From 2016-17, we permitted State Entities to also submit financial statements certified by the Chief Financial Officer (or equivalent). This allowed the audit to be completed and clearance provided to the audit committee, if relevant, prior to certification by the accountable authority.

Financial Statements certified by

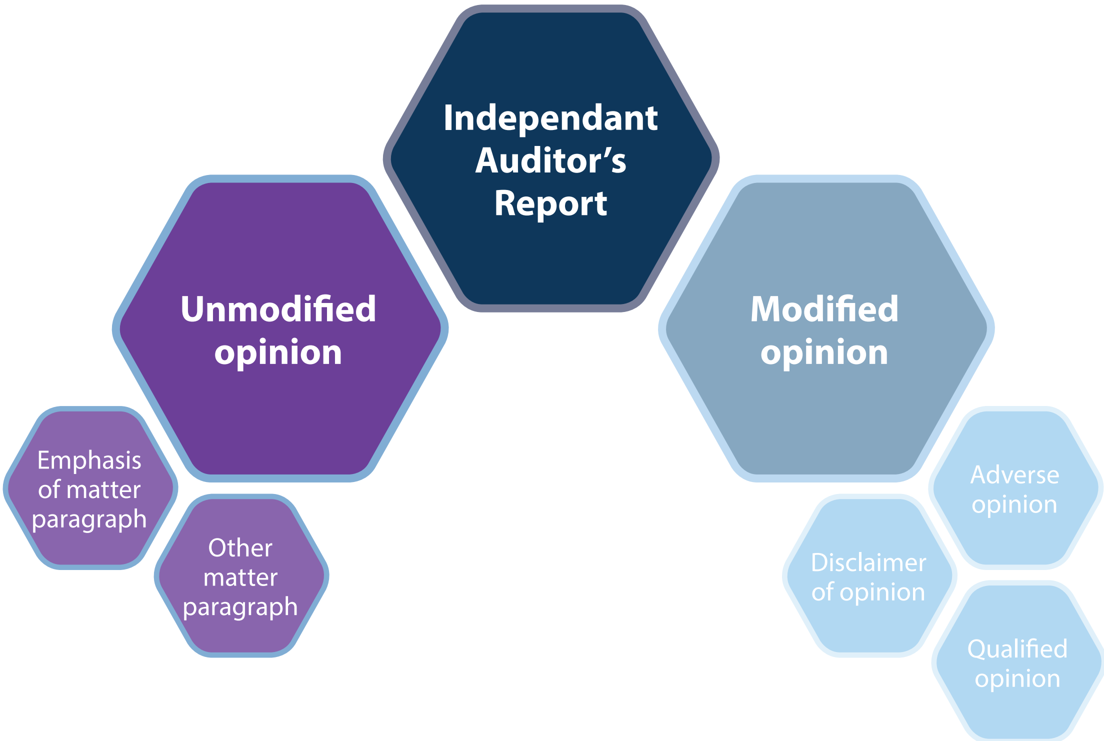
49	67
Management	Accountable Authority

FORMING AN OPINION AND REPORTING ON FINANCIAL STATEMENTS

The Auditor-General is required to issue an opinion on each financial statement audit under the Audit Act. Australian Auditing Standards prescribe the auditor's reporting responsibilities, including the responsibility to form an opinion on whether the financial statements are prepared, in all material respects, in accordance with the applicable financial reporting framework.

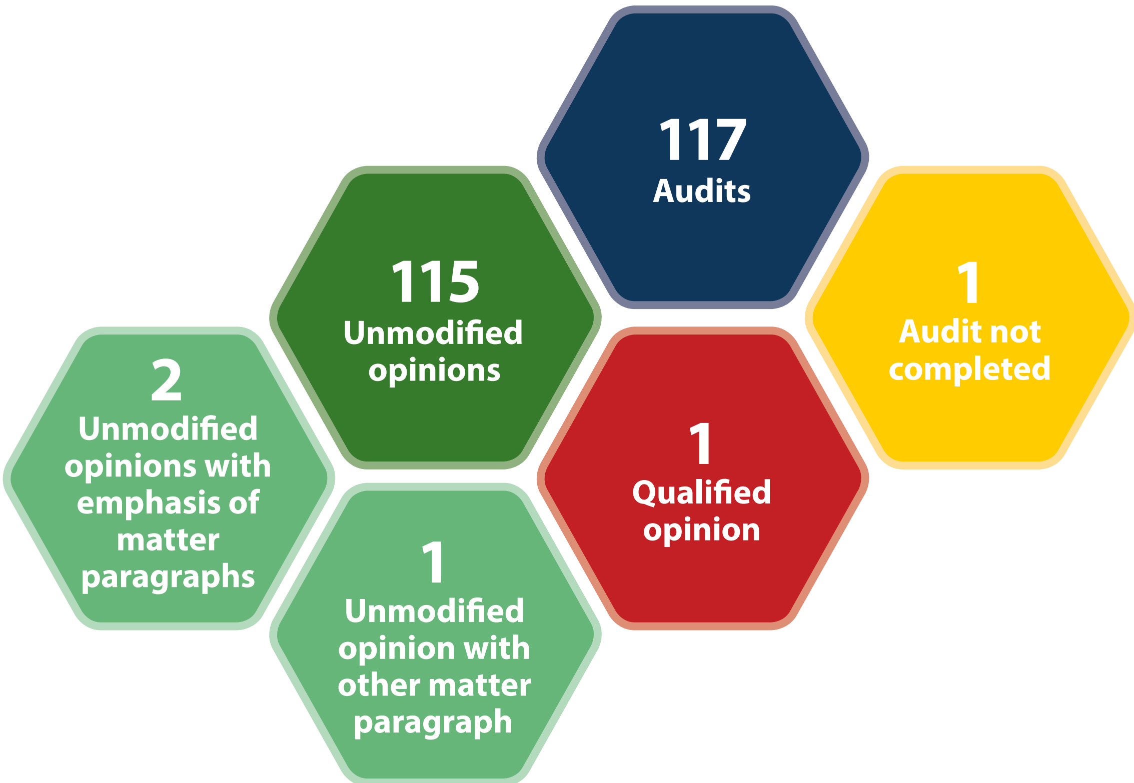
An opinion may be either:

- unmodified, when the auditor concludes that the financial statements were prepared, in all material respects, in accordance with the applicable financial reporting framework
- modified, if the auditor concludes that the financial statements as a whole were not free from material misstatement or was unable to obtain sufficient appropriate audit evidence.



The auditor may communicate additional matters in the auditor's report while still expressing an unmodified opinion on the financial statements. The purpose of this is to draw the attention of the users to relevant information, which itself is not significant enough to result in a modified opinion.

Audit Opinions on Financial Statements



115

Unmodified audit opinions issued on financial statements

We issued unmodified audit opinions on all financial statement audits completed during the 2017 audit cycle, except for the National Trust Australia (Tasmania). This gives the Parliament and Community assurance that the financial statements present fairly, in all material respects, the financial performance and position of State entities and were prepared in accordance with the relevant financial reporting frameworks.

1

Qualified opinion

We issued a qualified opinion when a specific part of the financial statements contains a material misstatement or we cannot obtain adequate evidence to support a material area, but rest of the financial statements are found to present a true and fair view, in accordance with accounting standards.

National Trust of Australia (Tasmania)	The Trust possesses certain heritage collections, but not all of these assets were recognised. Due to the nature of the assets, we were unable to quantify the financial effect.

1

Other matter paragraph

Two of the unmodified audit opinions contained an emphasis of matter paragraph. We include an emphasis of matter paragraph with audit opinions to highlight matters, although appropriately presented or disclosed in the financial statements, we believe are important to bring to the users' attention so as to assist with their understanding of the financial statements. Including an emphasis of matter does not modify our audit opinion.

Forestry	Emphasis of matter paragraph drew attention to a note which described Forestry's application of Treasurer's Instruction GBE-08-52-08P in respect of an exemption from application of the requirements of Australian Accounting Standard AASB 5 *Non-current Assets Held for Sale and Discontinued Operations*.
Tascorp	Emphasis of matter paragraph drew attention to a note which described Tascorp's application of Treasurer's Instruction GBE-08-051-08P in respect of $730.40m received from the Tasmanian Government on 29 June 2017 for the establishment of the Mersey Community Hospital Fund.

1

Other matter paragraph

One of the unmodified audit opinions contained an other matter paragraph. We include an other matter paragraph to highlight non-disclosures we believe are important to inform the users of the financial statements. Including an other matter paragraph does not modify our audit opinion.

West Coast Council	The other matter paragraph drew attention to West Coast Council failing to disclose overnight recreational vehicle parking and camping services as a significant business activity as required by the *Local Government Act 1993*. The disclosure was not made on the basis that Council disagreed with the findings of the Regulator and disputed that it provided any services at all.

AUDIT FINDINGS

2017		2016	
187	**119**	**209**	**85**
Audit matters raised	Audit matters raised in prior periods assessed as unresolved	Audit matters raised	Audit matters raised in prior periods assessed as unresolved

All deficiencies or weaknesses in internal control and other accounting or financial issues identified during audits were communicated to management at an appropriate level of responsibility. Significant matters were detailed in written reports, which included our recommendations for improvement and management responses. The reports were then communicated to those charged with governance, for example the Secretary, Chairperson of the Board or Mayor, with a copy sent to the Responsible Minister. We also reported significant matters to Parliament in Auditor-General's Reports on the Financial Statements of State entities.

We categorise each matter as high, moderate or low risk, depending on its potential impact, as shown below:

Risk category	Audit impact	Management action required
High	Matters categorised as high risk pose a significant business or financial risk to the entity and have resulted or could potentially result in a modified or qualified audit opinion if not addressed as a matter of urgency. High risk findings represent: • a control weakness which could have or is having a significant adverse effect on the ability to achieve process objectives and comply with relevant legislation • a material misstatement in the financial report is likely to occur or has already occurred.	Requires immediate management intervention with a detailed action plan to be implemented within one month. Requires management to correct the material misstatement in the financial report to avoid a modified audit opinion.

<table>
<tr><th>Risk category</th><th>Audit impact</th><th>Management action required</th></tr>
<tr><td>Moderate</td><td>Moderate risk findings are matters of a systemic nature that pose a moderate business or financial risk to the entity if not addressed as high priority within the current financial year, matters that may escalate to high risk if not addressed promptly or low risk matters which have been reported to management in the past but have not been satisfactorily resolved or addressed.
Moderate risk findings represent:
• a systemic control weakness which could have or is having a moderate adverse effect on the ability to achieve process objectives and comply with relevant legislation
• a misstatement in the financial report that is not material and has occurred.</td><td>Requires prompt management intervention with a detailed action plan implemented within three to six months.</td></tr>
<tr><td>Low</td><td>Matters categorised as low risk are isolated, non-systemic or procedural in nature and reflect relatively minor administrative shortcomings and could be addressed in the context of the entity's overall control environment.
Low risk findings represent
• an isolated or non-systemic control weakness with minimal but reportable impact on the ability to achieve process objectives and comply with relevant legislation
• a misstatement in the financial report that is likely to occur but is not expected to be material
• an opportunity to improve an existing process or internal control.</td><td>Requires management intervention with a detailed action plan implemented within six to 12 months.</td></tr>
</table>

Figure 6: 2017 Audit Findings by area

	High Risk	Moderate Risk	Low Risk	Total
Assets	8	12	13	33
IT Security	0	13	16	29
Expenditure	2	9	5	16
Payroll	0	22	13	35
Revenue/Debtors	1	7	5	13
Other	5	28	28	61
Total	**16**	**91**	**80**	**187**

High risk findings continued to be largely related to asset valuations. This is because of the high dollar values involved and the inherent subjectivity that is involved in estimating values and useful lives of assets. Other high risk findings related to bank reconciliations and segregation of duties.

Moderate risk findings covered an array of areas from corporate governance to information systems, together with internal control and accounting issues across most business cycles. Corporate governance type issues, included in the Other classification above, covered legislative compliance, such as audit panel arrangements, or outdated policies and procedures. Inadequate user access controls dominated findings in the IT Security area. We also found issues with excessive leave and breakdown of the system design and implementation relating to key controls in payroll, payments and receipting systems. Findings related to assets in this risk category had lesser significant impact on financial results than those classified as high risk.

Low risk findings found across all areas but were generally considered to be isolated, non-systemic or procedural in nature. In some cases they represented opportunities to improve existing processes or further strengthen existing controls.

Figure 7: 2017 Audit Findings by sector

	High Risk	Moderate Risk	Low Risk	Total
General Government Sector	4	30	15	49
Government businesses	2	16	24	42
Local government	10	43	39	92
Other	0	2	2	4
Total	**16**	**91**	**80**	**187**

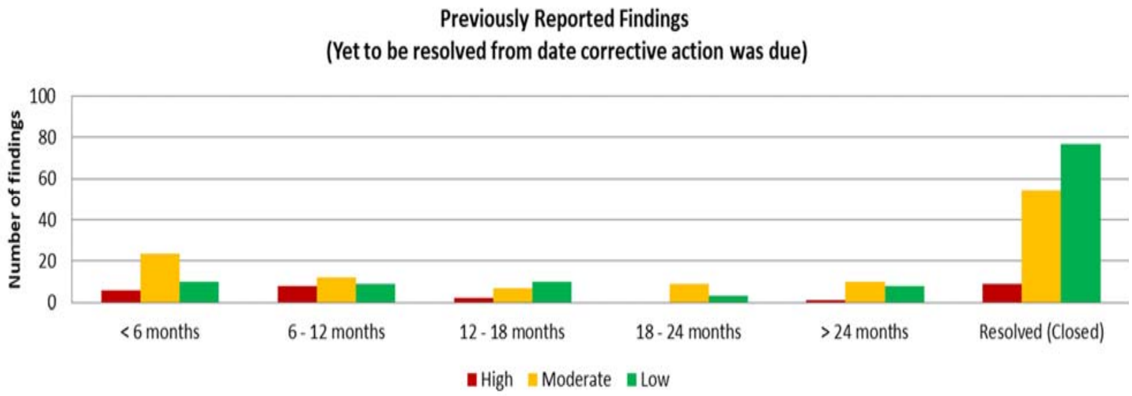
High risk issues were mostly prevalent in the Local Government sector. This is consistent with past years and the issues primarily relate to asset valuations.

40%

Issues previously reported remained unresolved

We considered all matters reported to management in the prior years when planning an audit as part of our risk assessment procedures. We performed audit testing to confirm that issues had been resolved.

Figure 8: Previously reported findings aging analysis



Efficient resolution of audit findings is crucial to reduce the organisations exposure to risk. Over 50% of issues previously reported were resolved in 2017, while the majority of outstanding issues were raised within the last 12 months. There are only two high risk issues yet to be resolved that are over 12 months old, one of which is over 24 months old which relates to the National Trust of Australia unrecorded collection assets.

Figure 9: Prior year unresolved Audit Findings by area

	High Risk	Moderate Risk	Low Risk	Total
Assets	9	20	12	41
IT Security	0	13	13	26
Expenditure	1	3	1	5
Payroll	0	6	5	11
Revenue/Debtors	1	4	5	10
Other	6	13	7	29
Total	**17**	**59**	**43**	**119**

High risk audit findings that were previously reported but are not yet resolved primarily related to Assets and more specifically, asset revaluations. These findings often remain outstanding until an entity conducts another revaluation of their assets, which can typically be within a three to five year cycle. The other high risk findings related to reconciliations and policies and procedures.

The majority of the prior year findings are in the Moderate risk category, covering a wide range of areas. Assets again features prominently, however they are primarily around the management of assets rather than revaluation. IT security also featured with the majority of concerns related to user access and passwords.

Figure 10: Prior year unresolved Audit Findings by sector

	High Risk	Moderate Risk	Low Risk	Total
General Government Sector	8	17	8	33
Government businesses	0	10	9	19
Local government	9	31	20	60
Other	0	1	6	7
Total	**17**	**59**	**43**	**119**

The local government sector had the largest number of prior year issues outstanding, and also the largest number of high risk findings outstanding. These high risk findings predominantly related to the revaluation of assets. The general government sector had eight high risk issues yet to be resolved with the majority related to asset valuations.

AUDITS DISPENSED WITH

SNAPSHOT

INTRODUCTION

The Auditor-General has the discretion under the Audit Act to dispense with certain audits if considered appropriate in the circumstances. The dispensation is subject to meeting one of the following conditions determined by the Auditor-General:

1. the entity must demonstrate to us that its financial reporting and auditing arrangements are appropriate. To satisfy this condition, the entity is required to submit their audited financial statements to the Auditor-General each year. The financial statements are reviewed and, where necessary, feedback on information presented in the financial statements is provided to the entity
2. the entity is controlled by a State entity and the financial transactions and balances of the controlled entity are subject to audit procedures as part of the group audit of the controlling entity.

It is important to note that dispensation of the audit does not limit any of the Auditor-General's functions or powers given under the Audit Act.

The Audit Act also requires the Auditor-General to consult with the Treasurer before exercising the power to dispense with audits. Following consultation with the Treasurer, the audits of the annual financial statements of the following specific audits or categories of audits were dispensed with:

Controlled Subsidiaries - Year Ended 30 June 2017 (controlling entity shown brackets)

- AETV Pty Ltd (Hydro Tasmania)
- Auroracom Pty Ltd (Tasmanian Networks Pty Ltd)
- Bell Bay Pty Ltd (Hydro Tasmania)
- Bell Bay Three Pty Ltd (Hydro Tasmania)
- Ezikey Group Pty Ltd (Tasmanian Networks Pty Ltd)
- Flinders Island Ports Corporation Pty Ltd (Tasmanian Ports Corporation Pty Ltd)
- Geeveston Town Hall Company Ltd (Huon Valley Council)
- Heemskirk Holdings Pty Ltd (Hydro Tasmania)
- Heritage Building Solutions Pty Ltd (Southern Midlands Council)
- Heritage Education & Skills Centre Pty Ltd (Southern Midlands Council)

- HT Wind Developments Pty Ltd (Hydro Tasmania)
- HT Wind Operations Pty Ltd (Hydro Tasmania)
- HT Wind New Zealand Pty Ltd (Hydro Tasmania)
- Hydro Tasmania Consulting (Holding) Pty Ltd (Hydro Tasmania)
- Hydro Tasmania Consulting India Private Limited (Hydro Tasmania)
- Hydro Tasmania Neusberg (Pty) Ltd (Hydro Tasmania)
- Hydro Tasmania South Africa (Pty) Ltd (Hydro Tasmania)
- Kingborough Waste Services Pty Ltd (Kingborough Council)
- King Island Ports Corporation Pty Ltd (Tasmanian Ports Corporation Pty Ltd)
- Lofty Ranges Power Pty Ltd (Hydro Tasmania)
- Metro Coaches (Tas) Pty Ltd (Metro Tasmania Pty Ltd)
- Newood Holdings Pty Ltd (Forestry Tasmania)
- Newood Energy Pty Ltd (Newood Holdings Pty Ltd)
- Newood Huon Pty Ltd (Newood Holdings Pty Ltd)
- Newood Smithton Pty Ltd (Newood Holdings Pty Ltd)
- palawa Enterprise Trust (Aboriginal Land Council of Tasmania)
- RE Storage Project Holdings Pty Ltd (Hydro Tasmania)
- Schools Registration Board (Department of Education)
- Woolnorth Bluff Point Holdings Pty Ltd (Hydro Tasmania)
- Woolnorth Studland Bay Holdings Pty Ltd (Hydro Tasmania).

Foreign Controlled Subsidiaries – Year Ended 30 June 2017 (controlling entity shown in brackets)

- Hydro Tasmania Consulting India Private Limited (Hydro Tasmania)
- Hydro Tasmania South Africa (Pty) Ltd (Hydro Tasmania)
- Hydro Tasmania Neusberg (Pty) Ltd (Hydro Tasmania).

Drainage Trusts – Year Ended 30 June 2017

- Egg Lagoon Drainage Trust
- Elizabeth Macquarie Irrigation Trust
- Forthside Irrigation Water Trust
- Lake Nowhere-Else Dam/Whitehawk Creek Irrigation Trust
- Lawrenny Irrigation Trust
- Mowbray Swamp Drainage Trust
- Richmond Irrigation Trust.

Other Boards and Authorities - Year Ended 30 June 2017

- Superannuation Commission
- Tasmanian Pharmacy Authority
- Tasmanian Timber Promotion Board.

Other Drainage Trusts – Prior Years Ended 30 June

- Togari Drainage Trust (2013, 2014, 2015 and 2016).

Controlled subsidiaries – Year Ended 31 December 2017 (controlling entity shown in brackets)

- Sense-Co Tasmania Ltd (University of Tasmania)
- UTAS Holdings Pty Ltd (University of Tasmania).

Other Boards - Year Ended 31 December 2017

- Board of Architects.

PREVIOUSELY DISPENSED WITH ENTITIES WITH FINANCIAL STATEMENTS OUTSTANDING

As indicated in the introductory section of this Chapter, audits are only dispensed with on the condition that the entity must demonstrate to us that its financial reporting and auditing arrangements are appropriate. To satisfy this condition, the dispensed with audit entities, like all State entities, are required to submit their audited financial statements to us each year in accordance with section 17 of the Audit Act.

Entities that do not meet their reporting obligations under the Audit Act and have not demonstrated to us a realistic commitment to meet their reporting requirements, risk an adverse recommendation by the Auditor-General to the Minister responsible for their enacting legislation. This can include a recommendation for the entity to be dissolved.

BASIS FOR SETTING FEES

BACKGROUND

Section 27 of the Audit Act provides that:

"1. The Auditor-General is to determine whether a fee is to be charged for an audit carried out by the Auditor-General under this Division and, if so –

a. the amount of that fee; and

b. the accountable authority liable to pay that fee."

In relation to the tabling of Auditor-General's reports on audits of the financial statements of State entities the Audit Act also requires the following at section 29(3):

"3. A report under subsection (1) is to describe the basis on which audit fees are calculated."

To comply with section 29(3), the basis for setting audit fees for conducting audits of the financial statements of State Entities is detailed in this Chapter. Audit fees are not charged for performance audits, compliance audits or investigations.

BASIS ON WHICH AUDIT FEES ARE CALCULATED

The Chapter explains the fee setting process for individual State entities, including:

- the specific factors taken into account in proposing the fee (particularly the risk assessment)
- the assumptions upon which the fee is based in terms of, for example, the standard of the entity's control environment, coverage of internal audit, quality of working papers and so on
- what is included in the fee and what is not included
- processes for agreeing additional fees if circumstances change or the assumptions upon which the fee is based are not met.

DETERMINATION

A matrix (audit fee scale) has been developed to provide a guide for determining the expected time to be taken on an audit. The scales are based on the following key variables:

Size of the entity based on its expected gross turnover

Size of the entity is used to determine the base amount of time required to conduct the audit. Turnover was based on the client's actual income and expenditure for the preceding financial year, adjusted for any known factors (Fixed element).

Risk and complexity profiles for each entity

These profiles are determined by our staff and consider the corporate structure, complexity of systems, operations and financial statement reporting requirements. The profile bands applied range from 40 per cent below to 40 per cent above the base time (Variable element).

The fee scales take account of:

- changes to Australian Auditing or Accounting Standards
- in some cases, particularly audits returning from contract, a change in scope of work being performed in line with our audit approach whereby selected probity matters will be considered during the course of all audits.

Fee scales are as follow:

Turnover*	Base Hours	Variable component
<$100 000	15	+/-40%
$101 000 to $1.5m	30	+/-40%
$1.5m to $10m	100	+/-40%
$10m to $55m	155	+/-40%
$55m to $121m	270	+/-40%
$121m to $200m	460	+/-40%
$200m to $410m	610	+/-40%
$410m to $1bn	830	+/-40%
>$1bn	1 350	+/-40%

** may be adjusted in line with CPI movements*

Bandings are based on current cost experience in conducting audits.

After applying the above model, the hours to undertake the audit are allocated according to the staff mix necessary to conduct the audit. The respective staff charge rates are then applied to the allocated hours so as to determine a dollar amount (the audit fee). Where applicable, travel and other direct costs (out of pocket expenses) are added to the audit fee on a full cost recovery basis.

FEE SETTING

It is emphasised that the fee scales only provide a framework within which set the actual fees charged to individual State entities.

The level of fee, and any change, experienced by individual State entities will therefore vary according to local circumstances and the risks each entity faces.

In certain circumstances, for example, where a State entity faces a particular challenge to manage high risks or there are particular local circumstances, a fee may fall outside the noted bands. In these cases, the audit fee will be determined in discussion between our staff and entity management, to reflect our assessment of risk and the extent and complexity of the audit work required.

SKILLS-RELATED FEE SCALES

In certain circumstances, we may need to use staff or contractors with specialist skills in order to review specific local issues. Where this is the case, it can result in higher costs being incurred. In these circumstances, the fee to be charged will be determined in discussion between our staff and entity management and will reflect the size, complexity or any other particular difficulties in respect of the audit work required. Where possible, we attempt to absorb such costs within the base audit fee.

PRINCIPLE FOR DETERMINING CHARGE RATES

Charge rates are based on the principle of the Office being able to recover its costs of operation. Charge rates comprise two parts, direct salary cost and overhead recovery. Direct travel time and costs attributable to each audit are billed separately and do not form part of our charge rates.

PRINCIPLE FOR AUDIT FEE DETERMINATION

Fees are set for each State entity commensurate with the size, complexity and risks of the engagement. These factors affect the mix of staff we assign to each audit and therefore the overall fee. Staff are assigned hourly charge rates for use in determining the allocation of work on the audit and in computing the fee.

There is an expectation that audits of similar complexity and risks will have a similar mix of staff.

BASIS OF FEES

Fees are calculated on the basis that:

- current accounting systems will be operating throughout the year with a satisfactory appraisal of internal control
- no errors or issues requiring significant additional audit work will be encountered during the course of the audit
- the standard period-end general ledger reconciliations will be available at the commencement of our year-end audit
- assistance for our staff will be provided with respect to reasonable requests for additional information throughout the audit
- agreed timetables will be met, within reason
- financial statements, complete in all material respects, are submitted to audit in accordance statutory time limits
- additional work (including work arising from the adoption of new accounting standards or issues associated with key risks and other matters arising) will be billed separately if it cannot be absorbed into the existing fee
- the nature of the entity's business and scale of operations will be similar to that of the previous financial year
- fees incorporate financial statement disclosure and other specific audit related advice.

COMMUNICATION OF AUDIT FEES

In all cases, fees are communicated to each accountable authority prior to audit commencement or during the planning phase. For 2017-18 financial year audits, the adjustment to fees was:

- 2.5% – 4.0% for General Government Sector entities
- 6.0% for Local Government Authorities
- 4.0% for Government Businesses.

This increase was primarily based on salary increases in the *2016-2018 Public Sector Union Wages Agreement* and as such reflects that employee costs are the main driver of our costs. The higher increase for local government audits was caused by the need for the Office to mitigate losses incurred across all audits within this sector.

ADDITIONAL AUDIT WORK

In carrying out additional audit work, including government grant acquittals and other similar returns, we will recover, in respect of such work, an amount that covers the full cost of the relevant work undertaken.

The actual fees to be charged will be determined in discussion between our staff and entity management to reflect the size, complexity or any other particular difficulties in respect of these types of audits. Fees will have regard to the time taken, the audit staff assigned and their respective charge rates.

ADDITIONAL AUDIT FEES

If the circumstances outlined under the section headed "Basis of Fees" change in a year, we would seek additional fees from the entity. Any future impact of agreed additional fees would be assessed in terms of the on-going audit fee.

ADJUSTMENT TO FEES

Fees may be adjusted in the following circumstances:

- changes to the size and nature of the entity and its operations
- changes to the risks associated with a particular engagement
- changes to accounting and auditing standards requiring greater effort on our part
- ad-hoc matters that impact upon significant balances within the financial statements, such as a significant asset revaluation
- unavoidable increases in costs of maintaining our Office.

There may also be circumstances where, based on our assessment of size, complexity and risks of the engagement, our fees may be reduced.

DEVELOPMENTS IN FINANCIAL REPORTING

SNAPSHOT

REPORTING IN THE PUBLIC SECTOR

International Public Sector Accounting Standards Boards (IPSASB)

With Australian Accounting Standards (AAS) primarily based on international standards, it is important to monitor emerging topics and developments. At a global level, the International Accounting Standards Board (IASB) sets International Financial Reporting Standards (IFRS). With IFRSs written from a for-profit entity perspective, some of the transactions and accounting policies that are prevalent in the public sector are either not addressed by IFRS, or not addressed well. As a consequence the AASB maintain a principle of transaction neutrality and, where appropriate, incorporates pronouncements from the IPSASB. Amendments are usually made where there is a type of transaction that is unique to the public sector or the prevalence/importance of the transaction to the public sector is disproportionately greater.

As part of this process the AASB closely monitors the work plan of the IPSASB and considers the adoption of IPSASB based standards/guides where appropriate. The development of recent standards addressing income for not-for-profit (NFP) entities are examples of this.

A review of the current IPSASB work program of key projects provides an insight into other topics which may be considered for Australian public sector reporting into the future. The work program includes the following public sector specific topics:

- Social Benefits
- Financial Instruments Update Project
- Leases
- Revenue
- Non-Exchange Expenditure
- Public Sector Measurement
- Infrastructure Assets

- Heritage
- Public Sector Specific Financial Instruments.

With the public sector part of a global economy facing similar challenges to others internationally, standard setters such as the IASB and IPSASB will continue to influence future developments in Australian public sector reporting as the general trend of convergence continues.

No More Special Purpose Financial Statements?

Change is coming for entities that are self-assessing themselves as a 'non-reporting' entity and only preparing special purpose financial statements. This change is imminent due to the IASB in March 2018 releasing a revised Conceptual Framework for Financial Reporting (Conceptual Framework). The Conceptual Framework is a comprehensive set of concepts for financial reporting. The IASB's revised Conceptual Framework applies to annual periods beginning on or after 1 January 2020.

In Australia, current legislation generally requires specified entities to prepare financial statements in accordance with AASs. The 'reporting entity' concept is given effect by AASB 1057: *Application of Australian Accounting Standards*. This effectively requires 'reporting entities' to prepare fully detailed general purpose financial statements; or statements on a reduced disclosure basis.

Statement of Accounting Concept 1(SAC 1) provides guidance that a reporting entity is one where there exists users who are dependent upon financial information for making and evaluating resource allocation decisions. Usually, such users are not in a position to require an entity to prepare reports tailored to their particular information needs. As a result statements are prepared in accordance with all accounting standards, as they all generally require application by reporting entities. Conversely, the IASB's approach is one of a 'public accountability' concept and will rely on a degree of regulators setting requirements for financial statement content.

In Australia however, if an entity self-assesses itself (via the criteria in SAC 1), as not being a reporting entity, it can elect to prepare special purpose financial statements, which need not comply with all Australian accounting standards. Consequently, entities are choosing which standards to apply and which they do not. Arguably in the public sector, there is the view that such an approach should not be used by any entity that utilise public funds and/or is legislatively based.

Given that we operate under an international regime and that it is not possible to have two definitions of a reporting entity in Australia, the revised international framework will need to be adopted and SAC 1 removed.

As a result entities that prepare statements under legislation, will no longer have the option to prepare special purpose financial statements.

As part of its Australian Financial Reporting Framework project, the AASB is working in collaboration with key stakeholders and regulators. A project plan maps out the various stages and key milestones over the next two years. Stage one of this process involves a Consultation Paper to seek feedback.

In the short term the Consultation Paper proposes interim arrangements allowing for two conceptual frameworks. The longer term proposal is the provision of two tiers of general purpose financial reporting requirements (Tier 1 and Tier 2). At the time of writing these options were:

Option 1 - the existing reduced disclosure requirements (RDR)

Option 2 - a new option representing the requirements in ASIC Regulatory Guide RG85: *Reporting requirements for non-reporting entities*. It proposes to comprise the full recognition, measurement, consolidation and equity method of accounting requirements, and disclosure requirements in:

AASB 101 *Presentation of Financial Statements*

AASB 107 *Statement of Cash Flows*

AASB 108 *Accounting Policies, Changes in Accounting Estimates and Errors*

AASB 1048 *Interpretation of Standards*

AASB 15 *Revenue from Contracts with Customers*

AASB 124 *Related Party Disclosures*

AASB 136 *Impairment of Assets*.

In addition, service performance reporting, fundraising and administration cost disclosures could be made mandatory for not-for-profit private sector entities.

At the time of writing the Consultation Paper was being finalised for issue, with comments on the longer-term approach requested by 31 August 2018.

REPORTING IN 2017-18

For the 2017-18 financial reporting period there will be very few new changes to reporting requirements in the public sector.

While a number of new and revised accounting standards offer the opportunity to early adopt and various transition options and practical expediencies, for the vast majority of State entities this will also depend upon the framework under which they operate. Entities reporting under the *Financial Management Audit Act 1990*, for example, are required to follow the prescribed model departmental financial statements prepared by the Department of Treasury and Finance (Treasury). These statements usually maintain consistency in reporting, with the adoption of any changes following the respective application date.

Reporting developments of significance for 2017-18 are discussed below.

Financing Activity Disclosures in the Statement of Cash Flows

Now fully compiled into the Statement of Cash Flows standard, AASB 2016-2 *Amendments to Australian Accounting Standards – Disclosure Initiative: Amendments to AASB 107*, became applicable to annual reporting periods beginning on or after 1 January 2017.

The amendment was aimed to improve disclosure of information relating to financing liabilities and was in response to requests from investors to help them better understand changes in an entity's debt structure. The standard now requires entities to provide disclosures that enable users of financial statements to evaluate changes in liabilities arising from financing activities, both changes arising from cash flow and non-cash flow movements.

One way to fulfil the disclosure requirements, included as an example in the amendment, is to provide a reconciliation between opening and closing balances in the Statement of Financial Position for assets and liabilities that relate to financing activities. Such an approach needs to include sufficient information to enable users to link items included in both the Statement of Financial Position and Statement of Cash Flows.

In the following example the entity entered into new leasing (Non-Cash) and borrowing (Cash Received) arrangements, as well as met existing leasing and borrowing cash repayments. Each entity will need to evaluate its own circumstances in determining how to present the necessary disclosure requirements.

Example - Reconciliation of liabilities arising from financing activities

		Non-Cash Changes				Cash Flows		
Liabilities	Closing Balance 2017 $'000	Transfers to/(from) other Government Entities $'000	New Leases Acquired $'000	Change in Fair Value $'000	Other (Specify) $'000	Cash Received $'000	Cash Repayments $'000	Closing Balance 2018 $'000
Leases	2,000	-	150	-	-	-	(100)	2,050
Borrowings	4,000	-	-	-	-	700	(500)	4,200
Other (Specify)	-	-	-	-	-	-	-	-
Total	**6,000**	-	**150**	-	-	**700**	**(600)**	**6,250**

In addition to just liabilities, the standard also applies to changes in financial assets (for example, assets that hedge liabilities arising from financing activities) if cash flows from those financial assets were, or future cash flows will be, included in cash flows from financing activities.

Model financial statements are now providing for this additional reconciliation requirement. Another approach would be to provide the disclosure requirements as part of a reconciliation of net debt. The requirement is prospective and entities are not required to provide comparative information for the preceding period.

Updated Government Business Remuneration Disclosure Template

Under the *Guidelines for Tasmanian Government Businesses - Director and Executive Remuneration*, Government Businesses are required to disclose the remuneration details of all directors and executive in the notes to the Financial Statements and to Treasury and the Government Business Executive Remuneration Advisory Panel (the Panel), as the advisors to the Shareholding Ministers. This disclosure must be consistent with the template approved by Treasury and is available from the TAO website.

Over the past year, the Panel made a number of recommendations to the Treasurer regarding the disclosure of director and executive remuneration. These included Treasury and the TAO reviewing the remuneration disclosure template to ensure it requires the inclusion of sufficient information to meet the reporting expectations of the Government.

An updated reporting template, incorporating a number of changes and additional disclosures, was approved in December 2017. These include updates to definitions and tables to clarify what payments are included for the purposes of addressing compliance with the Guidelines, a mandatory requirement to clearly specify the links between incentive payments and performance, and details on the composition of any termination benefits paid. Other changes include the disclosure of termination benefits outside of the executives' total remuneration package for the purposes of assessment with the Guidelines and updated instruction regarding the disclosure of related party transactions.

The revised template was updated on the TAO website in January and under "Other Client Information" in the "Resources" section.

Related Party Disclosures for Not-for-Profit Public Sector Entities

It was pleasing that the vast majority of entities in the Tasmanian non-for-profit public sector readily adopted the enhance transparency and improved governance disclosures that resulted from the extension of AASB 124 *Related Party Disclosures*.

To provide clarity in this complex area, the Office provided multiple presentations across the State, not only in the various client updates, but also in several other separate presentations. We thank those who sought our assistance and all those who attended. While the initial implementation was prospective, entities will now need to provide comparatives in their notes to their financial statements.

It is important to note that this standard applies to all State entities irrespective of their size or nature, and all those in a governance role, irrespective of title. It is the Office's view that further improvements can still be made with entities that are not required to follow government policy requirements and are providing only the minimum aggregated disclosure requirements. We will continue to work with government to improve sectors that currently only require limited disclosure requirements.

For the current 2017-18 financial reporting period we will again to work with entities to further improve and streamline their disclosure process.

LOOKING FURTHER FORWARD

Progressively over future reporting periods there are a number of new accounting standards that will become effective for the first time. State entities are encouraged to monitor and consider implementation of reporting requirements over the next few reporting periods to ensure smooth transition. The following commentary provides a high level overview of a selection of pertinent standards/projects.

Revenue from Contracts with Customers

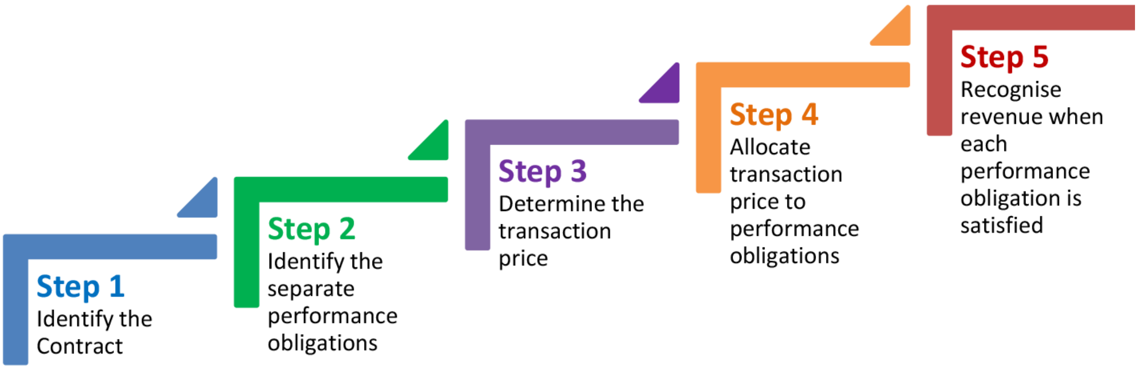
AASB 15 *Revenue from Contracts with Customers* was issued by the AASB in December 2014. AASB 15 replaces AASB 118 *Revenue*, AASB 11 *Construction Contracts* and five other revenue related interpretations. Although the standard originally had a lengthy two year lead time from issue before becoming effective from 1 January 2017, this was deferred in December 2016, following much discussion over implementation and readiness. While this allowed a further period for preparation, it is now due for adoption for for-profit entities in the next reporting period, NFP entities have one more years grace.

The effective dates are therefore:

- For-profit entities – 1 January 2018 (the 2018-19 reporting period)
- NFP entities – 1 January 2019 (the 2019-20 reporting period).

Earlier application of AASB 15 is permitted for NFP entities, provided AASB 1058 *Income of Not-for-Profit Entities* is also applied to the same period.

The core principle of the standard is that an entity will only recognise revenue upon the transfer of promised goods or services to customers, in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. Entities will need to apply a five-step model to determine when to recognise revenue, and at what amount.



This process requires an enforceable contract, with a sufficiently specific performance obligation for the transfer of the goods or services. Entities need to allocate a transaction price to each performance obligation in a contract and recognise the revenue only when the related obligation is satisfied.

This step process may appear straightforward, however there are many idiosyncrasies to consider. The standard prescribes treatment in a number of specific areas such as the bundling of transactions, discounts, variable components, non-cash consideration, sales with rights of return, warranties, non-refundable upfront fees and the treatment of any financing effect for transactions that are greater than a year.

AASB 15 has the potential to change the timing of revenue recognition for many types of transactions. In general, depending upon the actual transaction, this could include an increase in receivables for unbilled revenue items (contract assets) and an increase in liabilities (contract liabilities) for unfulfilled performance obligations. This may result in the need for entities to revaluate processes to capture such information and the need to reconsider internal controls to ensure the completeness and accuracy of information.

The standard requires retrospective application, but the transitional requirements allow two alternative retrospective methods:

- a fully retrospective approach which requires the restating of prior periods, with some relief for completed contracts
- the practical expediency approach, which allows for the recognition of the cumulative effect in the current year as an adjustment to the opening balance of retained earnings for all existing contracts, as of the effective date, and to contracts entered into subsequently.

Both approaches will require significant preparation and disclosure. Entities need to evaluate and decide as to which method best suits their individual situation. The lengthy period that has already been provided before application, reflects the fact that the standard's new rules are likely to have significant impacts on a wide range of organisations. Entities are encouraged to prepare early in anticipation of the many varied effects that these changes to revenue recognition will have on their operations.

AASB15 will apply to contracts of NFP entities that have reciprocal transactions. AASB 1004 *Contributions* will continue to apply to non-reciprocal transactions until AASB 1058 applies.

Income of Not-for-Profit Entities

AASB 1058 *Income of Not-for-Profit Entities* was issued in December 2016 and works in combination with AASB 15. Application aligns with AASB15, with an effective date of 1 January 2019 (the 2019-20 reporting period).

These standards supersede all the income recognition requirements for private sector NFP entities, and most of the income recognition requirements for public sector NFP entities, previously in AASB 1004 *Contributions*.

AASB 1058 applies to:

- transactions where consideration to acquire an asset is significantly less than fair value, principally to enable a NFP entity to further its objectives
- receipt of volunteer services.

On initial recognition of an asset an entity must recognise any related contributions by owners, increases in liabilities, decreases in assets and revenue (related amounts) in accordance with other AASs.

Entities must immediately recognise the difference between the fair value of the asset and any related amounts as income in the profit and loss. However, if the transaction enables the entity to acquire or construct a recognisable non-financial asset controlled by the entity (i.e. an in substance acquisition of a non-financial asset), the entity is required to recognises a liability representing the remaining obligation to acquire or construct and then recognises income as it satisfies its obligations under the transfer (similarly to income recognition for performance obligations under AASB 15).

A transfer of a financial asset to acquire or construct a recognisable non-financial asset controlled by the entity is one that:

- requires the entity to use that financial asset to acquire or construct a recognisable non-financial asset to identified specifications
- does not require the entity to transfer the non-financial asset to the transferor or other parties and
- occurs under an enforceable agreement.

AASB 1058 includes a consequential amendment to lessee accounting for the treatment of leases where the payments are zero, nominal or a 'peppercorn'. When AASB 1058 is applied in conjunction with AASB 16 *Leases*, such leases result in the recognition of a right-to-use asset acquired by the lessee at its fair value, with the difference with the lease liability, (i.e. the negligible minimum lease payments), recognised in the operating statement. This is a significant change from current practice in recognising below-market leases and likely to result in increases in revenue, in the year such arrangements are first entered into.

The standard also requires that local governments, government departments, general government sectors and whole of governments must recognise volunteer services if:

- they would have been purchased if not provided voluntarily and
- the fair value of those services can be measured reliably.

NFPs can also make an election to recognise volunteer services if the fair value of those services can be measured reliably, whether or not the services would have been purchased if they had not been donated.

For-profit entities will continue to account for grants and contributions under AASB 120 *Accounting for Government Grants and Disclosure of Government Assistance*.

Full or modified retrospective application will be required on initial adoption of AASB 1058. The transitional provisions include practical expedients for completed contracts and assets acquired for consideration significantly less than fair value principally to enable the entity to further its objectives. Practical examples accompany AASB 1058 demonstrating how a NFP entity applies the requirements in practice.

Preparing for changes to the revenue standards

In preparation for changes to revenue standards entities should:

- consider whether AASB 15 and AASB 1058 will change their income recognition policies. If it does, the impact must be disclosed before the application date, as either "full" or "modified" retrospective application will be required on adoption
- assess and ensure registers/databases of contracts with customers are complete and identify performance obligations within those contracts
- assess and ensure grants registers/databases are complete and identify whether the transaction enabled the entity to acquire or construct a recognisable non-financial asset controlled by the entity
- prepare for the significantly increased disclosures
- review standard contract templates to ensure new contracts clearly support revenue recognition with the goods and services sold
- ensure existing systems support income recognition and are capable of capturing the key information requirements of the new standards
- ensure the control environment supports robust estimates and judgements on income recognition
- plan appropriate training for affected staff in areas such as such as finance, grants, legal and other service delivery or customer service areas
- advise customers and other stakeholders if changes will be made to contracts, systems and processes
- discuss proposed income recognition policies and financial statement disclosures with auditors
- consider the impact on budgetary forecasts and reporting to stakeholders regarding financial position and performance
- ensure governance committees and other stakeholders are adequately informed.

Audit Committees and those charged with governance should:

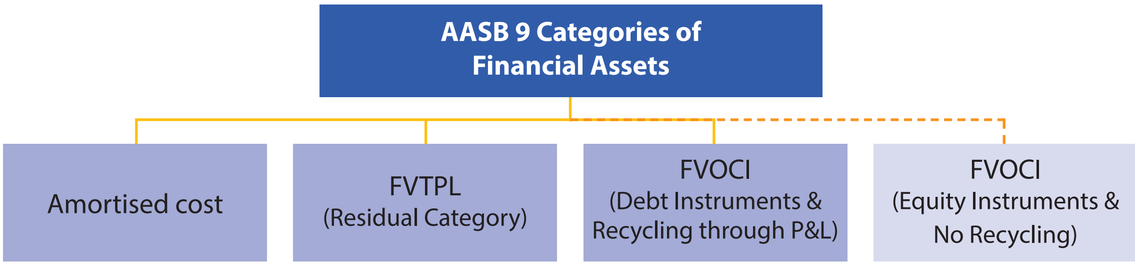
- understand AASB 15 and AASB 1058 and ensure management has adequately planned for their effective application, including disclosing the impact in the next financial report
- consider and confirm management's determination of whether to apply the new standards using a 'full' or a 'modified' retrospective approach
- monitor progress against the plan and against the requirements of the standards.

Entities must also consider and draft disclosures required by AASB 108 for the effects of AASB 15 and AASB 1058.

Financial Instruments

AASB 9 *Financial Instruments* supersedes previous versions of the standard (AASB 9 (2014)) and AASB 139 *Financial Instruments: Recognition and Measurement*. It applies to annual reporting periods beginning on or after 1 January 2018 and is available for early adoption. Application is retrospective so comparatives will require restatement in the prior period to the extent possible.

AASB 9 simplifies the model for classifying and recognising financial assets from four categories into three categories – financial assets as measured at amortised cost and financial assets measured at fair value through profit or loss (FVTPL) or through other comprehensive income (FVOCI). The two criteria used to determine how financial assets should be classified and measured are the entity's business model for managing the financial asset and the contractual cash flow characteristics.



Financial assets that are held in a business model to collect the contractual cash flows are measured at amortised cost. Those held in a business model whose objective is achieved by both collecting contractual cash flows and selling the financial asset are measured at FVOCI. When sold, the final effect is 'recycled' through the profit and loss. Any financial assets that are not held in one of the two business models noted above are measured at FVTPL. As such FVTPL represents the 'residual" category.

Arguably there is also a fourth category, as an entity can make an irrevocable election at initial recognition for certain equity instruments that would normally be measured at FVOCI. Under this approach there is no 'recycling' though the Profit and Loss when, or if, eventually sold. This, for example, is the category Councils will likely classify their equity investment in the Tasmanian Water and Sewerage Company Pty Ltd. These investments are currently treated by all Councils as an available-for-sale equity investment under AASB 139. This is a bit of a misnomer, as these long term strategic investments have never been, 'available-for-sale', but rather available-for-sale is the current residual category under AASB 139.

AASB 9 adopts an 'expected loss model' for impairment assessment, where expected losses are recognised throughout the life of a loan or other financial asset measured at amortised cost and not only after a loss event has been identified. The revised standard no longer requires a credit event (e.g. a receivable is past due) to have occurred before credit losses are recognised. Entities will need to ensure they develop a process to demonstrate their own history of past events and current conditions, when determining expectations of credit losses. Unless rebutted with reasonable and supportable information, the standard works on the presumption that credit risk increases when contractual payments are more than 30 days past due and risk of default increases when 90 days past due. As a result, impairment losses will be recognised earlier and at more regular intervals than under the existing 'incurred loss model' of AASB 139.

The standard also includes an improved hedge accounting model to better link the economics of risk management with its accounting treatment. There is no longer a need to separate embedded derivatives from their financial asset hosts. Instead, the entire instrument is assessed for classification.

Detailed application guidance is included in the appendices for assistance. Entities that hold investments under the current AASB 139 classifications of loans and receivables, held to maturity and available-for-sale, will need to reclassify them in line with their applicable business model on transition to AASB 9. Being a fully retrospective standard applicable for the 2019-20 reporting period, entities need to need to ensure that they are currently capturing information they will need for comparative purposes.

Australian Implementation Guidance for Not-for-Profit Entities

AASB 2016–8 *Australian Implementation Guidance for Not-for-Profit Entities*, inserts Australian requirements and authoritative implementation guidance into AASB 9 and AASB 15, to assist NFP entities apply these standards to certain transactions and other events. It aligns with these standards to apply to annual periods beginning on or after 1 January 2019 (the 2019-20 reporting period).

The AASB 9 amendments address the initial measurement and recognition of non-contractual receivables (such as taxes, rates and fines) arising from statutory requirements.

The AASB 15 amendments address the following aspects of accounting for contracts with customers:

- identifying a contract with a customer
- identifying performance obligations
- allocating the transaction price to performance obligations.

Early application is permitted, provided AASB 1058 is also applied.

Leases

The AASB issued a new leasing standard AASB 16 *Leases* in February 2016 to supersede the existing standard AASB 117 *Leases*. It applies for annual reporting periods beginning on or after 1 January 2019 (the 2019-20 reporting period), although early application is permitted provided AASB 15 is also applied. AASB 16 keeps the same accounting principles for lessors as in AASB 117. However, it eliminates the differentiation between operating and finance leases from the lessee's perspective by introducing a single lessee accounting model.

Under the new standard for lessees, the present value of future operating lease payments are capitalised and included on the balance sheet as a right-of-use lease asset with a corresponding lease liability. The right-of-use asset is then be subject to depreciation, while the lease payments, less the financing effect of interest, are recognised against the lease liability resulting in its amortisation over the lease term. This process is similar to how lessees currently account for other debt instruments including finance leases under AASB 117.

CHANGES TO LESSEE ACCOUNTING

Former operating leases capitalised similar to finance leases.

Balance sheet	Income statement	Cash flow statement
↑ Leased / right-of-use assets	↑ Depreciation expenses	↓ Operating cash outflows
↑ Financial liabilities	↓ Lease expenses	↑ Financing cash outflows
↓ Equity	↑ Finance costs	

Also additional disclosure requirements.

Under this model, the lessee recognises most operating leases on balance sheet, with short term leases less than 12 months and low value leases (individual assets with values less than, say, $7 500) as the only exemptions. Entities can present leased assets in their financial statements in a separate category of leased (right-of-use) assets, or together within the property, plant and equipment category.

Lessees will also likely see an impact in other statements. In the Statement of Comprehensive Income, the financing component of the lease expense will result in a larger portion of interest expense skewed to year one and then decreasing over the lease term as the lease liability declines. (The total cost of the lease over the entire lease term of course remains the same.)

In the Statement of Cash Flows the actual cash expense will remain the same, but the operating lease expense will be replaced with a finance liability repayment component (which will be lower in earlier years) and a finance cost component; often a financing activity (which will be higher in the early years).

The recognition of all lease assets and liabilities on balance sheet will increase the net debt of lessees. This grossing-up in the balance sheet may also cause a deterioration in debt ratios and return on assets compared with current reporting. While the net impact on operating surpluses is expected to be marginal, certain other performance and regulatory ratios may also be impacted. Entities may need to review how key performance ratios and indicators are impacted and communicate these with those charged with governance and other stakeholders. Impacts on future procurement practices, budgets and long term plans may also need revision.

A number of practical implementation challenges have been identified with the new standard. For example, working out the interest or discount rate implicit in the lease. Where this cannot be readily determined, the standard provides users with the option to use their incremental borrowing rate that would align with the lease term and security arrangements. Another anomaly likely to be common among longer term leases is variations in lease payment amounts arising from consumer price index increases will trigger re-measurement of the lease asset/liability in subsequent periods.

The new standard will drive a need for entities to critically assess how they manage existing leases and how they intend to transact in future lease negotiations. The effects of the financing expense component in early years may see a reduction in lease terms being adopted, along with a greater focus on non-lease components. There is an option to make an accounting policy election by lessees to recognise the lease and non-lease components as a single lease component on the balance sheet, but this would have the effect of increasing the total lease obligation. This could be an appealing option when non-leasing components are not significant. Under certain conditions there are also exemptions for leases of 12 months or less and leases of low value items (e.g. laptops or small items of furniture).

The standard provides two implementation options, full retrospective application to each prior reporting period presented, or retrospectively with a cumulative catch-up to the date of application. If the cumulative catch-up approach is adopted, comparative information is not required. This may provide some cost relief on transition, however this approach will not provide the same quality of information to users. Entities are encouraged to review their own situation including their current leasing arrangements when making their choice on implementation. Being a retrospective standard, entities need to ensure that they are currently capturing information they will require in future for comparative purposes.

Application guidance is included in the appendices and includes a flowchart to assist entities in making the assessment of whether a contract is, or contains a lease. Implementation examples are also available.

Preparing for changes to the leasing standard

Entities that use leases are encouraged to familiarise themselves with the standard, which will require significantly more effort. In preparation for implementing this new leasing standard, entities should:

- consider whether the impact must be disclosed before the application date, as either 'full' or 'cumulative' as retrospective application will be required on adoption
- assess and ensure registers/databases capture all operating leases
- identify changes required to internal processes or systems in order to capture the necessary information for processing and reporting purposes
- prepare for the significantly increased disclosures
- review service agreements to determine if it contains an embedded finance or operating lease that will need to be segregated from the service element to be reported on balance sheet
- plan appropriate training for affected staff in areas such as such as finance, and legal staff

- discuss proposed income recognition policies and financial statement disclosures with auditors
- consider the impact on budgetary forecasts and reporting to stakeholders regarding financial position and performance
- ensure governance committees and other stakeholders are adequately informed.

Audit Committees and those charged with governance should:

- understand the new standard and ensure management has adequately planned for its effective application, including disclosing the impact in the next financial report
- consider and confirm management's determination of previous off balance sheet leases and the retrospective implementation approach
- monitor progress against the plan and against the requirements of accounting standards.

Service Concession Arrangements: Grantors

The AASB issued the new standard AASB 1059 *Service Concession Arrangements: Grantors*, in July 2017 to address the gap in accounting for service concession arrangements (SCAs) from a public sector grantor perspective. It applies for annual reporting periods beginning on or after 1 January 2019 (the 2019-20 reporting period), although early application is permitted.

Public sector entities (grantors) often enter into contractual service arrangements to engage private sector businesses to design, finance and build infrastructure for the delivery of public services and to provide operational/management services. These are commonly referred to as SCAs, where the grantor is granting the right to operate. This includes public private partnership (PPP) arrangements where a private sector operator is providing a public asset or service to a State entity.

The aim of the standard is to ensure consistent, more transparent and comparable reporting of such arrangements by grantors. AASB 1059 requires the grantor to recognise the assets and liabilities of SCAs where the grantor controls or regulates the service potential and underlying asset. The grantor is required to initially measure SCAs at their fair value with the liability measured at the same amount. The adoption of this approach will result in the earlier recognition of assets and liabilities on a grantor's balance sheet.

Under the standard:

- there will be an earlier recognition of social infrastructure PPP's on the balance sheet, at the earlier of commencement of construction or contractual arrangement. This will bring forward the timing of the corresponding liability's recognition, and change the phasing profile of the net debt impact
- economic infrastructure PPPs will be brought onto balance sheet. The service concession asset will be recognised at its fair value with a corresponding deferred liability recognised as unearned revenue. This has no impact on net debt as it is not affecting financial assets or liabilities upon its initial recognition. The treatment may generate a positive impact on net result from transactions during the earlier years of the arrangement, because the phasing of depreciation over the useful life of the asset may be lower than the revenue recognised in each period over the shorter service concession period.

Whilst such arrangements are not prevalent in Tasmania, entities contemplating SCAs will need to consider their reporting requirements and financial impacts. Although the standard is retrospective, there is a choice of full retrospective restatement or a modified approach. The modified approach provides relief to those entities that may find it difficult to establish prior period information including replacement costs. Application guidance and implementation examples are included in the appendices.

Service Performance Reporting

The AASB issued ED 270 *Reporting Service Performance Information* for comment which closed 29 April 2016. The AASB are currently reviewing responses and conducting a literature review.

FINANCIAL AUDIT DEVELOPMENTS

CHANGES TO AUDITOR'S REPORT

In 2017-18 we will be continuing with our staged approach to the implementation of the new auditing standard, ASA 701 *Communicating Key Audit Matters* in the Independent Auditor's Report. In 2016-17, all Government Business Enterprises and State Owned Companies' auditor's reports included a section on key audit matters (KAMs). KAMs are matters which the auditor determines were of most significance to the audit, and are selected by taking into account areas of higher risk, significant auditor judgements, and the effect on the audit of significant events or transactions. We consider the reporting of KAMs improves the transparency of the audit process.

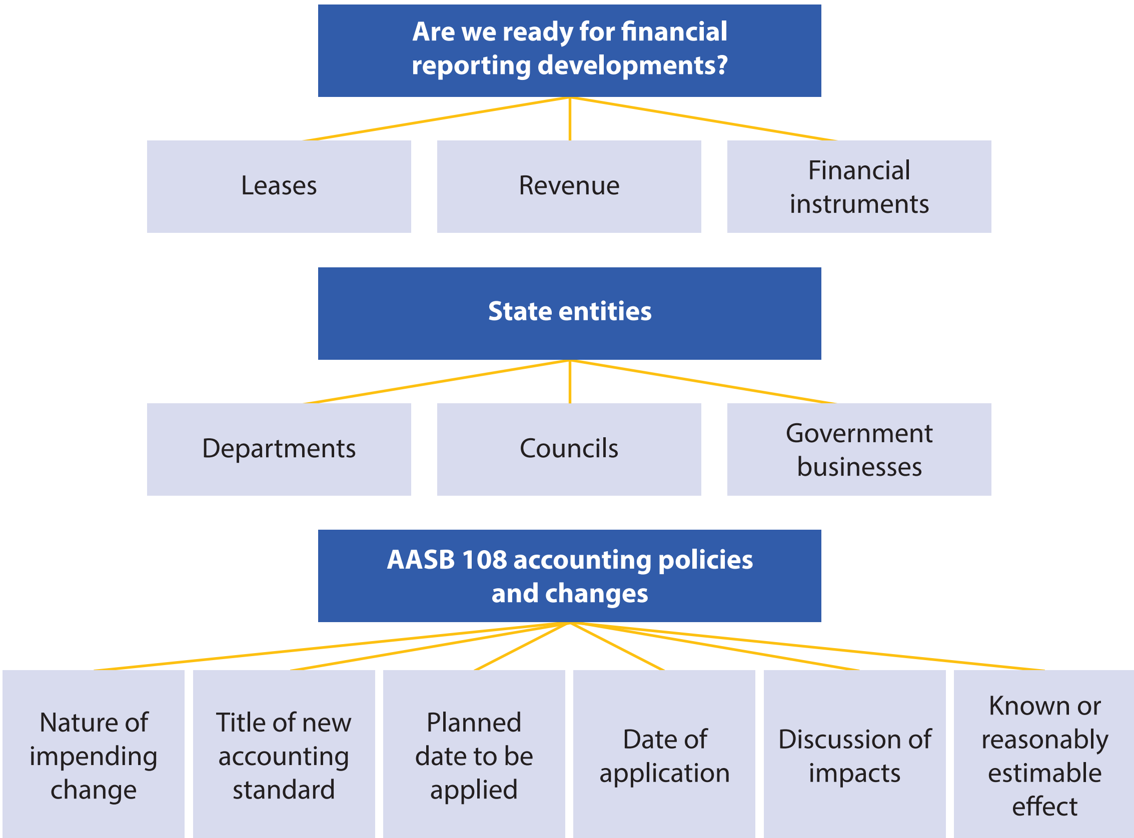
The KAM section of the auditor's report includes:

- a brief description of the key audit matters
- why audit considered them to be key to the audit
- what procedures were performed to address the matter.

In 2017-18, all government departments will include KAMs in their auditor's reports and in 2018-19 KAMs will be considered for all remaining State entities subject to audit.

PUBLIC SECTOR READINESS

SNAPSHOT



WHY DO WE NEED TO THINK ABOUT DEVELOPMENTS IN FINANCIAL REPORTING?

AASB 108 *Accounting Policies, Changes in Accounting Estimates and Errors*, requires entities to disclose the effect of accounting standards that have been issued up to, and including, when first adopted. From a user's or reader's perspective, AASB 108 provides a guide to what is pending and what may be impacting the entity in the near future.

As the effective date for a new standard becomes nearer, entities should be able to provide stakeholders with relevant and accurate information on the likely impacts of the new standard. As noted in the previous Chapter, there are a number of very significant changes pending in AASs. Many of these will not only affect financial reporting and disclosure, but may also have some operational impacts. Entities will need to scrutinise all new accounting developments to ensure they are appropriately planning for future operational implications and minimise surprises to users of the financial reports.

ARE WE READY FOR DEVELOPMENTS IN FINANCIAL REPORTING?

All entities will need to understand how and to what extent they will be impacted by ever changing accounting standards. Three key areas noted in the section *Looking Further Forward* of the previous Chapter were:

- Revenue (AASB 15 *Revenue from Contracts with Customers* and AASB 1058 *Income of Not-for-Profit Entities*)
- Financial instruments (AASB 9 *Financial Instruments*)
- Leases (AASB 16 *Leases*).

It is these three areas that this Chapter focuses, as all entities derive revenue, all have some form of financial instruments, even if it's just cash and receivables, and most have leases.

As noted previously, when preparing annual financial statements, AASB 108 requires an entity to disclose information when it has not yet applied a new accounting standard that has been issued, but is not yet effective. This disclosure includes known, or reasonably estimable, information relevant to assessing the possible impact that initial application will have on the entity's financial statements.

In this section, we look at a selection of Tasmanian State sector entities to gain an insight into compliance with AASB 108, including how prepared they are for new standards.

In our review, we looked at entities in three main groupings of State entities:

- Public Non-Financial Corporations (Government Businesses)*
- Departments
- Local Government (Urban Councils)

** For the purposes of this Chapter, these entities will be referred to as Government Businesses*

Our assessments discusses the preparedness in each of these three groupings. Before we do, it is important to understand what the disclosure requirements actually are.

Prescribed disclosure requirements

In Australia, AASB 108, prescribes the compulsory disclosure requirements. AASB 108 is based on the international version of the same name issued by the IASB, IAS 8.

AASB 108 requires:

30 *When an entity has not applied a new Australian Accounting Standard that has been issued but is not yet effective, the entity shall disclose:*

- *(a) this fact; and*
- *(b) known or reasonably estimable information relevant to assessing the possible impact that application of the new Australian Accounting Standard will have on the entity's financial statements in the period of initial application.*

31 *In complying with paragraph 30, an entity considers disclosing:*

- *(a) the title of the new Australian Accounting Standard;*
- *(b) the nature of the impending change or changes in accounting policy;*
- *(c) the date by which application of the Australian Accounting Standard is required;*
- *(d) the date as at which it plans to apply the Australian Accounting Standard initially; and*
- *(e) either:*
  - *(i) a discussion of the impact that initial application of the Australian Accounting Standard is expected to have on the entity's financial statements; or*
  - *(ii) if that impact is not known or reasonably estimable, a statement to that effect.*

Generally these requirements are presented in the notes to the financial statements as a listing of pending accounting standards including a short description of their likely impacts. Where the effects are yet to be determined, this is also disclosed.

Given the standards relating to all the areas of this review were issued some years ago, we would have expected entities to be well advanced in their assessment of impacts. It is also pertinent to note that these standards are all retrospective, meaning entities will need to ensure they collect information prior to the standard's application date to determine comparative amounts. As discussed in the *Reporting in 2017-18* section of the previous Chapter on *Developments in Financial Reporting*, there is variability in fully retrospective and cumulative catch-up approaches available and these affect when and what adjustments are made to equity. There are also some practical expediencies contained in transitional arrangements that provide some relief to what could be an onerous and costly process.

Whatever approach is taken, how an entity choses to adopt and implement these new standards requires serious consideration, not only from a financial statement presentation viewpoint, but also from an operational perspective, as on so many levels these standards may impact business operations.

WHAT WE FOUND

While a few entities presented disclosure of future accounting standard impacts well, there were quite a number of instances where there appeared to be a lack of understanding, non-engagement or standard template wording (boiler-plating) with short inadequate comments. This was evident where standards quoted were incorrect, had already been applied or didn't actually need to be included thereby adding clutter.

Examples of other observations included:

- a high proportion of entities were yet to assess impacts
- discussion of likely impacts were generally inadequate considering the length of time since these standards were released
- assessments stating "no expected impact" to certain standards was contrary to other accompanying financial statement disclosures, such as:
    - AASB 15 – significant revenue was derived from exchange transactions
    - AASB 1058 – entities received significant capital grants
    - AASB 9 – entities held significant financial assets or liabilities
    - AASB 16 – entities held significant leasing commitments
- quantification of estimable effects was rare
- no explanations on the method to be adopted on transition, fully retrospective or cumulative.

All entities need to be cognisant that disclosure requirements for pending accounting standards requires more than just a listing those that are relevant. Even where impacts may appear to be minimal, there is a need to revise policies to ensure appropriate compliance with changing recognition and disclosure requirements. Entities need to ensure they are fully informed and understand what effects each new standard brings.

It is evident from this review that many entities need to revisit and complete a revised assessment of the potential impacts of pending accounting standards on their entity. Our financial audit teams we will be engaging individually with entities during the course of the 2017-18 audits to ensure appropriate attention is applied to the significant changes ahead and appropriate presentation in financial statements.

AGENCY AUDIT COMMITTEES

BACKGROUND

Audit Committees play a key accountability role in the governance framework of Tasmanian public sector agencies. While management retains ultimate accountability for operations, the Audit Committee should independently review and assess the effectiveness of key aspects of operations.

In accordance with the *Financial Management and Audit Act 1990*, agencies are required to comply with *Treasurers Instructions*, which require each agency to have an Audit Committee and sets out the core requirements, responsibilities and functions the Audit Committee should comply with.

OBJECTIVE

We reviewed the effectiveness of the governance arrangements for the Audit Committees of all eight Departments in the Tasmanian public sector and the Tasmanian Health Service (referred to individually as agency and collectively as agencies in this section).

Our review assessed composition, operational arrangements, and the roles and responsibilities of Audit Committees in agencies against the requirements set out in the:

- Treasurer's Instruction TI 108 *Internal Audit*
- ANAO better practice guide.

The majority of the information assessed was documented in the current Charters of Audit Committees (referred to, in this section, as Charters).

COMPOSITION OF AUDIT COMMITTEE

An effective Audit Committee will comprise of members that:

- have an appropriate mix of skills and experience relevant to responsibilities of the agency
- are independent of management
- act objectively and impartially.

The number of Audit Committee members and the skills and experience that members require depends of the complexity, nature and scale of the agency's responsibilities, activities and systems.

Figure 11 summarises our assessment of compliance, by agencies, with the Audit Committee composition requirement in the Treasurer's Instruction.

Figure 11: Audit Committee composition — Treasurer's Instruction requirement

Requirement	Compliance
Minimum of 3 members	9/9

We also reviewed the independence of Audit Committee members against the better practice elements outlined in the ANAO better practice guide. The results of this review are provided in Figure 12.

Figure 12: Audit Committee composition and independence — better practice

ANAO better practice guide	Included in Charter
Majority of independent members	2/9
Appointment of external Chair	4/9
Member positions restrict independence	3/9

Each of the Audit Committees reviewed had at least the minimum of three members in accordance with the Treasurer's Instruction and the ANAO better practice guide. However, the Audit Committees of:

- five agencies did not have an independent Chair
- seven agencies did not have a majority of independent members.

Several of the members that were not independent:

- were Accountable Authorities, who have responsibility for the financial management of the agency
- acted in positions that make operational decisions for the agency, such as Chief Operating Officer, Chief Information Officer, Head of Corporate Services or Head of Internal Audit.

The Audit Committee members described above will be unable to provide independent assurance and advice to the Accountable Authority on the operations of the agency as they may have been involved in the making of operational decisions.

While the requirement under the Treasurer's Instruction for the Accountable Authority to appoint Audit Committee members reduces the degree of independence from management, there are a number of ways to strengthen the Audit Committee's actual and perceived independence. Options include:

- appointing an external Chair who can perform his or her role unencumbered by any management responsibilities
- appointing committee members who exhibit an independence of mind in their deliberations and do not act as a representative of a particular area within the agency or a particular stakeholder interest
- in the context of the committee having appropriate skills and experience, rotating Audit Committee members to enable new knowledge and experience to be introduced periodically to the committee
- ensuring the Audit Committee itself has no management responsibilities
- having policies in place to facilitate timely identification of changing relationships or circumstances that may affect the independence of Audit Committee members, including potential conflicts of interest.[1]

Recommendation 1

The Treasurer's Instruction is amended to ensure the composition of the Audit Committee supports an adequate level of independence to meet the required functions. The required composition should include:

- the appointment of an external chair
- the majority of members are independent/external
- regular rotation of Audit Committee membership.

MANAGING AUDIT COMMITTEES

In addition to having an appropriate composition, the operation of an Audit Committee is enhanced through appropriate support and management processes.

Figure 13 summarises our assessment of Audit Committee support and management against the better practice elements outlined in the ANAO better practice guide.

1. ANAO, *Public Sector Audit Committees: Independent assurance and advice for Accountable Authorities*, March 2015

Figure 13: Management of Audit Committees — better practice

ANAO better practice	Agencies
Charter up-to-date	2/9
One or more sub-committees established	1/1*
Effective secretariat support provided	9/9
Meeting agendas prepared	9/9
Forward meeting schedule in place	9/9
Assurance map utilised	3/9

**The other eight agencies deemed the use of a sub-committee to be not applicable.*

All agencies generally had sound management practices for their Audit Committees, with effective secretariat support, forward meeting schedules and meeting agendas.

Each Audit Committee had a Charter in place in accordance with the Treasurer's Instruction, however we noted that seven of the nine Charters had not been reviewed and updated in accordance with the prescribed timeframe. The ANAO better practice guide suggests the Charter should be reviewed and, where necessary, updated on an annual basis.

Only one out of the nine agencies reviewed had a sub-committee. The other agencies had assessed the use of sub-committees as not applicable to their needs of their agency.

Six out of the nine agencies had not commissioned an assurance map to help assist their management responsibilities. Entities typically have a variety of assurance mechanisms and arrangements including the control framework, internal audit and external audit. An agency-wide perspective of assurance activities can help the Audit Committee identify gaps or duplication. It can also help identify key risks that are not being addressed by any assurance activities.

Recommendation 2

The Treasurer's Instruction is amended to include the following requirements:

- Audit Committee Charters are reviewed and, where necessary, updated on an annual basis
- Audit Committee's commission an annual assurance map.

ENGAGEMENT WITH EXTERNAL AUDIT

A positive relationship with the external auditor, in this case the TAO, assists the Audit Committee to obtain insight into the effectiveness of risk, control, financial reporting and legislative-compliance frameworks.

The Treasurer's Instruction requires the Audit Committee to have a Charter that establishes its oversight of external audit functions.

We reviewed the Charters against the relevant elements of the ANAO best practice guide on engaging with external audit. The findings of this review are presented in Figure 14 over the page.

Figure 14: Engagement with external audit — good practice

ANAO better practice guide	Included in Charter
Provide input on, and discuss planned TAO financial and performance audit coverage	8/9
Monitor management's responses to all TAO financial statement management letters and performance audit reports, including implementation of recommendations	9/9
Provide advice to the accountable authority on action taken on significant issues raised in relevant TAO reports	9/9
Have a members-only meeting with the TAO at least once per year so that the committee can obtain the views of the TAO without internal audit or management being present	1/9
Periodically review the performance of external audit, and report the results to the Accountable Authority.	1/9

All Charters complied with the requirements of the Treasurer's Instruction to establish the roles and responsibilities of the Audit Committee in relation to external audit functions. They also generally comply with the ANAO better practice guide to have input on audit coverage and to monitor responses and action taken by management to address issues raised.

It was noted only one out of the nine Charters reviewed required the Audit Committee to hold members-only meetings with external audit and periodically review the performance of external audit.

Recommendation 3

Audit Committee Charters are amended to include the following roles and responsibilities in relation to engagement with external audit:

- have a members-only meeting with the TAO at least once per year so that the committee can obtain the views of the TAO without internal audit or management being present
- periodically review the performance of external audit, and report the results to the Accountable Authority.

FINANCIAL REPORTING OVERSIGHT

It is an important role of Audit Committees to review the financial reporting responsibilities of agencies and advise the Accountable Authority on the results of the review. The primary financial reporting responsibilities consist of the preparation of annual financial statements and the inclusion of the audited financial statements in the annual report.

The Treasurer's Instruction does not specifically refer to financial reporting as part of the oversight functions of an Audit Committee. However, it does specify that the oversight function includes the statutory and fiduciary duties of the agency. These duties include financial reporting.

We assessed the requirements of Audit Committees relating to oversight of financial reporting, as specified in the Charters, against the ANAO better practice guide. The findings are provided in Figure 15 over the page.

Figure 15: Financial reporting — good practice

ANAO better practice	Included in Charter
Review the financial statements and provide advice to the Accountable Authority (including recommending their signing by the Accountable Authority)	9/9
Ensure compliance with accounting standards	5/9
Review the appropriateness of accounting policies and disclosures, including any significant changes to accounting policies	5/9
Review areas of significant judgement and financial statement balances that require estimation	3/9
Review significant or unusual transactions	1/9
Ensure sign-off by management in relation to the quality of the financial statements, internal controls and compliance	5/9
Review the auditor's judgements about the adequacy of the accounting policies and the quality of the processes for the preparation of financial statements, through discussions with the external auditor	1/9
Ensure appropriate management action has been taken in response to any issues raised by the external audit, including financial statement adjustments or revised disclosures	7/9
Review the processes in place designed to ensure that financial information included in the annual report is consistent with the signed financial statements.	3/9

All of the Charters reviewed included responsibility for the Audit Committee to review the financial statements and provide advice to the Accountable Authority. However, the degree of detail provided in the Charter around this responsibility varied.

The functions least often prescribed were around the review of:

- significant judgements and estimations
- significant or unusual transactions
- external auditor's judgements.

These areas and transactions would generally be deemed to be at the greatest risk of material misstatement and therefore should be the major focus of the Audit Committee's review.

Recommendation 4

The Treasurer's Instruction is amended to include reviewing the financial reporting responsibilities and financial report as a role in the Audit Committee's oversight function.

Audit Committee Charters are more specific on the role of the Audit Committee in reviewing financial reporting responsibilities and the financial report.

PERFORMANCE REPORTING OVERSIGHT

The role of Audit Committees in relation to performance reporting will depend on the performance measurement requirements of agencies. The Treasurer's Instruction does not specifically refer to performance reporting as part of the oversight functions of an Audit Committee, but notes that Audit Committees must meet the statutory and fiduciary duties of agencies.

At a minimum, Audit Committees should have a good understanding of the approach to measuring performance and how performance is reported.

Figure 16 summarises our assessment of the Charters against the elements of the ANAO better practice guide that relate to performance reporting.

Figure 16: Performance reporting — good practice

ANAO better practice	Included in Charter
Review the systems and procedures for assessing and reporting performance	1/9
Satisfy itself that Budget Statements and/or corporate plan include details of how performance will be measured and assessed	1/9
Ensure that the approach to measuring its performance throughout the financial year against the performance measures included in Budget Statements and/or corporate plan is sound, and has taken into account guidance issued by Treasury	1/9
Ensure the proposed performance statement is not inconsistent with financial information, including its financial statements, which will be included in the annual report.	1/9

Performance reporting has been largely ignored in the Charters. There was only one agency that referred to performance reporting within the Audit Committee Charter as being a function for which the committee has oversight responsibility.

Recommendation 5

The Treasurer's Instruction is amended to include reviewing performance reporting responsibilities and as a role in the Audit Committee's oversight function.

Audit Committee Charters include the oversight of performance reporting as part of their roles and responsibilities.

OVERSIGHT OF RISK MANAGEMENT

Risk management is an essential part of effective corporate governance. The ultimate responsibility for the management of risk is with the Accountable Authority of the agency. However, it is expected that the Accountable Authority will seek assurance from the Audit Committee that the risk management arrangements are appropriate and effective.

The Treasurer's Instruction does not specifically require the oversight of risk management to be part of the Audit Committee's responsibilities.

Recommendation 6

The Treasurer's Instruction is amended to include the oversight of the Agency's risk management function as a responsibility and as a role of the Audit Committee.

The Treasurer's Instruction does refer specifically to the management of fraud risk requiring the Audit Committee to assist the Head of Agency in their oversight function, to ensure appropriate management of the exposure to fraud risk. Despite this, the responsibility is not clearly defined or referred to in three out of the nine Charters reviewed.

We also reviewed the role of Audit Committees in relation to the oversight of risk management against the ANAO better practice guide. The results are summarised in Figure 17.

Figure 17: Risk management oversight — good practice

ANAO better practice	Included in Charter
Review whether management has in place a current and sound enterprise risk management framework and associated internal controls for effective identification and management of business and financial risks, including fraud	6/9
Satisfy itself that a sound approach has been followed in managing the highest risks including those associated with individual projects, program implementation, and activities	5/9
Review the process of developing and implementing fraud control arrangements and satisfy itself that there are appropriate processes and systems in place to detect, capture and effectively respond to fraud risks	2/9
Review reports on fraud from management that outline any significant or systemic allegations of fraud, the status of any ongoing investigations and any changes to identified fraud risk	1/9
At least annually, commission an agency-wide assurance map that identifies key assurance arrangements	1/9

Recommendation 7

Audit Committee Charters include the oversight of the Agency's responsibility to manage the exposure to fraud risk in order to ensure that the Audit Committee complies with the Treasurer's Instruction.

SYSTEM OF INTERNAL CONTROL

The internal control responsibilities of Audit Committees are expected to include reviewing the adequacy of the internal control environment and providing assurance to management that processes are in place to provide feedback that key controls are operating as intended.

We also reviewed the Audit Committee Charters against the requirements in the Treasuer's Instruction and the expected Audit Committee responsibilities identified in the ANAO better practice guide relating to:

- the internal control framework
- engagement with internal audit
- legislative and policy compliance
- business continuity management
- delegations.

INTERNAL CONTROL FRAMEWORK

This function is specifically required by the Treasurer's Instruction that states the Audit Committee is to assist the Head of Agency in its oversight function to "…ensure internal controls are operating effectively".

Figure 18: Internal control framework — Treasurer's Instruction requirement

Requirement	Compliance
Audit Committee Charters are clear on their role related to internal controls	5/9

Despite being a requirement in the Treasurer's Instruction, the responsibility is clearly defined or referred to in just five out of the nine Audit Committee Charters reviewed. It is critical for the Charter to communicate all key roles and responsibilities of the Audit Committee to ensure the members understand and comply with the Treasurer's Instruction.

We also reviewed the Audit Committee Charters against the expected Audit Committee responsibilities identified in the ANAO better practice guide relating to the internal control framework.

Figure 19: Internal control framework — good practice

ANAO better practice	Included in Charter
Review management's approach to maintaining an effective internal control framework; this framework should include controls in relation to functions performed by external parties such as contractors and advisers	5/9
Review whether management has in place relevant policies and procedures, including Accountable Authority Instructions or their equivalent, and that these are periodically reviewed and updated	3/9
Satisfy itself that appropriate processes are in place to assess whether key policies and procedures are complied with	3/9
Satisfy itself that management periodically assesses the adequacy of information security arrangements, including complying with reporting obligations.	2/9

The majority of Charters did not require the review of:

- relevant policies or procedures
- associated compliance
- the adequacy of information security arrangements.

LEGISLATIVE AND POLICY COMPLIANCE

Agencies must comply with a considerable volume of complex legislation and policy. As a result, it is generally expected that Audit Committees would focus on aspects that pose the highest risk to the agency.

We reviewed the requirements in the Charters relating to legislative and policy compliance against the ANAO better practice guide in Figure 20.

Figure 20: Legislative and policy compliance

ANAO better practice	Included in Charter
Review the effectiveness of systems for monitoring compliance with relevant laws, regulations and associated government policies	3/9
Determine whether management has appropriately considered legal and compliance risks as part of the enterprise risk management plan	4/9
Provide advice to the Accountable Authority regarding the issue of the annual Compliance Report	1/9
Assess whether management has taken steps to embed a culture that promotes the proper use and management of public resources and is committed to ethical and lawful conduct.	4/9

The majority of Charters reviewed did not:

- establish oversight over the systems and controls in place to ensure compliance with legislation and policies relevant to the agency
- promote a positive culture and attitude around the adherence to legislative requirements and appropriate use of public resources.

In addition, only one of the nine Charters required the Audit Committee to provide advice on the preparation of an annual compliance report.

INTERNAL AUDIT OVERSIGHT

The Treasurer's Instruction details the requirements of Audit Committees in relation to internal audit oversight. Audit Committees are required to review the implementation of:

- the annual Internal Audit Plan
- implementation of audit recommendations
- identify areas worthy of examination
- provide a forum for discussing problems and issues that may affect the operations of the internal auditor.

Each of the Charters reviewed clearly established the role of the Audit Committees in relation to internal audit oversight.

Figure 21 summarises the findings of our review of the requirements in the Charters relating to internal audit against the ANAO better practice guide.

Figure 21: Internal audit oversight

ANAO better practice	Included in Charter
Review the proposed internal audit coverage, ensure the coverage takes key risks into account, and recommend approval of the Internal Audit Work Plan by the Accountable Authority or nominated delegate	9/9
Review all audit reports and provide advice to the Accountable Authority on significant issues identified in audit reports and recommend action on significant issues raised, including identification and dissemination of good practice	8/9

ANAO better practice	Included in Charter
Obtain an annual report from the Head of Internal Audit, or the outsourced internal audit service provider, on the overall state of the internal controls	2/9

Generally the Charters covered the areas of better practice with the exception of obtaining an annual report from the Head of Internal audit on the overall state of internal controls.

BUSINESS CONTINUITY MANAGEMENT

As part of the internal control environment, agencies are expected to have well designed business continuity and disaster recovery arrangements and the Audit Committee should satisfy itself these arrangements are in place.

We reviewed the requirements in the Charters relating to business continuity management against the ANAO better practice guide in Figure 22.

Figure 22: Business continuity management

ANAO better practice	Included in Charter
Satisfy itself that a sound approach has been followed in establishing the business continuity planning arrangements, including whether business continuity and disaster recovery plans have been periodically updated and tested.	3/9

DELEGATIONS

Delegations are another important element of the system of internal control. A review of the delegations by the Audit Committee is considered to be good practice.

Figure 23 summarises our review of Charters in respect to the requirement for Audit Committees to review delegations.

Figure 23: Delegations

ANAO better practice	Included in Charter
Review whether appropriate policies and associated procedures are in place for the management and exercise of delegations and authorisations.	2/9

Recommendation 8

It is recommended that the Treasurer's Instruction expands the oversight functions of the Audit Committee around the system of internal control to include:

- oversight of the Agency's system of internal control in order to ensure that the Audit Committee complies with the Treasurer's Instruction
- oversight of the Agency's systems for monitoring legislative and policy compliance
- promotion of ethical and lawful conduct
- obtaining an annual report from Internal Audit on the overall controls of the Agency
- business continuity management
- delegations

CONCLUSION

There is significant room for improvement in the governance arrangements for Audit Committees.

The independence of Audit Committees is the most critical area that needs to be addressed. We found that Audit Committees generally did not have a majority of independent members, an independent Chair and several instances where members held conflicting management positions within agencies.

While the managerial and operational support of Audit Committees was adequate, Audit Committees should also be supported in:

- reviewing Charters at least annually
- updating Charters when required
- establishing an assurance map to identify any duplication or gaps in assurance activities.

Audit Committees were found to successfully engage with external audit. Although Charters could be improved by requiring members-only meetings and review of external audit provider performance.

In relation to Audit Committee oversight functions, agencies had reasonable arrangements for financial reporting and internal audit oversight. However the oversight functions performed by Audit Committees could be improved by:

- clearly defining roles in Charters, particularly around the review of estimations and judgements
- commissioning an annual controls report from internal audit
- including the oversight of risk management, the internal control framework and performance reporting in Charters.

As a result of this review, several recommendations have been made to amend the Treasurer's Instruction, and improve Audit Committee governance arrangements through amendments to Charters.

SUBMISSIONS AND COMMENTS RECEIVED

DEPARTMENT OF TREASURY AND FINANCE

As a general comment, I note that the recommendations in the draft Audit Committee Chapter will require significant resourcing, particularly for smaller agencies, and the recommendations do not allow Heads of Agency to determine appropriate internal audit functions, roles and membership in the context of the particular agency's business requirements.

As you are aware, Treasury is currently reviewing all the Treasurer's Instructions (TI) as part of the implementation of the new *Financial Management Act*. The revised Treasurer's Instructions will be principles based and generally not be as prescriptive as current instructions. However better/best practice guidelines will be issued where relevant. Treasury intends to incorporate 'better practice guidelines' for Internal Audit Committees within the revised Treasurer's Instructions. This flexibility then allows agencies to meet best practice within the context of their business requirements and resourcing. Accordingly, many of Treasury's specific comments in the attachment state that the draft recommendations are more appropriate as 'better practice guidelines'.

RECOMMENDATION 1

The Treasurer's Instruction is amended to ensure the composition of the Audit Committee supports an adequate level of independence to meet the required functions. The required composition should include:

- the appointment of an external chair;
- the majority of members are independent/external; and
- regular rotation of Audit Committee membership.

Treasury Comment

Not considered applicable for inclusion as mandatory within the TI - will be considered for inclusion in guidance material as part of the TI review.

To remain as matters for individual Agencies to consider.

RECOMMENDATION 2

The Treasurer's Instruction is amended to include the following requirements:

- Audit Committee Charters are reviewed and, where necessary, updated on an annual basis; and
- Audit Committees' commission an annual.

Treasury Comment

Not considered applicable for inclusion as mandatory within the TI - will be considered for inclusion in guidance material as part of the TI review.

RECOMMENDATION 3

Audit Committee Charters are amended to include the following roles and responsibilities in relation to engagement with external audit:

- have a members-only meeting with the TAO at least once per year so that the Audit Committee can obtain the views of the TAO without internal audit or management being present; and
- periodically review the performance of external audit and report the results to the Accountable Authority.

Treasury Comment

To remain as matters for individual Agencies to consider.

RECOMMENDATION 4

The Treasurer's Instruction is amended to include reviewing the financial reporting responsibilities and financial report as a role in the Audit Committee's oversight function.

Audit Committee Charters are more specific on the role of the Audit Committee in reviewing financial reporting responsibilities and the financial report.

Treasury Comment

Not considered applicable for inclusion as mandatory within the TI - will be considered for inclusion in guidance material as part of the TI review.

To remain as matters for individual Agencies to consider.

RECOMMENDATION 5

The Treasurer's Instruction is amended to include reviewing performance reporting responsibilities and this responsibility is incorporated into the Audit Committee's oversight function.

Audit Committee Charters include the oversight of performance reporting as part of their roles and responsibilities.

Treasury Comment

Not considered applicable for inclusion as mandatory within the TI - will be considered for inclusion in guidance material as part of the TI review.

To remain as matters for individual Agencies to consider.

RECOMMENDATION 6

The Treasurer's Instruction is amended to include the oversight of the Agency's risk management function as a responsibility and this responsibility to be incorporated into the Audit Committee functions.

Treasury Comment

Not considered applicable for inclusion as mandatory within the TI - will be considered for inclusion in guidance material as part of the TI review.

RECOMMENDATION 7

Audit Committee Charters include the oversight of the Agency's responsibility to manage the exposure to fraud risk in order to ensure that the Audit Committee complies with the Treasurer's Instruction.

Treasury Comment

To remain as matters for individual Agencies to consider.

RECOMMENDATION 8

It is recommended that the Treasurer's Instruction expands the oversight functions of the Audit Committee around the system of internal control to include:

- oversight of the Agency's system of internal control in order to ensure that the Audit Committee complies with the Treasurer's Instruction;
- oversight of the Agency's systems for monitoring legislative and policy compliance;
- obtaining an annual report from internal Audit on the overall controls of the Agency;
- promotion of ethical and lawful conduct;
- business continuity management;
- delegations; and
- ethical and lawful conduct.

Treasury Comment

Not considered applicable for inclusion as mandatory within the TI - will be considered for inclusion in guidance material as part of the TI review.

Tony Ferrall
Secretary

LIST OF ACRONYMS AND ABBREVIATIONS

AAS	Australian Accounting Standards
AMC Search	AMC Search Limited
Audit Act	*Audit Act 2008*
Charters	Charters of Audit Committees
Conceptual Framework	Conceptual Framework for Financial Reporting
Copping	Copping Refuse Disposal Site Joint Authority
EFTSL	Equivalent full time student load
Forestry	Forestry Tasmania Pty Ltd
FTE	Full Time Equivalent
FVOCI	Fair value through profit or loss other comprehensive income
FVTPL	Fair value through profi t or loss
GORTO	Grant of right to operate
Government Businesses	Public Non-Financial Corporations
Grantors	Public sector entities
IASB	Accounting Standards Board
IFRS	International Financial Reporting Standards
IPSAM	Integrated Public Sector Audit Methodology
IPSASB	International Public Sector Accounting Standards Boards
KAMs	Key audit matters
NFP	Not-for-profit
NRAS	National Rental Affordability Scheme
PBSA	Purpose Built Student Accommodation
PPIS	Pitcher Partner Investment Services Pty Ltd
PPP	Public private partnership
RDR	Reduced disclosure requirements
SAC 1	Statement of Accounting Concept 1
SCAs	Service concession arrangements
Sense-Co	Sense-Co Tasmania Pty Ltd
SSAF	Student services and amenities fee
TAFR	Treasurer's Annual Financial Report
TAO	Tasmanian Audit Office
ANAO better practice guide	Australian National Audit Office's *Public Sector Audit Committees: Independent assurance and advice for Accountable Authorities*
Tascorp	Tasmanian Public Finance Corporation
The Council	University Council

The Panel	Government Business Executive Remuneration Advisory Panel
The Treasurer's Instruction	TI 108 *Internal Audit*
The Trust	River Clyde Trust
TI	Treasurer's Instructions
Treasury	Department of Treasury and Finance
TUU	Tasmanian University Union Inc
University	University of Tasmania
University Foundation	University of Tasmania Foundation Inc
UTAS Holdings	UTAS Holdings Pty Ltd

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AUDIT MANDATE AND STANDARDS APPLIED

Mandate

Section 17(1) of the *Audit Act 2008* states that:

> 'An accountable authority other than the Auditor-General, as soon as possible and within 45 days after the end of each financial year, is to prepare and forward to the Auditor-General a copy of the financial statements for that financial year which are complete in all material respects.'

Under the provisions of section 18, the Auditor-General:

'(1) is to audit the financial statements and any other information submitted by a State entity or an audited subsidiary of a State entity under section 17(1).'

Under the provisions of section 19, the Auditor-General:

'(1) is to prepare and sign an opinion on an audit carried out under section 18(1) in accordance with requirements determined by the Australian Auditing and Assurance Standards

(2) is to provide the opinion prepared and signed under subsection (1), and any formal communication of audit findings that is required to be prepared in accordance with the Australian Auditing and Assurance Standards, to the State entity's appropriate Minister and provide a copy to the relevant accountable authority.'

Standards Applied

Section 31 specifies that:

> 'The Auditor-General is to perform the audits required by this or any other Act in such a manner as the Auditor-General thinks fit having regard to –

(a) the character and effectiveness of the internal control and internal audit of the relevant State entity or audited subsidiary of a State entity; and

(b) the Australian Auditing and Assurance Standards.'

The auditing standards referred to are Australian Auditing Standards as issued by the Australian Auditing and Assurance Standards Board.

Tasmanian Audit Office

Cover photo: Tourism Tasmania & Garry Moore

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