Tasmanian Audit Office

Report of the Auditor-General No. 9 of 2018-19

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

Volume 1

State entities 31 December 2018

May 2019

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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.

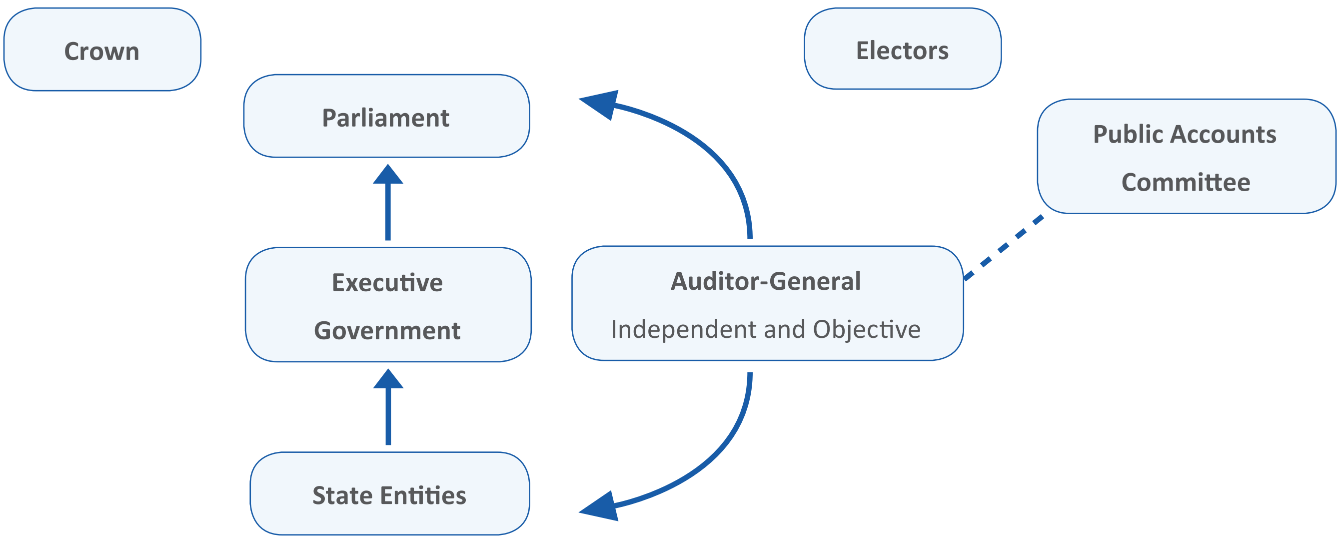
We can also carry out investigations but only relating to public money or to public property. In addition, the Auditor-General is now responsible for state service employer investigations.

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.



2019 (No. 7)

TASMANIA

2019
PARLIAMENT OF TASMANIA

Report of the Auditor-General
No. 9 of 2018-19

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

Volume 1

State entities 31 December 2018

May 2019

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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21 May 2019

President
Legislative Council
HOBART

Speaker
House of Assembly
HOBART

Dear President

Dear Ms Speaker

REPORT OF THE AUDITOR-GENERAL
No. 9 of 2018-19, Auditor-General's Report on the Financial Statements of State entities, Volume 1 - State entities 31 December 2018

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 1 - State entities 31 December 2018.

Yours sincerely

Rod Whitehead
Auditor-General

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EXECUTIVE SUMMARY

INTRODUCTION

This Report is the first volume in our series advising Parliament on the outcome of our financial audits for the 31 December 2018 and 30 June 2019 financial years. This report includes chapters on all 31 December 2018 audits and any 2017-18 audits that have not been included in previous reports. It also includes audits dispensed with and developments in financial reporting and auditing.

GUIDE TO USING THIS REPORT

Guidance relating to the use and interpretation of financial information included in this Report can be found on our website: www.audit.tas.gov.au

The guidance includes information on the calculation and explanation of financial ratios and performance indicators and the definition of audit finding risk ratings.

STATE ENTITIES COVERED IN THIS REPORT

Audits of State entity financial statements included in this Report are:

University of Tasmania and Controlled Entities 31 December 2018

- University of Tasmania
- AMC Search Limited
- Tasmania University Union Inc.
- University of Tasmania Foundation Inc.
- UTAS Holdings Pty Ltd

Other State Entities 31 December 2018

- Theatre Royal Management Board
- Solicitors' Trust
- Anzac Day Trust

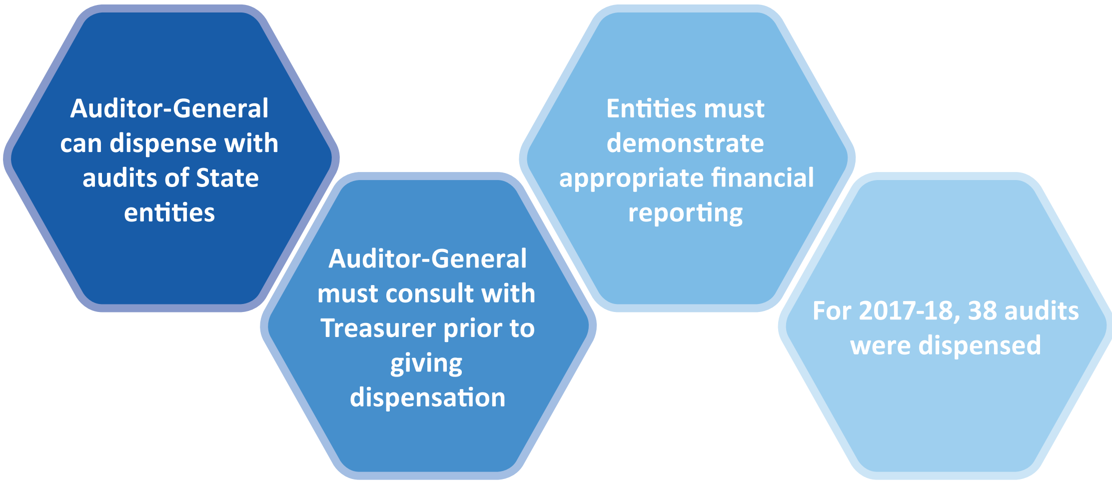
North East Care Incorporated

- 30 June 2016
- 30 June 2017
- 30 June 2018

Audit opinions issued and matters arising from the performance of our audits are summarised below:

Audit opinions	11 Unmodified audit opinions issued		
Audit findings	High Risk	Moderate Risk	Low Risk
Internal control findings reported	0	4	2
Accounting issues reported	0	1	0
Unresolved prior year findings	0	2	3

AUDITS 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. For 2017-18, 38 audits were dispensed.

FINANCIAL REPORTING DEVELOPMENTS

A significant change to financial reporting in 2018-19 for all public sector entities is the requirement to revise the treatment and reporting of financial instruments due to the introduction of AASB 9 *Financial Instruments*. For many the financial effect may be minimal, however for others, the complete change in terminology and disclosure requirements to explain an entity's judgements, assumptions and transition choices may be more challenging.

The other significant change to financial reporting in 2018-19 is the introduction AASB 15 *Revenue from Contracts with Customers* for for-profit entities. The application of this standard for not-for-profit entities is deferred until the 31 December 2019 and 30 June 2020 reporting periods. The core principal of the new standard is that revenue is recognised on a basis that reflects the transfer of promised goods or services to customers at an amount that reflects the consideration the entity expects to receive in exchange for those goods or services. This will require a shift in thinking to previous revenue recognition approaches.

Other significant future developments in reporting applying from the 31 December 2019 and 30 June 2020 reporting periods, include the introduction of new standards for Leases (AASB 16); Income of Not-for-Profit Entities (AASB 1058); and Service Concession Arrangements: Grantors (AASB 1059). The Australian Accounting Standards Board (AASB) is also revising the conceptual framework which is expected to result in Special Purpose Financial Statements no longer being prepared.

FINANCIAL AUDIT DEVELOPMENTS

In 2018-19 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 2018-19, all Council auditor reports will include key audit matters following the implementation to Government Business Enterprises, State Owned Companies and Government Department's over the last two years.

UNIVERSITY OF TASMANIA

INTRODUCTION

The University of Tasmania (University) was established in 1890 and is the fourth oldest university in Australia. It has campuses within the three main regions of Tasmania: Hobart in the south, Launceston in the north and Burnie in the north-west, and two campuses in Sydney: Rozelle and Darlinghurst.

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
- University College.

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

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

- AMC Search Limited (AMC Search)
- Sense-Co Tasmania Pty Ltd (Sense-Co)
- Tasmania University Union Inc. (TUU)
- University of Tasmania Foundation Inc. (Foundation)
- UTAS Holdings Pty Ltd. (UTAS Holdings).

AUDIT APPROACH

The following sections summarise factors that influenced our audit approach.

Understanding the University

Financial performance

The underlying result for the University for 2018 was a deficit of $10.57m, a deterioration from the underlying deficit of $6.58m in the previous year. The current year result was impacted by a 22.3% increase in international student revenue offset by a 2.5% decrease in domestic student revenue.

Employee related expenses increased by 2.2% reflecting the impact of the Enterprise Bargaining Agreement increase of 1.5% plus annual step increases, offset by lower than expected employee costs arising from the annualised impact of vacancies, largely in the College of Health and Medicine and College of Sciences and Engineering.

Property acquisitions and developments

Throughout 2018 the University continued to progress campus and property developments and acquire new properties. Details of significant developments and acquisitions are provided below.

University Northern Transformation project

Progress was made during 2018 on detailed planning for the new campuses at Inveresk in Launceston and West Park in Burnie. Work was done on the business case to clearly articulate the alignment of the strategy with the broader University organisational strategy. The year began with the announcement that $130.00m in Commonwealth funding for the Northern Transformation project, representing half its budget, was now flowing.

Capitalised costs at 31 December 2018 for the Northern Transformation project totalled $2.78m.

The Hedberg, Hobart

The University commenced the construction of its new performing arts centre, The Hedberg, in late 2016. The Hedberg will house the Tasmanian Conservatorium of Music and the Creative Exchange Institute, which will focus research on performance, design and creativity. The development is a partnership between the University, the Tasmanian Government and the Theatre Royal Management Board.

The Hedberg is expected to be completed in October 2019 with operations commencing from the start of semester 1 in 2020. A total of $49.24m has been spent on the project to 31 December 2018.

University City Apartments, Hobart

Following completion of the University City Apartments in mid-2017, the facility was officially opened on 20 October 2017. Students began occupying the facility before the commencement of semester 1 in 2018. The final construction cost for University City Apartments was $86.84m.

79-83 Melville Street, Hobart

The University purchased the property at 79-83 Melville Street in September 2018 for $15.00m to support future infrastructure plans in the Hobart central business district.

Additional 2.99Ha site at Taroona

The University reached agreement with the Tasmanian Government to purchase a 2.99Ha site, adjoining the Institute of Marine and Antarctic Studies (IMAS) site, at Crayfish Point, Taroona, for $2.20m. The University is planning to construct facilities on the site to facilitate the next stage of commercialisation of technology developed by IMAS.

New student accommodation

Mindful of the challenging Tasmanian residential accommodation market, during 2018 the University implemented measures to meet existing and expected future student demand. These included:

- Planning for the construction of a new 420 bed purpose built student accommodation complex at 40 Melville Street, Hobart. Private investment was secured to underwrite the complex. The construction is expected to be completed prior to semester 1 in 2021.
- Purchase of the Midcity Hotel during 2018 for $23.50m. By the end of December 2018, 141 beds were operational with an additional 21 one bedroom apartments to be constructed by early 2019.
- Purchase of the Fountainside Hotel for $18.76m to enable occupancy by students in semester 1 2019.

Southern campus strategy

During 2018, the University evaluated two models for the future of the southern campus:

- a city-centric model in which the University will operate across a closely connected set of precincts in the heart of Hobart, while retaining some accommodation and recreation facilities at Sandy Bay
- a distributed model which would see the Sandy Bay facilities rebuilt and developed in a redesigned landscape consolidated below Churchill Avenue.

A decision to proceed with the city-centric model was made by the University Council in April 2019.

University of Tasmania Foundation Inc.

Following an independent review of the structure and governance of the Foundation, on 30 April 2018 the assets of the Foundation were transferred into the University to facilitate the development of a modern and compliant approach to fundraising and philanthropy for the University. The Foundation legal entity is expected to be wound up during 2019.

Hobart floods in May 2018

Hobart experienced substantial flooding in May 2018 which caused extensive damage to the University Hobart Campus, and in particular, the Law and Engineering buildings. Many temporary arrangements, including revitalisation of the Commerce Building, were implemented to ensure operational functionality of the University continued. As at 31 December 2018, no refurbishment of the affected buildings had been undertaken and, accordingly, the temporary arrangements were still in place. A decision on the refurbishment of the damaged buildings will be made after the Southern campus strategy is finalised.

As a result of the flood damage, the University received insurance recoveries of $14.70m. An impairment expense of $4.93m was recognised for the high performance computer which was significantly damaged during the flood.

Reliance on management and internal controls

In conducting our audits we placed reliance on the control environment and internal controls where those controls are relevant to the audit and are operating effectively. Specific areas of control reliance for the 2018 audit are outlined below.

Reliance on internal audit

The University had a co-sourced internal audit arrangement with a primary internal audit provider and a panel of other internal audit service providers for more technical areas. The 2018 Follow-up of the MyHR Payroll internal audit was relied upon for our audit.

Reliance on internal controls

Financial statement areas where reliance was placed on the operating effectiveness of controls were revenue and receipts and payroll and personnel expenses.

AREAS OF AUDIT FOCUS

Areas requiring greater audit focus, which we categorised as key audit matters or significant risks, are summarised below.

Key audit matters

Key audit matters are those matters that, in our judgement, were of most significance in the audit of the financial statements.

Land and buildings

Valuation of land and buildings

The University's property, plant and equipment at 31 December 2018 included land and buildings totalling $512.72m recognised at fair value. The fair value of vacant land and general office buildings was valued with reference to observable prices in an active market.

For some land granted to the University, the Tasmanian Government reserves the right to resume the land (and improvements) in the event the current use of the land ceases. For the purpose of valuing land, it was assumed the Tasmanian Government would not exercise that right and that the land would remain in the ownership of the University.

The valuation of specific purpose buildings was based on current replacement cost, which required significant judgement in determining the cost to acquire or construct a substitute building with similar utility and adjustments for obsolescence which encompass the buildings' functional, economic and physical obsolescence.

The high dollar values involved together with the inherent volatility and subjectivity associated with the valuation of land and buildings and depreciation of buildings contributed to this being a key audit matter.

A revaluation of land and buildings was not undertaken for the year ended 31 December 2018. Fair values were based on independent valuations obtained for the Newnham and Burnie campuses during 2017, and the desktop valuation undertaken by management for all remaining land and buildings as at 31 December 2017.

Our assessment of the scope, expertise and independence of experts engaged to assist in the valuations, and evaluation of the appropriateness of the valuation methodology applied to determine fair values was undertaken during the 2017 audit. Our testing of the mathematical accuracy of the valuation calculations did not identify any errors.

Land and building acquisitions and disposals

The University acquired and disposed of a number of properties during 2018. As contracts may be subject to conditions precedent, there is a risk the property transactions may not be recorded in the correct financial period. Accounting standards also specify the accounting treatment for assets classified as held for sale. No exceptions were identified from our testing of land and buildings additions and disposals.

Depreciation of land and buildings

The calculation of building depreciation required estimation of asset useful lives, which involved a high degree of subjectivity. Changes in assumptions can significantly impact depreciation charged.

Management reassessed the useful lives of buildings during the year and adjusted useful lives in line with the following approach:

- Northern Transformation Buildings - depreciated over their remaining four year useful life
- buildings with a condition report will adopt remaining useful life calculated based on the condition report
- buildings without a condition report will adopt the remaining useful life as per the most recent valuation
- buildings with no condition report or valuation (generally recently acquired buildings) will adopt a useful life of 40 years until such time as a condition report is prepared or valuation is undertaken.

We evaluated the appropriateness of this approach and determined it was appropriate. We tested a sample of entries in the depreciation calculation to ensure the correct useful lives were applied and that depreciation was calculated correctly. We also performed substantive analytical procedures on building depreciation expense. No exceptions were identified.

Capital expenditure

Capital expenditure during 2018 totalled $110.64m. Capital projects can contain a combination of new construction, enhancement and maintenance activity which are not distinct and therefore the allocation of costs between capital and operating expenditure can be inherently judgmental.

The significant investment in the capital expenditure program and the diversity of projects gives rise of a number of financial statement risks including:

- potential misclassification of expenditure between projects
- potential misclassification between capital and operating expenses
- incorrect capitalisation of interest on qualifying assets
- timing of completion and conversion into depreciable assets
- lack of componentisation of assets in the asset register
- possible impairment of capital work in progress.

We reconciled the movement in work in progress for the year and tested a sample of additions and assets transferred from capital work in progress. We also assessed the appropriateness of items remaining in capital work in progress at 31 December 2018. No exceptions were identified.

Investments

The University held investments totalling $404.25m at 31 December 2018 which were recognised at fair value. A significant amount of the investment portfolio was managed by an investment manager. Of the portfolio, a large proportion was invested in unlisted managed funds, with the majority of these investing in listed equities or listed equity derivatives.

The majority of the investments in unlisted managed funds were valued using market quoted prices, resulting in the valuation of these investments being relatively non-judgmental. However, significant judgement was required for investments where no market data was available. Investments valuations were also subject to volatility in financial markets which could have a material impact on the financial statements.

We evaluated the University's monitoring controls over the performance of investment manager. We obtained an independent assurance report from the auditors of the investment manager confirming the controls applied by the investment manager were suitably designed throughout the year from 1 July 2017 to 30 June 2018 and provided reasonable assurance that the control objectives were achieved and operated effectively throughout that period. We also obtained confirmation from the investment manager that the controls, as audited, were still operating effectively during the period from 1 July 2018 to 31 December 2018.

We obtained direct confirmations from all managed investment funds at 31 December 2018 and no exceptions were noted. In addition, auditor control reports were received for most funds for the year ending 30 June 2018 and we obtained confirmations from the investment managers that the controls were operating effectively from 1 July 2018 to 31 December 2018. We also obtained audited financial statements for a sample of managed funds, noting these opinions were unmodified.

We evaluated the fair value of the University's investment in Education Australia Trust (an unlisted public company), noting the investment balance increased from $16.17m at the beginning of the year to $22.92m at 31 December 2018. We concluded the valuation of the investment was reasonable.

Significant risks

Significant risks represent the risks of a material misstatement in the financial statements that, in our judgement, require special audit consideration.

Student related revenue

The University received revenue of $440.40m from Australian Government financial assistance, excluding research related revenue, Higher Education Loan Programs (HELP) and student fees and charges, representing 61.8% of total revenue. The Australian Government financial assistance and HELP are paid from estimates and then adjusted. The student fees and charges, which are predominantly international student fees, are paid on enrolment. The Australian Government adjusts subsequent payments based on final enrolments. Student revenue is an area of audit risk due to the wide range of courses and the complexity of fee calculations.

We obtained a confirmation of revenue received from the Australian Government Department of Education and Training. We agreed revenue earned to the University's student management system for the Commonwealth Grant Scheme, $199.64m, and Higher Education Contribution Scheme (HECS)-HELP, $75.35m, which resulted in the total overpayment to the University of $7.62m. All amounts were appropriately recognised in the financial statements. We also performed testing and analytical procedures over international student fees received, $114.42m, with no exceptions identified.

At the end of the 2016 financial year the University recognised a provision for the potential repayment of discounts claimed on HECS fees where the fee was being waived. At 31 December 2018, this was no longer considered to be a liability and was reversed.

Research grant income

The University received research revenue of $94.60m from the Australian Government and the Australian Research Council, representing 13.3% of total revenue.

Factors contributing to misstatement risks for research revenue included:

- the large number of research projects undertaken
- revenue dependency on specified targets being delivered before payment was made
- grant milestones or trigger points required to be met before income could be recorded.

We tested the operating effectiveness of the controls relating to the recognition of research related grant income, ensuring the details were correctly entered into the research management database and trigger points were reached prior to raising invoices. We also tested a sample of research grant income transactions. No exceptions were identified from our testing.

Employee expenditure, benefits and provisions

At 31 December 2018, the University had 2 543 full-time equivalent employees. For 2018, employee related expenses of $379.86m represented 58.2% of the University's total expenditure. Misstatement risks relating to employee related expenses and benefit provisions included:

- the existence of a large decentralised employee base with various employee agreements and contracts in place
- the manual input of timesheets by payroll staff for a small number of field staff
- payments made to employees for services that have not been provided
- the possibility of payments made to employees at incorrect rates
- high incidence of adjustments to the payroll system
- incorrect calculation of employee expense accruals at year end
- the use of estimates and assumptions in employee benefit provision calculations.

Our audit approach included testing the operating effectiveness of controls relating to:

- fortnightly payroll transactions, which covered the use of checklists, payroll authorisations and segregation of personnel duties
- new starters, which examined the use of new starter checklists, controls over the entry of new starter information in the MyHR payroll system
- terminations which examined the use of separation checklists, controls over terminated employees being made inactive in the MyHR payroll system and controls over final payment calculations and approvals.

No exceptions were identified from our testing.

Employee benefit provisions at 31 December 2018 totalled $87.43m representing 23.3% of the University's total liabilities. We evaluated the assumptions used in the calculation of the provision for long service leave and tested a sample of employee entitlements. We concluded the provision was calculated appropriately and in accordance with the requirements of AASB 119 *Employee Benefits.*

We reconciled the movement in the provision for restructuring costs from 31 December 2017 to 31 December 2018, confirming all prior year liabilities has been extinguished and the liability of $3.64m the end of the year represented employees who had been appropriately identified and informed before 31 December 2018 in accordance with AASB 137 *Provisions, Contingent Liabilities and Contingent Assets.*

Analytical procedures were also performed over employee expenses and other employee benefit liabilities with variances within our expectation threshold.

Borrowings

At 31 December 2018, the University had a loan with Tasmanian Public Finance Corporation that was subject to various covenants, which if breached, would have resulted in reclassification of the loan as a current liability, or repayment of the loan under unfavourable circumstances.

We obtained a direct confirmation of the loan balance from Tasmanian Public Finance Corporation as at 31 December 2018 which verified the carrying amount of $93.60m and fair value of $103.14m. Our testing revealed compliance with loan covenants was being monitored by management with results reported to the University Audit and Risk Committee.

Management override of controls

To address the risk of management override of controls we:

- performed computer assisted audit procedures over all journals processed during the year ended 31 December 2018
- evaluated management's accounting estimates as outlined the commentary above
- examined transactions outside the normal course of business, which included:
  - land and building acquisitions and disposals
  - the recognition of $58.20m other revenue in the Parent Entity financial statements relating to the assets from the Foundation to the University. As the Foundation is a controlled entity of the University, the transaction was eliminated in the consolidated financial results
  - the receipt of insurance recoveries, $14.70m, relating to flood damage to the University's Sandy Bay campus, which were correctly recognised as other income.

AUDIT CONCLUSIONS

Audit opinion	Unmodified audit opinion issued		
Audit findings	High Risk	Moderate Risk	Low Risk
Internal control findings reported	0	2	1
Accounting issues reported	0	1	0
Unresolved prior year findings	0	2	2

Audit opinion

The signed financial report was received on 14 February 2019 and an unmodified audit opinion was issued on 22 February 2019.

Audit findings

In performing our audit we did not identify any high risk audit findings. We identified three moderate risk findings relating to:

- purchase orders being generated after supplier invoices were received
- the collection of an outstanding receivable not followed up in a timely manner
- the depreciation of the student accommodation service concession assets being based on a 5 or 40 year useful life, rather than on the actual remaining useful life of the individual student accommodation facilities.

Two previously reported findings remain unresolved relating to:

- the high number of credit card users, variety in monthly limits and large volume of credit card purchase transactions
- the existence of employees with excessive entitlements to annual leave and long service leave.

FINANCIAL SNAPSHOT

The results reported in this Chapter related to the University's consolidated financial performance and position. The University reports on a calendar year basis and therefore the financial results related to the year ended 31 December 2018.

Figure 1: University of Tasmania Financial Snapshot 2018

	2018 $'000s	Ind	2017 $'000s	Ind	2016 $'000s	Ind	2015 $'000s	Ind
Financial Performance								
Total Australian Government financial assistance	451 086	▲	425 489	●	420 249	●	406 726	●
Employee related expenses	379 860	●	371 593	●	360 747	▼	336 727	●
Reconciliation from underlying result to net result								
Underlying result	(10 565)	▼	(6 575)	▲	(17 573)	▼	(11 981)	▲
Net investment revenue	11 736	▼	33 511	▲	18 342	▼	24 668	▲
Capital income	12 758	▼	13 959	▲	10 831	▲	5 776	▼
Capital grants received	10 279	▼	13 116	▲	6 672	▼	10 550	▲
Net settlement of insurance claim	4 617	▲	0	●	0	●	0	●
Net movement in unspent research grants	23 398	▲	4 918	▲	4 013	▼	6 532	▲
Commonwealth grant scheme and HECS adjustments	6 906	▲	0	▼	2 776	▲	(7 109)	▼
Impairment expense and loss on disposal	0	●	0	▲	(10 127)	●	(10 268)	▼
Gain(Loss) on disposal of assets	0	●	0	●	0	▲	(9 250)	▼
Net result for the year[1]	59 129	●	58 929	▲	14 934	▲	8 918	▲
Financial position[2]								
Investments	404 254	●	419 633	▲	288 375	●	279 864	●
Property, plant and equipment	667 732	▲	603 651	▼	783 869	▲	745 636	▲
Service concession asset	140 824	●	143 512	▲	0	●	0	●
Borrowings	(93 600)	●	(93 600)	▲	(103 100)	▲	(118 600)	▼
Grant of right to operate liability	(127 117)	▲	(132 608)	▼	0		0	●
Employee provisions	(87 433)	●	(89 913)	●	(87 833)	▼	(79 308)	●
Net assets	971 362	▲	912 318	●	911 565	●	899 829	●
Key financial ratios								
Operating margin	1.04	▲	0.99	●	0.96	●	0.98	●
Own source revenue	43.8%	●	43.7%	▲	39.7%	●	39.8%	●
Liquidity ratio	1.82	▲	1.70	▲	0.76	▼	1.13	▼
Self-financing ratio	7.8%	▲	5.5%	▼	7.1%	▲	4.5%	▼
Debt to equity	9.6%	▲	10.3%	▲	11.3%	▲	13.2%	▼
Building sustainability	78.3%	▲	33.8%	▼	62.9%	▼	106.0%	▲

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

1. The impairment expense relating to the disposal of flood affected assets is included in the net settlement of insurance claim balance
2. Assets are positive, liabilities are negative

UNIVERSITY CONTROLLED ENTITIES

Entities included in this section are:

- AMC Search, 100% ownership
- Foundation, 100% ownership
- Sense-Co, 80% ownership
- TUU, controlled by the University
- UTAS Holdings, 100% ownership.

Audit approach

The following sections summarise factors that influenced our audit approach.

Understanding the entities

AMC Search

AMC Search is a company limited by guarantee which provides maritime training and consulting services.

Foundation

The Foundation is an incorporated association which acts as trustee for the University of Tasmania Foundation Trust. It raised money to endow scholarships, support research and build resources, while developing links between the University, industry and the community. On 30 April 2018, the Foundation transferred its assets, $58.20m, to the University. The Foundation legal entity is expected to be wound up during 2019.

Sense-Co

Sense-Co is a company limited by shares. The company was registered on 19 August 2014 and established to focus on the commercialisation opportunities of sensing technology. New shares were issued to a third party during the year resulting in the University's equity interest reducing from 100% to 80%. The company did not trade during the year ended 31 December 2018.

TUU

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 satisfied the definition of control and has consolidated the TUU into the University's financial statements since 2014.

UTAS Holdings

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.

Reliance on management and internal controls

The controlled entities did not have an internal audit function. We did not rely on controls specific to financial statement areas for any of the controlled entities.

Areas of audit focus

AMC Search

Revenue

Maritime training courses and programs were the primary source of income for AMC Search with revenue of $5.39m generated during 2018, representing 68.1% of total revenue. Course managers were responsible for maintaining records for the management of each course (e.g. attendance, course costs and receipt of trainee income on course completion) with these records independently reconciled by finance personnel to verify the accuracy of revenue for each course.

We tested a sample of fee invoices for training courses and programs to supporting documentation. We also examined supporting documentation for a sample of fees received in advance to ensure revenue had been recognised in the correct period. No exceptions were identified.

Related party transactions

The University processed payments for AMC Search expenditure and payroll, which were recognised through a loan between AMC Search and the University. The University also charged AMC Search a management fee for the use of University resources and facilities.

We examined the reconciliation of loan account transactions between AMC Search and the University, which included the management fee.

Management override of controls

To address the risk of management override of controls we:

- examined a sample of journals processed during the year ended 31 December 2018
- evaluated management's accounting estimates and assumptions relating to the collectability of receivables, useful lives of assets and employee benefit provisions
- examined transactions outside the normal course of business, which included the management fee charged.

Foundation

Investments

On 30 April 2018, the Foundation transferred assets totalling $58.20m to the University. Our testing including assessing and recalculating the apportionment methodology for investments between the Foundation and the University. We also examined documentation of the decision by the Foundation Directors to transfer the assets to the University.

Management override of controls

To address the risk of management override of controls we:

- examined a sample of journals processed during the year ended 31 December 2018
- evaluated management's accounting estimates and assumptions relating to the valuation of investments
- examined documentation supporting the transfer the assets to the Foundation to the University.

We did not identify any further significant transactions outside the normal course of business.

TUU

Cash and Investments

TUU held cash and investments of $9.09m at 31 December 2018, with a large portion managed by an investment manager. The investment portfolio comprised cash, domestic and international equities, domestic and international fixed interest, and domestic and international property investments. The valuation of investments can be subject to volatility in financial markets.

We confirmed cash and term deposit balances with the issuing financial institutions and obtained confirmation of the existence and valuation of investments managed by the investment manager

Management override of controls

To address the risk of management override of controls we:

- examined a sample of journals processed during the year ended 31 December 2018
- evaluated management's accounting estimates and assumptions relating to the useful lives of assets and employee benefit provisions

We did not identify any significant transactions outside the normal course of business.

UTAS Holdings

Investments

During 2018, UTAS Holdings received 2 820 896 shares in an Australian listed entity in exchange for an exclusive licence to patent technology held by UTAS Holdings. The fair value of the shares received was recognised as revenue on receipt of the shares. We assessed the fair value of the shares at 31 December 2018 in reference to market quoted prices.

There were no other transactions for UTAS Holdings during 2018.

Audit conclusions

Audit opinions	**4 Unmodified audit opinions issued**		
Audit findings	**High Risk**	**Moderate Risk**	**Low Risk**
Internal control findings reported	0	0	0
Accounting issues reported	0	0	0
Unresolved prior year findings	0	0	1

AMC Search

The signed financial report was received on 12 February 2019 and an unmodified audit opinion was issued on 18 February 2019. There was one low risk finding reported in a previous financial year that had yet to be resolved.

Foundation

The signed financial report was received on 14 February 2019 and an unmodified audit opinion was issued on 20 February 2019.

Sense-Co.

This audit was dispensed with in 2018.

TUU

The signed financial report was signed on 5 February 2019 and received on 12 February 2019 and an unmodified audit opinion was issued on 14 February 2019.

UTAS Holdings

The signed financial report was received on 14 February 2019 and an unmodified audit opinion was issued on 15 March 2019.

Financial snapshot

Figure 2 summarises the financial results and position of University controlled entities for 2018.

Figure 2: Financial Results

	Underlying surplus (deficit) $'000s	Net surplus (deficit) $'000s	Comprehensive surplus (deficit) $'000s	Net Assets 2018 $'000s	Net Assets 2017 $'000s
AMC Search	(1 494)	(1 494)	(1 494)	3 249	4 743
TUU	(58)	(58)	(58)	9 275	9 333
University Foundation	0	0	0	0	58 754
UTAS Holdings	367	367	367	367	0

OTHER STATE ENTITIES 31 DECEMBER 2018

This Chapter provides information on the following State entities who reported on a 31 December financial year basis:

- Theatre Royal Management Board (Board)
- Solicitors' Trust
- Anzac Day Trust.

AUDIT APPROACH

Our audit approach was influenced by the following factors.

Understanding the entities

Theatre Royal Management Board

The Theatre Royal is governed by the Board which was established under the *Theatre Royal Management Act 1986*.

The Theatre Royal presents live theatre, contemporary music, dance and entertainment. It is available for hire for special events, meetings, conferences and special gatherings.

Solicitors' Trust

The Solicitors' Trust is a body corporate established under the *Legal Professional Act 1959* and continues under the *Legal Professional Act 2007* (LPA 2007).

The Solicitors' Trust consists of three Trustees appointed by the Governor, comprising two legal practitioners nominated by the Law Society and one person nominated by the Minister who is a member of a recognised accounting body. The function of the Solicitors' Trust is to administer and manage the Solicitors' Guarantee Fund (Fund).

The Fund is utilised for operations prescribed under the LPA 2007 including funding the operation of the Legal Profession Board, the Disciplinary Tribunal, compensation of claimants who suffer pecuniary loss as a consequence of defaults by lawyers relating to trust money or trust property, administration and for any other purpose approved by the Minister.

Anzac Day Trust

The Anzac Day Trust Fund was created by the *Anzac Day Observance Act 1929* and is administered by Trustees appointed in accordance with this Act. The Anzac Day Trust provides grants to service organisations to assist with supporting the welfare of ex-service personnel and their dependents.

Reliance on management and internal controls

The three entities did not have an internal audit function. We did not rely on controls specific to financial statement areas for any of the three entities.

AREAS OF AUDIT FOCUS

Theatre Royal Management Board

Theatre Royal Redevelopment – Going Concern Assertion

The Theatre Royal building is being upgraded as part of the The Hedberg project, a major redevelopment undertaken by the University of Tasmania. The Hedberg is expected to be completed in October 2019 with operations commencing from the start of semester 1 in 2020.

The project required the Board to cease operations at the Theatre Royal for approximately eight months from October 2018. As part of completing the financial statements for 31 December 2018, the Board were required to assess the financial impact of ceasing operations and review its ability to continue as a going concern.

In assessing going concern, we reviewed the 2019 budget that projected a deficit of $0.13m at the end of April 2019. We determined there were sufficient liquid assets of $1.55m to cover this deficit and support a further 12 months operational costs.

We confirmed the Board received grant and other revenue from the Department of State Growth to reimburse it for revenue forgone due to its closure during the construction period and towards meeting costs to operate the new facilities once reopened.

On this basis, we agreed with the preparation of the financial report on a going concern basis and the appropriateness of the associated note disclosures in regard to going concern.

Development project income and expenses

The Board recorded development project income and expenses which related to the Board's investment in the project design and management. The expenses related to a conservative estimate of salaries and other costs, some of which may be reimbursed and noted as income.

We performed detailed testing and analytical procedures over income, $2.29m, and expenses, $2.28m, which included business development income and development project expenses with no exceptions identified.

Management override of controls

To address the risk of management override of controls we

- examined a sample of journals processed during the year ended 31 December 2018
- evaluated management's accounting estimates and assumptions relating to employee provisions, creditors, debtors and advanced ticket sales.

Other than the additional funding provided to the Board by the Department of State Growth, we did not identify any significant transactions outside the normal course of business.

Solicitors' Trust

Cash and investment balances

The Solicitors' Trust had a significant number of bank accounts which were held for investment.

We confirmed cash and term deposit balances with the issuing financial institutions to obtain confirmation of their existence and valuation. No exceptions were identified.

Management override of controls

To address the risk of management override of controls we examined a sample of journals processed during the year ended 31 December 2018. We did not identify any significant transactions outside the normal course of business.

Anzac Day Trust

Receipt and Disbursement of Grant Funding

The Anzac Day Trust has two significant transactions being the receipt of grant funding from the Department of Communities Tasmania and the disbursement of that funding to Hobart Legacy Inc.

We performed detailed testing of these transactions with no exceptions identified.

AUDIT CONCLUSIONS

Audit opinions	3 Unmodified audit opinions issued		
Audit findings	High Risk	Moderate Risk	Low Risk
Internal control findings reported	0	2	1
Accounting issues reported	0	0	0
Unresolved prior year findings	0	0	0

Theatre Royal Management Board

The signed financial report was received on 14 February 2019 and an unmodified audit opinion was issued on 7 March 2019.

We reported two moderate risk findings related to:

- the authorisation of payments above an employee's delegated dollar limit
- review of the Chief Executive Officer's corporate card statement by the Chair of the Board.

In addition there was one low risk finding. All prior year matters were resolved.

Solicitors' Trust

The signed financial report was received on 14 February 2019 and an unmodified audit opinion was issued on 1 April 2019.

There were no findings for the 2018 financial year.

Anzac Day Trust

The signed Statement of Receipts and Payments was received on 30 January 2019, and an unmodified audit opinion was issued on 20 February 2019. There were no findings for the 2018 financial year.

FINANCIAL SNAPSHOT 2018

Figure 3: Other Entities Financial Snapshot 2018

Entity	Underlying surplus (deficit) 2018 $'000s	Net surplus (deficit) 2018 $'000s	Net Assets 2018 $'000s	Net Assets 2017 $'000s
Theatre Royal Management Board	587	455	1 990	1 535
Solicitors' Trust	1 748	1 748	12 596	10 849
Anzac Day Trust	(1)	(1)	2	3

NORTH EAST CARE INCORPORATED

INTRODUCTION

In 2015, Presbyterian Care Tasmania Incorporated announced that they would be withdrawing as the operator of the Aminya Nursing Home in Scottsdale. North East Care Incorporated (NE Care), an incorporated charitable organisation, was established by Dorset Council in September 2015 to facilitate the ongoing operations of the nursing home for the North East Tasmania region and to support the new provider, May Shaw Health Centre Inc (May Shaw), in their management of the facility.

AUDIT APPROACH

The following sections summarise factors that influenced our audit approach.

Understanding North East Care

Determination of State Entity

In January 2018, as part of the planning of the audit of Dorset Council's financial statements, we assessed NE Care as being a State entity within the scope of the *Audit Act 2008* (Audit Act) as a result of Dorset Council having control over the NE Care. This facilitated the requirement for audits of the financial statements for the years ending 30 June 2016, 2017 and 2018.

Loan Payable

NE Care's primary financial activity was to pay May Shaw management fees for operating the facility. These management fees were paid by Dorset Council on behalf of NE Care which resulted in recognition of a loan payable between Dorset Council and NE Care. During 2018, Dorset Council determined the loan payable would be transferred to May Shaw.

As at 30 June 2018, the loan between NE Care and Dorset Council had been transferred to May Shaw and as such the money owing from NE Care to Dorset Council was no longer payable. The transfer of the loan ensured the continuation of services and left NE Care in a positive net asset position.

Reliance on management and internal controls

NE Care did not have an internal audit function. We did not rely on controls specific to financial statement areas for any of the three audits.

AREAS OF AUDIT FOCUS

Revenue

Other revenue in the form of donations, bequests and fundraising totalling $0.03m were the primary source of income for NE Care in 2016.

In 2017 and 2018 reimbursements from the State Government were the primary source of income with $0.60m and $0.49m received, respectively. These balances reduced the loan payable by NE Care to Dorset Council.

Reimbursement revenue and a sample of other revenue were tested during the audits. This involved tracing recorded amounts back to supporting documentation to ensure the amounts were accurate and recognised in the correct period.

Related party transactions

Dorset Council paid the management fees owing to May Shaw in 2016, 2017 and 2018. This resulted in NE Care recognising a loan payable to Dorset Council.

We examined the reconciliation of the loan account and transactions between NE Care and Dorset Council and verified that it correctly included the management fees. The loan was transferred to May Shaw in 2018.

AUDIT CONCLUSIONS

The three signed financial reports were received on 25 January 2019, which was almost six months after the 45 day deadline for the 30 June 2018 financial statements. Unmodified audit opinions were issued on 1 February 2019 for all three financial statements. There were no findings for these financial years.

Audit opinions	3 Unmodified audit opinions issued		
Audit findings	High Risk	Moderate Risk	Low Risk
Internal control findings reported	0	0	0
Accounting issues reported	0	0	0
Unresolved prior year findings	0	0	0

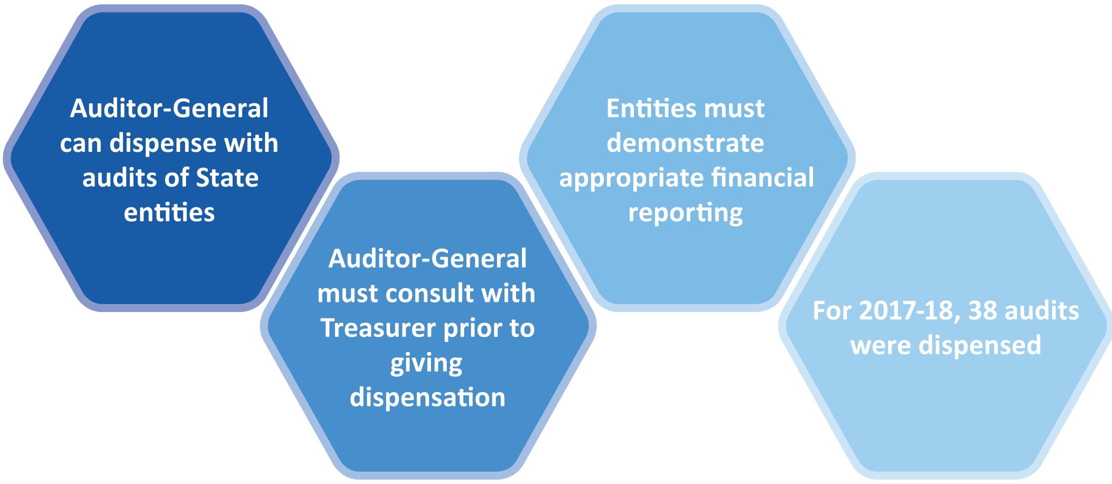
FINANCIAL SNAPSHOT 2016-2018

Figure 4: North East Care Financial Snapshot 2016-2018

	Underlying surplus (deficit) $'000s	Comprehensive income (deficit) $'000s	Loans and Borrowings $'000s	Net Assets $'000s
NE Care 2016	(499)	(499)	546	(499)
NE Care 2017	32	32	590	(467)
NE Care 2018	74	518	-	51

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.

Where the entity is of significant size or by its nature of particular public interest, it is unlikely a dispensation will be granted. 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 2018 (controlling entity shown in brackets)

- C-Cell Pty Ltd (Copping Refuse Disposal Site Joint Authority)
- Heemskirk Wind Farm Pty Ltd (Hydro Electric Corporation)
- palawa Enterprise Pty Ltd (Aboriginal Land Council of Tasmania)

In our earlier report, *Report of the Auditor-General No. 6 of 2018-19, Volume 4, Audit Summary 2017-18*, we dispensed with 35 entities. Combined with the above entities, this now totals 38 entities for 2017-18.

SUBMISSION OF FINANCIAL STATEMENTS

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.

FINANCIAL REPORTING DEVELOPMENTS

SNAPSHOT

REPORTING IN THE PUBLIC SECTOR

International Public Sector Accounting Standards Board

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 maintains a principle of transaction neutrality and, where appropriate, incorporates pronouncements from the International Public Sector Accounting Standards Board (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:

- 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

The AASB's Australian Financial Reporting Framework project continues to progress with its revision of the Conceptual Framework for financial reporting.

The reason for the change was due to the IASB issuing a revised Conceptual Framework in March 2018, which conflicts with the Australian approach of the 'reporting entity' concept. Under the current Australian approach an entity can self-assess itself as not being a reporting entity and elect to prepare special purpose financial statements, which need not comply with all Australian accounting standards. Consequently, entities are choosing which standards they apply and which they do not. There has been widespread acknowledgement in both the public and private sectors, particularly from users, that the current financial reporting framework does not provide consistent, comparable and transparent financial statements. Further details on the background behind the need to change can be found in my previous report; *Report of the Auditor General No.9 of 2017-18.*

In May 2018, the AASB issued a Consultation Paper to seek feedback from stakeholders and regulators. In the short-term, the Consultation Paper proposes interim arrangements allowing for two conceptual frameworks. The longer term proposal provides for two tiers of general purpose financial reporting requirements (Tier 1 and Tier 2).

As part of defining Tier 1, the AASB in January 2019 issued an Invitation to Comment on a fatal-flaw review version for a proposed new standard, 2019-X *Amendments to Australian Accounting Standards – References to the Conceptual Framework*.

At this stage application of the initial revision of the Conceptual Framework will be limited to:

(a) for-profit private sector entities that have public accountability and are required by legislation to comply with Australian Accounting Standards;

(b) other for-profit entities that voluntarily elect to apply the Conceptual Framework, which would permit compliance with Australian Accounting Standards and International Financial Reporting Standards.

The changes will enable publicly accountable for-profit private sector entities to state compliance with IFRS. As the amendment will remove the ability for for-profit private sector entities to self-assess, these entities will be required to prepare general purpose financial statements (GPFS). The fatal-flaw review version of the proposed Standard was open for comment until March 2019. The proposed Standard would apply to annual reporting periods beginning on or after 1 January 2020, with early adoption available. Comparatives will likely be required as the proposal requires retrospective application. The final amending Standard is expected to be issued by the end of June 2019.

The next phase of the project will be to develop a framework for Tier 2 by 2020. This will involve replacing the existing Tier 2 GPFS Reduced Disclosure Requirements framework with a framework that would still require compliance with all recognition and measurement requirements in AAS, including consolidation and equity accounting.

The next step for the AASB involves further consultation with regulators and stakeholders in 2019. While the main focus to date has been primarily in the for-profit sector, consultations in 2019 will include both the for-profit and NFP sectors, as the AASB continues to work through and determine future reporting requirements.

State entities that currently prepare special purpose financial statements under the existing Conceptual Framework need to be cognisant that going forward, they will likely be preparing some form of GPFS with a higher level of compliance with the recognition, measurement and disclosure requirements in AAS.

REPORTING IN 2018-19

A significant change to financial reporting in 2018-19 for all public sector entities is the requirement to revise the treatment and reporting of financial instruments due to the introduction of AASB 9 *Financial Instruments*. For many the financial effect may be minimal, however for others, the complete change in terminology and disclosure requirements to explain judgements, assumptions and transition choices may be more challenging.

The other significant change to financial reporting in 2018-19 is the introduction AASB 15 *Revenue from Contracts with Customers* for for-profit entities. The application of this standard for NFP entities is deferred until the 2019-20 reporting period. The core principal of the new standard is that revenue is recognised on a basis that reflects the transfer of promised goods or services to customers at an amount that reflects the consideration the entity expects to receive in exchange for those goods or services. This will require a shift in thinking to previous revenue recognition approaches.

While these and other pending and revised accounting standards offer various transition options, practical expediencies and the opportunity to early adopt, for the vast majority of State entities the application of these will 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. These statements usually maintain consistency in reporting, with the adoption of any changes following the respective application date.

Both AASB 9 and AASB 15 require retrospective application by either fully restating comparatives; including an adjustment to opening equity as if they had always been in effect (a 'Fully Retrospective' approach); or by only applying them in the current year of adoption in accordance with the transitional requirements, with a cumulative catch-up adjustment to opening equity on 1 July 2018 (a 'Cumulative Effect' approach). Both approaches require disclosure of sufficient information for users to understand the transitional process, options applied and to reconcile balances between policies previously applied and the new determinations in accordance with the new standards.

Where an entity applies the cumulative effect approach, the presentation of comparative information will be based on previous policies and judgments established under superseded standards, and current information will be presented in accordance with new policies and judgments in accordance with the new standards. Irrespective of the period presented, accounting standards require sufficient information presented in relation to policies and judgements, to ensure an understanding of the financial statements. As a consequence this will require the presentation of two sets of accounting policies for AASB 9 and AASB 15, the current year and the comparative. This will see a distinct increase in the volume of policy information in the year of adoption under a cumulative approach.

In future years, entities will need to adapt to the more explicit disclosure requirements under these and other pending standards. Many require significantly more detail than has previously been required, with the level of detail for entities revenue policies being a good example. Under previous revenue standards, we have observed many only provide brief or basic boiler plate disclosures in respect of revenue recognition. Under AASB 15, entities will need to provide more tailored and detailed disclosures.

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 for the inclusion of a guide to the future. The required disclosures includes known, or reasonably estimable, information relevant to assessing the possible impacts that initial application of a new standard will have on the entity's financial statements. As the effective date for a new standard becomes nearer, entities should be able to provide stakeholders with relevant and more accurate information on likely impacts.

These changes should not be taken lightly, entities need to reflect on their current systems, internal controls, policies and procedures to ensure they are able to collect and disclose the required information.

Reporting developments of significance for 2018-19 are discussed below.

Financial Instruments

AASB 9 is now applicable for all entities and supersedes AASB 139 *Financial Instruments: Recognition and Measurement*. Application is retrospective so will require restatement of prior period balances, to the extent possible, in accordance with the transitional options available (as discussed further below).

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 reclassify their equity investment in the Tasmanian Water and Sewerage Company Pty Ltd. Previously under AASB 139 all Councils treated these investments as an available-for-sale investment. This is a bit of a misnomer, as these long-term strategic investments have never been, 'available-for-sale', rather available-for-sale was the residual catch-all category under AASB 139.

AASB 9 introduces 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.

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. At the date of initial application, AASB 9 requires an entity to disclose and explain the changes in the measurement classifications of financial assets and financial liabilities between AASB 139 and AASB 9. One way to achieve this is by the inclusion of a reconciliation detailing the reclassifications between the two standards. Also required is the disclosure of qualitative information explaining how the classification requirements of AASB 9 were applied where classifications have changed and the reasoning behind any designation or de-designation of financial assets or liabilities measured at fair value through the profit or loss. Detailed application guidance is included in the appendices of AASB 9 for assistance.

The standard provides for either a full retrospective approach or pragmatic cumulative effect approach provided the practical expediencies are followed and a reconciliation is provided.

Upon transition to AASB 9 entities need to make sure they have clearly established business models for all instrument types to ensure appropriate classification under the new requirements. Past practice may not necessarily determine the classification going forward. Entities need to ensure they have appropriately prepared for the changes in financial instrument classifications and the increased disclosure requirements upon transition.

Revenue from Contracts with Customers

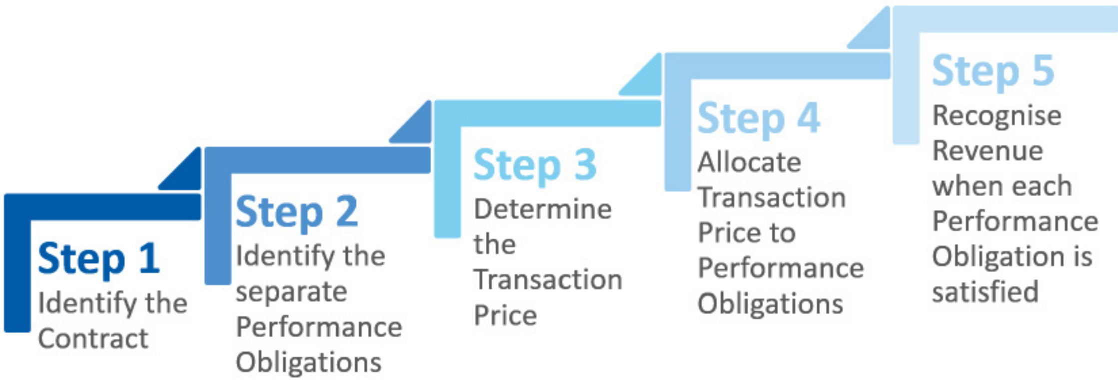
AASB 15 is a new standard aimed at aligning the timing of recognition of contract revenue with the transfer of goods and services. AASB 15 replaces AASB 118 *Revenue*, AASB 11 *Construction Contracts* and five other revenue related interpretations.

There has been a lengthy lead time from its original issue in December 2014, followed by a deferral in December 2016. While this has provided additional time for entities to ready themselves for its implementation, it is now due for adoption by for-profit entities, with NFP entities having an additional year before implementation. The effective dates are therefore:

- For-profit entities – financial years beginning on or after 1 January 2018
- NFP entities – financial years beginning on or after 1 January 2019.

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.

The standard requires the separate disclosure of revenue recognised from contracts with customers into categories that depict the nature, amount, timing and uncertainty about revenue and cash flows effected by economic factors. The application guidance explains that the most appropriate categories depend on facts and circumstances, however, an entity should consider how revenue is disaggregated in other reports or communications, or for the purposes of evaluating financial performance.

Entitles are also required to disclose qualitative information about the methods used in the recognition of revenues along with an explanation why the methods used provide a faithful depiction of the transfer of goods or services. Disclosing information about methods, inputs and assumptions used, and the allocation of the transaction price, will be a change in practice for some entities. Those with multiple or diverse contract types will find this process more onerous.

The introduction of AASB 15 may also see the presentation of new classifications in the statements of comprehensive income and financial position.

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 evaluate processes to capture such information and the need to consider 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 will need to prepare early in anticipation of the many varied effects that these changes to revenue recognition will have on their operations.

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 the impact of these new standards to ensure smooth transition. The following commentary provides a high level overview of a selection of pertinent standards/projects.

Revenue from Contracts with Customers – Not-for-Profit Entities

As noted above, the application of AASB 15 applies to NFP entities for financial years commencing on or after 1 January 2019.

AASB 15 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 was issued in December 2016 and works in combination with AASB 15 for NFP entities only. Application aligns with AASB 15, with the standard effective for financial years commencing on or after 1 January 2019.

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.

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 the asset 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*, the difference between the fair value of a right-of-use asset acquired by the lessee and the lease liability (i.e. the negligible minimum lease payments) is recognised as revenue 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.

At present, most NFP entities do not recognise lease assets from peppercorn leases. A key reason for this is that such assets usually contain restrictions on use. Currently there is diversity in how these restrictions should be considered in arriving at the fair value of public sector assets, which are generally held for delivery of service to the public and not to generate cash flows. The valuation of assets with restrictions, including valuation of right-of-use assets with restrictions, has been raised as a major issue to be addressed in the AASB's Fair Value Measurement for Public Sector Entities project.

In recognition of such issues the AASB issued AASB 2018-8 – *Amendments to Australian Accounting Standards – Right-of-Use Assets of Not-for-Profit Entities* in December 2018. It allows a temporary option for NFP entities to not measure right-of-use assets at initial recognition at fair value in respect of leases that have significantly below-market terms, since further guidance is expected to be developed to assist NFP entities in measuring right-of-use assets at fair value. The Standard requires an entity that elects to apply the option (i.e. measures a class or classes of such right-of-use assets at cost rather than fair value), to include additional disclosures about the terms of each material lease, or in aggregate for those of similar nature.

AASB 1058 also requires local governments, government departments, general government sectors and whole of governments to recognise volunteer services if:

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

Other NFP entities 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 to demonstrate how a NFP entity applies the requirements in practice.

Australian Implementation Guidance for Not-for-Profit Entities

AASB 2016–8 A*mendments to Australian Accounting Standards – 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 the adoption of AASB 15 and AASB 1058 for financial years beginning on or after 1 January 2019.

The AASB 9 amendments provide guidance to NFPs on the recognition and initial measurement of non-contractual receivables arising from statutory requirements. Such receivables include taxes, rates and fines. (Under AASB 15 such items do not create a promise to provide goods or services, or require performance obligations). The amendment provides clarity to AASB 1058 in the acquisition and recognition of such assets at less than fair value.

The AASB 15 amendments provide guidance to NFPs on accounting for contracts with customers and establishes that:

- the 'customer' does not need to be the recipient of goods or services
- the 'contract' could include an arrangement entered into under the direction of another party
- contracts are enforceable if they are enforceable by legal or 'equivalent means'
- contracts do not have to have commercial substance, only economic substance
- performance obligations need to be 'sufficiently specific' to be able to apply AASB 15 to these transactions.

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

Leases

The AASB issued a new leasing standard AASB 16 in February 2016 to supersede the existing standard AASB 117 *Leases*. It applies for annual reporting periods beginning on or after 1 January 2019, 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.

For lessees, under the new standard, the present value of future operating lease payments are capitalised and included on the Statement of Financial Position as a right-of-use lease asset with a corresponding lease liability. The right-of-use asset is then subject to depreciation, while the lease payments, less the financing effect of interest, reduce 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.		
Statement of Financial Position	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 the Statement of Financial Position, although exemptions are available for short term leases less than 12 months and low value leases (individual assets with values less than, say, $10 000). 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 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 financing activity finance cost component, which will be higher in the early years.

The recognition of all lease assets and liabilities on the Statement of Financial Position will increase the net debt of lessees. This 'grossing-up' effect may 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, are variations to lease payment amounts arising from consumer price index increases, which 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 for lessees to make an accounting policy election to recognise the lease and non-lease components as a single lease component on the Statement of Financial Position 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.

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 of AASB 16 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.

Entities that use leases are encouraged to thoroughly assess the current and future impacts the introduction of AASB 16 may have on their entity's operations and reporting.

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. Post issue, the AASB received comments from stakeholders preparing for the implementation of AASB 1059, some of whom requested a deferral of the mandatory effective date. The AASB noted the issues raised and decided to defer the effective date to assist stakeholders with their implementation efforts. AASB 1059 now applies for annual reporting periods beginning on or after 1 January 2020, although early application is still permitted.[1]

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.

1 AASB 2018-5 *Amendments to Australian Accounting Standards – Deferral of AASB 1059*, amends AASB 1059 to defer its effective date from annual reporting periods on or after 1 January 2019 to 1 January 2020.

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 Statement of Financial Position.

Under the standard:

- There will be an earlier recognition of social infrastructure PPPs on the Statement of Financial Position, 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 the Statement of Financial Position. 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 of the standard.

FINANCIAL AUDIT DEVELOPMENTS

CHANGES TO AUDITOR'S REPORT

In 2018-19 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 2017-18, all Government Business Enterprises, State Owned Companies and Department's auditor's reports included a section on key audit matters.

Key audit matters are matters which we determined 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 key audit matters improves the transparency of the audit process.

The key audit matters 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 2018-19, all Council auditor's reports will include key audit matters and in 2019-20 we will consider the inclusion of key audit matters in all the remaining State entities on a case-by-case basis.

ACRONYMS AND ABBREVIATIONS

AAS	Australian Accounting Standards
AASB	Australian Accounting Standards Board
AASB 9	AASB 9 *Financial Instruments*
AASB 15	AASB 15 *Revenue from Contracts with Customers*
AASB 16	AASB 16 *Leases*
AASB 108	AASB 108 *Accounting Policies, Changes in Accounting Estimates and Errors*
AASB 117	AASB 117 *Leases*
AASB 139	AASB 139 *Financial Instruments: Recognition and Measurement*
AASB 1004	AASB 1004 *Contributions*
AASB 1058	AASB 1058 *Income of Not-for-Profit Entities*
AASB 1059	AASB 1059 *Service Concession Arrangements: Grantors*
AMC Search	AMC Search Limited
Audit Act	Audit Act 2008
Board	Theatre Royal Management Board
Foundation	University of Tasmania Foundation Inc.
FVOCI	Fair value through other comprehensive income
FVTPL	Fair value through profit or loss
Fund	Solicitors' Guarantee Fund
GPFS	General purpose financial statements
HECS	Higher Education Contribution Scheme
HELP	Higher Education Loan Program
IASB	International Accounting Standards Board
IFRS	International Financial Reporting Standards
IMAS	Institute of Marine and Antarctic Studies
IPSASB	International Public Sector Accounting Standards Board
LPA 2007	Legal Professional Act 2007
May Shaw	May Shaw Health Centre Inc.
NE Care	North East Care Incorporated
NFP	Not-for-profit
PPP	Public private partnership
SCA	Service concession arrangements
Sense-Co	Sense-Co Tasmania Pty Ltd
TUU	Tasmanian University Union Inc.
University	University of Tasmania
UTAS Holdings	UTAS Holdings Pty Ltd

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.

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