



FINANCIAL AUDIT

10 DECEMBER 2019

Education 2019

NEW SOUTH WALES AUDITOR-GENERAL'S REPORT

THE ROLE OF THE AUDITOR-GENERAL

The roles and responsibilities of the Auditor-General, and hence the Audit Office, are set out in the *Public Finance and Audit Act 1983* and the *Local Government Act 1993*.

We conduct financial or 'attest' audits of State public sector and local government entities' financial statements. We also audit the Total State Sector Accounts, a consolidation of all agencies' accounts.

Financial audits are designed to add credibility to financial statements, enhancing their value to end-users. Also, the existence of such audits provides a constant stimulus to entities to ensure sound financial management.

Following a financial audit the Audit Office issues a variety of reports to entities and reports periodically to parliament. In combination these reports give opinions on the truth and fairness of financial statements, and comment on entity compliance with certain laws, regulations and government directives. They may comment on financial prudence, probity and waste, and recommend operational improvements.

We also conduct performance audits. These examine whether an entity is carrying out its activities effectively and doing so economically and efficiently and in compliance with relevant laws. Audits may cover all or parts of an entity's operations, or consider particular issues across a number of entities.

As well as financial and performance audits, the Auditor-General carries out special reviews and compliance engagements.

Performance audits are reported separately, with all other audits included in one of the regular volumes of the Auditor-General's Reports to Parliament – Financial Audits.

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In accordance with section 52B of the *Public Finance and Audit Act 1983*, I present a report titled '**Education 2019**'.

A handwritten signature in black ink, appearing to read 'Margaret Crawford'.

Margaret Crawford

Auditor-General
10 December 2019

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Education 2019

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Section one

Education 2019

This report analyses the results of our audits of the Education cluster agencies for the year ended 30 June 2019.

Executive summary

This report analyses the results of our audits of financial statements of entities within the Education cluster for the year ended 30 June 2019. The table below summarises our key observations.

1. Machinery of Government changes

The Education cluster has expanded

From 1 July 2019, the Technical and Further Education Commission, the NSW Skills Board and the functions and activities associated with vocational training and skills now form part of the Education cluster.

2. Financial reporting

Audit opinions

Unqualified audit opinions were issued for all cluster agencies' 30 June 2019 financial statements audits.

The number of corrections to disclosures in the financial statements, which increased this year, could have been reduced by a more thorough quality assurance over the information underpinning the financial statements.

Recommendation: Cluster agencies should improve their quality assurance processes for financial reporting to improve the accuracy of financial statements presented for audit.

Preparedness for new accounting standards

Agencies will implement four new accounting standards shortly. Three are effective from 1 July 2019 and the fourth is effective from 1 July 2020. Cluster agencies needed to do more work on their impact assessments to better prepare for their implementation from 1 July 2019.

Recommendation: Cluster agencies should finalise their plans to implement the new accounting standards as soon as possible.

Timeliness of financial reporting

All cluster agencies met the statutory deadline for completing early close procedures and submitting their financial statements for audit.

The Department of Education (the Department) delays tabling its financial statements in parliament so it can report its operational outcomes, which are aligned to the calendar year, in a single report. This reduces transparency over the Department's financial statements as they are tabled more than ten months after the end of the financial year.

Recommendation: The Department should table its financial statements in parliament earlier, in line with other NSW Government agencies.

Inconsistencies in the employee leave data

We continue to observe inconsistencies in the employee leave data reported from the Department's payroll system, which impacts the reliability of estimates of the Department's liability for employee benefits. The robustness of the Department's quality assurance over leave liability data should be improved.

3. Audit observations

Internal control deficiencies

We identified 55 internal control issues, including 14 findings that were repeated from the previous year.

Issues were identified with user access administration, segregation of duties in the Department's key application system and timely preparation and review of key reconciliations.

Recommendation: Cluster agencies should prioritise and action recommendations to address internal control weaknesses.

Schools review 2018

Our review of a selection of NSW schools identified deficiencies in how they applied the Department of Education's 'Finance in Schools Handbook', resulting in control weaknesses in key areas such as governance, cash management and procurement.

Recommendation: The Department should ensure all schools apply the Department's 'Finance in Schools Handbook' as it is a key internal control.

1. Introduction

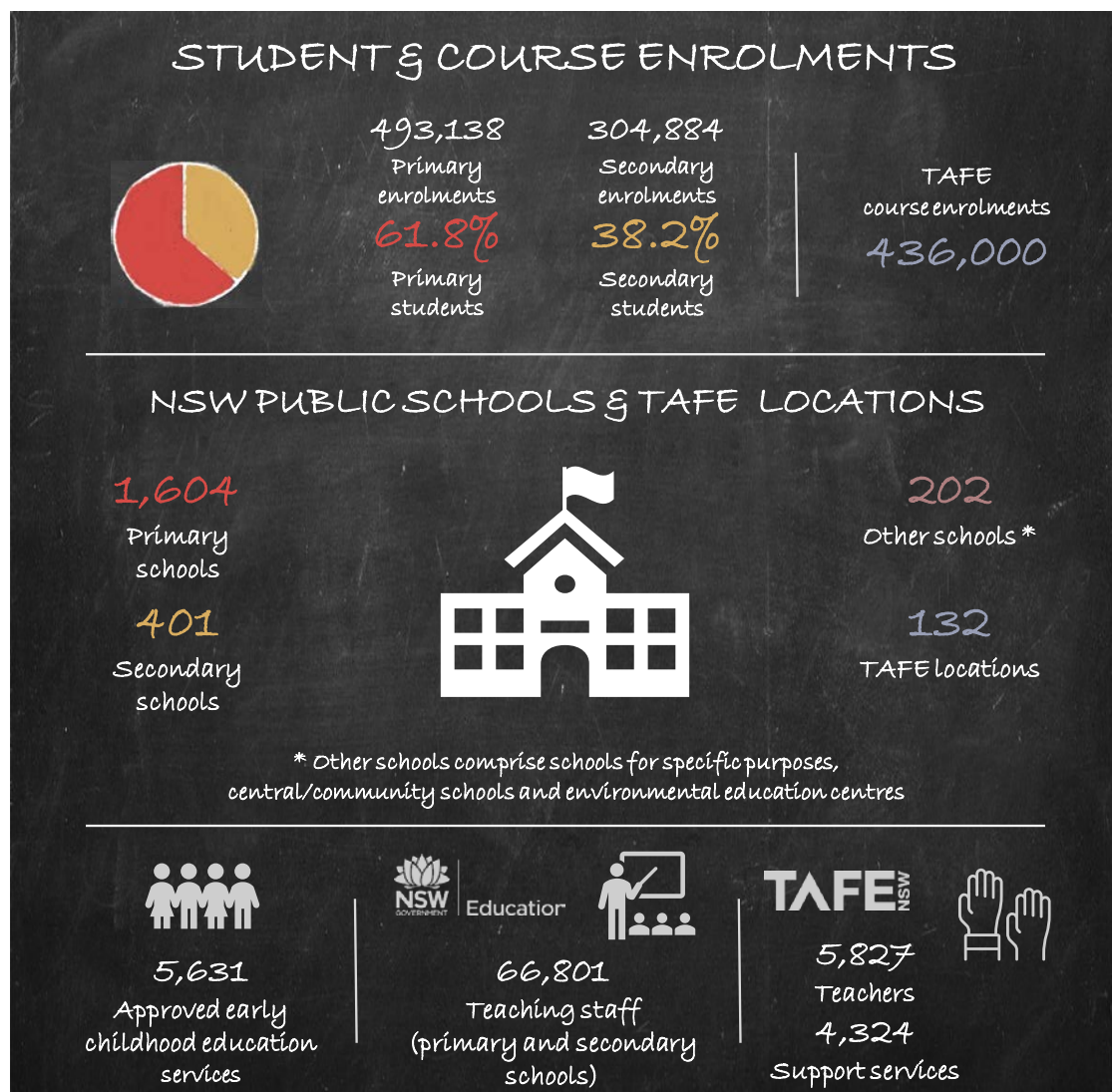
This report provides parliament and other users of the Education cluster's financial statements with the results of our audits, our observations, analysis, conclusions and recommendations in the following areas:

- financial reporting
- audit observations.

This cluster was significantly impacted by the Machinery of Government changes. The Technical and Further Education Commission and the NSW Skills Board, part of the former Industry cluster, were transferred on 1 July 2019. This report focusses on agencies in the Education cluster from 1 July 2019. Please refer to the section on Machinery of Government changes for more details.

1.1 Snapshot of the cluster

The Education cluster delivers and regulates education and training services for NSW students, workers and industry. This includes the early childhood education and care sector, government and non-government schools, and the vocation education and training sector.



Source: Department of Education and TAFE Commission.

1.2 Service delivery in the cluster

According to the 2019–20 NSW Budget Papers, the Education cluster will spend around \$21.0 billion (\$18.6 billion in recurrent expenses and \$2.4 billion in capital expenditure).

Education Cluster

Aims to deliver and regulate education and training services for students, workers and industry in NSW.

$$\begin{array}{rcl} \$18,600\text{m} & + & \$2,400\text{m} = \$21,000\text{m} \\ \text{Budgeted recurrent} & & \text{Budgeted capital} & & \text{Total budget} \\ \text{expenses 2019-20} & & \text{expenditure 2019-20} & & \end{array}$$

The Government's budget papers set priorities for the cluster to contribute to:

Providing education to all our communities and locations

Outcomes to be delivered

Educational foundations

Provide education for children and young people via the public-school system and providing support to non-government schools.

Recurrent expenses (M)		Capital expenditure (M)		Total budget (M)
\$15,700	+	\$2,200	=	\$17,900

Early childhood

Regulate and oversee the delivery of early childhood education services.

\$527	+	\$0	=	\$527
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Support teaching

Improve teacher quality through accrediting and regulating school and early childhood teachers via the NSW Education Standards Authority (NESA).

\$146	+	\$2	=	\$148
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Skilled and employable workforce

Support job growth by fostering a skilled workforce to meet the current and future requirements of business and industry, including the Technical and Further Education Commission (TAFE NSW).

\$2,300	+	\$138	=	\$2,438
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SOURCE: NSW Budget Papers 2019-20

2. Machinery of Government changes

Machinery of Government refers to how the government organises the structures and functions of the public service. Machinery of Government changes are where the government reorganises these structures and functions, and the changes are given effect by Administrative Arrangements Orders.

Section highlights

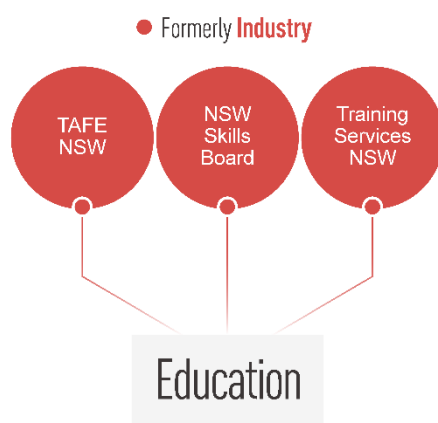
The 2019 Machinery of Government changes significantly impacted the Education cluster. From 1 July 2019, the functions and activities associated with the administration of legislation allocated to the Minister for Skills and Tertiary Education were transferred from the former Industry cluster to the Education cluster. Aboriginal Affairs NSW was transferred from the Department of Education (the Department) to the Department of Premier and Cabinet.

The Department is the principal agency in the cluster. The Machinery of Government changes bring new responsibilities, risks and challenges to the cluster.

2.1 Cluster changes

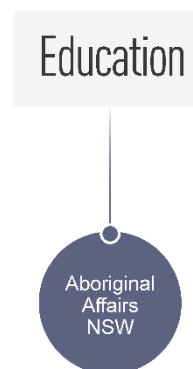
Machinery of Government changes

Key functions and agencies moved into the Education cluster as at 1 July 2019:



Key functions transferring out of the Education cluster as at 1 July 2019:

● To **Premier and Cabinet**



Training and skills return to the Education cluster

This year's Machinery of Government changes mark a return of the Technical and Further Education Commission (the Commission) and the NSW Skills Board into the Education cluster. These agencies were previously transferred from the Department of Education to the Department of Industry in 2015–16.

The Commission (trading as TAFE NSW) is the leading provider of vocational education and training in Australia. The Commission aims to contribute to job growth by delivering a highly skilled workforce that meets current and future requirements of NSW business and industry.

The NSW Skills Board (the Board) is charged with advising the NSW Government on how best to meet the skills and training needs of NSW individuals, industry, regions and the economy. The Board aims to provide independent, high-level, strategic advice on the vocational education and training system in NSW.

From 1 July 2019 employees involved in the administration of legislation allocated to the Minister for Skills and Tertiary Education were transferred from the former Department of Industry to the Department of Education. This included Training Services NSW, a division of the former Department of Industry and the corporate services support functions. Net liabilities of \$18.9 million comprising provisions and payables were transferred from the former Department of Industry to the Department of Education.

Aboriginal Affairs NSW transferred to the Premier and Cabinet cluster

Aboriginal Affairs NSW is charged with working with Aboriginal communities to promote social, economic and cultural wellbeing through opportunity, choice, healing, responsibility and empowerment. These functions were transferred from the Department of Education to the Department of Premier and Cabinet. From 1 July 2019, net liabilities of \$23.8 million, comprised mainly of liabilities associated with the Stolen Generations Reparations Scheme, were transferred from the Department of Education to the Department of Premier and Cabinet.

2.2 Agency preparation and implementation of changes

The Department continues to address the challenges of implementing Machinery of Government changes

The Department, as the lead cluster agency, participates in working groups established to manage the cluster changes at the sector and agency level.

The transfer of policy and program responsibilities between clusters poses challenges in:

- successfully integrating systems
- harmonising policies and procedures
- the transfer of personnel, physical records and budgets
- transitioning and maintaining existing levels of service to the public.

The Department continues to address these challenges by:

- providing ongoing corporate service support, including payroll, to Aboriginal Affairs NSW in accordance with a memorandum of understanding with the Department of Premier and Cabinet. The transition of all corporate services functions is expected to be completed by June 2020
- providing information and communications technology support to Training Services NSW through a transition plan expected to be completed by February 2020
- reviewing the existing policies of Training Services NSW for consistency with the Department's existing corporate policies
- revising its budget to reflect the recent Machinery of Government changes.

3. Financial reporting

Financial reporting is an important element of good governance. Confidence and transparency in public sector decision making are enhanced when financial reporting is accurate and timely.

This chapter outlines our audit observations related to the financial reporting of agencies in the Education cluster for 2019.

Section highlights

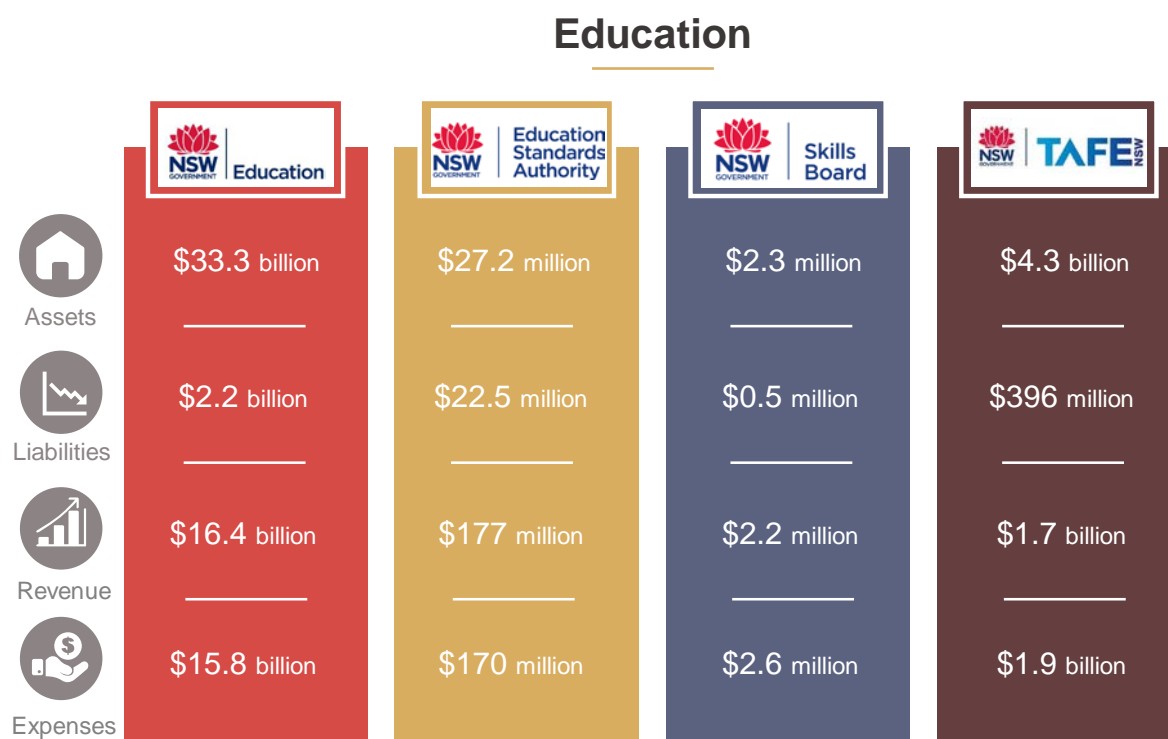
Unqualified audit opinions were issued on the financial statements of cluster agencies. However, a more thorough quality review process of the financial statements submitted for audit would help reduce the number of corrections to those statements.

All cluster agencies met the statutory deadlines for completing the early close procedures and submitting the financial statements.

We continue to observe inconsistencies in the employee leave data reported from the Department of Education's (the Department) payroll system. The robustness of the Department's quality assurance over leave liability data should be improved.

3.1 Financial snapshot

The snapshot below shows the financial positions at 30 June 2019 and the financial results for the year then ended for all agencies comprising the new Education cluster.



3.2 Quality of financial reporting

Audit opinions

Unqualified audit opinions were issued on the 30 June 2019 financial statements for all agencies in the cluster. Sufficient audit evidence was obtained to conclude the financial statements were free of material misstatement.

The number of misstatements identified in agency financial statements increased from the prior year

A misstatement is an error in amount, classification, presentation or disclosure in the financial statements initially submitted for audit.

In 2018–19, the number of monetary misstatements we identified through out audits of cluster agencies' financial statements increased to 42 (39 in 2017–18). We also observed an increase in the number of corrections made to disclosures in the financial statements submitted for audit - from 12 in the prior year to 19. This means the information presented for audit would have benefited from a more thorough quality assurance and review before they were submitted.

Recommendation

Cluster agencies should improve their quality assurance processes for financial reporting to improve the accuracy of the financial statements presented for audit.

Cluster agencies are preparing to implement new accounting standards

Cluster agencies will implement four new accounting standards shortly. Three are effective from 1 July 2019 and the fourth is effective from 1 July 2020. These standards are expected to significantly impact cluster agencies that receive fees for services and/or have leases of property plant and equipment. Given the breadth of anticipated changes for agencies in this cluster, it is important for those agencies to review their transaction flows, financial processes, controls within those processes including monitoring controls and the ability of those controls to detect errors.

As part of early close procedures, the Department and Technical and Further Education Commission (the Commission) had conducted preliminary assessments of the new accounting standards, estimating the financial impact on the date of initial application and subsequent years. These impacts were disclosed in the proforma financial statements.

Recommendation

Cluster agencies should finalise their plans to implement the new accounting standards as soon as possible.

Each agency is unique, and implementing the new standards is not straight forward. New principles will apply and management judgement is needed to interpret how those principles apply to revenue recognition from contracts with customers and for accounting for lease arrangements.

As a result, agencies face the following risks and challenges:

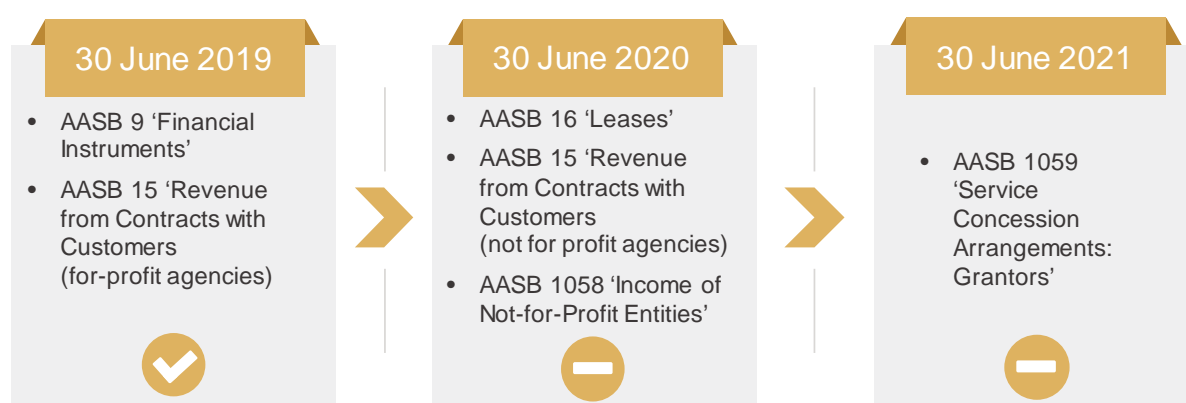
- supporting their staff with additional technical advice and resources
- having accurate data to assess the impacts
- correctly and consistently interpreting the new requirements
- adequately planning and preparing for their application
- implementing new systems to capture the information needed to meet the new reporting obligations.

To help agencies implement the new standards consistently, NSW Treasury:

- issued guidance to agencies
- prepared position papers on proposed accounting treatments
- provided briefing sessions to agencies
- mandated which option in the new standards agencies had to adopt on transition.

Preparing well in advance is key for agencies to effectively transition to the new standards. The transition requires significant planning and resources to ensure the impacts are appropriately assessed and all necessary information is captured accurately for reliable reporting. Key points to consider in the transition are included in the [Report on State Finances 2019](#).

Key dates



3.3 Key accounting issues

The Department continues to address long-standing issues with its leave data

At 30 June 2019 the Department reported employee benefit entitlements totalling \$1.1 billion. These entitlements, representing obligations to departmental staff for annual and vacation leave and long service and extended leave on-costs, are financially significant for the Department.

In our 2015–16 financial statement audit, we identified inconsistencies in the annual, long service and extended leave balances reported from the Department's payroll systems. These issues were not fully resolved and were reported to the Department as being a high risk in 2017–18.

This year, inconsistencies continued to be identified in the annual, long service and extended leave balances. The Department manually checks the data supporting leave entitlements before making payments to individuals when they leave the service. However, for the purposes of calculating the Department's overall provision for employee annual, long service and extended leave, the underlying data has known errors. Many of these data irregularities arise from award entitlements whereby teachers can preserve their leave entitlements when they take a break in service, rather than have them paid out. Many of the irregularities were known to exist in the Department's legacy payroll system but were migrated to the current SAP system because of the complexity of cleansing the data. Data irregularities include:

- staff with negative leave balances
- a lack of history to support balance entitlements carried forward
- duplicate records for the same staff member where they have had multiple positions and periods of service
- aged balances where employees have had extended breaks in service and are unlikely to return to work.

We found the quality and robustness of management's review should be improved to ensure the completeness and accuracy of these balances. Because the Department's employee long service and extended leave balances are assumed by the Crown, there is no net impact for the Department's financial statements.

During the year the Department engaged an external consultant to help address these matters, including the development of remediation strategies and management activities.

The Department is carrying employee entitlements for staff that are unlikely to return to service

As part of the Department's activities in addressing their ongoing issues with leave data, the Department identified employees whose break in service since the last date of their last employment ranged from five to 17 years. The estimated value of these entitlements is around \$6.4 million as at 30 June 2019. A further cohort of employees with breaks in service of between zero to five years have accrued entitlements of \$9.2 million.

A plan to validate and extinguish these obligations was established by the Department which included confirming employment status with these employees to ascertain their likelihood of return to service. In the case of employees that could not be contacted, notifications were provided to their next of kin.

Going forward, the Department will perform an annual review of the leave entitlements for employees who have not worked at the Department for five years or more.

Ongoing issues with the implementation of the TAFE Student Management System

In prior years we reported on information system limitations at the Commission, specifically relating to its student administration system. The Commission continues to implement additional processes to verify the accuracy and completeness of revenue from student fees for the 2018–19 financial year.

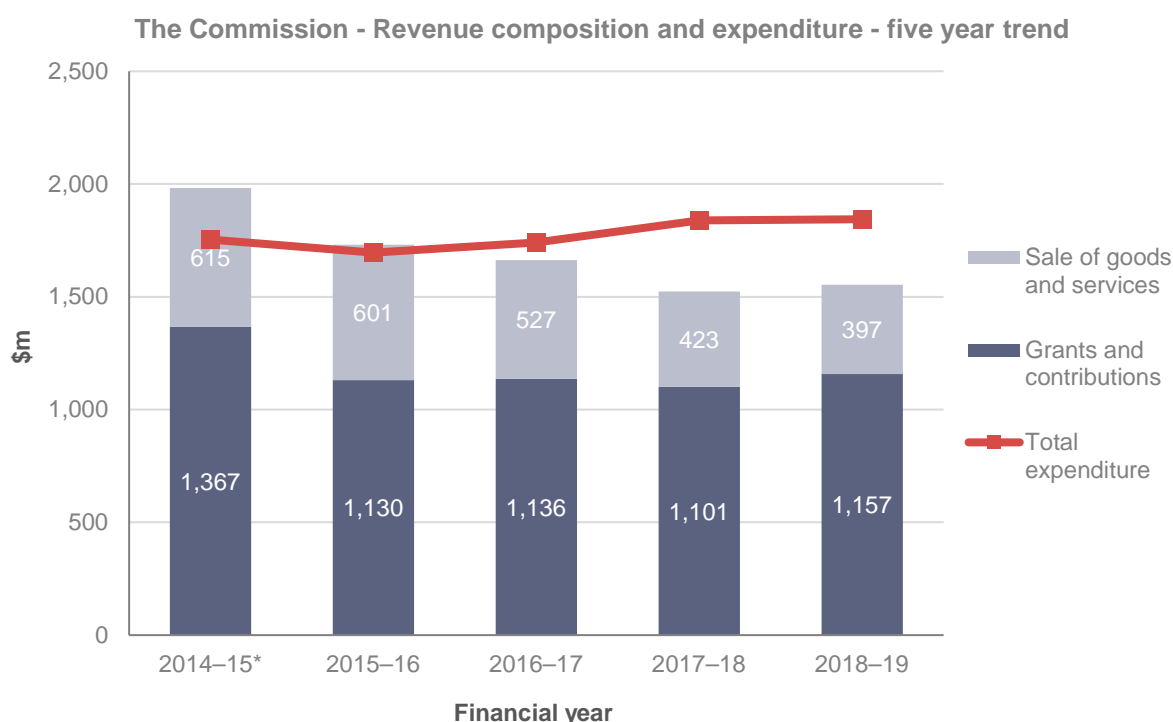
In 2017–18 the Commission started implementing a new student management system. Significant delays have occurred in implementing this system, mainly due to the complexity of integrating the vendor solution with the requirements of the Commission. Final project delivery timeframes and estimated completion costs are being reviewed. Costs incurred to date amount to \$67.0 million. The original budget for this new system is \$89.4 million.

3.4 Sustainability of cluster agencies

In 2018–19, two agencies reported net deficits for the year. The NSW Skills Board recorded a net deficit of \$0.4 million (2018: deficit \$0.2 million) while the Commission reported a net deficit of \$228 million (2018: deficit \$240 million).

The Commission continues to report deficit net results

The Commission has reported net deficits year on year since 2015–16*. Sales of goods and services, mainly comprising student fees, decreased by 34 per cent from \$601 million in 2015–16 to \$397 million in 2018–19. Over the same period, operating expenditure increased from \$1.7 billion to \$1.8 billion, largely driven by higher employee-related costs.



* The results for 2014–15 have been excluded from our analysis as the financial statements were qualified as we were unable to form an opinion on the appropriateness of amounts recorded for sales of goods and services.

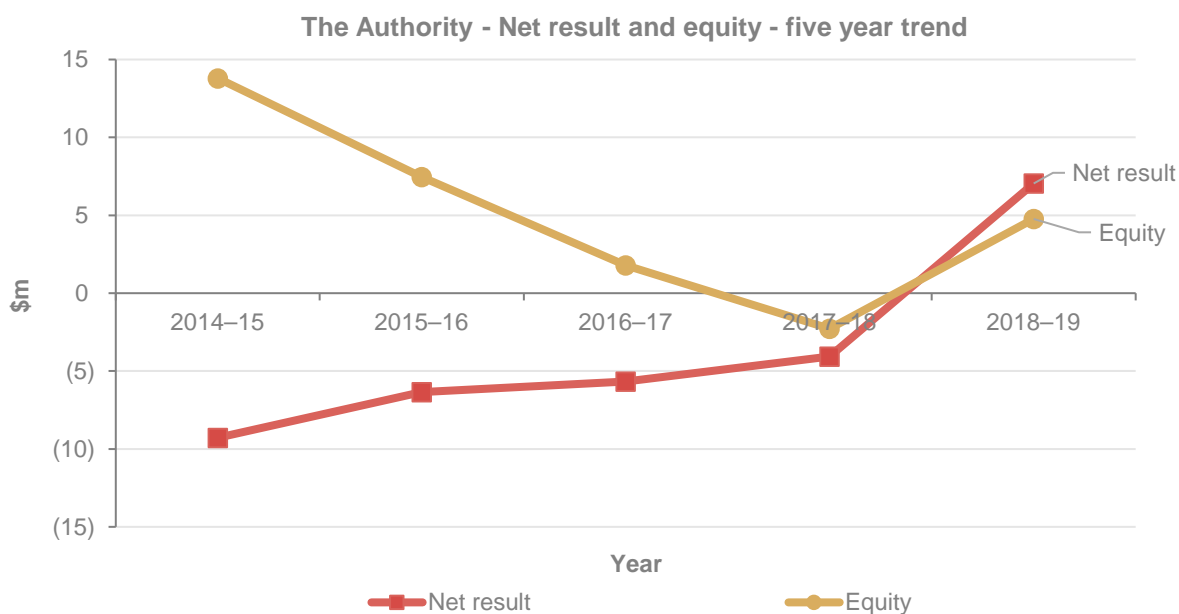
As sales of goods and services fall, the Commission is increasingly reliant on government funding and contributions to sustain its operations. In 2018–19, the proportion of income the Commission generated from the sale of goods and services had reduced from 33 per cent in 2015–16 to 24 per cent in 2018–19. On the other hand, the proportion of grants and contributions received by the Commission increased from 63 per cent to 70 per cent for the same period.

The Commission's cash balances have also declined each year. In 2018–19, the Commission received a \$100 million capital injection from NSW Treasury to supplement and manage its working capital.

On-going deficits and declining cash balances challenge agencies as they may struggle to absorb unforeseen expenses, operational needs and materialising risks, without significantly changing their revenue and expenditure strategies.

Grant funding for the NSW Education Standards Authority

The NSW Education Standards Authority (the Authority) previously reported net deficits and declining equity positions every year. However, towards the end of the financial year, the Department gave the Authority a one-off cluster grant totalling \$10.0 million in recognition of a range of services provided by the Authority to the government schooling system. As a result, the Authority reported a positive result of \$7.0 million and positive equity position of \$4.8 million.



While a one-off grant can improve the overall financial results of an agency at balance date, agencies can find it hard to anticipate the cash injection and plan the delivery of their services, budget expenditure and manage risks during the year.

3.5 Timeliness of financial reporting

Financial statements were submitted on time

In 2018-19, all agencies met the statutory deadlines for completing early close procedures and submitting financial statements. Audit opinions were also issued within the statutory dates.

The table below shows the timeliness of financial reporting for cluster agencies.

Timeliness of financial reporting			
Cluster agencies	Early close procedures	Financial statements	Audit report
Principal department			
Department of Education	✓	✓	✓
Agencies related to the Department			
NSW Education Standards Authority	✓	✓	✓
NSW Skills Board	✓	✓	✓
Technical and Further Education Commission	✓	✓	✓
Key	✓ Statutory reporting deadline was met	! Statutory reporting deadline was not met	

The Department delays tabling its financial statements each year so it can report its operational outcomes at the same time

The *Annual Reports (Departments) Act 1985* (the Act) prescribes the reporting and tabling requirements for all NSW departments. The annual report comprises a report of operations and audited financial statements and must be tabled within five months after the end of each financial year.

While the Department certified its financial statements and received their independent auditor's report by the statutory reporting deadlines, provisions in the Act allow it to prepare its annual report based on the calendar (school) year and table the annual report in May, following the end of the school year. While this allows the Department to include its operational outcomes and audited financial statements in a single annual report, it also means the Department's financial statements are tabled in parliament more than ten months after the end of the financial reporting year.

If the financial statements were tabled earlier as stand-alone document it would improve transparency and ensure members of the parliament and the public had more timely access to the Department's financial statements.

Recommendation

The Department should table its financial statements in parliament earlier, in line with other NSW Government agencies.

The NSW Education Standards Authority Staff Agency and TAFE Commission (Senior Executives) Staff Agency were no longer required to prepare financial statements

On 19 June 2019, the Executive Council approved the Public Finance and Audit Amendment (Financial Reporting and Auditing Exclusions) Regulation 2019. The regulation provided statutory financial reporting relief for a number of entities. These entities included NSW Education Standards Authority Staff Agency and TAFE Commission (Senior Executives) Staff Agency. The staff agencies were exempted from reporting arrangements as their activities, which solely comprise employing the staff for the relevant parent entity, are reported in the parent entity's consolidated financial statements.

3.6 Schools review 2018

The Department is the largest provider of education in Australia, with responsibility for delivering public education to two-thirds of the NSW student population. The state's 2,200 public schools are spread across NSW, servicing around 798,000 students and employing around 67,000 teachers.

The financial results of NSW public schools are included in the Department's financial statements each year and as such follow the financial framework set out by the Department.

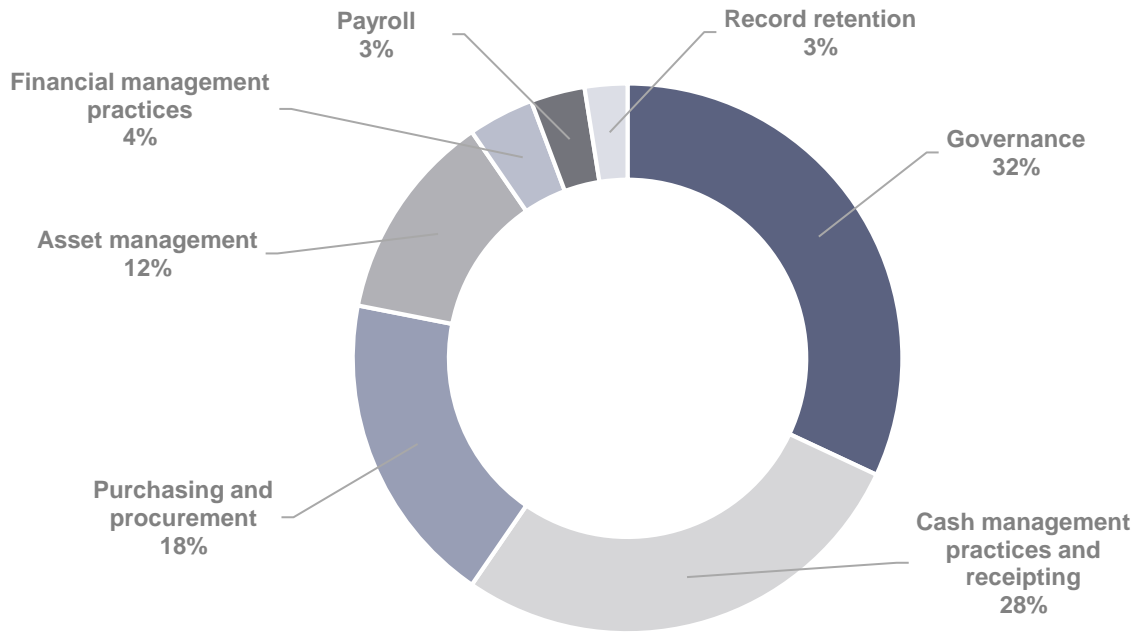
The decentralised nature of the Department's public school network inherently poses challenges in ensuring consistency in financial management, governance practices and internal controls. To that end, the Department issues guidelines known as the 'Finance in Schools Handbook' (the handbook). This handbook, which the Department plans to update as part of its Financial Management Optimisation project, is designed for principals, teachers and school administrative support staff. It aims to ensure:

- accuracy, reliability and integrity of accounting and administrative transactions
- safeguarding of assets
- efficient and effective operation of accounting and related administrative systems.

As part of our audit of the Department, we perform audit procedures over a cross-section of public schools in NSW. These schools ranged from primary to secondary, in metropolitan and regional areas and were large enough to be representative of all schools forming the broader public schools' network. Elements of our program were drawn from the Department's handbook and covered the controls we believe present a heightened risk for the Department's financial statements.

Our review of 70 NSW schools found weaknesses in key areas such as governance, cash management and procurement

We classified the 438 matters we identified in our review of 70 schools across NSW into the following categories:



Source: Audit Office management letters issued to schools.

Seventy-eight per cent of the deficiencies we identified related to governance, cash management practices and receipting, and purchasing and procurement. Further details on these findings can be found in Chapter 4 Audit observations.

4. Audit observations

Appropriate financial controls help ensure the efficient and effective use of resources and administration of agency policies. They are essential for quality and timely decision making.

This chapter outlines our observations and insights from our financial statement audits of agencies in the Education cluster. It also comments on our review of the financial control framework applied by 70 schools in NSW whose financial results form part of the Department of Education's (the Department) financial statements.

Section highlights

- Audit Office management letter recommendations to address internal control weaknesses should be actioned promptly, with a focus on addressing repeat issues. The 2018–19 financial audits of cluster agencies identified 55 internal control issues, including 14 that were carried forward from the previous year.
- Application controls are procedures that operate at a business process level designed to ensure the integrity of accounting records. The Department can mitigate the risk of fraud or error in preparing its financial statements if segregation of duties are appropriately configured in their key application system.
- Our review of a selection of schools across NSW identified deficiencies in how schools apply the Department's financial management practices and governance arrangements.

4.1 Internal control deficiencies

Management letter findings

Effective internal controls reduce the risk of fraud and error and help agencies operate efficiently and effectively and to comply with relevant laws, standards and policies. Our audits do not review every control every year. We select a range of measures, and report on those that present the most significant risks that agencies should mitigate. We report on deficiencies in internal controls, matters of governance interest and unresolved issues identified to management and those charged with governance. We do this through our management letters, which include our observations, related implications, recommendations and risk ratings. The table below presents the number of management letter findings for each agency within the cluster.

Management letter findings					
	Extreme	High	Moderate	Low	Repeat
Principal department					
Department of Education	--	--	9	2	2
Agencies related to the Department					
NSW Education Standards Authority	--	--	2	2	1
NSW Skills Board	--	--	--	--	--
Technical and Further Education Commission	--	--	30	10	11
Total			41	14	14

In 2018–19 we identified a total of 55 issues for cluster agencies, including 41 new issues and 14 issues repeated from previous years. We have classified these issues into common categories as follows:

- financial operational deficiencies
- IT operational deficiencies
- reporting deficiencies.



Recommendation

Cluster agencies should prioritise and action recommendations to address internal control weaknesses.



A delay in implementing audit recommendations increases the risk of intentional and accidental errors in processing information, producing management reports and generating financial statements. This can impair decision-making, affect service delivery and expose agencies to fraud, financial loss and reputational damage. Poor controls may also mean agency staff are less likely to follow internal policies, inadvertently causing the agency not to comply with legislation, regulation and central agency policies.

The table below describes the common issues identified across the cluster by category, risk ratings and implications.

Table: Common issues reported in cluster agencies' management letters



Operational - Financial			
	Moderate:	7 new	3 repeat
	Low:	2 new	1 repeat
Common issue	Findings	Implications	
Policies and procedures	Agencies have not established policies, have gaps in policies or have policies that are past their scheduled review date.	There is a risk that outdated policies and procedures may be followed, that policies and procedures do not reflect better practice, or where practice is not documented, the agency is at risk from the loss of corporate knowledge when staff turnover.	
Contract registers	Agencies have incomplete or inaccurate contract registers.	These agencies may face challenges with: <ul style="list-style-type: none"> • complying with GIPA obligations • effectively managing their contractual commitments • disclosing contractual commitments accurately in their financial statements. 	

Operational - IT

	Moderate:	7 new	5 repeat
	Low:	3 new	

Common issue	Findings	Implications
General controls	IT control deficiencies are related to IT governance, user access administration, program change and computer operations.	Inadequate control over the IT environment could create opportunities for fraud and error.
Application controls	Application controls are procedures that operate at a business process level designed to ensure the integrity of accounting records. We found the Department had not appropriately configured segregation of duties in their key application system.	Inadequate segregation of duties increases the risk of recording unauthorised or non-existent transactions.

Reporting

	Moderate:	16 new	3 repeat
	Low:	6 new	2 repeat




Common issue	Findings	Implications
Reconciliation controls	Key reconciliations were not prepared or were not reviewed in a timely manner. Reconciliations of inter-agency balances were not performed.	There is a risk of misstatements in financial statements.

Note: Management letter findings are based either on final management letters issued to agencies, or draft letters where findings have been agreed with management.

Our Internal controls and governance 2019 report (tabled November 2019) expands on the matters identified and also covers the findings and recommendations from our 2018–19 financial audits at 40 of the largest agencies in the NSW public sector. These 40 agencies included the Department of Education and the TAFE Commission.

Table: Findings from the review of controls in NSW Schools

The table below describes the most common deficiencies across the schools reviewed, their risk ratings and implications.

Category/risk rating	Findings	Implications
Governance  Moderate	<p>Our review of governance practices found instances where schools:</p> <ul style="list-style-type: none">• did not establish or maintain registers of financial items or a workplace gift register• did not retain, or had not formalised a school canteen agreement• canteen pricing policies were not approved by the principal.	<p>Not having adequate registers inhibits the ability for schools and the Department to maintain adequate oversight over management practices, compliance with requirements and internal policies.</p>
Cash management practices and receipting  Moderate	<p>Our review of cash management processes and procedures found instances where schools:</p> <ul style="list-style-type: none">• did not review or reconcile bank queries on a weekly basis• did not perform, or review the petty cash reconciliations• did not bank cash on hand when balances exceeded \$500• were unable to demonstrate an independent review had been conducted on check coversheets• did not adequately follow up identified discrepancies in cash balances held.	<p>Deficiencies in cash management practices inhibits the Department's ability to manage and mitigate fraud risk, error and compromises the accuracy of data transposed in internal and annual financial reporting.</p>
Purchasing and procurement  Moderate	<p>Our review of procurement and purchasing practices at the schools found instances whereby:</p> <ul style="list-style-type: none">• schools did not obtain the appropriate number of quotes for the purchase of goods and services• expenditure was incurred without prior approval• purchase orders were not raised for goods and services.	<p>The decentralised nature of the Department's procurement and purchasing lends itself to elevated risks of:</p> <ul style="list-style-type: none">• non-compliance with the Department's procurement guidelines• unauthorised or illegitimate purchases, exposing the Department to fraud risk or reputational damage.

Recommendation

The Department should ensure all schools apply the Department's 'Finance in Schools Handbook' as it is a key internal control.

4.2 Key issues

Local Schools, Local Decisions

In 2012, the Department launched the Local Schools, Local Decisions education reform. The reform aims to give NSW Government schools more authority to make local decisions about how best to meet the needs of their students. As such, an increasing portion of the education budget has been devolved to public schools. Sound financial management practices at individual schools are therefore important to ensure its success.

The Audit Office of New South Wales is conducting a performance audit report on 'Needs-based funding in government schools'. This audit will assess the effectiveness of the Department's support and oversight of school planning and use of needs-based funding. It will also focus on:

- the Department's accountability arrangements to oversee school management of needs-based funding
- support provided to build schools' capacity in planning for the use of needs-based funding.

The report is expected to be tabled in parliament in the first half of 2020.

Transition to NAPLAN Online

NAPLAN is an annual assessment for all students in Years 3, 5, 7 and 9. The tests cover student skills in reading, writing, spelling, grammar and punctuation, and numeracy.

Australian Government, state and territory education ministers agreed to move the annual NAPLAN assessments from pencil and paper to online testing by 2020. Unlike paper-based tests, NAPLAN Online adapts to student responses in real time. In 2018, the first year of transition, just over 25 per cent of schools participated in NAPLAN Online, compared with around 55 per cent of schools in 2019. The remainder of NSW schools are planned to transition by 2020.

In our previous reports we commented on the Department's progress against the State and Premier's Priority targets using final NAPLAN data released by the Australian Curriculum, Assessment and Reporting Authority. NAPLAN testing continues to transition from paper-based to online testing. Delays were expected in the release of the results because of connectivity issues and some students needed to resit tests. Final results are not available at the date of writing this report.

Outcome budgeting

Outcome budgeting was announced as a reform initiative in the 2017–18 State budget with the intention of transforming the way budget decisions are made, and how resources are managed in the NSW public sector.

Under this reform, the allocation of public resources will move away from amounts spent, or volume of services delivered, towards focussing on outcomes achieved for NSW citizens.

The Department volunteered to prepare its 2019–20 budget using the principles and framework outlined in Treasury's policy paper TPP 18-09 'Outcome Budgeting'.

Our Annual work program 2019–20 flagged our intention to conduct a performance audit on outcome based budgeting and will consider its implementation and agency uptake, and whether agencies are positioned to maximise its benefits.

Section two

Appendices

Appendix one – List of 2019 recommendations

The table below lists the recommendations made in this report.

1. Financial reporting

Quality of financial reporting

Cluster agencies should improve their quality assurance processes for financial reporting to improve the accuracy of financial statements presented for audit.



Preparedness for new accounting standards

Cluster agencies should finalise their plans to implement the new accounting standards as soon as possible.



Timeliness of financial reporting

The Department should table its financial statements in parliament earlier, in line with other NSW Government agencies.



2. Audit observations

Internal control deficiencies

Cluster agencies should prioritise and action recommendations to address internal control weaknesses.



Schools review 2018

The Department should ensure all schools apply the Department's 'Finance in Schools Handbook' as it is a key internal control.



Key



Low risks








Medium risks



High risks

Appendix two – Status of 2018 recommendations

Recommendation	Current status
The Department of Education should:	
Confirm leave data and review assumptions following deployment of the new HR/Payroll system to better estimate the liability for employee benefits and the amount to be assumed by the Crown Entity.	Whilst the Department has been more proactive in resolving this issue, inconsistencies in the leave data remains an issue at the Department. 
Cluster agencies should:	
Prioritise and action recommendations to address internal control weaknesses.	<p>All agencies are assigning ownership of recommendations and timeframes for completion. All agencies are also reporting on the status of outstanding recommendations to their audit and risk committee.</p> <p>Of the 66 recommendations raised in our management letters, 52 have been implemented.</p> 
Key	 Fully addressed  Partially addressed  Not addressed

Appendix three – Cluster agencies

Agency

Principal department

Department of Education

Agencies related to the Department

NSW Education Standards Authority

NSW Skills Board

TAFE Commission

Appendix four – Financial data

	Total assets		Total liabilities		Total revenue		Total expense	
	2019	2018	2019	2018	2019	2018	2019	2018
	\$m	\$m	\$m	\$m	\$m	\$m	\$m	\$m
Principal department								
Department of Education	33,304	32,458	2,196	1,952	16,388	14,339	15,820	14,369
Agencies related to the Department								
NSW Education Standards Authority	27	25	22	27	177	150	170	154
NSW Skills Board	2	3	0.5	0.8	2	2	3	2
TAFE Commission	4,317	4,434	396	371	1,650	1,602	1,877	1,842

OUR VISION

Our insights inform and challenge government to improve outcomes for citizens.

OUR PURPOSE

To help parliament hold government accountable for its use of public resources.

OUR VALUES

Pride in purpose

Curious and open-minded

Valuing people

Contagious integrity

Courage (even when it's uncomfortable)

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