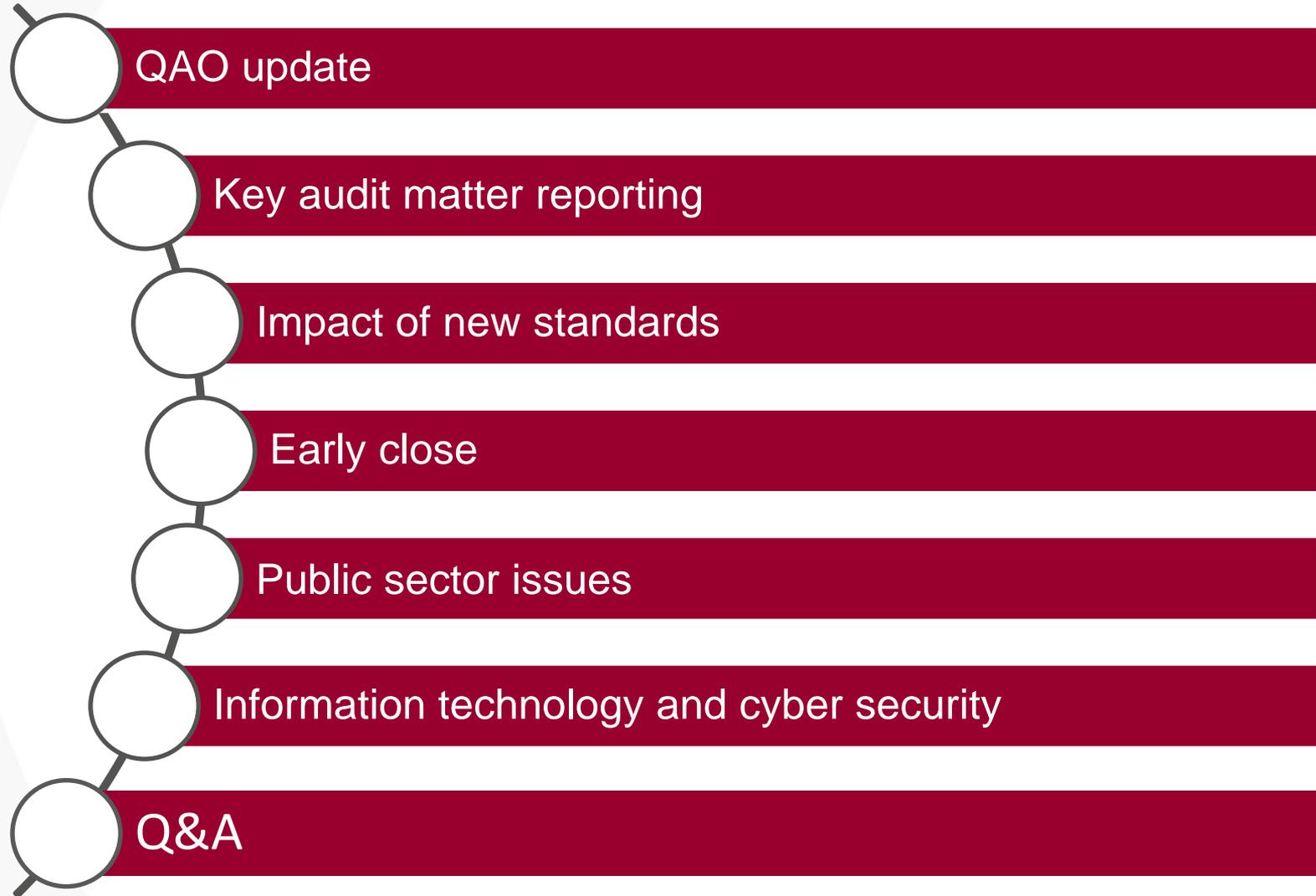


# QAO briefing for Audit Committee Chairs

7 December 2017





# QAO update

Brendan Worrall  
Auditor-General



**Vision** Better public services

**Purpose** Independent assurance and trusted advice

**Who we serve** The parliament and the public of Queensland, public sector entities, and local governments

**Values**



Objectives	Strategic risks	Strategies	Indicators of achievement
<ul style="list-style-type: none"> <li>We support and challenge our people to best serve parliament and our clients.</li> <li>Those we serve trust and value our services and advice.</li> <li>Our assurance services and advice are used to improve accountability and performance.</li> </ul>	<ul style="list-style-type: none"> <li>We do not uphold our values or professional, ethical and quality standards.</li> <li>We do not adapt our services in response to changing needs.</li> <li>We do not sufficiently understand our clients' organisations and context to deliver valuable assurance services.</li> </ul>	<ul style="list-style-type: none"> <li>Supporting our workforce to meet parliament's and our clients' service needs.</li> <li>Enhancing relationships.</li> <li>Adapting our assurance services to provide greater value.</li> </ul>	<ul style="list-style-type: none"> <li>Our people are professional, capable and engaged.</li> <li>Our relationships are valued.</li> <li>Parliament and our clients benefit from the assurance services and advice we provide.</li> </ul>

- My client engagement in 2018
- Simplifying reports to parliament
- Traffic lights to only cover 'significant deficiencies', 'deficiencies' as broad themes
- Refresh of Strategic Audit Plan
- Fraud risk in the public sector

Tone at the top

Contracts and variations

Power imbalance

Culture and ethics

Management override

Procurement

Influence

Conflict of interest

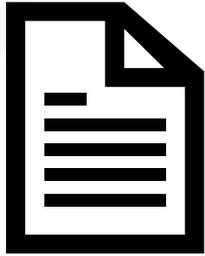
# Q&A

# Technical update

Karen Johnson

Assistant Auditor-General





We issued 60 IAR  
with KAMs



4 entities had 3 KAMs  
8 entities had 2 KAMs  
48 entities had 1 KAM

Types of KAMs	#
Valuation of PPE—specialised buildings	21
Valuation of PPE—other	20
Financial instruments and liabilities	8
Depreciation	6
Other (PPP, administered revenue, CSO, receivables)	5

- ✓ No KMP transactional disclosure required at either a Departmental or WOG level
- ✓ Minimal disclosures in statutory bodies
- ✓ Local governments – generally good but some under reporting



# Upcoming changes

**2018-19**

**AASB 15 Revenue  
For-profits**

**AASB 9 Financial  
Instruments**

**2019**

**AASB 15 Revenue  
+ AASB 1058  
Income for NFPs**

**AASB 16 Leases**

**AASB 1059  
Service  
concessions**

**Beyond**

**AASB 17  
Insurance  
contracts**

**RDR**

**Reporting entities**

- ❖ Have they identified their revenue sources?
- ❖ How far are they in evaluating the potential impact of the revenue/income standards?
- ❖ Have they obtained details of their operating leases?
- ❖ Have they identified their financial instruments?
- ❖ How far are they in evaluating any potential change in classification and accounting?
- ❖ What have they considered in relation to the new impairment loss model?
- ❖ Have they discussed the matters with you, and you with QAO, before they have undertaken extensive work or obtained advice?



Technical experts “at 10 paces”

# Why revise the financial instruments standard?

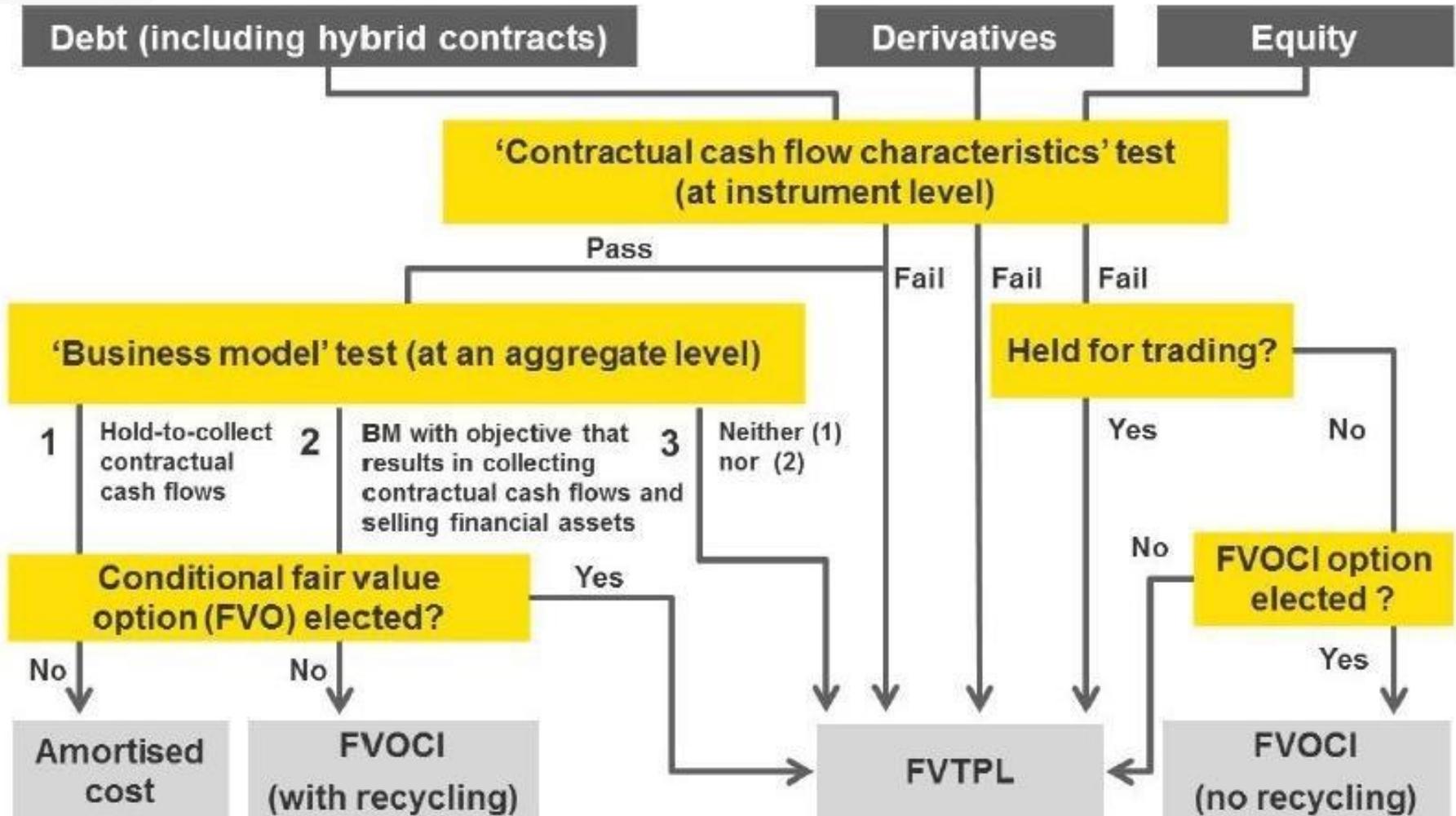
Answer = the complexity of the former standard (IAS 39 / AASB 139)

*‘Those that tell me they understand IAS 39,  
clearly haven’t read it properly’*

Sir David Tweedie, Chairman of the International Accounting Standards Board (IASB), FEE Seminar, Brussels, 1 December 2005

**AASB 139 is now replaced with AASB 9**

# Classification of financial assets



## Interest free loans (classification and measurement)

- Defined term
- Early repayment option

## Non-recourse loans (classification and measurement)

## Impairment for loans to government entities

- Federal – AAA rating
- Queensland – AA rating
- AAA corporates do default
- Governments do default
  - Australia defaulted in 1931

## AASB15

- Revenue recognition now related to performance obligation

## Income of not for profit

- Standard this year
- Remove reciprocal/non-reciprocal (sort of)

# Revenue recognition process – 5 steps

Identify contracts



Identify performance obligations



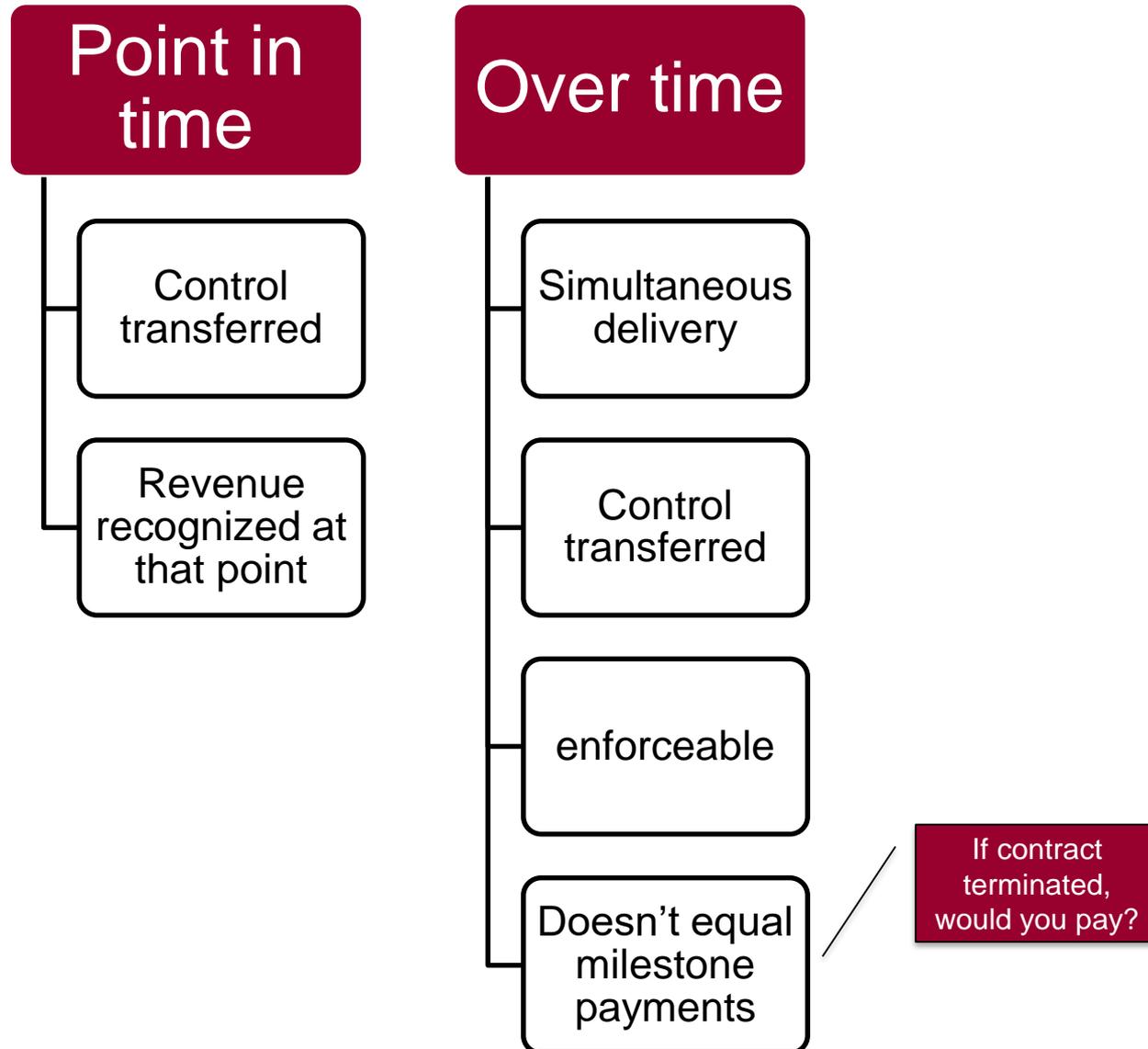
Determine price



Allocate transaction price to performance obligations

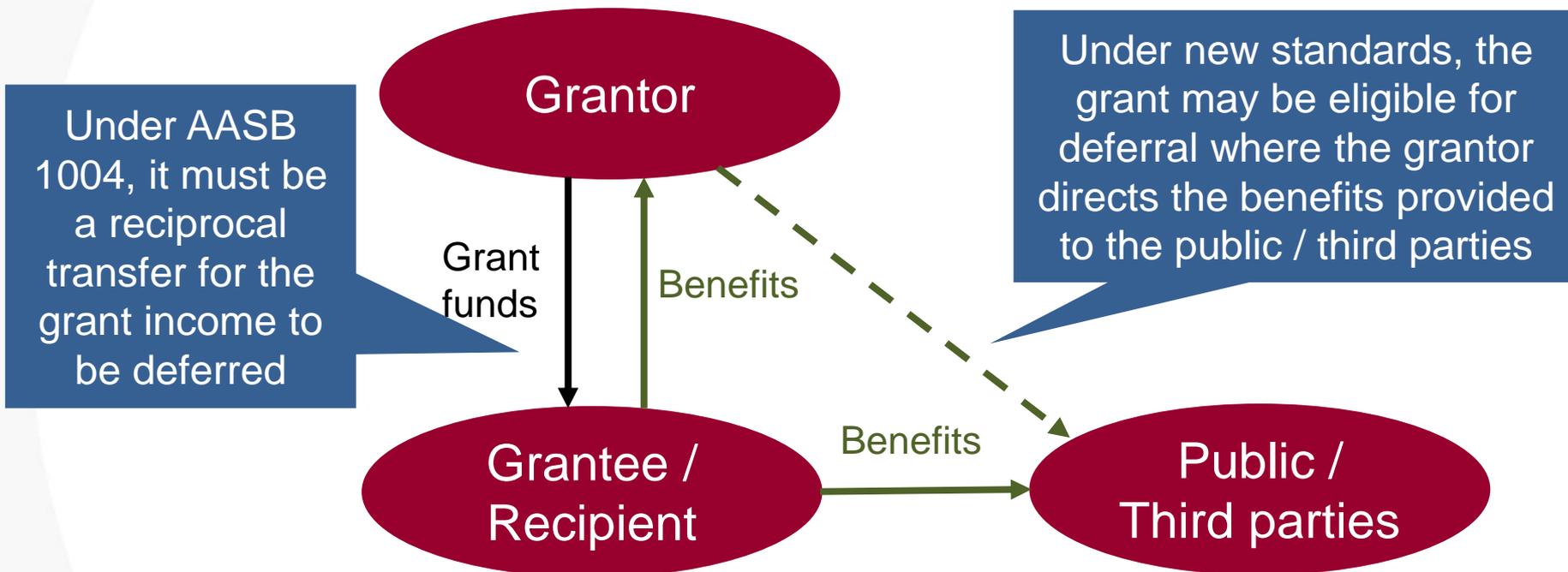


Recognise revenue when performance obligation is satisfied



# Revenue recognition changes—accounting for grant income

## Conceptual change from AASB 1004



# Are you AASB 1058/AASB 15 ready?

- ❖ What are your revenue, income and grant sources?
- ❖ Which sources involve activities in a different financial year to when the money is received?
- ❖ How will your accounting change? E.g. from up-front to deferral?
- ❖ Do you have systems to determine how much to recognise and how much to defer?
- ❖ Will you be preparing comparatives in the first year of application?



# AASB 16—lease accounting

## We did we need the change?

*‘One of my great ambitions before I die is to fly in an aircraft that is on an airline’s balance sheet’*

Sir David Tweedie, Chairman of the International Accounting Standards Board (IASB), April 25, 2008

## Same accounting treatment as for finance leases

- Determine term
- Determine rental payments (cash flows)
- Determine discount rate



## Recognise

- Lease liability
  - lease interest
- Lease asset (right-to-use asset)
  - depreciation

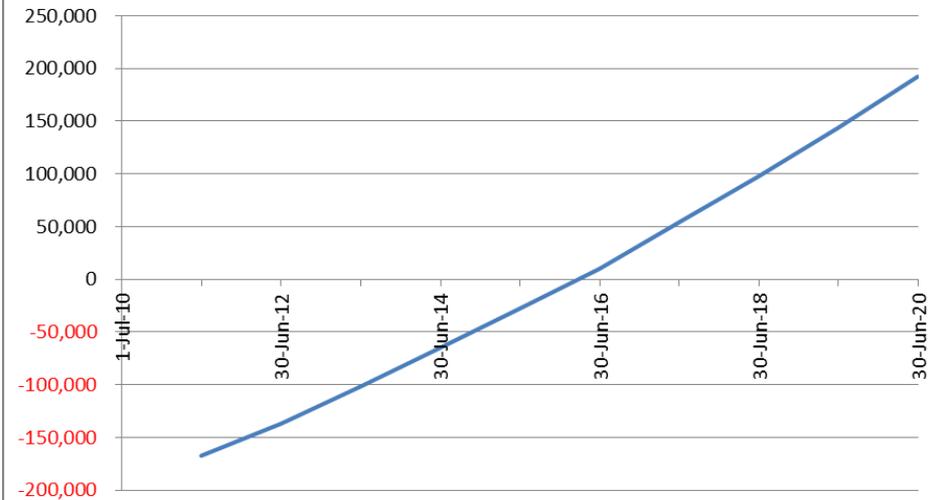


# Leases—Profit or loss effect

### Gross effect P&L Interest and dep'n c/f lease payment



### Net effect P&L



Ratio	Ratio formula	Effect
Working capital ratio	$\frac{\text{Current Assets}}{\text{Current Liabilities}}$	Lower
Gearing ratio	$\frac{\text{Interest Bearing Liabilities}}{\text{Equity}}$	Higher
Net profit margin	$\frac{\text{Net profit after tax}}{\text{Sales}}$	Financing effect
Return on assets	$\frac{\text{EBIT}}{\text{Assets}}$	Financing effect—profit Higher assets
Return on equity (return on capital employed)	$\frac{\text{Net profit after tax}}{\text{Equity}}$	Financing effect—profit Lower equity
Earnings per share	$\frac{\text{Net profit after tax}}{\text{Number of shares}}$	Financing effect

- ❖ Accounting for CPI increases
- ❖ Implicit interest rates
- ❖ Peppercorn and below-market rentals
- ❖ Recognise at fair value

# Are you AASB 16 ready?

- ❖ What operating leases do you have?
- ❖ Do any of them get excluded under the less than 12-month and low value (\$7 500 AUD) exemptions?
- ❖ Are you reasonably certain of exercising any options—even if at market value?
- ❖ How do your lease rentals change (e.g. CPI, fixed, market reviews)?
- ❖ When do your lease rentals change?



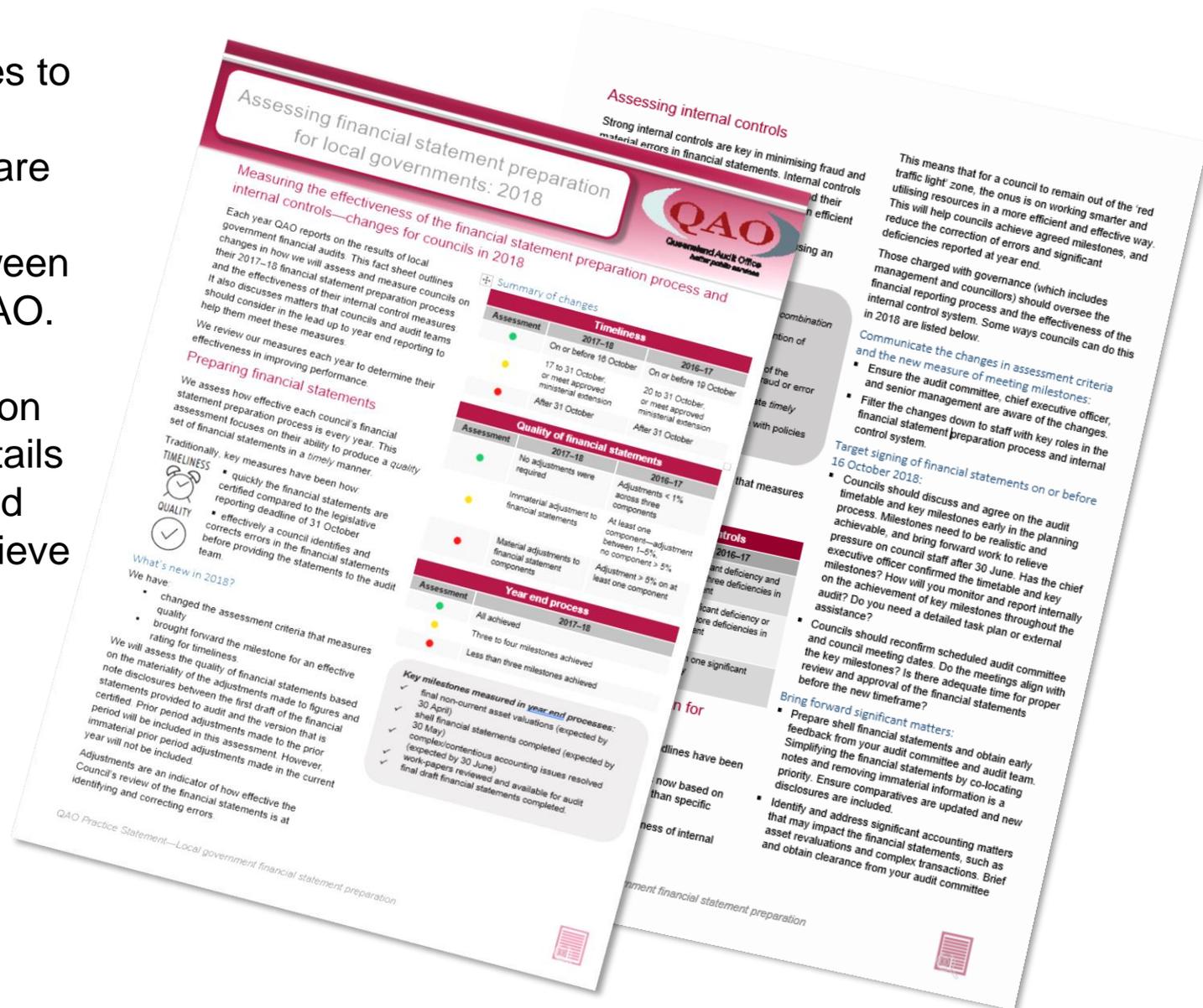
- Completing early close processes
- Non-current asset valuations by 31 May
- Pro forma financial statements by 30 April
- Resolving known accounting issues by 30 April
- Concluding all asset stocktakes by 30 June

Our rating	Year end close process assessment
● Implemented	All key processes were completed by the target date
● Partially implemented	Three key processes were completed within two weeks of the target date
● Not implemented	Less than two key processes were completed within two weeks of the target date

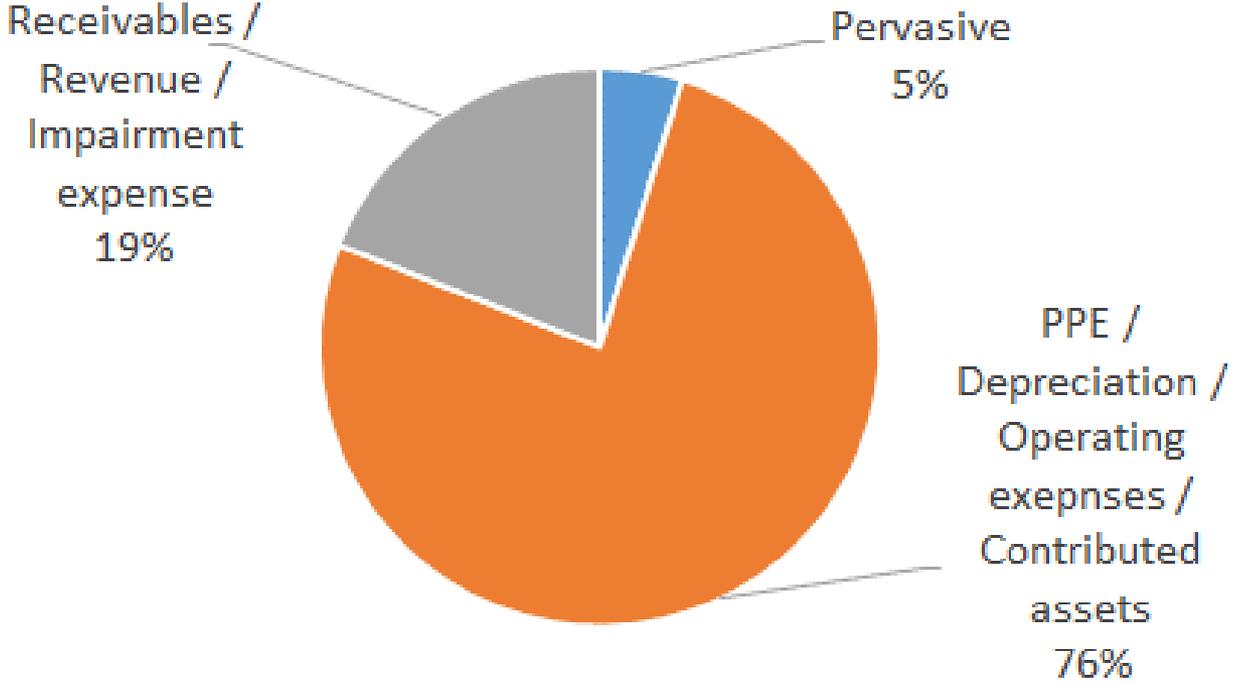
# Year end close process—councils

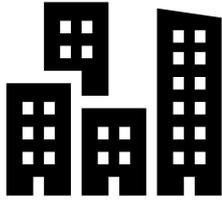
Five key milestones to assist in a smooth year end process are measured against dates agreed between council and the QAO.

See the factsheet on our website for details and some hints and tips on how to achieve the milestones.



### Errors by account balance





**70 per cent of KAMs relate to property plant and equipment**

## Areas for audit focus

- ✓ componentisation
- ✓ accuracy of unit rate source data
- ✓ adjustment for reductions in utility
- ✓ indexation (back test for reasonableness)
- ✓ useful life assessment
- ✓ Spreadsheet hygiene

# Q&A

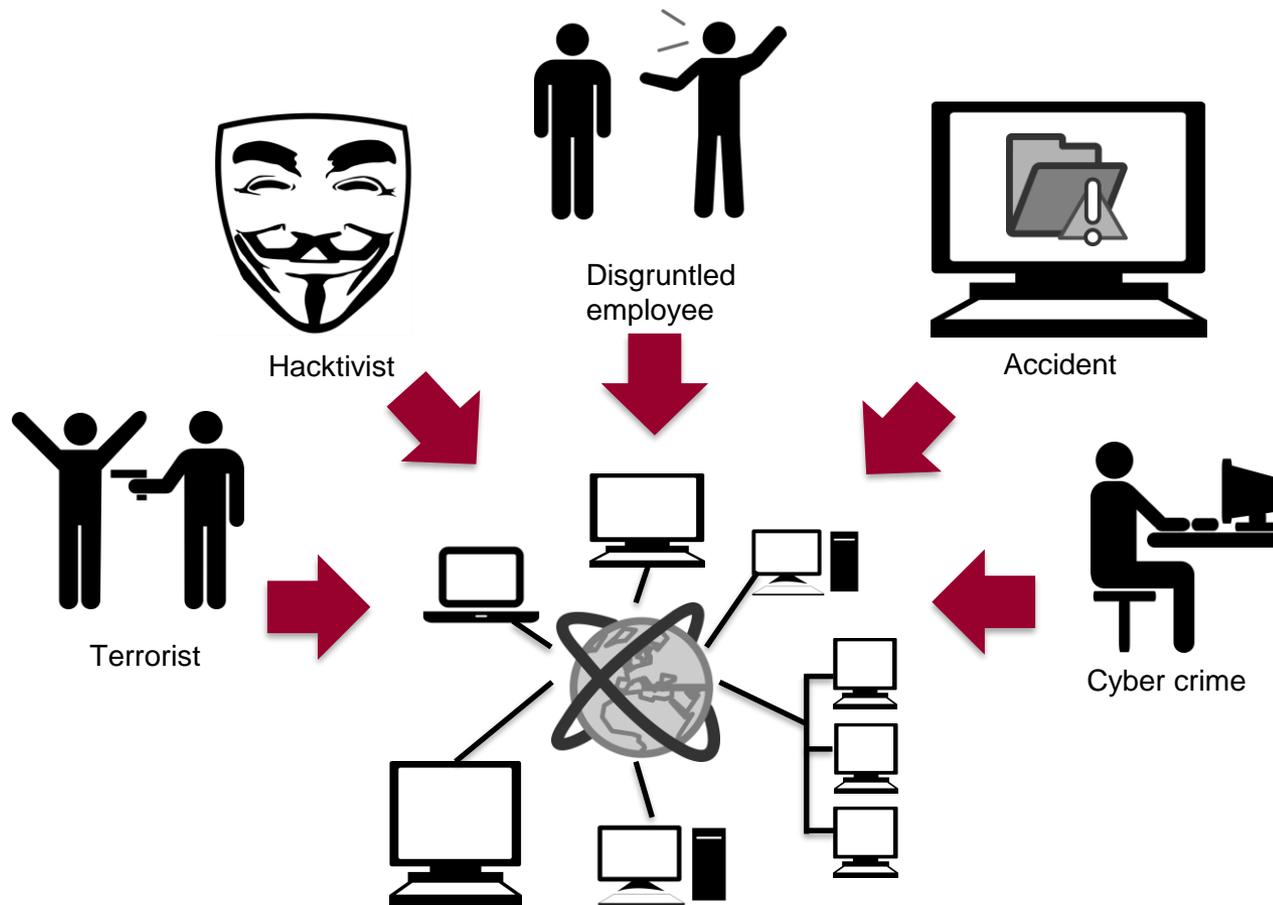
# IT security and cyber risk

Mayus Nath

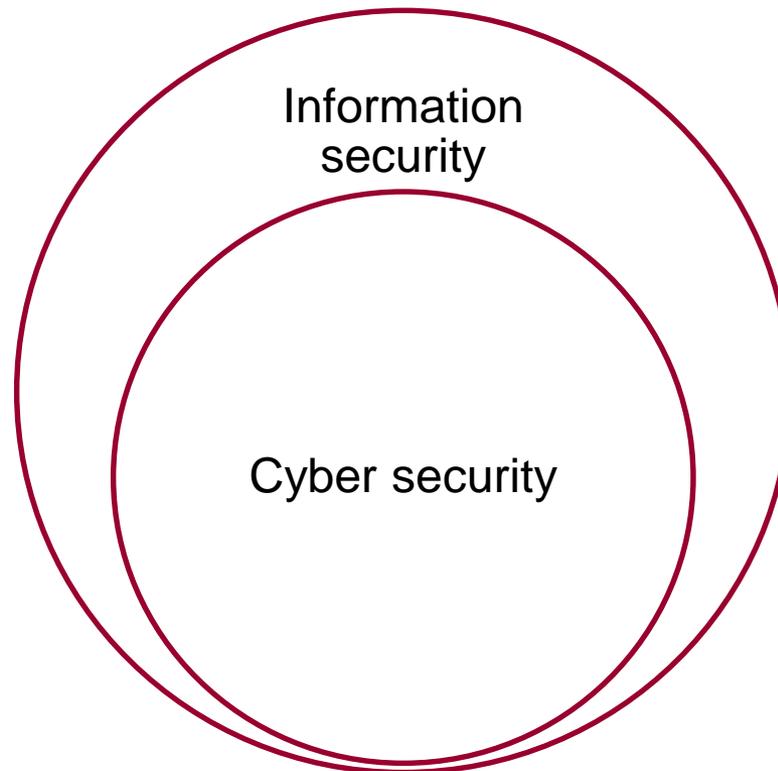
Director, Specialist Audit Services



## Reported attacks through information technology is on the rise



**Information security is for protecting data regardless of form and location and cyber security is related to the internet and electronic data**



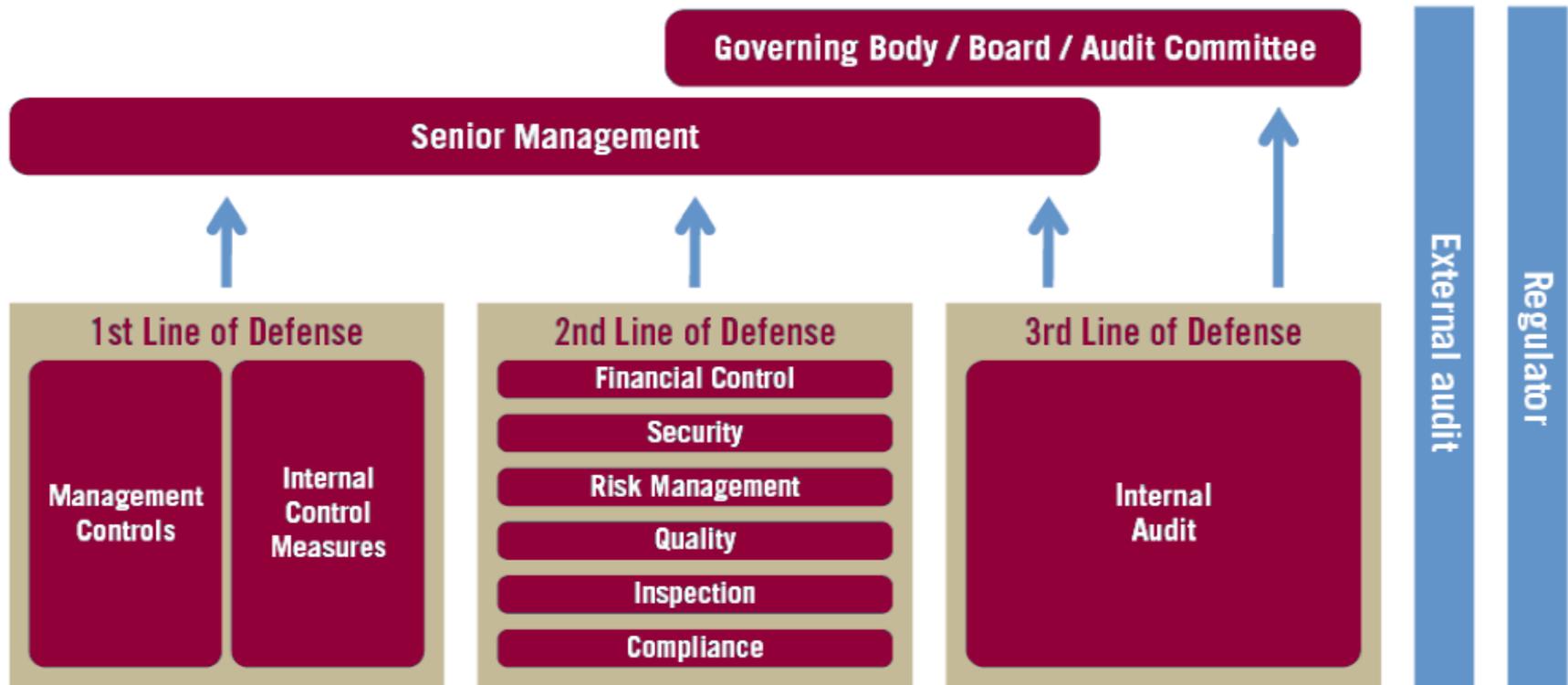
## There is a wide policy platform for information security across the Australian Government

- CERT Australia and Australian Signals Directorate advise on cybersecurity threats
- Queensland Government Chief Information Office sets policies and standards for securing information
- Each entity and person is responsible and accountable for information security

# Key questions for senior management



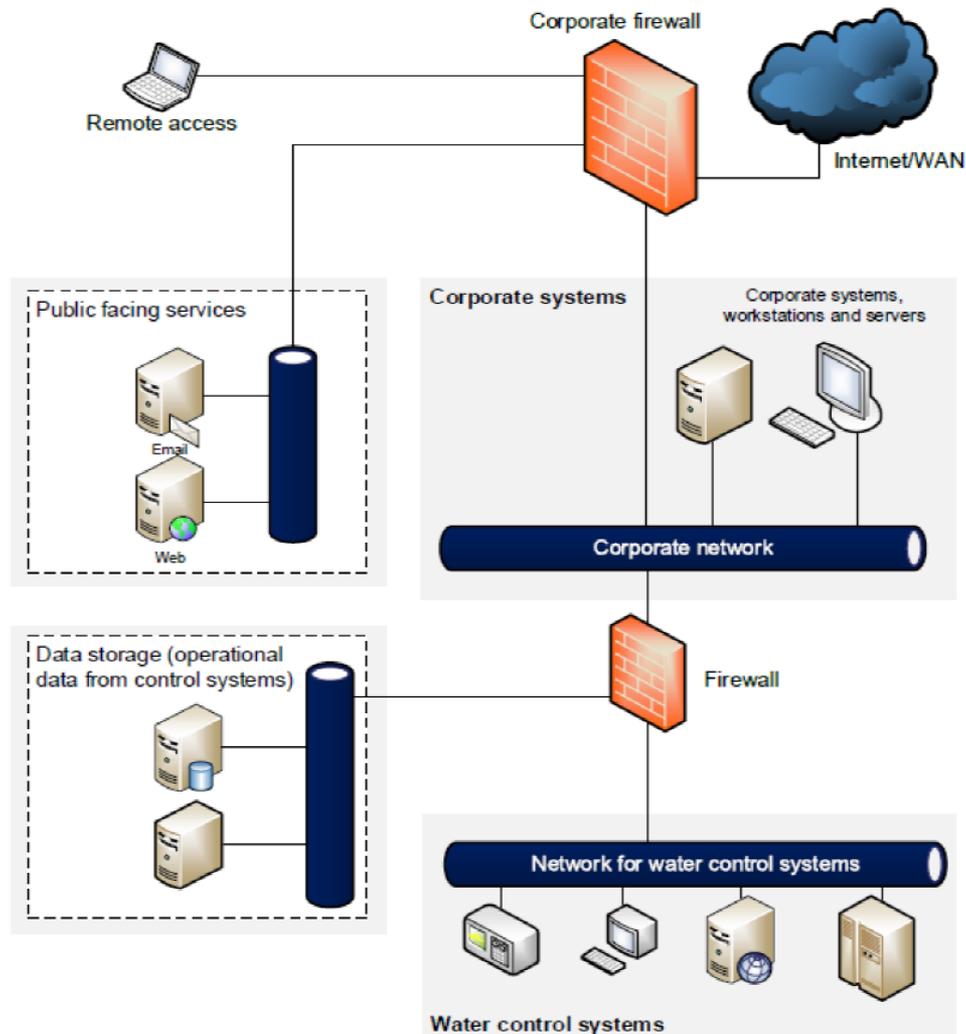
Figure 2C  
Three lines of defence model in risk management

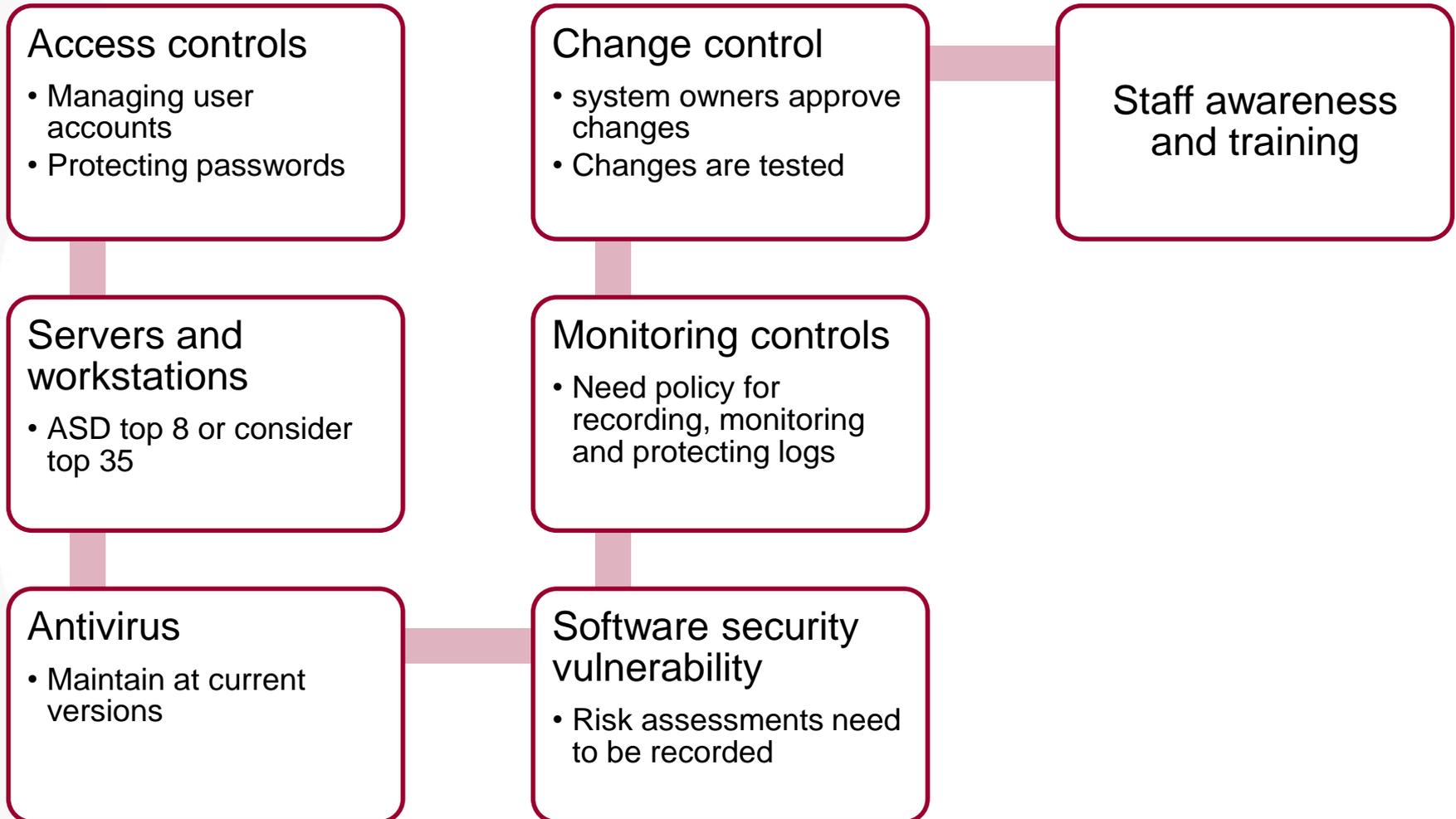


Adapted from ECIIA/FERMA *Guidance on the 8th EU Company Law Directive, article 41*

# Network segmentation

Figure 2D  
Example of network separation





## Entities must respond quickly and efficiently in the event of a security breach to minimise the amount of damage

- disaster recovery planning falls short
- do we have a list of all components of systems?
- what is critical to be recovered – costs versus benefits?
- have we quantified the risks?
- who is responsible for recovery?
- training

# Closing and Q&A

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