

Summary

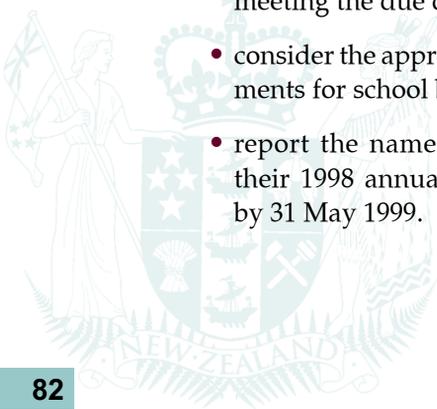
- 5.001 We have reported to the House three times on the accountability and audit of school boards of trustees (school boards) and the related issue of timeliness of reporting.¹
- 5.002 We commented favourably in our *Third Report for 1998* on the timeliness of reporting by school boards, and we do so again in this report. However, we are unable to report any significant improvement in meeting the requirements of the Public Finance Act 1989 for the issue of the audit reports within 30 days of receiving the financial statements.
- 5.003 The two different times for reporting – in the Education Act 1989 and the Public Finance Act – have different incentives associated with them. The consequences of failing to meet the Education Act deadline for school boards to forward their annual report to the Ministry of Education can be considerable. Boards and our auditors are also conscious that external accountability to the Minister of Education and parents – not solely the meeting of audit deadlines – is the essence of the reporting requirement.
- 5.004 Further, the requirement in the Public Finance Act does not take into account the realities of the school board audit or, indeed, of the audit process itself.
- 5.005 Therefore, in our opinion it would be more in keeping with the special circumstances that apply in the schools' sector, and with the accountability intentions, for the requirements of section 43 of the Public Finance Act in respect of school boards to be reviewed.

1 *First Report for 1997*, parliamentary paper B.29[97a], pages 93-105; *Third Report for 1997*, parliamentary paper B.29[97c], pages 81-87; and *Third Report for 1998*, parliamentary paper B.29[98c], pages 25-28.

- 5.006 Instead, and in order to focus on the outcome of timely reports to the stakeholders, it might be more appropriate to require a school board to:
- prepare its annual report, to include its *audited* financial statements, within five months of balance date;
 - make its annual report available to all parents and to the Ministry of Education within five months of balance date; and
 - in the case of parents, make the annual report available to them no less than 20 working days before the annual meeting.
- 5.007 There could be a consequential need to adjust the annual meeting requirements of the board.
- 5.008 We recommend a review of the two accountability requirements for reporting to Parliament on the schools' sector (see paragraph 5.018) to ensure that –
- the most recent financial information can be available; and
 - the appropriate administrative action can actually be carried out.

Purposes of This Article

- 5.009 The purposes of this article are to:
- describe the accountability requirements for school boards in the context of other accountability requirements;
 - describe the performance trends of school boards in meeting the due dates under those requirements;
 - consider the appropriateness of the accountability requirements for school boards; and
 - report the names of school boards that failed to send their 1998 annual report to the Secretary for Education by 31 May 1999.



The Accountability Requirements

Interests of Stakeholders

- 5.010 In most contexts, timely audited financial statements are recognised as an important element of accountability. For example, the board of every company is obliged to prepare an annual report² containing the audited financial statements³.
- 5.011 The focus of reporting by companies is on the accountability of the board of directors to the shareholders. The financial statements and any auditor’s report must be made available to every shareholder every year, before the annual meeting. The pre-eminent interest of a company’s shareholders is in the value of its shares. We would expect the audited financial statements to play an important role in a company’s accountability regime.
- 5.012 School boards have two principal stakeholders to whom they are accountable: the parent community and the Minister of Education. The accountability requirements for a school board in respect of these stakeholders are similar to those for the board of a company to its shareholders – but there are some important differences.
- 5.013 Audited financial statements also provide an important source of assurance to the school board’s two principal stakeholders. This is recognised in the Education Act, where the board is required to report as a Crown entity under the Public Finance Act.

2 Companies Act 1993, section 208 (1).

3 Ibid, section 211(1)(b) and (c). An auditor’s report on the financial statements is not required following a unanimous resolution by shareholders that no auditor be appointed for the year under section 196(2). Every listed company is required to have an auditor.

5.014 In our 1997 report we noted (in particular) the importance of the accountability of school boards to their local communities, and stated that:

In our opinion, audited financial statements should be available for the annual meeting. Otherwise the school community will not have the benefit of independent assurance that the contents of the financial statements are reliable.

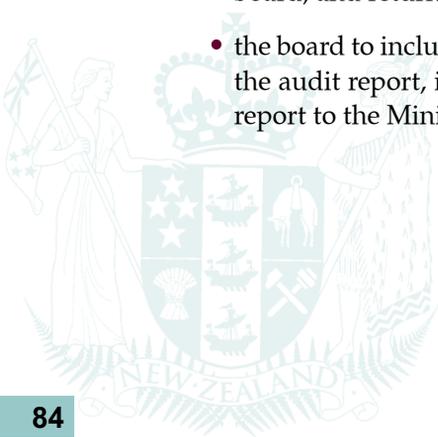
5.015 However, we would expect the school's stakeholders to have an overriding interest in the quality of educational outcomes. The accountability regime in the schools' sector gives greater emphasis to reporting – certainly in school reports to parents, for example – on educational achievement than on financial performance. We discuss the matter of reporting service performance in paragraphs 5.037-5.040.

5.016 The reporting and audit requirements of school boards are compared with those of government departments, other Crown entities, and companies in Figure 5.1 opposite.

Public Finance Act Requirements

5.017 The Public Finance Act requires:

- every school board (as a Crown entity) to prepare annual financial statements in the prescribed form and send them to the auditor within 90 days of the balance date of 31 December;
- the auditor to issue an audit report on the statements within 30 days of receiving the statements from the board, and return the statements to the board; and
- the board to include the audited statements, together with the audit report, in its annual report and send the annual report to the Minister of Education.



*Figure 5.1
Comparative Reporting and Audit Requirements*

Entity	Financial Statements To Auditor	Audit Report Issued	Annual Report To Stakeholders
Government department	Within 60 days of balance date.	Within 30 days of receipt of financial statements.	To Minister who must present it to the House within 6 sitting days of being returned by the auditor.
Crown entity	Within 90 days of balance date.	Within 30 days of receipt of financial statements.	To Minister who must present it to the House within 6 sitting days of being returned by the auditor.
School board	Within 90 days of balance date.	Within 30 days of receipt of financial statements.	To parents by 3rd Tuesday in May. To Ministry by 31 May. ⁴ Schools' sector report of Minister by 30 June. To electorate MP within 1 month of audit report being issued.
Company	Not specified.	Not specified, but with annual report (within 5 months of balance date).	Within 5 months of balance date. ⁵

⁴ The annual report may or may not include audited financial statements.

⁵ The annual report has to be distributed not less than 20 working days before the annual meeting, which must be held within 6 months of the balance date (Companies Act 1993, section 120).

5.018 The Minister in turn has two responsibilities under the Public Finance Act:

- to report to the House by 30 June each year on the performance of the schools' sector in the immediately preceding financial year;⁶ and
- to send to each member of Parliament a copy of the audited financial statements of schools in their electoral district⁷ within a month of the audit report being issued.

Education Act Requirements

5.019 The majority of schools' funding comes from money appropriated by Parliament. Therefore, the State also has a key interest in the schools achieving the administrative and educational objectives specified by the State. This is recognised by the Education Act requiring that:

- each school has a charter that is an undertaking by the school's board to the Minister with respect to the good management of the school and achievement of the objectives approved by the Minister;
- every school board has to report to parents at an annual meeting to be held between 31 March and the third Tuesday in May; and
- every school board must make its annual report available to the Minister of Education at a date specified under section 87 of the Act.

5.020 Reporting on the charter undertaking is an important aspect of the accountability arrangements for school boards. Therefore, the Minister can be expected to have a keen interest in the audited financial statements.

5.021 The Education Act requirement to have the annual report and financial statements available to the annual meeting compares with the Companies Act requirement. However, the important difference is that the Education Act stops short of making it mandatory for *audited* financial statements to be available at the annual meeting.

⁶ Public Finance Act 1989, section 44b.

⁷ Public Finance Act 1989, section 44c.

5.022 The Secretary for Education has fixed 31 May as the date by which the board's annual report (including the audited financial statements) is to be sent to the Ministry. This deadline is consistent with the five months from balance date within which the majority of companies have to prepare their annual report.

Trends in the Timeliness of Meeting Due Dates

5.023 Having reported on the timeliness of reporting by school boards over a five-year period, we are able to identify some particular trends in meeting the reporting and audit deadlines for:

- forwarding [by the board] of financial statements for audit;
- issuing [by the auditor] of the audit report; and
- reporting to the stakeholders.

5.024 The data behind these trends is set out in Tables 5.1 and 5.2 on pages 95-96.

Forwarding of Financial Statements for Audit

5.025 Financial statements are now being forwarded for audit on a more timely basis.

5.026 For 1994 our auditors reported that only 65% of boards sent their financial statements to them within 90 days of the end of the financial year, as required. By 1998 the figure had increased to 83%.

Quality of Financial Statements Forwarded for Audit

5.027 While there is apparently far less cause for concern over timeliness at this stage in the reporting process, it is a moot point whether improvement in the timeliness of forwarding financial statements is important in itself.

The quality of the financial statements received for audit is critical if the outcome of timely and reliable external reporting is the important concern. If the financial statements are of inadequate quality the audit report may be held up, and reporting to the stakeholders may be seriously delayed.

- 5.028 In this respect we note an increasing unwillingness on the part of our auditors to accept clearly substandard financial statements. There may be a case for increased advisory support from the Ministry of Education if school boards are to raise the quality of the financial statements to the level where they are acceptable when first submitted.
- 5.029 We acknowledge that the Ministry has recently increased the number of financial advisers from three to six, and note the Ministry's objective to make on-site visits to schools whose financial statements indicate areas of concern.⁸ We will be interested in the effects of this increased support.

Issuing of Audit Reports

- 5.030 There has been only slight improvement in the timeliness of the issuing of audit reports. We have drawn attention previously to this area as being of most concern.
- 5.031 Only about 30% of audit reports were issued within the statutory deadline each year over the period 1994-1997. For 1998, the proportion of audit reports that were issued within 30 days of the statutory deadline for receipt of the financial statements showed only a slight improvement, at 32%. The reasons for this are discussed later in paragraphs 5.049-5.053.

⁸ Ministry of Education, *Forecast Report 1999-2000*, parliamentary paper E.1FR(99), page 38.

Forwarding the Annual Report to the Ministry

- 5.032 School boards are improving their compliance with the deadline for sending their annual report to the Ministry of Education. In 1994 only 63% of boards had audited financial statements by 31 May – the deadline for sending their annual report to the Ministry. By 1997 the figure was 87%, and for 1998 it was 89%.
- 5.033 In our view, strong incentives have supported this steady improvement in meeting the reporting requirement. Failure to comply with this particular deadline may, and sometimes does, result in the Ministry withholding the next quarterly payment of the operations grant.
- 5.034 A board that breaches the 31 May deadline is also at risk of being named in a report such as this. These consequences therefore represent a greater risk than not meeting the 30-day deadline for the audit report to be issued, from which no such consequences result.

Making the Annual Report Available to Parents

- 5.035 We are aware that the requirement to have audited financial statements available to the annual meeting (which must be held between 31 March and the third Tuesday in May) is important to some school boards. However, this is not the general case. While we do not have specific data, we know that:
- boards usually regard the annual meeting as –
 - a formality;
 - poorly attended; and
 - not an effective mechanism for communicating with parents;⁹
 - the Education Act allows boards to present unaudited financial statements to the annual meeting¹⁰; and

9 See also Wylie, C *The Impact of Tomorrow's Schools in Primary Schools and Intermediates 1990 Survey*, NZCER Wellington 1991, page 62. Over a quarter of schools had no parents at their annual meeting. The usual meeting attracted 1-20 parents. Later surveys of the impact of the reforms did not retain the question relating to annual meetings, as they were so poorly attended.

10 Education Act 1989, section 100(2)(b).

- there is no equivalent to the Companies Act requirement that all shareholders have a copy of the annual report and the audited financial statements not less than 20 days before the annual meeting.

5.036 Given the importance of accountability to parents, in our view the current requirement needs to be reviewed to better achieve the intent that parents be fully informed in a timely way of the state of the school. We believe that the requirements should be such as to ensure that:

- the audited financial statements are available to every parent within no less time than would be expected by the Minister or, for instance, the shareholders of any listed company;
- parents receive at the same time an appropriate statement about the school's performance in delivering education (its service performance – see paragraphs 5.037-5.040); and
- the statements are received with ample time to consider them before the annual meeting, since that is the appropriate opportunity for the board to answer to its parent community for its performance.

Reporting Service Performance

5.037 In our *First Report for 1997*, we drew to Parliament's attention the importance of reporting service performance and the adverse effects of exempting boards from the requirement to so report.

5.038 The Minister of Finance can exempt school boards from having to prepare any of the required financial statements that *would be unduly onerous on the Board*.¹¹ A result of this has been the exemption for several years of school boards from preparing a Statement of Service Performance (SSP). As a consequence a school board's financial statements may have no SSP or, if they do, the SSP may be of poor quality. If an SSP is presented it will not be audited.

¹¹ Public Finance Act 1989, section 41A(2)(b).

5.039 Parents have to depend for information about the educational performance of the school on the less frequent reviews by the Education Review Office. In our 1997 report we observed that:

It could be argued that, of all the financial statements prepared by a board, the SSP is the most important.

5.040 The issue of reporting service performance remains unresolved, despite some attention having been given to it by a Ministerial inquiry.¹² We intend to raise this matter again in a subsequent report.

Appropriateness and Feasibility of the Statutory Auditing Requirements

Time-related Requirements

- 5.041 The time within which a company's auditor must complete the audit is dictated solely by the requirement placed on the board to make its audited financial statements available in the annual report within five months of the balance date. The situation is quite different in respect of the audit of schools and other Crown entities. (See Figure 5.1 on page 85.)
- 5.042 Section 43 of the Public Finance Act requires the auditor of a Crown entity (including a school board) to issue the audit report within 30 days of receiving the annual financial statements. These must be forwarded to the auditor within 90 days of the end of the financial year.
- 5.043 Thus, company audit requirements are focused on the final outcome – the timely availability of the annual report and audited financial statements – while Crown entity audit requirements are aimed as much at each step in the process toward that outcome.

¹² *Review of the Education External Evaluation System*, Wellington, 1997.

- 5.044 In our view, the Public Finance Act's auditing requirements could be improved to focus on the outcome of a timely report to key stakeholders and to be more practical.

Accountability to Parliament

- 5.045 We believe that consideration needs to be given to the reasonableness of two other accountability requirements.
- 5.046 The Minister's annual schools' sector report is required to contain information for the immediately preceding financial year ended on 31 December.¹³ However, the 1998 report was published in June 1999, and contained financial information for the 1997 financial year – not *the immediately preceding financial year* – and non-financial data relating to 1998.
- 5.047 We also observe that audited financial statements are not always getting to members of Parliament within the time prescribed by the Public Finance Act. Not unexpectedly, the Ministry forwards the school board's annual report to the member of Parliament within a month of receiving it – not within a month of the issuing of the audit report (since it is not required to be forwarded to the Ministry at that point). Consideration needs to be given to whether this accountability requirement is realistic.

A Case for Different Treatment

- 5.048 The Public Finance Act (as noted in paragraph 5.038) acknowledges that school boards warrant different consideration from other Crown entities as far as reporting is concerned. We also note the following differences in audits between school boards and other classes of entity:
- two different times for reporting exist – one in the Public Finance Act and one under the Education Act – which tend to be counteractive (see paragraphs 5.017 and 5.022);
 - there is a considerably greater volume of school board audits (approximately 2,700) than for any other class of Crown entity; and

¹³ Public Finance Act 1989, section 44b.

- the quality of financial statements submitted by school boards for audit is not as consistently good as those submitted by other Crown entities.
- 5.049 The workload of school board audits falls on a small number of auditors (often domiciled outside the large centres). Most of the auditors handle between 10 and 60 school board audits in a year. One firm audits 200 boards, and several audit over 100 boards. Thus, it may be difficult for our auditors to achieve a turn-around on all of the audits in the 30 days required by the Public Finance Act.
- 5.050 Financial statements all tending to arrive at the same time exacerbates the effect of the high volume of audits. For the 1998 year (see Table 5.2 on page 96):
- only 23.7% of school financial statements were received by our auditors by early March 1999; and
 - nearly 60% of school financial statements were received in March 1999 – over a quarter in the last week, including the 14.8% that were received on the very last day of March.
- 5.051 The standard of the school board financial statements that are initially forwarded to our auditors is often of poorer quality than those of other Crown entities. The people preparing the statements, especially for the smaller school boards, may be relatively unskilled. Some financial statements forwarded to our auditors are of “first draft” standard.
- 5.052 The auditor may have to engage in a major reconstruction exercise on the material presented, involving numerous queries and consultations with the relevant staff or accounting services provider. Should on-site work be required in such circumstances, the schools – unlike other Crown entities – are often distant from the auditor.
- 5.053 The availability of staff and school board members in the period when the audit is meant (according to the Public Finance Act) to take place is considerably affected by the nature of the education business – schools go on holiday while the audit is in progress. This is not the case with other Crown entities. While other timeliness requirements in March and May have improved in spite of this, the audit process is more vulnerable.

5.054 For all of the reasons already outlined, and in keeping with the special circumstances that apply in the schools' sector, we believe variations to the accountability and (particularly) audit requirements are appropriate.

5.055 Instead of the current requirements, the accountability and audit requirements for school boards should:

- focus on the outcome of timely reports to the stakeholders – in particular parents and the Minister as the two principal stakeholders – rather than on the steps in the process towards that outcome;
- require the board to prepare its annual report – to include its audited financial statements – within five months of balance date;
- require the board to make its annual report¹⁴ available to all parents within five months of balance date (that is, by 31 May), but in any case at least 20 working days before the annual meeting; and
- require the board to make its annual report available to the Ministry within five months of balance date (that is, by 31 May).

5.056 The present deadline for forwarding the annual report to the Ministry by 31 May would not change. Some concerns have been expressed to us that removal of the requirement for school boards to forward the financial statements to the auditor within 90 days of balance date is unnecessary and risky, given the already good timeliness of boards. We have some sympathy for this view.

5.057 However, the suggested change would shift the emphasis from an inappropriate focus on the audit process to an accountability outcome. There could be a consequential need to adjust the annual meeting requirements of the board (see paragraph 5.019).

¹⁴ The Companies Act 1993 allows the shareholder to waive the right to receive the annual report, but the shareholder *must be sent* the audited financial statements.

- 5.058 We believe it is no more risky to shift the focus to the accountability outcome – the external reporting deadline (currently 31 May) – which already has the added advantage of being subject to strong incentives (see paragraph 5.033).
- 5.059 Our proposals have the added benefit of all parents – not only those attending the annual meeting – being properly informed.

Naming Of Boards That Failed To Meet the Statutory Reporting Requirement – 1999

- 5.060 We have twice – for the 1995 and 1997 financial years – named those school boards that had failed to meet the statutory reporting deadline of 31 May fixed by the Secretary for Education.
- 5.061 This year we have chosen again to name the boards for which the audit report was signed after 31 May 1999 and where the delay in reporting cannot be attributed, in part or in whole, to the auditor. The boards are listed in Table 5.3 on pages 97-98.

*Table 5.1
Compliance with Reporting Deadlines 1994-1998*

Financial Year	Financial Statements To Auditor %	Audit Report Issued %	Annual Report to the Ministry %
(to 31 December)	(+90 days)	(+30 days)	(by 31 May)
1994	65	30	63
1995	61	25	70
1996	69	28	78
1997	79	30	87
1998	83	32	89

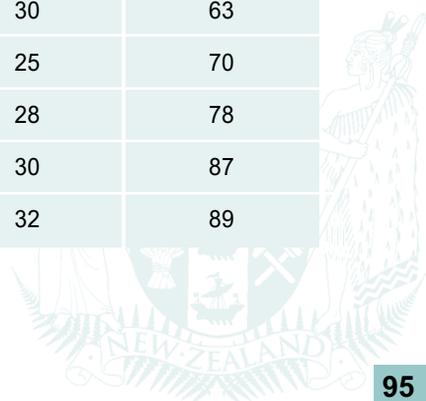


Table 5.2
Distribution of Auditor Receipt of Financial Statements for the Year Ended 31 December 1998

Week Ended	Number of Financial Statements Received		% of Financial Statements Received	
	For the Period	Cumulative	For the Period	Cumulative
to 6 Jan 1999	8	8	0.3	0.3
13 Jan 1999	1	9	<0.1	0.3
20 Jan 1999	4	13	0.2	0.5
27 Jan 1999	14	27	0.5	1.0
3 Feb 1999	36	63	1.4	2.4
10 Feb 1999	75	138	2.8	5.2
17 Feb 1999	117	255	4.4	9.6
24 Feb 1999	177	432	6.6	16.2
3 Mar 1999	203	635	7.6	23.8
10 Mar 1999	247	882	9.2	33.0
17 Mar 1999	274	1,156	10.3	43.3
24 Mar 1999	322	1,478	12.1	55.4
31 Mar 1999	727	2,205	27.2	82.6
from 1 April	464	2,669	17.4	100.0

*Table 5.3
School Boards that Failed to Send Their 1998 Annual Report to the Secretary for Education by 31 May 1999*

Aranga	Paerata
Avalon Intermediate	Pakaraka
Avalon	Parkway
Bideford	Patutahi
Cannington	Penrose High
Cobham	Piopio
Collingwood Intermediate	Pongakawa
Dannevirke High	Pukekohe Intermediate
Evans Bay Intermediate	Pukeoware
Greytown	Punaruksu
Hataitai	Puriri
Hinuera	Rangitahi College
Huntermore Consolidated	Raphael House Rudolf Steiner
Kotuku Rudolf Steiner	Raumanga Intermediate
Kuranui College	Rawene
Linden	Reporoa College
Mahana	Rewa Rewa
Masterton East	Riverdale (Gisborne)
Maungati	Riverview
Minginui Forest	Russell (Porirua)
North Taieri	Saint Bernard's (Brooklyn)
Omihi	Saint Joseph's (Dargaville)
Opoho	Saint Joseph's (Paeroa)
Opua	Saint Mary's (Blenheim)
Orauta	Saint Patrick's (Wainuiomata)
Oruawhoro	Saint Stephen's (Bombay)
Otangarei	Sara Cohen
Oxford Crescent	South End
Paekakariki	South Wellington Intermediate
Paengaroa	Taipuha



Tairangi	Te Kura Kaupapa Maori o Whakawatea
Tangiteroria	Te Kura Kaupapa o Nga Mokopuna
Taupo Intermediate	Te Kura o Rangiriri
Tawa College	Te Kura Reo Rua o Matawaia
Te Aro	Te Puia Springs
Te Horo (Whangarei)	Te Wharekura o Rakaumangamanga
Te Kopuru	Tikitiki
Te Kura Kaupapa Maori o Hoani Waititi Marae	Tirohia
Te Kura Kaupapa Maori o Mangere	Waikirikiri Bilingual
Te Kura Kaupapa Maori o Piripono Te Kura Whakahou (Otago)	Waiohau
Te Kura Kaupapa Maori o Te Raki Paewhenua	Waitara Central
Te Kura Kaupapa Maori o Waipiro	Waitotara
Te Kura Kaupapa Maori o Whakarewa Te Reo	Wakanui
	Whakatane High
	Wharekahika

