ACT AUDITOR–GENERAL'S REPORT

ACT GOVERNMENT SUPPORT TO THE UNIVERSITY OF CANBERRA FOR AFFORDABLE STUDENT ACCOMMODATION

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ACT Audit Office

AUDITOR-GENERAL AN OFFICER OF THE ACT LEGISLATIVE ASSEMBLY

PA 14/08

The Speaker
ACT Legislative Assembly
Civic Square, London Circuit
CANBERRA ACT 2601

Dear Madam Speaker

I am pleased to forward to you a Performance Audit Report titled 'ACT Government support to the University of Canberra for affordable student accommodation' for tabling in the Legislative Assembly pursuant to Subsection 17(5) of the *Auditor-General Act 1996*.

Yours sincerely

M. Cooper.

Dr Maxine Cooper
Auditor-General
12 June 2015

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SUMMARY

Between June 2011 and May 2013, the ACT Government provided the University of Canberra (UC) with financial and other support, including loans and credit facilities, a cash grant and a gift of property, for the purpose of providing affordable accommodation to students. The ACT Government has provided:

- a gift of property valued at $9.0 million;
- a cash grant of $6.0 million; and
- loan and credit facilities up to $97.4 million.

The Treasurer has also agreed to allow the UC to borrow up to $144 million in funds (from both the Territory and non-government lenders).

The ACT Government's support was primarily provided for the purpose of providing affordable accommodation to students under the auspices of the National Rental Affordability Scheme. Up to 1,000 new dwellings were to be provided as affordable accommodation for to up to 1,580 students under this scheme.

The UC advised that the National Rental Affordability Scheme provided a 'huge opportunity', including 'bringing modern student accommodation into the University's stock, suitable for today's student needs and expectations, and then receiving a Commonwealth rebate for 10 years, thus reducing the overall cost of accommodation significantly'.

In this respect, the UC further advised that its capital investment, including investment in student accommodation, was an important part of an overall growth strategy and asset renewal strategy, much of which was financed from borrowings. The UC also advised that it acknowledged that the overall growth and asset renewal strategy has resulted in its level of debt increasing (and that there are increased financial risks associated with this) and advises that these have been, and will continue to be, managed through its governance and oversight arrangements.

The UC also advised that in 2007 the University was in a dire financial position and its infrastructure had been neglected for many years. The UC advised that 'in the space of 8 years, UC has moved into surplus, grown significantly, entered world-rankings and, importantly, significantly reduced the risk of the ACT Government having to step in to rescue it; which was very much in prospect in 2007.'

Conclusion

ACT Government administrative and decision-making processes associated with the provision of financial and other support to the University of Canberra (UC) have been implemented effectively. Importantly, ACT Government agencies involved provided Cabinet with frank advice which sometimes differed. The Treasury Directorate's due diligence activities and advice has been effective in guiding the management of risks to the Territory.

The UC sought significantly more support than that which was subsequently agreed to by the ACT Government. The UC sought the Treasurer's approval to borrow up to $220.0 million, which included a $150.0 million loan from the Territory that would be subordinated to other lenders. The ACT Government only agreed to a borrowing limit of $144.0 million and non-subordinated ACT Government loans up to $97.4 million. The ACT Government gifted Arscott House, an off-campus student accommodation property, to the UC as a contribution towards the UC's participation in the NRAS. Under the NRAS, the UC was to receive support from the Australian Government and ACT Government to supply 1,000 new dwellings. While 605 of its planned 648 dwellings have been completed, the remaining 352 dwellings (35 percent) are at risk of not being completed by July 2016. The UC advised it has been considering a number of options for meeting the target but it has not been satisfied with any proposed commercial arrangements.

If the target of 1,000 dwellings is not achieved it would be appropriate for the Chief Minister, Treasury and Economic Development Directorate to re-assess the support that it has provided to the UC for the purpose of participating in the NRAS. Such a re-assessment would also be prudent on the basis that other components of the ACT Government's support to the UC, including the concessional interest rate benefits on loans to the UC, may not have materialised as expected.

The ACT Government lease associated with Arscott House states that it is to be used 'only for the purpose of educational establishment'. Arscott House is currently not being used for student accommodation or any other purpose. The UC has not made a decision on its future use. If changes to the use require a change in lease that results in the property value exceeding that provided by the ACT Government in support of NRAS ($9.0 million) an appropriate adjustment may need to be made.

The UC has repaid most of its debt to the ACT Government using funds from the sale of its future NRAS entitlements to Westpac. It now only has one loan with the ACT Government, the outstanding balance of which was $31.4 million as at 31 December 2014. The arrangement with Westpac has given rise to an ongoing financial liability for the UC and an obligation to Westpac for ensuring that NRAS dwellings are effectively managed so that Westpac receives NRAS payments from the Australian Government. While future NRAS payments from the Australian Government were always contingent on the UC's effective management of its NRAS-eligible properties, there is now a commercial remedy available to Westpac should it not do so.

In the last six years, particularly since 2010, the UC has significantly increased its debt to ACT Government and non-Government lenders. The UC advised that this is primarily due to its investment in accommodation for students and an overall growth and asset renewal strategy, which it regards as essential for its future growth and continued viability. Given this additional debt, the UC's capacity to sustain unexpected future financial shocks is at risk.

Modelling undertaken by the UC indicates that it has the capacity to repay its debts to the ACT Government. This is based on its ability to generate operating surpluses, primarily through revenue from the growth of students. Not achieving growth targets for student enrolments, or experiencing a reduction in growth, presents a financial risk to the UC. The UC nevertheless advised that, should student growth targets not be achieved, it has a range of options open to it to ensure that its debt is repaid.

Key findings

ACT GOVERNMENT ADMINISTRATIVE AND DECISION-MAKING PROCESSES	Paragraph
An analysis of the UC's borrowing limits and loan and credit facility approvals shows: • the Treasurer, through a combination of Treasury Authorisations (and Instruments) and Disallowable Instruments, has approved a number of different loans and credit facilities for the UC, both from the Territory and other parties, between June 2011 and June 2013; and • the total maximum borrowing limit of the UC has increased from $0 prior to August 2008 to $144.0 million since May 2013. This is a significant increase in the amount of funds that the UC may borrow. ($74.0 million of this related to specific loans for the provision of student accommodation and, once repaid, is no longer available to the UC. Accordingly, $70.0 million remains available on an ongoing basis to the UC.)	2.5
ACT Government decisions in relation to the provision of financial and other support to the UC for the purpose of providing student accommodation developed in response to a series of requests by the UC. Requests from the UC were initially in the form of general representations to Ministers, primarily for the purpose of supporting the UC's growth strategy.	2.11
Requests by the UC for financial and other support specifically for student accommodation were subsequently developed through discussion between the UC and the Economic Development Directorate and presented to Cabinet for consideration. As part of the Cabinet process, the Treasury Directorate provided advice, including on its due diligence analysis of the funding proposals.	2.13
In relation to the UC's requests for loan and credit facilities and increases to its borrowing limits, the ACT Government was primarily required to consider the UC's financial capacity to repay its loans. It did so through due diligence analysis.	2.17
As part of its due diligence analysis, in addition to considering the total amount of debt that the UC could appropriately borrow and repay, the Treasury Directorate documented two additional considerations, as follows: • potential increases in the UC's borrowing limits being interpreted by the broader lending market as an indication that the ACT Government might underwrite debts of that amount should the UC face difficulties in meeting repayments; and • the total amount of senior ranked debt that the UC could manage as a stand-alone entity, i.e. the debt that the UC could manage without putting the ACT Government at financial risk of having repayment of its loans subordinated to the repayment of other lenders' loans. This is a key risk to manage as lenders to Australian universities recognise that government funding underpins the operations of the sector. While	2.20

loan subordination is an option a government might chose to take, it increases cash flow risks and can negatively impact on a jurisdiction's own credit rating.

On 14 December 2011, Cabinet agreed to the direct sale of Arscott House to the UC for $0 (essentially a gift). As part of its decision, Cabinet noted 'the transfer represents an estimated $9 million of the required $22.85 million in support from the ACT Government which is required under NRAS' and 'the transfer will assist UC to develop additional student accommodation places because it will be recognised as an asset that the University of Canberra can use to secure finance against.' 2.30

The transfer of Arscott House in December 2011 was important to the UC, notwithstanding that there were no specific time pressures for the purposes of the NRAS, including not before the end of December 2011. 2.34

The UC has since advised that the transfer of Arscott House provided the security of a renewed lease before any capital investment was made in the facility. 2.36

The UC reports its financial statements on a calendar year basis. In accordance with relevant accounting standards, the transfer of Arscott House in December 2011 allowed the UC to report an amount of $9.0 million as revenue. In 2011, the UC made an operating surplus before tax of $10.1 million. 2.37

At present Arscott House is not available for student accommodation. The UC advised that it closed in 2015 while options for its future use were being considered. The UC also advised that a decision on capital expenditure to upgrade Arscott House is pending and negotiations are underway with one of the UC's student accommodation providers, with a view to the accommodation provider taking responsibility for the premises. 2.38

On 11 February 2011, the Vice-Chancellor of the UC wrote to the Treasurer requesting an increase in the UC's total borrowing limit to $80.0 million. At the time of the request, the UC could only borrow up to $20.0 million. The UC was seeking funding to support its 'wide-ranging reform and revitalisation program', which required large capital investments to expand campus facilities, address a backlog of maintenance and 'fund strategic infrastructure projects which will promote the University's long-term sustainability through appropriate use of its extensive campus.' 2.39

On 9 March 2012 the Vice Chancellor of the UC wrote to the Chief Minister requesting an increase in the UC's total borrowing limit to $220.0 million, including a loan of $150.0 million from the Territory. The UC requested that the loan from the Territory be subordinated to loans from other non-Government lenders, i.e. the other non-government lenders would have the first opportunity to reclaim any payments from the UC. The UC requested the funding to 'assist the University manage and fund its structural reforms and infrastructure projects' including its student accommodation projects. 2.61

The Treasury Directorate advised the Treasurer on 12 April 2012 that the UC's proposal raised 'matters of concern'. The Treasury Directorate reiterated its earlier advice in relation to establishing a borrowing limit and how that might 'imply a form of indirect guarantee on the borrowing by the ACT Government to the UC' and that 'in the event of a loan default by UC, creditors may seek compensation from the Territory if other avenues of compensation have been exhausted.' 2.68

The Treasury Directorate considered 'the request to increase the borrowing limit to $220 million to be very significant due to the potential financial consequences.' In this respect, the Treasury Directorate identified 'the Territory's cash position is under pressure' and that 'based on the current budget position, new loans provided to UC will need to be funded by new external general government borrowings.' 2.70

In relation to the proposed subordination of the Territory loan to other loans with non-government providers, the Treasury Directorate identified the risks of such an arrangement, noting 'this means ACT Government provided loans would rank below claims of other lenders in the event of a call in of UC assets' and that 'as a lender, it is imperative that the Territory understands the risks associated with the investment and fully provides for these risks in the terms and conditions of any loan agreement.' 2.71

The Treasury Directorate recommended that 'UC obtain a formal credit rating from a suitably, qualified, independent organisation such as Standard & Poors (S&P)'. 2.74

On 7 June 2012, a Cabinet submission was lodged by the Economic Development Directorate recommending *inter alia*: 2.78

- authorising the UC to borrow up to $220.0 million, being the aggregate of $150.0 million in loans from the Territory and $70.0 million in loans from parties other than the Territory;
- extending a line of credit to the UC up to $150.0 million to fund the development of student accommodation on the UC Bruce campus, at a rate 0.75 percent above the costs of finance to the Territory; and
- subordinating the UC's debt to the Territory to non-Government lenders.

The Cabinet submission identified that the additional funding would support the UC's growth strategy and plans to grow the number of students at the UC. The Cabinet submission also identified that the subordination of the Territory's debt to non-Government lenders would assist in giving the UC's balance sheet flexibility and in ensuring that its access to funding markets for strategic requirements was preserved. The Cabinet submission identified that, should the Territory be unwilling to agree to such an arrangement, a potential alternative arrangement was to provide for the full $220.0 million loan amount to be provided by the Territory. 2.79

On 4 June 2012, the Treasury Directorate sought external technical advice with 2.82

respect to a 'high level assessment of the University of Canberra's (UC) Credit Worthiness as a stand-alone institution'. The Treasury Directorate sought advice on 'whether, and to what extent UC would be able to borrow in its own right', with specific advice sought in relation to:

- the credit worthiness of the UC as a stand-alone institution, noting that 'if UC supplied the contained proposal to a bank, seeking funding on commercial terms, what would be the likelihood of UC being granted credit approval'; and
- 'would UC's credit proposal be sufficient (in content) to seek a loan as a stand-alone entity on commercial terms'.

The advice expressed doubt that the UC would be able to borrow the funds it was requesting in its own right from non-government lenders. 2.84

However, the independent advice also identified that there may be circumstances in which banks may give the UC's application favourable treatment, including: 2.86

- placing covenant restrictions on the use of the loan facilities, which 'would strictly restrict the terms and conditions under which the UC may draw on the facility, therefore placing the facility outside of ratio analysis';
- diversifying non-income generating assets so as to either 'pre-commit to pay down senior debt via asset sale' or 'generate additional revenue sources from new rental/leaseback opportunities'; or
- by treating the application as government risk.

The due diligence process that the Treasury Directorate undertook for the March 2012 request from the UC reflected a significantly increased level of risk to the UC and the ACT Government, inherent in a request for $220.0 million in total borrowings, of which $150.0 million would be subordinated Territory lending. The Treasury Directorate identified the potential impacts on the UC and also on the Territory's cash position, budget balance and credit rating. The Treasury Directorate's strategy of using external expert advice was appropriate, and its recommendations were consistent with this advice. The Treasury Directorate's advice reduced the exposure of the ACT Government to significant financial risk. 2.88

In a decision on 12 June 2012, Cabinet did not agree to the proposed increase in the UC's credit limit (to $220.0 million) or increase in the Territory's lending (to $150.0 million). The Cabinet decision aligned with the advice provided by the Treasury Directorate. 2.89

In May 2013 an external consulting firm (KPMG) was commissioned by the Treasury Directorate to 'assist with an analysis of the CW4 project [construction and operation of the Cameron Wing 4] and the resultant impact it will have on UC's financial position, particularly with respect to debt servicing.' The consulting firm's advice noted: 2.102

- on a "stand-alone" basis (defined as without implicit or explicit government support), the 'UC has limited capacity beyond the CW4

and Sporting Commons projects to undertake additional debt funded capital projects until key financial metrics return to at least an "intermediate" level based on S&P benchmarks';

- 'as the UC is entering into a period of significant financial risk, UC has diminished capacity to sustain shocks and maintain adequate liquidity levels. Failure to achieve projected student growth will exacerbate this financial risk'; and
- the UC has some financial flexibility through the ability to 'delay discretionary capital expenditure projects' and 'monetise their investment in student accommodation.'

In a subsequent briefing to the Treasurer dated 31 May 2013, in relation to the external consulting firm's advice, the Chief Minister and Treasury Directorate advised 'we note that the UC is going through a significant growth phase and based on the student accommodation business cases and funding commitments, this phase necessitates an increase in debt levels to achieve the growth. An increased level of financial risk is an unavoidable consequence.' 2.103

A due diligence process for the proposed loan of $24.0 million for Cameron Wing 4 was undertaken. As in the case of previous due diligence analysis, it was appropriate and provided a sound foundation for the advice provided to the Treasurer. 2.105

ASSESSMENT OF PERFORMANCE

Paragraph

An analysis of the UC's performance in supplying student accommodation shows the UC's accommodation supply targets, as provided for in the UC's *Accommodation Strategy 2011-15* (February 2011), have not been met. For example, in 2015 2,230 beds are available, which is 882 beds (28.3 percent) fewer than the target of 3,112. The closure of Arscott House for student accommodation in 2015 has reduced the UC's ability to achieve its targets. The UC advised that this closure is temporary. 3.4

The UC's target for the development of 1,000 NRAS dwellings has not been met. The UC has forfeited 43 of its 648 'Phase 1' NRAS allocations and achievement of the remaining 352 'Phase 2' NRAS allocations is at risk. This may result in the UC only delivering 60 percent of its NRAS dwelling targets by 2016. While this is the case, the UC advised that this reflects prudent decision-making on its part. The UC advised that a number of options for meeting this target had been considered, but it has not been satisfied with any commercial arrangements proposed. 3.10

An analysis of the UC's NRAS eligible student accommodation shows: 3.17

- the UC's 605 NRAS eligible dwellings are a mix of studio rooms and apartments, with anywhere between one to seven beds in the dwellings; and
- the UC's 605 dwellings include 896 beds. However, up to 926 individuals may be accommodated in these rooms, as 30 of the rooms are double rooms, and may support up to two people.

An analysis of the occupancy rates of UC's student accommodation properties shows: 3.19

- the dwelling occupancy rates and bed occupancy rates of the UC's NRAS-eligible student accommodation have increased over time; and
- the dwelling occupancy rates for the NRAS-eligible accommodation consistently exceeds the bed occupancy rates of the NRAS-eligible occupation. This is because a dwelling is considered to be fully occupied even if only one of the multiple beds that are available within the dwelling are occupied. In this situation the dwelling occupancy rate will exceed the bed occupancy rate.

Between 2011 and 2014 the bed occupancy rate of Arscott House declined from 99.1 percent in 2011 to 57.5 percent in 2014 (99.1 percent in 2011, 91.6 percent in 2012, 75.2 percent in 2013 and 57.5 percent in 2014). Arscott House has not been available for student accommodation purposes in 2015. The UC advised that the decline in Arscott House occupancy was due to issues associated with the management of the facility. The UC further advised that it decided not to make the Arscott House available for student accommodation purposes in 2015, to enable it to make an assessment of options to refurbish and manage the facility. 3.20

ACT Government objectives for providing financial and other support to the UC are implicit in the reasoning for the provision of financial support in the Cabinet documentation, and include: 3.21

- increasing the supply of affordable accommodation to students;
- achieving economic benefits for the ACT; and
- alleviating pressure on the broader ACT rental market.

The ACT Government has not assessed whether the expected economic benefits associated with the provision of financial support to the UC have been achieved or whether the supply of accommodation by the UC has alleviated pressure on the broader rental market. However, evaluating the direct effects of the additional supply of accommodation by the UC from the ACT Government's financial and other support would be difficult at this time as these benefits may not be realised until some time in the future. 3.39

A consideration of the ACT Government in providing financial support to the UC was to provide support without adverse fiscal consequences to the Territory. A key risk that the ACT Government sought to avoid was the inability of the UC to repay its debt. 3.40

An analysis of the UC's debt to equity ratio shows: 3.62

- the UC's debt to equity ratio increased significantly between 2005 and 2013, before declining in 2014. This shows that, between 2005 and 2013, the proportion of debt maintained by the UC increased at a faster rate than its equity. The primary reason for the decline in the debt to equity ratio in 2014 was the UC's repayment of a significant

amount of its debt it owed to the ACT Government in November 2014, as a condition of the ACT Government's agreement for the UC to sell its NRAS entitlements to Westpac. The UC advised that between 2005 and 2013, it had used debt to finance its growth and renewal strategy and that this would explain why its debt has increased at a faster rate than its equity; and

- when compared to a selection of five other universities, the UC's debt to equity ratio was the third lowest in 2008 and in 2013 significantly exceeded that of the other universities included in the audit analysis, which the UC advised is due to a greater reliance on debt as the source of funding for its growth and renewal strategy.

The UC advised that it recognises that the debt to equity ratio increased substantially compared to other universities however, the UC also advised that it considered this to be necessary to pursue a growth strategy to sustain the UC's long term future. It further advised that it does not have the advantage of a large investment or endowment portfolio or access to significant state grants. The debt to equity ratio declined in 2014 and the UC advised that its financial position is being carefully managed by the UC and its Council and that this will continue. 3.63

Westpac and the UC entered into an agreement on 25 November 2014 for the sale of 605 NRAS entitlements. In return for the sale of the NRAS entitlements, the UC received a cash payment of $42.4 million. Under this arrangement, the UC has relinquished any claims to future NRAS Incentives (which will now be received by Westpac) but does, as Westpac's agent, retain responsibility for managing the NRAS-eligible dwellings. The agreement allows Westpac to recover from the UC any future NRAS Incentives that are not paid by the Commonwealth Department of Social Services in the event that the UC does not continue to meet the ongoing eligibility requirements (e.g. occupancy rates). 3.70

As a condition of the ACT Government's approval for the sale of the NRAS entitlements, the UC has used the amount received to: 3.71

- fully repay its debt to the ACT Government relating to the Cameron Wing 4 loan; and
- make an early repayment of $18.5 million to the ACT Government relating to the Cooper Lodge loan. The UC now only has one loan from the ACT Government (relating to Cooper Lodge), the outstanding balance of which stands at $31.4 million as at 31 December 2014.

The sale of its NRAS entitlements provided an immediate cash receipt of $42.4 million for the UC. As a condition of its approval for the arrangement, the ACT Government ensured that the proceeds from the sale were used to pay some of the debt that the UC owed to the ACT Government. The sale has therefore had the effect of reducing aspects of the UC's more immediate financial liabilities (i.e. its debt to the ACT Government) while creating another ongoing financial liability for the UC. The ongoing financial liability places an onus on the UC to ensure that it maintains occupancy levels of its NRAS-eligible dwellings. Should the UC not be in a position to maintain occupancy levels of its NRAS-eligible dwellings, there are contractual remedies open to Westpac to recover payment from the UC. While not 3.75

maintaining occupancy levels was an existing risk for the UC (as Australian Government payments were contingent on this), there is now an additional incentive for the UC to maintain these levels, as Westpac may seek payment from the UC should Australian Government NRAS payments not be forthcoming.

As at 31 December 2014, the UC had the capacity to borrow up to $20.0 million from non-Government lenders, i.e. $19.0 million in loans from non-ACT Government lenders (i.e. $70.0 maximum borrowing limit less $51.0 million currently borrowed) and a $1.0 million bank overdraft facility with a non-Government lender. 3.78

The UC's cash flows for 2014 showed that the UC does not generate significant net inflows from its operations. The UC advised, however, that timing issues associated with the receipt and expenditure of grants has also impacted its net cash flows. Net cash inflows from operations are necessary for the UC to repay its debts. The UC's 2014 financial model indicates that it expects to improve its net cash inflows from operations and its capacity to repay its debts over 2014 to 2018. However, there are risks associated with achieving this. 3.88

The UC is reliant on increasing student revenue to generate operating surpluses. By 2018 the UC plans to enrol 16,500 full-time equivalent students. In 2014 the UC's equivalent full-time student load was 11,125 (a 3.5 percent increase on its 2013 equivalent full-time student load). The UC will need to increase its equivalent full-time student load by 48.3 percent between 2014 and 2018 to achieve its goal of 16,500 full-time equivalent students. 3.89

The UC's first semester enrolments for 2015 were 5,585 full-time equivalent students, as compared to 5,568 for the same period in 2014 (an increase of 0.3 percent). The UC's plan to increase its full-time equivalent student numbers by 48.3 percent between 2014 and 2018 is at risk if the trend between 2014 and 2015 first semester student enrolment numbers continues. 3.91

The UC advised that some of this growth will be outside Canberra through partnerships in Melbourne, Sydney and Brisbane as well as through growth in international students studying in Canberra. 3.92

Changes to the UC's business environment that affects student numbers will present a risk to the achievement of the UC's financial goals and its ability to repay its debts. It is noted, however, that other universities are likely to be facing similar challenges to those confronting the UC with respect to increasing student numbers. 3.93

The UC also advised that there were strong reasons for its growth strategy and that capital investment, including investment in student accommodation, has been an important part of this growth strategy, much of which has been financed from borrowings. The UC acknowledges that the level of debt has increased (and that there are increased financial risks associated with this) but that these have been and will continue to be managed through its governance and oversight arrangements. 3.102

There are risks associated with the UC's capacity to repay its debts to the ACT Government. There are, however, options available to the UC to reduce expenditure and obtain income in order to meet its debt obligations. These include reducing expenditure, deferring capital projects, and entering into partnerships for the development of the UC campus. It is important that the risks to the Territory are monitored and reported to the Chief Minister and Treasurer. 3.105

Recommendations

RECOMMENDATION 1 UC CREDIT RATING

The ACT Government should require the UC to provide an independent credit rating from a recognised credit rating agency before considering any further financial or other support for the UC.

RECOMMENDATION 2 MONITORING PERFORMANCE

The ACT Government should review the UC's performance in providing affordable accommodation to students against objectives and outcomes sought by the provision of ACT Government funding.

RECOMMENDATION 3 ACT GOVERNMENT MONITORING OF UC FINANCIAL POSITION

The Chief Minister, Treasury and Economic Development Directorate should monitor risks to the Territory associated with the UC's debts and its capacity to repay its debts and brief the Chief Minister and Treasurer on the effectiveness of the UC's strategies to address the potential risks.

RECOMMENDATION 4 ASSESSMENT OF SUPPORT FOR THE PROVISION OF AFFORDABLE STUDENT ACCOMMODATION

The ACT Government and the University of Canberra should assess the level of ACT Government support that has been provided for the purpose of the NRAS and make any necessary adjustments should a shortfall occur in the provision of student accommodation against the target.

RECOMMENDATION 5 ARSCOTT HOUSE

The University of Canberra should determine the future use for Arscott House. If it is not to be used for student accommodation or educational purposes as planned and changes to the use require a change in lease whereby the property value exceeds that provided by it in support of NRAS ($9.0 million) it would be equitable for an appropriate adjustment to be made to the ACT Government.

Auditees' responses

In accordance with section 18 of the *Auditor-General Act 1996*, a final proposed report was provided to the Director-General of the Chief Minister, Treasury and Economic Development Directorate and the Vice Chancellor of the UC for consideration and comment. The Director-General provided comments which resulted in some minor changes. Following this, no further comments were made. The Vice Chancellor of the UC provided comments which resulted in changes, and provided a statement for inclusion in the summary chapter. This is presented, in full, below.

University of Canberra

The University accepts the recommendations in the report insofar as they relate to it, and will work with the ACT Government in relation to other recommendations to the extent they are applicable in the future.

The University notes the Auditor-General's support for the due diligence undertaken by the ACT Government before agreeing to the loans, thus rendering the bulk of the audit report of unclear relevance given the primary purpose of the audit. Throughout the period in question the University's financial statements have been audited by the Auditor-General, and every year the audit has been unqualified, which includes consideration of whether the University is able to pay its debts as and when they fall due.

The University has been pursuing an ambitious growth strategy and had no option except to supplement the funding available from internal operations with debt facility funding. The University and its Council continue to monitor and manage any associated risks and the increase in debt funding is temporary.

The University Council members, the majority of whom are appointed by the Chief Minister, are fully supportive of the way that the University's financial position is managed and is conscious that the University needs to be ready for a much more competitive higher education market. Failure to have good quality affordable student accommodation which can be guaranteed to out of state and international students would be a considerable barrier to success in a fast-changing university sector. In 2008, the University had limited student accommodation which was of poor quality and in need of maintenance. Now, the University through a combination of arrangements has sufficient and attractive accommodation, with a range of price

points for students of different means, and the newer residence blocks are effectively 100% full. The University is well-positioned to take advantage of the revival in international student demand following the down-turn around Australia in 2011-12, and also to take advantage of the increase in university age students expected in the local region from around 2018.

The University considers itself fortunate to be one of only 6 universities in the country to win NRAS subsidies for new student accommodation and is grateful for the ACT Government's contribution. In effect, the University has borrowed funds to create income-producing assets that will be subsidised by the Commonwealth for ten years and will then continue to provide benefit to the University and the Territory for many more years after that. Even with the benefit of hindsight, it would do the same again.

Audit Office comment

The Audit Office notes the response from the UC and the statement:

> Throughout the period in question the University's financial statements have been audited by the Auditor-General, and every year the audit has been unqualified, which includes consideration of whether the University is able to pay its debts as and when they fall due.

In relation to this statement, the Audit Office notes that, as part of the annual financial statements prepared by the UC, the UC Council provides a statement with respect to whether there are reasonable grounds to believe that the UC will be able to pay its debts as and when they fall due. For example, in the UC Member's Declaration to the 2014 financial statements the UC Council stated:

> In our opinion, at the time of the report there are reasonable grounds to believe that the University of Canberra will be able to pay its debts as and they fall due.

In forming the unqualified audit opinion on the 2014 financial statements of the UC, the Audit Office considered whether the use of going concern assumption in the preparation of the financial statements was reasonable, including whether the statement by members of the UC Council that 'there are reasonable grounds to believe that the UC will be able to pay its debts as and they fall due' was reasonable at the time the audit report was signed.

The Auditor-General formed the opinion that there were 'reasonable grounds to believe' that the UC can pay its debts as and when they fall due, in the forthcoming year. The Auditor-General will again assess whether there continues to be reasonable grounds to believe that the UC can pay its debts as and when they fall due as part of future annual audits of the financial statements of the UC.

1 INTRODUCTION

1.1 This chapter provides information on the financial and other support provided to the UC by the ACT Government and includes a discussion on:

- the National Rental Affordability Scheme (NRAS) (a key Council of Australian Governments initiative for the provision of affordable accommodation);
- the UC's student numbers and student accommodation goals; and
- the UC's funding arrangements, including revenue and debt sources of funding.

1.2 It also presents the objective, criteria and method for the audit.

ACT Government support for National Rental Affordability Scheme (NRAS) participation by the UC

1.3 Financial and other support has been provided to the UC by the ACT Government primarily to assist the UC to participate in the National Rental Affordability Scheme (NRAS) for the purpose of providing student accommodation.

1.4 Direct ACT Government support for the UC's participation in the NRAS comprised of:

- a loan facility of up to $23.4 million to the UC for the purpose of providing support for the redevelopment of existing office space in Belconnen to be used as student accommodation;
- a cash grant of $6.0 million, to be paid over nine years; and
- the gift of Arscott House to the UC. Arscott House was valued at $9.0 million for the UC and $5.0 million for the ACT Government.

Loan (July 2011) ($23.4 million)

1.5 In July 2011 a loan facility of up to $23.4 million was provided to the UC by the ACT Government. It was provided to assist the UC to purchase and redevelop Wing 5 of the Cameron Offices in Belconnen for student accommodation. The Cameron Offices, located at Chandler Street in Belconnen, had previously been used as office accommodation.

Cash grant (March 2011) ($6.0 million)

1.6 In March 2011 a cash grant of $6.0 million was agreed to by the ACT Government to assist the UC to purchase and redevelop Wing 5 of the Cameron Offices in Belconnen for the purpose of student accommodation.

Gift of Arscott House (December 2011) (value $9.0 million to the UC, $5.0 million to the ACT Government)

1.7 In December 2011 Arscott House was transferred from the ACT Government to the UC. At the time of its transfer, Arscott House was a property asset registered as part of the Economic Development Directorate property portfolio, which was being leased to the UC for no payment for the purpose of providing student accommodation. Arscott House is located on Aikman Drive in Belconnen, adjacent to Lake Ginninderra and the UC campus in Belconnen.

Other ACT Government financial support

1.8 In addition to the first loan facility of $23.4 million, the ACT Government has provided two additional loan and credit facilities to the UC for the purpose of providing affordable student accommodation.

Credit facility (September 2012) ($50.0 million)

1.9 In September 2012, a credit facility of up to $50.0 million was provided to the UC by the ACT Government. The purpose of the credit facility was to enable 'the design and construction of student accommodation and ancillary facilities on the UC campus which will result in 297 dwellings consistent with the UC's obligations under the Commonwealth NRAS arrangements'.

Credit facility (June 2013) ($24.0 million)

1.10 In June 2013 a credit facility of up to $24.0 million was provided to the UC by the ACT Government. The purpose of the credit facility was to enable 'the purchase and redevelopment of Wing 4 Cameron Offices ... for student accommodation which will result in 131 dwellings consistent with the UC's obligations under the Commonwealth NRAS arrangements.'

1.11 The UC has since repaid some of the loan amounts to the ACT Government. Table 1-1 summarises ACT Government loans provided to the UC for the purpose of providing affordable accommodation to students and outstanding loan amounts.

Table 1-1 ACT Government loan and credit facility support to the UC for the purpose of providing affordable student accommodation

Loan	Loan amount ($m)	Outstanding loan amount ($m)	Explanation
Loan - July 2011	$23.35	Nil	Repaid in May 2014
Credit facility - September 2012	$50.00	$31.40	Partly repaid in November 2014
Credit facility - June 2013	$24.00	Nil	Repaid in November 2014
Total	**$97.35**	**$31.40**	

Source: Audit Office, based on information from University of Canberra

Rental affordability and government policy responses

National Rental Affordability Scheme

1.12 The National Rental Affordability Scheme (NRAS), which commenced in 2008, is a Council of Australian Governments initiative between the Australian Government and the states and territories to invest in affordable rental housing. The NRAS 'seeks to address the shortage of rental housing and rapidly rising rents' by offering financial support to providers of new rental dwellings. Financial support:

> ... is offered on the condition that dwellings are rented to eligible low and moderate income households at a rate that is at least 20 per cent below the prevailing market rate. By requiring a reduction on market rent of at least 20 per cent, the Scheme substantially improves affordability for tenants.

1.13 The NRAS is discussed in further detail in paragraphs 1.22 to 1.32.

ACT Affordable Housing Action Plan

1.14 In August 2006, the ACT Government established an Affordable Housing Steering Group. Deriving from the work of the Affordable Housing Steering Group, in April 2007, the ACT Government released its *Affordable Housing Action Plan*.

1.15 The ACT Government's 2007 *Affordable Housing Action Plan* stated:

> Small investors dominate the private rental market, which provides approximately 26,000 dwellings in the ACT. The current rental vacancy rate in the ACT is very low, at around 1.6 per cent. Average rents in the ACT are currently also the highest in the nation. Access options for households just above the eligibility criteria for public housing have become limited.

1.16 Since 2007 three phases of the *Affordable Housing Action Plan* have been developed.

Student accommodation needs and the Affordable Housing Action Plan

1.17 There are no specific actions related to the provision of student accommodation in the ACT Government's *Affordable Housing Action Plan*.

1.18 Nevertheless, Phase III of the *Affordable Housing Action Plan* (June 2012) reported:

> ... More than 2,600 new rental dwellings will be built and rented at no more than 80 per cent of the market rate for 10 years through the National Rental Affordability Scheme. This includes the development of 1,000 new student accommodation dwellings each at the University of Canberra and the Australian National University, and more than 600 dwellings to be built by CHC Affordable Housing.

Standing Committee on Education, Training and Youth Affairs 2012 inquiry

1.19 In August 2012, the Standing Committee on Education, Training and Youth Affairs completed an inquiry into the accommodation needs of tertiary education students in the ACT.

1.20 The inquiry made a total of ten recommendations. Key recommendations included:

> RECOMMENDATION 1
>
> The Committee recommends that planning for housing suitable for development as student accommodation be included in the ACT Government's Affordable Housing Action Plan, including consideration of how development of student accommodation could be supported and encouraged.
>
> RECOMMENDATION 2
>
> The Committee recommends that the ACT Government continue its policy of encouraging student-specific accommodation projects along the lines of existing developments such as the ANU City West projects.

1.21 In February 2013, the ACT Government released its response to the inquiry, indicating that it agreed, at least in part, to all ten recommendations. Recommendations 1 and 2, as listed above, were agreed to as follows:

> *Recommendation 1 – Agreed in part* - A third phase of the ACT Government's Affordable Housing Action Plan was released in June 2012. Many of the actions in Phase III are aimed at improving affordability in the private rental market, particularly for lower income households. While Phase III does not explicitly refer to student accommodation, tertiary students generally fall within the cohorts targeted by these initiatives.
>
> *Recommendation 2 – Agreed* - The ACT Government has provided support for a range of student accommodation projects including the recent 'Campus 1' developments at the University of Canberra, the Lena Karmel Lodge at the Australian National University and the leasing of a student-specific residence to the Canberra Institute of Technology.
>
> In addition to the Australian National University/City West developments, the Government is supporting the construction of 1,000 new student dwellings by the University of Canberra.

National Rental Affordability Scheme

1.22 The National Rental Affordability Scheme has been an important feature of the UC's efforts to provide student accommodation.

1.23 According to the *National Rental Affordability Scheme Policy Guidelines* (June 2011), the NRAS has three objectives:

1. to stimulate the supply of up to 50,000 new affordable rental dwellings [nationally];
2. to reduce rental costs for low and moderate income households by making these dwellings available for rent at a rate that is at least 20 per cent below the prevailing market rate; and
3. to encourage large-scale investment and innovative delivery of affordable housing.

1.24 The *National Rental Affordability Scheme Policy Guidelines* (June 2011) note that student accommodation may be eligible under the NRAS where the accommodation meets the requirements of the NRAS, including being:

- considered capable of being lived in as a separate residence; and
- subject to the landlord, tenancy, building, health and safety laws of the State or Territory and Local Government area in which it is located.

1.25 A key feature of the NRAS are National Rental Incentives.

National Rental Incentives

1.26 National Rental Incentives are financial incentives provided to persons or entities to build and rent dwellings to low and moderate income households under the NRAS. National Rental Incentives are available annually to approved participants for up to 10 years for each approved rental dwelling that complies with the requirements of the NRAS. National Rental Incentives are made up of contributions from both the Australian Government and the relevant State or Territory Government, at a ratio of 3:1, i.e. for every $3 of contribution from the Commonwealth, the State or Territory Government is to provide $1.

1.27 National Rental Incentives comprise:

- an Australian Government contribution in the form of a refundable tax offset or payment (indexed annually but approximately $8,000 p/a in 2014-15); and
- a State/Territory contribution (indexed annually but approximately $2,700 p/a in 2014-15) in the form of direct financial support of a specified value or some other support of equivalent value.

1.28 National Rental Incentives are provided on a pro rata basis for the number of days in the NRAS year (1 May – 30 April) that the approved rental dwelling was available for rent and complied with all NRAS requirements.

State and Territory contribution to National Rental Incentives

1.29 While the Commonwealth's contribution to National Rental Incentives are to be provided as refundable tax offsets or payments over the ten-year period, the State or Territory contribution may be made as a cash or an in-kind contribution and provided as a one-off up-front payment or paid over time.

1.30 The National Rental Affordability Scheme Policy Guidelines (June 2011) provide:

> State and Territory Governments have agreed to a minimum contribution as a payment or by in-kind support of equivalent value. They may choose to increase the value of their contribution.

1.31 The National Rental Affordability Scheme Policy Guidelines (June 2011) also provide:

> State and Territory Governments may provide in-kind support ... rather than a payment ... Possible examples include:
>
> - a discount on stamp duty, land taxes or infrastructure charges;
> - tenancy and property management on a fee for service basis only where there are no suitable alternatives and where the State Housing Authority is asked to perform that role; and
> - discounted price of land.

1.32 The National Rental Affordability Scheme Policy Guidelines (June 2011) also provide:

> State and Territory Governments may provide their contributions to the National Rental Incentive for future years in advance.

2014 Australian Government budget announcement on NRAS

1.33 On 13 May 2014, the Australian Government announced that it would not proceed with further applications to the NRAS. The Commonwealth Department of Social Security website states:

> The scheme has been slow in delivering affordable homes and has failed to achieve its delivery targets despite ongoing Government funding. The Government remains committed to improving the administration of the scheme for incentives already allocated.

1.34 In explaining the reasons for stopping NRAS applications, the Commonwealth Minister for Social Services stated:

> The National Rental Affordability Scheme has fallen well short of expectations—it has simply failed to deliver for low and moderate income Australians. The scheme has been plagued by the late delivery of dwellings, trading of incentives, multiple changes to agreed locations, leasing to international students and rorting.

1.35 Although new participants in the NRAS are not allowed, incentives already allocated will continue to be paid for up to ten years, as long as eligibility requirements are met and accommodation under construction or committed is completed according to agreed timeframes and in agreed locations.

University of Canberra financial performance

1.36 The UC has experienced growth in recent years, including in student numbers and revenue. Paragraphs 1.42 to 1.43 discuss the UC's growth in student numbers between 2009 and 2014.

1.37 Table 1-2 shows the growth in UC's revenue from 2007 to 2014 and its overall financial performance during this period.

Table 1-2 UC financial performance (2007 to 2014)

	2007	2008	2009	2010	2011	2012	2013	2014
Total income from continuing operations ($000)	129,516	145,358	167,085	194,131	210,336	240,253	254,940	273,475
Total expenses from continuing operations ($000)	145,604	145,411	164,966	185,113	200,253	225,827	238,889	272,671
Operating surplus before tax ($000)	(16,088)	(53)	2,119	9,018	10,083	14,426	16,051	804
Total assets ($000)	293,455	288,672	328,718	346,646	416,032	435,285	523,722	542,002
Total liabilities ($000)	30,070	38,692	50,439	59,556	119,143	125,303	198,972	212,618
Net assets ($000)	263,385	249,980	278,279	287,090	296,889	309,982	324,750	329,384

Source: Audit Office, based on information from University of Canberra annual reports

Note: The table shows the consolidated financial performance of the UC group, which includes the university entity, as well as other entities including: University of Canberra College Pty Ltd, UCU Ltd and UC Global Pty Ltd (formerly NATSEM Pty Ltd).

1.38 An analysis of the UC's financial performance from 2007 to 2014 shows:

- the UC's total income from continuing operations has increased from $129.5 million in 2007 to $274.5 million in 2014 (an increase of 112 percent), while its total expenses from continuing operations has increased from $145.6 million in 2007 to $272.6 million in 2014 (an increase of 87.3 percent); and
- the UC experienced an operating loss in 2007 and 2008 ($16.1 million and $0.05 million respectively), before experiencing increasing operating surpluses up to 2013 ($16.1 million). The UC's operating surplus declined in 2014 to $0.8 million.

1.39 The UC's reported financial performance is affected by the timing of grant funding receipt and expenditure. For example, in 2012 and 2013 the UC received Australian Government Structural Adjustment Fund grant income of approximately $10.8 million and $15.1 million respectively, of which only approximately $5.7 million was spent in 2013, with the balance being spent in 2014. Since 2010, as part of its annual Financial Audits report, the Audit Office has identified:

- the reported operating surplus of the UC which, as required under relevant accounting standards, includes grant funding when it was received, and expenditure when it was incurred; and

- the operating surplus (or deficit) of the UC taking into account timing differences associated with the UC's grant funding.

1.40 Table 1-3 shows the UC's reported results and the UC's results, taking into account timing differences associated with its grant funding.

Table 1-3 UC's reported operating surpluses (or deficits) and UC operating surpluses (or deficits) taking into account timing differences associated with grant funding

	2010 ($m)	2011 ($m)	2012 ($m)	2013 ($m)	2014 ($m)
Reported operating surplus (or deficit)	8.0	9.1	14.1	14.7	(2.0)
Surplus (or deficit) taking into account timing differences associated with grant funding	(5.1)	(6.6)	0.4	4.6	4.9

Source: Audit Office Financial Audit reports (2011 to 2014) and other information

Note: The table relates to the University of Canberra entity's financial performance and does not reflect the UC's consolidated financial results, which also includes other entities; University of Canberra College Pty Ltd, UCU Ltd and UC Global Pty Ltd (formerly NATSEM Pty Ltd). Accordingly the data in this table does not reconcile with the reported results in Table 1-2.

The 2014 surplus taking into account timing differences associated with grant funding was provided by the UC on 10 June 2015. It was yet to be agreed for the purpose of inclusion in the Audit Office Financial Audit report for 2015.

1.41 The table shows that the timing of grant funding receipt and expenditure can have an impact on the UC's reported results. For example, in 2012 and 2013 the UC's university entity reported operating surpluses of $14.1 million and $14.7 million respectively, while the actual surplus, taking into timing differences associated with grant funding receipt and expenditure, was $0.4 million and $4.6 million respectively. Similarly, in 2014 the UC's university entity reported an operating deficit of $2.0 million, while its operating surplus, taking into account timing differences associated with grant funding receipt and expenditure, was $4.5 million.

University of Canberra student numbers and accommodation needs

Student numbers

1.42 Student numbers are a key driver of any university's revenue and funding. Since 2009 the UC's student numbers have been steadily increasing, as shown in Table 1-4, which shows the UC's Equivalent Full-Time Student Load (EFTSL) since 2009.

Table 1-4 UC Equivalent Full-Time Student Load

	2009	2010	2011	2012	2013	2014
ACT/Queanbeyan	4,629	5,180	5,505	5,730	5,825	6,066
Greater Sydney	376	399	423	399	356	361
NSW Country	1,130	1,438	1,565	1,646	1,604	1,501
Other	244	268	297	274	462	518
Domestic (total)	**6,379**	**7,285**	**7,790**	**8,049**	**8,247**	**8,445**
International (total)	**1,690**	**2,245**	**2,650**	**2,613**	**2,501**	**2,680**
Total	**8,069**	**9,530**	**10,440**	**10,662**	**10,748**	**11,125**

Source: Audit Office, based on information from University of Canberra annual reports

1.43 An analysis of the UC's student numbers shows:

- the UC's Equivalent Full-Time Student Load has increased from 8,069 in 2009 to 11,125 in 2014 (37.9 percent overall increase between 2009 and 2014);
- key drivers in the increase in the UC's Equivalent Full-Time Student load have been international students (58.6 percent overall increase between 2009 and 2014), students from country New South Wales (32.8 percent overall increase between 2009 and 2014) and students from ACT/Queanbeyan (31.0 percent overall increase between 2009 and 2014);
- the overall Equivalent Full-Time Student load attributable to international students has varied between 2009 and 2014. This figure peaked in 2011, before declining in 2012 and 2013, before increasing again in 2014; and
- overall student numbers increased from 10,748 in 2013 to 11,125 in 2014 (3.5 percent increase).

UC Accommodation Strategy 2011-15

1.44 In February 2011, the UC developed its *Accommodation Strategy 2011-15* 'for the period 2011-2015 to guide its planning and resource investment in meeting the needs of both domestic and international students'. The *Accommodation Strategy 2011-15* identified the expected continuing growth in student numbers, including students from overseas, as well as the scarcity of affordable private rental accommodation in the ACT, as key considerations in the provision of student accommodation. The UC's accommodation strategy has not been revised or updated since 2011.

1.45 In this respect, the introduction to the *Accommodation Strategy 2011-15* (February 2011) stated:

> The University of Canberra draws students from the Australian Capital Territory, regional New South Wales, Australia more broadly, and from across the world. In 2010 approximately 19% of the University's students were citizens of other countries. The University aspires to grow that percentage to 25% over the next few years. Given the number of students who travel to attend UC, the University believes it has a responsibility to consider the accommodation needs of its students. In particular, the University recognises that:
>
> – Affordable private rental accommodation is scarce in Canberra. Housing data does not suggest this will improve significantly in the short to medium term;
> – Many students are attracted to living on campus in a college environment with the social, pastoral, learning and sporting opportunities that that environment can present;
> – Safety is a critical concern for parents of students, and students themselves. Travelling long distances between places of study and accommodation exposes students to a range of safety issues not present when living on campus; and
> – The University's competitors are attempting to meet the accommodation needs of their own students, for many of the reasons outlined above. A university which can guarantee student accommodation will likely enjoy a competitive advantage in an increasingly competitive market.

1.46 In its *Accommodation Strategy 2011-15* (February 2011) the UC forecast non-ACT based student numbers at the UC's Bruce campus to 2018. Table 1-5 shows actual non-ACT based student numbers to 2010 and the forecast growth in non-ACT based student numbers to 2018.

Table 1-5 Non- ACT and international student numbers (2008 to 2018)

	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
	(actual)			(estimated)							
Domestic											
Domestic (non ACT/QBN) - TOTAL	1,876	2,202	2,490	2,688	2,846	2,963	2,978	2,986	2,988	2,988	2,988
Year on year growth (%)		*17.4*	*13.1*	*7.9*	*5.9*	*4.1*	*0.5*	*0.3*	*0.1*	*0.0*	*0.0*
International											
International Onshore - TOTAL	1,067	1,588	2,062	2,587	2,828	2,982	3,106	3,237	3,372	3,512	3,658
Year on year growth (%)		*48.8*	*29.8*	*25.5*	*9.3*	*5.4*	*4.2*	*4.2*	*4.2*	*4.1*	*4.2*
Total non-local student	2,943	3,790	4,552	5,275	5,674	5,945	6,084	6,224	6,360	6,500	6,646
Year on year growth (%)		*28.8*	*20.1*	*15.9*	*7.6*	*4.8*	*2.3*	*2.3*	*2.2*	*2.2*	*2.3*

Source: UC *Accommodation Strategy 2011-15* (February 2011)

Note: 2008 to 2010 student figures are actual figures, while 2011 to 2018 figures are estimates.

1.47 An analysis of the UC's *Accommodation Strategy 2011-15* (February 2011) shows:

- the total number of domestic (non-ACT and Queanbeyan students) and international students attending the UC's Canberra campus increased significantly between 2008 and 2010 (from a combined total of 2,943 students in 2008 to 4,552 students in 2010), with the most significant increases apparent in international students (from 1,067 in 2008 to 2,062 in 2010);
- the total number of domestic (non-ACT and Queanbeyan students) and international students attending the UC's Canberra campus was expected to continue increasing to 2018, albeit it a slower rate. The percentage growth in numbers was expected to progressively decrease from a growth rate of 15.9 percent in 2011 to a growth rate of approximately 2.2 to 2.3 percent each year between 2014 and 2018; and
- most of the growth in the total number of domestic (non-ACT and Queanbeyan students) and international students attending the UC's Canberra campus was expected to be from international students, with the number of international students expected to surpass domestic (non-ACT and Queanbeyan) students in 2013 and continue increasing at a stronger growth rate to 2018.

1.48 The risk associated with the expected increase in international student numbers, as shown in Table 1-4, was know by the UC. For example, UC Finance Committee meeting minutes from 17 September 2010 identified that a serious risk facing the UC was that international student enrolments would fall significantly and that this situation would be closely monitored as the potential loss of income could have serious financial implications for the UC. The UC advised that the market for international students in 2015 is significantly different to the market in 2010, and that this is a risk that is monitored by the UC Council.

Student accommodation targets

1.49 The UC's *Accommodation Strategy 2011-15* (February 2011) identified a target for the provision of accommodation to students. The strategy noted that the UC was expected to provide accommodation for approximately 32 percent of its students from outside the ACT in 2011, but that it intended to provide accommodation to 35 percent by the end of 2013 and 50 percent by the end of 2015.

1.50 The Accommodation Strategy 2011-15 (February 2011) stated:

> With reference to actual demand for places at UC, the University's planned student profile, and the shortage of accommodation in the private market, the University has adopted the following target:
>
> - To provide on-campus accommodation for 35% of our out-of-town students by end 2013 and for 50% by end 2015.

1.51 The *Accommodation Strategy 2011-15* (February 2011) identified a number of initiatives that were already underway in February 2011 (or soon to be commenced), which would increase the amount of accommodation available to students, including the redevelopment of existing on-campus accommodation buildings. The strategy also noted a bid had already been submitted for participation in the NRAS for 1,000 dwellings and that as part of the NRAS (or if unsuccessful in its application, as part of a separate approach to the market through an expression of interest process) a new 500 bed facility could also be developed on campus.

1.52 The *Accommodation Strategy 2011-15* (February 2011) noted that the development plans then in place would not produce the target number of places, and concluded that 'NRAS or a separate approach to the market will be critical to the University achieving its overall target'.

1.53 Table 1-6 shows actual accommodation supply to 2011 and forecast supply to 2018, including supply forecasts on the basis of existing initiatives and supply forecasts on the basis of an additional 500 beds.

Table 1-6 Supply of accommodation (2008 to 2018)

	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Total beds required (50% target)	**1,472**	**1,895**	**2,276**	**2,637**	**2,837**	**2,972**	**3,042**	**3,112**	**3,180**	**3,250**	**3,323**
Accommodation stock (without NRAS allocations)											
Actual or estimated supply	1,050	1,250	1,543	1,667	1,879	2,103	2,103	2,367	2,367	2,367	2,367
Difference (to target)	(422)	(645)	(733)	(970)	(958)	(869)	(939)	(745)	(813)	(883)	(956)
Actual percentage	36%	33%	34%	32%	33%	35%	35%	38%	37%	36%	36%
Accommodation stock (with NRAS allocations)											
Actual or estimated supply	1,050	1,250	1,543	1,667	1,879	2,103	2,103	2,867	2,867	2,867	2,867
Difference (to target)	(422)	(645)	(733)	(970)	(958)	(869)	(939)	(245)	(313)	(383)	(456)
Actual percentage	36%	33%	34%	32%	33%	35%	35%	46%	45%	44%	43%

Source: UC *Accommodation Strategy 2011-15* (February 2011)

Note: 2008 to 2011 figures are actual figures, while 2012 to 2018 figures are estimates.

1.54 Analysis of the UC's *Accommodation Strategy 2011-15* (February 2011) shows:

- the actual supply of accommodation at the UC increased from 1,050 beds in 2008 to 1,667 in 2011;
- the implementation of existing initiatives underway in 2011 was expected to increase the supply of accommodation at the UC from 1,667 beds in 2011 to 2,367 beds by 2015. This was not going to meet the UC's target of providing accommodation for 50 percent of out-of-town students, but would instead supply accommodation to 38 percent of out-of-town students in 2015, decreasing to 36 percent by 2018; and
- the implementation of additional initiative(s), either through NRAS or a separate approach to the market, to supply an additional 500 beds by 2015 would still not meet the UC's target of providing accommodation for 50 percent of out-of-town students, but would instead supply accommodation to 46 percent of out-of-town students in 2015, decreasing to 43 percent by 2018.

UC application for NRAS participation

1.55 Participation in the NRAS was an important component of the UC's *Accommodation Strategy 2011-15* (February 2011) and was a key driver of ACT Government financial and other support for the UC.

1.56 The UC submitted an application for 1,000 NRAS incentives for 1,000 dwellings in December 2010. The UC was the identified 'applicant' for the purpose of the scheme, but submitted the application as a representative of a consortium involving Campus Living Villages Pty Ltd and Campus Living Villages (Canberra) Pty Ltd.

1.57 The UC's application to NRAS contained the following statement in order to demonstrate a need for the proposal:

> UC predicts there will be sufficient demand to fill the proposed accommodation. The Student Accommodation Strategy 2010-2015 prepared by UC identifies a significant gap between the level of accommodation currently provided and the forecast growth in the population of non-local students over this period. An estimated 1700 additional beds will be required over the years 2011 to 2015 to satisfy population projections and achieve a small undersupply of 2%.

1.58 As part of its application the UC also noted:

> Low rental vacancy rates, increasing student numbers, rising cost of land surrounding the University, increased construction costs and limited bank funding due to the GFC is resulting in a lack of affordable accommodation for students close to where they are studying.

1.59 As part of its application the UC also noted:

> NRAS funding of this proposal will help provide much needed affordable accommodation for students close to their place of study and relieve the pressure on students. In turn it may also help to improve vacancy rates in surrounding suburbs to UC with the relocation of students from the private rental market into managed student accommodation.

1.60 The application proposed the development of 1,000 dwellings, to be delivered in two phases. The first 320 dwellings were to be developed on the UC campus, through a Build, Own, Operate and Transfer (BOOT) scheme, with Campus Living Villages (Canberra) Pty Ltd to be the lessee and Campus Living Villages Pty Ltd to be the operator and development manager.[1] The UC intended to issue a request for tender for a developer to deliver the remaining 680 dwellings.

1.61 As part of its application, the UC also advised:

> The final details of this proposal will be dependent on the level of NRAS support achieved and full demand and market studies. As such detailed design, development approval or finance has not been sourced or secured to date.

1.62 The UC identified that the accommodation to be provided was to be targeted towards full-time tertiary students studying at the UC, but that in the event that demand was not met by these students, the accommodation could be made available to 'students of other nearby universities, university staff and the general public.'

[1] A Build, Own, Operate and Transfer (BOOT) scheme is a form of project financing, wherein a private sector entity receives a concession from the public sector to finance, design, construct, and operate a facility. This enables the project proponent to recover its investment, operating and maintenance expenses in the project.

1.63 As part of its application the UC also advised:

> The proposed accommodation will target full-time tertiary students studying at UC. As a result, the tenant mix will be characterised by an international and domestic student population. The accommodation will provide housing for students undertaking both undergraduate and post-graduate courses. In the event that take-up level for the proposal results in a surplus of available beds, accommodation may be made available to students of other nearby institutions, university staff and the general public. Generally, and subject to demand levels, all occupants of the NRAS dwellings would have to qualify under the relevant NRAS criteria for the NRAS period.

1.64 In October 2011, the UC was notified that its application for NRAS participation was successful. On 7 October 2011 the UC issued a media release, which stated:

> An additional 1580 students will be offered accommodation at the University of Canberra after three new projects were given the go ahead today in an announcement of the biggest grant won in the University's history, involving $96 million from the Commonwealth coupled with $32 million worth of support from the ACT Government.
>
> Under its National Rental Affordability Scheme, the Commonwealth Government has agreed to a multimillion dollar subsidy to support various student accommodation projects, totalling $128 million.

1.65 On 12 October 2011 the UC received formal approval for 1,000 National Rental Incentives for 1,000 dwellings from the Australian Government. This offer was formally accepted by the UC on 21 October 2011.

Benefits of the NRAS student accommodation

1.66 The UC has advised there were significant benefits to the UC in participating in the NRAS, as it is 'bringing modern student accommodation into the University's stock, suitable for today's student needs and expectations, and then receiving a Commonwealth rebate for 10 years, thus reducing the overall cost of the accommodation significantly.' Participating in the NRAS was therefore a 'huge opportunity'.

1.67 Furthermore, the UC advised:

> Independent studies have shown that affordable accommodation, on campus or close to campus, is very important to attract non-ACT and international students as well as being important to their well-being. The increased quality and quantity of student accommodation would have been a big influence on the increase in non-ACT and international student numbers and the positive contribution that brings to UC finances.

1.68 The UC further advised that it 'took appropriate and reasonable steps in a difficult period to grasp an opportunity, the beneficiaries of which will be the ACT community.'

1.69 The UC also advised that a report prepared by Deloitte Access Economics in July 2014 on behalf of the Australian National University and the UC: *Higher learning: Economic and social impact of the major universities in the ACT*, identifies the economic contribution to

the ACT of the two universities. The report states that 'overall, the university sector was estimated to contribute $1.7 billion in value added to the ACT economy and $1.9 billion to the Australian economy as a whole ... Every dollar of expenditure related to the ACT University-related sector is associated with 80 cents of value added.'

1.70 The UC needed funds to develop the accommodation to be provided under the NRAS. Broad funding sources for the UC and its activities may be characterised as:

- revenue; and
- debt.

1.71 These are discussed in the following section of the report.

UC funding arrangements

Revenue

1.72 The UC receives income from a variety of different sources, including the Australian Government as well as income from fees and charges for services.

1.73 Table 1-7 shows the major sources of income for the UC since 2007.

Table 1-7 Sources of income for the UC (2007 to 2014)

	2007	2008	2009	2010	2011	2012	2013	2014
Australian Government Grants [1] ($m)	51,677	64,119	71,202	79,558	77,529	99,164	111,106	106,512
Proportion of total income (%)	39.9	44.1	42.6	41.0	36.9	41.3	43.6	38.8
HELP - Australian Government payments [2] ($m)	22,130	27,224	30,632	37,110	39,805	49,739	54,656	57,834
Proportion of total income (%)	17.1	18.7	18.3	19.1	18.9	20.7	21.4	21.1
Fees and charges [3] ($m)	28,574	24,216	31,075	42,968	51,164	58,408	59,011	72,828
Proportion of total income (%)	22.1	16.7	18.6	22.1	24.3	24.3	23.1	26.6
Other income from continuing operations [4] ($m)	14,903	15,185	16,832	21,207	16,744	15,398	12,437	17,471
Proportion of total income (%)	11.5	10.5	10.1	10.9	8.0	6.4	4.9	6.4
Total income from continuing operations ($m)	129,516	145,358	167,085	194,131	210,336	240,253	254,940	273,475

Source: University of Canberra financial statements 2007 to 2014.

Note1: Australian Government Grants refers to a range of financial assistance grants received from the Australian Government. This figure includes funds received under the Commonwealth Grants Scheme.

Note 2: HELP - Australian Government payments relates to payments received from the Australian Government relating to student education.

Note 3: Fees and charges income refers to a range of income received by the UC for other services.

Note 4: Other income from continuing operations refers to a range of other income received by the UC for other services.

1.74 An analysis of the UC's income shows:

- the UC's total income from continuing operations has increased from $129.5 million in 2007 to $274.5 million in 2014 (an increase of 112 percent);
- Australian Government grant funding is the largest single source of income for the UC, representing approximately 38.8 percent of total income from continuing operations in 2014. This is not significantly different from 2007, where Australian Government grant funding represented 39.9 percent of total income from continuing operations; and
- Australian Government HELP payments are the second largest source of income for the UC, representing approximately 21.1 percent of total income from continuing operations in 2014 (in 2007 this figure was 17.1 percent).

Proposed Australian Government reforms to higher education funding

1.75 Potential reforms to higher education funding may present a challenge to the UC and its operations. The sector, not only UC, is likely to face similar challenges.

1.76 As part of the 2014-15 Commonwealth Budget, the Australian Government sought to deregulate the higher education sector by allowing:

- non-university providers access to funding for Commonwealth supported places; and
- higher education providers to set their own uncapped prices for student contributions towards higher education.

1.77 These reforms have been identified as moving 'the sector to a greater user-pays and market-driven model.' These reforms have not been approved by the Senate.

1.78 The UC currently relies significantly on Australian Government grant funding for the majority of its revenue. Any reduction in future Australian Government grant funding to the UC, as part of potential reforms to higher education funding, could expose the UC to potentially significant financial pressures. The UC advised that its situation is not dissimilar to other Australian universities, but that it does not have the benefit of large endowments or investments.

Debt

1.79 The UC seeks to borrow money as a source of funding for its activities. The *University of Canberra Act 1989* and the *Financial Management Act 1996* specify requirements for the borrowing of money by the UC, including that the UC may only borrow money within limits established by the Treasurer.

1.80 The UC advised that it generally uses funds from operations for ongoing capital requirements and only borrows money for significant capital investments and that decision-making associated with whether to use debt financing depends on business cases and the UC's broader financial position.

Legislative requirements

1.81 The *University of Canberra Act 1989* places constraints on the UC's ability to borrow money. Section 34 of the *University of Canberra Act 1989* provides:

1) Subject to subsection (2), the university may borrow money.
2) The university's power to borrow is subject to the limits that the Treasurer decides about -
    a) the total amount of money (other than interest) that may be owed by the university at any time as a result of borrowings; and
    b) the periods for which money may be borrowed.

1.82 The *Financial Management Act 1996* similarly places constraints on the UC's ability to borrow money, as a territory authority. Section 59 of the *Financial Management Act 1996* provides:

(1) A territory authority must not borrow unless -

a) the borrowing is approved in writing by the Treasury; and

b) the terms and conditions of the borrowing include the terms and conditions (if any) specified in the approval and are otherwise consistent with the approval; and

c) the borrowing limit is within the borrowing limits (if any) of the authority for the financial year in which the borrowing is entered into, that are approved in writing by the Treasurer.

(2) However, subsection (1)(a) and (b)does not apply to a loan made to a territory authority under section 59(1)(b).

1.83 Section 59 of the *Financial Management Act 1996* provides:

(1) The Treasurer may, on the terms and conditions the Treasurer considers appropriate-

a) borrow money for a territory authority; or

b) lend public money to a territory authority.

(2) A borrowing may be secured by the territory authority's assets approved by the Treasurer for this section.

(3) A territory authority may arrange an overdraft or credit facility only with the written approval of the Treasurer.

(4) A loan under subsection (1)(b) may be made only from-

a) money appropriated for the purpose of making the loan; or

b) money appropriated for purposes that include the purpose of making the loan.

(5) However, subsection (4) does not apply to an overdraft or credit facility for a territory authority from the territory banking account that is approved by the Treasurer for the authority.

(6) The Treasurer may approve an overdraft or credit facility for a territory authority under subsection (5) only if satisfied that it is for a purpose consistent with a function of the authority.

(7) An approval under subsection (5) must state, for the overdraft or credit facility-

a) each purpose for which it may be used; and

b) the maximum amount that may be outstanding at any time; and

c) conditions about-

i) the repayment of principal; and

ii) the interest rate; and

iii) the repayment of interest.

(8) An approval under subsection (5) may also state any other condition that the Treasurer requires.

(9) An approval under subsection (5) is a disallowable instrument.

(10) An overdraft or credit facility approved under subsection (5) must be reviewed annually by the Treasurer.

Audit objective, criteria and method

Audit objective

1.84 The objective of this audit is to provide an independent opinion to the Legislative Assembly on the administrative effectiveness of the ACT Government's support for the University of Canberra for the provision of affordable student accommodation.

1.85 The audit specifically examined:

- whether ACT Government administrative and decision-making processes associated with the provision of the support were appropriate, including due diligence activities prior to the provision of loans and a credit facility; and
- whether the ACT Government's support for the University of Canberra, for the provision of affordable accommodation to students, has achieved intended ACT Government outcomes.

1.86 In examining the ACT Government's due diligence activities prior to the provision of loans and a credit facility, the audit also gave consideration to the University of Canberra's capacity to repay any debts owed to the ACT Government. This involved consideration of the UC's overall financial situation.

Audit criteria

1.87 The following criteria were used for the audit:

- were ACT Government administrative and decision-making processes associated with the provision of the financial and other support to the UC appropriate?
  - was the provision of financial and other support to the UC in accordance with legislative and policy requirements?
  - did the ACT Government implement appropriate safeguards to ensure that the support provided to the UC would be used for the purpose of providing affordable housing to students?
  - did the ACT Government conduct appropriate due diligence activities prior to the provision of loans and a credit facility to the UC, in order to safeguard the repayment of monies owed to the ACT Government?

- has the ACT Government's support for the University of Canberra for the provision of affordable accommodation to students achieved intended ACT Government outcomes?
  - did the ACT Government identify targets for affordable housing to students?
  - have identified targets for the provision of affordable housing to students been met?
  - is there evidence that the provision of affordable housing to students by the UC is meeting students' accommodation needs?
  - has the provision of affordable housing to students by the UC contributed to the achievement of the ACT Government's Affordable Housing Action Plan?
- does the UC have the capacity to repay any debts owed to the ACT Government?

Consideration of the UC's capacity to repay debts to the ACT Government

1.88 The UC has repaid a substantial amount of its debt to the ACT Government but, as at 31 December 2014, had approximately $31.4 million in debt owing to the ACT Government. In giving consideration to the UC's capacity to repay this debt to the ACT Government, the Audit Office necessarily considered the UC's total debt position, noting that the ACT Government is one of a number of lenders to the UC. The UC's capacity to repay any debts owed to the ACT Government is addressed in paragraphs 3.76 to 3.104 of the report.

Audit scope

1.89 In this audit, the financial and other support provided to the UC by the ACT Government for the purpose of providing affordable accommodation to students was examined. This included an analysis of:

- financial and other support provided in 2011 to the UC by the ACT Government for participation in the National Rental Affordability Scheme. This includes a loan, cash grant and direct land sale of Arscott House; and
- financial support provided to the UC by the ACT Government in 2012 and 2013, in the form of loans and credit facilities, for participation in the National Rental Affordability Scheme.

1.90 Also examined in this audit is the management and administrative activities of ACT Government agencies and the UC with respect to:

- the provision of the financial and other support; and
- the ongoing management and monitoring of the financial and other support.

1.91 The scope of the audit also included consideration of UC's capacity to repay any debts owed to the ACT Government.

Audit method

1.92 The audit method consisted of:

- interviews and discussions with key staff of the UC and the Chief Minister, Treasury and Economic Development Directorate;
- a review of documentation associated with the UC's participation in the National Rental Affordability Scheme and provision of affordable housing to students, including:
  - documentation maintained by UC associated with its participation in the NRAS; and
  - documentation maintained by the ACT Government associated with the UC's participation in the NRAS;
- a review of documentation maintained by the Chief Minister, Treasury and Economic Development Directorate, including:
  - documentation associated with decision-making processes to provide the UC with financial and other support;
  - documentation associated with the provision of financial and other support, including loan agreements and other relevant documentation; and
  - documentation associated with the ongoing management and administration of the financial and other support provided to the UC, as relevant;
- an analysis of the UC's financial situation and ability to repay its debts;
- a review of relevant Cabinet documentation associated with the provision of financial and other support to the UC; and
- securing legal advice on some issues.

Disclosure of deliberative information in this report

1.93 Section 20 of the *Auditor-General Act 1996* (the Act) provides for the disclosure of 'deliberative information' in Audit Office reports. Section 20 of the *Auditor-General Act 1996* provides that the Auditor-General may only include 'deliberative information' in a report:

- if the auditor-general considers that it is in the 'public interest' to do so; and
- after consulting with the Chief Minister.

1.94 'Deliberative information' is defined in the Act as 'information that discloses a deliberation or decision of the Executive.'

1.95 'Deliberative information' contained in Cabinet documentation is used to support the findings and conclusions of this audit. Chapter 3 refers to Cabinet decisions, and documentation provided to Cabinet (including Cabinet submissions and ACT Government agencies' comments on Cabinet submissions.

1.96 'Deliberative information' is disclosed in this audit report.

Reasons why the Audit Office considers that the inclusion of 'deliberative information' in this report is in the 'public interest'

1.97 Paragraphs 1.84 to 1.91 discuss the objective and scope of the audit. It is considered that it is in the 'public interest' to disclose 'deliberative information' in this audit report because:

- the ACT Government's decision-making processes, which resulted in the provision of significant support to the UC, and other decisions not to provide significant support requested by the UC, were decisions made by Cabinet after the consideration of information provided to Cabinet; and
- it represents important evidence that was considered by the Auditor-General in forming an independent opinion. Such evidence needs to be transparent to hold the ACT Government to account, and also the Auditor-General for the audit opinion. Its inclusion also promotes public understanding on an important issue.

1.98 Information referenced and quoted was judiciously selected to respect the importance of the confidentiality of the Cabinet process to facilitate robust, frank discussion that includes varying points of view

Consultation with the Chief Minister

1.99 Subsection 20(2) of the Act provides that 'the auditor-general must consult the Chief Minister in deciding whether it is in the public interest to include particular deliberative information in a report.'

1.100 Subsection 20(3) of the Act states that 'If the Chief Minister objects to the inclusion of particular deliberative information in a report, the Auditor-General (a) may include the information in the report; but (b) if the information is included, must tell the Chief Minister about the inclusion at least 7 days before the report is published.'

1.101 The Chief Minister was consulted in deciding whether it is the 'public interest' to include particular deliberative information in this audit report.

1.102 The Chief Minister advised that:

> The Government does not seek specific changes to the draft report in relation to its use of Cabinet material. It is important that disclosure of Cabinet deliberative material does not go beyond what is necessary for the legitimate discharge of the Auditor-General's functions, to avoid risk of impairing the frankness of advice into the Cabinet process.

2 ACT GOVERNMENT ADMINISTRATIVE AND DECISION-MAKING PROCESSES

2.1 This chapter discusses the ACT Government's administrative and decision making processes for the provision of financial and other support to the UC for the purpose of affordable student housing. The chapter considers the different funding requests that had been made by the UC to the ACT Government, as well as the UC's requests for increases to its overall borrowing amounts.

2.2 This chapter discloses 'deliberative information', including Cabinet decisions, and documentation provided to Cabinet (including Cabinet submissions and ACT Government agencies' comments on Cabinet submissions). The disclosure of the 'deliberative information' in this report is discussed in paragraphs 1.93 to 1.102.

Summary

Key findings

	Paragraph
An analysis of the UC's borrowing limits and loan and credit facility approvals shows: • the Treasurer, through a combination of Treasury Authorisations (and Instruments) and Disallowable Instruments, has approved a number of different loans and credit facilities for the UC, both from the Territory and other parties, between June 2011 and June 2013; and • the total maximum borrowing limit of the UC has increased from $0 prior to August 2008 to $144.0 million since May 2013. This is a significant increase in the amount of funds that the UC may borrow. ($74.0 million of this related to specific loans for the provision of student accommodation and, once repaid, is no longer available to the UC. Accordingly, $70.0 million remains available on an ongoing basis to the UC.)	2.5
ACT Government decisions in relation to the provision of financial and other support to the UC for the purpose of providing student accommodation developed in response to a series of requests by the UC. Requests from the UC were initially in the form of general representations to Ministers, primarily for the purpose of supporting the UC's growth strategy.	2.11
Requests by the UC for financial and other support specifically for student accommodation were subsequently developed through discussion between the UC and the Economic Development Directorate and presented to Cabinet for	2.13

consideration. As part of the Cabinet process, the Treasury Directorate provided advice, including on its due diligence analysis of the funding proposals.

In relation to the UC's requests for loan and credit facilities and increases to its borrowing limits, the ACT Government was primarily required to consider the UC's financial capacity to repay its loans. It did so through due diligence analysis. 2.17

As part of its due diligence analysis, in addition to considering the total amount of debt that the UC could appropriately borrow and repay, the Treasury Directorate documented two additional considerations, as follows: 2.20

- potential increases in the UC's borrowing limits being interpreted by the broader lending market as an indication that the ACT Government might underwrite debts of that amount should the UC face difficulties in meeting repayments; and
- the total amount of senior ranked debt that the UC could manage as a stand-alone entity, i.e. the debt that the UC could manage without putting the ACT Government at financial risk of having repayment of its loans subordinated to the repayment of other lenders' loans. This is a key risk to manage as lenders to Australian universities recognise that government funding underpins the operations of the sector. While loan subordination is an option a government might chose to take, it increases cash flow risks and can negatively impact on a jurisdiction's own credit rating.

On 14 December 2011, Cabinet agreed to the direct sale of Arscott House to the UC for $0 (essentially a gift). As part of its decision, Cabinet noted 'the transfer represents an estimated $9 million of the required $22.85 million in support from the ACT Government which is required under NRAS' and 'the transfer will assist UC to develop additional student accommodation places because it will be recognised as an asset that the University of Canberra can use to secure finance against.' 2.30

The transfer of Arscott House in December 2011 was important to the UC, notwithstanding that there were no specific time pressures for the purposes of the NRAS, including not before the end of December 2011. 2.34

The UC has since advised that the transfer of Arscott House provided the security of a renewed lease before any capital investment was made in the facility. 2.36

The UC reports its financial statements on a calendar year basis. In accordance with relevant accounting standards, the transfer of Arscott House in December 2011 allowed the UC to report an amount of $9.0 million as revenue. In 2011, the UC made an operating surplus before tax of $10.1 million. 2.37

At present Arscott House is not available for student accommodation. The UC advised that it closed in 2015 while options for its future use were being considered. The UC also advised that a decision on capital expenditure to upgrade Arscott House is pending and negotiations are underway with one of the UC's student accommodation providers, with a view to the accommodation provider taking responsibility for the premises. 2.38

On 11 February 2011, the Vice-Chancellor of the UC wrote to the Treasurer requesting an increase in the UC's total borrowing limit to $80.0 million. At the time of the request, the UC could only borrow up to $20.0 million. The UC was seeking funding to support its 'wide-ranging reform and revitalisation program', which required large capital investments to expand campus facilities, address a backlog of maintenance and 'fund strategic infrastructure projects which will promote the University's long-term sustainability through appropriate use of its extensive campus.' 2.39

On 9 March 2012 the Vice Chancellor of the UC wrote to the Chief Minister requesting an increase in the UC's total borrowing limit to $220.0 million, including a loan of $150.0 million from the Territory. The UC requested that the loan from the Territory be subordinated to loans from other non-Government lenders, i.e. the other non-government lenders would have the first opportunity to reclaim any payments from the UC. The UC requested the funding to 'assist the University manage and fund its structural reforms and infrastructure projects' including its student accommodation projects. 2.61

The Treasury Directorate advised the Treasurer on 12 April 2012 that the UC's proposal raised 'matters of concern'. The Treasury Directorate reiterated its earlier advice in relation to establishing a borrowing limit and how that might 'imply a form of indirect guarantee on the borrowing by the ACT Government to the UC' and that 'in the event of a loan default by UC, creditors may seek compensation from the Territory if other avenues of compensation have been exhausted.' 2.68

The Treasury Directorate considered 'the request to increase the borrowing limit to $220 million to be very significant due to the potential financial consequences.' In this respect, the Treasury Directorate identified 'the Territory's cash position is under pressure' and that 'based on the current budget position, new loans provided to UC will need to be funded by new external general government borrowings.' 2.70

In relation to the proposed subordination of the Territory loan to other loans with non-government providers, the Treasury Directorate identified the risks of such an arrangement, noting 'this means ACT Government provided loans would rank below claims of other lenders in the event of a call in of UC assets' and that 'as a 2.71

lender, it is imperative that the Territory understands the risks associated with the investment and fully provides for these risks in the terms and conditions of any loan agreement.'

The Treasury Directorate recommended that 'UC obtain a formal credit rating from a suitably, qualified, independent organisation such as Standard & Poors (S&P)'. 2.74

On 7 June 2012, a Cabinet submission was lodged by the Economic Development Directorate recommending *inter alia*: 2.78

- authorising the UC to borrow up to $220.0 million, being the aggregate of $150.0 million in loans from the Territory and $70.0 million in loans from parties other than the Territory;
- extending a line of credit to the UC up to $150.0 million to fund the development of student accommodation on the UC Bruce campus, at a rate 0.75 percent above the costs of finance to the Territory; and
- subordinating the UC's debt to the Territory to non-Government lenders.

The Cabinet submission identified that the additional funding would support the UC's growth strategy and plans to grow the number of students at the UC. The Cabinet submission also identified that the subordination of the Territory's debt to non-Government lenders would assist in giving the UC's balance sheet flexibility and in ensuring that its access to funding markets for strategic requirements was preserved. The Cabinet submission identified that, should the Territory be unwilling to agree to such an arrangement, a potential alternative arrangement was to provide for the full $220.0 million loan amount to be provided by the Territory. 2.79

On 4 June 2012, the Treasury Directorate sought external technical advice with respect to a 'high level assessment of the University of Canberra's (UC) Credit Worthiness as a stand-alone institution'. The Treasury Directorate sought advice on 'whether, and to what extent UC would be able to borrow in its own right', with specific advice sought in relation to: 2.82

- the credit worthiness of the UC as a stand-alone institution, noting that 'if UC supplied the contained proposal to a bank, seeking funding on commercial terms, what would be the likelihood of UC being granted credit approval'; and
- 'would UC's credit proposal be sufficient (in content) to seek a loan as a stand-alone entity on commercial terms'.

The advice expressed doubt that the UC would be able to borrow the funds it was requesting in its own right from non-government lenders. 2.84

However, the independent advice also identified that there may be circumstances 2.86

in which banks may give the UC's application favourable treatment, including:

- placing covenant restrictions on the use of the loan facilities, which 'would strictly restrict the terms and conditions under which the UC may draw on the facility, therefore placing the facility outside of ratio analysis';
- diversifying non-income generating assets so as to either 'pre-commit to pay down senior debt via asset sale' or 'generate additional revenue sources from new rental/leaseback opportunities'; or
- by treating the application as government risk.

2.88 The due diligence process that the Treasury Directorate undertook for the March 2012 request from the UC reflected a significantly increased level of risk to the UC and the ACT Government, inherent in a request for $220.0 million in total borrowings, of which $150.0 million would be subordinated Territory lending. The Treasury Directorate identified the potential impacts on the UC and also on the Territory's cash position, budget balance and credit rating. The Treasury Directorate's strategy of using external expert advice was appropriate, and its recommendations were consistent with this advice. The Treasury Directorate's advice reduced the exposure of the ACT Government to significant financial risk.

2.89 In a decision on 12 June 2012, Cabinet did not agree to the proposed increase in the UC's credit limit (to $220.0 million) or increase in the Territory's lending (to $150.0 million). The Cabinet decision aligned with the advice provided by the Treasury Directorate.

2.102 In May 2013 an external consulting firm (KPMG) was commissioned by the Treasury Directorate to 'assist with an analysis of the CW4 project [construction and operation of the Cameron Wing 4] and the resultant impact it will have on UC's financial position, particularly with respect to debt servicing.' The consulting firm's advice noted:

- on a "stand-alone" basis (defined as without implicit or explicit government support), the 'UC has limited capacity beyond the CW4 and Sporting Commons projects to undertake additional debt funded capital projects until key financial metrics return to at least an "intermediate" level based on S&P benchmarks';
- 'as the UC is entering into a period of significant financial risk, UC has diminished capacity to sustain shocks and maintain adequate liquidity levels. Failure to achieve projected student growth will exacerbate this financial risk'; and
- the UC has some financial flexibility through the ability to 'delay discretionary capital expenditure projects' and 'monetise their investment in student accommodation.'

2.103 In a subsequent briefing to the Treasurer dated 31 May 2013, in relation to the external consulting firm's advice, the Chief Minister and Treasury Directorate

advised 'we note that the UC is going through a significant growth phase and based on the student accommodation business cases and funding commitments, this phase necessitates an increase in debt levels to achieve the growth. An increased level of financial risk is an unavoidable consequence.'

A due diligence process for the proposed loan of $24.0 million for Cameron Wing 4 was undertaken. As in the case of previous due diligence analysis, it was appropriate and provided a sound foundation for the advice provided to the Treasurer. 2.105

UC borrowing limits, loan and credit approvals since 2008

2.3 Table 2-1 shows the UC's borrowing limits, Territory loan and credit facility approvals, as approved by Cabinet (for loan and credit facilities) and the Treasurer (for borrowing limits), since 2008.

Table 2-1 UC borrowing limits, loan and credit facility approvals since 2008

Date	Instrument	Provision	Amount ($m)	Maximum borrowing limit ($m)
23/4/08	Nil	Approval of borrowing limit (total maximum, Territory and/or other parties not specified)	20.00	**20.00**
30/6/11	TI2011/3	Approval of Territory loan to the UC	23.35	**70.00** (23.35 from Territory and 46.65 from other parties)
		Approval of loan facilities with Westpac Banking Corporation and Commonwealth Bank of Australia	80.00	
30/6/11	TI2011/7	Approval of borrowing limit from Territory	23.35	
		Approval of borrowing limit from other parties	46.65	
20/8/12	DI2012-208	Approval of Territory credit facility to the UC	50.00	**120.00** (23.35 from Territory, 46.65 from other parties and 50.00 credit facility from Territory)
20/8/12	TI2012/12	Approval of borrowing limit from Territory	23.35	
		Approval of borrowing limit from other parties	46.65	
		Approval of credit facility from Territory	50.00	
7/5/13	DI2013-40	Approval of Territory credit facility to the UC	24.00	**144.00** (23.35 from Territory, 46.65 from other parties and 50.00 and 24.00 credit facility from Territory)
7/5/13	TI2013/6	Approval of borrowing limit from Territory	23.35	
		Approval of borrowing limit from other parties	46.65	
		Approval of credit facility from Territory	50.00	
		Approval of credit facility from Territory	24.00	

Date	Instrument	Provision	Amount ($m)	Maximum borrowing limit ($m)
27/6/13	TI2013/9	Approval of borrowing limit (total maximum, Territory and/or other parties not specified)	70.00	**144.00** (23.35 from Territory, 46.65 from other parties and 50.00 and 24.00 credit facility from Territory)
		Approval of credit facility from Territory	50.00	
		Approval of credit facility by Territory	24.00	

Source: Audit Office, based on Treasury Instruments and Disallowable Instruments

2.4 The loan and credit facilities and increases to the borrowing limits are outlined in further detail in Appendix A.

2.5 An analysis of the UC's borrowing limits and loan and credit facility approvals shows:

- the Treasurer, through a combination of Treasury Authorisations (and Instruments) and Disallowable Instruments, has approved a number of different loans and credit facilities for the UC, both from the Territory and other parties, between June 2011 and June 2013; and
- the total maximum borrowing limit of the UC has increased from $0 prior to August 2008 to $144.0 million since May 2013. This is a significant increase in the amount of funds that the UC may borrow. ($74.0 million of this related to specific loans for the provision of student accommodation and, once repaid, is no longer available to the UC. Accordingly, $70.0 million remains available on an ongoing basis to the UC.)

ACT Government roles and responsibilities

2.6 Between 2010 and 2014, a number of ACT Government directorates and agencies have had a role in the ACT Government's funding arrangements for the UC. These include:

- the Economic Development Directorate (previously known as Land and Property Services);
- the Treasury Directorate; and
- the Chief Minister and Cabinet Directorate.

2.7 Since July 2014 the functions and activities of these entities have been consolidated within the Chief Minister, Treasury and Economic Development Directorate.

2.8 The Economic Development Directorate, and its predecessor the Department of Land and Property Services, has been the main contact between the UC and the ACT Government for the purpose of providing financial and administrative support for the provision of student accommodation. This was evident through:

- the Economic Development Directorate taking primary carriage of discussions with the UC; and
- the Economic Development Directorate taking responsibility for the formulation of advice for the ACT Government's consideration.

2.9 The Treasury Directorate had a role in assessing the financial implications of the UC's requests for additional funding and support. It provided advice to the ACT Government in relation to requests for increases to borrowing limits and additional funding through loan and credit facilities and facilitated the engagement of independent financial advisers.

2.10 Similar to the Treasury Directorate, the Chief Minister and Cabinet Directorate had a role in providing advice to Government in relation to increases to borrowing limits and additional funding through loan and credit facilities.

ACT Government policy and administrative processes for assistance to UC

2.11 ACT Government decisions in relation to the provision of financial and other support to the UC for the purpose of providing student accommodation developed in response to a series of requests by the UC. Requests from the UC were initially in the form of general representations to Ministers, primarily for the purpose of supporting the UC's growth strategy.

2.12 In February 2011, the Vice Chancellor of the UC wrote to the Treasurer requesting approval for an increase in its borrowing limit 'to assist the University manage and fund its reforms and infrastructure projects.' Similarly, in March 2012 the Vice Chancellor of the UC wrote to the Chief Minister seeking approval for an increase in its borrowing limit again 'to assist the University manage and fund its reforms and infrastructure projects.'

2.13 Requests by the UC for financial and other support specifically for student accommodation were subsequently developed through discussion between the UC and the Economic Development Directorate and presented to Cabinet for consideration. As part of the Cabinet process, the Treasury Directorate provided advice, including on its due diligence analysis of the funding proposals.

2.14 Cabinet was requested to consider the provision of financial and other support for the UC for the purpose of providing affordable accommodation to students, with regard to:

- the ACT's contribution to the UC's participation in NRAS (throughout 2011), including:
  - request for a loan of $23.4 million (March 2011);
  - approval of ACT Government contributions to NRAS-approved participants (June 2011); and
  - transfer of Arscott House (December 2011); and
- request for a cash advance facility of $56.7 million (April 2011);

- request to increase the UC's total borrowing limit to $220 million, inclusive of a Territory line of credit up to $150 million (June 2012);
- request for a $50 million line of credit from the Territory (July 2012); and
- request to increase UC borrowing limit and an increase in the Territory line of credit of $24 million (April 2013).

Considerations for National Rental Affordability Scheme (NRAS) participation

2.15 In relation to NRAS participation and its associated contributions, the ACT Government was primarily requested to consider:

- whether it supported the UC's application (as well as applications that had been made by other entities); and
- what would be the Territory's direct support. (The Territory was required to provide a matching contribution to National Rental Incentives, at a ratio of 3:1, i.e. for every $3 of contribution from the Commonwealth, the Territory was to provide $1).

2.16 As discussed in paragraph 1.4, the ACT Government's co-contribution ultimately comprised grant funding, the transfer of the crown lease on Arscott House, and concessional interest on loans used to fund the construction of student accommodation in the former Cameron Offices and on campus.

Considerations for loan and credit facilities and increases in borrowing limits

2.17 In relation to the UC's requests for loan and credit facilities and increases to its borrowing limits, the ACT Government was primarily required to consider the UC's financial capacity to repay its loans. It did so through due diligence analysis.

Due diligence

2.18 A key element of any process associated with providing a loan or credit facility is due diligence. Due diligence entails the analysis of a borrowing entity's business and financial risks, to determine whether a proposed loan aligns with a borrowing entity's business strategy and can be managed and repaid. The kind and extent of due diligence analysis performed needs to be commensurate with the risk a lender assumes. The greater the risk, the more rigorous and systematic the due diligence analysis needs to be.

2.19 The Treasury Directorate was responsible for performing due diligence on the UC's requests for loan and credit facilities from the ACT Government. Subsection 34(2) of the *University of Canberra Act 1989* requires the UC to obtain the Treasurer's approval for the total amount of its borrowings. Consequently, and in addition to considering each lending

request from the UC on its merits, the Treasury Directorate's due diligence also considered the total amount of the UC's borrowings from all sources.

2.20 As part of its due diligence analysis, in addition to considering the total amount of debt that the UC could appropriately borrow and repay, the Treasury Directorate documented two additional considerations, as follows:

- potential increases in the UC's borrowing limits being interpreted by the broader lending market as an indication that the ACT Government might underwrite debts of that amount should the UC face difficulties in meeting repayments; and
- the total amount of senior ranked debt that the UC could manage as a stand-alone entity, i.e. the debt that the UC could manage without putting the ACT Government at financial risk of having repayment of its loans subordinated to the repayment of other lenders' loans. This is a key risk to manage as lenders to Australian universities recognise that government funding underpins the operations of the sector. While loan subordination is an option a government might chose to take, it increases cash flow risks and can negatively impact on a jurisdiction's own credit rating.

NRAS support and participation

ACT Government endorsement of NRAS applications (June 2011)

2.21 In June 2011, the ACT Government was requested to consider its support for ACT NRAS applications (the UC and other organisations). A Cabinet submission prepared by the Economic Development Directorate noted that the combined applications were expected to deliver 1,481 new affordable rental properties in the ACT and that 'the increased number of new, affordable housing properties is expected to ease pressures on housing affordability in the Territory.'

2.22 In support of the applications, the submission stated:

> The combined applications will deliver 1,481 new affordable residential rental properties in the ACT including 1,000 dwellings for university students. Properties will be offered exclusively to low and moderate income earners at rents at least 20% below the market rate.
>
> The increased number of new, affordable housing properties is expected to ease pressures on housing affordability in the Territory.
>
> If successful, the combined applications will secure $99 million in funding from the Commonwealth over a ten year period for the proponents to construct new affordable residences in the ACT.

2.23 As part of its advice, the Economic Development Directorate identified that the request by the UC for financial support involved the direct sale of Arscott House to the UC at no cost (essentially a gift). In relation to Arscott House, the Cabinet submission identified *inter alia*:

- as part of its overall student accommodation strategy the UC planned to refurbish Arscott House and make improvements to enable it to continue to be used for student accommodation;
- the UC had advised that it needed to gain greater security of tenure over Arscott House to allow it to make significant investments in the property;
- the UC had advised that if it had to pay market value for the property it would be in a worse financial position than it was with the lease arrangements current at that time; and
- the UC advised that it needed to have 'off campus' assets like Arscott House to enable it to raise the finance required to progress its accommodation strategy. (The advice noted that the UC's on-campus assets could not be used as security for loans because a potential lender could not realise the asset in the event of a default by the UC. On 27 June 2011, Cabinet agreed to support the UC's NRAS application for 1,000 dwellings.

Transfer of Arscott House (December 2011)

2.24 The Cabinet decision in June 2011 to support the UC's application for NRAS funding included an in-principle agreement to transfer the crown lease on Arscott House.

UC's initial proposal (August 2010)

2.25 The request to transfer Arscott House originally came from the UC, in a submission made to the ACT Government on 31 August 2010. As part of its submission, the UC identified that the upgrade and extension of Arscott House was central to its accommodation strategy and that the 'maintenance of Arscott House as viable and attractive undergraduate accommodation is central to the longer-term objectives of the University of Canberra.'

2.26 In its 2010 submission the UC stated:

> In recent years affordable student accommodation has become increasingly important to the delivery of higher education, particularly for students from regional and rural areas and for international students.
>
> Whilst the University is dedicated to supporting the requirements of our students, providing appropriate accommodation for the current student load is challenging. There are some 1100 students living on campus at present. Based on growth predictions and the University's intention to ensure that no newly commencing student will be left homeless, it is estimated that the University must add some 1,700 beds in the next five years to accommodate non ACT-based students. This will still present as an undersupply situation for approximately 100 beds, equal to about 2% of the non-local student population. Access to other affordable housing options within the ACT is also nearing crisis level.
>
> The University is exploring a range of options to meet the student accommodation demand (including renting property off-campus) and has developed a draft accommodation strategy to address the needs of both domestic and international

students. Central to this strategy is the need to upgrade and extend Arscott House as a priority.

The University has prepared a campus master plan, which has confirmed the existing locations of residential precincts for students on the southwestern quarter of the main campus. Arscott House on Block 42 Section 65 Belconnen, directly across Aikman Drive from this residential precinct, and bordering the new University of Canberra Senior Secondary College Lake Ginninderra, is the most suitable land for student accommodation in the immediate vicinity of the campus. Such use is consistent with the functions of the University and with the planning parameters for the land.

Providing student accommodation on-campus and off-campus will generate the right range of accommodation types and rental prices, ad recognises the key contribution that student accommodation makes to university life. Future expansion on Block 42 Section 65 Belconnen to meet current and future student demand will consolidate quality student accommodation close to the academic heart of the campus.

...

Arscott House is the only off-campus residential building operated by the University of Canberra. Its location close to the significant precinct of student housing already available on the campus is an important factor in consolidating and enhancing living and learning environments within the University and the essential and desirable connections of the University to the Belconnen town centre. At the same time, the immediate conjunction of Arscott House with the buildings and grounds of the University of Canberra Senior Secondary College Lake Ginninderra offers flexibility to meet a range of expectations for community facilities in the future. From a purely strategic point of view, therefore, maintenance of Arscott House as viable and attractive undergraduate accommodation is central to the longer-term objectives of the University of Canberra.

...

Arscott House is now more than 30 years and will soon require almost continuous attention and modernisation. The University of Canberra is understandably reluctant to commit to the considerable additional expenditure for these works in the absence of security of tenure. The University seeks to extinguish the present sub-lease and accept a Crown Lease for a term of 99 years. In consideration of the expenditure to date in the maintenance and improvement of Arscott House, the University asks that the sale/transfer of the property be at no cost to the University. The issue of a Crown Lease for the site would provide certainty for the University and allow it to make the necessary future significant investments in the property and its immediate environs.

The University of Canberra confirms that it satisfies criterion (b) for the direct sale by the Territory of a lease to the University, and that the University will provide the funds necessary to develop and manage the land at Block 42 Section 65 Belconnen, known as Arscott House.

...

The University requests that the ACT Government give urgent attention to this submission so that it can make the necessary financial investment in the refurbishment and extension of Arscott House with certainty into the future.

2.27 The UC's August 2010 submission makes it clear that the UC intended to re-develop Arscott House to continue its use for student accommodation. The Cabinet decision of June 2011, which gave consideration to the UC's participation in the NRAS, similarly attests to the understanding in the ACT Government that the transfer would facilitate development of student accommodation. Arscott House, however, could not be used for the purpose of NRAS accommodation and the receipt of NRAS Incentives as it was existing property.

Cabinet Submission (December 2011)

2.28 In December 2011, a Cabinet submission prepared by the Economic Development Directorate in relation to the direct sale of Arscott House noted *inter alia*:

- the inter-agency Direct Sale Panel had considered the UC's application for a direct sale of Arscott House and had satisfactorily demonstrated that the direct sale was consistent with the UC's functions and was the most suitable land for the proposed use, the UC had the necessary funding capacity to continue to maintain and manage the property and the use of the land by the UC was consistent with its operations as a university (section 6 of the *University of Canberra Act 1989*);
- the ACT Government was not currently receiving any income from the UC in relation to Arscott House; and
- the UC had advised it needed 'off-campus' assets like Arscott House to enable it to raise the finance required to progress the university's student accommodation strategy.

2.29 The Cabinet submission noted:

> ... although Arscott House is a Government asset, the Government does not currently receive any income from it. The book value of the asset has been assessed as $4.8 million and this was highlighted as a budget impact in the submission. The value of the contribution for NRAS purposes is equivalent to market value which was estimated to be $9 million.
>
> The UC has stated that it needs "off campus" assets like Arscott House to enable it to raise the finance required to progress the University's student accommodation strategy. The University's on-campus assets cannot be used as security for loans because the finance provider cannot realise the assets should it need to do so.
>
> Therefore, a direct sale of Arscott House to UC at no cost would provide significant benefit to the University.

Cabinet decision

2.30 On 14 December 2011, Cabinet agreed to the direct sale of Arscott House to the UC for $0 (essentially a gift). As part of its decision, Cabinet noted 'the transfer represents an estimated $9 million of the required $22.85 million in support from the ACT Government which is required under NRAS' and 'the transfer will assist UC to develop additional student accommodation places because it will be recognised as an asset that the University of Canberra can use to secure finance against.'

2.31 On 20 December 2011, a letter of offer was sent to the Vice Chancellor of the UC for the granting of a 99 year crown lease over Arscott House. The terms of offer for the lease stated:

> The grant of a crown lease to the university represents part of the contribution from the ACT Government required under the National Rental Affordability Scheme (NRAS).

2.32 The lease for the property (executed on 21 December 2011) specified that the UC was 'to use the premises only for the purpose of educational establishment', which is defined as 'use of the land for the purpose [sic] tuition, training or research directed towards the discovery or application of knowledge, whether or not for the purposes of gain, and may include associated residential accommodation.'

2.33 On 19 December 2011, the ACT Property Group transferred Arscott House to the UC. In accordance with accounting standards, the ACT Government recorded the value of Arscott House as $5.0 million, while the UC recorded the value at $9.0 million (in its financial statements as both an addition to its Property, Plant and as State and Local Government Financial Assistance revenue). The $9.0 million represented fair market value, although this highlights the benefit obtained by the UC from the transaction.

Timing of the transfer of Arscott House

2.34 The transfer of Arscott House in December 2011 was important to the UC, notwithstanding that there were no specific time pressures for the purposes of the NRAS, including not before the end of December 2011.

2.35 For example, in response to a request for a delay in the consideration of the transfer of Arscott House to early 2012, the Vice Chancellor of the UC noted:

> It is imperative that Arscott House go through. We have pressed and pressed on this. Yes, it is important for the UC 2011 result.

2.36 The UC has since advised that the transfer of Arscott House provided the security of a renewed lease before any capital investment was made in the facility.

2.37 The UC reports its financial statements on a calendar year basis. In accordance with relevant accounting standards, the transfer of Arscott House in December 2011 allowed the UC to report an amount of $9.0 million as revenue. In 2011, the UC made an operating surplus before tax of $10.1 million.

Subsequent use of Arscott House

2.38 At present Arscott House is not available for student accommodation. The UC advised that it closed in 2015 while options for its future use were being considered. The UC also advised that a decision on capital expenditure to upgrade Arscott House is pending and negotiations are underway with one of the UC's student accommodation providers, with a view to the accommodation provider taking responsibility for the premises.

UC request for increase in borrowing limit to $80.0 million (February 2011)

Vice Chancellor letter to Treasurer

2.39 On 11 February 2011, the Vice-Chancellor of the UC wrote to the Treasurer requesting an increase in the UC's total borrowing limit to $80.0 million. At the time of the request, the UC could only borrow up to $20.0 million. The UC was seeking funding to support its 'wide-ranging reform and revitalisation program', which required large capital investments to expand campus facilities, address a backlog of maintenance and 'fund strategic infrastructure projects which will promote the University's long-term sustainability through appropriate use of its extensive campus.'

2.40 In the letter the Vice Chancellor of the UC noted:

> ... the University has been undertaking a wide-ranging reform and revitalisation program. This is a multi-year undertaking involving structural, operational and infrastructural improvements focused on the Bruce campus. The next phase of our program will require large capital investments as we expand campus facilities, address a backlog of maintenance which, as the then Commonwealth Department of Education, Science and Training pointed out at the time of my arrival in 2007 was already at a critical stage, and fund strategic infrastructure projects which will promote the University's long-term sustainability through appropriate use of its extensive campus.

Loan facility of $23.4 million and cash grant of $6.0 million (March 2011)

2.41 In March 2011 a submission was lodged with Cabinet seeking Cabinet's agreement to provide a $23.4 million loan facility and a $9.0 million cash grant to the UC for the purchase and refurbishment of Wing 5 of Cameron Offices in Belconnen. The Cabinet submission identified that the UC planned to refurbish the property from office accommodation to student accommodation for 212 students.

2.42 The Cabinet submission identified that the UC was seeking to expand its enrolment numbers and was expecting an increase in international student numbers. The advice identified 'a growth in international student numbers will place considerable stress on the existing accommodation infrastructure within the education sector, leading to increased pressure on affordable housing more broadly' and that the 'current shortage of student accommodation may also pose a capacity constraint that could limit future growth within the education industry.'

2.43 The Cabinet submission sought assistance in the form of:

- a $23.4 million loan facility to the UC at an interest rate of 6.5 percent per year; and
- a contribution of $9.0 million in total to be paid as a grant of $1.0 million per year over nine years.

2.44 The Cabinet submission noted:

- the UC was seeking to expand its enrolment numbers from 2012 onwards (when the Commonwealth funding model was expected to change so that funding was no longer capped, providing an incentive to maximise enrolment numbers);
- an expected growth in international student numbers would place considerable stress on existing accommodation infrastructure, leading to increased pressure on affordable housing more broadly;
- there was a current shortage of student accommodation, that could pose a capacity constraint that could limit future growth within the education industry;
- tertiary institutions (and the UC more specifically) did not have the capacity to use their own capital resources to fund such projects;
- the redevelopment of Wing 5 of the Cameron Offices in Belconnen would help the UC to compete with Sydney and Melbourne for international students as the UC could offer enrolments with accommodation; and
- the UC was unable to finance the project without assistance because most of the UC's assets are on-campus and unable to be realised, and the assets cannot be used as security to seek finance.

2.45 The submission proposed a $23.4 million loan to the UC and a grant of $9.0 million to be paid over 9 years. The rationale for the grant was:

> ... the short life of the refurbishment (only twelve years) which, if correct, means the University would carry a non-productive loan for the final thirteen years. The $9 million grant would release University funds for other works.

2.46 Cabinet was requested to make a decision quickly, with the UC requesting that a decision be made by April 2011, in order for construction to commence in time for the 2012 academic year.

2.47 On 21 March 2011, Cabinet agreed in-principle to support the UC to purchase and redevelop Cameron Wing 5. The agreement-in principle was provided:

> ... subject to further work clarifying the:
>
> a) loan details;
>
> b) the possibility of using unallocated funds from the 'Tune-Up Program'; and
>
> c) whether the Change of Use Charge is applicable.

2.48 Cabinet agreed that support would be provided to the UC in the form of:

- a $23.4 million loan facility, at an interest rate of 6.5 percent per annum; and
- a $6.0 million grant, to be paid over nine years. ($3.0 million less than what was requested).

2.49 The Cabinet decision noted *inter alia*:

- ... the new student facility would enable the UC to attract an additional 212 students per annum to the ACT and enable then to compete more effectively with other jurisdictions for international students in the future;
- the value of the low interest loan was equivalent to $2.8 million and the total assistance package equated to $8.8 million; and
- the UC was a significant contributor to the ACT economy and international education was the second largest export industry in the ACT.

2.50 In July 2011, the UC signed a loan agreement with the ACT Government for $23.4 million. The agreement stipulated that this funding was intended to provide funds for the construction of affordable off campus accommodation for students at UC.

Request for cash advance facility of $56.7 million (April 2011)

2.51 On 12 April 2011, a Cabinet submission was made seeking approval for 'Cabinet agreement to establish a cash advance facility for the University of Canberra (UC) to enable them to undertake a range of property development, capital works and infrastructure renewal activities.'

2.52 The Cabinet submission sought Government approval for:

- the establishment of a cash advance facility for the UC for the purposes of property development, capital work activities and renewal of University infrastructure;
- the value of the cash advance facility not to exceed $56.7 million;
- each draw down to relate to a specific initiative endorsed by the UC Board and the ACT Government;
- each funding initiative would be assessed on its merits and the cash advance facility would include mechanisms to enable the adoption of appropriate terms and conditions;
- initiatives over $5 million to require the Treasurer's approval; and
- the facility to be provided for an initial period of 15 years.

2.53 As part of the Cabinet submission, it was noted:

- impending changes to Commonwealth funding would provide incentives for universities to maximise their enrolment numbers and would result in more direct competition for international students in particular; and

- the UC had developed its *Accommodation Strategy 2011-15* (February 2011), and that the strategy 'aimed to increase its proportion of international students from 19 per cent to 25 per cent over the next four years.'

2.54 The Cabinet submission also noted tertiary institutions generally did not have the capacity to use their own capital resources to fund major projects, with most assets held in the form of educational facilities that have no direct revenue producing potential, and that Government assistance was sought in the form of a loan facility to cover the costs of the proposed development activities.

Treasury analysis (April 2011)

2.55 In preparation for providing advice to Government, the Treasury Directorate analysed the UC's level of financial risk and its ability to pay debts, using financial information and ratios supplied by the UC. The Treasury Directorate highlighted a number of concerns with respect to the UC's capacity to repay its loan. In a briefing document prepared in relation to the submission it noted the submission 'contains no financial analysis demonstrating UC's ability to meet the ongoing servicing costs of any borrowings or evidence to support the UC's capacity to make any loan repayments.' In a briefing document prepared by the Treasury Directorate in relation to the Cabinet submission it was noted:

> The decision to approve an increased borrowing limit for UC must t*ake into a*ccount any potential financial risks that the Territory may ultimately be exposed to.
>
> > Notwithstanding any borrowing is unlikely to have an explicit government guarantee, by implication of approving the borrowing limit, a Treasurer's approval would recognise there is a sound financial basis and *business* case for the borrowings.
> >
> > In the event of any loan default by the UC, it would be possible that creditors could seek compensation from the Territory, recognising that the Territory's representative approved the borrowing limit and given the nature of UC's assets which are largely unrealisable and of limited commercial value for private sector lenders.

2.56 On 18 April 2011, the Budget Committee of Cabinet did not agree to the submission, as made, but otherwise agreed that:

a) relevant officials be authorised to work with the University of Canberra (UC) in the development of particular infrastructure proposals of mutual interest and benefit to UC and the Government, for which the Government may choose to provide some form of financial support; and

b) consideration be given to any such proposals on a case by case basis in future budget contexts.

Treasury analysis (June 2011)

2.57 In June 2011, the Treasury Directorate provided advice to the Treasurer with respect to the UC's February 2011 request for an increase in its borrowing limit. The advice recommended that the UC's borrowing limit be set at $70 million.

2.58 The advice stated:

> Authorising the borrowing limit requires the Territory to be prudent when establishing the limit. The authorisation of a level of borrowing could imply some form of indirect guarantee on the borrowing. In the event of a loan default by UC, creditors may seek compensation from the Territory if other avenues of compensation have been exhausted.
>
> This risk would be mitigated to the extent that the original decision to authorise the borrowing limit was taken following proper due diligence.

2.59 In support of its advice, the Treasury Directorate undertook an analysis of the UC's financial position and financial projections over a forward period of ten years. The Treasury Directorate advised the Treasurer:

> An examination of all key financial and financial risk ratios finds the financial measures fall within an acceptable range, indicating that a total borrowing not exceeding $70 million is not beyond UC's financial capacity.
>
> ...
>
> The financial capacity of UC to support a total borrowing at this time of $70 million is dependent on the UC maintaining a strict discipline of repaying borrowing over time in accordance with the budgeted financial projections provided to Treasury for analysis.

2.60 On 30 June 2011, the Treasurer approved an increase in the borrowing limit of the UC to $70.0 million through Treasury Instrument TI2011/7. The $70.0 million borrowing limit was the aggregate of $46.65 million in loans from other parties and $23.35 million by way of a loan from the Territory (refer to paragraphs 2.41 to 2.51).

Request for increase in borrowing limit to $220.0 million, including a $150.0 million Territory loan (March 2012)

Vice Chancellor letter to Chief Minister

2.61 On 9 March 2012 the Vice Chancellor of the UC wrote to the Chief Minister requesting an increase in the UC's total borrowing limit to $220.0 million, including a loan of $150.0 million from the Territory. The UC requested that the loan from the Territory be subordinated to loans from other non-Government lenders, i.e. the other non-government lenders would have the first opportunity to reclaim any payments from the UC. The UC requested the funding to 'assist the University manage and fund its structural reforms and infrastructure projects' including its student accommodation projects.

2.62 The letter stated:

> To assist the University manage and fund its structural reforms and infrastructure projects, I request your approval, as set out in more detail below, to create a separate debt of $150m in relation to student accommodation, subordinated to non-Government lenders, transfer the existing $22m loan from the ACT Government in

> relation to the Cameron Building into that $150m facility; and allow the University to incur borrowings for other purposes up to the existing limit of $70m.
>
> The upshot would be two areas of borrowing: up to $150m for student accommodation and up to $70m for other capital purposes as described in the following paragraphs.

2.63 The Vice Chancellor of the UC's letter explained that the $150.0 million funding would be used to support the construction of 1,000 NRAS supported student accommodation places and that the additional $70.0 million would be used for other capital projects.

2.64 The letter from the Vice Chancellor of the UC also noted:

> We [the UC] would like to discuss the subordination of this debt to non-Government lenders so that the University's balance sheet flexibility and access to funding markets for strategic requirements are preserved.

Treasury request for credit rating

2.65 To assist its decision-making, the Treasury Directorate requested that the UC provide information on its credit rating. The UC did not have an independent credit assessment at the time, nor has it obtained a credit rating since then.

2.66 In the absence of an independent credit rating assessment, the UC provided a copy of a credit assessment presentation made by one of its commercial lenders (Westpac) in December 2011. This presentation pre-dates the March 2012 request to the ACT Government for a total borrowing amount of $220.0 million. The credit assessment presentation concluded that:

> UC can increase its debt levels by $30 million and would retain an investment grade credit profile at 'A' levels. An increase in debt to $225 million would strain key debt protection measures and put downward pressure on the University's credit profile. To retain financial flexibility, UC should consider subordinating future loans from the ACT Government.

2.67 This assessment, while not independent, indicates that the UC was taking a very significant step in making its request, countenancing a move from a moderate financial risk position to a more aggressive leveraging stance, which would entail both stretching its debt holdings and becoming more reliant on the backing of the ACT Government to meet its repayment obligations. The UC advised, however, that expenditure would be incurred only after business cases were prepared and considered by the UC's governance committees. The UC also advised that there would be substantial benefit for the UC associated with new student accommodation.

Treasury Analysis (April 2012)

2.68 The Treasury Directorate advised the Treasurer on 12 April 2012 that the UC's proposal raised 'matters of concern'. The Treasury Directorate reiterated its earlier advice in relation to establishing a borrowing limit and how that might 'imply a form of indirect guarantee on the borrowing by the ACT Government to the UC' and that 'in the event of a

loan default by UC, creditors may seek compensation from the Territory if other avenues of compensation have been exhausted.'

2.69 The Treasury Directorate further identified 'a number of critical aspects of the UC borrowing limit increase that require examination' namely:

- 'the financial capacity of the UC to support a +200 per cent increase in the borrowing limit';
- 'the determination of an appropriate lending rate to apply to reflect the credit quality of the UC and the request that ACT Government loans would be subordinated to other lenders' and
- 'the impact on the Territory's cash position, and therefore borrowing requirements, and indeed the Territory's own credit rating'.

2.70 The Treasury Directorate considered 'the request to increase the borrowing limit to $220 million to be very significant due to the potential financial consequences.' In this respect, the Treasury Directorate identified 'the Territory's cash position is under pressure' and that 'based on the current budget position, new loans provided to UC will need to be funded by new external general government borrowings.'

2.71 In relation to the proposed subordination of the Territory loan to other loans with non-government providers, the Treasury Directorate identified the risks of such an arrangement, noting 'this means ACT Government provided loans would rank below claims of other lenders in the event of a call in of UC assets' and that 'as a lender, it is imperative that the Territory understands the risks associated with the investment and fully provides for these risks in the terms and conditions of any loan agreement.'

2.72 The Treasury Directorate noted that 'the UC has indicated that it has received advice from Westpac confirming the necessary financial parameters for an investment grade credit rating and that internal UC analysis confirms the capacity to support the increased borrowings'. However, the Treasury Directorate advised caution with respect to this information, noting that 'Westpac does have a potential conflict of interest on the grounds that it has an existing loan facility…'

2.73 The Treasury Directorate also noted:

> Treasury has no basis for assessing the extent to which Westpac, or any other external lender, may or may not make allowances in a credit assessment of any implicit ACT Government guarantee.

2.74 The Treasury Directorate recommended that 'UC obtain a formal credit rating from a suitably, qualified, independent organisation such as Standard & Poors (S&P)'.

2.75 The Treasurer subsequently wrote to the Vice Chancellor of the UC indicating that in order for the ACT Government to consider the UC's request it would need to undertake extensive due diligence, and requested that more information be provided to support this

analysis. The Treasurer informed the Vice Chancellor of the UC that a decision on funding would not be taken until such time as the due diligence was completed.

Cabinet submission

2.76 In April 2012, the Economic Development Directorate was preparing a submission for Cabinet in relation to the UC's request for an increase in its borrowing limit and a Territory loan. In relation to a draft Cabinet submission prepared by the Economic Development Directorate the Treasury Directorate further reiterated, in correspondence to the Economic Development Directorate, that it did not support the submission and that fundamental due diligence and financial analysis was required on the proposal.

2.77 On 20 April 2012, the Treasury Directorate noted:

- any decision to increase the University's borrowing limit would have potential consequences for the Territory's budget, credit rating and the Territory's own borrowing program;
- fundamental due diligence and analysis of the financial projections and risks associated with the proposed arrangements needed to be undertaken in order for properly constructed advice to be provided; and
- it would be appropriate for the UC to obtain a formal stand-alone credit rating from a suitably qualified, independent organisation such as Standard & Poors (S&P).

2.78 On 7 June 2012, a Cabinet submission was lodged by the Economic Development Directorate recommending *inter alia*:

- authorising the UC to borrow up to $220.0 million, being the aggregate of $150.0 million in loans from the Territory and $70.0 million in loans from parties other than the Territory;
- extending a line of credit to the UC up to $150.0 million to fund the development of student accommodation on the UC Bruce campus, at a rate 0.75 percent above the costs of finance to the Territory; and
- subordinating the UC's debt to the Territory to non-Government lenders.

2.79 The Cabinet submission identified that the additional funding would support the UC's growth strategy and plans to grow the number of students at the UC. The Cabinet submission also identified that the subordination of the Territory's debt to non-Government lenders would assist in giving the UC's balance sheet flexibility and in ensuring that its access to funding markets for strategic requirements was preserved. The Cabinet submission identified that, should the Territory be unwilling to agree to such an arrangement, a potential alternative arrangement was to provide for the full $220.0 million loan amount to be provided by the Territory.

2.80 The Cabinet submission noted:

- the UC's aim was to grow student numbers to 16,100 Equivalent Full-Time Student Load (EFTSL) by 2018 and that this would increase the number of interstate and international students staying at the UC and would increase the demand for student accommodation;
- the economic benefits to the ACT from the growth in student numbers would be significant and would include benefits from:
  - expenditure generated by increases in interstate and overseas students;
  - substantial increase in staff to support students (of around 400 full-time ongoing staff and 400 part-time and casual staff); and
  - average construction employment of 100 jobs per day (peaking to 150 jobs) over the period of construction; and
- while the UC had initially had the intention of financing its student accommodation project through BOOT [Build Own Operate Transfer] schemes, the UC's preference was to finance the project *via* a low-interest loan facility from the Government as it would be a lower cost option.'

2.81 The Cabinet submission further noted:

- demand for student accommodation was very high and expected to grow over the next few years and that the likelihood of default on the loan was low;
- the student accommodation developments at UC represented valuable core infrastructure for building the University in line with the Government's 2011-12 priorities for an 'increase in student accommodation places' and 'support for the expansion of our tertiary institutions' as well as serving to reduce pressure on the wider rental market, thereby alleviating housing stress for others seeking rental accommodation;
- the subordination of the ACT Government debt to non-Government lenders would give the University's balance sheet flexibility and ensure that its access to funding markets for strategic requirements was preserved; and
- should the Territory be unwilling to agree to the subordination, an alternative would have been for the Government to extend the limit on the University's capacity to borrow from the Territory to allow the Territory to fund its strategic program activities entirely from Government borrowings, i.e. a Territory loan of $220.0 million with no private sector component.

Independent advice sought on the UC's credit-worthiness

2.82 On 4 June 2012, the Treasury Directorate sought external technical advice with respect to a 'high level assessment of the University of Canberra's (UC) Credit Worthiness as a stand-alone institution'. The Treasury Directorate sought advice on 'whether, and to what extent UC would be able to borrow in its own right', with specific advice sought in relation to:

- the credit worthiness of the UC as a stand-alone institution, noting that 'if UC supplied the contained proposal to a bank, seeking funding on commercial terms, what would be the likelihood of UC being granted credit approval'; and
- 'would UC's credit proposal be sufficient (in content) to seek a loan as a stand-alone entity on commercial terms'.

2.83 The independent advice noted that the 'underlying credit is implied government backed quality and risk' and that 'a Bank's credit team may assess the application in a more favourable light, therefore standard credit terms may not apply' and that 'the final structure of the facilities would significantly influence the decision process.'

2.84 The advice expressed doubt that the UC would be able to borrow the funds it was requesting in its own right from non-government lenders.

2.85 The advice also noted *inter alia*:

> If UC were to apply for senior debt facilities totalling $220m (being the combined total of requested funding parcels...on a pure commercial basis (as a commercial trading entity) UC would be unlikely to obtain approval. The combined debt parcel would place UC well outside key bank ratios, in particular Debt/Leverage, Interest Cover and Debt Cover ratios. All of these ratios would tend to indicate an inability for UC to service and pay down the requested funding within standard commercial terms.

2.86 However, the independent advice also identified that there may be circumstances in which banks may give the UC's application favourable treatment, including:

- placing covenant restrictions on the use of the loan facilities, which 'would strictly restrict the terms and conditions under which the UC may draw on the facility, therefore placing the facility outside of ratio analysis';
- diversifying non-income generating assets so as to either 'pre-commit to pay down senior debt via asset sale' or 'generate additional revenue sources from new rental/leaseback opportunities'; or
- by treating the application as government risk.

2.87 In relation to the quality of information provided by the UC in its proposal, the independent advice noted 'it is our view that UC would be required to submit significantly more information for a Bank's Credit department to assess the proposal on commercial terms'.

2.88 The due diligence process that the Treasury Directorate undertook for the March 2012 request from the UC reflected a significantly increased level of risk to the UC and the ACT Government, inherent in a request for $220.0 million in total borrowings, of which $150.0 million would be subordinated Territory lending. The Treasury Directorate identified the potential impacts on the UC and also on the Territory's cash position, budget balance and credit rating. The Treasury Directorate's strategy of using external expert advice was appropriate, and its recommendations were consistent with this advice. The Treasury

Directorate's advice reduced the exposure of the ACT Government to significant financial risk.

2.89 In a decision on 12 June 2012, Cabinet did not agree to the proposed increase in the UC's credit limit (to $220.0 million) or increase in the Territory's lending (to $150.0 million). The Cabinet decision aligned with the advice provided by the Treasury Directorate.

Request to increase borrowing limit to $120.0 million, including a $50.0 million credit facility (July 2012)

2.90 On 23 July 2012, the Economic Development Directorate prepared a Cabinet submission seeking agreement to *inter alia*:

- increase the borrowing limit of the UC to $120.0 million to enable the University to borrow funds to finance the development of on-campus accommodation; and
- extend a line of credit under subsection 59(9) of the *Financial Management Act 1996* to allow the University to finance the building of the first tranche of its new student accommodation program.

2.91 The Cabinet submission identified that the funds are 'justified in terms of the achievement of strategic objectives, including as an option to fulfil the Government's earlier commitment to support UC's NRAS application' and that there was an urgent need for the funds to support 'an urgent start to the work in order for the University to meet the construction schedule for an opening to the student accommodation in first semester 2014.'

2.92 The Cabinet submission provided options including:

- increasing the UC's borrowing limit to allow the UC to borrow the money from private banking sources to finance the construction; or
- increasing the UC's borrowing limit *and* extend to the University a line of government credit sufficient to finance the construction which the University would pay back on agreed terms.

2.93 The Cabinet submission noted that the first option was the preferred option, noting that having to raise funds from private sources would delay the commencement of construction beyond the date required to ensure that the accommodation is ready for the first intake of students in 2014.

2.94 In July 2012 Cabinet agreed:

- to increase the UC's borrowing limit to $120.0 million (from $70.0 million) 'to enable the University to finance the development, which is the subject of the business case attached to the Submission';

- to extend a line of credit for up to $50.0 million 'to fund the first tranche of the UC student accommodation building program ... subject to the Minister for Economic Development bringing a further Submission to Cabinet for confirmation'; and
- that 'the further Submission is to provide details of the contractual terms of the proposed line of credit, as well as detailed legal and financial information relating to property agreed by the University, to be used to secure the loan. This should include advice of all other existing financial interests held over University property'.

2.95 On 20 August 2012, the Treasurer approved an increase in the borrowing limit of the UC to $120.0 million through Treasury Instrument TI2012/12. The $120.0 million borrowing limit was the aggregate of $46.65 million in loans from other parties, $23.35 million by way of a loan from the Territory and $50.0 million which was to be provided by way of a credit facility from the Territory.

Request to increase borrowing limit to $144.0 million, including a $24.0 million credit facility (April 2013)

2.96 On 19 April 2013, the Economic Development Directorate lodged a Cabinet submission to Government which sought to:

- increase the UC's borrowing limit to $144.0 million (from $120.0 million) 'to enable the University to borrow funds to finance the purchase and refurbishment of Wing 4 Cameron offices'; and
- extend the line of credit for up to $24.0 million 'to fund the purchase and refurbishment of Wing 4 Cameron offices'.

2.97 The Cabinet submission noted:

- the request brought forward another component of the University's request for support which is for funding via a Government credit facility under subsection 59(5) of the *Financial Management Act 1999*; and
- the UC was seeking a line of credit from the government for $24.0 million to purchase and refurbish the building, at a rate which was 0.75 per cent above the rate at which the government is able to borrow the funds. The University proposes to repay the loan in full by 2028.

2.98 The Cabinet submission further noted two options for the Government, either partial or full support, as follows:

- increasing the University's borrowing limit to allow the University to borrow money from private banking sources to finance the construction. This option would also include the UC using its cash reserves (estimated at probably no more than around $8 million during the period of construction); or

- increasing the University's borrowing limit and extending to the University a line of government credit of $24 million under the provisions of which the University would then pay back on agreed terms.

2.99 The Cabinet submission advised that the project could only be achieved in the timeframe available under the second option.

2.100 On 1 May 2013, the Budget Committee of Cabinet agreed:

- to the increase in the UC's borrowing limit to $144.0 million 'to enable the University to borrow funds to finance the purchase and refurbishment of Wing 4 Cameron offices';
- to extend the line of credit for up to $24.0 million 'to fund the purchase and refurbishment of Wing 4 Cameron offices'; and
- 'that final release of the funds will be subject to an independent financial assessment of the University's financial position, which will be commissioned by Treasury and funded by the University, and to be concluded by 6 June 2013'.

2.101 On 7 May 2013, the Treasurer approved an increase in the borrowing limit of the UC to $144.0 million through Treasury Instrument TI2013/6. The $144.0 million borrowing limit was the aggregate of $46.65 million in loans from other parties, $23.35 million by way of a loan from the Territory and $50.0 million and $24.0 million which was to be provided by way of two credit facilities from the Territory.

External financial assessment

2.102 In May 2013 an external consulting firm (KPMG) was commissioned by the Treasury Directorate to 'assist with an analysis of the CW4 project [construction and operation of the Cameron Wing 4] and the resultant impact it will have on UC's financial position, particularly with respect to debt servicing.' The consulting firm's advice noted:

- on a "stand-alone" basis (defined as without implicit or explicit government support), the 'UC has limited capacity beyond the CW4 and Sporting Commons projects to undertake additional debt funded capital projects until key financial metrics return to at least an "intermediate" level based on S&P benchmarks';
- 'as the UC is entering into a period of significant financial risk, UC has diminished capacity to sustain shocks and maintain adequate liquidity levels. Failure to achieve projected student growth will exacerbate this financial risk'; and
- the UC has some financial flexibility through the ability to 'delay discretionary capital expenditure projects' and 'monetise their investment in student accommodation.'

2.103 In a subsequent briefing to the Treasurer dated 31 May 2013, in relation to the external consulting firm's advice, the Chief Minister and Treasury Directorate advised 'we note that the UC is going through a significant growth phase and based on the student accommodation business cases and funding commitments, this phase necessitates an

increase in debt levels to achieve the growth. An increased level of financial risk is an unavoidable consequence.'

2.104 The Chief Minister and Treasury Directorate further advised:

> Noting that Cabinet has provided in-principle support to UC's plans to grow University enrolments and add to its existing accommodation stock, this recognises that the Government is providing an element of imbedded support to the UC to the extent that the UC's risk profile may be such that external financing may otherwise not be available.
>
> The ongoing question for the Government is therefore, whether this amount of support has reached an upper limit for the moment.
>
> As highlighted in the [external consulting firm] review, the most significant risk that the UC is exposed to over the next few years is the achievement of the targeted growth in student numbers and accommodation occupancy rates.
>
> We consider it crucial therefore, that both parties, the Government and the UC, are attuned to the student growth task. Taking on the additional risk means that the UC will need to have an absolute focus on achieving the growth strategy targets which may require, at least initially, deferring new capital projects and prioritising other discretionary capital expenditure.
>
> Notwithstanding the current risk profile of the UC, the UC does have some financial flexibility to manage emerging cash flow pressures. To the extent that the UC is able to maintain discipline with regard to the achievement of the growth strategy, the financial estimates indicate a return to an 'intermediate' financial risk level after around three years.
>
> All future UC capital project proposals seeking Government support, by way of loan funding or explicit guarantee, should be presented to the Government for review in the form of a comprehensive business case. Financial and economic analysis on a basis similar to that undertaken in the [external consulting firm] review, should support any business case. This is consistent with the previous Cabinet decision...

2.105 A due diligence process for the proposed loan of $24.0 million for Cameron Wing 4 was undertaken. As in the case of previous due diligence analysis, it was appropriate and provided a sound foundation for the advice provided to the Treasurer.

2.106 The process for assessing the UC's request for debt funding for Cameron Wing 4 highlights the importance of due diligence processes. The due diligence analysis conducted by the external consulting firm on behalf of the Treasury Directorate in May 2013 identified that '[the] UC has limited capacity beyond the [Cameron Wing 4] and Sporting Commons projects to undertake additional debt funded capital projects until key financial metrics return to at least an "intermediate" level based on [Standard & Poors] benchmarks.' This implied that it was nearing its capacity to manage debt as a standalone entity, and that further applications could place the ACT Government in the position of subordinate debtor, a position that could only be contemplated with a very clear understanding of the impacts on the Budget and the Territory's financial position and credit rating.

2.107 Following the provision of the external consulting firm's report, an agreement was signed between the Territory and the UC on 25 June 2013 for the provision of the $24.0 million credit facility for the redevelopment of Cameron Wing 4.

2.108 The due diligence activities undertaken by the Chief Minister and Treasury Directorate were conducted without the benefit of the UC having an independent credit rating from a recognised credit rating agency. While an independent credit rating should not be the sole basis on which the ACT Government makes decisions with respect to the provision of financial and other support to the UC, such a rating would have provided the Chief Minister and Treasury Directorate with a stronger basis on which to conduct its due diligence activities.

RECOMMENDATION 1 UC CREDIT RATING

The ACT Government should require the UC to provide an independent credit rating from a recognised credit rating agency before considering any further financial or other support for the UC.

3 ASSESSMENT OF PERFORMANCE

3.1 This chapter discusses the performance of the UC with respect to the provision of affordable student accommodation. It also provides information on the UC's financial position and examines its capacity to repay its loans.

Summary

Key findings

	Paragraph
An analysis of the UC's performance in supplying student accommodation shows the UC's accommodation supply targets, as provided for in the UC's *Accommodation Strategy 2011-15* (February 2011), have not been met. For example, in 2015 2,230 beds are available, which is 882 beds (28.3 percent) fewer than the target of 3,112. The closure of Arscott House for student accommodation in 2015 has reduced the UC's ability to achieve its targets. The UC advised that this closure is temporary.	3.4
The UC's target for the development of 1,000 NRAS dwellings has not been met. The UC has forfeited 43 of its 648 'Phase 1' NRAS allocations and achievement of the remaining 352 'Phase 2' NRAS allocations is at risk. This may result in the UC only delivering 60 percent of its NRAS dwelling targets by 2016. While this is the case, the UC advised that this reflects prudent decision-making on its part. The UC advised that a number of options for meeting this target had been considered, but it has not been satisfied with any commercial arrangements proposed.	3.10
An analysis of the UC's NRAS eligible student accommodation shows: • the UC's 605 NRAS eligible dwellings are a mix of studio rooms and apartments, with anywhere between one to seven beds in the dwellings; and • the UC's 605 dwellings include 896 beds. However, up to 926 individuals may be accommodated in these rooms, as 30 of the rooms are double rooms, and may support up to two people.	3.17
An analysis of the occupancy rates of UC's student accommodation properties shows: • the dwelling occupancy rates and bed occupancy rates of the UC's NRAS-eligible student accommodation have increased over time; and • the dwelling occupancy rates for the NRAS-eligible accommodation consistently exceeds the bed occupancy rates of the NRAS-eligible occupation. This is because a dwelling is considered to be fully	3.19

occupied even if only one of the multiple beds that are available within the dwelling are occupied. In this situation the dwelling occupancy rate will exceed the bed occupancy rate.

Between 2011 and 2014 the bed occupancy rate of Arscott House declined from 99.1 percent in 2011 to 57.5 percent in 2014 (99.1 percent in 2011, 91.6 percent in 2012, 75.2 percent in 2013 and 57.5 percent in 2014). Arscott House has not been available for student accommodation purposes in 2015. The UC advised that the decline in Arscott House occupancy was due to issues associated with the management of the facility. The UC further advised that it decided not to make the Arscott House available for student accommodation purposes in 2015, to enable it to make an assessment of options to refurbish and manage the facility. 3.20

ACT Government objectives for providing financial and other support to the UC are implicit in the reasoning for the provision of financial support in the Cabinet documentation, and include: 3.21

- increasing the supply of affordable accommodation to students;
- achieving economic benefits for the ACT; and
- alleviating pressure on the broader ACT rental market.

The ACT Government has not assessed whether the expected economic benefits associated with the provision of financial support to the UC have been achieved or whether the supply of accommodation by the UC has alleviated pressure on the broader rental market. However, evaluating the direct effects of the additional supply of accommodation by the UC from the ACT Government's financial and other support would be difficult at this time as these benefits may not be realised until some time in the future. 3.39

A consideration of the ACT Government in providing financial support to the UC was to provide support without adverse fiscal consequences to the Territory. A key risk that the ACT Government sought to avoid was the inability of the UC to repay its debt. 3.40

An analysis of the UC's debt to equity ratio shows: 3.62

- the UC's debt to equity ratio increased significantly between 2005 and 2013, before declining in 2014. This shows that, between 2005 and 2013, the proportion of debt maintained by the UC increased at a faster rate than its equity. The primary reason for the decline in the debt to equity ratio in 2014 was the UC's repayment of a significant amount of its debt it owed to the ACT Government in November 2014, as a condition of the ACT Government's agreement for the UC to sell its NRAS entitlements to Westpac. The UC advised that between 2005 and 2013, it had used debt to finance its growth and renewal strategy and that this would explain why its debt has increased at a faster rate than its equity; and

- when compared to a selection of five other universities, the UC's debt to equity ratio was the third lowest in 2008 and in 2013 significantly exceeded that of the other universities included in the audit analysis, which the UC advised is due to a greater reliance on debt as the source of funding for its growth and renewal strategy.

3.63 The UC advised that it recognises that the debt to equity ratio increased substantially compared to other universities however, the UC also advised that it considered this to be necessary to pursue a growth strategy to sustain the UC's long term future. It further advised that it does not have the advantage of a large investment or endowment portfolio or access to significant state grants. The debt to equity ratio declined in 2014 and the UC advised that its financial position is being carefully managed by the UC and its Council and that this will continue.

3.70 Westpac and the UC entered into an agreement on 25 November 2014 for the sale of 605 NRAS entitlements. In return for the sale of the NRAS entitlements, the UC received a cash payment of $42.4 million. Under this arrangement, the UC has relinquished any claims to future NRAS Incentives (which will now be received by Westpac) but does, as Westpac's agent, retain responsibility for managing the NRAS-eligible dwellings. The agreement allows Westpac to recover from the UC any future NRAS Incentives that are not paid by the Commonwealth Department of Social Services in the event that the UC does not continue to meet the ongoing eligibility requirements (e.g. occupancy rates).

3.71 As a condition of the ACT Government's approval for the sale of the NRAS entitlements, the UC has used the amount received to:

- fully repay its debt to the ACT Government relating to the Cameron Wing 4 loan; and
- make an early repayment of $18.5 million to the ACT Government relating to the Cooper Lodge loan. The UC now only has one loan from the ACT Government (relating to Cooper Lodge), the outstanding balance of which stands at $31.4 million as at 31 December 2014.

3.75 The sale of its NRAS entitlements provided an immediate cash receipt of $42.4 million for the UC. As a condition of its approval for the arrangement, the ACT Government ensured that the proceeds from the sale were used to pay some of the debt that the UC owed to the ACT Government. The sale has therefore had the effect of reducing aspects of the UC's more immediate financial liabilities (i.e. its debt to the ACT Government) while creating another ongoing financial liability for the UC. The ongoing financial liability places an onus on the UC to ensure that it maintains occupancy levels of its NRAS-eligible dwellings. Should the UC not be in a position to maintain occupancy levels of its NRAS-eligible dwellings, there are contractual remedies open to Westpac to recover payment from the UC. While not maintaining occupancy levels was an existing risk for the UC (as Australian

Government payments were contingent on this), there is now an additional incentive for the UC to maintain these levels, as Westpac may seek payment from the UC should Australian Government NRAS payments not be forthcoming.

As at 31 December 2014, the UC had the capacity to borrow up to $20.0 million from non-Government lenders, i.e. $19.0 million in loans from non-ACT Government lenders (i.e. $70.0 maximum borrowing limit less $51.0 million currently borrowed) and a $1.0 million bank overdraft facility with a non-Government lender. 3.78

The UC's cash flows for 2014 showed that the UC does not generate significant net inflows from its operations. The UC advised, however, that timing issues associated with the receipt and expenditure of grants has also impacted its net cash flows. Net cash inflows from operations are necessary for the UC to repay its debts. The UC's 2014 financial model indicates that it expects to improve its net cash inflows from operations and its capacity to repay its debts over 2014 to 2018. However, there are risks associated with achieving this. 3.88

The UC is reliant on increasing student revenue to generate operating surpluses. By 2018 the UC plans to enrol 16,500 full-time equivalent students. In 2014 the UC's equivalent full-time student load was 11,125 (a 3.5 percent increase on its 2013 equivalent full-time student load). The UC will need to increase its equivalent full-time student load by 48.3 percent between 2014 and 2018 to achieve its goal of 16,500 full-time equivalent students. 3.89

The UC's first semester enrolments for 2015 were 5,585 full-time equivalent students, as compared to 5,568 for the same period in 2014 (an increase of 0.3 percent). The UC's plan to increase its full-time equivalent student numbers by 48.3 percent between 2014 and 2018 is at risk if the trend between 2014 and 2015 first semester student enrolment numbers continues. 3.91

The UC advised that some of this growth will be outside Canberra through partnerships in Melbourne, Sydney and Brisbane as well as through growth in international students studying in Canberra. 3.92

Changes to the UC's business environment that affects student numbers will present a risk to the achievement of the UC's financial goals and its ability to repay its debts. It is noted, however, that other universities are likely to be facing similar challenges to those confronting the UC with respect to increasing student numbers. 3.93

The UC also advised that there were strong reasons for its growth strategy and that capital investment, including investment in student accommodation, has been an important part of this growth strategy, much of which has been financed from 3.102

borrowings. The UC acknowledges that the level of debt has increased (and that there are increased financial risks associated with this) but that these have been and will continue to be managed through its governance and oversight arrangements.

There are risks associated with the UC's capacity to repay its debts to the ACT Government. There are, however, options available to the UC to reduce expenditure and obtain income in order to meet its debt obligations. These include reducing expenditure, deferring capital projects, and entering into partnerships for the development of the UC campus. It is important that the risks to the Territory are monitored and reported to the Chief Minister and Treasurer. 3.105

UC objectives for obtaining financial and other support from the ACT Government

3.2 A key feature of the UC's requests for ACT Government assistance was to increase the supply of accommodation to students under the auspices of the National Rental Affordability Scheme (NRAS). The UC's explicit recognition and reliance on the NRAS, including the substantial financial support it offered through NRAS Incentive payments from the Commonwealth, was a means of achieving the development and delivery of student accommodation.

UC provision of student accommodation

Increasing the supply of accommodation to students

3.3 As discussed in paragraphs 1.44 to 1.54, the UC's *Accommodation Strategy 2011-15* (February 2011) identified a series of targets for the provision of accommodation to students. Table 3-1 shows key targets identified in the *Accommodation Strategy 2011-15* (February 2011) and the UC's performance in meeting these targets.

Table 3-1 Supply of accommodation by the UC (2012 to 2015)

	2012	2013	2014	2015
Total beds required (50% target)	**2,837**	**2,972**	**3,042**	**3,112**
Achievement	**1,853**	**1,767**	**2,444**	**2,230**
Arscott House	214	214	214	0
Campus Living Village	1,420	1,334	1,334	1,334
Weeden Lodge Wing 5	219	219	220	220
Weeden Lodge Wing 4	-	-	260	260
Cooper Lodge	-	-	416	416

Source: Audit Office, based on information provided by the University of Canberra

3.4 An analysis of the UC's performance in supplying student accommodation shows the UC's accommodation supply targets, as provided for in the UC's *Accommodation Strategy 2011-15* (February 2011), have not been met. For example, in 2015 2,230 beds are available, which is 882 beds (28.3 percent) fewer than the target of 3,112. The closure of Arscott House for student accommodation in 2015 has reduced the UC's ability to achieve its targets. The UC advised that this closure is temporary.

3.5 The UC advised that the availability of fewer beds than that envisaged in the UC's *Accommodation Strategy 2011-15* (February 2011) is not considered by it to be a 'failure' but is reflective of prudent decision-making. The UC advised that a key consideration is that all first year students and all international students are currently guaranteed accommodation.

NRAS-eligible accommodation

3.6 As discussed in paragraph 1.65, a total of 1,000 NRAS Incentives for 1,000 dwellings were allocated to the UC for the purpose of the NRAS. As part of the conditions for approval, the UC was required to complete and make available:

- 648 dwellings by 1 July 2014; and
- 352 dwellings between 1 July 2015 and 30 June 2016.

3.7 Table 3-2 shows the UC's performance in achieving its NRAS Incentive allocation.

Table 3-2 NRAS dwelling availability

Property	No of dwellings	Available
Weeden Lodge Wing 5 (220 beds)	174	Early 2012
Weeden Lodge Wing 4 (260 beds)	135	Early 2014
Cooper Lodge (416 beds)	296	Early 2014
Total	**605**	

Source: Audit Office, based on information provided by the University of Canberra

3.8 An analysis of the UC's performance in providing NRAS dwellings shows:

- the UC has developed 605 dwellings, which are currently available; and
- the UC has not completed a further 43 dwellings within the required timeframe.

3.9 As part of the conditions for approval for participation in the NRAS, the UC is required to complete and make available the remaining 352 dwellings. The UC has advised that completion of the remaining 352 NRAS allocations is 'at risk' of achievement by the 30 June 2016 deadline required by the Commonwealth Government under the NRAS.

3.10 The UC's target for the development of 1,000 NRAS dwellings has not been met. The UC has forfeited 43 of its 648 'Phase 1' NRAS allocations and achievement of the remaining 352 'Phase 2' NRAS allocations is at risk. This may result in the UC only delivering 60

percent of its NRAS dwelling targets by 2016. While this is the case, the UC advised that this reflects prudent decision-making on its part. The UC advised that a number of options for meeting this target had been considered, but it has not been satisfied with any commercial arrangements proposed.

Calculating NRAS performance

3.11 Section 4 of the *National Rental Affordability Scheme Act 2008* (Cth) provides for a definition of a rental dwelling for the purpose of the NRAS, as follows:

> **rental dwelling** means a dwelling for which rent is payable and includes:
>
> a) a part of a dwelling or building that is capable of being lived in as a separate residence; and
>
> b) a unit that is a dwelling; and
>
> c) any dwelling prescribed by the regulations to be a rental dwelling for the purposes of this definition;
>
> but does not include a caravan, houseboat, another kind of mobile dwelling or any dwelling prescribed by the regulations not to be a rental dwelling for the purposes of this definition.

3.12 The NRAS Guidelines further state:

> For the purposes of the Scheme, a rental dwelling will be considered to be able to be lived in as a separate residence where it can be demonstrated that a tenant, or tenants, would be able to live independently within the dwelling and not need to access external or common facilities. That is, the dwelling must provide the following:
>
> - A bathroom and kitchen facilities;
> - A bedroom and living space (the bedroom and living space may be combined within a single large room, as in the case of studio apartments); and
> - A separate lockable entrance which can be accessed either externally or via an internal hallway or common entrance. The entrance must not be accessed only through entering another dwelling.

3.13 Many of the UC dwellings eligible for NRAS Incentives have multiple bedrooms, e.g. a single dwelling may have a common kitchen, lounge and bathroom area and between two to seven bedrooms. Notwithstanding the number of bedrooms in each of the NRAS dwellings (and number of occupants), each NRAS dwelling is eligible for one NRAS Incentive.

3.14 Accordingly, should each of the NRAS dwellings have just one occupant and all other requirements are met, then the UC will be eligible to receive the NRAS Incentive.

3.15 The UC advised that, in settling the design of the student accommodation, it aimed to meet the preferences of different kinds of students. The UC advised that some students want single bed studios, while others want to live in multi-room apartments at reduced cost per room. The UC also advised that it wanted to ensure maximum flexibility with respect to alternative use in the future.

3.16 Table 3-3 shows the composition of the different NRAS properties with respect to the number of bedrooms.

Table 3-3 Composition of NRAS eligible properties

	Room type	No of rooms	No of beds
Weeden Lodge	Single studio	150	150
	Single accessible large	2	2
	Single studio superior	6	6
	Studio doubles	17	17
	Twin share	12	24
	Twin share large	5	10
	Two bedroom studio	101	202
	Three bedroom apartment	7	21
	Four bedroom apartment	5	20
	Seven bedroom apartment	4	28
Total for Weeden Lodge		**309**	**480**
Cooper Lodge	Single studio	184	184
	Single studio deluxe	63	63
	Double studio	13	13
	1 bedroom apartment	6	6
	5 bedroom apartment	30	150
Total for Cooper Lodge		**296**	**416**
Total for both Weeden Lodge and Cooper Lodge		**605**	**896**

Source: Audit Office, based on information provided by the University of Canberra

3.17 An analysis of the UC's NRAS eligible student accommodation shows:

- the UC's 605 NRAS eligible dwellings are a mix of studio rooms and apartments, with anywhere between one to seven beds in the dwellings; and
- the UC's 605 dwellings include 896 beds. However, up to 926 individuals may be accommodated in these rooms, as 30 of the rooms are double rooms, and may support up to two people.

3.18 Table 3-4 shows the occupancy rates of the different student accommodation provided at the UC since 2012.

Table 3-4 Occupancy rates of UC NRAS properties between 2012-2015 (dwelling and bed occupancy)

Property	2012		2013		2014		2015	
	Bed	Dwelling	Bed	Dwelling	Bed	Dwelling	Bed	Dwelling
Weeden Lodge Wing 5 (220 beds)	74.1	77.39	92.7	95.50	77.5	86.47	87.76 (YTD)	98.64 (YTD)
Weeden Lodge Wing 4 (260 beds)	N/A	N/A	N/A	N/A	60.4	73.54	87.13 (YTD)	98.46 (YTD)
Cooper Lodge (416 beds)	N/A	N/A	N/A	N/A	89.1	93.08	95.29 (YTD)	100.00

Source: Audit Office, based on information provided by the University of Canberra

3.19 An analysis of the occupancy rates of UC's student accommodation properties shows:

- the dwelling occupancy rates and bed occupancy rates of the UC's NRAS-eligible student accommodation have increased over time; and
- the dwelling occupancy rates for the NRAS-eligible accommodation consistently exceeds the bed occupancy rates of the NRAS-eligible occupation. This is because a dwelling is considered to be fully occupied even if only one of the multiple beds that are available within the dwelling are occupied. In this situation the dwelling occupancy rate will exceed the bed occupancy rate.

3.20 Between 2011 and 2014 the bed occupancy rate of Arscott House declined from 99.1 percent in 2011 to 57.5 percent in 2014 (99.1 percent in 2011, 91.6 percent in 2012, 75.2 percent in 2013 and 57.5 percent in 2014). Arscott House has not been available for student accommodation purposes in 2015. The UC advised that the decline in Arscott House occupancy was due to issues associated with the management of the facility. The UC further advised that it decided not to make the Arscott House available for student accommodation purposes in 2015, to enable it to make an assessment of options to refurbish and manage the facility.

ACT Government objectives for providing financial and other support to the UC

3.21 ACT Government objectives for providing financial and other support to the UC are implicit in the reasoning for the provision of financial support in the Cabinet documentation, and include:

- increasing the supply of affordable accommodation to students;
- achieving economic benefits for the ACT; and
- alleviating pressure on the broader ACT rental market.

3.22 An additional consideration of the ACT Government in providing financial and other support to the UC was to avoid adverse fiscal consequences from entering into such arrangements with the UC.

3.23 The objectives of the UC and the ACT Government coincided with respect to the provision of financial support for the purpose of providing student accommodation. However, these objectives have never been developed into a single set of agreed and measurable expectations

3.24 The following section of the report outlines performance against the ACT Government's implicit objectives for providing financial support to the UC for the provision of student accommodation.

Increasing the supply of affordable accommodation for students

3.25 One of the ACT Government's implied objectives in providing financial and other support to the UC has been to increase the supply of affordable accommodation to students. For the purpose of this discussion, 'affordable accommodation' is taken to be accommodation for which NRAS Incentive payments may be received.

3.26 The discussion in paragraphs 3.3 to 3.20, which discusses the UC's performance in supplying accommodation to students, is relevant for the purpose of assessing the ACT Government's achievements in meeting this objective.

Specification of requirements in loan agreements

3.27 A key objective of the National Rental Affordability Scheme is 'to reduce rental costs for low and moderate income households by making these dwellings available for rent at a rate that is at least 20 per cent below the prevailing market rate.'

3.28 In the absence of a single set of agreed and measurable expectations for the provision of ACT Government support to the UC, the loan agreements between the Territory and the UC represent the most relevant documentation associated with the support that was provided. The Treasury Directorate was responsible for developing the loan agreements, including statements of loan goals. Table 3-5 summarises the key loan goal provisions included in the three loan agreements.

Table 3-5 Loan goals included in UC student accommodation loan agreements

Date	Loan	Goal
25 July 2011	Cameron Wing 5	Increase the supply of high quality student accommodation by 210 beds by 30 June 2012 and continue to offer those additional 210 beds during the term of the loan.
13 September 2012	On-campus Stage 1	Increase the supply of student accommodation by 297 beds by 30 June 2014 and continue to offer those additional 297 beds during the term of the credit facility.
25 June 2013	Cameron Wing 4	Increase the supply of student accommodation by 131 beds by 30 June 2014 and continue to offer those additional 131 beds during the term of the credit facility.

Source: Audit Office, based on information in ACT Government loan agreements with the UC

3.29 The loan agreements between the Territory and the UC effectively establish the terms and conditions of the relevant loan and the specific use of the funds. However, they do not serve a useful purpose in safeguarding the provision of affordable accommodation to students as they do not include reference to NRAS objectives, including the need to make NRAS dwellings available for rent at a rate that is at least 20 per cent below the prevailing market rate.

3.30 The Chief Minister, Treasury and Economic Development Directorate advised that the loan agreements were appropriate for their purpose, which was to establish the terms and conditions of the relevant loan and the use of the funds, and that the UC was obliged to provide affordable accommodation to students through conditions and requirements imposed by the National Rental Affordability Scheme.

Monitoring the loan agreements

3.31 The Treasury Directorate has undertaken monitoring of the UC's performance in developing and providing student accommodation. The Treasury Directorate developed loan agreements that specified that the UC should provide the Territory with details of any material changes in the student accommodation, which must be to the reasonable satisfaction of the Territory. Loan reporting provisions in the agreements also required the UC to provide detailed information every six months, including financial statements, five year financial projections and assumptions. The loan agreements also provided for independent review of the UC's progress, by the ACT Government, at its discretion.

3.32 The UC has provided reports to the Treasury Directorate, in response to these loan agreement requirements, including:

- an annual report for the Cameron Wing 5 loan (1 July 2014); and
- six monthly reports for all loans (31 December 2013 and 30 June 2014).

3.33 The Treasury Directorate also commissioned an independent assessment of the student accommodation in Cameron Wing 5 in August 2013, with the objective of determining

whether the UC had met its obligations under the loan and provided the required student accommodation.

3.34 In accordance with the requirement that the Treasurer review the credit facilities annually, the Treasury Directorate provided a report on the status of the Cooper Lodge loan and Cameron Wing 5 loan to the Treasurer in December 2013. This report is required to address, but is not limited to, compliance with the approved terms of the facility, and the UC's ongoing ability to make repayments. The report concluded that both facilities were on track towards practical completion and that the UC was taking appropriate steps to ensuring levels of occupancy. The report also concluded that the UC was meeting its obligations and that there were no risks or issues emerging.

Monitoring the UC's achievements in supplying affordable accommodation to students

3.35 Apart from its review and monitoring of the UC's compliance with its loan agreements and credit facilities, the Chief Minister, Treasury and Economic Development Directorate does not actively monitor the UC's achievements in providing affordable accommodation to students in accordance with the NRAS. The Chief Minister, Treasury and Economic Development Directorate does, however, receive an annual report from the Australian Government Department of Social Security, with respect to occupancy rates of NRAS-eligible properties in the ACT.

3.36 The Chief Minister, Treasury and Economic Development Directorate's reliance on the Australian Government Department of Social Security to provide it with assurance with respect to the UC's performance in delivering accommodation in accordance with the requirements of the NRAS demonstrates an appropriate use of resources. In this way, the Chief Minister, Treasury and Economic Development Directorate does not seek to duplicate monitoring or assurance activities undertaken by the Australian Government Department of Social Security.

3.37 It is noted that the UC's sale of its NRAS entitlements to Westpac, which has created an ongoing financial liability for the UC, provides an additional commercial incentive for the UC to ensure that it continues to meet NRAS program and performance requirements. This is discussed in paragraphs 3.67 to 3.89 of the report.

Achieving economic benefits and alleviating pressure on the broader ACT rental market

3.38 Two of the ACT Government's implicit objectives in providing financial and other support to the UC have been to achieve economic benefits for the ACT and alleviate pressure on the broader rental market.

3.39 The ACT Government has not assessed whether the expected economic benefits associated with the provision of financial support to the UC have been achieved or whether the supply of accommodation by the UC has alleviated pressure on the broader rental market. However, evaluating the direct effects of the additional supply of

accommodation by the UC from the ACT Government's financial and other support would be difficult at this time as these benefits may not be realised until some time in the future.

RECOMMENDATION 2 MONITORING PERFORMANCE

The ACT Government should review the UC's performance in providing affordable accommodation to students against objectives and outcomes sought by the provision of ACT Government funding.

Avoiding adverse fiscal consequences

3.40 A consideration of the ACT Government in providing financial support to the UC was to provide support without adverse fiscal consequences to the Territory. A key risk that the ACT Government sought to avoid was the inability of the UC to repay its debt.

3.41 Of ongoing relevance to the ACT Government's consideration of requests for financial support from the UC was whether the UC would be able to pay its debts to the ACT Government and other lenders as and when they fall due. This necessitated consideration of the UC's financial position and its ability to manage its liabilities.

3.42 As discussed in paragraph 2.102 to 2.105, in May 2013 the Treasury Directorate obtained external advice on the UC's financial risk position. The external advice contained information on the financial ratios of several universities. The consultant used its experience in dealing with not-for-profit organisations across the education and health sectors, to determine typical Debt/EBITDA and FFO/Debt levels and also sought publically available benchmarks in the sector. The publically available benchmark universities used for comparison were the Australian National University, University of Melbourne, La Trobe University, University of Wollongong and Macquarie University.

3.43 The consultant did not perform a credit rating assessment. Nevertheless, the reference in the report to the Standard & Poors methodology provided a framework for measuring financial risk and the benchmarks were relevant in the context of assessing the UC's financial position following the Cameron Wing 4 project. Table 3-6 presents a summary of this information, which shows the financial risk profile of these universities, in comparison with the financial risk profile of the UC.

3.44 Funds flow from operations to debt ratio (FFO/Debt ratio) and debt to earnings before interest, tax, depreciation and amortisation ratio (Debt/EBITDA ratio) are ratios which provide an indication of an entity's ability to repay debt from operational income.

3.45 The debt to capital ratio is a ratio which provides an indication of the extent to which an entity relies on debt to operate.

Table 3-6 Financial risk profile of UC in comparison to other universities

	FFO to Debt Ratio	Debt to EBITDA Ratio	Debt to Capital Ratio
Aggressive		❍	
Significant	●●❍		
Intermediate		●●●	
Modest			❍
Minimal	●●●	●●	●●●●●

Source: Based on independent financial evaluation by KPMG for Treasury dated (May 2013).

Note: The other universities used for comparison by KPMG were the Australian National University, University of Melbourne, La Trobe University, University of Wollongong and Macquarie University.

University of Canberra - ❍

University peers - ●

3.46 The May 2013 financial evaluation by KPMG indicated that the UC was at the higher end of the risk spectrum in terms of its:

- ability to repay debts. The Debt to EBITDA Ratio indicates the UC had an 'aggressive' risk profile, which exceeded the 'intermediate' and 'minimal' risk profiles of the other universities. The FFO to Debt Ratio indicates that the UC had a 'significant' risk profile which was similar to two of the other universities, and exceeded three of the other universities; and
- reliance on debt to operate. The Debt to Capital Ratio indicated that the UC had a 'moderate' risk profile compared to the 'minimal 'risk profile of the other universities.

3.47 The UC advised that the increase in its financial risk profile is temporary and it is expected to improve in the future (refer to Table 3-9).

3.48 The May 2013 financial evaluation by KPMG also stated:

> As at December 2012, UC's total borrowings as a percentage of total capital (debt / debt + equity) represented 17.2%. This is higher than sector comparisons, however, a significant portion of this debt relates to specific student accommodation projects where the Commonwealth and ACT Government have provided NRAS incentives.

3.49 It further stated:

> It is expected that Australian universities will utilise more debt in the medium term, which will in turn increase the average financial risk of the sector from an overall conservative base.

3.50 In relation to the Debt to Capital ratio information presented in Table 3-6, the UC advised that the ratio (and accompanying analysis) is:

> ... a point in time measurement and that UC is being compared to well established universities whereas UC is under 50 years old and is continuing to grow and strengthen its financial position.

Analysis of the UC's current liabilities

3.51 As at 31 December 2014, the UC had total liabilities of $212.6 million ($76.2 million in current liabilities and $136.4 million in non-current liabilities). The UC's total liabilities at 31 December 2014 include $82.4 million in borrowings and $82.6 million in other liabilities. The UC's other liabilities include revenue received in advance, prepaid rent, deferred income and a liability relating to an arrangement for the securitisation of NRAS entitlements.

3.52 As at 31 December 2014, the UC owed the ACT Government $31.4 million.

3.53 Table 3-7 shows the UC's borrowings and financial liabilities, classified as current or non-current, since 2007. For comparison, the table also includes assets and total equity over the same period.

Table 3-7 UC borrowings and other liabilities since 2007

	2007 $'000	2008 $'000	2009 $'000	2010 $'000	2011 $'000	2012 $'000	2013 $'000	2014 $'000
Current								
Borrowings	3,770	389	774	644	4	21,800	1,142	409
Other liabilities	948	8,782	9,601	10,259	6,693	11,648	22,341	33,846
Total current liabilities	**24,813**	**28,228**	**34,781**	**39,325**	**43,572**	**72,119**	**76,640**	**76,230**
Total current assets	**9,342**	**23,061**	**25,188**	**22,606**	**25,621**	**33,429**	**39,934**	**45,418**
Net current liabilities	***15,471***	***5,167***	***9 593***	***16,719***	***17,951***	***38,690***	***36 706***	***30 812***
Non-current								
Borrowings	3,661	224	3,111	10,004	56,956	42,545	99,543	82,000
Other liabilities		6,667	10,680	7,342	7,075	6,809	18,920	48,728
Total non-current liabilities	**5,257**	**8,534**	**15,652**	**20,231**	**68,261**	**53,184**	**122,332**	**136,388**
Total non-current assets	**284,113**	**173,516**	**303,530**	**324,040**	**383,101**	**401,856**	**483,788**	**496,584**
Total equity/net assets	***263,385***	***259,815***	***278,279***	***287,090***	***296,889***	***309,982***	***324,750***	***329,384***

Source: University of Canberra annual reports.

3.54 An analysis of the UC's borrowings and other liabilities since 2007 shows that the UC's:

- current liabilities increased by $51.4 million (207.3 percent) from $24.8 million in 2007 to $76.2 million in 2014 (an average annual increase of 29.6 percent). In 2007 the UC's current liabilities comprised of $4.3 million in trade and other payables, $15.8 million in provisions (relating primarily to employee entitlements), $0.9 million in other liabilities, including revenue received in advance, while in 2014 the UC's current liabilities comprised of $22.0 million in trade and other payables, $25.6 million in provisions (relating primarily to employee entitlements), $33.8 million in other liabilities, including revenue received in advance. Over this period, current assets increased by $36.1 million (388.2 percent) from $9.3 million to $45.4 million (an average annual increase of 55.4 percent);

- net current liabilities increased by $15.3 million (98.7 percent) from $15.5 million in 2007 to $30.8 million in 2014 (an average annual increase of 14.1 percent);
- non-current liabilities increased by $131.1 million (2,473.5 percent) from $5.3 million in 2007 to $136.4 million in 2014 (an average annual increase of 353.4 percent). Over this period, the UC's non-current assets increased by $212.5 million (74.8 percent) from $284.1 million to $496.6 million (an average annual increase of 10.7 percent); and
- net assets increased by $66.0 million (25.0 percent) from $263.4 million in 2007 to $329.4 million in 2014 (an average annual increase of 3.6 percent).

3.55 Over this period, the UC's revenue increased from $129.5 million in 2007 to $273.5 million in 2014 (an increase of 111.2 percent), while the UC's expenses increased from $145.6 million in 2007 to $272.7 million in 2014 (an increase of 87.3 percent). The UC advises that the significant change in borrowings and other liabilities from 2007 to 2014 is reflective of the growth in its operations and also the growth and renewal strategy adopted with respect to capital investments.

Finance costs

3.56 Table 3-8 shows the UC's finance costs since 2007.

Table 3-8 UC finance costs (2007 to 2014)

	2007 $'000	2008 $'000	2009 $'000	2010 $'000	2011 $'000	2012 $'000	2013 $'000	2014 $'000
Finance costs	73	88	175	410	1,207	1,890	1,858	5,688

Source: University of Canberra annual reports.

3.57 The significant increase in liabilities, in particular interest-bearing liabilities such as borrowings, has resulted in higher costs of financing liabilities (interest paid on borrowings and other liabilities). The UC advises that the cost of financing liabilities is taken into account in the business cases prepared for each significant capital investment.

3.58 The UC's finance costs have increased by $5.6 million (7,691.8 percent) from $0.7 million in 2007 to $5.7 million in 2014 (an average annual increase of 1,018.8 percent).

Debt to equity analysis

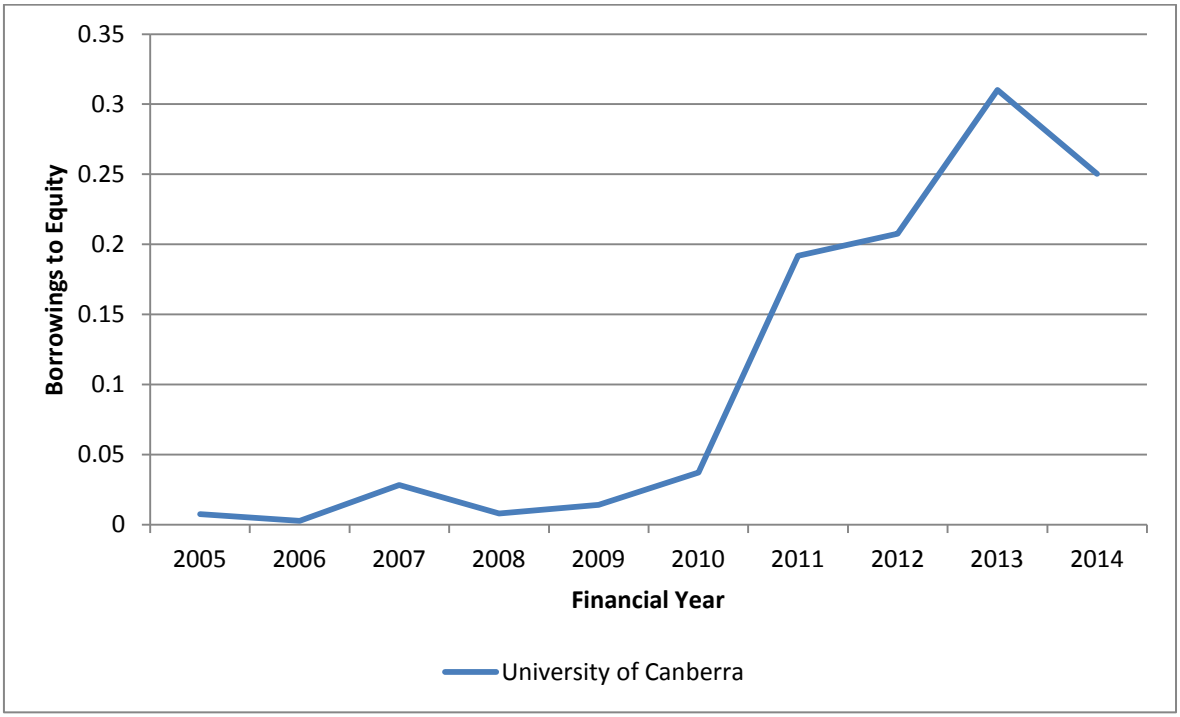
3.59 This section of the report shows an analysis of the UC's debt to equity ratio, as compared to a selection of other universities. The debt to equity ratio shows the relationship between debt financing and equity financing i.e. the proportion of debt that an organisation has relative to equity. The larger the ratio, the greater the proportion of debt to equity of an organisation.

3.60 The UC's debt to equity ratio has been compared to a selection of universities. including: Central Queensland University; Edith Cowan University, Southern Cross University; University of Southern Queensland; and University of the Sunshine Coast.. The Audit

Office has conducted an analysis on a range of additional universities. The universities presented in this report have been requested by the UC. The comparison is presented for context.

3.61 Figure 3-1 shows the UC's debt to equity ratio between 2005 and 2014, while Figure 3-2 compares the UC's debt to equity ratio with a selection of other universities for the period 2008 to 2013.

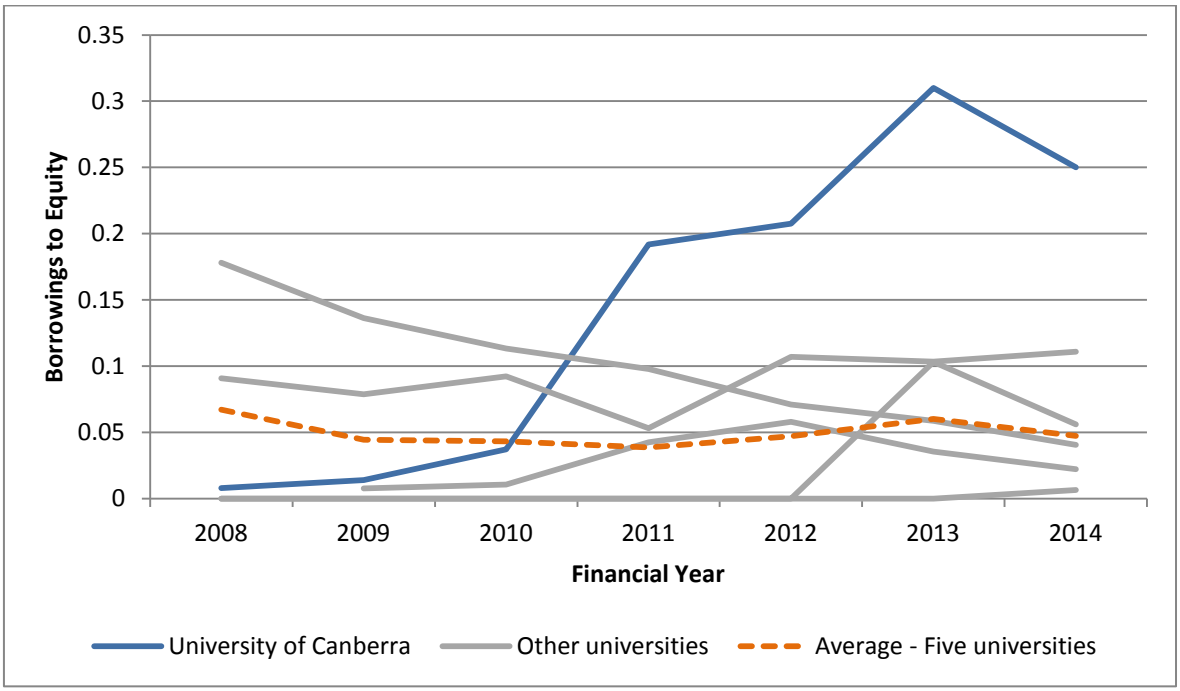
Figure 3-1 UC debt to equity ratio (2005 to 2014)



Source: Audit Office analysis, based on information in University of Canberra annual reports.

Note: The debt to equity ratio is calculated on the basis of total debt financing (i.e. borrowings) and total equity.

Figure 3-2 UC debt to equity ratio compared to other universities (2008 to 2014)



Source: Audit Office analysis, based on information in University of Canberra and other universities' annual reports.

Note: The debt to equity ratio is calculated on the basis of total debt financing (i.e. borrowings) and total equity.

3.62 An analysis of the UC's debt to equity ratio shows:

- the UC's debt to equity ratio increased significantly between 2005 and 2013, before declining in 2014. This shows that, between 2005 and 2013, the proportion of debt maintained by the UC increased at a faster rate than its equity. The primary reason for the decline in the debt to equity ratio in 2014 was the UC's repayment of a significant amount of its debt it owed to the ACT Government in November 2014, as a condition of the ACT Government's agreement for the UC to sell its NRAS entitlements to Westpac. The UC advised that between 2005 and 2013, it had used debt to finance its growth and renewal strategy and that this would explain why its debt has increased at a faster rate than its equity; and
- when compared to a selection of five other universities, the UC's debt to equity ratio was the third lowest in 2008 and in 2013 significantly exceeded that of the other universities included in the audit analysis, which the UC advised is due to a greater reliance on debt as the source of funding for its growth and renewal strategy.

3.63 The UC advised that it recognises that the debt to equity ratio increased substantially compared to other universities however, the UC also advised that it considered this to be necessary to pursue a growth strategy to sustain the UC's long term future. It further advised that it does not have the advantage of a large investment or endowment portfolio or access to significant state grants. The debt to equity ratio declined in 2014 and the UC advised that its financial position is being carefully managed by the UC and its Council and that this will continue.

Sale of the UC's NRAS entitlements

3.64 In November 2014, the UC entered into an arrangement to sell its rights to its future NRAS Incentives to Westpac Banking Corporation (Westpac) for $42.4 million, in an arrangement also referred to as 'securitisation'.

Transfer of the UC's NRAS allocations

3.65 On 21 August 2014, the UC lodged an application with the Commonwealth Department of Social Services to transfer its NRAS allocations to Westpac.

3.66 On 12 March 2012, the Vice Chancellor of the UC stated in a letter to the Chief Minister:

> The University recognises it is important to remain financially sustainable and to continue generating a surplus as well as maintaining an investment grade credit rating. We have received advice from Westpac which confirms the financial parameters required for an investment grade entity and the analysis has capacity to support further borrowings.

3.67 The Vice Chancellor of the UC went on to discuss a 'contingency plan in case operating outcomes significantly differ from projections', noting that one of the possible strategies would be to:

> … securitise the NRAS incentives and use this cash to reduce debt to other parties.

ACT Government approval

3.68 On 6 November 2014, the Vice Chancellor of the UC wrote to the Treasurer concerning 'the University's proposed transaction with Westpac Banking Corporation for the securitisation of our National Rental Affordability Scheme ('NRAS') incentives and to request your approval on behalf of the ACT Government, as required by the Commonwealth Department of Social Services'.

3.69 On 10 November 2014 the Treasurer sent a letter to the Vice Chancellor of the UC agreeing to the sale of the NRAS entitlements. In doing so, however, the Treasurer set the following conditions:

1. Westpac will not be provided with a mortgage or any other form of security over the UC's assets as part of the conditions of the NRAS securitisation transaction;
2. The proceeds from the securitisation transaction will be used to repay, in full, the $24 million Cameron Wing 4 loan with the Territory and the residual balance on the proceeds will be applied in early repayment towards the $50 million on-campus (Cooper Lodge) loan with the Territory;
3. To clarify that the securitisation transaction relates only to the Commonwealth component of the NRAS incentives and that Westpac has no claims over the Territory as a result of the transaction, a Deed will be established between the three parties to establish this indemnity;

4. The $50 million on-campus (Cooper Lodge) loan agreement be amended to clarify that the NRAS related accommodations are offered to the broader market consistent with the NRAS rules; and
5. The Deeds referred to above at item 3 and 4 must be executed prior to the settlement of the NRAS securitisation transaction.

Outcomes of the securitisation

3.70 Westpac and the UC entered into an agreement on 25 November 2014 for the sale of 605 NRAS entitlements. In return for the sale of the NRAS entitlements, the UC received a cash payment of $42.4 million. Under this arrangement, the UC has relinquished any claims to future NRAS Incentives (which will now be received by Westpac) but does, as Westpac's agent, retain responsibility for managing the NRAS-eligible dwellings. The agreement allows Westpac to recover from the UC any future NRAS Incentives that are not paid by the Commonwealth Department of Social Services in the event that the UC does not continue to meet the ongoing eligibility requirements (e.g. occupancy rates).

3.71 As a condition of the ACT Government's approval for the sale of the NRAS entitlements, the UC has used the amount received to:

- fully repay its debt to the ACT Government relating to the Cameron Wing 4 loan; and
- make an early repayment of $18.5 million to the ACT Government relating to the Cooper Lodge loan. The UC now only has one loan from the ACT Government (relating to Cooper Lodge), the outstanding balance of which stands at $31.4 million as at 31 December 2014.

3.72 The securitisation arrangement has resulted in the UC's recording of future NRAS entitlements as an 'other financial liability' in its financial statements.

3.73 A note to the UC's 2014 financial statements states *inter alia*:

> The purchase price was based on the expectation that the University dwellings will achieve 98% occupancy over the NRAS entitlement period and will comply with the NRAS Regulations. The University is contractually obligated to deliver the NRAS entitlements to the third party over the entitlement period of 10 years. In the case that the actual entitlements are less than then expected entitlements, the University must compensate the third party for the residual amount. If the actual entitlements are greater than the expected entitlements, the third party must pay the residual amount to the University. Given the University is exposed to the risks and rewards of the NRAS entitlements, this arrangement represents a financial liability to be measured at amortised cost.

3.74 While the securitisation arrangement has had the effect of increasing the cash holdings of the UC (i.e. increasing its current assets) it also places an obligation on the UC to deliver future cash flows arising from the NRAS entitlements to Westpac for the remainder of the ten-year period in which NRAS entitlements are due.

3.75 The sale of its NRAS entitlements provided an immediate cash receipt of $42.4 million for the UC. As a condition of its approval for the arrangement, the ACT Government ensured that the proceeds from the sale were used to pay some of the debt that the UC owed to the ACT Government. The sale has therefore had the effect of reducing aspects of the UC's more immediate financial liabilities (i.e. its debt to the ACT Government) while creating another ongoing financial liability for the UC. The ongoing financial liability places an onus on the UC to ensure that it maintains occupancy levels of its NRAS-eligible dwellings. Should the UC not be in a position to maintain occupancy levels of its NRAS-eligible dwellings, there are contractual remedies open to Westpac to recover payment from the UC. While not maintaining occupancy levels was an existing risk for the UC (as Australian Government payments were contingent on this), there is now an additional incentive for the UC to maintain these levels, as Westpac may seek payment from the UC should Australian Government NRAS payments not be forthcoming.

Capacity of the UC to repay its debt

3.76 The UC's borrowing limit, as approved by the Treasurer, is $144.0 million. This comprises:

- $70.0 million that the UC may borrow from non-Government lenders;
- $50.0 million relating to the construction of Cooper Lodge; and
- $24.0 million relating to the construction of Weeden Lodge.

3.77 As at 31 December 2014 the UC had:

- $51.0 million in non-current borrowings with a commercial lender;
- $31.0 million in non-current borrowings with the ACT Government (Cooper Lodge); and
- $0.4 million in current borrowings with the ACT Government (Weeden Lodge).

3.78 As at 31 December 2014, the UC had the capacity to borrow up to $20.0 million from non-Government lenders, i.e. $19.0 million in loans from non-ACT Government lenders (i.e. $70.0 maximum borrowing limit less $51.0 million currently borrowed) and a $1.0 million bank overdraft facility with a non-Government lender.

Strategic plans and growth

3.79 The UC's *Strategic Plan 2013-2018* identifies that the UC will have a strong growth focus into the future. The *Strategic Plan 2013-2018* identifies a range of goals, including:

- enrolment of 16,500 full-time equivalent students;
- operating surpluses between 2013 and 2018 and an underlying operating surplus of at least 5 percent by 2018 (for the UC group as a whole); and
- an AA+ indicative credit rating.

UC financial modelling

3.80 During audit fieldwork, in 2014, the UC provided a long term financial model (for the UC group as a whole) to the Audit Office. The model showed balance sheet, operating statement and cash flow statements out to 2018. The model factored in the repayment of debts to the ACT Government in accordance with the UC's loan and credit facility agreements with the ACT Government at the time.

3.81 The model showed that the UC expected that its:

- debt holdings would peak in 2014, and the UC would begin paying down debt from 2015; and
- capital expenditure will reduce significantly, as work on infrastructure was completed.

3.82 The model provided to the Audit Office was prepared prior to the changes to the UC's financial situation arising from the sale of its NRAS entitlements and its partial repayment of some of its loans to the ACT Government. In June 2015 the Audit Office was provided with updated calculations by the UC for its Debt to EBITDA Ratio and Debt to Capital Ratio.

3.83 Table 3-9 shows leveraging and debt repayment ability metrics using the UC's June 2015 calculations, based on Standard & Poor's corporate benchmarks.

Table 3-9 UC forecasted leveraging and debt repayment position

	2014	2015	2016	2017	2018
Debt/EBIDTA	Significant (3.31)	Intermediate (2.05)	Modest (1.53)	Minimal (1.16)	Minimal (0.94)
Debt/Capital	Minimal (20.0%)	Minimal (18.5%)	Minimal (15.6%)	Minimal (12.6%)	Minimal (9.5%)

Source: Audit Office analysis, based on UC information (2014) and Standard & Poor's corporate benchmarks.

3.84 An analysis of the UC's June 2015 calculations indicates that the UC expected to improve its capacity to repay debts over 2014 to 2018. While the UC expects to repay its debts, this depends on the achievement of budget forecasts and, in particular, increasing student revenue, to achieve planned cash flows from operations.

Net cash inflows from operating activities

3.85 In 2014 the UC's net cash inflow from operating activities was $21.3 million, which was a reduction from $54.2 million in 2013. The reduced cash inflow was primarily due to reduced grant receipts from the Australian Government. Reduced grant receipts were, however, offset by increased receipts from student fees and other customers. In 2014, the UC also had a reduced net cash inflow from its financing activities (from $36.3 million in 2013 to $24.0 million in 2014). Reduced net cash inflows from operating activities and financing activities were offset by improved cash flows from investment activities.

3.86 In 2014 there was a net cash outflow of $46.4 million, which was less than the net cash outflow figure of $91.5 million for 2013. The UC's cash and cash equivalents as at 31 December 2014 was $3.3 million, which was a reduction from the 2013 figure of $4.4 million.

3.87 The UC advised that fluctuation in its cash flows was due to timing differences with respect to the receipt and expenditure of Australian Government Structural Adjustment Fund grant funding. The UC advised that Structural Adjustment Fund grant funding was received in 2012 and 2013, of which only approximately $5.7 million was spent, with the balance being spent in 2014. The UC also advised that, over this period there has also been a significant investment in property, plant and equipment ($46.8 million in 2014 and $91.8 million in 2013).

Summary

3.88 The UC's cash flows for 2014 showed that the UC does not generate significant net inflows from its operations. The UC advised, however, that timing issues associated with the receipt and expenditure of grants has also impacted its net cash flows. Net cash inflows from operations are necessary for the UC to repay its debts. The UC's 2014 financial model indicates that it expects to improve its net cash inflows from operations and its capacity to repay its debts over 2014 to 2018. However, there are risks associated with achieving this.

3.89 The UC is reliant on increasing student revenue to generate operating surpluses. By 2018 the UC plans to enrol 16,500 full-time equivalent students. In 2014 the UC's equivalent full-time student load was 11,125 (a 3.5 percent increase on its 2013 equivalent full-time student load). The UC will need to increase its equivalent full-time student load by 48.3 percent between 2014 and 2018 to achieve its goal of 16,500 full-time equivalent students.

3.90 Table 3-10 shows the UC's 2015 full-time equivalent student load for the first semester for 2015, compared to the first semester of 2014.

Table 3-10 UC Equivalent Full-Time Student Load (first semester) 2014 and 2015

	2014	2015
ACT/Queanbeyan	2,662.29	2,689.13
Greater Sydney	295.54	277.88
NSW Country	1,020.16	969.87
Other	385.93	416.35
Domestic (total)	**4,363.93**	**4,353.22**
International (total)	**1,204.13**	**1,231.88**
Total	**5,568.05**	**5,585.09**

Source: Audit Office, based on information from the University of Canberra

3.91 The UC's first semester enrolments for 2015 were 5,585 full-time equivalent students, as compared to 5,568 for the same period in 2014 (an increase of 0.3 percent). The UC's plan to increase its full-time equivalent student numbers by 48.3 percent between 2014 and 2018 is at risk if the trend between 2014 and 2015 first semester student enrolment numbers continues.

3.92 The UC advised that some of this growth will be outside Canberra through partnerships in Melbourne, Sydney and Brisbane as well as through growth in international students studying in Canberra.

3.93 Changes to the UC's business environment that affects student numbers will present a risk to the achievement of the UC's financial goals and its ability to repay its debts. It is noted, however, that other universities are likely to be facing similar challenges to those confronting the UC with respect to increasing student numbers.

UC financial statements (Note 36 Financial risk management)

3.94 The UC advised that Note 36 'Financial risk management' of the 2014 financial statements explains the arrangement to manage financial risks and that this statement was examined as part of the audit of the financial statements undertaken by the ACT Audit Office.

3.95 Note 36 states that:

> The University's activities expose it to a variety of financial risks. The University Council through the Audit and Risk Management Committee monitors and manages the financial risks relating to the operations of the University. These risks include credit risk, liquidity risk and market risk (including currency risk, interest rate risk and price risk).
>
> ...
>
> Liquidity risk is the risk that the University will encounter difficulties in meeting its financial obligations as they fall due. Ultimate responsibility for liquidity risk management rests with the University Council through the University's Audit and Risk Management Committee, which has established an appropriate liquidity risk management framework for the management of the University's short, medium and long-term funding and liquidity management requirements. The University manages liquidity risk by maintaining adequate reserves and banking facilities, and by continuously monitoring forecast and actual cash flows.
>
> The University current holds sufficient cash on hand to meet its immediate operating requirements. Commonwealth funding received for operational requirements, such as managing student enrolments and capital expenditure activities, are paid to the University on a fortnightly basis throughout the year. Income from other operational activities is invoiced progressively throughout the year to manage cash flow.
>
> The University can use its overdraft and cash advance facilities to meet any shortfall, if a need arises. Note 23(b) Financing arrangements sets out details of undrawn facilities that the University has at its disposal to further reduce liquidity risk.

3.96 Note 23(b) Financing arrangements outlines the UC's financing arrangements, and the facilities available to the UC to meet any shortfall in its liquidity.

3.97 Note 1(e): 'Critical accounting estimates and judgements' to the financial statements also discloses a critical judgement on 'Meeting Current Liabilities'. Note 1(e) states that:

> The statement of financial position shows that the Group's current liabilities exceed its current assets. The University considers that it is able to meet its current liabilities expected to mature in the next 12 months as it has debt facilities with banks to allow it to manage its working capital requirements. The University has available undrawn debt facilities at balance date of $20 million (2013 $63.5 million). - Refer Note 23 Borrowings for further details. The University is also a recipient of regular fortnightly payments from the Commonwealth for its Commonwealth Supported Place (CSP) students. These two factors enable the University to meet its ongoing cash commitments when required.

3.98 In the UC Member's Declaration to the 2014 financial statements the UC Council states that:

> In our opinion, at the time of the report there are reasonable grounds to believe that the University of Canberra will be able to pay its debts as and they fall due.

3.99 In forming the unqualified audit opinion on the 2014 financial statements of the UC, the Audit Office considered whether the use of going concern assumption in the preparation of the financial statements was reasonable, including whether the statement by members of the UC Council that 'there are reasonable grounds to believe that the UC will be able to pay its debts as and they fall due' was reasonable at the time the audit report was signed.

3.100 The Auditor-General formed the opinion that there were 'reasonable grounds to believe' that the UC can pay its debts as and when they fall due, in the forthcoming year. The Auditor-General will again assess whether there continues to be reasonable grounds to believe that the UC can pay its debts as and when they fall due as part of future annual audits of the financial statements of the UC.

Capacity to repay debts

3.101 In relation to the UC's capacity to repay its debts, the UC advised:

> ... there are strong reasons for UC's growth strategy. When the growth phase started, the University was in a very poor financial position (an operating deficit of nearly $15.9m in 2007) and its future viability was under question. It is now in a much better financial position, with several years of operating surpluses, and a future that looks much brighter. The public profile of the University is much stronger and this 'branding' has helped a lot.
>
> ...
>
> Capital investment, including student accommodation, has been an essential part of the growth strategy and much of it has been financed from borrowings given the previous poor financial position of the University and endowments are not as high as for older Universities. Consequently, after consideration of business cases, the level of debt has increased and it is recognised that there are increased financial risks associated with it and that these have to be carefully managed. As you know, the growth strategy and the supporting financial decisions and arrangements have the unanimous support of Council.

> ... the level of debt peaked during 2014 and this is shown in forecasts for 2015 and beyond.

3.102 The UC also advised that there were strong reasons for its growth strategy and that capital investment, including investment in student accommodation, has been an important part of this growth strategy, much of which has been financed from borrowings. The UC acknowledges that the level of debt has increased (and that there are increased financial risks associated with this) but that these have been and will continue to be managed through its governance and oversight arrangements.

3.103 The UC further advised:

> Whilst there has been decline in some key financial ratios related to debt, this is to better set up UC for the future when these ratios would be expected to improve starting from 2015. This is consistent with good practice.
>
> ...
>
> Council recognises that short to medium term financial risk has increased. There is good reason for that. It is essential for the long term viability of the University. There is no disagreement among Council members about that. The issue is to ensure that it is well managed, which I believe it has been in the past and will continue to be in the future.
>
> The current strategic and financial plan relies on increases in student numbers. As anticipated there is no growth in ACT (or region) based domestic students due primarily to demographic reasons but there remains strong growth in international students and domestic students from outside the ACT. This is why you have put special effort into obtaining students from these sources and the availability of affordable accommodation is important to that effort. Other universities are offering accommodation guarantees and Council agrees that UC must be able to make similar offers.
>
> It is recognised that there is some risk that the growth in student numbers will not be obtained despite the considerable effort being put into increasing student numbers. We get a report on this at virtually every Council meeting and it is recognised by Council as a key strategic risk. However, there are a range of contingencies that can be activated if this occurs. The UC has shown itself as being adroit at doing this in the past when required. Some of the options that have been considered are:
>
> - Reduced expenditures especially on the use of contract staff (with some corresponding reductions on outputs especially in those areas where student numbers are not as high as expected)
> - Deferral of capital projects, whilst considering the impact of such deferrals
> - Partial sale of UCC of unlocking the value of the college and working in partnership with an experienced provider to increase the flow through of students to UC (already agreed by Council)
> - Partnerships involving the development of the campus in line with the Council approved 'Urban Plan' for UC.

3.104 In relation to the recognition and management of these risks, the UC also advised that changes to the UC's business environment are being monitored by UC management it has

governance committee oversight and risk management strategies in place. The UC advised:

> Council and supporting Committees have not taken their eyes off the ball with respect to the University's debt position.
>
> ...
>
> As the draft Report highlights, future financial projections depend on student growth assumptions but Council has been made aware of several contingencies that could be activated if the growth assumptions are not realised. The recent consideration of the opportunities to unlock the value of land on the UC campus that will not be required for academic purposes is a good example of how UC can strengthen its future financial position.

3.105 There are risks associated with the UC's capacity to repay its debts to the ACT Government. There are, however, options available to the UC to reduce expenditure and obtain income in order to meet its debt obligations. These include reducing expenditure, deferring capital projects, and entering into partnerships for the development of the UC campus. It is important that the risks to the Territory are monitored and reported to the Chief Minister and Treasurer.

RECOMMENDATION 3	ACT GOVERNMENT MONITORING OF UC FINANCIAL POSITION

The Chief Minister, Treasury and Economic Development Directorate should monitor risks to the Territory associated with the UC's debts and its capacity to repay its debts and brief the Chief Minister and Treasurer on the effectiveness of the UC's strategies to address the potential risks.

ACT Government funding obligations under the NRAS

3.106 One of the ACT Government's objectives in relation to the funding support it has given to the UC was to ensure that the Government meets its funding obligations under the NRAS scheme, equivalent to one-third of the Commonwealth's assistance, through cash or in-kind assistance.

Calculation of ACT Government support for the purpose of NRAS

3.107 Between 2011 and 2013 there were a number of different estimates and calculations, from both the UC and the ACT Government, associated with the ACT Government's contribution for the purpose of participating in NRAS. These estimates ranged from $22.9 million to $32.0 million, and were supported by analyses of differing detail and comprehensiveness.

3.108 In order to inform Cabinet deliberations on the proposed transfer of Arscott House, in December 2011 the Treasury Directorate calculated the value of the ACT Government's contributions to the UC for the purpose of participating in NRAS and in doing so, the Treasury Directorate provided a breakdown of the support to be provided. The Treasury Directorate's December 2011 calculation of the various contributions is shown in Table 3-11.

Table 3-11 ACT Government component of NRAS contribution to UC

Contribution	Value ($m)
Concessional interest rate benefit on the loan of $23.35 million, calculated as the difference between interest payable at a commercial rate and interest payable at a lower ACT Government rate	3.1
Cash grant	6.0
Transfer of Arscott House	9.0
Foregone estimated increase in the value of Arscott House value over ten years and stamp duty	8.6
Total	**26.7**

Source: Audit Office, based on ACT Government analysis

Changes to NRAS delivery

3.109 Since the ACT Government's calculation of its NRAS contribution in December 2011, there have been a number of changes to the UC's delivery of NRAS-eligible student accommodation and the financial and other support provided by the ACT Government. These include:

- the UC's non-delivery of 43 NRAS dwellings by the required date of 1 July 2014; and
- the UC's refinancing of its loans with the ACT Government. This means that the interest rate 'benefit' that was provided to the UC as part of the ACT Government's in-kind support has not materialised as expected.

3.110 Furthermore, as discussed in paragraph 3.10, there is a risk that the UC will not be in a position to deliver the remaining 352 entitlements between 1 July 2015 and 30 June 2016.

3.111 There is a need for the ACT Government and the UC to assess the level of support that the ACT Government has provided for the purpose of assisting the UC's participation in NRAS and determine if adjustments are appropriate.

RECOMMENDATION 4	ASSESSMENT OF SUPPORT FOR THE PROVISION OF AFFORDABLE STUDENT ACCOMMODATION

The ACT Government and the University of Canberra should assess the level of ACT Government support that has been provided for the purpose of the NRAS and make any necessary adjustments should a shortfall occur in the provision of student accommodation against the target.

RECOMMENDATION 5	ARSCOTT HOUSE

The University of Canberra should determine the future use for Arscott House. If it is not to be used for student accommodation or educational purposes as planned and changes to the use require a change in lease whereby the property value exceeds that provided by it in support of NRAS ($9.0 million) it would be equitable for an appropriate adjustment to be made to the ACT Government.

APPENDIX A: TREASURER APPROVALS FOR BORROWING LIMITS, LOAN AND CREDIT FACILITIES

2008 borrowing approval

On 18 April 2008, a minute was provided to the Treasurer from the Treasury Directorate, seeking the Treasurer's approval to approve a borrowing limit of $20 million for the UC. The minute stated 'it is clear that the proposed borrowings are for liquidity purposes while the University undertakes corrective action to improve its financial performance.' The borrowing limit was approved by the Treasurer on 23 April 2008.

Treasury Instrument TI2011/3

Treasury Instrument TI2011/3 was signed by the Treasurer on 30 June 2011. TI2011/3 provided for:

- approval of a Territory loan to the UC for 'an amount not exceeding $23.35 million'; and
- approval of loan facilities to be entered into by the UC with Westpac Banking Corporation and the Commonwealth Bank of Australia 'with a combined draw down limit not exceeding a total of $80 million'.

TI2011/3 provided that 'the Loan may only be used by the University of Canberra for the purchase and refurbishment (to a high standard) of the Premises, to provide for no less than 200 student accommodation places, with the student accommodation to be open and fully operational by 30 June 2012.'

Notwithstanding the approval of loan facilities up to $80 million, TI 2011/3 provided that 'the aggregate amount (excluding interest) drawn down by the University of Canberra...must not exceed...the borrowing limit set out in Treasury Instrument TI2011/7 dated on or about the date of this Instrument'.

Treasury Instrument TI2011/7

Treasury Instrument TI2011/7 was signed by the Treasurer on 30 June 2011. TI2011/7 provided for an increase in the authorised borrowing limit of the UC and approval of a maximum term for borrowings. TI2011/7 provided that the UC may owe up to a total of $70 million (excluding interest) at any time as a result of borrowings, which is the aggregate of:

- $46.65 million in loans from other parties; and
- $23.35 million by way of a loan from the Territory.

Disallowable Instrument 2012-208

Disallowable Instrument 2012-208 was signed by the Treasurer on 20 August 2012. DI 2012-208 provided for a $50 million credit facility to be provided to the UC from the Territory, for the purpose of enabling 'the design and construction of student accommodation and ancillary facilities on the UC campus which will result in 297 dwellings consistent with the UC's obligations under the Commonwealth NRAS arrangements'.

Treasury Authorisation 2012/12

Treasury Authorisation TI2012/12 was signed by the Treasurer on 20 August 2012. TI2012/12 provided for an increase in the authorised borrowing limit of the UC and approval of a maximum term for borrowings. TI2012/12 provided that the UC may owe up to a total of $120 million (including capitalised interest) at any time as a result of borrowings, which is the aggregate of:

- $46.65 million in loans from other parties;
- $23.35 million by way of a loan from the Territory; and
- $50.00 million which is to be provided by way of a credit facility from the Territory.

Disallowable Instrument 2013-40

Disallowable Instrument 2013-40 was signed by the Treasurer on 7 May 2013. DI 2013-40 provided for a $24 million credit facility to be provided to the UC from the Territory, for the purpose of enabling 'the purchase and redevelopment of Wing 4 Cameron Offices, 70 Chandler Street Belconnen (situated at Block 7, Section 44 Belconnen) (Wing 4 Cameron) for student accommodation which will result in 131 dwellings consistent with the UC's obligations under the Commonwealth NRAS arrangements.'

Treasury Authorisation 2013/6

Treasury Authorisation TI2013/6 was signed by the Treasurer on 7 May 2013. TI2013/6 provided for an increase in the authorised borrowing limit of the UC and approval of a maximum term for borrowings. TI2013/6 provided that the UC may owe up to a total of $144 million (excluding capitalised interest) at any time as a result of borrowings, which is the aggregate of:

- $46.65 million in loans from other parties;
- $23.35 million by way of a loan from the Territory;
- $50.00 million which is to be provided by way of a credit facility from the Territory; and
- $24.00 million which is to be provided by way of a credit facility from the Territory.

Treasury Authorisation 2013/9

Treasury Authorisation TI2013/9 was signed by the Treasurer on 27 June 2013. TI2013/9 provided for amendments to the authorised borrowing limits and borrowing arrangements of the UC as set

out in TI2013/6. Similar to TI2013/6, TI2013/9 provided that the UC may owe up to a total of $144 million (excluding capitalised interest) at any time as a result of borrowings. However, the approved borrowing arrangements were amended as follows:

- $70.00 million in loans from other parties;
- $50.00 million which is to be provided by way of a credit facility from the Territory; and
- $24.00 million which is to be provided by way of a credit facility from the Territory.

Audit reports

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