

City of Cockburn
Audit & Strategic Finance Committee
Addendum Agenda

For Thursday, 21 March 2019

CITY OF COCKBURN

SUMMARY OF ADDENDUM AGENDA TO BE PRESENTED TO THE AUDIT & STRATEGIC FINANCE COMMITTEE MEETING TO BE HELD ON THURSDAY, 21 MARCH 2019 AT 6:00 PM

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CITY OF COCKBURN

ADDENDUM AGENDA TO BE PRESENTED TO THE AUDIT & STRATEGIC FINANCE COMMITTEE MEETING TO BE HELD ON THURSDAY, 21 MARCH 2019 AT 6:00 PM

19. NEW BUSINESS OF AN URGENT NATURE INTRODUCED BY MEMBERS OR OFFICERS

19.1 APPOINTMENT OF INDEPENDENT MEMBER TO THE AUDIT AND STRATEGIC FINANCE COMMITTEE

Author(s)	S Downing
Attachments	<ol style="list-style-type: none"> 1. Recruitment Advert - Independent Member Audit and Strategic Finance Committee ↓ 2. Application Ms Susan Smith - Independent Member Audit and Strategic Finance Committee ↓ 3. CV (Resume) Ms Susan Smith - Independent Member Audit and Strategic Finance Committee ↓

RECOMMENDATION

That Council:

- (1) appointment Ms Susan Smith as the Independent Member of the Audit and Strategic Finance Committee;
- (2) endorse the initial appointment for a period of twelve months at which time a review of the appointment is to be undertaken for the Audit and Strategic Finance Committee's consideration; and
- (3) will remunerate by way of reimbursement of time of the Independent Member based on four hours for each meeting of the Audit and Strategic Finance Committee.

Background

The City of Cockburn believes that the appointment of an independent member to the Audit and Strategic Finance Committee will strengthen the governance processes of the Committee by providing an independent view of matters brought to the Committee by City management.

This will be the first such appointment for the City of Cockburn and coincides with a number of other Council across Western Australia appointing independent members to their Audit Committees.

The appointment will also be in line with the Guidelines issued by the then Department of Local Government and Communities Guideline No.9 – Audit Committees.

Submission

N/A

Report

The City advertised the position of independent member of the Audit and Strategic Finance Committee in September 2018. A copy of the advert is attached.

The advertising process attracted a limited response of three applications. The most suitable application, matching the criteria came from Ms Susan Smith. A copy of Ms Smith's application and CV (resume) are attached.

Ms Smith's extensive audit experience will add to the broad experience brought to the Audit and Strategic Finance Committee by Elected Members and City staff.

The initial term of the appointment will be for twelve months, from 1 July 2019 to 30 June 2020. At the conclusion of the first twelve months, a review will be undertaken by the CEO as to the effectiveness of the role of the independent member. The review will consult with both the Chair and members of the Audit and Strategic Finance Committee. The findings of the review will then be presented to the Audit and Strategic Finance committee for its consideration.

The intention is that after the initial twelve months, the appointment will be two years and coincide with the municipal year – November to October.

The remuneration of the Independent Member will be based on the Department of Local Government and Communities (DLGC)'s Guideline No 9 – Audit Committees: "*...it is permissible for a payment to be made as a reimbursement of expenses incurred, commensurate with the expertise and knowledge such people bring to the committee.*"

The City will reimburse the Independent Member based on four hours per meeting of the Audit and Strategic Finance Committee, which covers travel time, reading the agenda and attending the meeting of the Committee.

Ms Smith has agreed to the above conditions of the appointment. In addition, Ms Smith will be required to undertake an induction process to educate the Independent Member on governance, meeting procedures, standing orders and code of conduct matters.

Strategic Plans/Policy Implications

Leading & Listening

Deliver sustainable governance through transparent and robust policy and processes.

Budget/Financial Implications

An amount of \$5,000 will be provided in the draft 2019-2020 Municipal budget to fund the appointment of the Independent Member of the Audit and Strategic Finance Committee.

Legal Implications

Department of Local Government and Communities (DLGC)'s Guideline No 9 – Audit Committees.

Community Consultation

N/A

Risk Management Implications

The appointment of the Independent Member of the Audit and Strategic Finance Committee will provide additional reviewing capacity of all matters submitted to the Committee.

The biggest risk is the potential failure of the Independent Member to understand Council standing orders and meeting procedures frustrating both the newly Independent Member and fellow members of the Audit and Strategic Finance Committee. City staff will provide an induction to the newly appointed Independent Member to minimise this risk.

Advice to Proponent(s)/Submitters

N/A

Implications of Section 3.18(3) *Local Government Act, 1995*

N/A

AUDIT & STRATEGIC FINANCE COMMITTEE POSITION AVAILABLE

The City of Cockburn is seeking applications from interested persons with senior business or financial management/reporting knowledge, and experience with financial, and/or risk management, to become a member of the City's Audit and Strategic Finance Committee.

One fixed two years term position is available, with the option of extending.

The Audit and Strategic Finance Committee objectives are to facilitate:

- the enhancement of the credibility and objectivity of internal and external financial reporting;
- effective management of financial and other risks and the protection of Council assets;
- compliance with laws and regulations as well as use of best practice guidelines;
- the effectiveness of the internal audit function;
- the provision of an effective means of communication between the external auditor, internal audit, management and the Council.

The successful person, who must be independent of Council, will ideally be able to demonstrate extensive knowledge and experience of:

- Financial management, risk management, governance and audit (internal and external)
- Understanding of the duties and responsibilities of the position;
- ideally with respect to local government financial reporting and auditing requirements
- Strong communication skills
- Skills and experience in providing independent expert advice.

Please submit your written application to Stuart Downing, Director, Finance & Corporate Services at sdowning@cockburn.wa.gov.au by **25 September 2018**. If you require additional information contact Stuart on **9411 3444**.

The Audit and Strategic Finance Committee Terms of Reference can be found on the City's website.

Susan Smith - Statement - Audit and Strategic Finance Committee Member Application, City of Cockburn

Financial management, risk management, governance and audit knowledge and experience

I am an assurance and management consulting professional with 15 years experience providing internal audit, external audit and consulting services for predominantly Western Australia public sector and local government clients. I have 15 years experience conducting engagements in accordance with Australian Accounting and Auditing Standards and the International Standards for the Professional Practices of Internal Auditing. I have a Bachelor of Commerce degree - majoring in Professional Accounting and a Bachelor of Legal Studies - majoring in Criminology from Murdoch University. In addition I am a qualified CPA, advancing to CPA status in 2008.

While the majority of my professional experience has focussed on internal audit, risk management, governance and management consulting, I have adequate experience and significant knowledge and skills relevant to external audit to add value to the City of Cockburn's Audit and Strategic Finance Committee. When I started my career with Stanton Partners I completed external audits and financial assurance engagements for a variety of clients including the City of South Perth. In my role with the Department of Agriculture and Food I reviewed the first draft of the financial statements and annual report prior to external audit review and the review of the final draft prior to publication. Under my own name I have completed financial audits for Rotary clubs, Lions clubs, political parties, NGOs and community groups since 2010. I have significant skills and experience performing financial controls assessments which are an integral component of all engagements, internal or external, with a financial management scope.

I have substantial financial management, risk management, governance and audit knowledge and experience from my 15 years assurance and management consulting experience. This has included:

- Providing advice and assistance in relation to audit assurance, governance, risk management and the preparation of strategic audit plans.
- Completion of planning, reviewing fieldwork and reporting in a range of performance, financial, compliance and operational audit and review areas.
- Procurement consulting and contract management facilitation.
- Probity audit services for complex procurement projects, project management, identifying potential conflict of interest issues and providing independent proactive advice to evaluation teams and management.
- Facilitation of Risk Management Workshops and performance of Risk Management reviews.
- Corporate governance consulting and training to Boards and individual Directors.
- Monitoring and managing the reporting of implementation of audit recommendations.

I remain abreast of trends, development and best practice in financial management, risk management, governance and audit through professional reading and ongoing professional development. Over the last 8 years, my roles have increasingly included a larger proportion

of management consulting work where I provided advice to clients on legislative and standards compliance requirements, risk management and governance best practice. My advice extends beyond compliance requirements and best practice and I assist clients in problem solving to ensure the implementation of improvements is practical and improves efficiency and effectiveness.

Understanding of the duties and responsibilities of the position

I have familiarised myself with the City of Cockburn's Audit and Strategic Finance Committee's Terms of Reference. I understand the role the audit committee plays in assisting local government to fulfil its governance and oversight responsibilities in relation to financial reporting, internal control structures, risk management systems, legislative compliance, ethical accountability and the internal and external audit functions. I have remained abreast of the local government auditing reforms and the move towards greater independence of audit committees with the transition of the responsibility of local government audits to the Office of the Auditor General.

I have 15 years experience reporting to audit committees and have worked successfully with audit committees in a variety of shapes and forms. I understand the duties and responsibilities of local government audit committee members generally and understand the requirements for this position as the external committee member to provide independent expert advice in the areas of financial management, risk management, governance and audit.

Local government financial reporting and auditing knowledge and experience

I have been involved with the external audit of the City of South Perth and managed the outsourced internal audit services of the Eastern Metropolitan Regional Council. This gave me exposure to the nuances of local government and the specific legislative requirements of the Local Government Act and Financial Management Regulations.

My knowledge and experience of local government specific requirements has been further developed through engagements for the City of Canning since 2014. This has included a number of probity assignments where I provided assurance that the procurements were conducted in accordance with the City's procurement policy, local government regulations and probity principles. These probity assignments also gave me a great background in urban design and sustainability principles and practices, facilitating development outcomes and activation. I completed the City of Canning's financial management reviews in 2017 and 2018 as well as a separate capital works project review and a project management review of the City's largest, longest highest value project. My experience has given me knowledge of local government legislation and the ability to apply my financial management, risk management, governance and audit skills in the local government context.

Strong communication skills

I have excellent interpersonal, verbal and written communication skills and the ability to communicate calmly, clearly and effectively. This contributes greatly to my ability to influence, negotiate, build trust and establish strategic partnerships and positive working relationships. My communication skills have been refined through nearly 15 years of

assurance and consulting work. This has included interviews, discussions and meetings with stakeholders, preparation and review of reports and presentation of findings and recommendations to senior management, executive and boards including negotiating acceptance of critical findings and buy in to proposed solutions. I use my interpersonal skills to identify the root cause of issues allowing effective long term solutions to be achieved through system improvements, changes in practices or negotiated agreements as appropriate.

I have the ability to communicate the application of financial, risk management, governance and audit concepts to others in practical language as well as engaging in challenging technical discussion. In addition, I have excellent conceptual and analytical skills. These skills combined with my extensive knowledge and experience in assurance and consulting allow me to identify areas that require particular attention. In this way I believe I would be an asset to the committee using my expertise and experience to highlight areas for attention, explain the context and allow robust discussion of issues. I am a confident person but not overly domineering. These personal attributes have allowed me to build capacity within Boards through my corporate governance consulting. I look forward to the opportunity to work collaboratively with other committee members to ensure the committee is effective in achieving it's objectives, assists the CEO and supports the auditor as required by the local government auditing reforms.

Skills and experience in providing independent expert advice

My work in all aspects of assurance and consulting including performance and operational audits has given me significant experience working in areas of grey in contrast to financial audits which are far more black and white. I am confident, capable and experienced in interpreting information and making assessments where there is uncertainty or room for interpretation. I consider all aspects of the environment and ensure I have the full picture in my evaluations. I am flexible and adaptable and adapt my communication style and methods to suit the audience and needs.

I have 15 years experience providing independent expert advice in assurance, management consultancy and corporate governance advisory services engagements. I have ongoing positive working relationships with clients where I am trusted and have earned respect by providing quality, credible advice and professional expertise based on the latest research and best practice. In my management consulting work I have provided strategic management advice to clients and guided them through critical decision making. I have a strong work ethic and would work hard to provide valuable advice and deliver results by critically analysing reports presented to the committee and highlighting any areas that require further explanation or clarification. I am by nature, friendly, helpful and personable whilst always maintaining professionalism. I pride myself on being well prepared, researching and reviewing available information prior to meetings. I look forward to this opportunity to join the committee and work with council to enhance the governance and accountability of the City of Cockburn and the effectiveness of it's audit programme.

Susan Smith - Curriculum Vitae/CV

Key Strengths, Skills and Achievements –

- Excellent interpersonal, communication and presentation skills
- Significant experience providing credible expert advice on financial management, risk management, governance and audit matters
- Local government audit experience (internal and external)
- Strong leadership, operational and strategic management abilities
- Excellent decision making and problem solving skills
- Demonstrated ability to engage with stakeholders at all levels and establish successful relationships
- Commitment and desire to successfully achieve

Summary of Experience –

- 15 years experience providing assurance and management consulting services in Western Australia.
- 2 years experience specialising in corporate governance, risk and control consulting.
- Internal audit and consulting including compliance reviews, operational/performance audits, risk management, probity audit and preparation of strategic audit plans.
- Probity audit services for complex procurement projects.
- Management consulting including complete business reviews, developing and implementing new plans, budgets, policies, procedures and systems.
- Project management of multiple projects simultaneously.
- Procurement consulting services for procurements up to \$50 million.
- Corporate governance consulting and training to individuals and boards seeking advice to meet expectations and obligations.
- 3.5 years experience providing external audit services to public sector, local government, manufacturing and mining.

Professional History –

- **February 2012 – present – Manager – Quantum Assurance**
 - Management of a wide variety of engagements for a variety of clients including Legal Aid WA, Department of Education, Ombudsman WA, Economic Regulation Authority, Perth Theatre Trust, ScreenWest, Health and Disability Services Complaints Office, City of Canning, The Master Plumbers and Gasfitters Association of WA, UniCredit, Regional Development and Land, Burswood Park Board, Kimberley Community Legal Service and Department of Fire and Emergency Services. This role involved
 - Management consulting in relation to all aspects of operational and strategic management.

- Interpreting and providing advice on Acts, regulations, instructions, policies and procedures in internal audit reviews and probity assignments.
 - Providing advice and assistance in relation to audit assurance, governance, risk management and the preparation of strategic audit plans.
 - Procurement consulting and contract management facilitation.
 - Completion of planning, reviewing fieldwork and reporting in a range of financial, compliance, performance and operational audit and review areas.
 - Probity audit services for complex procurement projects, project management, identifying potential conflict of interest issues and providing independent proactive advice to evaluation teams and management.
 - Facilitation of Risk Management Workshops and performance of Risk Management reviews.
 - Project Management reviews and advice as well as the application of project management best practice internally.
 - Management of an assistant on projects when required.
- **April 2010 – present – Owner - Susan M Smith, Assurance Consulting & Advisory Services**
- Working privately to better meet client needs with a smaller client base.
 - Business management, consulting and advice to small business.
 - Corporate governance consulting and training to boards and individuals seeking advice to meet shareholder and/or community expectations and their increasing obligations relating to responsibilities of Directors, Board Members and other roles requiring good corporate governance in evolving regulatory environments.
 - Ad hoc assurance and probity services for organisations requiring financial and grant audits and other compliance assignments including Rotary Clubs, Lions Clubs, political parties, NGOs and community groups.
 - Honorary services as Treasurer and Board Member for community groups and schools
- **August 2009 – April 2010 – Manager, Governance Services – Braxford Consultancy**
- Management of the internal audit and management consulting services.
 - Development of a marketing strategy.
 - Preparation of a Corporatisation Options discussion paper for Greyhounds WA.
 - Internal audits of the Public Sector Agencies including the Office of the Inspector for Custodial Services and a finance function review for a large public sector department.
 - Managing a team of two staff.

- **December 2007 – August 2009 – Manager, Assurance & Consulting – Stantons International**
 - Management of the internal audit and consulting services of Stantons Western Australian client base of mainly public sector entities including the Department of Fisheries, Department of Premier and Cabinet, Office of the Director of Public Prosecutions, Aqwest, Department of Education Services, Eastern Metropolitan Regional Council, Esperance Port Authority, Forest Products Commission, Healthways, Midland Redevelopment Authority, National Trust, Office of Energy, Department of Sport and Recreation, Western Australian Industrial Relations Commission and the Water Corporation. This role involved managing all engagements relating to:
 - Providing advice and assistance in relation to audit assurance, governance, risk management and the preparation of strategic audit plans.
 - Interpreting and providing advice on Acts, regulations, instructions, policies and procedures in internal audit reviews and probity assignments.
 - Completion of planning, reviewing fieldwork and reporting in a range of financial, compliance, performance and operational audit and review areas.
 - Probity audit services for complex procurement projects, identifying potential conflict of interest issues and providing independent proactive advice to evaluation teams and management.
 - Managing a team of five staff plus additional resources in peak periods.

- **July 2007 – December 2007 – Senior Auditor – Department of Agriculture & Food**
 - Conducting audits and reviews aimed at assessing the Department's control environment, making recommendations for corporate governance best practise and identifying opportunities for business improvement.
 - Undertaking follow-up audits and special investigations and assisting in overall audit planning and administration

- **September 2003 – May 2007 – Senior Auditor – Stanton Partners & Stantons International**
 - Internal audit and consulting services to a client base of public and private sector entities in Western Australia including Department of Fisheries, Public Transport Authority – New Metro Rail, WA Planning Commission, Department of Treasury and Finance, Eastern Metropolitan Regional Council, Department of the Premier and Cabinet, Healthways, Water Corporation, Forest Products Commission, Western Power, Rottnest Island Authority, Central TAFE, West Coast College of TAFE, Synergy and Verve Energy.
 - External audit and corporate services including control system assessments and financial assurance to public sector, local government,

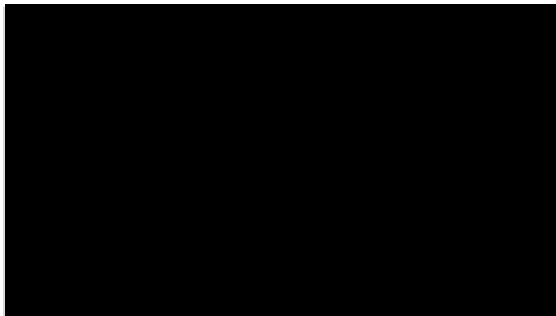
mining and manufacturing including City of South Perth, Verve Energy and Red Island.

Education and Qualifications –

- Tertiary Qualifications – Completed in 2005
 - Bachelor of Commerce - majoring in Professional Accounting (Murdoch University, Western Australia)
 - Bachelor of Legal Studies (majoring in Criminology) (Murdoch University, Western Australia)
 - These qualifications were achieved with a distinction average.
- CPA Australia Member – Advanced to CPA status in 2008
 - Winner of the CPA Program Excellence Awards in recognition of achieving the highest marks in Assurance Services and Auditing and Strategic Management Accounting.
- Certified Internal Auditor Part 1 Governance, Risk and Control – completed in May 2010.
- Real Estate Sales Representative Course – Completed in August 2010.
- Advanced Taxation - CPA Advanced Taxation unit; completed in October 2010.

Hobbies/Interests –

- Travel, snorkelling, dining out, gardening, spending time with family and keeping backyard chickens.



19.2 RESPONSE TO AUDIT RESULTS REPORT - ANNUAL 2017-2018 FINANCIAL AUDITS OF LOCAL GOVERNMENT ENTITIES BY THE AUDITOR GENERAL OF W.A.

Author(s)	S Downing
Attachments	1. Audit Results Report - Annual 2017-2018 Financial Audits of Local Government Entities ↓

RECOMMENDATION

That Council note the report.

Background

At the conclusion of the first year of financial audits undertaken by the Auditor General of Western Australia, a report was tabled to the WA Parliament outlining the findings as a result of the work completed by the Office of the Auditor General (OAG).

Submission

N/A

Report

The Auditor General tabled the attached report arising from the completion of the first year of financial audits undertaken by the Auditor General on 42 Local Governments.

The Auditor General made ten recommendations and below are the ten recommendations with a comment from the City on each of the recommendations.

Recommendation 1

Local Governments should ensure they maintain the integrity of their financial control environment by:

Recommendation 1a

Periodically reviewing and updating all financial, asset, human resources, governance, information systems and other management policies and procedures, and communicating these to staff.

City Response:

The City reviews all policies and procedures annually and takes the results to Council through the Delegated Authorities, Policies and Position Statements (DAPPS) Committee.

Recommendation 1b

Conducting ongoing reviews and improvement of internal control systems in response to regular risk assessments

City Response:

The City will undertake a review of financial controls prior to the completion of the current financial year. The review will then be provided to the Audit and Strategic Finance Committee for its consideration. The CEO will take a report on internal controls to council every two years.

Recommendation 1c

Regularly monitoring compliance with relevant legislation

City Response:

The completion of the Compliance Audit Return ensures compliance.

Recommendation 1 d

Promptly addressing control weaknesses brought to their attention by our (OAG) audits.

City Response:

The City puts into effect any management changes suggested or reported by and agreed on arising from the financial audit. For 2017-18, one change report on and agreed was the placement of investments. The change was to ensure that every placement of an investment was approved by the relevant City officer given delegation authority to place investments with recording in writing the approval of every such investment.

Recommendation 2

In addition to compliance with legislation, management should promote a culture of applying better practice financial management and complying with internal policies

City Response:

The City does have a history of ensuring management complies with better practice financial management and internal policies. This is achieved through internal audits of systems undertaken by an external firm of auditors, Deloitte.

Recommendation 3

An in-depth audit exit meeting should be held with audit committees, in advance of council meetings. As far as practicable, the audit committee should include a few council members, rather than the entire council.

City Response:

The City does provide the Auditor with unfettered access to the members of the Audit and Strategic Finance Committee for presentation of audit findings with appropriate responses by the CEO and staff. The meeting always precedes the Council meeting.

Recommendation 4

An audit entrance meeting should be held with the audit committee.

City Response:

The City will organise an entrance meeting with the OAG, KPMG and the Audit and Strategic Finance Committee for the 2018-19 audit.

Recommendation 5

Audit exit meetings should provide the auditor the opportunity to highlight the key audit issues, in a structured manner, and the CEO adequate opportunity to comment.

City Response:

The City does provide the Auditor with unfettered access to the members of the Audit and Strategic Finance Committee for presentation of audit findings with appropriate responses by the CEO and staff.

Recommendation 6

Local Governments should not make interim audit findings public until they are received as part of our (OAG) Audit Report on completion of the audit, unless specific urgent needs warrant earlier release.

City Response:

For 2017-18, the interim findings were not published until the audit had been completed, this was because the interim findings were not made available to Council officers until the audit was finalised. This is not consistent with prior years. This was because the interim findings were made available by the auditor much earlier. Comment from the members of the Audit and Strategic Finance Committee will be sought to this recommendation.

Recommendation 7

The Department of Local Government, Sport and Cultural Industries (the Department) should re-assess the potential advantages if Local Governments are required to report equipment assets using the cost model.

City Response:

The City supports this recommendation for the reporting of equipment assets (trucks, cars, plant and equipment) to be valued not at fair values but using the cost model.

Recommendation 8

Local Governments should robustly assess the assumptions and methodology of their valuers, in particular the approach for valuing land assets with restricted use.

City Response:

The City does review the valuation reports when they are received for valuation movements in assets by class and assets trying to understand the major or significant movement in dollar value terms.

As the industry uses a variety of valuers, there is inconsistency in the way valuers treat assets for valuation purposes. The outcome of the next recommendation (no.9) may see less inconsistency in the way assets are valued if the accounting standards provided more guidance.

Recommendation 9

Local Governments and the Department should monitor the progress of the Australian Accounting Standards Board and Internal Public Sector Accounting Standards Boards public sector fair value projects.

City Response:

The City is looking forward to receiving the outcome of the Fair Value review report being undertaken by the two accounting bodies.

Recommendation 10

Local Governments should continue to make timely preparations for implementation of the upcoming accounting standards changes, and the new regulation requiring assets with a value at acquisition below \$5,000 to be expensed.

City Response:

The significant accounting change for 2019/20 is in relation to Rates received in advance. Currently the accounting standard requires the Council to account for such money as income in the year received. The change will take it back to the prior accounting treatment of showing it on the balance sheet of Council as unearned income. The Council has been briefed on this item and has the relevant funds set aside to account for this change in accounting standard.

The City already expenses all assets purchased with a value of \$5,000 or less at the time of acquisition.

Strategic Plans/Policy Implications

Leading & Listening

Deliver sustainable governance through transparent and robust policy and processes.

Ensure sound long term financial management and deliver value for money.

Budget/Financial Implications

N/A

Legal Implications

N/A

Community Consultation

N/A

Risk Management Implications

The issues raised by the OAG's report to Parliament attempts to minimise risks seen by the OAG across the Local Government industry. The City looks to review each of the OAG's recommendations so as to learn from the broader approach provided by the OAG's team.

Advice to Proponent(s)/Submitters

N/A

Implications of Section 3.18(3) *Local Government Act, 1995*

Nil

Western Australian Auditor General's Report



Audit Results Report – Annual 2017-18 Financial Audits of Local Government Entities



Report 15: March 2019

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WESTERN AUSTRALIAN AUDITOR GENERAL'S REPORT

**Audit Results Report – Annual 2017-18
Financial Audits of Local Government Entities**

Report 15
March 2019



**THE PRESIDENT
LEGISLATIVE COUNCIL**

**THE SPEAKER
LEGISLATIVE ASSEMBLY**

**AUDIT RESULTS REPORT – ANNUAL 2017-18 FINANCIAL AUDITS OF LOCAL
GOVERNMENT ENTITIES**

Under section 24 of the *Auditor General Act 2006*, this report covers the first year of a 4-year transition for my Office to conduct the annual financial audits of the local government sector, following proclamation of the *Local Government Amendment (Auditing) Act 2017*.

The 2017-18 financial audits of 42 local government entities completed to date include:

- Results of the audits of local government entities' annual financial reports, and their compliance with applicable legislation for the financial year ending 30 June 2018.
- Issues identified during these annual audits that are significant enough to bring to the attention of the Parliament.

I wish to acknowledge the assistance provided by the councils, their chief executive officers, finance officers, and others including my dedicated staff and contract audit firms throughout the annual financial audit program and in finalising this report.

A handwritten signature in black ink, appearing to read 'C Spencer'.

CAROLINE SPENCER
AUDITOR GENERAL
7 March 2019

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Auditor General's overview

This report summarises the results of 42 local government entities' annual financial report audits completed by my Office to date for the year ending 30 June 2018, following proclamation of the *Local Government Amendment (Auditing) Act 2017*. This was the first of a 4-year transition of local government financial auditing to the Office of the Auditor General.

In addition to reporting the results of the audits to Parliament, this report is intended to provide further insight for Parliament and the local government sector to our approach for performing and reporting on financial audits.



I recognise that we, together with the sector, have only just begun our journey in this new era of local government financial auditing. The 42 audits completed in 2017-18 represent approximately one third of all WA local government entity audits.

During our audits, in addition to routine but important audit findings, we have made other observations about what we found is working well in the sector, where improvements may be considered and where opportunities exist. One such stark governance-related opportunity relates to audit committees.

Audit committees play a key role in assisting boards, councils and chief executive officers with financial management, control, and reporting. In this report, I have included a few preliminary observations about the role of audit committees in the annual reporting and audit process. I recognise the challenges regional local government entities may have in appointing independent members with financial or audit expertise, and intend to report more broadly on the role of audit committees and internal audit in the future.

In our first year auditing local government entities, we were concerned that some local government staff considered an audit finding not worthy of formal reporting if the control weakness did not result in a breach of legislation or misstatement. My Office reports weaknesses in internal controls and governance, so that they can be remedied before they potentially lead to non-compliance with legislation including misstatement due to fraud or error.

We also identified the need for more emphasis on auditor independence. We noted it was often common practice for auditors to perform other work for local government entities, in addition to the annual financial audit. As this can impair an auditor's independence, we have tightened controls around our contracted local government auditors performing this work, as we do for state government, while recognising practical challenges - such as limited availability of alternate skills in some regional areas.

I wish to thank my staff, our contract auditors, and staff in the local government entities we audited who contributed and assisted during our first year of transition into the sector and our first annual financial audits.

I am looking forward to working with the sector over the coming years to deliver high quality audits that contribute to enhancing the financial management and performance of local governments for the benefit of the WA community.

Executive summary

This Audit Results Report contains findings from the annual financial audits of local government entities (LGs) that we audited for the 2017-18 financial year.

Following proclamation of the *Local Government Amendment (Auditing) Act 2017* (Amendment Act), the Auditor General assumed responsibility for the audits of the 2017-18 annual financial reports of 46 LGs. The annual financial audits of remaining LGs are due to transition to the Auditor General by 2021.

Under the Amendment Act, the Office of the Auditor General (OAG) also assumed responsibility for performance audits of the local government sector. These audits are reported in separate reports to Parliament when they are completed.

Key findings

- We issued auditor's reports for 42 LGs by 1 March 2019 relating to their 2017-18 financial year. (Page 10)
- All but 2 auditor's reports included clear (unqualified) audit opinions on the financial reports. We issued qualified auditor's reports on the financial reports of the Shire of Brookton and the Town of Cambridge. (Page 10)
- We reported 36 material matters of non-compliance with the *Local Government Act 1995*, *Local Government (Financial Management) Regulations 1996*, or other written law in 24 of our auditor's reports. (Page 11)
- In addition to material matters of non-compliance reported in auditor's reports, we reported 290 financial management and control matters of varying significance to management in our management letters. (Page 15)
- In accordance with the *Local Government (Audit) Regulations 1996*, we reported adverse trends in the financial position of 24 LGs. (Page 13)
- In our first year of performing annual financial audits in the local government sector, we have made some general observations and included these in the report, with a view to improving audit outcomes in the future. These relate mainly to audit committees and reporting practices. (Page 17)
- The report includes details of our response, in the context of auditor independence, to existing practices where audit firms performed other work at local governments they were auditing. (Page 19)
- We detail our concerns that valuation methodologies used by various valuers to fair value property, plant, equipment and infrastructure, often differ significantly, potentially affecting comparability of asset values across local governments. (Page 20)
- We recommend that LGs make timely preparations for upcoming changes to Australian Accounting Standards and a local government regulation. (Page 22)

Recommendations

1. LGs should ensure they maintain the integrity of their financial control environment by:
 - a. periodically reviewing and updating all financial, asset, human resources, governance, information systems and other management policies and procedures, and communicating these to staff.
 - b. conducting ongoing reviews and improvement of internal control systems in response to regular risk assessments.
 - c. regularly monitoring compliance with relevant legislation.
 - d. promptly addressing control weaknesses brought to their attention by our audits. (Page 16)
2. In addition to compliance with legislation, management should promote a culture of applying better practice financial management and complying with internal policies. (Page 18)
3. An in-depth audit exit meeting should be held with audit committees, in advance of council meetings. As far as is practicable, the audit committee should include a few council members, rather than the entire council. (Page 18)
4. An audit entrance meeting should be held with the audit committee. (Page 18)
5. Audit exit meetings should provide the auditor the opportunity to highlight the key audit issues, in a structured manner, and the CEO adequate opportunity to comment. (Page 18)
6. LGs should not make interim audit findings public until they are received as part of our Audit Report on completion of the audit, unless specific urgent needs warrant earlier release. (Page 18)
7. The Department of Local Government, Sport and Cultural Industries (the Department) should re-assess the potential advantages if LGs are required to report equipment assets using the cost model. (Page 21)
8. LGs should robustly assess the assumptions and methodology of their valuers, in particular the approach for valuing land assets with restricted use. (Page 21)
9. LGs and the Department should monitor the progress of the Australian Accounting Standards Board and International Public Sector Accounting Standards Board public sector fair value projects. (Page 21)
10. LGs should continue to make timely preparations for implementation of the upcoming accounting standards changes, and the new regulation requiring assets with a value at acquisition below \$5,000 to be expensed. (Page 23)

Introduction

Under the *Local Government Amendment (Auditing) Act 2017* (Amendment Act), proclaimed in October 2017, a staged transition has commenced for local government entities (LGs) annual financial audits to transition to the Auditor General as and when existing audit contracts between audit firms and LGs expire. The Office of the Auditor General (OAG) assumed responsibility for 46 audits from the 2017-18 financial year, with full take up of all financial audits by 2020-21.

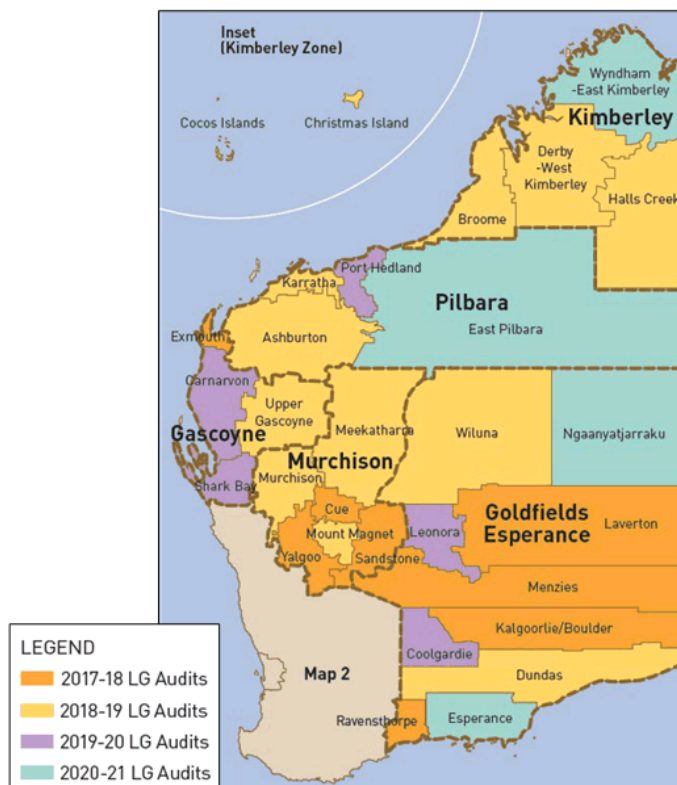
In 2017-18, OAG audit staff performed 3 of the 46 financial audits, with the others performed by contract audit firms on our behalf. Our oversight of these audits, coupled with in-house OAG audits, has provided our staff with valuable insight and understanding of the sector. From 2018-19, we will increase the number of audits performed using in-house audit teams.

For almost all of the contracted audits, we retained the existing audit firm for 2017-18 to maintain some continuity of the audit team. However, to provide open and fair competition and to ensure value for money, for 2018-19 we have now re-tendered most of these audits.

We are also committed to supporting local industry, and where possible and appropriate, we propose to use local financial auditing professionals in regional areas.

Local government entities audit program: 2017 onwards

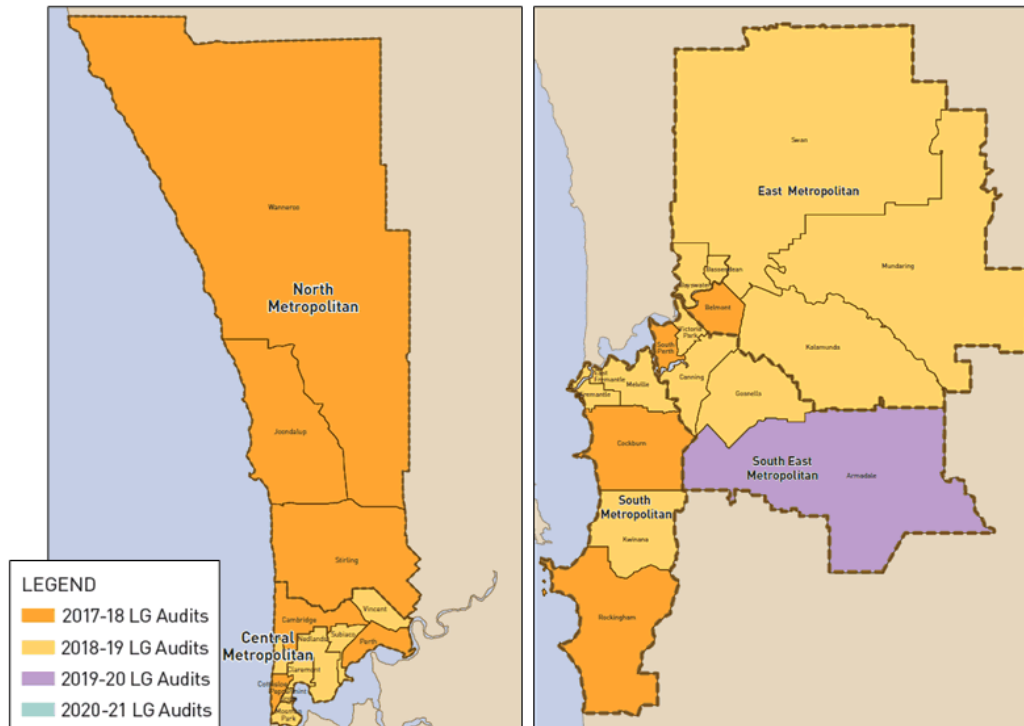
The following maps show the local governments where we performed annual financial audits for 2017-18 (these are also listed at Appendix 1) and the transitioning schedule for other local governments over the next 3 years:



Map 1: Regional WA showing Auditor General's staged transition of audits



Map 2: South West region showing the Auditor General's staged transition of audits



Maps 3 and 4: Metropolitan WA showing Auditor General's staged transition of audits

Local government entity annual financial reporting framework and timeline

Each LG is required to prepare an annual financial report that includes:

- a Statement of Financial Position, Statement of Comprehensive Income by Nature or Type, Statement of Comprehensive Income by Program, Statement of Changes in Equity and Statement of Cash Flows
- a Rate Setting Statement
- seven financial ratios required under section 50(1) of the Local Government (Financial Management) Regulations 1996 (LG Financial Management Regulations), to be reported in the Notes to the financial report.

Under section 6.4(3) of the *Local Government Act 1995* (LG Act), a LG must submit its financial report for audit to the OAG by 30 September. Many of the 46 LGs we audited for 2017-18 submitted their financial reports for audit well in advance of this deadline. However, 10 submitted after 30 September 2018.

We completed 38 of the audits by 31 December 2018 as required by section 7.9 of the LG Act. A further 4 were completed after 31 December, and 4 are still being finalised, of which 3 were due to difficulties finalising asset balances.

Summary of auditor's reports issued

At 1 March 2019, we had issued auditor's reports for 42 LGs for the financial year ending 30 June 2018.

The auditor's report includes:

- the audit opinion on the annual financial report
- a description of significant non-compliance (if any) in relation to the financial report or other financial management practices
- an opinion whether there were any material matters that indicate significant adverse trends in the financial position of the LG.

Under the Amendment Act, the chief executive officer (CEO) is required to publish the annual report, including the audited financial report and the Auditor General's auditor's report, on the LG's website within 14 days of the annual report being accepted by the LG. A table of all auditor's reports issued by the Auditor General for 2017-18 is in Appendix 1.

Audit opinions on annual financial reports

An unqualified audit opinion in the auditor's report indicates the annual financial report was based on proper accounts and records, and fairly represented performance during the year and the financial position at year end. All but 2 LGs received unqualified (clear) audit opinions.

We issue a qualified opinion in our auditor's report on a LG's annual financial report if we consider it is necessary to alert readers to material inaccuracies or limitations in the financial report that could mislead readers. The following 2 LGs received a qualified opinion:

Shire of Brookton

We issued a qualified opinion as the Shire did not recognise the 2018-19 financial assistance grant of \$504,598 received from the Commonwealth Government in June 2018 as revenue in accordance with Australian Accounting Standard AASB 1004 'Contributions'.

Instead, the Shire advised that it intended to recognise the revenue in 2018-19, and recorded the grant as Trade and other payables at 30 June 2018.

This resulted in the Shire's net result for the year being understated by \$504,598 in its Statements of Comprehensive Income and its Trade and other payables in the Statement of Financial Position being overstated by the same amount.

In addition, this resulted in understatement of the current, debt service cover and operating surplus ratios disclosed in the Notes to their financial report.

Town of Cambridge

The opinion of the Town was qualified because in previous years the interest earned on invested trust funds was incorrectly recognised as income instead of being returned to the entitled recipients as required by the LG Act.

In 2017-18, to partially address this, the Town made a prior year adjustment to reduce income and cash balances, and also revised related Notes to the financial report.

The Town's best estimate of the cumulative effect of interest earned on trust funds at 30 June 2018 was approximately \$450,000, of which a portion that had not yet been determined should have already been paid back to entitled recipients.

Prior year qualified opinion – 2017-18 audit still in progress

In 2016-17 the Shire of Laverton received a qualified opinion on its financial report because the auditor was unable to confirm that land, buildings, plant and equipment, furniture and equipment tools and infrastructure assets were reported at fair value.

The 2017-18 audit is still in progress because key aspects of a valuation, performed during the year, are still being reviewed.

Material matters of non-compliance with legislation

Regulation 10(3)(b) of the Local Government (Audit) Regulations 1996 (LG Audit Regulations) requires the auditor to report, in the auditor's report, any matters indicating non-compliance with Part 6 of the LG Act, the Local Government (Financial Management) Regulations 1996 (LG Financial Management Regulations) or applicable financial controls in any other written law. These matters may relate to the financial report or to other financial management matters.

In determining which matters to report, we apply the principles of materiality, as required by Australian Auditing Standard ASA 320 *Materiality in Planning and Performing an Audit*. Factors that we consider include the extent and frequency of the non-compliance, and the effect or potential effect.

Some of the matters we have reported relate to non-compliance with specific sections of the LG Act or regulations. We consider regulation 5(1) of the LG Financial Management Regulations to be particularly important, because failure to effectively apply those requirements can result in significant financial loss, inefficiency, financial misreporting or fraud. Regulation 5(1) requires efficient systems and procedures to be established, including:

- for the proper maintenance and security of the financial records of the LG
- to ensure proper accounting for municipal or trust revenue, expenses, assets and liabilities
- to ensure proper authorisation for the incurring of liabilities and the making of payments
- for the maintenance of payroll, stock control and costing records
- to assist in the preparation of ... accounts and reports required by the Act or the regulations.

We considered many of the findings that we reported to represent non-compliance with this important section of the LG Financial Management Regulations.

Our individual findings were included in our auditor's reports which are included in annual reports on each LG's website. For the convenience of Parliament and the public, we have summarised the matters we reported in the following table:

Issue	Finding
Controls over accounting journal entries	At 12 LGs, we found that accounting journal entries were posted with no evidence of independent review and approval by another person. Accounting journals can represent significant adjustments to previously approved accounting transactions, and could result in, for example, one type of expenditure being re-coded to another type of expenditure. Journals should therefore be subject to independent review.
Quotes not obtained for purchases below the tender threshold	At 4 LGs, 26% to 57% of purchases we sampled below the \$150,000 tender threshold had inadequate or no evidence that a sufficient number of

	<p>quotations was obtained, to test the market. There was no documentation to explain why other quotes were not sought.</p> <p>This practice increases the likelihood of not receiving value for money in procurement. This could also result in favouring of certain suppliers, although our audits did not identify any instances.</p>
Review not performed of systems and procedures	At Bunbury-Harvey Regional Council, a review of the appropriateness and effectiveness of the Council's systems and procedures in relation to risk management, internal controls and legislative compliance was not completed at least once every two years as required by Regulation 17 of the LG Audit Regulations. The last review was in 2014.
Approval to make investments	At City of Cockburn, the officer sending communications to the City's investment advisor, instructing them to make investments, had not been delegated with authority to issue these instructions. Although management advised that another officer with delegation was consulted before making investment decisions, there was no evidence of consultation and no approval of the instructions to invest.
Inadequate recordkeeping for infrastructure assets	<p>A stocktake of infrastructure was conducted at the City of South Perth for the first time in a number of years, and the City found \$21 million of infrastructure assets that was not recorded on the asset register.</p> <p>The asset register has however now been appropriately updated.</p>
System access controls	<p>More employees than necessary at the Shire of Brookton had the ability to make modifications in the system to the rates used for fees and charges. The Shire did not have a system logging process to report and review changes made to fees and charges.</p> <p>In addition, a shared account could be used to modify creditor and debtor details in the system. This increased the risk of unauthorised changes to key information, although our audit sampling did not identify any.</p>
Financial ratio not reported	<p>The Shire of Bruce Rock did not report the Asset Renewal Funding Ratio in the annual financial report as required by regulation 50(1)(c) of the LG Financial Management Regulations, as planned capital renewals and required capital expenditure were not estimated in a long term financial plan and asset management plan respectively.</p> <p>The Shire has advised that the plans are currently being completed.</p>
Financial ratios not reported	<p>The Shire of Denmark did not report the Asset Renewal Funding Ratio in the annual financial report as required by regulation 50(1)(c) of the LG Financial Management Regulations, as planned capital renewals and required capital expenditure were not estimated in a long term financial plan and asset management plan respectively.</p> <p>The Shire also did not report the Asset Consumption Ratio for 2017 and 2016 in the annual financial report as required by regulation 50(1)(c) of the LG Financial Management Regulations, as current replacement cost of depreciable assets was not estimated in previous years.</p>
Financial ratio not reported	The Shire of Kondinin did not report the Asset Renewal Funding Ratio in the annual financial report as required by section 50(1)(c) of the LG Financial Management Regulations, as management considered the available information on planned capital renewals and required capital expenditure was unreliable.
No signed employment contracts for 3 staff	For 3 employees at the Shire of Koorda, there were no signed employment contracts or letters of employment in the Shire's records.

Lack of policies, review not performed of systems and procedures, and financial ratio not reported	<p>The Shire of Nungarin had not developed key policies and procedures, such as purchasing and risk management policies.</p> <p>A review of the appropriateness and effectiveness of the Council's systems and procedures in relation to risk management, internal controls and legislative compliance was not completed at least once every two calendar years as required by Regulation 17 of the LG Audit Regulations.</p> <p>The Shire has not reported the Asset Renewal Funding Ratio for 2016, as planned capital renewals and required capital expenditure were not estimated in a long term financial plan or asset management plan, as required by the LG Financial Management Regulations.</p>
Bank reconciliation	<p>Several monthly bank reconciliations at Shire of Perenjori were not completed in a timely manner, and some were not independently reviewed by management. In addition, one had alterations that were not explained, and one did not have schedules to support the reconciling items.</p>
Review not performed of systems and procedures	<p>A review of the appropriateness and effectiveness of the Council's systems and procedures in relation to risk management, internal controls, and legislative compliance was not completed by the Shire of Tammin at least once every two calendar years as required by Regulation 17 of the LG Audit Regulations.</p>
Approval of payments, bank reconciliations and reporting to Council	<p>For 19 of 26 payments we sampled at Shire of Yalgoo, there was no evidence of the signing officers examining supporting documentation to payments and documenting approval.</p> <p>Several monthly bank reconciliations were not completed in a timely manner, and some were not independently reviewed by management. In addition, the 30 June 2018 bank reconciliation included numerous uncleared payments and deposits in excess of 12 months old.</p> <p>Due to difficulties implementing new accounting software, four statements of financial activity were not presented at an ordinary meeting of Council within two months after the end of the month to which the statement relates, which is not in compliance with Regulation 34(4)(a) of the LG Financial Management Regulations.</p>
Delegations, reporting of financial ratio, and reporting of a separate balance sheet for a trading undertaking	<p>In April 2018 at the Town of Cambridge, Council approved a delegation to the CEO to make payments from the municipal fund. Management was however not able to provide evidence that these powers had been delegated prior to that date. Payments from the municipal fund were approved by the CEO or other staff prior to April 2018.</p> <p>The Town also did not report the Asset Renewal Funding Ratio for 2016 and 2017 as planned capital renewals and required capital expenditure were not estimated in the long term financial plan and asset management plan respectively, as required by the LG Financial Management Regulations.</p> <p>The Town did not report a balance sheet for its major trading undertaking, the Wembley Golf Course, in the Notes to the financial report, as required by regulation 45 of the LG Financial Management Regulations.</p>

Table 1: Material non-compliance with legislation reported in auditor's reports

Adverse trends in the financial position of local government entities

Regulation 10(3)(a) of the LG Audit Regulations requires the auditor to report, in the auditor's report 'any material matters that in the opinion of the auditor indicate significant adverse trends in the financial position or the financial management practices of the local government'.

A performance audit of adverse financial trends would typically consider numerous aspects of a LG's finances, and inter-relationships between financial ratios. However, for purposes of the annual financial audit process, we have limited our audit to a high level assessment of whether the 7 financial ratios reported in the notes to the financial report achieved the standards set by the Department of Local Government, Sport and Cultural Industries (the Department). When determining whether a trend was significant, in some instances we allowed for a ratio to be slightly lower than the Department's standard, in recognition that failing to meet some standards is more significant than failing to meet others.

LGs report these ratios for the current year and the preceding 2 years. Our trend analysis was limited to these 3 years of information.

The 7 ratios, defined in regulation 50(1) of the LG Financial Management Regulations are:

- current ratio
- asset consumption ratio
- asset renewal funding ratio
- asset sustainability ratio
- debt service cover ratio
- operating surplus ratio
- own source revenue coverage ratio.

We reported that 38 ratios at 24 LGs indicated adverse trends. It is important to note that although most of the ratios are useful indicators, further assessment would be necessary before concluding on the overall financial position of an entity.

Emphasis of Matter included in auditor's reports

Regulation 16(a) of the LG Financial Management Regulations requires that the financial report of a LG is not to include the value of certain types of land, including land under roads, that are managed by or under the control of the LG. The Department informed us that it considered that the benefits of reporting land under roads did not justify the cost of its periodic valuation. The exclusion of any land under roads acquired on or after 1 July 2008 is inconsistent with Australian Accounting Standard AASB 1051 *Land Under Roads*. Regulation 4(2) of the LG Financial Management Regulations provides that if a provision of the Australian Accounting Standards is inconsistent with a provision of a regulation, then the regulation prevails to the extent of the inconsistency.

We noted that this significant divergence from the accounting standards was not being clearly disclosed in the annual financial reports of LGs. As land under roads is reported for the WA State Government sector and some other LG jurisdictions, we considered it important to alert readers to this different method of reporting. We requested that LGs prominently disclose this in their accounting policy notes to their financial reports. Although we considered that this inconsistency between the regulations and the accounting standards did not warrant a qualified audit opinion, we included an Emphasis of Matter paragraph in our auditor's reports to highlight this accounting treatment for readers:

Regulation 16 of the Local Government (Financial Management) Regulations 1996 does not allow a local government to recognise some categories of land, including land under roads, as assets in the annual financial report. My opinion is not modified in respect of this matter.

Financial and management controls

In addition to the material non-compliance matters reported in our auditor's reports (see Table 1 on pages 11 to 13), we reported other matters to management, including less material non-compliance as well as financial management and information system control weaknesses identified in our audits. These management letters, together with the auditor's report, form part of our overall audit report that we provide under section 7.12AD of the LG Act to the mayor, president or chairperson, the CEO and the Minister for Local Government on completion of the audit.

In our management letters, we provide a rating for each matter reported. We rate matters according to their potential impact, and base our ratings on the audit team's assessment of risks and concerns about the probability and/or consequence of adverse outcomes if action is not taken. We consider the:

- quantitative impact – for example, financial loss
- qualitative impact – for example, inefficiency, non-compliance, poor service to the public or loss of public confidence.

Risk category	Audit impact
Significant	Those findings where there is potentially a significant risk to the entity should the finding not be addressed by the entity promptly.
Moderate	Those findings which are of sufficient concern to warrant action being taken by the entity as soon as practicable.
Minor	Those findings that are not of primary concern but still warrant action being taken.

Table 2: Risk categories for matters reported to management

We give LG management the opportunity to review our audit findings and provide us comments prior to completion of the audit. When management responds to our draft management letters, we request them to set a time frame for remedial action to be completed. Often management improves policies, procedures or practices soon after we raise them and before the audit is completed. Other matters may take longer to remedy and we will follow them up during our subsequent annual audits.

During 2017-18, we alerted 40 LGs to control weaknesses that needed their attention. We reported 290 control weaknesses, of which 56 rated as significant and 186 as moderate.

Figure 4 shows a breakdown of the categories of control weaknesses identified in our 2017-18 management letters.

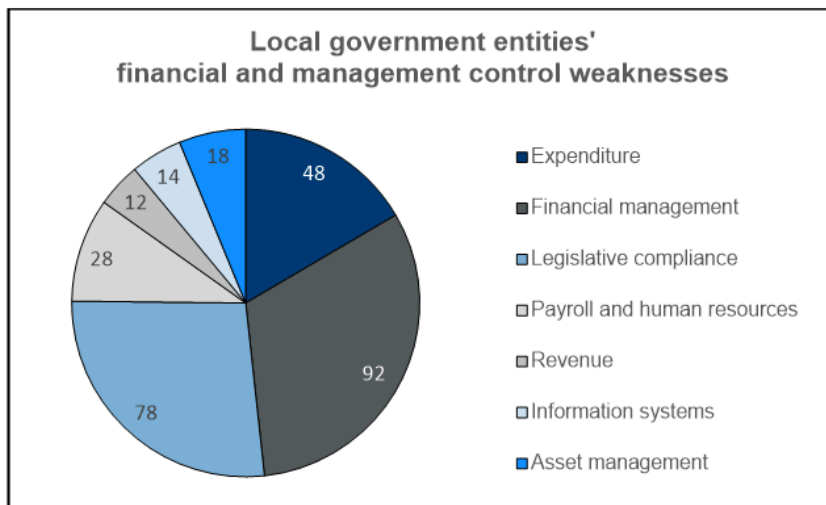


Figure 4: Financial and management control weaknesses reported to LGs

Recommendations

LGs should ensure they maintain the integrity of their financial control environment by:

- a. periodically reviewing and updating all financial, asset, human resources, governance, information systems and other management policies and procedures and communicating these to staff
- b. conducting ongoing reviews and improvement of internal control systems in response to regular risk assessments
- c. regularly monitoring compliance with relevant legislation
- d. promptly addressing control weaknesses brought to their attention by our audits.

Observations that may improve audit outcomes

The annual financial audit is focussed on providing assurance over a LG's annual financial report. During the audit we also make audit findings regarding compliance and financial and information system controls.

In this first year of auditing local government we have made some initial observations regarding opportunities for improving audit outcomes which would contribute to improved governance, financial management and performance for enhanced community satisfaction and confidence in LGs. It is important to note that each of the following issues was observed, with differing frequency across the LGs we audited.

Compliance vs better practice

At some LGs we noted an emphasis on minimum compliance (with the detailed regulations), rather than broader principles of good internal control and governance. In some instances, LG officers questioned why we were reporting their failure to comply with internal policies – it was apparent that some only regarded non-compliance with legislation to be an audit issue.

In our reporting we have made, and intend to continue making recommendations that not only address non-compliance, but which also assist to achieve better practice in financial management and control. This is aimed at remedying weaknesses before they contribute to potential breaches of legislation.

Internal audit

Only 11 of the 42 LGs we surveyed had an internal audit function. An effective internal audit function is important for ongoing maintenance and improvement of risk management, internal control and governance processes. The internal audit function acts as the independent eyes and ears for council on LG administration in key areas of risk. While recognising the difficulties for regional LGs to maintain an effective, independent internal audit function, we encourage LGs to collaborate with a view to effective internal audit assurance. We propose to cover this topic further in future performance audits.

Interaction with audit committees - audit entrance and exit meetings

Effective audit entrance and exit meetings are essential to good audit outcomes. These should facilitate informed, respectful and robust exchange between the auditors, management and the audit committee. This was the case for several of the 2017-18 audits.

On other audits however, the exit meeting was held with the entire council and this often hindered detailed discussion of the audit issues, due to the formality of proceedings and number of attendees. Section 7.12A of the LG Act requires the LG to meet with the auditor at least once each year, with the meeting typically occurring on completion of the audit. We strongly support this approach.

However, because of the number of attendees and time pressures at a full council meeting, it is preferable that, in advance of the council meeting, a more detailed exit meeting is held with the audit committee. The committee should preferably include a few council members only, with relevant skills/background in finance, risk management or auditing. We noted that 27 out of 42 LGs we surveyed had audit committees which included 5 or more council members. This is not considered better practice for facilitating effective entity-auditor communication, however we do recognise the potential challenges for regional entities in appointing members with specialist skills to their audit committees and the evident interest of councillors in audit-related matters.

We also made the following observations:

- In the past, it has generally not been common practice for audit entrance meetings to be held with the audit committee or council, and some exit meetings have also not been held with the audit committee or council. Australian Auditing Standard ASA 260 *Communication With Those Charged With Governance* requires the auditor to discuss certain key aspects of the audit planning and the audit results with those charged with governance. As a committee of council, the audit committee is the usual forum to enable effective audit communication.
- It is better practice for the auditors to highlight and explain the key elements of their entrance or closing report to the audit committee and management. Most of the meetings, especially exit meetings, did not follow a format that facilitated this but rather moved straight to councillors questioning the auditors. While this is important and as auditors we are happy to answer questions, as outlined above there are key matters that an auditor should directly communicate to those charged with governance.
- In some exit meetings, CEOs were, in our view, not given adequate opportunity to participate due to the formality of proceedings during audit meetings. CEOs and finance officers provide important information to those charged with governance, including updates on how audit findings have been prioritised and actioned.

At Appendix 3, we have briefly set out better practice guidelines for communications between auditors, management and councils.

Disclosure of audit communications

Sometimes during our planning or interim audit visit, we issue interim management letters to the CEO and council, to provide them early advice of our audit findings, to enable them to take timely remedial action.

However, these findings only form part of our report under section 7.12AD of the LG Act when we issue them as part of our report on completion of our audit. For this reason, our interim management letters advise that they may not be suitable for other purposes. They are not intended for public release until we issue them as part of our Audit Report, and indeed in our performance audit processes disclosure of draft findings is prohibited by the *Auditor General Act 2006* (AG Act).

Some LGs have made these interim management letters public. However, we regard them as 'working documents' until we issue them formally to the mayor, president or chairperson, the CEO and the Minister for Local Government as part of our final report.

Recommendations

1. In addition to compliance with legislation, management should promote a culture of applying better practice and complying with internal policies.
2. An in-depth audit exit meeting should be held with the audit committee, in advance of the council meeting. As far as is practicable, the audit committee should include a few council members, rather than the entire council.
3. An audit entrance meeting should be held with the audit committee.
4. Audit exit meetings should provide the auditor the opportunity to highlight the key audit issues, in a structured manner, and the CEO adequate opportunity to comment.
5. LGs should not make interim audit findings public until they are received as part of our Audit Report on completion of the audit, unless specific urgent needs warrant earlier release.

Auditor independence

OAG staff and contractors are required, by the AG Act, the ethical requirements of the Accounting Professional and Ethical Standards Board's APES 110 *Code of Ethics for Professional Accountants* and APES 320 *Quality Control for Firms*, and auditing standard ASQC1¹, to be independent of the entities we audit.

Prior to assuming responsibility for LG financial audits, we were aware that it was often common practice for the existing auditors to perform other work for LGs, in addition to the annual financial audit. This can impair an auditor's independence. We have therefore given careful consideration to this, taking into account factors including:

- limited access to alternate accounting firms in regional areas to perform these other tasks
- the efficiencies that can sometimes be achieved if, for example, the auditor of the annual financial report also audits grant acquittals
- the key principle that auditors should not audit financial reports that they have prepared, to avoid the 'self-review threat to independence'
- whether some of the "other" tasks should be performed as part of the annual financial audit rather than as a separate task.

In 2017-18, we approved our contract auditors to perform various other audit tasks, in addition to the annual financial audit. We require our contractors to seek our approval, in advance. This is mainly to ensure that the nature of the proposed task does not impair their independence, and also to ensure that their fee is not too high in comparison to the fee for the annual financial audit, as that could also impair auditor independence.

For grant acquittals, including Royalties for Regions or Roads to Recovery, we generally permitted our contract auditors to, after obtaining our approval, engage directly with LGs and complete the required acquittals.

We also noted that some other work performed by audit firms was being regarded as separate from the annual financial audit, with separate fees, whereas part of the work should be routinely performed during the annual financial audit. For example, audit firms have often performed reviews of systems and procedures for the CEO as required by regulation 17 of the LG Audit Regulations or regulation 5(2)(c) of the LG Financial Management Regulations. Much of this work should already be covered during the annual financial audit and included in that audit fee. In our view, this had the effect of under-stating the audit fees for annual financial audits. We have taken steps to ensure adequate review of systems and controls as part of our annual financial audit process.

Some LGs also inquired whether our contract auditors could provide training to LGs where they were performing audits on our behalf. It is OAG practice that our contract auditors may provide general training in areas such as accounting principles or new accounting standards to entities, provided the fees are not so high as to impair their audit independence.

Independence can also be impaired through auditors instructing accounting staff on specific accounting entries that the auditors would subsequently audit. All additional work must be considered on a case by case basis for threats to impairment of auditor independence.

¹ ASQC1 Quality Control for Firms that Perform Audits and Reviews of Financial Reports and Other Financial Information, Other Assurance Engagements and Related Services Engagements

Financial reporting challenges relating to asset valuations

During our audits we noted a variety of valuation methodologies being used for property, plant, equipment and infrastructure in the WA LG sector. In this first year of our LG financial auditing, we noted several issues relating to these valuations. One issue was the timely completion of valuations – at least 3 audits were completed late because the LGs received their valuation reports too late.

Two other aspects were of particular concern:

- the cost of performing valuations
- inconsistent valuation methods.

The cost of performing valuations

Australian Accounting Standard 116 *Property, Plant and Equipment* requires entities to elect to measure property, plant and equipment, including infrastructure, using either a revaluation model (at fair value) or a cost model. In the public sector, it is common practice to measure assets such as land, buildings and infrastructure at fair value, requiring periodic valuations. However, it is more common for the public sector to measure assets such as equipment (including computing equipment), some plant, furnishings and motor vehicles at cost less accumulated depreciation, thereby avoiding the often significant expense and effort of periodically valuing the assets and auditing the valuations.

The WA State public sector measures these assets at cost, whereas local governments are required, by Regulation 17A of the LG Financial Management Regulations, to fair value the assets through periodic valuations. A recent revision to the LG Financial Management Regulations, effective 1 July 2018, will remove the requirement to value assets below \$5,000. However, we suggest consideration also be given to requiring local governments to report all assets in these asset sub-classes using the cost model.

Inconsistent valuation methods

Valuation methodologies used for property, plant, equipment and infrastructure in the LG sector sometimes vary significantly across the different valuers. Some revaluations performed in 2017-18 yielded significant increments or decrements compared to the values of the previous revaluations, which were generally performed between 2013 and 2015. We concluded that most of the revalued assets were reported at amounts that materially represented fair value. However, in some instances, we asked LGs and their valuers to revisit the estimated values, resulting in some amendments.

Of particular concern is the inconsistent approach across different LGs, for valuing land assets that have restricted use. These include sports grounds, parks, gardens, sumps, foreshore, or land reserved as 'bush forever'. One of the reasons for inconsistency is differing interpretations of the principles in Australian Accounting Standard AASB 13 *Fair Value Measurement*. In particular, the standard requires valuers to take into account the highest and best use to which a market participant could put the asset. However, the standard also specifies the need to take into account the characteristics of the asset, including any restrictions on sale or use.

Different valuers are applying different interpretations of these principles, resulting in significant differences in values attributed to these types of restricted use assets. This impacts comparability of the assets of local governments. Both the Australian Accounting Standards Board (AASB) and the International Public Sector Accounting Standards Board

(IPSASB) currently have projects under way relating to fair value of public sector assets, and it is anticipated that they will provide guidance that could then be consistently applied in the LG sector.

Recommendations

1. The Department should re-assess the potential advantages if LGs are required to report equipment assets using the cost model.
2. LGs should robustly assess the assumptions and methodology of their valuers, in particular the approach for valuing land assets with restricted use.
3. LGs and the Department should monitor the progress of the AASB and IPSASB public sector fair value projects.

Upcoming changes to accounting standards and the local government regulations

A number of significant changes to Australian Accounting Standards will be applicable over the next few years, some commencing in 2018-19. These, and a change to the LG Financial Management Regulations are expected to require close attention by entities' finance officers and our audit teams.

Expensing assets with a value at acquisition under \$5,000

Regulation 17A(5) of the LG Financial Management Regulations requires, with effect from 2018-19, assets with a value below \$5,000 at the time of acquisition, to be excluded from the assets reported in the financial report. These assets will instead be reported as an expense in the statement of comprehensive income in the year of acquisition.

Australian Accounting Standard AASB 108 *Accounting Policies, Changes in Accounting Estimates and Errors*, requires this amendment to the asset values to be treated as a change in accounting policy. The standard requires balances to be adjusted retrospectively, unless it is impracticable to determine the period-specific or cumulative effects of the change.

Future impact of changes to accounting standards

The following new and revised standards issued by the AASB are expected to impact LGs to varying extent:

- **AASB 9 – *Financial Instruments*** – This standard changed the classification and measurement of financial assets from 1 January 2018 and therefore applies to LGs for the 2018-19 reporting year. Another change is earlier recognition of provisions for bad/doubtful debts based on expected credit losses.
- **AASB 15 – *Revenue from Contracts with Customers*** – This standard requires revenue to be recognised by entities on the fulfilment of the performance obligations of an enforceable contract at a point in time or over time, as applicable. An example for LGs is receiving grant moneys. LGs need to allocate the grant amount to each performance obligation in the contract and recognise the revenue only when the related performance obligations are satisfied. This will be consistent with current practice for the private sector.

Also, authoritative implementation guidance has been issued for not-for-profit public sector licensors reporting transactions involving the issue of licences. This standard applied from 1 January 2018 reporting for for-profit entities, and from 1 January 2019 reporting for not-for-profit entities.

- **AASB 1058 – *Income of Not-for-profit Entities*** – This standard, in combination with AASB 15, establishes new principles for income recognition for not-for-profit entities from 1 January 2019 reporting and will therefore apply to LGs for the 2019-20 reporting year. AASB 1058 applies to transactions where assets are acquired at significantly less than fair value, including rates and grant moneys. It is anticipated that the implementation of these two standards will result in more delayed income recognition.
- **AASB 16 – *Leases*** – For lessees, this standard removes the distinction between operating leases and finance leases, and requires all leases (except short-term leases and leases of low-value assets) to be recognised as lease assets and lease liabilities on the balance sheet. This will result in the grossing-up of the balance sheet and higher expense in the early years of the lease term. Peppercorn lease assets can be elected to

be measured either at cost or at fair value. This standard applies from 1 January 2019 and will therefore apply to local governments for the 2019-20 reporting year.

- AASB 1059 – *Service Concession Arrangements: Grantors* – This standard is applicable to public sector entities (grantors) that enter into service concession arrangements with private sector operators. It requires grantors to recognise a service concession asset and, where applicable, a service concession liability on the balance sheet. The initial balance sheet accounting, as well as the ongoing income statement impacts, will have implications for grantors. AASB 1059 will apply for years beginning on or after 1 January 2020 and will apply to local governments for the 2020-21 reporting year.

We acknowledge that there are varying degrees of readiness and preparation for these new accounting standards. We are preparing and training financial audit staff in the new and revised requirements and updating relevant audit policies and procedures.

Recommendation

Local governments should continue to make timely preparations for implementation of the upcoming accounting standards changes, and the new regulation requiring assets with a value at acquisition below \$5,000 to be expensed.

Appendix 1: Local government entities audited

We have to date completed 42 of the 46 audits for 2017-18. The auditor's reports issued are listed in the table below.

LGs are listed alphabetically.

Local government	Opinion issued
Bunbury-Harvey Regional Council	29/10/2018
City of Belmont	31/10/2018
City of Bunbury	17/10/2018
City of Cockburn	27/11/2018
City of Joondalup	14/11/2018
City of Kalgoorlie-Boulder	29/11/2018
City of Perth	13/12/2018
City of Rockingham	09/11/2018
City of South Perth	29/11/2018
City of Stirling	09/11/2018
City of Wanneroo	15/11/2018
Eastern Metropolitan Regional Council	05/10/2018
Pilbara Regional Council	14/12/2018
Rivers Regional Council	11/12/2018
Shire of Brookton	13/12/2018
Shire of Bruce Rock	13/12/2018
Shire of Capel	29/11/2018
Shire of Cranbrook	01/03/2019
Shire of Cue	11/12/2018
Shire of Cunderdin	Not finalised
Shire of Dandaragan	07/12/2018
Shire of Denmark	18/12/2018
Shire of Exmouth	27/11/2018
Shire of Jerramungup	11/02/2019
Shire of Kellerberrin	05/12/2018
Shire of Kondinin	12/12/2018
Shire of Koorda	18/10/2018
Shire of Laverton	Not finalised
Shire of Menzies	Not finalised
Shire of Moora	30/11/2018
Shire of Morawa	05/12/2018
Shire of Narrogin	20/12/2018
Shire of Northampton	03/12/2018

Shire of Nungarin	31/01/2019
Shire of Perenjori	10/12/2018
Shire of Ravensthorpe	Not finalised
Shire of Sandstone	30/10/2018
Shire of Tammin	31/01/2019
Shire of Three Springs	11/12/2018
Shire of West Arthur	13/12/2018
Shire of Woodanilling	18/12/2018
Shire of Wyalkatchem	18/01/2019
Shire of Yalgoo	18/12/2018
Shire of York	27/11/2018
Town of Cambridge	17/12/2018
Town of Cottesloe	05/12/2018

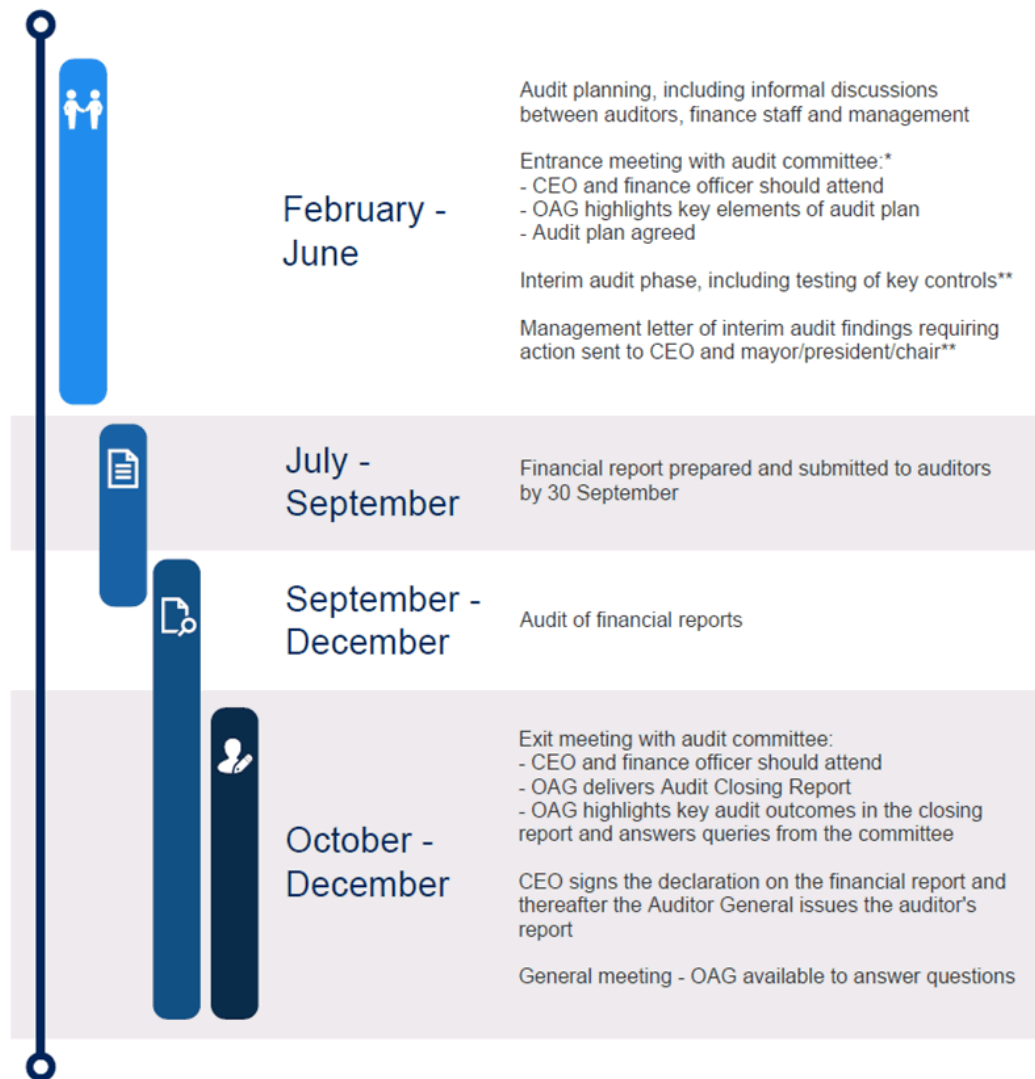
Appendix 2: Local government entity certifications issued

In addition to annual auditor's reports, some LGs needed to acquit moneys received from other sources under grant agreements or other legislation. We issued the following 3 certifications on statements of income and expenditure of LGs, to help them discharge their financial reporting obligations, some being for Commonwealth grants.

LGs are listed alphabetically.

Local government	Opinions issued
City of South Perth – <i>National Land Transport Act 2014</i> – Roads to Recovery Funding	25/10/2018
Shire of Brookton – Pensioner Deferments	13/12/2018
Town of Cambridge – <i>National Land Transport Act 2014</i> – Roads to Recovery Funding	10/12/2018

Appendix 3: Timeline of communications between auditors, management and council members



Source: OAG

Notes

Meetings with some remote LGs will be conducted by teleconference due to cost and logistical reasons.

* If it is not practicable for the audit committee to meet for an audit entrance meeting, we suggest at least one councillor attends the entrance meeting.

** For small regional LGs, there may not be an interim audit visit. This work is usually completed at the same time as the audit of the financial report, and findings are reported at that time. The extent and proposed timing of interim work will be outlined in the audit plan.

Glossary and acronyms

AASB	Australian Accounting Standards Board
AG Act	<i>Auditor General Act 2006</i>
Amendment Act	<i>Local Government Amendment (Auditing) Act 2017</i>
Auditor's Report	The Auditor General's Auditor's Report that is published in the local government's annual report by the CEO, in accordance with section 5.55A of the LG Act.
Audit Report	The overall report under section 7.12AD of the LG Act, formally issued to the Mayor, President or Chairperson, the CEO and the Minister for Local Government on completion of the audit, including the Auditor's Report and the management letter(s).
CEO	Chief executive officer
Clear opinion (or unqualified opinion)	Auditor General's opinion expressed when an annual financial audit concludes that in all material respects the financial report is presented fairly in accordance with the <i>Local Government Act 1995</i> and, to the extent that they are not inconsistent with the Act, Australian Accounting Standards.
Contract audit	Audit of a local government undertaken by an appropriately qualified individual or firm, on behalf of the Auditor General, appointed under a contract.
Department	Department of Local Government, Sport and Cultural Industries
Emphasis of Matter	A paragraph included in an auditor's report that refers to a matter that is appropriately presented or disclosed in the financial report but which, in the auditor's judgment, is of such importance that it should be emphasised in the auditor's report.
Financial audit	Work performed to enable an opinion to be expressed regarding a financial report prepared by the party who is accountable for the financial transactions.
IS	Information systems, primarily computerised systems
LG Act	<i>Local Government Act 1995</i>
LG Audit Regulations	Local Government (Audit) Regulations 1996
LGs	Local government entities, being Western Australian local governments and regional councils
LG Financial Management Regulations	Local Government (Financial Management) Regulations 1996
Management letter	A letter to management of a local government that conveys significant audit findings and results of the audit. On completion of the audit, the management letter forms part of the audit report sent to the CEO, to the Mayor, President or Chairperson, and to the Minister for Local Government.
Materiality	The characteristic based on the size and/or nature of an omission or misstatement of accounting or compliance information that, in the light of context or circumstances, has the potential to adversely affect the economic decisions of users of the information or the discharge of accountability by senior management.
OAG	Office of the Auditor General
Qualified opinion	Auditor General's opinion expressed when an audit identifies aspects of the annual financial report that are likely to be misleading to users, there was material conflict with applicable financial reporting frameworks or a limitation of scope on audit work.
Significance	Relative importance in the circumstances, in relation to audit objectives, of an item, event or information, or problem the auditor identifies.

Auditor General's Reports

Report number	Reports	Date tabled
14	Opinions on Ministerial Notifications	13 February 2019
13	Opinion on Ministerial Notification	23 January 2019
12	Managing Disruptive Behaviour in Public Housing	20 December 2018
11	Opinions on Ministerial Notifications	20 December 2018
10	Opinions on Ministerial Notifications	18 December 2018
9	Treatment Services for People with Methamphetamine Dependence	18 December 2018
8	Opinions on Ministerial Notifications	10 December 2018
7	Audit Results Report – Annual 2017-18 Financial Audits of State Government Entities	8 November 2018
6	Opinion on Ministerial Notification	31 October 2018
5	Local Government Procurement	11 October 2018
4	Opinions on Ministerial Notifications	30 August 2018
3	Implementation of the GovNext-ICT Program	30 August 2018
2	Young People Leaving Care	22 August 2018
1	Information Systems Audit Report 2018	21 August 2018



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