

4 REPORTS OF OFFICERS

4.1 ANNUAL AUDIT REPORT

Section 5.23 – Applicability

Location:

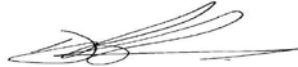
Portfolio: Governance, Administration and Finance
Cr JM Stratford

File Reference: ADM 0114

Disclosure Of Interest: No interest declared by the CEO

Author: Lana Foote, Manager of Finance & Administration

Signature of CEO



Attachment: Annual Financial Statements with Draft OAG Audit Opinion

Background:

The Draft Independent Auditor's Opinion on the Audit of the Financial Report for the year ending 30 June 2018 has been received. A copy is attached for Councillors along with the Annual Report and Annual Financial Statements for the 2017/2018 year.

This meeting will act as an exit meeting as part of the new audit requirements with the Office of Auditor General. Once the Chief Executive Officer has endorsed the audited financials and the findings, the Auditor General will respond and issue the final report and sign off within three to five business days. We hope this will be available for the October Council Meeting for Council to adopt the annual financial statements for the 2017/2018 financial year.

Comment

The audit report raised concern with the ratios, and minor issues with missing signed employee contracts. The auditor comments are clearly identified in the bellow section (the navy text being the findings from the audit, and the black text being the staff comment). The below navy exerts are from the Audit opinion, hence the personal comments.

In accordance with the *Local Government (Audit) Regulations 1996* the Auditor reports that;

(i) In my opinion, the following material matters indicate significant adverse trends in the financial position or the financial management practices of the Shire:

a. The Asset Sustainability Ratio has been below the Department of Local Government, Sport and Cultural Industries (DLGSCI) standard for the past 3 years.

The Asset Sustainability Ratio is an indicator of the extent of which assets managed by Local Government are being renewed or replaced as they reach the end of their useful lives. Standard is met if the ration can be measured and is at least 0.9. Standard is improving if this ratio is between 0.9 and 1.1. The ratio is the addition of the capital renewal and replacement expenditure, divided by the depreciation expense.

Our current asset sustainability ratio is currently sitting at 0.42. This is due to the fact, as mentioned in the previous annual financials, Council have been saving funds in reserve for the large scale recreation project and therefore as the asset is depreciating, little money is being spent and is being saved to do a large scale project. In coming years, once this large project has been

complete it may see this Asset sustainability ratio being over the “standard” figure as in one financial year, more money was spent on the asset than needed in relation to the depreciation figure.

In accordance with our long term financial plan, our Asset Sustainability Ratio does fit within the “standard.”

Comments were sought from our accountants, Moore Stephens on this note;

The Asset Sustainability Ratio – The departments standard does not consider funds accumulated in reserves for the longer term replacement of assets (given a number of assets have a useful life exceeding 10 years). Between 2017 and 2018 years the level of cash backed reserves has escalated by \$757k from \$4.8m to \$5.6m. Over the course of the last 3 years the Shire has spent significant amounts on the construction of new assets had these funds been spent renewing assets the ratio would have been 2018 – 0.91 / 2017 - 1.07 / 2016 – 0.99 all of which are above the departments target of 0.90. Whilst the ratio indicates assets are not being adequately replaced this should be considered in light of the level of spend on new assets which may be effectively replacing the services previously provided to the community by old assets. This requires further detailed analysis before determining if the ratio is in fact indicating a significant adverse trend.

- b. *The Operating Surplus Ratio for 2017-18 is below the DLGSCI standard and prior year result. The financial ratios are reported at Note 26 to the financial report.*

The Operating Surplus Ratio is an indicator of the extent to which revenue raised not only covers operational expenses, but also provides for capital funding. Basic standard between 0 and 1.5 and advanced with ratio greater than 1.5. The ratio is operating revenue minus operating expenses divided by own source operating revenue.

Our current operating surplus ratio is sitting at -0.50. Council heavily rely on grants for operational expenditure and capital renewal. Staff will investigate this further to ensure there are not long term adverse trends Council needs to be aware of.

Comments were sought from our accountants, Moore Stephens on this note;

The Operating Surplus Ratio – The Departments Benchmark of 0 indicates and expectation Shires should raise rates to a level where revenues (excluding Non-operating Grants) are able to cover the cost of all operating expenses including depreciation expense. This is despite the fact a large portion of the grants (Roads to Recovery and Regional Road Group Funding) are used for the renewal of the very assets generating the depreciation expense. Had the non-operating grants of \$900k for the renewal of assets not been excluded the Shire of Koorda would have had a positive ratio.

The ratio is heavily impacted on an annual basis by timing differences between the raising of revenue and the expenditure of this revenue as highlighted by the impact of the early payment of the FAGS grant allocations. Again far greater analysis of the matters highlighted by the ratio is required before determining if in fact there is a significant adverse trend in the financial management of the Shire.

These issues with the ratios have been previously discussed with the department and is acknowledged by their intention to revisit the ratios as part of the Local Government Act reform.

- (ii) The following material matter indicating non-compliance with Part 6 of the *Local Government Act 1995*, the *Local Government (Financial Management) Regulations 1996* or applicable financial controls of any other written law was identified during the course of my audit:
 - a. For 3 employees, there were no signed employment contracts or letters of employment in the Shire's records.
These letters were overlooked at the time of employment. Since the interim audit all three employees have now got a signed contract and letter on their file. Staff have also put procedures in place to ensure this is a standard process with a checklist to ensure documents are not forgotten and this does not happen again.
- (iii) All required information and explanations were obtained by me.
- (iv) All audit procedures were satisfactorily completed.
- (v) In my opinion, the asset consumption ratio and the asset renewal funding ratio included in the annual financial report were supported by verifiable information and reasonable assumptions.

The items raised in the Management Letter are not major issues, but if they are not looked into further, then they may become larger issues in the future. Therefore, staff will be looking into the items to where corrective actions can be taken.

Consultation:

Robert Hall – Butler Settineri
Ann Ang – Office of the Auditor General for WA
Mandy Wynne – Moore Stephens
Russell Barnes – Moore Stephens

Statutory Environment:

- Local Government Act 1995 Section 6.10 & 7.9(1)
- Local Government Financial Management Regulation 1996 Part 2
- Local Government (Audit) Regulations 1996 – Reg 10

Policy Implications:

Nil

Financial Implications:

Nil

Strategic Implications:

C 1.1 - Enhance open and interactive communication between Council and the community (ongoing)

C 3.2 - Enhance the capacity and effectiveness of administrative processes (short term)

C 3.3 - Provide reporting processes in a transparent, accountable and timely manner (short term)

Voting Requirement:

Simple majority

COMMITTEE DECISION
Office Recommendation

Moved Cr PL McWha

Seconded Cr JM Stratford

That the Audit Report, Management Letter and Annual Financial Report be received and noted with the Chief Executive Officer looking into items further where required.

PUT & CARRIED: 3/0