

### 10.3 REPORT ON AUDIT MATTER

APPLICANT: Shire of Cue  
 DISCLOSURE OF INTEREST: Nil  
 AUTHOR: Richard Towell – Acting Chief Executive Officer  
 DATE: 11 July 2019

**Matters for Consideration:**

Receiving of the report prepared to address matters identified as significant by the Auditor in the 2017-2018 Audit Report.

**Background:**

The Shire has received correspondence from the Department of Local Government, Sport and Cultural Industries (Department) dated 20 June 2018 in which the Department considers the Shire's 2017-18 Audit Report from the Auditor General dated 11 December 2018 (Audit Report) to contain a significant matter requiring the Chief Executive Officer to undertake the actions required by *Section 7.12 of the Local Government Act 1995*. This correspondence is attached at [Appendix 3](#).

**Comments:**

*Section 7.12 of the Local Government Act 1995* requires a local government to prepare a report addressing any matters identified as significant by the Auditor in the Audit Report. This report has been prepared and is attached at [Appendix 4](#).

The report has been prepared in the format recommended in Departmental Circular 05-2019, Local Government Auditing to identify the matters and outline actions taken or intended to be taken to address the matters.

The references to the appendices in the report ([Appendix 4](#)) are the same appendices included in this agenda, being [Appendix 3](#), [Appendix 5](#) and [Appendix 6](#).

**Statutory Environment:**

*Local Government Act 1995*

*7.12A. Duties of local government with respect to audits*

- (4) *A local government must —*
- (a) *prepare a report addressing any matters identified as significant by the auditor in the audit report, and stating what action the local government has taken or intends to take with respect to each of those matters; and*
  - (b) *give a copy of that report to the Minister within 3 months after the audit report is received by the local government.*
- (5) *Within 14 days after a local government gives a report to the Minister under subsection (4)(b), the CEO must publish a copy of the report on the local government's official website.*

*Local Government (Audit) Regulations 1996*

16. *Functions of audit committee*

*An audit committee has the following functions —*

- (f) to oversee the implementation of any action that the local government —*
- (ii) has stated it has taken or intends to take in a report prepared under section 7.12A(4)(a);*

**Policy Implications:**

Nil

**Financial Implications:**

Nil

**Strategic Implications:**

*Shire of Cue Strategic Community Plan 2017-2027*

*Outcome 2.1.3 Maintain accountability and financial responsibility.*

**Consultation:**

Rob Madson – Chief Executive Officer

Travis Bate – RSM Australia Pty Ltd

Julie Humphreys – CRC Coordinator

**Committee Decision:**

**Voting Requirement:** Simple Majority

That Council receives the report addressing the significant matters raised in the 2017-2018 Audit Report.

**Committee Decision: 04072019**

**Voting requirement:** Simple Majority

**MOVED: CR PRICE**

**SECONDED: CR DENNIS**

That Council receives the report addressing the significant matters raised in the 2017-2018 Audit Report.

**CARRIED: 7/0**

# APPENDIX 3



Department of  
**Local Government, Sport  
and Cultural Industries**

27 JUN 2019

Our ref CU3-4#04 E1914509  
Enquiries Stuart Fraser  
Phone 65521586  
Email [stuart.fraser@dlgsc.wa.gov.au](mailto:stuart.fraser@dlgsc.wa.gov.au)

Mr Rob Madson  
Chief Executive Officer  
Shire of Cue  
PO Box 84  
CUE WA 6640

SHIRE OF CUE	
Received .....	27/6/19
Refer to .....	CEO
File No.....	00016
Dealt With.....	

Dear Mr Madson

The Department of Local Government, Sport and Cultural Industries (the Department) has received the Shire's 2017-18 Audit Report from the Auditor General dated 11 December 2018.

The Audit Report identifies matters as significant in regard to adverse trends, qualified audits and other matters. The following matter is identified as significant by the auditor:

- Significant adverse trends in the financial position; Asset Sustainability Ratio and Asset Renewal Funding Ratio below the Department standard for the last three years.

Section 7.12A(4) of the *Local Government Act 1995* states that a local government must:

*prepare a report addressing any matters identified as significant by the auditor in the audit report, and stating what action the local government has taken or intends to take with respect to each of those matters; and*

*(b) give a copy of that report to the Minister within 3 months after the audit report is received by the local government.*

*Within 14 days after a local government gives a report to the Minister under subsection (4)(b), the CEO must publish a copy of the report on the local government's official website.*

To date it appears that a report has not been received and has not been published on the Shire's official website in accordance with Section 7.12A.

As a matter of priority the Shire must prepare a report for its Audit Committee and seek council's endorsement before forwarding a copy to the Department at [audits@dlgsc.wa.gov.au](mailto:audits@dlgsc.wa.gov.au)

As this report is now overdue, the Department requires the local government to remedy this non-compliance within the next 60 days from the date of this letter.

Gordon Stephenson House, 140 William Street  
PO Box 8349 Perth Business Centre, WA 6849  
Telephone (08) 6552 7300  
Email [info@dlgsc.wa.gov.au](mailto:info@dlgsc.wa.gov.au)  
Web [www.dlgsc.wa.gov.au](http://www.dlgsc.wa.gov.au)

For further information please review the Department's Circulars 05-2019 Local Government Auditing and 02-2018 Guide to Local Government Auditing Reforms (page 8) which are published on the Department's website.

Should you have any queries please contact the Department on the above email address or phone 65527300.

Yours sincerely



Narrell Lethorn  
Director Industry and Sector Regulation

20 June 2019

Cc Cr Ross Pigdon, President, Shire of Cue

# APPENDIX 4

## REPORT

Section 7.12A(4)(a) of the *Local Government Act 1995*

### Shire of Cue

#### **Report addressing any matters identified as significant by the auditor in the 2017-2018 Audit Report.**

##### **Purpose of Report**

Section 7.12A(4) of the *Local Government Act 1995* (Act) states that a local government must:

*Prepare a report addressing any matters identified as significant by the auditor in the audit report, and stating what action the local government has taken or intends to take with respect to each of those matters; and*

*(b) give a copy of that report to the Minister within 3 months after the audit report is received by the local government.*

*Within 14 days after a local government gives a report to the Minister under subsection 4(b), the CEO must publish a copy of the report on the local government's official website.*

The Shire has received correspondence from the Department of Local Government, Sport and Cultural Industries (Department) dated 20 June 2018 in which the Department considers the Shire's 2017-18 Audit Report from the Auditor General dated 11 December 2018 (Audit Report) to contain a significant matter requiring the CEO to undertake the actions required by Section 7.12 of the Act. This correspondence is attached at [Appendix 1](#).

The purpose of this report is to outline the actions the CEO has taken in relation to the significant matter raised in the 2018 Audit Report.

##### **Significant Matter Identified by OAG**

The Shire's 2017-18 Audit Report from the Auditor General dated 11 December 2018 (attached at [Appendix 3](#)) identified the following significant matter:

*In my opinion, the following material matters indicate significant adverse trends in the financial position 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 three years.*
- b. *The Asset Renewal Funding Ratio has been below the DLGSCI standard for the past three years.*

## Asset Sustainability Ratio

The Asset Sustainability Ratio (ASR) is calculated in accordance with *Local Government (Financial Management) Regulations 1996 R50(2)* as:

$$\frac{\text{capital renewal and replacement expenditure}}{\text{depreciation;}}$$

The ASR is reported in Note 33 of the Shire's 2018 Annual Financial Report as follows:

<b>2018</b>	<b>2017</b>	<b>2016</b>
0.43	0.64	0.67

*Local Government Operational Guidelines Number 18 – June 2013 (Guidelines)* sets out standards for each of the ratios required to be calculated under *Local Government (Financial Management) Regulations 1996 R50(2)*. The basic standard for the ASR per the Guidelines is 0.90.

## Asset Renewal Funding Ratio

The Asset Renewal Funding Ratio (ARFR) is calculated in accordance with *Local Government (Financial Management) Regulations 1996 R50(2)* as:

$$\frac{\text{NPV of planned capital renewals over 10 years}}{\text{NPV of required capital expenditure over 10 years;}}$$

The ARFR is reported in Note 33 of the Shire's 2018 Annual Financial Report as follows:

<b>2018</b>	<b>2017</b>	<b>2016</b>
0.51	0.55	0.54

The basic standard for the ARFR per the Guidelines is 0.75.

## Implication

The Asset Sustainability Ratio is an approximation of the extent to which assets managed by a local government are being replaced as these reach the end of their useful lives. The ratio indicates whether a local government is replacing or renewing existing non-financial assets at the same rate that its overall asset stock is wearing out.



The Asset Renewal Funding Ratio indicates whether the local government has the financial capacity to fund assets renewal as required, and can continue to provide existing levels of services in future, without additional income; or reductions in operating expenses. The ratio is a measure of the ability of a local government to fund its projected asset renewal / replacements in the future.

### **Management Comment**

The calculation of the Asset Sustainability Ratio excludes expenditure on new or upgrades to assets. A lot of the capital expenditure over the time line has included upgrades to assets which has excluded the expenditure from the calculations. For example the expenditure on the Post Office building fell into the category of upgrade so excluded it from the expenditure calculation, however this was a significant spend on an existing asset to repurpose it and bring it up to a new condition.

Management will consider a less conservative approach towards the expenditure that should be included in this ratio calculation in future to more closely reflect what is being spent on the renewal of existing assets.

The Asset Renewal Funding Ratio is calculated using figures from the Long Term Financial Plan and Asset Management Plan. The recent adoption of the new Strategic Resource Plan incorporating the Long Term Financial Plan and Asset Management Plan addresses this ratio to bring it within the Local Government Operational Guidelines.

### **Action Taken or Intended to be Taken**

Subsequent to the issuing of the audit report, the Shire has adopted the Strategic Resource Plan (SRP) at the 16 April 2019 Ordinary Council Meeting.

The SRP forecasts future financial ratios, including the ASR and ARFR (See [Appendix 4](#)). For both ratios identified in the 2018 Audit Report as falling below the Guidelines, the SRP forecasts these ratios to improve above the minimum level set in the Guidelines from the 2019 financial year onwards for the duration of the SRP. Please refer to the SRP for further detail.

### **Completion or Proposed Completion Date**

Management will monitor capital expenditure on asset renewals against the projected outcomes of the Strategic Resource Plan with the expectation that the ratios will improve above the minimum level set in the guidelines as projected in the SRP.

**Recommendation**

That the audit committee recommend that Council receive this report and monitor future expenditure in line with the outcomes of the Strategic Resource Plan.

# APPENDIX 5



## Auditor General

### INDEPENDENT AUDITOR'S REPORT

To the Council of the Shire of Cue

#### Report on the Audit of the Financial Report

##### **Opinion**

I have audited the annual financial report of the Shire of Cue which comprises the Statement of Financial Position as at 30 June 2018, the Statement of Comprehensive Income by Nature or Type, Statement of Comprehensive Income by Program, Statement of Changes in Equity, Statement of Cash Flows and Rate Setting Statement for the year then ended, and notes comprising a summary of significant accounting policies and other explanatory information, and the Statement by the Chief Executive Officer.

In my opinion the annual financial report of the Shire of Cue:

- (i) is based on proper accounts and records; and
- (ii) fairly represents, in all material respects, the results of the operations of the Shire for the year ended 30 June 2018 and its financial position at the end of that period in accordance with the *Local Government Act 1995* (the Act) and, to the extent that they are not inconsistent with the Act, Australian Accounting Standards.

##### **Basis for Opinion**

I conducted my audit in accordance with Australian Auditing Standards. My responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Financial Report* section of my report. I am independent of the Shire in accordance with the *Auditor General Act 2006* and the relevant ethical requirements of the Accounting Professional and Ethical Standards Board's APES 110 *Code of Ethics for Professional Accountants* (the Code) that are relevant to my audit of the financial report. I have also fulfilled my other ethical responsibilities in accordance with the Code. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my opinion.

##### **Emphasis of Matter – Basis of Accounting**

I draw attention to Note 10 to the financial report, which describes the basis of accounting. The financial report has been prepared for the purpose of fulfilling the Shire's financial reporting responsibilities under the Act. Regulation 16 of the Local Government (Financial Management) Regulations 1996 (Regulations), 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.

##### **Responsibilities of the Chief Executive Officer and Council for the Financial Report**

The Chief Executive Officer (CEO) of the Shire is responsible for the preparation and fair presentation of the annual financial report in accordance with the requirements of the Act, the Regulations and, to the extent that they are not inconsistent with the Act, Australian Accounting Standards. The CEO is also responsible for such internal control as the CEO determines is necessary to enable the preparation of a financial report that is free from material misstatement, whether due to fraud or error.

In preparing the financial report, the CEO is responsible for assessing the Shire's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the State government has made decisions affecting the continued existence of the Shire.



The Council is responsible for overseeing the Shire's financial reporting process.

### ***Auditor's Responsibility for the Audit of the Financial Report***

The objectives of my audit are to obtain reasonable assurance about whether the financial report as a whole is free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes my opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with Australian Auditing Standards will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of the financial report.

As part of an audit in accordance with Australian Auditing Standards, I exercise professional judgment and maintain professional scepticism throughout the audit. I also:

- Identify and assess the risks of material misstatement of the financial report, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for my opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Shire's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the CEO.
- Conclude on the appropriateness of the CEO's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Shire's ability to continue as a going concern. If I conclude that a material uncertainty exists, I am required to draw attention in my auditor's report to the related disclosures in the financial report or, if such disclosures are inadequate, to modify my opinion. My conclusions are based on the audit evidence obtained up to the date of my auditor's report, as we cannot predict future events or conditions that may have an impact.
- Evaluate the overall presentation, structure and content of the financial report, including the disclosures, and whether the financial report represents the underlying transactions and events in a manner that achieves fair presentation.

I communicate with the Council and the CEO regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that I identify during my audit.

### **Report on Other Legal and Regulatory Requirements**

In accordance with the *Local Government (Audit) Regulations 1996* I report that:

- (i) In my opinion, the following material matters indicate significant adverse trends in the financial position 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 three years.



- b. The Asset Renewal Funding Ratio has been below the DLGSCI standard for the past three years.  
The financial ratios are reported in Note 33 of the financial report.
- (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 were identified during the course of my audit:
  - a. 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 should therefore be independently reviewed and approved with evidence of this review being retained.
- (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.

#### **Other Matter**

The financial report of the Shire for the year ended 30 June 2017 was audited by another auditor who expressed an unmodified opinion on that financial report. The financial ratios for 2017 and 2016 in Note 33 of the audited financial report were included in the supplementary information and/or audited financial report for those years.

#### **Matters Relating to the Electronic Publication of the Audited Financial Report**

This auditor's report relates to the annual financial report of the Shire of Cue for the year ended 30 June 2018 included on the Shire's website. The Shire's management is responsible for the integrity of the Shire's website. This audit does not provide assurance on the integrity of the Shire's website. The auditor's report refers only to the financial report described above. It does not provide an opinion on any other information which may have been hyperlinked to/from this financial report. If users of the financial report are concerned with the inherent risks arising from publication on a website, they are advised to refer to the hard copy of the audited financial report to confirm the information contained in this website version of the financial report.



SANDRA LABUSCHAGNE  
ACTING DEPUTY AUDITOR GENERAL  
Delegate of the Auditor General for Western Australia  
Perth, Western Australia  
11 December 2018

# APPENDIX 6

**SHIRE OF CUE**  
**Asset Management Plan and Long Term Financial Plan**  
**2018 to 2033**

**Financial Ratios (Continued)**

	18 / 19	19 / 20	20 / 21	21 / 22	22 / 23	23 / 24	24 / 25	25 / 26	26 / 27	27 / 28	28 / 29	29 / 30	30 / 31	31 / 32	32 / 33	
	\$ 000s	\$ 000s	\$ 000s	\$ 000s	\$ 000s	\$ 000s	\$ 000s	\$ 000s	\$ 000s	\$ 000s	\$ 000s	\$ 000s	\$ 000s	\$ 000s	\$ 000s	
<b>DEBT SERVICE COVERAGE RATIO</b>																
Operating Surplus	633	1,614	1,674	1,738	1,804	1,872	1,944	2,019	2,097	2,178	2,263	2,351	2,443	2,539	2,639	
Principle and Interest	-	114	114	114	114	114	114	114	114	114	114	-	-	-	-	-
<b>Ratio</b>	-	<b>14</b>	<b>15</b>	<b>15</b>	<b>16</b>	<b>16</b>	<b>17</b>	<b>18</b>	<b>18</b>	<b>19</b>	<b>20</b>	-	-	-	-	-

**ASSET SUSTAINABILITY RATIO**

Capital Renewal Expenditure	2,875	2,561	2,298	2,081	2,333	3,846	2,434	2,417	2,643	3,253	2,712	2,894	2,512	2,878	2,689
Depreciation Expense	2,498	2,605	2,696	2,763	2,793	2,834	2,895	2,909	2,905	2,906	2,906	2,907	2,896	2,880	2,865
<b>Ratio</b>	<b>115%</b>	<b>98%</b>	<b>85%</b>	<b>75%</b>	<b>84%</b>	<b>136%</b>	<b>84%</b>	<b>83%</b>	<b>91%</b>	<b>112%</b>	<b>93%</b>	<b>100%</b>	<b>87%</b>	<b>100%</b>	<b>94%</b>

**ASSET CONSUMPTION RATIO**

Depreciated Replacement Cost	56,829	59,548	62,304	64,339	63,987	65,125	65,327	65,018	64,843	64,847	64,667	64,937	64,499	64,194	63,851
Current Replacement Cost	77,099	82,528	87,996	92,900	95,369	99,456	102,634	105,383	108,238	111,615	114,516	118,031	120,743	123,577	126,290
<b>Ratio</b>	<b>74%</b>	<b>72%</b>	<b>71%</b>	<b>69%</b>	<b>67%</b>	<b>65%</b>	<b>64%</b>	<b>62%</b>	<b>60%</b>	<b>58%</b>	<b>56%</b>	<b>55%</b>	<b>53%</b>	<b>52%</b>	<b>51%</b>

**ASSET RENEWAL FUNDING RATIO**

NPV of Planned Renewals	23,329	23,156	23,435	23,684	24,444	24,823									
NPV of Required Renewals	26,962	27,176	29,112	30,783	21,748	19,702									
<b>Ratio</b>	<b>87%</b>	<b>85%</b>	<b>80%</b>	<b>77%</b>	<b>112%</b>	<b>126%</b>									