

Audit & Risk Committee Meeting

Minutes for Monday 9 December 2013

UNCONFIRMED



**shire of
kalamunda**

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MINUTES

1.0 OFFICIAL OPENING

The Presiding Member opened the meeting at 6.45pm and welcomed Councillors and Staff.

2.0 ATTENDANCE, APOLOGIES AND LEAVE OF ABSENCE PREVIOUSLY APPROVED

2.1 Attendance

Councillors

Sue Bilich	(Shire President)	North Ward
Margaret Thomas		North Ward
Noreen Townsend		South West Ward
Allan Morton		South West Ward
Geoff Stallard		South East Ward
John Giardina		South East Ward
Frank Lindsey		South East Ward
Andrew Waddell		North West Ward
Dylan O'Connor	(Presiding Member)	North West Ward
Bob Emery		North West Ward

Members of Staff

Rhonda Hardy	Chief Executive Officer
Warwick Carter	Director Development Services
Gary Ticehurst	Director Corporate Services
Darrell Forrest	Manager Governance
Rajesh Malde	Manager Finance
Peter Hayes	Internal Auditor
Donna McPherson	Executive Research Officer/Minute Secretary

2.2 Apologies

Councillors

Simon Di Rosso	North Ward
Justin Whitten	South West Ward

2.3 Leave of Absence Previously Approved Nil

3.0 CONFIRMATION OF THE PREVIOUS MINUTES

3.1 That the Minutes of the Special Audit and Risk Committee Meeting held on 21 October 2013 are confirmed as a true and accurate record of the proceedings.

Moved: **Cr Noreen Townsend**

Seconded: **Cr Allan Morton**

Vote: **CARRIED UNANIMOUSLY (10/0)**

3.2 That the Minutes of the Audit and Risk Committee Meeting held on 5 August 2013 are confirmed as a true and accurate record of the proceedings.

Moved: **Cr Geoff Stallard**

Seconded: **Cr Andrew Waddell**

Vote: **CARRIED UNANIMOUSLY (10/0)**

4.0 CONFIDENTIAL ITEMS

4.1 N/A

5.0 DISCLOSURE OF INTERESTS

5.1 Disclosure of Financial and Proximity Interests

- a. Members must disclose the nature of their interest in matters to be discussed at the meeting. (Sections 5.60B and 5.65 of the *Local Government Act 1995*.)
- b. Employees must disclose the nature of their interest in reports or advice when giving the report or advice to the meeting. (Sections 5.70 and 5.71 of the *Local Government Act 1995*.)

Nil.

5.2 Disclosure of Interest Affecting Impartiality

- a. Members and staff must disclose their interest in matters to be discussed at the meeting in respect of which the member or employee had given or will give advice.

Nil.

6.0 REPORTS TO COUNCIL

Please Note: declaration of financial/conflict of interests to be recorded prior to dealing with each item.

Declaration of financial / conflict of interests to be recorded prior to dealing with each item.

14. Financial Statements for year ended 30 June 2013

Previous Items	Nil
Responsible Officer	Director Corporate Services
Service Area	Finance
File Reference	
Applicant	N/A
Owner	N/A
Attachment 1	Financial Statements for the year ended 30 June 2013
Attachment 2	Auditor's Report for the financial year ended 30 June 2013
Confidential Attachment 3	Audit Management Letters and Administration's Response <i>Reason for Confidentiality – Local Government (Administration) Regulations 1996</i> R14 (2) "Nothing in Sub regulation (1) entitles members of the public to inspect the information referred to in that sub regulation if in the CEO's opinion, the meeting or that part of the meeting to which the information refers is likely to be closed to members of the public under section 5.23(2)."

PURPOSE

1. To present to the Audit and Risk Committee the audited Annual Financial Statements for the year ended 30 June 2013 and receive the audit report as per Attachments 1 and 2.
2. For the Audit and Risk Committee to note the Audit Management Letter and the response provided to the issues raised.

BACKGROUND

3. The Annual Financial Statements for the year ended 30 June 2013 were prepared in accordance with the requirements of the *Local Government Act 1995 (the Act)*, the *Local Government (Financial Management) Regulations 1996*, and Australian Accounting Standards presented for audit to the Shire's Auditor, UHY Haines Norton, Chartered Accountants.

DETAILS

4. The external auditor has completed the audit and issued an independent audit report on the financial statements for the year ended 30 June 2013. Aside from two matters of regulatory non-compliance the auditor is satisfied that the Financial Statements of the Shire of Kalamunda for the year ended 30 June 2013 is in accordance with the the Act; and
 - a) gives a true and fair view of the Shire's financial position as at the 30 June 2013 and of its performance for the year ended on that date; and

- b) complies with Australian Accounting Standards, the Act and the Local Government (Financial Management) Regulations 1996 (as amended) (the Regulations).

STATUTORY AND LEGAL IMPLICATIONS

5. *Local Government Act 1995*, Section 6.4 – Financial Report
Local Government (Financial Management) Regulations 1996, Regulation 51 – Annual Financial Report to be signed by CEO and given to Department of Local Government & Communities.
Local Government (Financial Management) Regulations 1996, Regulation 16 – Land under local government's control, accounting for.
Local Government (Financial Management) Regulations 1996, Regulation 17A – Assets, valuation of for financial reports.

POLICY IMPLICATIONS

6. Nil.

PUBLIC CONSULTATION/COMMUNICATION

7. Nil.

FINANCIAL IMPLICATIONS

8. The Shire is required to present the Financial Statements reflecting its true and fair position at 30 June 2013. The Shire would be required to address at its earliest any negative observations noted during the audit.

STRATEGIC AND SUSTAINABILITY IMPLICATIONS

Strategic Planning Implications

9. The Shire undertook two budget reviews during the year to ensure its levels of income and expenditure was in line with the adopted annual budget.

Sustainability Implications

Strategic Planning Alignment

10. *Kalamunda Advancing: Strategic Community Plan to 2023*
Objective 6.8 – To ensure financial sustainability through the implementation of effective financial management, systems and plans.
Strategy 6.8.4 Provide effective financial services to support the Shire's Operations and to meet sustainability planning, reporting and accountability requirements.

Social implications

11. Nil.

Economic Implications

12. Nil

Environmental Implications

13. . Nil.

RISK MANAGEMENT CONSIDERATIONS

14. The following risks have been considered:

Risk	Likelihood	Consequence	Action / Strategy
Over expenditure compared to budget	Medium	Major	<ul style="list-style-type: none">• Monthly management reports are reviewed by the Shire.• Weekly engineering reports on major projects and maintenance. Reviewed by the Shire.
Insufficient disclosure	Low	Major	<ul style="list-style-type: none">• The financial report is scrutinized by the Shire to ensure that all statutory requirements are met.

OFFICER COMMENT

15. This report focuses on five Statements included in the Annual Financial Statements for the year ended 30 June 2013 in attachment 1, being:

1. Statement of Comprehensive Income by Nature and Type (Page 3).
2. Statement of Comprehensive Income by Program (Page 4).
3. Statement of Financial Position (Page 5).
4. Rate Setting Statement (Page 8).
5. Note 13. Cash-Backed Reserves (Page 37-41).

1 Statement of Comprehensive Income by Nature and Type

16. The Total Comprehensive Income of \$2,342,096 is \$1,940,099 less than budget. Some of the more significant items contributing to the lower net result are:
- | | | |
|----|---|----------------|
| a. | Write off of assets of | (\$2,750,070) |
| b. | Decrease in fees and charges of | (\$612,772) |
| c. | Increase in utility charges of | (\$404,794) |
| d. | Increase in other revenue of | \$2,226,281 |
| e. | Decrease in profit on disposal of assets of | (\$2,252,216) |
| f. | Increase in equity in EMRC of | \$2,516,642 |
| g. | Decrease in interest of | (\$90,941) |
| h. | Increase in rates of | \$692,983 |
17. a The following assets were written off during the financial year:
- Alan Fernie Pavilion, 35 Weston Road, Pickering Brook
 - Hartfield Park House
 - Kiosk - Hartfield Park
 - Kiosk - Kostera Oval
 - Fleming Reserve Toilets
 - Lewis Road Residence
 - Maida Vale Iron Clad Shed - Scouts
- b. Decrease in fees and charges arose principally due to an error in computing pensioners rebate for the waste fees required to recover the costs incurred. This was approximately \$550,000.
- c. Utility Charges for electricity increased excessively again this financial year made up by approximately 50% from street lighting, and the rest from Shire properties. The Shire has been actively looking at its own energy use with the commencement of energy audits of its main sites and reviewing its tariff rates with Synergy. Initiatives will commence in 2013/2014 to introduce these strategies
- d. Other revenues are significantly higher due to the initial recognition of the Hartfield Park Golf Course in line with legislative changes introduced by Regulation 16 of the Local Government (Financial Management) Regulations 1996. The amount recognised a valuation of \$2,249,250.
- e. The decrease in profit on sale of land is due to the deferment of the land sales related to Edney Road/Cygnet Court and Hale Road.
- f. Recognition of increase in Equity in Eastern Metropolitan Regional Council (EMRC) as per their audited financial statements.
- g. Decrease interest earning was affected by the late raising of rates and lower interest rates on investments.
- h. Rates revenue was higher due to additional interim rates raised in the year worth \$614,995.
- i. Employee Costs were slightly under budget due to staff vacancies in various operational units.
- j. Materials and Contracts expenditure suffered a significant increase due to higher than expected costs for verge collection conducted in

June 2013 and infrastructure maintenance costs due to ageing assets. To allow for this over- expenditure, the Shire made a decision to defer recruitment of some vacant positions to the following year.

- k. Other expenses ran significantly higher than expected by 47 per cent. This was principally due to a reclassifications between materials and contracts and other expenditure for project related expenditure.

2 **Statement of Comprehensive Income by Program.**

Income

- 18.
- Variance on Governance revenue is principally due to contributions received from Fire and Emergency Services Administration (FESA) for the costs incurred for having a dedicated officer at the Shire.
 - General Purpose Funding and Other Property and Services need to be considered together with a net positive variance being \$583,229 which mainly related to generation of higher interim rates than estimated.
 - Law, Order and Public Safety was slightly higher with a grant received for implementing the Cat Act 2011 worth \$26,000 and increased infringements issued by the Rangers worth \$18,000;
 - Health fees were higher with the introduction of provision of services to regional Shires, higher supervision fees;
 - Recreation and Culture is significantly higher income due to the recognition of the Hartfield Park Golf Course, \$2,249,250 offset by lower Lease and Licences fees approximately \$141,000 and deferral of the Healthy Communities Project grant funds amounting to \$140,000; and
 - Transport variance is related to lower receipt of capital contributions.

Expenditure

- 19.
- Governance was higher than expected due to the funding of the community poll which hadn't been originally budgeted for, costing \$75,244.
 - General Purpose Funding variance is emanating from monies spent on the forensic audit and associated legal expenses which went over budget by \$105,000 offset by lower debt collection charges by \$36,000;
 - Education and welfare variance is due to savings on employees costs of \$200,000 and the operation of HACC community care programme expenditure which resulted in a \$284,000 lower than budgeted outcome. This was due to a lower demand for services;
 - Community Amenities was higher due to increased Waste charges of \$476,000 with higher charges for verge collection attributed to larger

than anticipated volume of waste being disposed of and the change in services for 2013/2014;

- Economic Services variance relates to additional employee costs in the building maintenance area as a result of the restructure of the Infrastructure Services and increase demand in maintaining community facilities; and
- In Other Property and Services, the variance relates to lower staff costs due to vacant positions part of the year in Finance and Customer Service sections.

3 Rate Setting Statement

20. The main reason for the significant changes are as follows:

The Rate Setting Statement disclosed a surplus of \$5,077,852 for the year ended 30 June 2013. This in part was due to the actual surplus after audit of the year-end financial statements being \$2,308,520 whereas the adopted 2012/2013 Annual Budget has a brought forward estimated surplus of \$303,941.

Major areas of savings include:

- Deferral on land development projects Edney Road/Cygnets Court and Hale Road resulting in a \$3.16 million saving.
- Lower land and building development resulting in \$1.29 million carry over to 2013/2014.
- Lower Infrastructure completion of \$2.83 million. Of this amount various roads made up \$2.3 million.

4 Statement of Financial Position

21. A key factor in the Statement of Financial Position is an improvement in the Net Current Position (NCA). At the 30 June 2013 the Net Current Asset position stood at of \$5,000,656 which is a significant improvement on the previous financial year previous when the NCA position was \$2,206,078.

This has been brought about by the Shire changing its cash profile which has resulted in an increase in its cash holding by 125% and shows that the various Shire strategies to improve the Shire's liquidity are effective.

5 Note 13. Cash-Backed Reserves

22. The Act required funds disclosed as being held in various Reserves be cash-backed. Compliance with this requirement has been achieved through the establishment of separate bank accounts in accordance with Regulation 8(1)(c) of the Act.

23. The net reserves balance at year-end has declined by 19% to \$2,160,828. This is a reduction of \$516,638 from the previous year, and can be attributed to two factors:
- Shire placing more funds into its municipal bank in order to increase maintenance of Shire facilities.
 - A decrease in income from land sales resulting in less funds being transferred to reserves.

Asset Valuations

24. Assets can be divided into three (3) categories
1. Plant, Furniture, Equipment.
 2. Land and Buildings.
 3. Infrastructure.
25. Treatment in the accounts for the above three (3) is generally at cost however, new Regulation 17(A) of the Regulations and Australian Accounting Standards require that all three categories should be recognised at fair value and this treatment phased in over three years. In 2012/2013 all Plant, Furniture and Equipment was brought in at fair value.
26. Land and Buildings previously revalued, has an established Asset Revaluation Reserve which currently stands at \$126,930,008. This class of asset will be revalued next year.
27. Movements during the year included the following:
- Revaluation increase of Plant and Equipment by \$481,711. The valuations were based on open market values of similar assets adjusted for condition and comparability having regard for current replacement cost, remaining useful life and residual values.
 - Write-off of several community facilities earmarked for demolition and one which was identified as in-correctly as a Shire asset resulting in an adjustment for \$3,217,332.
28. The Shire's is currently working on "fair value" for the Shire's Infrastructure and it is proposed to incorporate the revaluation into the 2014/2015 Financial Accounts via the Asset Revaluation Reserve.

Financial Ratios

29. This financial year resulted in the removal of six old financial ratios and the introduction of six new ones in accordance with new regulations. This change now places increased emphasis on asset management and sustainability. The only ratio that was retained from the previous financial years was the modified current ratio.

Of the new ratios, the Shire did not meet the preferred benchmark on 2 of the six new ratios. These were the:

- a. Asset Sustainability Ratio:
This ratio is an indication a local government is sustaining its non-

current assets by comparing the replacement and renewal of assets with the depletion of assets through depreciation. The ratio came in at 0.395 whereas the target is between 0.9 and 1.1.

The reason for this was:

- That capital expenditure over the past 2-3 years has focused on new assets and not the renewal and replacement of existing assets. For example such as the new Zig Zag Cultural Centre, new depot building and refurbishment and new equipment for the Kalamunda Water Park and expansion of Kalamunda Road. This has increased the Shire's depreciation expenditure, and had a detrimental impact on the Asset Sustainability Ratio.
- To improve the ratio in the future will there will be a strong emphasis on renewal and replacement rather than on new capital expenditure in the Long Term Financial Plan for 2014/2023 and the Asset Management Plans 2014/2023;
- The Shire has also commenced a review of the asset conditions and depreciation;
- The Shire will complete a revaluation of the Shire's Building in 2013/2014 providing correct asset values, condition assessments and revised depreciation rates.

It is interesting to note that of five Metro Local Government's randomly selected to compare the Shire's result against this specific ratio, almost all are struggling to meet the minimum benchmark for this ratio. Meeting benchmark for these new Asset Ratios will be a challenge for the local government sector.

b. Operating Surplus Ratio:

The purpose of this ratio is to ensure all operating expenditure of a local government is being funded from its own sources of revenue, leaving a surplus to fund capital expenditure. A preferred ratio of between 0.01 and 0.15 indicates a local government has sufficient surplus funds after operations to fund its capital expenditure.

- The ratio came in at (0.022). The calculations for this year included the recognition of the Hartfield Park Golf course land and significant write-off on buildings, both non-cash movements which if taken out resulted in a revised computation of (0.004) or the lower end of the target.
- The Shire was impacted by higher operating expenditure during 2012/2013, such as:
 - Depreciation was higher than estimated by \$143,789;
 - Utility costs by \$404,794 of which half related to excessive increases in street lighting costs not envisaged; and
 - Cost over runs on bulk waste verge collection programme which has been partly due to the change in method of collection from 2013/2014 and delays in collection resulting in a higher tonnage of waste having to be cleared.

The Shire recognises the importance of this ratio and will continue to keep a tight control on expenditure and expand its revenue generating capacities on all categories.

The liquidity ratio provides information on the ability of the Shire to meet its short-term financial obligations out of the unrestricted current assets at the 30 June 2013. The preferred ratio is greater than 1 meaning that for every dollar of current liability there is in excess of a dollar in unrestricted current asset. This year the ratio came in at 1.16 which shows a significant improvement from last year of 0.853 and a even better improvement from previous year of 0.138. Again, the Shire has been focussed in its outlook on income and expenditure flows with strategies in place to control financial results effectively.

30. As noted above, all ratios except for the Asset Sustainability ratio and Operating Surplus Ratio are within acceptable benchmarks as follows:-

Ratio	2013 Result	Minimum accepted benchmarks
Current Ratio	1.16	>1.0
Asset Sustainability Ratio	0.395	>0.9
Debt Service Cover Ratio	8.49	>2.0
Operating Surplus Ratio	(0.022)	>0.01
Own Source Revenue Coverage Ratio	0.781	>0.60
Asset Consumption Ratio	0.812	>0.50
Asset Renewal Funding Ratio	0.981	>0.75

It should be noted that, no one ratio should be looked at in isolation and one needs to consider the cyclical nature of capital expenditure which could result in swings from one year to the next. It may be better to review these new ratios over five years to ensure that the Shire is trending towards the required benchmarks. This will be the goal for financial management moving forward.

31. To meet the requirements of Section 7.12A(2) of the Act, the Auditors have met with Council and presented their findings.
32. The Shire's end of year financial result for 2012/2013 demonstrates the Shire is operating responsibly and is financially sustainable.

Councillors sought clarification in relation to a number of issues including:

1. *Ratios*
2. *Business Continuity Plan*
3. *Disposal of Assets*
4. *Depreciation.*

The Chief Executive Officer advised written responses would be provided.

Voting Requirement – Simple Majority

COMMITTEE RECOMMENDATION TO COUNCIL (A&R 14/2013)

That the Committee recommend that Council:

1. Receive the Audited Financial Report for the year ended 30 June 2013 shown as Attachment 1.
2. Receive the Independent Audit Report of the Shire of Kalamunda for the financial year ended 30 June 2013 as presented as Attachment 2.
3. The Committee notes the Administration's response to the Management Letters as per Confidential Attachment 3.

Moved: **Cr Margaret Thomas**

Seconded: **Cr Andrew Waddell**

Vote: **CARRIED UNANIMOUSLY**

7.0 CLOSURE

7.1 There being no further business the Presiding Member declared the meeting closed at 7.12pm.

I confirm these Minutes to be a true and accurate record of the proceedings of this Council.

Signed: _____
Presiding Member

Dated this _____ day of _____ 2013