



Shire of
Serpentine
Jarrahdale

Audit, Risk and Governance Committee Meeting

Confirmed Minutes

Tuesday 20 November 2018
5.30pm

Endorsed Council 26/11/18
OCM8.1/11/18

Contact Us

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In Person

Shire of Serpentine Jarrahdale
6 Paterson Street, Mundijong WA 6123
Open Monday to Friday 8.30am-5pm (closed public holidays)



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Minutes of the Audit, Risk and Governance Committee Meeting held in the Council Chambers, Civic Centre, 6 Paterson Street, Mundijong on Tuesday 20 November 2018.

The Presiding Member, Councillor See declared the meeting open at 5.30pm and welcomed Councillors, Committee Members, Mr Greg Godwin, Auditor Moore Stephens and Staff, and acknowledged that the meeting was being held on the traditional land of the Noongar People and paid her respects to their Elders past and present.

Minutes

1. Attendances and apologies (including leave of absence):

Councillors: Cr J See Presiding Member
Cr M Byas
Cr M Rich
Cr R Coales
Cr K McConkey

Independent Members: Ms E Newby
Mr S Casilli

Officers: Mr K Donohoe Chief Executive Officer
Mr F Sullivan Director Corporate Services
Mr S Harding Director Infrastructure Services
Ms H Sarcich Deputy CEO / Director Community Services
Mr A Schonfeldt Director Development Services
Ms A Liersch Agendas and Minutes Officer (Minute Taker)

Apologies: Nil.

Visitor: Mr Greg Godwin, Auditor, Moore Stephens

Members of the Public: Nil.

2. Public question time:

2.1 Response to previous public questions taken on notice

Nil.

2.2 Public questions

Nil.

3. Public statement time:

Nil.



4. Petitions and deputations:

Nil.

5. Declaration of Councillors and Officers interest:

Nil.

6. Receipt of minutes or reports and consideration of adoption of recommendations from Committee meetings held since the previous Council meetings:

6.1 Minutes of previous Audit, Risk and Governance Committee Meeting:

6.1.1 Audit, Risk and Governance Committee Meeting – 21 August 2018

AUDIT, RISK & GOVERNANCE COMMITTEE RESOLUTION

Moved Ms Newby, seconded Cr Rich

That the minutes of the Audit, Risk and Governance Committee Meeting held on 21 August 2018 be confirmed (E18/9202).

CARRIED UNANIMOUSLY 7/0

6.2 Reports for consideration:

ARG009/11/18 – Annual Financial Statements and Audit Report 2017- 2018 (SJ800)	
Responsible Officer:	Acting Manager Finance
Senior Officer:	Director Corporate Services
Disclosure of Officers Interest:	No officer involved in the preparation of this report has an interest to declare in accordance with the provisions of the <i>Local Government Act 1995</i> .

Report Purpose

This report presents the audited Annual Financial Statements and Audit Management Report for the 2017/2018 financial year. The Shire's Auditor, Moore Stephens, has provided the Audit Report and Management Report for the financial year ended 30 June 2018.

Relevant Previous Decisions of Council

The 2016/17 Annual Financial Report was presented to the Audit, Risk and Governance Committee on 5th December 2017 (ARG 010/23/17) and to Council at the Ordinary Council meeting on 18th December 2017 (OCM 180/12/17).

Background

Pursuant to Sections 6.4, 7.2, and 7.9 of the *Local Government Act 1995*, Local Governments are required each year to have the accounts and annual financial report of the Shire audited by an auditor appointed by the local government.



Community / Stakeholder Consultation

Nil.

Statutory Environment

Section 6.4 of the *Local Government Act 1995* states that, “the local government is to prepare an annual financial report for the preceding financial year, and submit to its auditor by 30 September following each financial year, including the accounts of the local government balanced up to the last day of the preceding financial year.

Section 7.2 of the *Local Government Act 1995* states that, “the accounts and financial statements of a local government for each financial year are to be audited by an auditor appointed by the local government.”

Section 7.9 (1) of the *Local Government Act 1995* states, “An auditor is required to examine the accounts and annual financial report submitted for audit and, by 31 December next following the financial year to which the accounts and report relate or such later date as may be prescribed, to prepare a report thereon and forward a copy of the report to:

- a) The Mayor or President;
- b) The Chief Executive Officer of the local government; and
- c) The Minister.”

Comment

Audit Report

The Audit Report from Moore Stephens includes the following emphasis of matters:

Basis of Preparation

“We draw attention to Note 1 to the financial report, which describes the basis of preparation. 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*, does not allow a local government to recognise some categories of land, including land under roads, as assets in the annual financial report. Our opinion is not modified in respect of this matter.”

Officers Comment

In respect of land under roads acquired on or after 1 July 2008, *Local Government (Financial Management Regulation 16(a)(i)* prohibits local governments from recognising such land as an asset.

Recognition of Assets Contributed by Developers

“We draw attention to Note 12 (a) to the financial report, which describes the reason for the recognition of assets contributed by developers through the revaluation surplus rather than revenue as prescribed by paragraph 12 of *AASB 1004; Contributions*. Our opinion is not modified in respect of this matter.”



Officers Comment

Whilst this information has been provided to the organisation from developers via the engineering subdivision team and has been captured within the Graphical Information System (GIS), it has not been brought into the finance function for recording. The Shire now has a dedicated cross Directorate Asset Management Team, which will assist in the management of assets going forward. This Team has been established to develop a process to ensure that these assets contributed from developers are captured at handover and recognised through the accounts as revenue, rather than through the revaluation process.

Audit Management Report

In the Moore Stephens Management Report for the financial year ended 30 June 2018, Moore Stephens would like to bring to Council's attention a significant adverse trend in financial position as evidenced by trends in ratios as discussed below;

Operating Surplus Ratio

The Operating Surplus Ratio has been below the Department of Local Government, Sport and Cultural Industries standard for the past 3 years.

The Operating Surplus Ratio represents the percentage by which the operating surplus (or deficit) differs from the Shire's own source revenue which includes rates and operating grants.

The Shire's operating result (ignoring non-operating grants, subsidies and contributions) for the year ended 30 June 2018 recorded a net deficit of \$2,825,565 which occurs when operating revenue is lower than operating expenses. We consider the Shire may have a structural deficit in its operations evidenced by the Operating Surplus Ratio trending downwards in the last 3 years and being below the target level of 0.01 for 4 of the last 5 years.

Officers Comment

The Shire has limited options to improve its income through rates or fees and charges, however there will be a continued focus on expenditure reduction and process improvement, looking for ways to reduce costs wherever possible which will see an overall improvement in the both the Operating Surplus Ratio and the Current ratio. In the last 12 months the Shire has implemented a dedicated procurement team, and processes around procurement are under constant review. Early savings identified by procurement processes have been invested in new and improved technology and an internal auditor. This should see a progressive improvement in the Shires' ability to provide increasing service levels at a lesser cost.

It is anticipated that the double impact of an increase in effectiveness and efficiency derived from the measure detailed above and redeployment of funds currently being used to implement new technology into capital projects should greatly assist Council improve this ratio.



The below table shows the trend in ratios over the last 5 years.

	Councils Adjusted Ratios (1)					5 Year Average (2)	
	2018	2017	2016	2015	2014	Regional	State
Current Ratio *	0.90	1.41	1.25	1.46	1.39	1.12	2.22
Asset Sustainability Ratio	0.66	0.64	0.71	0.84	1.22	0.87	1.18
Debt Service Ratio *	7.12	9.43	11.50	4.89	0.63	4.27	12.41
Operating Surplus Ratio *	(0.10)	(0.04)	(0.01)	0.04	(0.05)	(0.12)	(0.11)
Own Source Revenue Coverage Ratio	0.82	0.86	0.87	0.90	0.86	0.76	0.67
Asset Consumption Ratio	0.77	0.96	0.98	0.74	0.78	0.71	0.73
Asset Renewal Funding Ratio	0.46	0.67	0.56	0.44	0.62	0.97	0.94

Notes;

1. The ratios indicated with (*) have been distorted by the early receipt of Financial Assistance Grants relating to a subsequent year. They have been removed from the calculation of those ratios presented above.
2. The 5 year average is the average to 30 June 2017, as per statistics gathered by Moore Stephens and reported in the 2016/17 Management Report.

Asset Sustainability Ratio

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

The Asset Sustainability Ratio expresses capital expenditure on renewal and replacement of existing assets as a percentage of depreciation costs. This ratio is used to identify any potential decline or improvement in asset conditions.

Capital renewal and replacement expenditure was below budgeted levels for the year ended 30 June 2018, which, when coupled with an increase in the depreciation expense, indicates assets may be deteriorating at a greater rate than they are being renewed or replaced.

Officers Comment

Fair value assessment has resulted in a valuation increment of \$137 million over the last 3 years from 1 July 2015. This has resulted in an increase in depreciation expense from \$2.9 million as at 30 June 2015, to \$6.3 million as at 30 June 2018. Depreciation expense impacts significantly on the asset sustainability ratio and is the major reason for the downward trend. The Shire of Serpentine Jarrahdale is one of the fastest growing local governments in all of Australia, and the large increase in the value of our assets is reflective of the significant amount of new assets which are being handed over to the Shire by developers. The estimated useful lives of all asset classes will continue to be reviewed for appropriateness, as this also will have a significant impact on the asset sustainability ratio in future years.



Asset Renewal Funding Ratio

“The Asset Renewal Funding Ratio has been below the Department of Local Government, Sport and Cultural Industries standard for the past 3 years.

The Asset Renewal Funding ratio indicates whether the Shire’s planned capital renewal expenditure over the next 10 years as per its Long Term Financial Plan (LTFP) is sufficient to meet the required capital renewal expenditure over the next 10 years as per its Asset Management Plans (AMPs).

We note the required capital renewal expenditure is higher than the planned capital renewal expenditure by \$31.5 million over the next 10 years. Council should identify reasons why its Asset Management Plans require more renewal expenditure than is provided for in its Long Term Financial Plan. Council should also consider a review of the Shire’s long term capital investment program to help ensure asset renewal is maintained at an appropriate level with sufficient funding support in the future.”

Officers Comment

The data used in the calculation of the asset renewal funding ratios is taken from the current Asset Management Plans which have been adopted by council, and the Long Term Financial Plan. These Asset Management Plans are in the process of being updated and it is expected that the new Asset Management Plans will be presented to Council in the coming months. Once this data becomes available it will be used to update the Long Term Financial Plan, and the impact on ratios will be reviewed.

It is important that the Long Term Financial Plan and Asset Management Plans are continually reviewed with the aim of seeing a continuous improvement in these ratios. Adequate resources need to be provided for the renewal of the Shires existing assets, whilst also providing the new infrastructure that a rapidly growing Shire needs.

Current Ratio

“The Current Ratio for 2017/18 is below the Department of Local Government, Sport and Cultural Industries standard, below its level for the 2 prior years and is more than 10% below last year’s ratio.

The ratio is a measure of short term (unrestricted) liquidity. That is, the ability of the local government to meet its short term financial obligations from unrestricted current assets when they fall due.

The level of the adjusted current ratio (0.90) has reduced below the Department of Local Government, Sport and Cultural Industries target level of 1.0 and has reduced by 36% from its level last year, indicating a downward trend.

Notwithstanding this, as the current portion of borrowings is included in the calculation, we have concluded the local government does not have a short term liquidity issue. Repayment of borrowings is budgeted out of 2018-19 revenue and not from current assets as at 30 June 2018. If excluded from the calculation, the current ratio would be 1.1.”

Moore Stephens would also like to bring to Council’s attention an issue in relation to the recognition of contributed assets from developers.

“In accordance with AASB 1004 – Contributions, contributed assets should be measured at fair value and recognised as income at the time of receipt. As noted at Note 12(a) in the



financial report, insufficient data is available to accurately allocate developer contributions in revenue in each financial year. Although these assets have been recognised as part of the fair value exercise, records of all contributed assets to be recognised as income when received.

Based on our discussion with management, the Shire has a new asset coordinator and an asset management working group has been formed to address the matter.”

Officers Comment

The current ratio calculation also excludes funds currently prudently employed in a diversified portfolio as long term investments. Should this potential source of funds have been included in the calculation the ratio would have been 1.36.

Attachments

- [ARG009.1/11/18](#) - Annual Financial Report – 30 June 2018 (E18/12630)
- [ARG009.2/11/18](#) - Audit Management Report – 30 June 2018 (E18/12631)

Alignment with our Strategic Community Plan

Outcome 4.1	A resilient, efficient and effective organisation
Strategy 4.1.1	Provide efficient, effective, innovative, professional management of Shire operations to deliver the best outcome for the community within allocated resources.

Financial Implications

Nil.

Risk Implications

Risk has been assessed on the basis of the Officer's Recommendation.

Risk	Risk Likelihood (based on history and with existing controls)	Risk Impact / Consequence	Risk Rating (Prior to Treatment or Control)	Principal Risk Theme	Risk Action Plan (Controls or Treatment proposed)
That Council not adopt the Annual Financial Report	Unlikely (2)	Insignificant (1)	Low (1-4)	Compliance - 3 Moderate - Non-compliance with significant regulatory requirements imposed	Accept Officer Recommendation



Risk Matrix

Consequence		Insignificant	Minor	Moderate	Major	Catastrophic	
		1	2	3	4	5	
Likelihood	Almost Certain	5	Medium (5)	High (10)	High (15)	Extreme (20)	Extreme (25)
	Likely	4	Low (4)	Medium (8)	High (12)	High (16)	Extreme (20)
Possible	3	Low (3)	Medium (6)	Medium (9)	High (12)	High (15)	
Unlikely	2	Low (2)	Low (4)	Medium (6)	Medium (8)	High (10)	
Rare	1	Low (1)	Low (2)	Low (3)	Low (4)	Medium (5)	

A risk is often specified in terms of an event or circumstance and the consequences that may flow from it. An effect may be positive, negative or a deviation from the expected and may be related to the following objectives; occupational health and safety, financial, service interruption, compliance, reputation and environment. A risk matrix has been prepared and a risk rating of 6 has been determined for this item. Any items with a risk rating over 10 (considered to be high or extreme risk) will be added to the Risk Register, and any item with a risk rating over 17 will require a specific risk treatment plan to be developed.

Voting Requirements: **Absolute Majority**

ARG009/11/18 Officer Recommendation:

Moved Cr Coales, seconded Cr Rich

That the Audit Risk and Governance Committee recommends that Council:

1. Adopts the 2017/2018 Annual Financial Report including Independent Audit Report from Moore Stephens as per attachment ARG009.1/11/18, in accordance with Section 7.2 of the *Local Government Act 1995*.
2. Receives the Moore Stephens Audit Management Report as per attachment ARG009.2/11/18.

Presentation by Mr Greg Godwin, Auditor, Moore Stephens on the 2017 / 18 Independent Auditor's Report for the Shire of Serpentine Jarrahdale and Mr Frazer Sullivan, Director Corporate Services, on the 10 year Financial Plan.



**ARG009/11/18 AUDIT, RISK & GOVERNANCE COMMITTEE DECISION /
Officer Recommendation:**

Moved Cr Coales, seconded Cr Rich

That the Audit Risk and Governance Committee recommends that Council:

- 1. Adopts the 2017/2018 Annual Financial Report including Independent Audit Report from Moore Stephens as per attachment ARG009.1/11/18, in accordance with Section 7.2 of the *Local Government Act 1995*.**
- 2. Receives the Moore Stephens Audit Management Report as per attachment ARG009.2/11/18.**

CARRIED BY ABSOLUTE MAJORITY 7/0

Please note that the Audit, Risk and Governance Committee does not have delegated authority to make decisions. All recommendations of the Audit, Risk and Governance Committee are presented to Council for ratification.

7. Motions of which notice has been given:

Nil.

8. Urgent business:

Nil.

9. Closure:

There being no further business, the Presiding Member declared the meeting closed at 6.10pm.

I certify that these minutes were confirmed at the
Audit, Risk & Governance Committee Meeting held on

.....
Presiding Member – Councillor J See

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Date