City of Wanneroo

File Ref: 35363 (19/332143)
Enquiries: Rajesh Malde – 9405 5663

3 September 2019

Hon David Templeman
Minister for Local Government, Heritage, Culture and the Arts
7th Floor, Dumas House
2 Havelock Street
WEST PERTH WA 6005

Dear Minister

MATTERS OF SIGNIFICANCE - 2017/18 Audit Report

The City of Wanneroo received a letter from the Department of Local Government, Sport and Cultural Industries (the Department) dated 20 June 2019 in relation to the reporting non-compliance of the matter of significance as highlighted by the Office of the Auditor General (OAG).

The OAG identified in its Audit report dated 15 November 2018 that there was a significant adverse trend in the financial position: Current Ratio and Asset Sustainability Ratio below the Department standard for the last three years. This adverse position was presented to the Audit and Risk Committee on the 13 November 2018 and Council on the 27 November 2018.

As required by the Local Government Act section 7.12A (4), this non-compliance was reported to the Audit and Risk Committee on the 13 August 2019 and subsequently to Council on 27 August 2019 (Reference CS01 – 08/19).

Please find attached a report addressing this matter and the actions the City intends to take in respect of those matters. This report will be published on our website as required by the Local Government Act section 7.12A (5).

Yours sincerely

DANIEL SIMMS
CHIEF EXECUTIVE OFFICER

Attachments:
1. Report on Matters of Significance – 2017/18 Audit Report
2. Council Report CS01-08/19 – Report on Matters of Significance highlighted in the 2017/18 Audit Report

cc: Narrell Lethorn, Director Industry and Sector Regulation, Department of Local Government, Sport and Cultural Industries

REPORT ON MATTERS OF SIGNIFICANCE - 2017/18 AUDIT REPORT

Background

As part of the Statutory Audit process of the Annual Financial Statements, the OAG is required to report of any matters relating to Legal and Regulatory Requirements that come to their attention. For the City's Annual Financial Statement for the year ended 30 June 2018, the OAG identified the City was not compliant with the Current Ratio and the Asset Sustainability Ratio standard set by the DLGSCI for the past three years, which was highlighted in their Independent Auditor's Report dated 15 November 2018

This adverse position was presented to the Audit and Risk Committee on the 13 November 2018 and Council on the 27 November 2018.

As required by the Local Government Act section 7.12A (4), this non-compliance, was reported to the Audit and Risk Committee on the 13 August 2019 and subsequently to Council on 27 August 2019 (Reference CS01 – 08/19), attached for your perusal.

Detail

Please find below specific details of the two adverse ratios and the reasons explaining why the City is unable to meet the set parameters.

1. **Current Ratio**

Description	**2017/18**	**2016/17**	**2015/16**	**Benchmark**
Current Ratio	0.85:1	0.86:1	0.88:1	**1.00:1**

Extract from the DLGSCI Guidelines on Ratio's:

"Current Ratio = (Current Assets MINUS Restricted Assets) / (Current Liabilities MINUS Liabilities Associated with Restricted Assets)

Purpose: This is a modified commercial ratio designed to focus on the liquidity position of a local government that has arisen from past year's transactions.

Standards: The standard is not met if the ratio is lower than 1:1 (less than 100%) The standard is met if the ratio is greater than 1:1 (100% or greater) A ratio less than 1:1 means that a local government does not have sufficient assets that can be quickly converted into cash to meet its immediate cash commitments. This may arise from a budget deficit from the past year, a Council decision to operate an overdraft or a decision to fund leave entitlements from next year's revenues.

This ratio is used to determine if a Local Government (LG) has sufficient assets to meet its short term commitments. A ratio of less than 1 would mean that the LG may struggle to meet its short term commitments."

The City does not believe the above generalised view is correct as it deems "restricted" cash as un-accessible. While it is acknowledged that the City's Special Purpose Cash Backed Reserves are set aside for a specific purpose, the City has a detailed cash flow forecasting model in place which tracks all operating and capital inflows and outflows including the realisation of investments and transfers from/ to restricted reserves. It has managed its payment commitments without any recorded delay's in its payment cycles for creditor and staff commitments.

The City's cash holdings (restricted and un-restricted) have been progressively improving as noted below:

2014/15	2015/16	2016/17	2017/18
$316.9m	$338.7m	$340.8m	$363.5m

The City has a deliberate strategy to improve its Cash Backed Reserves Balances to enable financially sustainable and responsible management of the deliverability of large multi-year projects and long term liabilities. This strategy enables the City to ensure that it has the capacity to manage future General Rate rises/declines.

An additional benefit of having the cash holdings in Reserves is that interest income from investments can be maximised providing an additional income stream thereby reducing the need to raise additional funds from General Rates.

It should be noted that Council has the ability to transfer funds from a number of restricted reserves (e.g. Strategic Project/Initiatives Reserve) to unrestricted cash holdings should the need arise to meet cash shortfalls.

Nevertheless as it stands the City does not meet the DLGSI guidelines. However as noted above, this is by choice to ensure the City has appropriate reserves which will help smoothen General Rate rises/declines in the future.

2. **Asset Sustainability Ratio**

Description	2017/18	2016/17	2015/16	Benchmark
Asset Sustainability Ratio	0.34:1	0.32:1	0.45:1	**0.90:1**

The DLGSCI Asset Management Framework and Guidelines publication provides the following explanation in respect to the Asset Sustainability Ratio (**ASR**):

> *"If capital expenditure on renewing or replacing assets is at least equal to depreciation on average over time, then the local government is ensuring the value of its existing stock of physical assets is maintained. If capital expenditure on existing assets is less than depreciation then, unless a local government's overall asset stock is relatively new, it is likely that it is underspending on renewal or replacement."*

A large percentage of the City's assets are in new to very good condition with approximately 85% of the total asset base at or below condition two (a rating of '0' represents a new asset and a '10' represents an asset that has failed). Less than 1% of the asset base is at or above condition eight, which represents assets that require intervention.

With the City's current mix of old and new assets and continued high growth, a lower than average ASR is expected, and the current condition of assets and level of renewal expenditure confirms this position. As the stock ages and renewal expenditure incrementally increases the ratio will increase, however continued growth may keep it relatively lower than the industry standard.

Taking a long term view, the level of asset stock and renewal demand necessitates the development of strategies to address the future impact and ensure that the City can continue to grow and maintain its assets in a financially sustainable manner. Given that renewal expenditure is lower than the depreciation being charged and that certain years' experience significant spikes in demand, a specific Asset Renewal Reserve has been established.

We further note that the issue of adverse Ratio's is a Council wide issue and were discussed at the Local Government Professional's workshop held on the 23rd August 2019 at City of Kwinana.

At this meeting the Department representative acknowledged the issue required reviewing and have commenced the consultation process with the West Australian Local Government Association (WALGA) and the Local Government Professionals Australia WA.

We await the outcome of these consultations.

Rajesh Malde 27 Aug 2019

CS01-08/19 Report on Matters of Significance highlighted in the 2017-18 Audit Report

File Ref:	35363 – 19/314827
Responsible Officer:	Director Corporate Strategy & Performance
Disclosure of Interest:	Nil
Attachments:	2

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Issue

To consider the matters identified as significant by the Office of the Auditor General (OAG) as part of the 30 June 2018 Independent Auditors Report. Specifically, adverse trends of some of the reportable Ratios which were calculated in-line with reporting requirements as specified in the guidelines issued by the DLGSCI.

The matters require specific action and disclosure as per section 7.12A(4) and (5) of the Act which has not been met. This report is to remedy this compliance oversight.

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Background

As part of the Statutory Audit process of the Annual Financial Statements, the OAG is required to report of any matters relating to Legal and Regulatory Requirements that come to their attention. For the City's Annual Financial Statement for the year ended 30 June 2018, the OAG identified the City was not compliant with the Current Ratio and the Asset Sustainability Ratio standard set by the DLGSCI for the past three years, which was highlighted in their Independent Auditor's Report dated 15 November 2018 (**Attachment 1**).

On 20 June 2019, the DLGSCI brought to the City's attention (**Attachment 2**) that it has not fulfilled its requirement under the Act as noted below:

Under section 7.12A(4) and (5) of the Act, 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.*

This report is to remedy the above matter which has been an oversight by the City.

Detail

As indicated above, the OAG has highlighted under the heading, 'Report on Other Legal and Regulatory Requirements' in the Independent Auditor's Report dated 15 November 2018 that the Current Ratio and the Asset Sustainability Ratio have been below the DLGSCI set standard for the past three years.

The adverse position has been presented to the Audit and Risk Committee on the 13 November 2018 and Council on the 27 November 2018. Explanation of this position is detailed below.

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Taking a long term view, the level of asset stock and renewal demand necessitates the development of strategies to address the future impact and ensure that the City can continue to grow and maintain its assets in a financially sustainable manner. Given that renewal expenditure is lower than the depreciation being charged and that certain years' experience significant spikes in demand, a specific Asset Renewal Reserve has been established.

Consultation

The timing of the report has been discussed with DLGSCI and at the Audit and Risk Committee held on the 13 August 2019.

Comment

Necessary controls and training has been provided to the relevant staff to ensure that such future compliance reporting requirements are better managed.

On receipt of this report, the Chief Executive Officer (CEO) must notify the Minister of the action taken and ensure the same is published on the City's website within 14 days of issuance of the letter.

DLGSCI has allowed 60 days from 20 June 2019 to complete these requirements. Given the Council meeting cycle the City sought extension to this deadline and informed the DLGSCI that this report will be provided upon Council endorsement.

The above non-compliance will be required to be notified on the compilation of the Compliance Audit Return for 2018/19.

Given the City is unable to meet these ratios and it is further believed to be an industry issue, it is intended that we write to the DLGSCI explaining this situation and entering into dialogue to have these ratios reviewed.

Statutory Compliance

Local Government Act 1995, Part 7
Local Government (Audit) Regulations 1996
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Strategic Implications

The proposal aligns with the following objective within the Strategic Community Plan 2017 – 2027:

"4 *Civic Leadership*

4.2 *Good Governance*

4.2.1 Provide transparent and accountable governance and leadership"
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Risk Management Considerations

Risk Title	Risk Rating
Financial Management	Moderate
Accountability	**Action Planning Option**
Executive Management Team	Manage

The above risk relating to the issue contained within this report has been identified and considered within the City's Corporate Risk Register. Action plans have been developed to manage this risk to improve the existing management systems.

Policy Implications

Nil

Financial Implications

Nil

Voting Requirements

Simple Majority
Do not delete this line

Recommendation

That Council:-

1. NOTES the matters identified in the Independent Auditors Report to the City of Wanneroo Council for the year ended 30 June 2018, as shown in Attachment 1;

2. NOTES that the City of Wanneroo is in breach of Section 7 12A (4) and (5) of the *Local Government Act 1995* as detailed in the letter from Department of Local Government, Sports and Cultural Industries dated 23 June 2019 as shown in Attachment 2;

3. APPROVES this report identifying reasons for matters identified as significant by the Office of Auditor General in their Independent Auditors Report dated 15 November 2018; and

4. REQUESTS the Chief Executive Officer to submit a report to the Minister for Local Government, Sports and Cultural Industries commenting on the reasons for the deficiencies noted by the Office of the Auditor General and actions to be

taken, and publish this report on the City of Wanneroo's website within 14 days of submitting the report to the Minister.

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Attachments:

1.	*Independent Auditors Report (OAG Audit Opinion) - City of Wanneroo - For year ended 30 June 2018*	18/494863	*Minuted*
2.	*Request Report - Audit Report 2017-18 - 16 November 2018*	19/256916	*Minuted*