



A G E N D A

FOR CITY AUDIT COMMITTEE TO BE HELD IN THE COMMITTEE ROOM,
ADMINISTRATION CENTRE, 7 ORCHARD AVENUE, ARMADALE ON TUESDAY, 11
OCTOBER 2005 AT 5:00PM

PRESENT:

APOLOGIES:

OBSERVERS:

IN ATTENDANCE:

ELECTION OF CHAIR AND DEPUTY CHAIR

As this is the first meeting of the City Audit Committee since the May 2005 Elections, the first item of business is the Election of Committee Chair and Deputy Chair.

The Executive Director Corporate Services will call for nominations for the position of Chair and having elected the Chair, the Chair will then call for nominations for the position of Deputy Chair.

*Note: Pursuant to the requirements of the Local Government Act 1995, nominations are to be **in writing** either before the meeting or at the meeting before the close of nominations. If an election is required for either of the positions then it will be conducted on the first past the post basis.*

DECLARATION OF MEMBERS' INTERESTS

PUBLIC QUESTION TIME

Note:

Meetings of the City Audit Committee are closed to the public on the basis that matters to be dealt with by Committee will generally be of a sensitive and confidential nature which, if disclosed, could reasonably be expected to impair the effectiveness of the audit process – Council resolution CS18/2001 refers.

DEPUTATION

Nil

CONFIRMATION OF MINUTES

RESOLVED

Minutes of the City Audit Committee Meeting held on 14TH March 2005, be confirmed.

I N D E X

CITY AUDIT COMMITTEE

11 OCTOBER 2005

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2005 YEAR INTERIM AUDIT ADVICE

WARD ALL
FILE REF: FIN/6
DATE 4 October 2005
REF AFM & NC
RESPONSIBLE MANAGER EDCorpS

In Brief:

This Report presents matters arising from the Interim Audit conducted by Council's Auditor which have already either been addressed by management or are in the process of being addressed.

Tabled Items

Nil

Officer Interest Declaration

Nil

Strategic Implications

Effective governance and administration of the City's services.

Legislation Implications

Local Government Act 1995 (as amended) and all associated Regulations
Australian Accounting Standards

Council Policy/Local Law Implications

Nil

Budget/Financial Implications

Nil

Consultation

Council's Auditor
Chief Executive Officer

BACKGROUND

Each year, as part of Council's audit process, an Interim Audit is undertaken to ascertain any areas of potential review associated with Council's financial systems/processes. The advice received through the interim audit is then assessed by City officers who note the comments and take action as required. The Interim Audit was undertaken in April 2005 and notes from the visit are now presented for Committee's consideration.

Council's Auditor, Mr Tony Macri, and his Audit Manager Mr. Sukumaran Menon will be in attendance at the meeting to speak to the interim audit advice and take questions from Committee members.

DETAILS OF PROPOSAL

As part of Council's committee structure, the Audit Committee has been established to review areas of an audit or compliance nature. The Interim Audit is forwarded under separate cover and summarised in the following report. It is to be noted that the interim audit is primarily concerned with a review of internal controls/practices/procedures and management's compliance with those controls. The Interim Audit has been fully performed and only reports on an exception basis those items that require management's attention.

COMMENTAnalysis

Matters raised by the Auditor and Management's response to each, are as follows:

Sundry Debtors*Auditor's Advice*

- The sundry debtors aged trial balance report as at 18 March 2005 showed approximately 7% of the outstanding debts were in the 4 months or over category. This compared with our previous review carried out in April 2004 which showed approximately 32% of the outstanding debts in the 4 months or over category, indicating that management has given due attention to this area. The provision for doubtful debts at 30 June 2004 was \$122,378. Management should consider its adequacy for the financial year ending 30 June 2005.

Management response

- The 25% reduction in the 4 month & over debtor category is a good result and could not have been achieved without Council's support in terms of resource allocations to negotiate outcomes with debtors and its pragmatic approach to issues which often had a long history. Regards the adequacy of the provision for doubtful debts, adequate allowance has been made for separate to the \$122,378 provision, there is an allocation in the 2005-06 adopted budget for debtor write-offs of \$106,000. Monitoring of debtor balances will continue to occur.

Bank Reconciliations*Auditor's Advice*

- At the time of our visit, we noted that bank reconciliations had not been carried out for the municipal bank account since November 2004. The trust account and reserve account bank reconciliations have also not been performed for months of January and February 2005. As an important control procedure the bank reconciliations, in our opinion, should be done on a monthly basis. At the date of this report, we are aware that management has staff dedicated to perform the bank reconciliations up to date.

Management Response

- The Auditor's opinion regards bank reconciliations being done monthly is fully supported and indeed up until this recent time had been performed on a monthly basis. The bank reconciliations were brought up to date back in May/early June 2005 and reconciliations have been done each month since and this practice will continue. The reason for the reconciliations not being done was of a 'one-off' nature due in part to staff absences and knowledge of the new accounting system software.

Purchasing and Payments*Auditor's Advice*

- Management has addressed the majority of issues raised in our previous management letter and has further strengthened the internal control procedures in this area since the introduction of the new system. However the following matter, we believe, still requires addressing: we noted that in a number of instances purchase orders are still being raised after the materials have been delivered or the jobs completed and the invoices received.

Management Response

- As was anticipated last year when the auditor made similar comments in their advice, the new accounting/financial software has considerably reduced the number of orders being raised after either materials and/or invoices have been received which is a good outcome. However with incidences still occurring at more than an occasional rate, further education of officers remains an ongoing task.

Fixed Assets*Auditor's Advice*

- We noted that Council has not carried out a complete inventory check of fixed assets for some time. We recommend that Council undertake a full physical check of the assets with a view to updating the asset register.

Management Response

- An inventory check of buildings was completed in July 2005 which included a basic condition analysis and valuation. Inventory checks on furniture and equipment as well as small plant and equipment will be undertaken during the remainder of the current financial year.

Investment of Surplus Funds*Auditor's Advice*

- We recommend that the Council establish a formal investment policy taking into account the need to ensure that adequate control exists over the investment of surplus funds by providing guidance to be followed by employees.

Management Response

- The matter of developing an investment policy and an associated management practice is currently being researched and developed. The current practice (although not documented) is to place all investments with

Council's banker; investments are held in either '11am call accounts' or "bank accepted bills" both of which are very secure and traditional forms of investment and full details of all investments are reported monthly to Council.

Information Technology

Auditor's Advice

- Recommendation – when officers of Council's software supplier request access to the Armadale network a basic log should be kept detailing the reason as to why the request has been made. On completion of the remote session, the City should immediately change the password or have the account disabled until the next access request.
- Recommendation – to provide consistent levels of security for Council's software supplier, the password changes for that application should be brought into line with network standards and changed with sufficient regularity.

Management Response

- On the first of the above recommendations, remote access is a matter that is subject to contractual obligations and whilst a security risk is present, it's not considered of a sufficient scale to warrant a change in process. All remote access is performed using encrypted access lines and all software supplier officers are qualified. Sufficient audit trails of remote access are kept by the software supplier.
- On the other recommendation, the Auditor's comments are fully supported and methods of how this can occur are currently being investigated.

Conclusion

All in all the Auditor's Interim Audit advice reflects favourably upon the financial and accounting systems/procedures currently in place but as with any system/procedure there will be areas requiring improvement and the advice provided by the Auditor provides that direction for both management and Council.

RECOMMEND

That Council, through the City Audit Committee, be provided with a Report Update on the following matters arising from the Auditor's Interim Audit Visit Advice dated 20th April 2005, ie.

- **Purchasing – measures be taken like officer education to further reduce the incidence of orders being raised after either materials and/or invoices have been received;**
- **Fixed Assets – an inventory check on furniture and equipment as well as small plant and equipment be undertaken during the remainder of the current financial year;**
- **Investment of Surplus Funds – a Council Investment Policy and Management Practice be developed; and**

- **Information Technology – a password security process for remote access by Council’s software provider, which is consistent with other network password standards, be investigated and implemented.**

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PUBLIC ACCOUNTS COMMITTEE INQUIRY

WARD ALL
FILE REF: FIN/6
DATE 4 October 2005
REF AFM
RESPONSIBLE MANAGER EDCorpS

In Brief:

This report presents details of the recently announced Public Accounts Committee (PAC) Inquiry into the effectiveness and/or adequacy of accountability mechanisms for local government and gives consideration as to whether a submission to the PAC is warranted.

Tabled Items

Nil

Officer Interest Declaration

Nil

Strategic Implications

The effective governance and administration of the City's services

Legislation Implications

Local Governments are already subject to numerous Acts and Regulations which advocate an array of accountability and governance requirements.

Council Policy/Local Law Implications

Nil

Budget/Financial Implications

If as an outcome of the Inquiry the State Auditor General does in the future become involved in local government audit processes, then it is likely that the audit fund allocations currently provided in the Fifteen Year Financial Plan -\$45,000 per annum - may not be sufficient by a factor of perhaps up to \$20,000 pa.

Consultation

Western Australian Local Government Association (WALGA)
Management Executive Group

BACKGROUND

The background to this matter is explained as follows:

- Correspondence has been received from the Public Accounts Committee, their advice in part being, quote:

The Public Accounts Committee has resolved to undertake an inquiry into the effectiveness and/or adequacy of accountability mechanisms for local government authorities. Following recent events involving a number of local councils, the Committee is concerned as to whether the accountability

mechanisms for local government expenditure are adequate. The Terms of Reference are as follows:

The Public Accounts Committee will examine and report on:

- 1. current accountability mechanisms for local government in Western Australia, including finance, probity and performance;*
- 2. the capacity of the Department of Local Government and Regional Development to examine local government finance, probity and performance issues;*
- 3. whether the State Auditor General should have a role in local government audit processes; and*
- 4. other matters deemed relevant by the Committee.*

The Committee invites your organization to make a submission to the above inquiry. The closing date for submissions is 11th November 2005.

- The membership and powers/functions of the Public Accounts Committee are as follows:

Membership:

- ✓ Mr John Quigley, MLA Chairman (Member for Mindarie);
- ✓ Mr Norm Marlborough, MLA (Member for Peel);
- ✓ Mr Tony McRae (Member for Riverton);
- ✓ Mr Terry Redman, MLA (Member for Stirling); and
- ✓ Dr Steve Thomas, MLA (Member for Capel).

Powers and Functions:

The Public Accounts Committee's establishment, powers and functions are provided for within Standing Orders 284-286 of the Legislative Assembly. Under its Standing Orders, the PAC is empowered to inquire into and report on any proposal, matter or thing it considers necessary, connected with the receipt and expenditure of public moneys, including monies allocated under the annual Appropriation bills and Loan Fund.

Under Standing Order 285, the PAC may:

- examine the financial affairs and accounts of government agencies of the State which includes any statutory board, commission, authority, committee, or trust established or appointed pursuant to any rule, regulation, by-law, order, order in Council, proclamation, ministerial direction or any other like means.
- inquire into and report to the Assembly on any questions which:
 - it deems necessary to investigate;
 - is referred to it by resolution of the Assembly;
 - is referred to it by a Minister; or
 - is referred to it by the Auditor General.
- consider any papers on public expenditure presented to the assembly and such of the expenditure as it sees fit to examine.
- consider whether the objectives of public expenditure are being achieved, or may be achieved more economically.

- The Inquiry was the subject of a Report by WALGA in the most recent September 2005 South East Zone Meeting Agenda. Relevant extracts from WALGA's report are as follows:

Preliminary discussions have been held with the Department of Local Government and Regional Development, and it would appear that neither the Department nor the Minister were aware of the Inquiry. Whilst it is recognised that the Committee is an independent body, it would seem that there may be a number of outcomes of which the industry is not aware and therefore will be difficult to provide an effective response.

It is proposed to make submission to the Inquiry, and as part of that process, a questionnaire will be distributed to members seeking their feedback. There is also some consideration being given to joining with the Local Government Managers' Association (LGMA) to prepare any submission given the close interests and the short period of time to respond.

Details of Proposal

COMMENT

Analysis

More recent advice received from WALGA indicates that the focus for local government is likely to be part 3 of the Terms of Reference to do with "whether the State Auditor General should have a role in local government audit processes" – apparently there is a view that the current audit processes in local government need to be more rigorous, be based upon a more uniform approach and be expanded to include non-financial type compliance issues and key performance indicators.

The reasons for reporting the matter of the Inquiry to Committee/Council are as follows:

- firstly, for Committee/Council awareness purposes,
- secondly, to consider whether there is merit in Council making a submission separate to those proposed by WALGA and the LGMA, and
- thirdly, if there is support for a Council submission, then consideration of what aspects might the submission focus upon.

Relevant considerations to making a Council submission are suggested as being:

- unless Committee/Council has particular views on certain aspects which it believes may not be adequately reflected in the WALGA and LGMA submissions then there is probably limited value/merit in making separate submission,
- related to the above dot point is the resource/cost implications of preparing a separate submission – the likely outcome of resources being committed to the preparation of a submission is that other current tasks and projects will be deferred/delayed,
- if as suggested by WALGA the focus of the Inquiry for local government is the possible involvement of the Auditor General in local government audit processes, then other than maybe the issue of the Auditor General's ability and capacity to deliver an efficient and cost effective service (about which local government would require advance assurances) it shouldn't necessarily matter to Council for the audit function/process itself will generally not change no matter who provides the service.

Conclusion

Having regard for the considerations reported above as relating to the merits of a Council submission, it is on balance recommended that Council not make a submission.

RECOMMEND

That Council not make a separate submission to the Public Accounts Committee Inquiry into local government accountability for the reasons that:

- (i) the Western Australian Local Government Association (WALGA) and the Local Government Managers' Association (LGMA) will be making submission advocating the interests of the industry and that WALGA's submission will be based upon member feedback via a member survey thereby presenting the opportunity for Council's input; and**
- (ii) as a general principle, Council is supportive of initiatives that improve the accountability of local government including perhaps an audit role by the State Auditor General however the possible involvement of the Auditor General should be predicted upon assurances from the state government in regard to associated costs being reasonable and a capacity by the Auditor General to deliver an effective and timely service.**

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****GUIDELINES FOR AUDIT COMMITTEES**

WARD ALL
FILE REF: FIN/6
DATE 4 October 2005
REF AFM
RESPONSIBLE MANAGER EDCorpS

In Brief:

This Report presents details of the Department of Local Government & Regional Development's recent published Operational Guideline relating to the appointment, function and responsibilities of Audit Committees in Local Government.

Tabled Items**Officer Interest Declaration**

Nil

Strategic Implications

The effective governance and administration of the City's services

Legislation Implications

Local Government Act 1995 – Part 7 – Audit;
Local Government (Audit) Regulations 1996.

Council Policy/Local Law Implications

Nil

Budget/Financial Implications

Nil

Consultation

Department of Local Government & Regional Development

BACKGROUND

As a follow-up to the recent amendments to the Local Government Act and Local Government Audit Regulations relating to the audit function, the Department has produced an Operational Guideline relating to the appointment, function and responsibilities of Audit Committees in Local Government – a copy of the Guideline is attached to this agenda. **(Refer to Attachment "A-1" – Summary of Attachments.)**

COMMENT

The Guideline is a useful and timely reference for not only does it bring together the various recent legislative changes in a concise and informative manner but as well, it importantly seeks to translate the legislation from an operational perspective, ie. the models contained in the Guideline relating to the Terms of Reference for Audit Committees and Minimum Audit Specifications are reasonably good examples of the intent of the legislation.

Comparing the Guidelines to the City's approach to its audit responsibilities (noting that the City has had an audit committee for sometime prior to the recent legislation changes making such committees mandatory) shows very few variations in approach which is reassuring from both a Council and management perspective. Many of the now legislated/prescribed roles and responsibilities of the audit committee have been the practice of Council's Audit Committee over several years, like for example:

- reviewing the Statutory Compliance Return each year and making recommendation to Council on its adoption;
- developing and recommending to council a process for the selection and appointment of a person as council's auditor;
- recommending to Council the person to be appointed as the Council's auditor;
- meeting with the auditor to discuss and scope audit plans and programs;
- meeting with the auditor to review the findings of the auditor's interim audit (the earlier report in this agenda deals with this very matter); and
- reviewing the appropriateness and effectiveness of Council's financial management systems and procedures and reporting to Council the results of such reviews.

One of the variations requiring a possible further action by Council relates to the new requirement for the local government to meet with its auditor at least once in every year. The following extract from the Guidelines explains, ie.

The legislation specifies that a local government is required to meet with its auditor at least once in every year. The term "local government" in this context means the Council. If Council so resolved via a formal delegation, a meeting between the audit committee and the auditor would satisfy this requirement.

Therefore, if Council is happy to have the audit committee meet with its auditor as has been the practice since the audit committee was established several years ago and which is a more practical approach, then for that arrangement to continue an absolute majority resolution delegating that function to the audit committee is required.

CONCLUSION

The Department's recently published Operational Guideline re: *Audit Committees in Local Government* provides a useful and practical reference for all councillors and management, particularly those having a more direct involvement with Council's Audit Committee.

RECOMMEND

That Council, pursuant to section 7.1B of the Local Government Act 1995 (the Act), delegate to its City Audit Committee the duty to meet with Council's Auditor at least once in every year as provided for at section 7.12A(2) of the Act.

****ABSOLUTE MAJORITY RESOLUTION REQUIRED**

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CITY AUDIT COMMITTEE

SUMMARY OF "A" ATTACHMENTS

11 OCTOBER 2005

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Audit Committees in Local Government

Their appointment, function
and responsibilities

LOCAL GOVERNMENT
OPERATIONAL GUIDELINES

Number 9

July 2005



Department of Local Government
and Regional Development
Government of Western Australia

www.dlgrd.wa.gov.au

Audit Committees in Local Government Their appointment, function and responsibilities

1. INTRODUCTION

An amendment to the *Local Government Act 1995* (the Act) in 2005 introduced a requirement that all local governments establish an audit committee. Such committees are to provide an independent oversight of the financial systems of a local government on behalf of the Council. As such, the committee will operate to assist Council to fulfil its corporate governance, stewardship, leadership and control responsibilities in relation to the local government's financial reporting and audit responsibilities.

The purpose of this guideline is to assist local governments to establish and operate an effective audit committee. Clear and comprehensive terms of reference, setting out the committee's roles and responsibilities, is essential and a model terms of reference for an audit committee is provided with this guideline. Matters such as the governing legislation, membership, primary roles and responsibilities of the committee and ancillary functions are also addressed. Guidance is provided to the committee as it approaches its task of appointing an external auditor through provision of a minimum standard audit specification.

2. LEGISLATION

The relevant parts of the Act and regulations that relate to financial management, audits and audit committees are listed below.

2.1 Financial Management

In relation to financial management under Part 6 of the Act, a local government is to -

- a) prepare and adopt an annual budget in the form and manner prescribed. A copy of the budget is to be sent to the Department within 30 days of adoption.
- b) prepare an annual financial report and such other financial reports as are prescribed. The accounts of the local government and annual financial report are to be submitted to the auditor for audit by 30 September.
- c) have a municipal fund and a separate and distinct trust fund.
- d) establish and maintain reserve funds for the holding of monies set aside for future use.

2.2 Audit requirements for local governments

Part 7 of the Act and the *Local Government (Audit) Regulations 1996* (the Regulations) address the situation of audit. In relation to the duties of the local government with respect to audits -

- a) the local government is to do everything in its power to -
 - i. assist the auditor to conduct an audit and carry out his or her other duties under the Act; and
 - ii. ensure that audits are conducted successfully and expeditiously.
- b) a local government is to meet with its auditor at least once in every year.
- c) a local government is to examine the report of the auditor and is to -
 - i. determine if any matters raised require action to be taken by the local government; and
 - ii. ensure that appropriate action is taken in respect of those matters.

- d) a local government is to -
 - i. prepare a report on any actions taken in respect of any matters raised in the report of the auditor; and
 - ii. forward a copy of that report to the Minister by the end of the next financial year, or 6 months after the last report prepared by the auditor is received by the local government, whichever is the latest in time.

2.3 Audit Committees

The Act and Regulations provide that -

2.3.1 In relation to the establishment of an audit committee -

- a) each local government is to establish an audit committee consisting of three or more persons to exercise the powers and discharge the duties conferred on it.
- b) members of the committee are to be appointed by an absolute majority decision of Council. At least three of the members, and the majority of the members, are to be elected members.
- c) the CEO is not to be a member of the committee and may not nominate a person to be a member or have a person to represent him or her as a member of the committee.
- d) an employee is not to be a member of the committee.
- e) the only powers and duties that can be delegated to a committee are any of the powers and duties of the local government under Part 7 of the Act. The committee cannot on-delegate the powers and duties delegated to it.
- f) an audit committee with a person other than an elected member as a member can be delegated powers and duties.
- g) a decision of the committee is to be made by simple majority.

2.3.2 As part of its function an audit committee -

- a) is to provide guidance and assistance to the local government -
 - i. as to the carrying out of its functions in relation to audits;
 - ii. as to the development of a process to be used to select and appoint a person to be the auditor; and
- b) may provide guidance and assistance to the local government as to -
 - i. matters to be audited;
 - ii. the scope of the audit;
 - iii. its functions under Part 6 of the Act that relate to financial management; and
 - iv. the carrying out of its functions relating to other audits and other matters related to financial management.

2.4 Appointment of the Auditor

The Act and Regulations provide that -

- a) on the recommendation of the audit committee a local government is to from time to time appoint, by absolute majority, a person to be its auditor.
- b) the local government may appoint one or more persons as its auditor.
- c) the local government's auditor is to be a person who is -
 - i. a registered company auditor; or
 - ii. an auditor approved by the Minister.
- d) a person may not be appointed as a local government auditor if that person is -
 - i. a councillor or employee of the local government;
 - ii. in debt to the local government for more than \$5,000;
 - iii. a councillor or employee of a regional local government in which the local government is a participant;

- iv. a member of an incorporated association formed by the local government; or
- v. a class of persons as prescribed in the Regulations.
- e) an auditor is not to be appointed for more than five years.
- f) the appointment of a person as an auditor is to be made by agreement in writing and is to include –
 - i. the objectives of the audit;
 - ii. the scope of the audit;
 - iii. a plan for the audit;
 - iv. details of the remuneration and expenses to be paid to the auditor; and
 - v. the method to be used by the local government to communicate with, and supply information to, the auditor.

2.5 Conduct of the Audit

The Act and Regulations provide that –

- a) the auditor is required by 31 December next following the financial year to which the audit relates, to examine the accounts and annual financial report submitted for audit.
- b) the auditor is to form an opinion as to whether –
 - i. the accounts are properly kept; and
 - ii. the annual financial report –
 - is prepared in accordance with the financial records; and
 - represents fairly the results of the operations of the local government and its financial position at 30 June.
- c) the auditor is to prepare a report on the audit and within 30 days of completing the audit forward a copy to –
 - i. the mayor or president;
 - ii. the CEO of the local government; and
 - iii. the Minister.
- d) the report is to give the auditor's opinion on –
 - i. the financial position of the local government; and
 - ii. the results of the operation of the local government.
- e) the report is to include –
 - i. any material matters that indicate significant adverse trends in the financial position or the financial management practices of the local government;
 - ii. any matters indicating non-compliance with financial management requirements of the Act, Regulations and any other written law;
 - iii. details of whether information and explanations were obtained; and
 - iv. a report on the conduct of the audit.
- f) where it is considered appropriate to do so the auditor is to prepare a management report to accompany the auditor's report.
- g) where the auditor considers that –
 - i. there is any error or deficiency in an account or financial report;
 - ii. any money paid from, or due to the local government has been, or may have been misapplied; or
 - iii. there is a matter arising from the audit that needs to be addressed by the local government;details are to be included in the report to the Minister.
- h) the auditor has a right of access at all reasonable times to such books, accounts, documents and assets of the local government as are in the opinion of the auditor necessary to allow the audit to be conducted.

3. OPERATION OF AUDIT COMMITTEES

3.1 Role and Responsibilities

The role of the audit committee is to support Council in its endeavours to provide effective corporate governance and fulfil its responsibilities in relation to directing and controlling the affairs of the local government.

The essential role for an audit committee is oversight for all matters that relate to the conduct of audits. The committee's effectiveness will be greater if it is also given responsibility for oversight of financial management processes within the local government but only where a Council does not have a finance committee.

Please note that an audit committee (or any other committee) cannot be given a management task where the Act and Regulations make the CEO specifically responsible. Where the local government is assigned the function through the legislation the audit committee may have a role unless the function has been delegated to the CEO by the Council.

The deliberations and recommendations of the committee must be independent and autonomous. Therefore, the Act prohibits the CEO being a member of the committee. However, it is essential that the CEO be given every opportunity to provide his/her expert advice to the committee as he/she does with full Council and other committees. Therefore, the CEO or their nominated representative must be given official adviser status and attend all meetings.

A model terms of reference is attached as Appendix 1 to assist local governments to define an appropriate role for its audit committee. When considering the model, local governments need to remember it is a guide and they can delete or modify any matters they believe not applicable.

It is important to note that the legislation gives the audit committee a specific role in appointing the auditor. It is to recommend to the Council who should be appointed as the auditor. Attached as Appendix 2 is a model 'Minimum Standard Audit Specification' that local governments can use when developing a process to be used to select and appoint a person to be the auditor. Local governments can amend the document to suit their individual requirements. Any scope adopted must meet, as a minimum, the legislative requirements.

The legislation specifies that a local government is required to meet with its auditor at least once in every year. The term "local government" in this context means the Council. If Council so resolved via a formal delegation, a meeting between the audit committee and the auditor would satisfy this requirement.

It is acknowledged that the requirement to meet at least once per year may incur a significant financial burden for the more remote local governments. In such circumstances the meeting can be conducted by telephone or video conference. The Council or audit committee should resolve how the meeting with the auditor will be conducted and for the record of the meeting to show that the auditor was involved and the matters discussed. It would be inappropriate for Council representatives to meet with the auditor in their offices unless they were members of the Audit Committee or a significant majority of the members.

The committee may need to liaise regularly with the external auditor to discuss the audit plan, results of the audit and implementation of any recommendations for action emerging from the audit. The method of liaison between auditor and committee should be addressed in the agreement of appointment.

Advice from the auditor may address issues such as:

- (i) an assessment of accounting procedures;
- (ii) an assessment of internal controls;
- (iii) an assessment of risk;
- (iv) compliance with the *Local Government Act 1995* and associated regulations;
- (v) compliance with Council policies;
- (vi) performance assessments on the efficiency and effectiveness of operations;
- (vii) processes of the internal audit;
- (viii) outcomes of the external audit prior to issue of management and audit reports; and
- (ix) changes to accounting standards and legislation and the impact on the local government.

The audit committee should examine the auditor and management reports. The committee would then determine if any matters raised in the reports require action to be taken by the local government and to ensure that appropriate action is implemented.

A further role for the audit committee would be to receive and authorise the report relating to the audit prepared by the CEO that is to be sent to the Minister. This report would outline any actions the local government has taken or intends to take in relation to the matters identified by the auditor.

The role of the audit committee in relation to the internal audit function is a matter of conjecture. Most CEOs would argue that where there is a formal internal audit that it is an operational function and is their responsibility. The role of the Audit Committee may be to ensure that an internal audit function is put in place where required and that its processes are appropriate, accountable and transparent. The role of the external auditor in this regard can be established at the time of appointment.

3.2 Membership

An audit committee is required to consist of at least three persons, with the majority being elected members. Local governments may decide to appoint a committee involving only elected members or they may appoint one or more persons who are external to the Council. If a Council considers it appropriate the whole Council can be appointed as the audit committee.

If the local government wishes to appoint one or more persons other than elected members to the committee, it should ensure that they have the requisite knowledge and skills to provide benefit to the committee.

3.3 Operation of the Committee

Irrespective of the membership of the committee, all legislative requirements relating to committee meetings such as advertising meeting dates, notice of meeting and keeping minutes of meetings need to be complied with.

The legislation prevents a meeting fee being paid to an external person but it is permissible for a payment to be made, commensurate with the expertise and knowledge such people bring to the committee. The Council will need to determine whether payment will be offered and the level of that payment.

Members of the committee should be encouraged to attend appropriate courses to keep them up to date with legislation, accounting and other relevant issues.

3.4 Other Responsibilities

Local governments are required by legislation to complete a statutory compliance return and have the return adopted by Council. The return is a comprehensive checklist of a local government's compliance with the requirements of the *Local Government Act 1995* and all its Regulations. After adoption, the return is to be signed by the Mayor or President and the CEO prior to it being forwarded to the Department.

The detailed nature of the return makes it difficult for Council to assess any implications arising from the return at its Ordinary Council Meetings. In addition, the return covers a significant number of compliance matters that relate to the management of financial processes and procedures.

Therefore, as an option Council could consider allocating to the audit committee the role of reviewing the return and making a recommendation on its adoption. The audit committee could also consider proposals from the CEO as to whether the compliance audit is undertaken internally or an external party is contracted to undertake the task. In the case of an external party the audit committee would have the responsibility to receive the report and make recommendations on it to full Council.

4. THE EXTERNAL AUDITOR

4.1 Appointment of an Auditor

The Act requires that each local government, from time to time, appoint an auditor on the recommendation of the audit committee. The committee should undertake a proper selection and appointment process as part of appointing an auditor.

It is important to realise that the Act specifies that it is a person(s) that is appointed as auditor, not the company which employs the person. Therefore, when the audit report is received it must be signed by the person(s) appointed as the auditor; it cannot be the generic signature identifying the firm.

4.2 Scope of the Audit

The Act and Regulations prescribe the scope of the external audit of the annual financial statements of a local government.

The scope details are going to vary between local governments but as an aid a model minimum standard audit specification is attached as Appendix 2 to this guideline. Individual local governments can amend that document to suit their particular needs.

4.3 Reporting by the auditor

Regulations require the auditor, where appropriate, to prepare a management report to accompany the auditors report. Although there is no legislative requirement for the auditor to prepare a management report unless he or she deems it appropriate, local government may wish to require the auditor to prepare a report on all issues identified during the audit.

The auditor, after completing the audit, is to forward a copy of his or her audit and management report to:

- the Mayor or President;
- the CEO of the local government; and
- the Minister.

The CEO should be assigned the task of providing the report to the audit committee.

Appendix 1

**MODEL TERMS OF REFERENCE –
AUDIT COMMITTEES**

Important: The following Model Terms of Reference contains clauses that may not be applicable to each local government. Local governments will need to consider each clause and only adopt those that are applicable to the roles and responsibilities and delegated powers and functions that will apply to their Audit Committee.

The clauses that are considered optional have been asterisked (*).

1. Objectives of Audit Committees

The primary objective of the Audit Committee is to accept responsibility for the annual external audit and liaise with the local government's auditor so that Council can be satisfied with the performance of the local government in managing its financial affairs.

Reports from the committee will assist Council in discharging its legislative responsibilities of controlling the local government's affairs, determining the local government's policies and overseeing the allocation of the local government's finances and resources. The committee will ensure openness in the local government's financial reporting and will liaise with the CEO to ensure the effective and efficient management of local government's financial accounting systems and compliance with legislation.

The committee is to facilitate:

- the enhancement of the credibility and objectivity of *internal and external financial reporting;
- *effective management of financial and other risks and the protection of Council assets;
- compliance with laws and regulations as well as use of best practice guidelines relative to auditing;
- *the coordination of the internal audit function with the external audit;
- the provision of an effective means of communication between the external auditor, *internal auditor, the CEO and the Council.

2. Powers of the Audit Committee

The committee is a formally appointed committee of Council and is responsible to that body. The committee does not have executive powers or authority to implement actions in areas over which the CEO has legislative responsibility and does not have any delegated financial responsibility. The committee does not have any management functions and cannot involve itself in management processes or procedures.

The committee is to report to Council and provide appropriate advice and recommendations on matters relevant to its term of reference in order to facilitate informed decision-making by Council in relation to the legislative functions and duties of the local government that have not been delegated to the CEO.

3. Membership

The committee will consist of *four members with three elected and *one external person. All members shall have full voting rights.

*External persons appointed to the committee will have business or financial management/reporting knowledge and experience, and be conversant with financial and other reporting requirements.

*Appointment of external persons shall be made by Council by way of a public advertisement and be for a maximum term of two years. The terms of the appointment should be arranged to ensure an orderly rotation and continuity of membership despite changes to Council's elected representatives.

*Remuneration will be paid to each external person who is a member of the committee on the basis of an annual fee.

The CEO and employees are not members of the committee.

The CEO or his/her nominee is to attend all meetings to provide advice and guidance to the committee.

The local government shall provide secretarial and administrative support to the committee.

4. Meetings

The committee shall meet at least *quarterly.

Additional meetings shall be convened at the discretion of the presiding person.

5. Reporting

Reports and recommendations of each committee meeting shall be presented to the next ordinary meeting of the Council.

*The committee shall report annually to the Council summarising its activities during the previous financial year.

6. Duties and Responsibilities

The duties and responsibilities of the committee will be –

- a) Provide guidance and assistance to Council as to the carrying out the functions of the local government in relation to audits.
- b) Develop and recommend to Council an appropriate process for the selection and appointment of a person as the local government's auditor.
- c) Develop and recommend to Council –
 - a list of those matters to be audited; and
 - the scope of the audit to be undertaken.
- d) Recommend to Council the person or persons to be appointed as auditor.
- e) Develop and recommend to Council a written agreement for the appointment of the auditor. The agreement is to include –
 - the objectives of the audit;
 - the scope of the audit;
 - a plan of the audit;
 - details of the remuneration and expenses to be paid to the auditor; and
 - the method to be used by the local government to communicate with, and supply information to, the auditor.
- f) *Meet with the auditor once in each year and provide a report to Council on the matters discussed and outcome of those discussions.
- g) Liaise with the CEO to ensure that the local government does everything in its power to –
 - assist the auditor to conduct the audit and carry out his or her other duties under the *Local Government Act 1995*; and
 - ensure that audits are conducted successfully and expeditiously.
- h) Examine the reports of the auditor after receiving a report from the CEO on the matters and –
 - determine if any matters raised require action to be taken by the local government; and
 - ensure that appropriate action is taken in respect of those matters.
- i) Review the report prepared by the CEO on any actions taken in respect of any matters raised in the report of the auditor and presenting the report to Council for adoption prior to the end of the next financial year or 6 months after the last report prepared by the auditor is received, whichever is the latest in time.

- i) Review the scope of the audit plan and program and its effectiveness.
- k) *Review the appropriateness of special internal audit assignments undertaken by internal audit at the request of Council or Chief Executive Officer.
- l) *Review the level of resources allocated to internal audit and the scope of its authority.
- m) *Review reports of internal audits and by monitoring the implementation of recommendations made by the audit and reviewing the extent to which Council and management reacts to matters raised.
- n) *Facilitate liaison between the internal and external auditor to promote compatibility, to the extent appropriate, between their audit programs.
- o) *Review the local government's draft annual financial report, focusing on:
 - accounting policies and practices;
 - changes to accounting policies and practices;
 - the process used in making significant accounting estimates;
 - significant adjustments to the financial report (if any) arising from the audit process;
 - compliance with accounting standards and other reporting requirements;
 - significant variances from prior years.
- p) *Consider and recommend adoption of the annual financial report to Council. Review any significant changes that may arise subsequent to any such recommendation but before the annual financial report is signed.
- q) *Address issues brought to the attention of the committee, including responding to requests from Council for advice that are within the parameters of the committee's terms of reference.
- r) Seek information or obtain expert advice through the CEO on matters of concern within the scope of the committee's terms of reference following authorisation from the Council.
- s) *Review the Statutory Compliance Return and make a recommendation on its adoption to Council.

Appendix 2

MODEL MINIMUM STANDARD AUDIT SPECIFICATION

IMPORTANT: The following Model Minimum Standard Audit Specification may be used as the basis for the calling of tenders or seeking of quotes for the appointment of an auditor. Local governments need to consider the Model to ensure that only those clauses applicable to its requirements are used. This applies, in particular, to the "Critical matters to be audited".

1. Introduction

This document is provided for the assistance of auditors who wish to apply for the role of auditor with the City/Town/Shire

Auditors are required to address all of the matters outlined in the specification.

Auditors who submit an application may be asked to provide further information and/or make a presentation to the Audit Committee.

2. Objectives of the Audit

To provide an independent audit opinion of the accounts and annual financial reports of the local government for each financial year covered by the term of the audit appointment.

3. Term of Audit Appointment

For the financial years commencing 1 July through to 30 June..... (not more than 5 years)

4. Scope of the Audit

The auditor is to –

- 4.1 Carry out such work as is necessary to form an opinion as to whether -
 - (a) the accounts are properly kept; and
 - (b) the annual financial report:
 - (i) is prepared in accordance with the financial records; and
 - (ii) represents fairly the results of the operations of the local government and the financial position of the local government at 30 June in accordance with the Australian Accounting Standards, the *Local Government Act 1995* (as amended), the *Local Government (Financial Management) Regulations 1996* (as amended) and other mandatory professional reporting requirements.
- 4.2 Give an opinion in his or her audit report on –
 - (a) the financial position of the local government; and
 - (b) the results of the operation of the local government.
- 4.3 Include in his or her audit report –
 - (a) any material matters that indicate significant adverse trends in the financial position or the financial management practices of the local government;
 - (b) any matters indicating non-compliance with financial management requirements of the Act, Regulations and any other written law.

5. Audit Methodology and Approach

- (a) The auditor is required to comply with the requirements of section 7.9 of the *Local Government Act 1995* and the *Local Government (Audit) Regulations 1996*.
- (b) An audit is to be carried out in accordance with "Auditing Standards" and "Auditing Guidance Statements" adopted from time to time by the Australian Society of Certified Practising Accountants and the Institute of Chartered Accountants in Australia.
- (c) The auditor is to provide the local government with a general outline of his/her methodology.
- (d) The auditor is to provide the local government with a plan for the audit including:
 - timing of interim audit visits;
 - final audit visit (within 30 days of being advised that the accounts and annual financial report are available for audit);
 - timing of the legislative requirement to meet with the local government and whether that meeting will be in person or by some other means; and
 - the method to be used to communicate with, and provide advice and information to, the local government.

- (e) The auditor is required to produce an audit report as required by section 7.9 of the *Local Government Act 1995* and, if considered appropriate by the auditor, a management report.

6. Critical Matters to be Audited

The auditor is to include in his or her application the extent to which the critical matters outlined below will be audited so as to form an opinion on the manner in which they have been maintained.

- (i) Revenue
 - Rates revenue
 - Government grants
 - User pays revenue
 - Profit on sale of non-current assets
 - Other income
- (ii) Expenditure
 - Salary and wage costs
 - Depreciation
 - Materials and contract expenditure
 - Loss on sale of non-current assets
 - Insurances
 - Bad debts
 - Other expenditure
- (iii) Current Assets
 - Bank and short term investments
 - Receivables and prepayments
 - Inventory
- (iv) Non-Current Assets
 - Property, plant, furniture and equipment
 - Infrastructure and depreciation
 - Other receivables
- (v) Liabilities (Current and non-current)
 - Creditors and accruals
 - Loan borrowings including new loans raised
 - Provision for annual and long service leave entitlements
- (vi) Reserve Funds
- (vii) Contingent Liabilities
- (viii) Capital Commitments
- (ix) Accounting Policies and Notes to the Financial Statements
- (x) Cash Flow Statement
- (xi) The financial ratios required by the Local Government (Financial Management) Regulations 1996

7. Hours, Fees and Expenditure

The auditor is to provide:

- Estimate of the time to be spent on the audit.
- Fees for completing the audit in accordance with this specification.
- Nominated auditor(s) and registered company audit number(s).
- Experience of the nominated auditors in completing local government audits.

The auditor is to provide a fee for any additional audit requested by Council.

8. Terms

Conditions to be noted by auditors:

- The auditor shall not sub contract to a third party.
- The auditor shall not, and has no right to, assign the audit contract to third parties.
- The auditor shall not be engaged by the local government to undertake any financial consultancy with the local government that requires the preparation of financial information that will be the subject of the annual audit.
- The auditor shall confirm that he or she has, and will maintain during the duration of the audit term, professional indemnity insurance covering the legal liability arising out of any neglect, default, error, or omission.

9. Termination of Appointment

The appointment as auditor is terminated if:

- (a) the auditor ceases to be a registered company auditor;
- (b) the auditor ceases to be an approved auditor under Section 7.5 of the *Local Government Act 1995*;
- (c) the auditor is a disqualified person under Section 7.4(2) of the *Local Government Act 1995*;
- (d) the auditor resigns by notice in writing to Council;
- (e) Council serves notice in writing to the auditor terminating the appointment.

ABOUT THE GUIDELINE SERIES

This document and others in the series are intended as a guide to good practice and should not be taken as a compliance requirement. The content is based on Departmental officers' knowledge, understanding, observation of, and appropriate consultation on contemporary good practice in local government. Guidelines may also involve the Department's views on the intent and interpretation of relevant legislation.

All guidelines are subject to review, amendment and re-publishing as required. Therefore, comments on any aspect of the guideline are welcome. Advice of methods of improvement in the area of the guideline topic that can be reported to other local governments will be especially beneficial.

Further Information

For more information about this and other guidelines, contact the Local Government Support and Development Branch of the Department of Local Government and Regional Development on 9217 1500 or e-mail lgd@dlgrd.wa.gov.au

These guidelines are also available on the Department's website at <http://www.dlgrd.wa.gov.au>