

Gore District Council

Report to the Finance & Policy Committee
for the Year Ended 30 June 2016



September 2016

29 September 2016

The Finance & Policy Committee
Gore District Council
P O Box 8
GORE 9740

Dear Committee

REPORT TO THE FINANCE AND POLICY COMMITTEE FOR THE YEAR ENDED 30 JUNE 2016

In accordance with our normal practice, we include in the attached report all matters arising from our audit of the financial statements of Gore District Council ("Council" or "GDC") for the year ended 30 June 2016 which we consider appropriate for the attention of the Finance and Policy Committee ("the Committee"). These matters have been discussed with management and their comments have been reflected in our observations, where appropriate.

We have substantially completed our audit subject to:

- The receipt of the signed annual report and representation letter, and
- The performance of subsequent event procedures to the date the annual report is approved by the Council.

This correspondence is part of our ongoing discussions as auditor in accordance with our engagement letter and as required by New Zealand auditing standards. This report includes only those matters that have come to our attention as a result of performing our audit procedures and which we believe are appropriate to communicate to the Committee. The audit does not relieve management or Council of their responsibilities. The ultimate responsibility for the preparation and presentation of the financial statements rests with the Council.

We have prepared this report solely for the use of the Committee and it would be inappropriate for this report to be made available to third parties and, if such a third party were to obtain a copy without our prior written consent, we would not accept responsibility for any reliance that they might place on it.

We would like to take this opportunity to extend our appreciation to management and staff for their assistance and co-operation during the course of our audit.

Yours sincerely



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1. Executive Summary

Audit Scope	<p>We have performed an audit of Gore District Council for the year ended 30 June 2016 in accordance with the Auditing Standards published by the Office of the Auditor-General ('OAG'). Our audit is performed pursuant to the requirements of the Local Government Act 2002 and the Financial Reporting Act 2013, with the objective of forming and expressing an opinion on the financial statements, non-financial performance information and other information required by Schedule 10 of the Local Government Act 2002, and summary financial statements.</p>
Key Areas of Focus	<p>Our audit procedures were focused on those areas in Council's activities that are considered to represent the key audit risks, including:</p> <ul style="list-style-type: none">• Rates• Revaluation of Infrastructure Assets• Local Government Funding Agency• Statement of Service Performance <p>In addition, the OAG Audit Brief for 2016 audit engagements outlined the following areas of audit focus:</p> <ul style="list-style-type: none">• Sensitive Expenditure• Information• Related Party Transactions and Conflicts of Interest• Legislative Compliance <p>These matters are discussed in Section 3.</p> <p>We are satisfied that these key areas of focus have been addressed appropriately and are properly reflected in the annual report.</p>
Internal Controls	<p>During the course of our audit the following matters that warrant communication with the Committee were identified:</p> <ul style="list-style-type: none">• Capital Expenditure Underspend• Review of Asset Useful Lives• Interest Rate Swaps• Review of Holiday Pay Calculation• Incomplete Interest Register <p>These matters are discussed in Section 4.</p> <p>In performing our audit we have not identified any material weaknesses in internal controls which would impact upon our ability to provide our opinion on the financial statements.</p>
Summary of unadjusted differences and disclosure deficiencies	<p>In performing our audit of Council for the year ended 30 June 2016 we have not identified any uncorrected misstatements or omitted disclosures that could, either individually or in aggregate, have a significant effect on the financial statements for the year ended 30 June 2016. Unadjusted differences and omitted disclosures have been discussed in Section 5.</p>

Other Communications

Various matters are communicated in accordance with the requirements of New Zealand auditing standards:

- Independence
- Professional fees / Relationships
- Written representations
- Non-compliance with laws and regulations
- Related parties
- Fraud
- Accounting policies / Financial reporting

These matters are discussed in Section 6.



2. Audit Scope

2.1. Purpose of Report

This report has been prepared for the Finance and Policy Committee ("the Committee") of the Gore District Council ("Council") and is part of our ongoing discussions as auditor in accordance with our engagement letter dated 13 March 2014 and as required by New Zealand auditing standards. This report includes only those matters that have come to our attention as a result of performing our audit procedures and which we believe are appropriate to communicate to the Committee. The ultimate responsibility for the preparation and presentation of the financial statements rests with the Council.

2.2. Responsibilities

We are responsible for conducting an audit of Gore District Council for the year ended 30 June 2016 in accordance with the Auditing Standards published by the Auditor-General (the "Auditing Standards"), which incorporate the New Zealand Auditing Standards issued by the External Reporting Board ("XRB"). Our audit is performed pursuant to the requirements of the Local Government Act 2002 and the Financial Reporting Act 2013, with the objective of forming and expressing an opinion on the financial statements, non-financial performance information and other information required by Schedule 10 of the Local Government Act 2002, and summary financial statements that have been prepared by management with the oversight of the Councillors. The audit was also completed under the terms of our contract with the Office of the Auditor General. The audit of the financial statements does not relieve management or the Councillors of their responsibilities.

3. Key Areas of Focus & Audit Response

Our audit procedures were focused on those areas of Council's activities that are considered to represent the key audit risks identified during the risk assessment process undertaken during the planning stage of our engagement. Provided below is a summary of these key areas of focus and our responses in respect of each matter following the completion of our audit. We are satisfied that these areas have been addressed appropriately and are properly reflected in the financial statements.

3.1. Rates

Focus Area	Response
<p>Issues within the Local Government sector with regards to problems with rates not being set in accordance with the Local Government (Rating) Act 2002 ('LGRA') has made the legality of rates a top priority with the OAG. Compliance with the detail of the LGRA is vital: if the rate is not within the range of options and restrictions provided for in that Act, it may not be valid.</p> <p>Management and Council need to continue to ensure that the requirements of the LGRA are adhered to and that there is consistency between the rates resolution, the Funding Impact Statement for that year, and the Revenue and Financing Policy in the respective Long Term Plan ('LTP') or Annual Plan ('AP').</p>	<p>Our audit procedures have focussed on the following areas in relation to rates revenue:</p> <ul style="list-style-type: none">• Completing the 'rates questionnaire' compiled by the OAG, (similar to that completed in the prior year), to assess whether rates have been set correctly at the Council;• Reviewing the meeting minutes recording the adoption of the rates resolution, ensuring the rates are in accordance with the revenue and financing policy as well as reviewing any other information available with regard to rates; and• Reconciling the rates strike to general ledger. <p>We have not noted any matters during our rates procedures which we believe should be brought to the attention of the Committee.</p>

3.2. Revaluation

Focus Area	Response			
Gore District Council obtained a revaluation of the infrastructure assets as at 30 June 2016, in accordance with the accounting policy of obtaining a revaluation every three years. Water and roading infrastructural assets were last revalued as at 30 June 2013.	<p>In relation to the 2016 valuations, we completed the following audit procedures:</p> <ul style="list-style-type: none"> Obtained a copy of the valuations and undertook audit procedures regarding the completeness and accuracy of the valuations themselves as well as reviewing and testing underlying assumptions. As part of this process we participated in discussions/correspondence with the valuers to better understand the valuation process, the nature and cause of movements between the 2016 and prior period valuations, and the valuation methodologies applied; Confirmed management has had proper oversight and ownership of the valuations; Confirmed the valuations were accurately reflected in the fixed asset register and general ledger; Reconciled the valuation to the underlying fixed asset register; Challenged the valuer's assumptions; Reviewed the accounting treatment against the requirements of NZ PBE ISPAS 17: Property, Plant and Equipment; and Obtained representations from the valuers with respect to their independence, qualifications, familiarity with NZ PBE IPSAS 17, and the scope, completeness and reasonableness of the valuations, as well as our ability to rely on it. 			
	Roading \$m	Three Waters \$m	L&B \$m	Total
At Previous Valuation Date	\$306.4	\$38.6	\$24.2	\$369.2
Carrying Value (pre valuation)	\$306.7	\$35.4	\$23.7	\$365.8
Revaluation gain	\$6.8	\$2.2	\$4.9	\$13.9
Carrying Value at 30 June 2016 (post valuation)	\$313.5	\$37.6	\$28.6	\$379.7

3.3. Local Government Funding Agency

Focus Area	Response
<p>During the 2015/16 financial year, Council joined the NZ Local Government Funding Agency ('LGFA').</p> <ul style="list-style-type: none"> As at 30 June 2016, total borrowings from the LGFA are \$12m (2015:\$nil). 	<p>We have reviewed the funding documentation and assessed whether the accounting treatment of the debt is appropriate and in line with guidance provided to the Local Government sector. We have reviewed the disclosure relating to borrowings in the financial statements.</p> <p>We have not identified any issues in relation to LGFA borrowings or how these are disclosed in the financial statements.</p> <p>We highlight that because of the requirements relating to LGFA, as auditors, we are required to undertake additional work in respect of a separate audit of the debenture and security stock register, and a separate report to the Trustee. These are separate pieces of work and as such are subject to additional letters of engagement and fees.</p>

3.4. Statement of Service Performance

Focus Area	Response
<p>The Council's annual report is required to include an audited Statement of Service Performance ('SSP') which reports against the performance framework included in the LTP.</p> <p>The SSP is an important part of Council's annual performance reporting and it is important it adequately "tells the performance story" for each Group of activities.</p> <p>Our audit opinion considers whether the service provision information:</p> <ul style="list-style-type: none"> Is based on appropriately identified elements (outcomes, impacts, outputs), performance measures, targets/results; and Fairly reflects actual service performance for the year (i.e. not just reports against forecast). 	<p>No issues were noted during our work.</p>

3.5. Governance, Reporting & Legislative Compliance

Focus Area	Response
<p>Council is subject to significant regulatory and legislative compliance requirements. As such, Council needs to have adequate systems in place to monitor compliance with legislation along with any changes occurring in the applicable legislation.</p> <p>Under the OAG auditing standards we are required to perform sufficient audit work to be satisfied that Council has processes in place to comply with material legislative and regulatory requirements.</p> <p>We are also required to consider governance and accountability within the local authority and report and comment on effectiveness, strengths and weaknesses. Governance and accountability covers a broad range of areas including:</p> <ul style="list-style-type: none">• legislative compliance;• monitoring of financial results;• risk management; and• sensitive expenditure.	<p>We reviewed the systems for monitoring legislative compliance for Council and, in a similar process to 2015, completed an assessment of the Council's rating procedures against the legislative requirements and found no material issues.</p> <p>We note that Council uses external legal Counsel to perform reviews of relevant laws and compliance where necessary. In 2015, Council had the rates resolution reviewed by Simpson Grierson who made minor comments in regards to improvements which could be made.</p> <p><u>Sensitive Expenditure</u></p> <p>The Council is subject to scrutiny and attention in regards to sensitive expenditure as is normal in public sector entities. Areas that tend to be particularly sensitive include:</p> <ul style="list-style-type: none">• Council fees and expenses;• Sensitive expenditure (travel, entertainment, expense reimbursement etc.);• Severance payments;• Chair, Chief Executive and Senior Management expenditure, reimbursements, and related party transactions. <p>No issues were noted as part of our work.</p>

4. Internal Controls & Other Recommendations

Our audit approach requires us to obtain an understanding of an entity's internal controls, sufficient to identify and assess the risks of material misstatement of the financial statements whether due to fraud or error but is not designed to provide assurance as to the overall effectiveness of controls operating within the Council.

We have not identified any material weaknesses in internal controls relating to the prevention and detection of fraud and error which would impact upon our ability to provide our opinion on the financial statements. However, we did note a number of control observations and have reported our recommendations for improvement to management. The more significant observations which we consider warrant reporting to the Council are detailed below. The matters being communicated are limited to those deficiencies that we have identified during the audit and that we have concluded are of sufficient importance to merit being reported. These recommendations should be assessed by you for their full commercial implications before they are implemented.

4.1 Capital Expenditure Underspend

Observation	Issue	Recommendation
The results of the infrastructure revaluation in the current year highlighted that Council are not spending enough on capital expenditure. This is demonstrated across all infrastructure assets (notably 3 Waters) where the revaluation has decreased relative to the cost of the assets. We also note that Council have failed to meet the Essential Services benchmark in the last 5 years.	This poses a risk of Council creating intergenerational inequity.	<p>We understand that significant capital works were planned for this year, in relation to Ajax pump station. Additionally, the 2015/25 LTP signalled significant capital works during the plan period. However the Ajax pump station timing was delayed as Council were required to seek arbitration to secure the easement across private property. The easement has now been secured and work will be completed in the 2016/17 financial year. This project has a budgeted spend of approximately \$3m.</p> <p>We recommend that council ensure capital works budgeted can be reasonably expected to be achieved to reduce risks around creating intergenerational inequity.</p>

4.2 Review of Assets Useful Lives

Observation	Issue	Recommendation
Through our review of the Fixed Asset Register we identified assets that remain in use and are fully depreciated. The total number of assets per the Fixed Asset register at 30 June 2016 is 1,337, and of this 498 are fully depreciated (37%). We note that majority of these assets fall within the Office Equipment (269 assets) and Plant and Equipment (175 assets) asset classes.	This indicates useful lives may need to be considered at a more granular level. The \$ amounts included are not significant given the nature of the assets.	We recommend a review is undertaken of the useful life of this type of asset or consideration is given to fully writing off the asset from the fixed asset register.

4.3 Interest Rate Swaps

Observation	Issue	Recommendation
We understand that in the current year, Council repaid the loans held with ANZ and obtained funding from the LGFA, as it provided a lower cost of servicing. When the debt was held with ANZ, the Council had interest rates swaps in place to stabilise the cost of funding.	The Council will be paying interest rate swap amounts that are out of the money for the remaining duration of the swap lives, assuming there are no changes to interest rates themselves.	The swaps provide an economic hedge of the current interest rates. However, Council may consider whether there are more cost effective options available, which may include closing out the swaps early.

4.4 Holiday Pay Act 2003 – Calculation of Leave Entitlements

Observation	Issue	Recommendation
<p>The Ministry of Business, Innovation and Employment's (MBIE) publication SUMMARY PROBLEM DEFINITION - Holidays Act 2003 – non-compliance [ID: MBIE-MAKO-27530664] outlines issues identified in the calculation of employee leave entitlements including:</p> <ul style="list-style-type: none"> • substandard payroll systems in the New Zealand market • poor configuration of payroll systems • poor use of payroll systems by payroll practitioners due to a generally insufficient understanding of the complexities involved in ensuring compliance with employment standards legislation • undervaluation of the importance of payroll functions • insufficient resources dedicated to compliance including low demand for and supply of skilled payroll practitioners • Difficulties understanding the [Holidays] Act [2003]. 	<p>Holiday pay entitlements may be calculated incorrectly.</p>	<p>We noted no issues with respect to payroll in the course of planning and performing our standard audit procedures to obtain reasonable assurance that the financial statements are free of material misstatement.</p> <p>However, we recommend that the Council should look to take steps in order to obtain assurance over the accuracy and integrity of their payroll system for their own purposes.</p>



Issues Identified in the Prior Year that Remain Pertinent in 2016

We note below issues raised in prior years. Some of these issues have been raised for more than one year. Council should focus on addressing the points during 2015/16, or providing a reason for accepting the risk associated with the issue.

Observation	Issue	Recommendation
Councillor's Interest Register	All Council members are subject to the Local Authorities (Members' Interest) Act 1968. The Act requires that the Council or Committee members must not discuss or vote on a matter in which they have a pecuniary interest when it is being considered by the Council or a committee of the Council. We note that the current Interest Register has not been updated since the 2012 audit of the financial statements.	<p>Council should update the Interest Register on a regular basis.</p> <p>2016 Update</p> <p>We note that the interest register has been updated in the current year, however, not all interests had been disclosed by Councillors. In some instances Councillors had not completed their interest disclosure form.</p>



5. Summary of Unadjusted Differences

5.1. Unadjusted Differences

In performing our audit of Council for the year ended 30 June 2016 we have not identified any uncorrected errors that could, either individually or in aggregate, have a material effect on the financial statements for the year.

Unadjusted misstatements identified	Assets Dr/(Cr) (\$ '000)	Liabilities Dr/(Cr) (\$ '000)	Equity Dr/(Cr) (\$ '000)	Profit & loss Dr/(Cr) (\$ '000)
Current Year				
Water supply additions not accounted for in the Opus Valuation	\$41	-	(\$41)	-
Prior Year				
<u>Matters Relating to the Prior year Identified in the Current Year</u>				
None noted.	-	-	-	-
Total	\$41	-	(\$41)	-

5.2. Omitted Disclosures Assessed by Management as not being Material

In performing our audit we have not identified any omitted disclosures that have not been adjusted in the financial statements for the year ended 30 June 2016.

6. Other Communications

The following matters are communicated in accordance with the requirements of New Zealand auditing standards.

Matter to be communicated	Response
Independence	We confirm that we have maintained our independence in accordance with the independence requirements of the Auditor- General which includes <i>Professional and Ethical Standard 1 (Revised): Code of Ethics for Assurance Practitioners</i> issued by the External Reporting Board and, in our professional judgement, we are independent and the objectivity of the audit engagement partner and audit staff are not compromised.
Written representations	A copy of the representation letter to be signed on behalf of the Council has been circulated separately.
Non-compliance with applicable laws and regulations	We did not become aware of any non-compliance with applicable laws and regulations that may have an impact on the determination of material amounts and disclosures in the financial statements.
Fraud	No matters relating to fraud, concerning either employees or management came to our attention.
Accounting policies and financial reporting	<p>Council adopted PBE IPSAS financial reporting standards during the prior year. There were no material changes in accounting policies during the year ended 30 June 2016.</p> <p>We have not become aware of any significant qualitative aspects of the entity's accounting practices, including judgements about accounting policies, accounting estimates and financial statement disclosures that need to be communicated to the Committee, other than those already communicated in this report.</p>
Related parties	No significant related party matters other than those reflected in the financial statements came to our attention that, in our professional judgement, need to be communicated to the Committee.
Professional fees / relationships	In performing our audit of Council for the year ended 30 June 2016, no relationships existed between the firm, network firms and Council that, in our professional judgement, may reasonably be thought to bear on independence. Other assurance fees in respect of the audit of the register and trustee reporting have been charged to Council during the 2015/16 year.



Appendix A - Analysis of Professional Fees

The professional fees earned by Deloitte in the period from 1 July 2015 to 30 June 2016 are disclosed in the financial statements as follows:

	Council	
	2016 (\$000)	2015 (\$000)
Statutory audit (excludes OAG contribution and disbursements)	92	90
Audit of long term plan	-	86
Fees paid to auditor for other audit, assurance and related services*	5	-
TOTAL	97	176

*Relates to fees in respect of the audit of the register and trustee reporting (both as a result of Gore becoming part of the LGFA).



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