



Audit New Zealand
Te Tari Arotake o te Motu
Wellington Office
Level 9
St Paul's Square
45 Pipitea Street
Thorndon
Private Box 99
Wellington
New Zealand
Telephone +64-4 496 5099
Facsimile +64-4 496 5195
Website www.auditnz.govt.nz

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30 November 2003

Greg Schollum
Chief Financial Officer
Greater Wellington Regional Council
PO Box 11-646
WELLINGTON

Dear Greg

GREATER WELLINGTON REGIONAL COUNCIL AUDIT FOR THE YEAR ENDED 30 JUNE 2003

1 INTRODUCTION

We have completed the audit of Greater Wellington Regional Council ("the Council") for the year ended 30 June 2003. This letter provides a summary of:

- ▲ the audit opinion
- ▲ our assessment of your financial and non financial management
- ▲ our assessment of your compliance with legislative requirements
- ▲ significant matters arising from the audit.

We also refer you to the interim management report dated 11 April 2003.

2 AUDIT OPINION

An unqualified audit opinion was issued on the Council's financial statements.

3 FINANCIAL AND SERVICE PERFORMANCE MANAGEMENT

Our interim report dated 11 April 2003 included an interim assessment of the Council's control environment for 2002/03 based on the work performed to date. We have since completed our assessment of both systems and the management control environment for service performance information, and these grades, together with an update of the financial grades, are included below.

Matters identified in the "comments" column are reported more fully in later sections of this letter.

Management aspect	Assessment	Comment
Financial control systems	Excellent (2002: Excellent)	<p>The Council's financial control systems are working well. Our work in this area indicated the following:</p> <ul style="list-style-type: none"> ▲ Sound controls operate over Council's key financial systems. Transactions are authorised and changes to the masterfile systems are monitored and reviewed. ▲ Formal delegations are in place and are appropriate. ▲ Key asset management plans have been updated and the information is linked into the long-term council community plan (LTCCP). These appear to be in the nature of working documents by which Council can more effectively manage key assets and feed appropriate information into Council's planning process. ▲ We are satisfied with the level of controls over the purchasing system and sensitive expenditure.
Financial management information systems	Excellent (2002: Excellent)	<p>Overall the information systems to support the operational activities of Council are well managed. Work is continuing in some areas to move procedures further towards good practice, specifically:</p> <ul style="list-style-type: none"> ▲ Controls over the use and monitoring of super user access to SAP. ▲ Establishment of an Information Systems Management Group to provide direction for future IT requirements. ▲ Development of an IT security and use policy. ▲ Development of a short to medium-term IT strategy.

Management aspect	Assessment	Comment
Financial management control environment	Excellent (2002: Excellent)	<p>The financial control environment is sound. This is evident by the following:</p> <ul style="list-style-type: none"> ▲ Budgets are reviewed at divisional level and overall Council level. The Council's budgetary processes are rigorous with close monitoring of expenditure throughout the financial year. The Council also recently developed a Long Term Council Community Plan (LTCCP) covering the years 2003-2013. ▲ Monthly reports are produced at divisional level, while both financial and performance reports are provided to the Policy, Finance and Strategy Committee on a quarterly basis, with monthly reporting by exception in between. ▲ The Policy, Finance and Strategy Committee fulfils the function of an Audit Committee. ▲ Financial management policies and procedures are in place.
Service performance information and information systems	Excellent (2002: Excellent)	<ul style="list-style-type: none"> ▲ Service performance information systems are appropriate for the nature of the organisation. ▲ The Council has good systems to record service performance and the internal controls over non-financial data are well established.
Service performance management control environment	Excellent (2002: Excellent)	<p>The Council has excellent higher level controls including:</p> <ul style="list-style-type: none"> ▲ Quality assurance ▲ Self-review procedures ▲ Planning processes ▲ Exception reporting <p>Performance standards are outcome focused and are linked to the day-to-day operations of the Council. The Council reports regularly on service performance, enabling the effective monitoring of service provision.</p>

4 COMPLIANCE WITH LEGISLATIVE REQUIREMENTS

We have reviewed the systems and procedures that the Council employ to identify and comply with legislative requirements. We note that, as part of its overall approach to meeting its legal compliance obligations, Council is part of the SOLGM Legal Compliance project.

We did not note any instances of non-compliance with legislation other than the technical breach of legislation arising from the Council's ownership of the Waterloo Interchange which has now been resolved with the passing of the Land Transport Management Act.

5 SIGNIFICANT MATTERS

5.1 Long Term Council Community Plan (LTCCP) – Statement of Service Performance

The Council has developed a Long Term Council Community Plan (LTCCP) for 2003-2013 based on an overall goal of a sustainable region and ten community outcome areas. We reviewed the draft LTCCP and a letter was issued to the Council dated 8 May 2003 with our recommendations. This included the following:

- ▲ Legislative compliance – Overall, we were satisfied that the Council had complied with all material aspects of the Local Government Act 2002, taking into account the transition provisions contained within the Act. We were also satisfied that the Council's proposed timetable for the adoption of the LTCCP complied with the Act.
- ▲ Performance measures – We found that there were good linkages between the "Take 10 Quality for Life" elements and the specific goals, targets and measures. The performance measures appear to reflect the significant groups of activities undertaken by the Council.

We acknowledge that in preparing the LTCCP for adoption in 2003, the Council was one of a small number of early adopters and therefore was pioneering the approach to be taken in a number of areas.

We recognise that "best practice" for a number of policies and requirements of the Act is still being developed by the sector, and as such some of the issues we raised are comments and suggestions only, and do not necessarily reflect a legislative breach.

The Council agreed to incorporate some of our recommendations into the final LTCCP, which was adopted on the 30 June 2003 in accordance with section 93 of the Local Government Act 2002.

5.2 Provisions and accruals

As part of our audit review we assess whether the Council's provisions comply with the definition of a liability as defined in the Statement of Concepts prepared by the Institute of Chartered Accountants of New Zealand. Liabilities are the future sacrifices of service potential or of future economic benefits that the Council is presently obliged to make to other entities as a result of past transactions or other past events.

As mentioned in previous management reports there are several Council provisions that do not meet the definition of a liability. However, the Council has made progress in decreasing the number of provisions and it is pleasing to note that the total value of these provisions has decreased from \$0.9 million in 2002 to \$0.5 million in 2003.

We also noted in the current year that one division of the Council accrued costs of \$100,000 for the purchase of a fixed asset in order to meet budget targets. The fixed asset had not left the supplier's premises at balance date and ownership of the goods had not transferred. In this case the obligation does not exist at balance date and therefore the definition is not met. We also note that the accrual of this cost was carried through into the Statement of Service Performance in the Annual Report.

We recognise that the Council does have a mechanism in place for re-budgeting at year-end, and that there is a quality review completed by Finance of all accruals submitted by the divisional accountants. However, this item was still incorrectly accrued.

We have assessed the impact of the above on the financial statements as not material. However, we strongly recommend that the Council comply with generally accepted accounting practice.

Management response

We agree that the provisions that did not meet the liability definition were not material. The incidence of accruing costs in order to meet budget targets will be followed up to ensure the situation does not recur.

5.3 Doubtful debts provision

The Council has a general provision for doubtful debts of \$1,150,000 to cover rates receivable. Our discussions with Council personnel highlighted that this provision for rates receivable is a general rather than a specific provision and may be used to cover successful challenges to past rates which could go beyond the extent of unpaid rates at 30 June in any given year. This method of determining the doubtful debts provision has been followed in prior years.

It is generally accepted accounting practice to provide for existing rather than potential doubtful debts. Where general provisions are used they should be calculated

on a reasonable basis, such as the Council's past history of debts written off as uncollectible or all debts that are a certain number of days old.

Although we assessed the impact of the above on the financial statements as not material, it is significant enough to cause us some concern and we recommend that the Council reassess the rationale it uses to provide for doubtful debts.

Management response

The provision is considered prudent given the Council does not have total control over the valuation and rates collection process.

6 LESS SIGNIFICANT MATTERS

Less significant matters are detailed in Appendix One to this letter.

7 UPDATE OF KEY MATTERS RAISED IN PREVIOUS MANAGEMENT LETTER

The current status of each of the items that were "outstanding" at the end of the 2003 interim audit is detailed in Appendix Two.

8 REVIEWS ON BEHALF OF THE AUDITOR-GENERAL

Appendix Three details the results of the reviews we performed on behalf of the Auditor-General. No issues arose out of these reviews that would require your attention.

9 ACKNOWLEDGEMENT

I would like to express our appreciation for the assistance provided to us by your staff during our audit. If you have any queries on the above matters, please do not hesitate to contact me on 496 3099.

Yours sincerely



Rudie Tomlinson
Director

cc Paul Laplanche, Finance Manager

APPENDIX 1

LESS SIGNIFICANT MATTERS

1 WORK IN PROGRESS (WIP) – ASSETS IN USE REMAIN IN WIP

During our review of the system for Water Reticulation infrastructural assets, it was noted that assets in Work In Progress (WIP) are not transferred until year-end. This could result in an asset being in use during the year, but not being transferred from WIP until the end of the financial year. This will result in an understatement of depreciation.

We suggest that for depreciation expense to be charged correctly, all assets should be transferred from WIP as soon as they are in use and appropriate depreciation charged.

Management response

We will investigate the practicality of what is suggested.

2 EXPENSE REIMBURSEMENT CODING

During our testing of the “staff expense reimbursement” general ledger coding, we identified several items which were incorrectly classified. These items were made up of a variety of travel type items, such as taxi and train fares.

We recommend that greater care is taken when coding expenditure items into the general ledger in order to ensure that individual expenditure categories are accurate and include all items associated with that expenditure type.

Management response

It is extremely difficult to ensure all items of expenditure are always correctly coded. However, staff will be reminded of the importance coding.

APPENDIX 2

STATUS OF MATTERS PREVIOUSLY REPORTED

Issue	Current status
<p>Infrastructural assets revaluation: Flood protection assets</p> <p>Flood protection assets were revalued as at 30 June 2002 as part of the Council's fixed asset revaluation cycle. We made several recommendations as a result of our review. These were as follows:</p> <ul style="list-style-type: none"> ▲ Valuers are informed that the valuations that they are to carry out should be in accordance with Financial Reporting Standard-3. ▲ That the Council maintain the level of asset information for flood protection assets at component level. ▲ That any assets found subsequent to balance date be treated as additions, rather than be wrapped up in the next revaluation cycle. 	<p><i>The Council has applied the lessons learnt from the revaluation of flood protection assets to their revaluation of parks and reserves.</i></p> <p><i>Issue cleared.</i></p>
<p>Parks and reserves: vested and heritage assets</p> <p>During our 2002 audit we discussed with the Council the scheduled revaluation of its parks and reserves for the 2003 financial statements. We raised several matters for the Council to consider as part of the revaluation exercise.</p> <ul style="list-style-type: none"> ▲ That the Council critically reviews the results of the valuation to determine whether the revaluation has been impacted by the inclusion of previously unrecorded assets. ▲ That Council are aware of the possibility that further environmental obligations may be identified as a result of the revaluation. ▲ That the vested nature of parks and reserves be considered by the valuer when they are valuing the assets and by Council in considering whether such restrictions should be disclosed. ▲ That Council consider the potential existence of heritage assets. 	<p><i>The Council has applied the lessons learnt from the revaluation of flood protection assets during their revaluation of parks and reserves.</i></p> <p><i>Issue cleared.</i></p>

Issue	Current status
<p>FRS-3 compliance</p> <p>The Council does not disclose in the Annual Report the split between those assets valued at historical cost and those that have been revalued</p> <p>Financial Reporting Standard No.3 (FRS-3) requires that the financial statements disclose, where more than one basis is used, the gross carrying amount relating to each basis. For example, where the carrying amounts of some items are revalued amounts, but other items are capitalised at cost before the next revaluation occurs, the gross carrying amounts attributable to each measurement base within the class are to be disclosed (Paragraph 11.1).</p> <p>We recommended that the Council make this distinction in future to fully comply with the requirements of FRS-3.</p>	<p><i>The Council have disclosed in the 2002/03 Annual Report the split between those assets valued at historical cost and those that have been revalued.</i></p> <p><i>Issue cleared.</i></p>
<p>Employee Provisions</p> <p>▲ Separation of current and non-current liabilities</p> <p>Note 8 "Current Liabilities" of the Council's Annual Report includes Employee Provisions. This provision represents long service leave, retirement leave and annual leave balances. A portion of this leave will not be taken within the next financial year and therefore this portion of the liability is not "current".</p> <p>Financial Reporting Standard No.2 (FRS-2) requires current and non-current liabilities to be separately disclosed (paragraph 8.5). We recommended that the Council consider determining the amount of the employee provisions that are long term and disclose the split between current and long term liabilities. The Council may need actuary advice in order to determine how much of the liability is long term.</p>	<p><i>The Council have disclosed in the 2002/03 Annual Report the split between Employee provisions that are considered to be generally current or non current.</i></p> <p><i>Issue cleared</i></p>
<p>▲ Retirement leave</p> <p>We noted during our review of the actuary retirement leave provision calculation that there were three people that have not yet had their retirement leave frozen. From our discussions with the Employment Relations Manager it was discovered that the incorrect three people had been selected from the information provided by the Employment Relations department to Finance. We assessed the misstatement arising from the above error as minimal. We recommended that the retirement leave report be corrected for the above error.</p>	<p><i>The error was considered isolated.</i></p> <p><i>Due to the costs of completing an actuarial calculation annually the Council have decided to revert to a three yearly cycle with annual reasonableness checks. They have confirmed that the balance as at 30 June 2003 was reasonable.</i></p> <p><i>Issue cleared</i></p>

Issue	Current status
<p>▲ Long service leave</p> <p>We found during our review of Finance's actuarial long service leave calculation that not all the required information had been updated appropriately.</p> <p>Employment Relations should ensure that each employee's information is updated on an annual basis in the model including: contract type, salary level, long service leave days taken, terminations and any new employees.</p> <p>Employment Relations has also informed us that the collective employment contract is currently being updated, and they will need to consider this when updating the model for any changes to long service leave entitlements during the next financial year.</p> <p>We recommended that the long service leave report be corrected.</p>	<p><i>The error was considered isolated.</i></p> <p><i>Due to the costs of completing an actuarial calculation annually the Council have decided to revert to a three yearly cycle with annual reasonableness checks. They have confirmed that the balance as at 30 June 2003 was reasonable.</i></p> <p><i>Issue cleared</i></p>
<p>Entertainment expense disclosure</p> <p>The Local Government Act 1974 section 223J requires certain expenditure to be disclosed separately in the financial statements including entertainment expenditure. The Council currently is not disclosing this expenditure separately in the financial statements.</p> <p>Our review of the expense codes of the Council indicates that there are not separate account codes set up for these types of expenditure. We do not anticipate these expenses to be material but as the Local Government Act requires disclosure we recommend that the Council set up account codes to ensure that this type of expenditure is captured and reported in the Council's financial statements.</p>	<p><i>Separate account codes have not yet been set up for these types of expenditure.</i></p> <p><i>Issue applies to the Annual Report for the year ending 30 June 2003. Disclosure will not be required under the Local Government Act 2002, which will apply to the Annual Report for the year ending 30 June 2004.</i></p>
<p>Weighted Average Calculations</p> <p>The investment note disclosure in the Council's financial statements refers to weighted average interest rates. Our review of these rates suggests that they do not reflect the average of the full financial year.</p> <p>We recommended that the Council consider calculating the weighted average interest rate for its investments disclosure to reflect interest rates throughout the year.</p>	<p><i>Client commented that their current disclosure is clear. No change is proposed.</i></p> <p><i>Issue cleared.</i></p>

Issue	Current status
<p>Annual Plan improvement</p> <p>We noted during our comparison of Annual Plan with the 2001/02 and 2002/03 Annual Reports that some of the Annual Plan comparatives had been adjusted to assist with comparability. The main area of concern is that the Annual Plan does not differentiate between current and long term assets & liabilities and therefore finance is required to split the total for these items at the end of the financial year to provide comparatives.</p> <p>We recommend that in future the Annual Plan include the split between current and long term assets and liabilities to improve the quality of the comparatives provided.</p>	<p><i>The split between current and long-term assets and liabilities was not completed for the 2002/03 Annual Plan. However, this improvement has been implemented into the 2003-2013 Long Term Council Community Plan.</i></p> <p><i>Issue cleared.</i></p>
<p>Air Tel Limited shareholding</p> <p>The Council holds 21,000 fully paid shares in AirTel Limited that were acquired at no cost in 2001 as a result of the Wairarapa radio Telephone Users Association's decision to form a limited liability company and issue shares to users. The shares have a nominal value of \$1 per share and cannot be sold by the Council until 2005. The Council has disclosed this investment by way of note in the financial statements.</p> <p>We recommend that the Council include the shares as an investment, valued at their nominal value of \$1 per share, in their financial statements. This is consistent with the Council's treatment of its share holding in New Zealand Local Government Insurance Corporation Ltd.</p>	<p><i>Client has disclosed this information by way of note. The amount is not considered material.</i></p> <p><i>Issue cleared.</i></p>
<p>IT security and use policy not documented</p> <p>We have noted that the IT department's policies and procedures for governing security of the system (eg, use of passwords, backups, change management) and use of the system by staff (eg, internet use, installing of software) are not currently documented or distributed to staff.</p>	<p><i>An Information and Technology and Support Services Continuity Plan was developed in October 2001. However, this does not cover the policies and procedures on IT security.</i></p> <p><i>Issue outstanding</i></p>

<p>IT strategy</p> <p>While IT features in the Long Term Financial Strategy (LTFS), the Council does not have a short to medium term IT strategy.</p>	<p><i>It is pleasing to note that the IT manager liaises with Support Services and the divisions regarding IT requirements.</i></p> <p><i>At the final audit it was noted that an Information Systems Management Group is still to be established.</i></p> <p><i>The IT manager has an objective to document and report on the state of IT systems across the council this financial year.</i></p> <p><i>We will follow up this next year.</i></p> <p><i>Issue outstanding.</i></p>
<p>Super users</p> <p>The SAP_ALL user profile allows user access to make changes to general ledger transactions, payroll transactions and changes to the suppliers masterfile. There are currently no controls in place to ensure that those with SAP_ALL access have not made any unauthorised changes to the general ledger transactions.</p>	<p><i>WRC have created a new profile for the system administrators and put in place adequate mitigating controls. We noted that:</i></p> <ul style="list-style-type: none"> ▪ <i>The new system administrator profile (Z_WRC_SYSTEM_ADMIN) provides system wide reporting, enquiry, access to system management tools, and limited access to update records. This profile is a combination of 9 standard SAP profiles.</i> ▪ <i>SAP_ALL and SAP_NEW are still within the system and access is restricted to Deloitte Consulting and emergencies.</i> ▪ <i>In the event of an emergency CFO approval must be obtained before the system administrator can access SAP_ALL.</i> ▪ <i>Any changes to the system administrator profiles need approval of the Finance or Employment Relations Manager.</i> ▪ <i>Audit reports have been set up for Finance and Employment Relations to check changes made to the profiles, master data and accounting documents.</i> <p><i>Issue cleared</i></p>

<p>Annual leave balances</p> <p>We noted that annual leave balances remained high which poses a significant liability to the Council. This increases further with salary increments.</p> <p>We suggested that Council discuss with individual employees a plan to reduce their leave balances.</p>	<p><i>The Council has an action plan for the timely review of annual leave balances.</i></p> <p><i>Council have written to all staff regarding the level of leave balances held. Business Unit Managers are responsible for actively monitoring, and managing employees' leave balances.</i></p> <p><i>At final audit the action plan for the timely review of annual leave balances is in place. The annual leave balances remained high and we will continue monitor future progress on this issue.</i></p> <p><i>Issue cleared.</i></p>
<p>Protected Disclosures Act 2000</p>	
<p>We noted that a new policy on the Protected Disclosures Act 2000 had been developed and distributed to Council staff.</p> <p>In our view the policy could be enhanced by covering the following points:</p> <ul style="list-style-type: none"> ▲ Specific mention of accepting anonymous disclosures ▲ Include a definition of "serious wrongdoing" ▲ Include a definition of "employee" ▲ Define all parties included as appropriate authorities ▲ Describe which disclosures can be made per section 6 of the Act ▲ Exclude disclosure of professional legal privilege <p>Due to the sensitive nature of any potential protected disclosures, staff members should be able to gain sufficient understanding from the policy to carry out a protected disclosure without any further consultation. Accordingly, the policy should be a standalone document and no reference to legislation should be necessary.</p>	<p><i>The current PDA 2000 policy remains in place.</i></p> <p><i>At final audit, the Council will update the policy for our recommendations.</i></p> <p><i>Issue outstanding</i></p>

APPENDIX 3

REVIEWS ON BEHALF OF THE AUDITOR-GENERAL

Issue	Status/Findings
<p>Implementation of the Local Government (Rating) Act 2002</p> <p>In particular:</p> <ul style="list-style-type: none"> ▲ Review the information Council has available in order to comply with the new legislation. ▲ Review the rates cap calculation to confirm that the Council's targeted rates and uniform annual charges fall within the threshold ▲ Review the Council's Financial Impact Statement and establish the extent of change towards the use of targeted rates compared with the previous use of separate rates. ▲ Assess whether the Council has met its obligations to adopt new policy requirements where it intends to exercise its powers under the Act. 	<p><i>We assessed that the Council has adopted rates remissions and postponements policies with the exception of an early payments policy. Hence, we have concluded that the Council has met its statutory obligations under the Act to adopt the relevant policies where it intends to exercise these powers.</i></p> <p><i>We reviewed the rates cap calculation and have concluded that the Council is fully aware of the rating cap and that they have ensured that they are within the 30% cap requirement under section 21 of the new Act.</i></p> <p><i>Based on the above findings, the Council has met the requirements of the Local Government Act 2002 and the Rating Act 2002 in setting rating information in its Financial Impact Statement. The Council has also appropriately adjusted for any changes in the use of targeted rates from separate rates.</i></p>
<p>Implementation of the Local Government Act 2002</p> <p>In particular:</p> <ul style="list-style-type: none"> ▲ The adequacy of information to allow the Council to specify service levels and performance targets for its activities. ▲ The Council's asset management information base and progress towards advanced asset management planning. <p>The concept of significance is central to the Act and is intended to help local councils direct the appropriate level of attention to decisions. The OAG intends to carry out an analysis of councils' significance policies. We will forward a copy of the Council's policy for this purpose.</p>	<p><i>In general, the Council's Asset Management Plans provide appropriate information at both an individual asset and network level. They clearly define the level of service required and translate through to the operational plans of the Council. The Council has robust asset information to support its LTCCP.</i></p> <p><i>In terms of service levels, we have selected the Council's resource consents for the regulatory service and transport for the community service. The Council clearly defined the level of service required and translate through to the operational plan of the Council.</i></p> <p><i>As for the significance policies, a copy of the Council's significance policies has been forwarded to the OAG. The policy was signed off on 18 March 2003 and our comments were incorporated in the feedback letter on the LTCCP. The final LTCCP and policies were adopted on 30 June 2003.</i></p> <p><i>We have concluded that the Council has met its obligations under the new Act and adopted a significance policy before 1 July 2003.</i></p>