

Office of the Auditor General  
Western Australia

# Annual Financial Report Audit - Planning Summary

## City of Kalamunda

Year ended 30 June 2020

13 May 2020



## 1. The Planning Summary

This Summary of our Audit Plan explains our approach to the audit of the annual financial report.

In particular, this Summary includes:

- Introduction
- Our Audit Approach
- Significant Risks and Other Audit Issues
- Audit Emphasis and Significant Account Balances
- Internal Audit
- Management Representation Letter
- Related Entities
- Reporting Protocols
- Proposed Audit Schedule
- Specific Audit Requirements
- Audit Fee
- Your Audit Team
- Other Audit Activities

If there are any matters in the Summary that you would like clarified, please do not hesitate to contact us.

There may be areas where you would like us to increase the audit focus. We would be pleased to discuss these to determine the most efficient and effective approach to performing this work.

## 2. Introduction

The annual financial statement audit of your local government is one of 132 that the Auditor General will perform for 2019-20. We have elected to use our OAG staff to perform your audit in-house.

Our audit approach is designed to specifically focus audit attention on the key areas of risk you face in reporting on your finances and performance.

It is important to note that:

- Under the *Local Government Act 1995* and associated regulations, the Council and the CEO are responsible for keeping proper accounts and records, maintaining effective internal controls, preparing the annual financial report, and complying with the Local Government Act and Regulations, and other legislative requirements.
- An audit does not guarantee that every amount and disclosure in the annual financial report is error free. Also, an audit does not examine all evidence and every transaction. However, our audit procedures should identify errors or omissions significant enough to adversely affect the decisions of users of the annual financial report.
- The Council and CEO are responsible for ensuring the accuracy and fair presentation of all information in its annual report, and that it is consistent with the audited annual financial report. We do not provide assurance over your annual report.
- Under the *Local Government Act 1995* and associated regulations, the Council and the CEO have responsibility for maintaining internal controls that prevent or detect fraud or error and to ensure regulatory compliance. The Audit Committee and the Auditor General should be informed by management of any fraud or material errors. During the audit we will make inquiries with management about their process for identifying and responding to the risks of fraud, including management override. It should be noted that our audit is not designed to detect fraud, however should instances of fraud come to our attention, we will report them to you.

Our audit is conducted in accordance with Australian Auditing Standards. Our aim is to provide reasonable assurance whether the annual financial report is free of material misstatement, whether due to fraud or error. We perform audit procedures to assess whether, in all material respects, the annual financial report is presented fairly in accordance with the *Local Government Act 1995*, *Local Government (Financial Management) Regulations 1996* and Australian Accounting Standards.

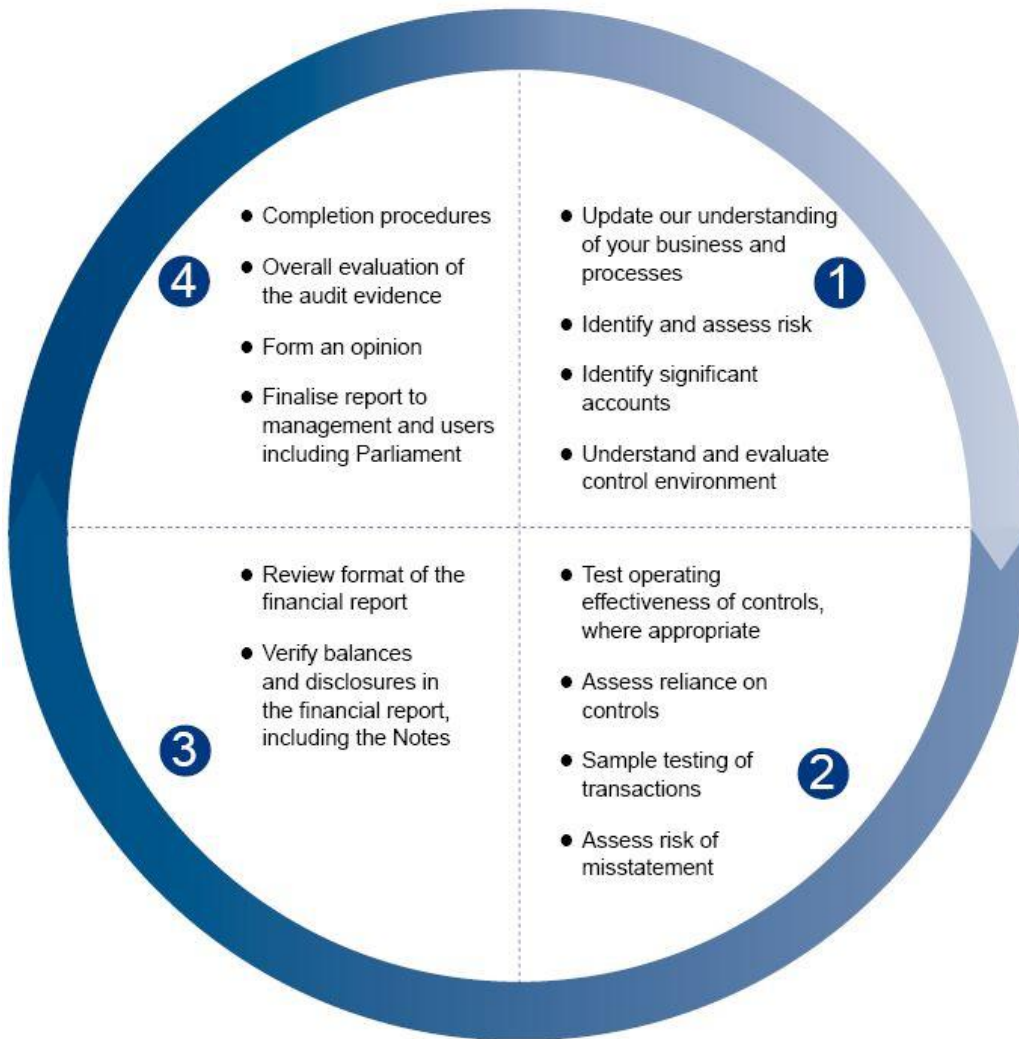
The nature of the audit is influenced by factors such as:

- the use of professional judgement
- selective testing
- the inherent limitations of internal controls
- the availability of persuasive rather than conclusive evidence.

As a result, an audit cannot guarantee that all material misstatements will be detected. We examine, on a test basis, information to provide evidence supporting the amounts and disclosures in the annual financial report, and assess the appropriateness of the accounting policies and disclosures used and the reasonableness of significant accounting estimates made by management.

### 3. Our Audit Approach

Our nationally recognised audit approach comprises four steps:



## 4. Significant Risks and Other Audit Issues

Through discussions with your staff, we have identified the following issues and key areas of risk affecting the audit.

Details of Risk / Issue	Audit Approach
<p>COVID-19</p>	<p>We will work with your management to minimise the risk for your staff and councillors, our staff, and to your operations, while completing audits in the best timeframe possible under the circumstances.</p> <p>This will likely involve more audit work being performed remotely rather than at your premises, and/or delaying audit work as and when unforeseen circumstances arise.</p> <p>We have existing processes for auditing remotely, and consider these adequate for the COVID-19 circumstances. However we are ready to discuss your needs, provided they do not restrict the scope of our audit.</p> <p>In this online working environment, we take the following precautions:</p> <ul style="list-style-type: none"> <li>• our portal through which entities transfer audit related information, has separate secure folders accessible only by the relevant entity</li> <li>• As always, information from entities is stored and reviewed in our secure IPSAM audit software.</li> <li>• Our laptops are password protected at the BIOS, hardware and Operating System level, and the hard drives are encrypted and cannot be accessed if removed.</li> <li>• We have commenced using Microsoft Teams for meetings and for some audit discussions.</li> <li>• We take precautions to ensure that entity staff and our staff are not deceived by outside parties into divulging information. We welcome discussion of any specific requirements you may have in this regard.</li> </ul>
<p>Audit findings reported in the previous audit:</p> <ul style="list-style-type: none"> <li>• Financial audit – 2 significant and 10 moderate findings</li> <li>• Information System audit - 8 moderate and 2 minor findings</li> </ul>	<p>We will follow up these issues to assess the extent of action taken.</p>
<p>Key changes to accounting standards that impact your entity for the first time this year:</p> <ul style="list-style-type: none"> <li>• <u><a href="#">AASB 15 Revenue from Contracts with Customers</a></u></li> </ul>	<p>We will review management’s assessment of the impact of the new standards, determine whether, to the extent necessary, your entity has applied the standards correctly, and ensure the annual financial report complies with the revised requirements of each standard.</p>

Details of Risk / Issue	Audit Approach
<p>New requirements for recognising revenue i.e. when performance obligations are satisfied. Critical elements that need to be satisfied:</p> <ul style="list-style-type: none"> <li>- Agreement between parties must create 'enforceable' rights and obligations</li> <li>- Entity's promise to transfer goods or services needs to be 'sufficiently specific' to be able to determine when the obligation is satisfied.</li> </ul> <ul style="list-style-type: none"> <li>• <u>AASB 1058 Income of Not-for-Profit Entities</u> Applies to transactions of not-for-profit entities where the consideration to acquire an asset is significantly less than fair value principally to enable the entity to further its objectives. Whether income is recognised and its timing will depend on whether a transaction gives rise to a performance obligation, liability or contribution by owners. Transactions include those where an entity acquires or receives an asset in exchange for no consideration (i.e. cash grants, taxes and rates).</li> <li>• <u>AASB 16 Leases</u> For lessees the distinction between operating leases and finance leases has been removed and requires all leases (except short term leases and leases of low-value) to be recognised as lease assets and lease liabilities on the balance sheet. This will result in the grossing up of the balance sheet and higher expenses in the early years of the lease term. Lessor accounting remains similar to current practice (i.e. lessors continue to distinguish between operating leases and finance leases).</li> </ul>	
<p>Amendments to the following regulations due to COVID-19:</p> <ul style="list-style-type: none"> <li>• <i>Local Government (Financial Management) Regulations 1996</i></li> <li>• <i>Local Government (Functions and General) Regulations 1996</i></li> <li>• <i>Local Government (Long Service Leave) Regulations</i></li> </ul>	<p>On 9 April 2020 changes in local government regulations were made as practical assistance for local governments to respond during a state of emergency (Covid-19). These changes deal with flexibility in local government entities' access to funding, procurement and long services leave during the Covid-19 outbreak.</p> <p>We will assess management's implementation of the changes to regulations to confirm that no control weaknesses have occurred.</p>
<p>Non-current assets subject to valuation in the current year includes:</p> <ul style="list-style-type: none"> <li>• Land and buildings</li> </ul>	<p>We will review management's processes of determining the fair value of these assets and review the reasonableness of assumptions used.</p> <p>We will also review management's process of ensuring that the carrying value of asset classes not subject to revaluation in the current year do</p>

Details of Risk / Issue	Audit Approach
	not materially differ from their fair value in the financial statements.
New financial management systems that impact for the first time this year	No system changes have been identified at this stage.
<p>The following annual financial report items are derived from accounting estimates and hence will receive specific audit attention:</p> <ul style="list-style-type: none"> <li>• Provision for annual and long service leave</li> <li>• Allowance for impairment of trade receivables</li> <li>• Fair value of assets</li> <li>• Impairment of assets</li> <li>• Useful lives of assets</li> </ul>	<p>We will review the method and underlying data that management and where applicable third parties use when determining critical accounting estimates.</p> <p>This will include considering the reasonableness of assumptions and corroborating representations.</p>
Important changes in management or the control environment	We are not aware of any such changes at this stage.

## 5. Audit Emphasis and Significant Account Balances

Our audit approach involves assessing your overall control environment and understanding key business processes/cycles and internal controls relevant to the audit.

Our audit methodology provides for business cycle controls to be tested on a rotation basis over a period of three years.

The extent of our reliance on controls, together with the materiality level, determines the nature and extent of our audit procedures to verify individual account balances.

This year, we will test controls on the following business cycles:

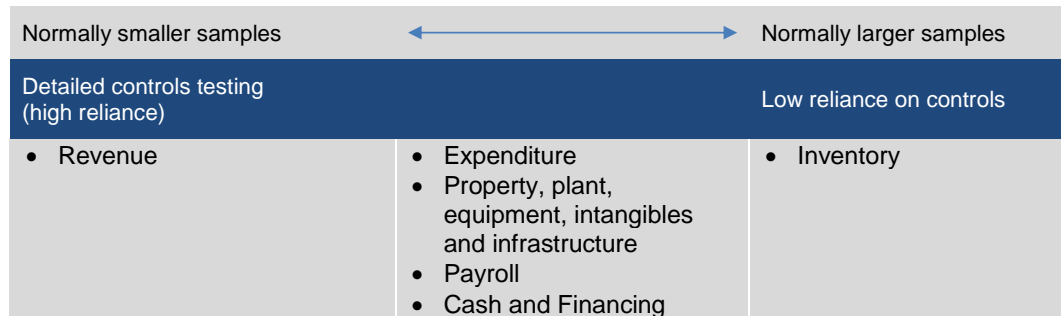
- Revenue

The controls for the following business cycles will be reconfirmed, as we understand that there have been no significant changes since they were last tested:

- Expenditure
- Property, plant, equipment, intangibles and infrastructure
- Payroll
- Cash and Financing
- Inventory

In addition, we will audit key information systems controls and perform a capability maturity assessment of your information system management processes and controls. This will be based on the assessment of our information system audit staff, but will also give consideration to a self assessment by your ICT staff.

The following diagram indicates the approach this year to auditing the material balances in your financial statements. As can be seen, we have determined that for some balances it is more efficient and/or effective for the audit to rely on the financial controls. For other balances, analytical review and sample testing of transactions is more appropriate.



Our audit will be split into two components, the interim audit and the final audit.

The interim audit includes:

- understanding your current business practices
- understanding the control environment and evaluating the design and implementation of key controls and, where appropriate, whether they are operating effectively
- testing transactions to confirm the accuracy and completeness of processing accounting transactions
- clarifying significant accounting issues before the annual financial report is prepared for audit.

The final audit focuses on verifying the annual financial report and associated notes, and includes:

- verifying material account balances using a combination of substantive analytical procedures, tests of details, substantiation to subsidiary records and confirmation with external parties
- reviewing the annual financial report and notes for compliance with the *Local Government Act 1995*, *Local Government (Financial Management) Regulations 1996* and Australian Accounting Standards.

The table below lists those items in the Statement of Financial Position and the Statement of Comprehensive Income that are significant account balances, and our planned audit approach for these balances. When selecting significant account balances, we consider materiality, the nature of the balance, inherent risk and the sensitivity of disclosures.



Significant Account	2019 Audited Balance \$000s	Audit Approach
<b>Statement of Financial Position</b>		
Cash and cash equivalents	20,738	<ul style="list-style-type: none"> <li>Review internal controls and reconciliations</li> <li>Verify year end balance through bank confirmations</li> <li>Analytical review</li> </ul>
Investments accounted for using the equity method	31,408	<ul style="list-style-type: none"> <li>Review the associated entity's audited financial report to confirm its total net assets at year end.</li> <li>Review the calculation of the City's share in the associated entity's total net assets.</li> </ul>
Receivables	3,885	<ul style="list-style-type: none"> <li>Year end cut-off testing</li> <li>Review subsequent receipts</li> <li>Review the calculation of the allowance for impaired receivables</li> <li>Analytical review</li> </ul>
Property, plant, equipment, intangibles, and infrastructure	521,881	<ul style="list-style-type: none"> <li>Review of key process and controls</li> <li>Verify asset additions and disposals</li> <li>Assess assets for impairment</li> <li>Test items posted to construction in progress to assess appropriateness of expenses being capitalised</li> <li>Assess whether carrying amounts approximate fair value</li> <li>Confirm balances to independent valuation reports</li> </ul>
Payables	6,302	<ul style="list-style-type: none"> <li>Review of key processes/controls</li> <li>Test for unrecorded liabilities</li> <li>Year end cut off testing</li> <li>Analytical review</li> </ul>
Borrowings	4,954	<ul style="list-style-type: none"> <li>Agree amounts to WATC confirmation</li> </ul>
Provisions	4,178	<ul style="list-style-type: none"> <li>Review the reasonableness of assumptions and calculations</li> <li>Agree amounts to actuary/expert's report</li> <li>Analytical review</li> </ul>
Leaseholder liability	--	<ul style="list-style-type: none"> <li>Review internal controls and reconciliations</li> <li>Review the reasonableness of assumptions and calculations</li> <li>Analytical review</li> </ul>
<b>Statement of Comprehensive Income</b>		
Rates revenue	37,436	<ul style="list-style-type: none"> <li>Review and assess the operating effectiveness of controls</li> <li>Analytical review</li> <li>Year end cut off testing</li> </ul>
Fees and charges	15,459	<ul style="list-style-type: none"> <li>Review and assess the operating effectiveness of</li> </ul>

Significant Account	2019 Audited Balance \$000s	Audit Approach
		controls <ul style="list-style-type: none"> <li>Analytical review</li> <li>Year end cut off testing</li> </ul>
Employee related expenses	25,254	<ul style="list-style-type: none"> <li>Review of key processes and controls</li> <li>Sample testing of transactions</li> <li>Analytical review</li> </ul>
Materials and contracts	20,391	<ul style="list-style-type: none"> <li>Review of key processes and controls</li> <li>Sample testing of transactions</li> </ul>
Depreciation and amortisation	10,987	<ul style="list-style-type: none"> <li>Review of management's assessment of the useful lives of assets and assess reasonableness.</li> <li>Analytical review</li> </ul>

## 6. Internal Audit

We seek to rely on internal audit work to reduce our own audit work wherever possible. This avoids duplication of audit effort and the associated workload on your operational and administrative staff.

This year, reliance is planned to be placed on internal audits relevant to the following areas:

Audit Topic
Developer Contribution Plans
Grants Management
General Financial Controls (excluding Procurement and Tendering)
ICT Governance
Risk Management
Procurement and Tendering
Review of Financial Controls as per LG Act

The amount of reliance we place on internal audit depends on the period covered by the internal audit work, and the degree of alignment between our planned controls testing and the testing carried out by internal audit. It is also dependent on the quality of the internal audit function.

## 7. Management Representation Letter

The above audit procedures assume that management expects to be in a position to sign a management representation letter. The proposed letter for this purpose is attached. This letter should be reviewed and tailored to meet your local government's particular circumstances, and be signed and dated by the CEO and Director Corporate Services as close as practicable to the date of the proposed auditor's report. Ordinarily, this would be no longer than five working days prior to the issue of the auditor's report.

We will also be relying on the signed Statement by CEO in the annual financial report as evidence that they confirm:

- they have fulfilled their responsibility for the preparation of the annual financial report in accordance with the *Local Government Act 1995*, *Local Government (Financial Management) Regulations 1996* and Australian Accounting Standards
- they have provided us with all relevant information necessary or requested for the purpose of the audit
- all transactions have been recorded and are reflected in the annual financial report.

## 8. Related Entities

Section 7.12AL of the *Local Government Act 1995* applies section 17 of the *Auditor General Act 2006* to a local government. Section 17 requires a local government to advise the Auditor General in writing of details of all related entities that are in existence.

## 9. Reporting Protocols

Significant issues identified during the course of the audit will be discussed with relevant staff and management as soon as possible after being identified. Draft management letters will be provided to your Director Corporate Services (or other nominated representative) for coordination of comments from appropriate members of your management. We request that these be returned quickly, preferably within 10 working days.

At the conclusion of the audit, the abovementioned management letter will accompany the auditor's report and the audited annual financial report forwarded to the Mayor, the CEO and the Minister for Local Government. The management letter is intended to communicate issues arising from the audit that may impact on internal control, compliance, and financial reporting.

Where considered appropriate, and to ensure timely reporting of audit findings and action by management, interim management letters may be issued to the CEO.

On conclusion of the audit we propose to discuss the audit outcomes with the audit committee, CEO and Councillors.

Thereafter, as required by section 7.12AD(2) of the *Local Government Amendment (Auditing) Act 2017* we will give our auditor's report to the CEO, the Mayor and Minister. We will also give them any management letter issues, including interim management letters.

Specific matters resulting from issues identified during the audit may be reported in an Auditor General's Report to Parliament. Should this occur, you will be consulted in advance to assure the context and facts of the issue are adequately represented.

## 10. Proposed Audit Schedule

	Date
Planning	April 2020
Information Systems Audit	July 2020
Interim Audit	18 – 29 May 2020
Final Audit	5 – 23 October 2020
Critical Target Dates	
Interim Management Letter	12 June 2020
Receipt of proforma Annual Financial Report	By 15 June

Final Trial Balance	30 September 2020
Receipt of Annual Financial Report	30 September 2020
Exit Meeting (week ending)	6 November 2020
Issue of Auditor's Report	13 November 2020

## 11. Audit Evidence – Specific Audit Requirements

We will discuss our requirements with your staff to facilitate a timely, efficient and effective audit. We will formally agree our information requirements and timeframes for the final audit with your Director Corporate Services using our Prepared by Client Listing. This Listing is intended to help your staff to have various documents readily available when we perform our audit. Please note however that in several instances, particularly during our audit sampling at the interim visits, audit staff will need to retrieve some evidence themselves, rather than being given the evidence by your staff. This is essential for an independent audit.

## 12. Audit Fee

Our indicative audit fee for this year's audit is \$40,000.

The indicative fee is based on full cost recovery. It is calculated from an estimate of the time required by our staff to complete your audit, and includes a proportion of the OAG's financial audit related overheads, for example the cost of preparing reports to Parliament.

We are constantly searching for ways to improve efficiency and reduce audit costs within the constraints of legislative requirements and auditing standards. However, your entity can also contribute to reducing the cost of your audit. A well prepared financial report, working papers, and internal audit programs that dovetail well with the work we are required to perform are some ways that costs can be contained.

Additional costs requiring a supplementary fee can arise from such things as significant accounting issues, errors in the financial report, breakdowns in internal controls, delays in providing information to audit staff, or your staff being unavailable to discuss issues with the audit team. Where circumstances arise that impact on our audit costs we may need to revise the indicative fee at the completion of the audit.

## 13. Your Audit Team

	Name	Contact
A/Assistant Auditor General	Patrick Arulsingham	6557 7644 <a href="mailto:Patrick.Arulsingham@audit.wa.gov.au">Patrick.Arulsingham@audit.wa.gov.au</a>
Assistant Director	Suraj Karki	6557 7551

	Name	Contact
		<a href="mailto:Suraj.Karki@audit.wa.gov.au">Suraj.Karki@audit.wa.gov.au</a>
Team Leader	Vignesh Raj	6557 7605 <a href="mailto:Vignesh.Raj@audit.wa.gov.au">Vignesh.Raj@audit.wa.gov.au</a>
Other Audit Staff	Main Bhuiyan Kevin Sathasivam Nikkita Day	<a href="mailto:Main.Bhuiyan@audit.wa.gov.au">Main.Bhuiyan@audit.wa.gov.au</a> <a href="mailto:Kevin.Sathasivam@audit.wa.gov.au">Kevin.Sathasivam@audit.wa.gov.au</a> <a href="mailto:Nikkita.Day@audit.wa.gov.au">Nikkita.Day@audit.wa.gov.au</a>
Information Systems Audit Consultant	Kamran Aslam	6557 7582 <a href="mailto:Kamran.Aslam@audit.wa.gov.au">Kamran.Aslam@audit.wa.gov.au</a>
Assistant Auditor General	Don Cunninghame	6557 7526

Patrick Arulsingham is responsible for the overall quality of the audit. As your primary contact, Patrick will communicate progress and any emerging issues to you.

## 14. Other Audit Activities

The OAG has recently tabled the following reports in Parliament. These are available at [www.audit.wa.gov.au](http://www.audit.wa.gov.au) along with details of other audits we are currently performing. In reporting, we aim to identify good practice and opportunities for improvement. You may therefore wish to review these reports as they may have relevance to your local government.

Report	Date Tabled
Local Government Contract Extensions and Variations	4 May 2020
Audit Results Report – Annual 2018-19 Financial Audits of Local Government Entities	11 March 2020
Audit Results Report – Annual 2018-19 Financial Audits of State Government Entities	14 November 2019
Fraud Prevention in Local Government	15 August 2019
Verifying Employee Identity and Credentials	19 June 2019
Information Systems Audit Report	15 May 2019
Audit Results Report – Annual 2017-18 Financial Audits of Local Government Entities	7 March 2019