

Report to the Council on the audit of

Wellington City Council

for the year ended 30 June 2010

Management report

Audit New Zealand has carried out this audit on behalf of the Controller and Auditor-General.

We are responsible for expressing an independent opinion on the financial statements and service performance information and reporting that opinion to you. This responsibility arises from section 15 of the Public Audit Act 2001.

Our audit has been carried out in accordance with the Auditor-General's auditing standards. The audit cannot and should not be relied upon to detect every instance of misstatement, fraud, irregularity, or inefficiency that is not material to your financial statements.

Implementing and maintaining systems of internal control for detecting these matters remains the responsibility of the Council and management.

Statement of auditor independence

We confirm that, for the audit of Wellington City Council's financial statements for the year ended 30 June 2010, we have maintained our independence in accordance with the requirements of the Auditor-General, which incorporate the independence requirements of the Institute of Chartered Accountants of New Zealand.

Other than the audit and a review of the Clifton Terrace Carpark managed by the City Council on behalf of the New Zealand Transport Agency, we have not provided any engagements for the Wellington City Council during the year ended 30 June 2010. In addition, we have no relationships with, or interests in, the Wellington City Council or any of its subsidiaries.

Unresolved disagreements

We have no unresolved disagreements with management about matters that individually or in aggregate could be significant to the financial statements. Management has not sought to influence our views on matters relevant to our audit opinion.

Other relationships

We are not aware of any situations where a spouse or close relative of a staff member involved in the audit occupies a position with the Wellington City Council that is significant to the audit.

We are not aware of any situations where a staff member of Audit New Zealand has accepted a position of employment with the Wellington City Council during or since the end of the financial year.

Report to the Council

from the audit for the year ended 30 June 2010.

We have completed the audit for the year ended 30 June 2010. This report sets out our findings from the audit and draws attention to areas where Wellington City Council (the Council) is performing well and other areas where we make recommendations for improvement.

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Key messages

Key issues considered during the audit were:

An unqualified opinion was issued – This means that we were satisfied that the financial statements and statement of service performance fairly reflected the Council's activity for the year and its financial position at the end of the year.

The Council has accounted appropriately for its leaky homes obligations – Council has updated its provision for costs associated with non-weather tight homes. We agree with the changes Council has made to its provision. The Council continues to identify an additional contingent liability in respect of potential claims which may arise in the future.

We commend management's focus on, and commitment to, continuous improvement in service performance reporting – We are satisfied that the service performance statements comply with generally accepted accounting practice and fairly reflected the actual achievements and performance of the Council.

The Council's procurement policies have been prepared to a very high standard – The Council's procurement documentation addresses all the key areas of the Procurement Policy Standards expected.

Thank you

We would like to thank the Council and management for their co-operation and assistance during the course of the audit. As in previous years, the audit was completed within two months of balance date. Documentation to support the audit continues to be to a high standard.

Section A: Significant risks and issues

Our planned audit approach, following discussions with management and the Audit and Risk Management Subcommittee (ARMS), identified the following risks to be considered during the audit. These issues are discussed in this section of the report:

- Weather tight homes provision and contingent liability.
- Property, plant and equipment – Infrastructure assets revaluation.
- Service provision reporting.
- Policies for funding arrangements and procurement.
- Facilities Maintenance Aggregation Project Review.
- Financial Information System (FMIS) Upgrade.
- Annual leave management.

1 Our audit opinion

1.1 We issued an unqualified audit opinion

We issued an unqualified audit opinion on 25 August 2010. This means that we were satisfied that the financial statements and statement of service performance fairly reflected the Council's activity for the year and its financial position at the end of the year.

In forming our audit opinion, we considered the following matters.

1.2 Unadjusted misstatements

The financial statements are free from material misstatements, including omissions.

1.3 Management control environment

The management control environment is determined by the attitude, awareness and actions of the governing body, management and others, who have the ability to influence the reliability of control systems concerning the importance of internal controls.

The control environment encompasses the entity's control culture and values, organisation and governance structures and its commitment to designing and maintaining reliable accountability systems. It also includes its attitude and approach to planning,

budgeting, performance monitoring and compliance with legislative requirements. These translate into internal control procedures that are established to provide reasonable assurance that entity objectives will be achieved. The internal controls build into the following processes:

- governance structures and mechanisms;
- risk management;
- financial planning, budgeting, reporting and monitoring;
- operational financial controls; and
- quality assurance procedures.

The stronger the management control environment, the greater the likelihood that these processes at different levels within the organisation will operate as designed and that organisations' objectives will be achieved.

We found that, consistent with previous years, the Council continues to operate a sound management control environment and there are effective financial management processes in place. We have identified the following as some of the key aspects of the management control environment:

- The Council and management have demonstrated a commitment to appropriate management control systems being in place and operating effectively. This includes both the maintenance of essential transactional recording systems as well as detailed financial analysis and management reporting throughout relevant levels of the Council.
- Budgeting and monitoring of financial performance is very effective due to the systems and processes in place. A key aspect of this is the role of the business analysts in budgeting and monitoring processes.
- An experienced executive team which displays a consistent level of commitment to maintaining a strong control environment.
- The Council's governance structures provide a clear division of responsibilities between the Council and management.
- There is an effective risk assurance (internal audit) function operating within the Council.
- There is an active and effective Audit and Risk Management Subcommittee, which brings a high level of scrutiny to organisational risk and general management issues.

2 Business risks/issues

During the planning stage of the audit, we identified the key business risks and issues, and documented these in the Planned Audit Approach. In this section of the report, we comment on our findings on those matters.

2.1 Weather tightness provision and contingent liability

Exposure to liabilities from leaky home claims remains a significant issue for the local government sector. Early in 2007 there was sensitive publicity surrounding this issue with significant media coverage of the judgment in the *Dicks v Hobson Swan Construction Limited (in liquidation)* (2006) 7 NZCPR 881 case.

In previous years we recommended that the Council consider providing for future legal costs as part of the weather tightness provision.

The Council included legal cost in the provision this year. This has had an impact on the Council's surplus as the extra provision was unbudgeted. We reviewed the methodology behind the calculation of the Council's provision and are satisfied that it complies with appropriate accounting standards.

This provision is based on an estimate of expected liability in relation to known claims made against the Council. This includes claims reported to the Weathertight Homes Resolution Service (WHRS) and passed to the Council for settlement, and claims currently with the WHRS as well as claims made through civil proceedings.

The Council continues to identify an additional contingent liability in respect of potential claims which may arise in the future. Given the continuing uncertainties around future costs of WHRS claims, including the likely implications of the Government proposal announced in May 2010, the Council does not have sufficient information to reliably quantify that contingent liability at this time.

2.2 Property, plant and equipment – Infrastructure assets revaluation

The Council has a three-yearly revaluation cycle. The relevant accounting standard (NZ IAS-16) requires that when the fair value of a revalued asset differs materially from its carrying amount, a further revaluation is required in that year.

The Council engaged with a valuer to perform an independent assessment of the fair value movement of infrastructure assets. Based on this assessment, and management's assessment of materiality no revaluation of infrastructural assets was undertaken this year.

We reviewed the assessment and are satisfied that a revaluation of infrastructure assets was not required this year.

2.3 Service performance reporting

We audited the reported service performance information in the Annual Report.

We focused on:

- the quality of the overall "story" the performance reporting tells;
- the reliability and accuracy of the reporting;
- the completeness of the reporting against the performance framework as outlined in the LTCCP; and
- compliance with relevant legislation (in particular the Local Government Act 2002, Schedule 10).

When we performed the audit of Council's 2009-19 LTCCP we concluded that the performance framework provides an appropriate basis for the meaningful assessment of its actual performance reporting. We have updated our assessment to take into account any changes in Council's business and activities since the LTCCP was adopted.

Our assessment involved a review of the management control environment (MCE) with respect to service performance information. We have assessed the MCE as effective for the following reasons:

- Council has been pro-active in improving its service performance reporting. Staff recognise the importance of, and are committed to improving service performance reporting. Council has actively involved itself in this work across the organisation.
- Our audit work and discussions with the various business units highlighted that Council staff generally had an appropriate understanding of the LTCCP performance framework, and awareness of the performance measures and how they contribute to Council's performance.
- We reassessed the appropriateness of the Council's performance framework as part of this year's audit. From our audit work, we assessed that for the significant performance measures tested, the performance measures did drive the Council's business, contribute to and fairly measure Council's performance.
- Performance is monitored and managed by the senior management team throughout the year.

- Clear accountabilities are in place for non-financial performance (from Council to Chief Executive Officer to Directors and to Business Unit Managers).
- Proactive attitude that was evident from discussions with the Chief Executive Officer (CEO) and all Directors to ensure that:
 - systems are in place to enable the Council to collect and report information; and
 - Council look to improve the performance framework, and systems, in the future.

We are satisfied that Council's performance framework continues to provide an appropriate basis on which to assess Council's performance.

We are satisfied that the service performance statements comply with generally accepted accounting practice and fairly reflected the actual achievements and performance of the Council.

Management comment

We thank Audit New Zealand for their comments.

2.4 Policies for funding arrangements and procurement

The Council has compared its policies for funding arrangements and procurement against guidance published by the Auditor-General.

We reviewed the Council's procurement documentation, which addressed all the key areas of the Procurement Policy Standards expected. There was extensive coverage of the key procurement areas of:

- status and availability;
- general provisions, obligations and approach;
- legal considerations;
- ethical provisions;
- economic considerations;
- sustainability;
- risk management;
- procurement planning and methods; and
- procurement processes and management.

We found that the set of procurement documentation provided was to a very high standard and is reflective of modern, public sector procurement standards.

Management comment

We thank Audit New Zealand for their comments.

2.5 Facilities Maintenance Aggregation Project

The Council let a significant Facilities Maintenance Aggregation contract in 2008.

Given the scale of that Project, and the potential to learn from its implementation, the Council is to be commended for commissioning a post-implementation review of its performance in letting the contract.

We have reviewed that post implementation review report, which we found to be robust. The review identified some important lessons to be learned for the management of future significant project management processes.

The review report has been considered by the Management Board and the Council's Project Management Office.

These matters have been picked up by the establishment of a dedicated project management office as a centre of excellence – which has been resourced to undertake such projects in future; and its work in establishing and

strengthening project management skills, experience, capability and project management processes and standards.

Management comment

We thank Audit New Zealand for their comments.

2.6 Financial Information System (FMIS) upgrade

Our review of the Council's Financial Management Information System (FMIS) upgrade confirmed that the FMIS project implementation was successful and has complied with good practice.

Our review involved:

- Engaging with the FMIS upgrade team to determine whether each stage of the upgrade was managed appropriately.
- Determining whether sufficient controls had been implemented by the project team, to ensure that the integrity of the information migrated from the old version of the FMIS was maintained.

Management comment

We thank Audit New Zealand for their comments.

2.7 Annual leave management

The Council has been increasing its focus in recent years on the management of staff with high annual leave balances. In 2008 we recommended that the Council put in place leave plans with employees to reduce annual leave balances to a manageable level, acknowledging at that time that Council had been considering a range of options to reduce its employee leave liability. Systems changes introduced included:

- Monthly report to the CEO on the shape and nature of the leave liability;
- Monthly reporting to Human Resource Consultants (HRCs);
- The top five employees by annual leave liability to be reported to the directors in the three-monthly HR report; and
- Framework put in place requiring business units to put leave plans in place for individuals with high balances.

In 2009 we noted that the Council had started to proactively look at annual leave balances at the business unit level. The Council had incorporated a dashboard system which lists each business unit manager and the total leave balances for all staff members under their responsibility.

We reviewed the number of employees with over 30 days leave owing. We were pleased to note that at 30 June 2010 the number of people with more than 30 days leave owing had fallen to 70 from 83 last year.

We believe that 70 people is a large number of employees with more than 30 days leave owing and we recommend the Council monitor this closely, and manage the number of people with high balances down.

Management comment

We continue to work across the organisation to reduce our leave liability and have made progress on this in 2009/10 as noted by Audit New Zealand. This is a key focus within the Council.

Section B: Other matters

Every year, we identify common sector wide matters that are considered as part of the audits of all Local Authorities. Our findings on these sector matters, other than those already covered earlier in this report, are discussed in this section.

We have provided management with a supplementary report that discusses our findings and recommendations about less significant and miscellaneous matters.

The status of each matter that was outstanding in last year's report to the Council is included in Appendix 1.

3 Sector matters

We completed reviews on our areas of interest across all Local Authorities. Most of our findings have been incorporated in the relevant sections of this report. Our comments on the issues not already addressed elsewhere are as follows:

3.1 Elections

The next election is scheduled for 9 October 2010. The Single Transferable Voting (STV) electoral system will be used for the 2010 elections.

We reviewed the content of Annual Report to ensure the content did not contain information that could be seen as electioneering.

During our audit, we did not find any indication of electioneering.

3.2 Elected members – remuneration and allowances

We reviewed the Council's compliance with the requirement to disclose the remuneration of each member of the local authority in the annual report against the Local Government Elected Members Determination.

The Council comply with the requirements appropriately.

3.3 LTCCP amendments

We remained alert for possible amendments throughout the year, particularly during the preparation of the annual plan.

No amendments to the LTCCP were identified.

3.4 New Zealand Transport Agency (NZTA) funding

The national land transport programme (NLTP) has been released for the three years beginning 1 July 2009. As a result the Council received less funding than anticipated and budgeted for in the 2009-19 Long Term Community Plan (LTCCP). The Council have made adjustments to budgets accordingly.

This year's NZTA funding decrease is not significant for the Council and no amendment to the LTCCP was required.

3.5 Emissions Trading Scheme

The Local Government Act requires Local Authorities to take a sustainable development approach to mitigate the effects of their activities on economic, social, environmental and cultural wellbeing. We have been asked by the OAG to gather information about the activities of local authorities in the area of emissions measurement and reduction to obtain baseline information for 2009/10.

We did not identify any issues of concern in relation to the Emissions Trading Scheme.

3.6 Development contributions

We assessed the process for setting development contributions and reviewed the collectability of unpaid development contributions. We enquired as to claims or potential claims that may indicate that development contributions could be challenged.

We did not identify any significant issue in relation to development contributions during our audit.

3.7 The Council's fraud policy and assessment of areas susceptible to fraud

We checked to see that the Council has recently (within the last year) undertaken a robust review of transactions, activities or locations that may be susceptible to fraud.

The Council has an appropriate fraud policy. Risk Assurance has a continuous auditing programme that examines sensitive and fraud risk areas including, discretionary expenditure, accounts payable and payroll systems transactions for control effectiveness and/or fraud, waste and abuse.

Risk Assurance reported against its continuous audit programme as part of its reporting to the Audit and Risk Management Sub-committee.

Risk Assurance reported that none of the issues investigated or arising from the continuous controls testing programme have given concern regarding significant or systematic breakdown in controls.

3.8 Transparency, Accountability and Financial Management (TAFM)

No changes were made to the Local Government Act 2002 (LGA) by the time of the annual report adoption. Therefore no changes were required to the Council's annual report.

We will continue to maintain an awareness of the proposed content and progress of the TAFM reforms, in particular focussing on any proposed amendments to the LGA that impact on disclosures and audit requirements for the 2009/10 year.

3.9 Council governance role in completion of Council Controlled Organisation (CCO) SOIs

We considered whether the Council has appropriate arrangements in place for effectively fulfilling their oversight responsibilities relating to CCOs.

The Council has a dedicated CCO unit which manage the relations with all Councils and Council's CCOs.

The Council has a relationship manager assigned to each of the CCOs with clear accountabilities and reporting requirements. These managers work closely with the relevant business unit managers of Council.

The CCO unit is responsible for the collection and collation of the CCO information which forms the annual report. This information is provided to Strategy Performance and reporting (SPP) team for inclusion in the annual report.

We are satisfied that the Council has appropriate arrangements in place for effectively fulfilling their oversight responsibilities relating to CCOs.

3.10 Treaty settlements and co-management

We are not aware of any new Treaty of Waitangi settlements or co-management arrangements or developments with existing agreements.

3.11 Severance payments

We reviewed the Council severance payments that occurred during the year against schedule 10 of the Local Government Act 2002 with a focus on settlements which could be seen to be excessive or unusual.

We confirmed the payments against the annual report. No issues arose from our review.

3.12 Audit Committees – Audit Risk Management Subcommittee (ARMS)

ARMS members were asked to complete an audit committee effectiveness evaluation checklist in order to review the Sub-committee's effectiveness.

The answers and comments indicate that current ARMS processes and practice are in line with the principles and good practices set out in the OAG Guidelines. The following areas of improvement were identified:

- Consider the approach for the appointment of external members to the ARMS to ensure that the composition of the audit committee is conducive to maintaining continuity and ensuring a fresh perspective.
- Review the induction programme provided for new and existing committee members to ensure it covers the role of the audit committee, expected time commitment and overview of the organisation.
- Review the ARMS terms of reference (Charter) annually. Any changes must be approved by Council.

- Include in the ARMS forward programme an annual review of the Whistleblower function and the effectiveness of the Council ethics and values programmes.
- Establish an independent review/validation of the activities of the internal audit function in 2010, and every five years in line with best practice.
- Review the ARMS forward programme to ensure alignment with its terms of reference.
- Provide the audit committee with the internal audit charter.

ARMS decided to re-visit the implementation of these recommendations after the elections. In our view ARMS should also consider:

- Its role in reviewing the integrity of non-financial performance information.
- Reviews the effectiveness of the external audit process and performance.

Management comment

Recommendations agreed. The areas identified for improvement have been progressed for implementation at the start of the new Triennium.

3.13 Sensitive expenditure

We selected a sample of transactions from areas of sensitive expenditure incurred during the year and reviewed them for compliance with the Council's practices and accepted good practice in the public sector.

We identified some instances where more guidance is required to explain the Council's policies, to assist in ensuring that they are consistently applied.

We have raised the specifics of these findings with the management, and discussed opportunities to further develop guidance in this area.

Management comment

Recommendation agreed. Sensitive expenditure policies are currently under review to ensure they are consistently understood and applied across Council.

3.14 Conflicts of interest

We remained alert for conflicts of interest in the course of our audit work.

We are aware that Risk and Assurance plans to implement a "senior management – conflict of interest policy" and an annual declaration. We see this as a proactive step in managing conflicts of interest.

No conflict of interest issues were identified during the audit.

4 Details of reviews on behalf of the Auditor-General

We completed the reviews required by the Auditor-General, as set out in our Planned Audit Approach, and cleared them with appropriate members of your management team. Appendix 2 sets out the results of the reviews where not covered in the main body of this report.

Appendices

Appendix 1: Status of recommendations made in prior years

Appendix 2: Details of reviews on behalf of the Auditor-General

Appendix 1: Status of recommendations made in prior years

Outstanding matters

Matter	Recommendation	Outcome and status
Information Systems		
<p>Council does not have one overarching IS/IT Security Policy. This potentially allows unauthorised access to systems and/or fraudulent, malicious or unintended transactions to be posted.</p> <p>Council's Knowledge Solutions (KS) organisation is not aware of the extent of end-user applications and does not have controls in place to manage end-user computing.</p> <p>The risk around end-user computing applications (such as Excel spreadsheets and Access databases) is that they might be used for key business processes, and/or business decisions and/or reporting without (at the same time) being subject to the same level of controls as business key systems.</p>	<p>Develop and implement an IS/IT Security Policy as an overall statement of the importance of security to the organisation.</p> <p>Develop and implement a policy for end-user computing as a basis for controlling the employment of end-user application.</p>	<p>In progress.</p> <p>We are aware that the Council have recently recruited a Security Architect whose primary role is to write a security policy framework and thereafter obtain IT acceptance and ongoing implementation and adherence.</p> <p>We will continue to follow the Council's progress on this issue.</p> <p>Management comment</p> <p><i>While we do not have an overarching security policy we do follow recommended best practice for security on all our systems, including Peoplesoft.</i></p>

Appendix 2: Details of reviews on behalf of the Auditor-General

Issue	Status/findings
Annual Report Adoption and Public Release Dates	<p>We have been asked to note the dates that the Council adopts its annual report, and makes the full and summary annual reports available to the public. This information will be forwarded to the Office of the Auditor-General (OAG).</p> <p>We will submit this information to the OAG once Council release the Annual Report and Summary Annual Report to the public.</p>
Local Authority Exemptions for Council Controlled Organisations (CCOs)	<p>We have been asked to advise the OAG on Council's use of Section 7 of the Local Government Act 2002. Under section 7 of the LGA 2002, a local authority may exempt a "small" CCO from the accountability regime that applies to CCOs under that Act.</p> <p>At Council's meeting of 29 August 2007, Council exempted the Hutt Minoh House Friendship Trust, and the Joe Aspell Trust for a period of three years to 30 June 2010.</p>
Local Authorities emissions and measurement and reduction	<p>We have been asked by the OAG to gather information about the activities of local authorities in the area of emissions measurement and reduction with a view to obtaining baseline information for 2009-10.</p> <p>We found that the Council has a system in place for measuring the Council's emissions information as well as a 2010 Climate Change Action Plan (CCAP) with the aim to reduce emissions.</p>