

# AUDIT AND RISK MANAGEMENT SUBCOMMITTEE

18 June 2012



**REPORT 4**  
(12 15/52/01/IM)

## DRAFT 2011/12 FINANCIAL STATEMENTS, DRAFT FINANCIAL OVERVIEW AND PROPOSED SIGN OFF PROCESS

### 1. Purpose of report

The purpose of this report is to obtain the agreement of the Subcommittee as to the proposed format and disclosures for the Council's 2011/12 financial statements, the format of the financial overview and the associated sign-off process for those financial statements.

### 2. Recommendations

Officers recommend that the Audit and Risk Management Subcommittee:

1. *Receive the information.*
2. *Note that the 2011/12 financial statements template has recently been reviewed by Audit New Zealand and that their comments/recommendations have been reflected in the template.*
3. *Note that all new standards, amendments and interpretations which are applicable for the 2011/12 financial statements have been considered by officers (refer Appendix 1) and notes that we are not planning to early adopt any new standards, amendments and interpretations.*
4. *Approve the proposed format and disclosures for the 2011/12 financial statements subject to:*
  - (a) *consideration of the implications of any changes in NZ GAAP arising up to 30 June 2012 which may be required to be applied retrospectively;*
  - (b) *the determination and disclosure of the final results of operations, cashflows and financial position for the year ending 30 June 2012 (and any subsequent impact on the notes to the financial statements); and*
  - (c) *receiving final clearance from Audit New Zealand.*
5. *Approve the sign-off process and timetable for the 2010/12 financial statements (refer Appendix 2).*
6. *Approve the proposed format of the financial overview template for the 2011/12 financial year (refer Appendix 4).*

### **3. Background**

Section 98 of the LGA 2002 requires the Council to prepare and adopt an Annual Report containing specified disclosures within four months after the end of the financial year. Section 111 of the LGA 2002 requires Council to comply with generally accepted accounting practice (GAAP) in preparing the Annual Report.

Council officers propose to prepare the 2011/12 Annual Report for adoption on 29 August 2012. In order to achieve this timeframe, a draft template has been prepared for the Subcommittee's review which identifies the proposed financial statement format and disclosures. This report also outlines the proposed sign-off process and timetable for the adoption of the 2011/12 Annual Report.

The template for the financial statements has recently been reviewed by Audit New Zealand as part of their financial statements audit for the year ending 30 June 2012 and their comments/recommendations have been incorporated.

### **4. Significant changes in the content and format of the Council's financial statements**

#### **4.1 Process**

The template has been drafted by the Council's Financial Accounting team. We are mindful of the need to modify the presentation of the financial statements to maintain best practice. A process of review was undertaken looking at recently published annual reports prepared in accordance with NZ IFRS and other relevant material (NZ IFRS models, NZ IFRS updates and pending changes to NZ IFRS). In addition, we will also review the presentation and content of the annual report summary.

Throughout the year we consider amendments made to NZ IFRS and update the Subcommittee with any implications for the Council. A full listing of all new standards, amendments and interpretations which are applicable for the 2011/12 financial statements are shown in Appendix 1. Where the adoption of these new or revised standards is mandatory for the 2011/12 financial statements, any required changes have been included in the template. The Council is not proposing to early adopt any standards, amendments or interpretations.

It is important to note that the template reflects applicable NZ IFRS as at the date of preparation. If necessary, it will be updated to reflect ongoing amendments to NZ IFRS between the date of preparation and the date of the next Subcommittee meeting.

#### **4.2 Key changes in the financial statements template**

Key changes to the draft financial statements template (Appendix 3) are shown in shaded grey. The key changes to the financial statements include:

- No significant changes in accounting standards or new standards introduced.
- Accounting policy for carbon credits

During the year the Council changed its accounting policy regarding the recognition of carbon credits. Carbon credits are now recognised at cost rather than at fair value at the date of allocation. While there is no accounting standard specifically relating to carbon credits this is the most common treatment of carbon credits within the European ETS and the Council believes it is a more appropriate method of recognising the revenue from our free allocation of credits from the Government.

- Local Government Funding Authority (LGFA)

The NZ Local Government Funding Agency, which commenced in December 2011 is the new alternative debt provider majority owned by and operated for local authorities. The Council is an establishment shareholder and has invested two million dollars in paid up capital. As a shareholder and borrower the Council will benefit from lower borrowing costs and a return on its investment.

Each of the local authority shareholders of the LGFA is a party to a deed of guarantee, whereby the parties to the deed guarantee the obligations of the LGFA and the guarantee obligations of other participating local authorities to the LGFA, in the event of default. In such event, each guarantor would be liable to pay a proportion of the amount owing.

The relevant disclosures have been included in the financial statements in notes: 13, 37 and 42).

- Continuing focus on “plain English”

Throughout the whole Annual Report process our focus will be on “plain English” financial reporting as we continue to strive to make the financial statements as readable and understandable as possible for our residents while still meeting the compliance requirements of NZ GAAP and the Local Government Act.

## **5. Significant Areas of Focus for the Financial Statements for the year ending 30 June 2012**

Significant areas of focus identified to date as part of the preparation of the financial statements for the year ended 30 June 2012 are as follows:

- Reassessment of fair values / impairment testing

The Council conducts revaluations of certain classes of property, plant and equipment on a rolling three year cycle. Revaluations are staggered over the three year period to spread the cost and workload involved. We are required to review the off-cycle classes to ensure that the carrying value of these assets is not materially different from fair value.

Operational land and buildings are due to be revalued as at 30 June 2012 and the results of the revaluation will be presented to the subcommittee in August. Of the other classes subject to the revaluation model, libraries and infrastructural assets were last revalued at 30 June 2011.

We reviewed the off-cycle classes of property, plant and equipment, applying appropriate indices. The increase in asset value of 2.7% was not considered material and accordingly we concluded that there is no indication that fair values have shifted materially since the last valuations were completed which would necessitate an off-cycle revaluation. This conclusion has been accepted by Audit New Zealand.

- Investment property revaluation

Investment properties comprise ground leases as well as land and buildings held for investment purposes (commercial rental or capital growth). In accordance with NZ IAS 40: Investment Property, these are revalued annually to market value and all changes in fair value are shown within the surplus or deficit. All investment properties (including those in the Wellington Waterfront Project), will be revalued as at 30 June 2012.

- Impairment of Assets

The Council is required to regularly consider impairment in accordance with NZ IAS 36: Impairment of Assets. Given the difficult economic climate over the last few years and its potential impact on asset values, this remains a particular area of focus for 2011/12. We are looking closely at all of our assets to ensure that we have appropriately reflected any impairment issues. At the next Subcommittee meeting we will provide further information on the overall impairment for the 2011/12 financial year.

- Weathertightness (leaky homes) provision

Exposure to liabilities from leaky home claims remains a significant issue for both the Council and wider sector. The new Financial Assistance Package (FAP) was made available during the current financial year (from 29 July 2011). The Council is in the process of reviewing the assessment of the leaky homes provision.

## **6. Financial Overview**

The draft template for the Financial Overview is included in Appendix 4. By necessity the template for the financial overview requires figures to be included for the 2011/12 year. The 2011/12 figures are not yet available. The 2011/12 figures shown in the financial overview are a repeat of the figures from 2010/11.

The significant changes to the financial overview from 2010/11 are:

- References have been added to direct readers to the main body of the financial statements where they can find more information.
- Trends graphs now show the current year and four years of comparative information
- The 2010/11 financial overview used two separate graphs to show the percentage of rates collected from residential and commercial ratepayers and another to show the proportion of rateable value of residential and commercial ratepayers. In the 2011/12 financial overview these two graphs are combined in to one graph to more directly show the relationship.

## **7. Year-End Financial Results**

This report has focused on the template for the year-end financial statements, the disclosures and financial overview. Any significant movements from budgeted results or issues arising will be reported to the Subcommittee during the scheduled year end meeting on 22 August 2012.

## **8. Proposed Sign-Off Process for the 2011/12 Financial Statements**

On the basis that the Subcommittee has been delegated the primary responsibility for the audit of the Council's financial statements, a proposed sign-off process and timetable has been developed in order to adopt the 2011/12 Annual Report. This is outlined in Appendix 2 to this report.

## **9. Conclusion**

Section 98 of the Local Government Act 2002 requires the Council to prepare and adopt an Annual Report that includes audited financial statements. The Act requires that the financial statements be prepared in accordance with NZ GAAP.

The attached financial statements template and overview template have been prepared for the Subcommittee's review and approval, as part of the overall sign-off process for the 2011/12 Annual Report.

Accordingly, it is recommended that the Subcommittee approve the reporting template for use in preparing the final consolidated financial statements and financial overview.

In addition, it is recommended that the Subcommittee approves the proposed sign-off process and timetable as detailed in Appendix 2.

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## SUPPORTING INFORMATION

### 1) Strategic fit / Strategic outcome

This project supports strategic area of focus 1: Governance: As per the Annual Plan, Governance includes all those activities that make the Council accountable to the people of Wellington and ensure the smooth running of the city. That includes all meetings of the Council and its committees.

### 2) LTP/Annual Plan reference and long term financial impact

Relates to C534: Committee and Council process.

### 3) Treaty of Waitangi considerations

There are no specific Treaty of Waitangi considerations.

### 4) Decision-making

There are no significant decisions required by the paper.

### 5) Consultation

#### a) General consultation

Not required.

#### b) Consultation with Maori

Not required.

### 6) Legal implications

This report has no specific legal implications.

### 7) Consistency with existing policy

This report is consistent with existing policy.

## Appendix 1: New standards, amendments and interpretations applicable for the 2011/12 financial statements

| <b>Standard with amendment / New standard</b> | <b>Application date</b>       | <b>Nature of amendment</b>   | <b>Impact for the Council</b>  |
|---|-------------------------------|--|--|
| Various                                       | 1 July 2010 or 1 January 2011 | Annual improvements process – 2010   | Various minor amendments and clarifications. The Council does not anticipate a significant impact on its financial statements.       |
| NZ IAS 24                                     | 1 January 2011                | Related Parties (Revised 2009)   | Removes some inconsistencies with the definition of a related party and requires the disclosure of commitments with related parties. |
| NZ IFRIC 14                                   | 1 January 2011                | Amendments to IFRIC 14 Prepayments of a Minimum Funding Requirement          | We note that this is not relevant to the Council as we do not have a defined benefit plan.   |
| NZ IAS 26                                     | 1 April 2011                  | Amendments to NZ IAS 26 Accounting and Reporting by Retirement Benefit Plans | The Council does not anticipate any significant impact on its financial statements.  |
| FRS 44  | 1 July 2011                   | New Zealand Additional Disclosures   | The Council does not anticipate any significant impact on its financial statements.  |
| NZ IFRS 7                                     | 1 July 2011                   | Amendments to NZ IFRS 7 Financial Instruments: Disclosures                   | The Council does not anticipate any significant impact on its financial statements.  |
| Various                                       | 1 July 2011                   | Harmonisation Amendments (with Australia)                                    | The Council does not anticipate any significant impact on its financial statements.  |

|                  |                |   |  |
|------------------|----------------|---|--|
| NZ IFRS 1        | 1 July 2011    | Amendments to NZ IFRS 1 First-time Adoption of New Zealand Equivalents to International Financial Reporting Standards | The Council does not anticipate any significant impact on its financial statements.  |
| NZ IAS 12        | 1 January 2012 | Deferred Tax: Recovery of Underlying Assets   | The Council does not anticipate any significant impact on its financial statements.  |
| NZ IFRS 9 (2009) | 1 January 2013 | NZ IFRS 9: Financial Instruments  | Will affect the categories under which financial assets are classified, but will have no impact on the values currently reported in the Annual Report. |
| NZ IFRS 9 (2010) | 1 January 2015 | Amendments to IFRS 9: Fair Value Option for Financial Liabilities   | The Council does not anticipate any significant impact on its financial statements.  |

NOTE: This list does not include any new standards or interpretations that are not applicable to PBEs.

## Appendix 2: Proposed sign off process and timetable for the 2011/12 Annual Report

| <b>Date:</b>                           | <b>Action:</b>   |
|--|--|
| <b>18 June 2012<br/>(scheduled)</b>    | <i>Audit and Risk Management Subcommittee Meeting</i><br>Subcommittee to review and conditionally approve draft format for the 2011/12 financial statements, the format for the 2011/12 financial overview and the proposed sign-off process.  |
| <b>30 July 2012</b>                    | Audit New Zealand commence final audit fieldwork   |
| <b>1 August 2012</b>                   | Consolidated draft financial statements, including results of operations and cashflows for the year ending 30 June 2012, financial position as at 30 June 2012 and financial overview available for final internal review and management sign off.   |
| <b>August 2012<br/>To be scheduled</b> | Audit and Risk Management Subcommittee briefing on major provisions and issues.  |
| <b>22 August 2012<br/>(scheduled)</b>  | <i>Audit and Risk Management Subcommittee Meeting</i><br>Subcommittee to review consolidated draft financial statements, including results of operations and cashflows for the year ending 30 June 2012, financial position as at 30 June 2012 and financial overview, subject to final Audit New Zealand clearance. Subcommittee to also review Statements of Service Performance, report on CCOs and report on mana whenua partnership.<br><br>Subcommittee to review the draft letter of representation letter.<br><br>Subcommittee to recommend adoption of 2011/12 financial statements to Strategy and Policy Committee and the letter of representation.<br><br>Audit New Zealand to issue letter of comfort to strategy and Policy Committee as to whether an unqualified, or qualified, audit opinion will be issued. |
| <b>29 August 2012<br/>(scheduled)</b>  | <i>Special Strategy and Policy Committee Meeting</i><br>Committee to recommend adoption of 2010/11 financial statements to Council.  |
| <b>29 August 2011<br/>(scheduled)</b>  | <i>Council Meeting</i><br>Council to adopt 2011/12 financial statements.<br>Management Letter of Representation issued to Audit New Zealand.<br>Audit New Zealand sign Audit Opinion.<br>Media Release – Financial Results for the year ending 30 June 2012.   |
| <b>28 September<br/>2012</b>           | Release of published Annual Report.  |

## **Appendix 3: Draft 2011/12 financial statements**

## **Appendix 4: Draft 2011/12 financial overview**