

14 December 2017

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Bruce Smith
Mayor
Westland District Council
Private Bag 704
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cc Simon Bastion, Chief Executive
Lesley Crichton, GM Corporate Services

Dear Bruce

Final report on the audit of Westland District Council for the year ended 30 June 2017

1 Introduction

We have completed the audit for the year ended 30 June 2017 of Westland District Council (the District Council). This report sets out our findings from the audit and where appropriate makes recommendations for improvement. It covers our findings from our final audit.

We issued a separate interim management reported dated 28 August 2017.

2 Our audit opinion

We issued an unmodified audit opinion on 31 October 2017. This means that we were satisfied that the financial statements and statement of service performance presented fairly in all material aspects the District 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.

2.1 Uncorrected misstatements

The financial statements are free from material misstatements, including omissions. During the audit, we discussed with management any misstatements we found, other than those which were clearly trivial. All misstatements discussed with management were adjusted. We are satisfied that any uncorrected misstatements are individually and collectively immaterial.

2.2 Assessment of the control environment

As outlined in our interim report to the Council dated 28 August 2017, the October 2016 election delivered a new council, with only one councillor returning from the previous council. In addition to these changes to the governing body, three of the four senior managers resigned during the financial year. This has meant that staff in key roles were stretched over the latter parts of this financial year in particular. This affected all areas of the business, but in particular the assets and the Finance teams. The disruption and the need to keep the District Council's services operating meant a heightened risk that some key aspects of the control environment did not operate effectively throughout the year.

In assessing the effectiveness of the control environment through discussion and observation, we focussed in particular on the financial management processes and the financial and non-financial systems that directly impacted the annual report. We gained an understanding of how key aspects of the high level control environment were operating. Overall, we did not identify any significant new deficiencies that we needed to bring to your attention.

Following our final audit our assessment on the control environment remains unchanged.

2.3 Property, plant and equipment valuations

PBE IPSAS 17 Property, Plant and Equipment, requires that valuations are carried out with sufficient regularity to ensure that the carrying amount of an asset class does not differ materially from its fair value.

The District Council last revalued Land and buildings in 2015 and infrastructure assets in 2016. The District Council is required to demonstrate that the fair value of these assets had not significantly changed since that last valuation.

Management prepared an assessment for land and buildings and engaged an external valuer ANA group, to carry out a fair value assessment of all its infrastructure assets. ANA were the valuers that carried out the last two infrastructure valuations of these assets. ANA has a good knowledge of the assets under review.

Management concluded the fair value of property plant and equipment was not materially different from the carrying value. We reviewed the assessments provided, and agreed with management's conclusion that no revaluation was required.

Land and buildings are due to be revalued in 2017/18. This will be an area of focus for the 2018 audit.

Infrastructure assets are not due for revaluation until the 2018/19 year. The District Council will need to carry out a fair value assessment close to 30 June 2018 to determine if unit rates have materially moved or not. If the movement is significant, the District Council may need to revalue its infrastructure assets earlier than planned. It should also consider whether the current valuations provide a sufficiently robust base for developing the forecasts in the 2018-28 LTP.

We ask that the Finance team keep us informed on progress on this matter during the LTP and 2018 audits.

2.4 Severance payments

During the year there were three severance payments totalling \$230k.

We reviewed all three payments and sought advice from our accounting technical team and the legal team at the Office of the Auditor-General. This advice confirmed the amounts disclosed in the annual report were in accordance with the requirements of Schedule 10 clause 33 of the Local Government Act (LGA) 2002.

In our review we considered whether:

- The payments were based on sound decisions to settle.

We understand the District Council took legal advice prior to resolving the dispute and finalising the settlement.
- The payments were reasonable for the public sector.

The payments are relatively large compared to most payments in Local government. The settlements were a result of arms' length negotiations.
- There were any issues of probity.

While there was the issue of the SFO investigation, we were satisfied there were no probity issues directly impacting either of the agreements themselves.
- Payments were approved in accordance with financial delegations.

We draw to your attention the possibility that some aspects of the settlement agreements may give rise to some tax exposure for the District Council (as outlined below):

2.4.1 PAYE exposure

Recommendations

Seek professional advice and if appropriate consider making a voluntary disclosure to the IRD.

Findings

The District Council has a potential PAYE exposure in relation to payments made to former employees as some of the payments made through the settlement agreements were tax free.

Management comments

Management will take independent tax advice on the tax issues raised.

3 Significant matters, issues, or risks considered in this audit

3.1 Capacity and capability of the Finance Team

Due to on-going staff changes across the District Council over the past few years, and in Finance in particular, staff have been stretched. During the year the Finance team lost the GM Corporate Services and the Strategy and Communications Advisor. However, all vacant roles in the Finance team were filled by financial year end.

Having a full Finance team has meant the 2016/17 annual report process has been better than previous years. The new Finance team was able to provide us with an almost complete draft annual report at the start of the audit. Other information was largely provided as per the agreed timeframes outlined in our audit arrangements letter date 23 June 2017. However, again this year the delivery of service performance information caused delays to the audit process. We acknowledge that key staff change was the main reason why information was not prepared on time. Our discussions with staff and management identified there were poor handover processes resulting leaving gaps in knowledge. The loss in knowledge has meant extra time and effort spent on completing this part of the audit by both staff and the audit team. We expect this part of the audit to run more smoothly next year due to existing staff now understanding what is required.

3.2 Audit arrangements

For the first time this year, at managements' request we shortened our time on-site from five days per week to three days per week. The arrangement worked well and was positive for both us and the District Council. The arrangement provided Finance with the opportunity each week to progress work while we were working off site. It enabled the audit team to spend less time away on travel. It also reduced the disbursement costs for the audit this year.

The arrangement did not significantly hinder our ability to complete the audit. We completed our audit within the District Council's statutory reporting deadline of 31 October 2017. We acknowledge the assistance management and the Finance team provided to us during the audit.

We will continue to work with management to improve the audit process. We plan to hold a post audit debrief with management to go over how the process can be further enhanced on both sides.

3.3 Non-financial performance reporting

We reviewed the District Council's control environment, processes, and controls for developing its service performance objectives and targets, as well as reporting and monitoring on its performance.

As part of our year-end audit of the District Council's reported service performance information, we focused on:

- the quality of the overall "story" the performance reporting tells;
- the reliability/accuracy of the reporting;

- the completeness of the reporting against the performance framework as outlined in the LTP; and
- compliance with relevant legislation (in particular the Local Government Act 2002, Schedule 10).

Consistent with our conclusion in the prior year, we found that the Statement of Service Performance had some shortcomings. However, overall we were able to issue an unmodified audit opinion because the systems and processes supporting the key performance measures were sufficiently reliable. The narrative complemented this information by providing a reasonable “performance story”.

This was the second year that the District Council has had to report on the mandatory performance measures required by Department of Internal Affairs. While in the overall context of the annual report the systems and reporting were sufficiently reliable for our audit purposes, there are areas identified where systems and reporting need to be improved. We discussed this with the District Council staff during the audit.

Our recommendations for system improvements are included below:

3.3.1 Service requests

Recommendations

- 1 In relation to the system which supports a number of customer requests/complaints measures, develop processes and controls that can be put into place to:
 - Record the time of notification and ensure all customer services requests are recorded in a consistent manner (i.e. record all calls/complaints about sewerage or drinking water supply in the customer service request system at the time those calls are received).
 - Accurately record the time of attendance by the contractor – explore options with the contractor to record job data and auto-update the information in the customer service request system. The District Council needs to consider what controls it can put in place to ensure that the attendance time recorded on the paper job card is transferred accurately into the service request system;
 - Accurately record the resolution time by the contractor. The same considerations need to be given to this as above for attendance times; and
 - Provide training and develop guidance material for the customer service officers that are taking the calls in the first instance so that the classification for such events is accurate.
- 2 For information provided from the contractor, the District Council will need to engage and train the contractor on how to record the required information. The contractor may need live access to the service request module to achieve this.

Findings

We confirmed the reported result in the statement of service performance (SSP), for each measure we considered significant. For these measures overall, we found the information in the SSP to be complete, and a reasonable reflection of the Council's performance during the year.

However, we found that the District Council was unable to accurately report against the completion times for the mandatory services request performance measures. This affected three performance measures in the 3 waters and transport activities.

The District Council was able to report reliably the number of requests it received during the financial year and it has reported this information. It clearly disclosed the lack of relevant and available information regarding response times against each measure.

Management comment

Improving Council's ability to monitor and report on performance measures is a priority and a Service Request System review process is already underway with more work to come. Council is aware of the reporting requirements of the Act and is improving the Service Request System's ability to report against these measures. This is a long term project. Some improvements have already been noted however more improvements are needed over the next 12 months including:

- 1 *Programming the service request fields to automatically default select the appropriate response timeline as set out in the Long Term Plan.*
- 2 *Continuing 1:1 and group service request training tutorials to identify limitations of the current system, identify and implement solutions and ensure all new and existing staff are trained in the correct processes and that this knowledge is refreshed regularly.*
- 3 *Creating a full service request manual covering how to accurately log, update and sign off various scenarios.*
- 4 *Upgrading staff knowledge of how to accurately generate reports of the data contained with the service request database.*
- 5 *Removing redundant/confusing fields in service request system to reduce the ability for human error.*
- 6 *Improving the culture of staff and contractors to ensure that service requests are updated and closed off in a timely manner.*
- 7 *Ensuring that Council can report not only on the timeframes regarding the resolution of an issue, but also the timeframe in which an incident was attended by Council's contractors, and ensuring that this data is recorded not only in the Service Request System but also the records of our contractors e.g. job sheets.*

3.3.2 Dry weather overflows

Recommendation

Implement a system to capture wet weather sewer overflow events. In the interim the contractor should record the weather conditions when they attend sewer overflows.

Findings

The District Council is required to report all its dry weather overflows as outlined in one of the mandatory performance measures set by DIA.

Because the District Council does not have the systems to track rain events it is unable to exclude wet weather overflows from the measure. National rain data does not cover all areas of Westland district. Management believes the cost exceeds the benefit if it was to implement rain gauges across the whole district. Due to the high rainfall in the District this would also require additional staff to read these meters. All overflows have been reported as dry weather overflows. We have accepted this approach on the basis of materiality as there were only three sewer overflows during the year.

Management comment

As noted above, the national measure is not particularly applicable to Westland region. Average monthly rainfall in Westland District varies between just over 150mm in the driest parts of the year (February) to just under 300mm most other months of the year (refer <https://weather-and-climate.com/average-monthly-Rainfall-Temperature-Sunshine,Hokitika,New-Zealand>). This represents on a daily basis an average rainfall of between 5 and 10mm of rain per day.

Therefore, Council believes that the resources needed to establish whether the conditions for a wet weather overflow (i.e. 1mm of rain in a 24 hour period) have been met or not are not only cost prohibitive but also not a good use of resources given the very few instances of sewer overflows.

3.4 Kumara and Whataroa water treatment plant upgrades

The District Council awarded a contract to upgrade the two water schemes to Techno Economic Services (NZ) Limited (TES). The contract was subsequently terminated due to delays in implementation of the project and due to the contract being put on hold for the District Council internal investigation. We sighted a letter from TES's lawyer dated 20 June 2017 confirming the termination of the contract by mutual agreement between both parties.

We followed up whether any review was carried out on the process for awarding the contract. We understand the acting Chief Executive, engaged a local engineering firm, MWH/Stantec to carry out a review of the tendering process to ensure the District Council has complied with its internal processes. MWH/Stantec verbally confirmed to the Acting Chief Executive that the District Council had followed its processes.

Management comments

There was no formal engagement for this review. The CE met with a consultant of MWH/Stantec to discuss the tender evaluation process that had been used. The consultant was on the original evaluation panel. The discussion was verbal and was reported back to Council, that management were satisfied with the process followed.

3.5 Asset Management

We followed up on the District Council's progress in updating its asset management plans for the 2018-28 LTP. Management informed us that the asset management plans are in the process of being updated with help from the external consultant ANA Group.

We will review the updated asset management plans as part of the 2018-28 Long-Term Plan audit.

3.6 Fixed asset register

Recommendation

As management is not going to migrate the fixed asset register spreadsheet data in to the finance system (MagiQ), we recommend that someone regularly reviews the manual spreadsheet register to ensure changes to the spreadsheet such as asset additions and depreciation are being correctly calculated. It is also important this spreadsheet is regularly reconciled with general ledger within the Finance system.

Findings

Currently the Finance team manages the fixed asset register in a manual Excel spreadsheet. Management has informed us that that currently MagiQ does not meet the users' needs. Using a manual Excel spreadsheet gives rise to additional risk. In particular the added risk of human error in managing the spreadsheet, such as, inputting incorrect formula into depreciation calculations, tracking changes to the spreadsheet, identifying duplicate assets and making transposition errors when updating the general ledger

We understand the District Council is planning to upgrade the current MagiQ in March 2018. If the module meets the needs the Finance team, it may also migrate the current fixed asset register to MagiQ.

Management comment

The MagiQ system does not contain the functionality to break down assets into the component level that is required to provide meaningful data and ensure that depreciation rates are correct for each component class of asset.

There has not been any consideration to migrate back to the MagiQ Fixed Asset System. There may be other systems other than MagiQ explored in the future, until that time the Fixed Asset Register will remain an excel model.

Management will investigate building checks and controls into the excel model.

4 Other areas of interest

4.1 Rates

As part of our audit, we reviewed the District Council's compliance with key aspects of the Local Government Rating Act 2002 (LGRA). We focussed on the rates setting process – the consistency and completeness of the resolution and the Funding Impact Statement (FIS). We also reviewed a sample of targeted rates to assess whether the matters and factors used are consistent with the LGRA.

No issues were noted from our review to bring to your attention.

It is important to note that our review of compliance with legislation is for the purposes of expressing our audit opinion. It is not, and should not be seen, as a comprehensive legal review. This is beyond the scope of the audit, and our expertise as auditors. The Council is responsible for ensuring that it complies with applicable laws and regulations.

4.2 The District Council's governance role in completion of SOIs for CCOs

CCOs are responsible for meeting their accountability requirements under the Local Government Act 2002 (LGA). This includes preparing SOIs with appropriate involvement from their parent entities.

Local Authorities are responsible for the effective oversight of their CCOs. This includes reviewing and commenting on draft SOIs within the timeframe in the LGA. They should also monitor the CCOs' performance against the SOI targets.

Our review this year has confirmed non-compliance with the LGA 2002. In particular Schedule 2 part 8 which required the Board of the CCO to provide its draft Statement of Intent to its shareholder before 1 March. Due to the uncertainty of the group structure Westland Holdings Limited's 2017/18 draft Statement of Intent was not submitted to the Council for approval by 1 March 2017.

No other breaches of significant legislations were noted. We encourage the District Council to work with its CCOs to ensure compliance with significant legislative requirements.

4.3 Potential changes to the structure of the District Council's CCOs

4.3.1 Change in group structure

During the financial year, the District Council proposed changes to the Westland Holdings Limited Group. This included the disestablishment of Westland Holdings Limited and the merging of the Hokitika Airport Limited and Westland District Property Limited. The changes were planned to be in place before 30 June 2017.

As a result of this proposed merger, there was a change in Board members of Westland Holdings and a joint board, of new board members, was formed for the Hokitika Airport Limited and Westland District Property Limited. These new board members were appointed by Westland District Council not Westland Holdings Limited.

The proposed changes to the group structure have not gone ahead yet. We understand the District Council is reconsidering the future structure. The two entities are continuing to operate as separate entities with a common CEO, and Board, and combined processes.

Please keep us up to date with any potential changes to the structure of the group.

4.4 Other sector issues interest noted in our audit planning letter

As part of the audit we confirmed that the District Council complied with the Local Government Elected Members Determination and disclosed the remuneration of each member in the annual report. We noted the Mayor was overpaid by \$41 due to an incorrect formula in the spreadsheet. We confirmed the overpayment was subsequently reimbursed.

We also noted that the change in the determination meant the underpayment of the Deputy Mayors' and the Chairs of Audit and Risk Committee (pre and post-election). The remuneration for these additional responsibilities has increased with the updated determination. This resulted in an under payment of around \$1200 for the previous Deputy Mayor and Chair of Audit and Risk pre-election, and \$200 for Deputy Mayors and Chair Audit and risk committee post-election. We verbally informed management of the underpayment during the final audit.

No issues were noted from our review of related parties and conflicts of interest.

No fraud has been noted from our audit review and our enquiries of management and council.

5 Status of previous recommendations

The status of each matter that was outstanding in last year's report to the District Council is summarised in Appendix 2 (unless it is mentioned in the body of the report).

We have not revisited some matters in our interim management report around the systems of internal controls improvements as the final audit focussed on the audit of the Annual Report. This will be followed up as part of the 2018 interim visit and reported to the District Council in the 2018 interim management report.

Summary of action taken against previous years' recommendations:

| Number of recommendations from previous years' audits | Current status |
|--|---------------------------------|
| 3 | Matters that have been resolved |
| 5 | Still outstanding |

Appendix 1: Explanation of priority rating system

Our recommendations for improvement and their priority are based on our assessment of how far short the District Council is from a standard that is appropriate for the size, nature, and complexity of its business.

We have developed the following priority ratings for our recommended improvements:

| | |
|--|--|
| <p>Urgent Major improvements required</p> | <p>Needs to be addressed <i>urgently</i> These recommendations relate to a significant deficiency that exposes the District Council to significant risk. Risks could include a material error in the financial statements and the non-financial information; a breach of significant legislation; or the risk of reputational harm.</p> |
| <p>Necessary Improvements are necessary</p> | <p>Address at the earliest reasonable opportunity, generally <i>within 6 months</i> These recommendations relate to deficiencies that need to be addressed to meet expected standards of good practice. These include any control weakness that could undermine the system of internal control or create operational inefficiency.</p> |
| <p>Beneficial Some improvement required</p> | <p>Address, generally <i>within 6 to 12 months</i> These recommendations relate to deficiencies that result in the District Council falling short of best practice. These include weaknesses that do not result in internal controls being undermined or create a risk to operational effectiveness. However, in our view it is beneficial for management to address these.</p> |

Appendix 2: Status of previous recommendations

The recommendations raised in our previous management reports are still valid and are being progressed. Cleared issues and outstanding issues have been summarised below:

Matters that have been resolved

| Issues | Outcome |
|--|---|
| Landfill provision calculation | |
| Provide information to support the landfill inputs included in the landfill calculation. | An updated landfill provision calculation was provided to us during the final audit. We are satisfied that the rates used in the calculations are adequately supported and the provision has been calculated in compliance with accounting standards. |
| Receipt of year-end financial information from the Council's CCO | |
| Request draft financial information from the CCOs at an earlier date. | The District Council received the financial information from the Westland Holdings group in time for the preparation of the District Council's annual report. |
| Journals review | |
| Journals should be reviewed by an independent person before being posted. | There are now adequate controls in place to ensure segregation of duties around journal processes. |

Matters still outstanding

| Recommendation | Priority | Management comment |
|---|-----------|---|
| Renewals planned expenditure against actual expenditure | | |
| Ensure planned renewal expenditure are sufficient to avoid significant failure of assets in future years due to delayed maintenance not being carried out. | Necessary | <p>Funding has been allocated to replace assets based on material type and age using our database. This process is now being enhanced with funding being made available to test representative samples of assets such as pipes to enable condition rating in conjunction with age and material.</p> <p>Additional audit comment We will focus on the levels of renewals as part of the LTP audit.</p> |
| Legislative compliance | | |
| Introduce a formal legislative compliance system. This should identify legislative risks and responses, as part of a broader risk management framework. Ideally this would be integrated within the District Council's risk management software system. | Necessary | <p>This complies with and can be seen within all plans, reports, policies and decision making.</p> <p>Additional audit comment We acknowledge that these processes are a way of checking compliance with legislation as the District Council makes decisions. However a sound legal compliance system has organisation level processes for identifying and recording potential risks and assessing the likelihood of those risks across all activities of the organisation. Relying solely on the knowledge of staff exposes the organisation to risk, especially when staff change.</p> |
| IT Disaster Recovery Plan (DRP) | | |
| Update the DRP plan. | Necessary | Currently in progress. |
| Fraud process | | |
| Regularly review areas susceptible of fraud and update the fraud policy. We understand an external review of the fraud policy and internal controls was due to be completed by October 2017, however we understand this was pushed back to later in 2017. | Necessary | The review process started in November 2017. A draft report is expected to be available by the end of December 2017 with a final report early 2018. |

| Recommendation | Priority | Management comment |
|---|-------------------|--|
| Assets stocktake | | |
| Perform a physical stocktake to verify assets included in the fixed asset register still exist. | Beneficial | <i>A new engineering role has been created that has 50% of time dedicated to asset management data update and review. Data is also being transferred into a more reliable and accessible system to assist the data management process. Annual audits and documentation of 'critical' assets is being progressed.</i> |

Appendix 3: Mandatory disclosures

| Area | Key messages |
|--|---|
| Our responsibilities in conducting the audit | <p>We 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 reporting that opinion to you. This responsibility arises from section 15 of the Public Audit Act 2001.</p> <p>The audit of the financial statements does not relieve management or the District Council of their responsibilities.</p> <p>Our audit engagement letter contains a detailed explanation of the respective responsibilities of the auditor and the District Council.</p> |
| Auditing standards | <p>We carry out our audit in accordance with generally accepted audit standards. The audit cannot and should not be relied upon to detect every instance of misstatement, fraud, irregularity or inefficiency that are immaterial to your financial statements. The District Council and management are responsible for implementing and maintaining your systems of controls for detecting these matters.</p> |
| Auditor independence | <p>We confirm that, for the audit of the District Council's financial statements for the year ended 30 June 2017, we have maintained our independence in accordance with the requirements of the Auditor-General, which incorporate the independence requirements of the External Reporting Board.</p> <p>Other than the audit of the Group and its subsidiaries, we have not provided any engagements for the District Council during the year ended 30 June 2017. In addition, we have no relationships with, or interests in, the District Council.</p> |
| Other relationships | <p>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 District Council that is significant to the audit.</p> <p>We are not aware of any situations where a staff member of Audit New Zealand has accepted a position of employment with the District Council during or since the end of the financial year.</p> |
| Unresolved disagreements | <p>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.</p> |