

VICTORIA

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Victorian  
Auditor-General

Audit summary  
of  
Local Government:  
Interim Results of the  
2009–10 Audits

Tabled in Parliament  
11 August 2010

# Audit summary

## Background

This report informs Parliament of our findings about the effectiveness of internal controls arising from our interim financial audits of 79 councils, the 13 entities they control and the 12 regional library corporations (RLCs).

All public sector entities should have adequate internal controls to assure the reliability of their financial reporting, the efficiency and effectiveness of their operations and compliance with all relevant laws and regulations. In our annual financial statement audits, we focus on controls relating to financial reporting. While it is not our responsibility to form an opinion about internal controls, we nevertheless raise any control weaknesses or breakdowns we identify with management.

## Overall conclusion

Councils need to further strengthen their internal controls, particularly those over information technology change management policies and declarations of interest.

The utility and consistency of financial reporting across the local government sector is reduced by a lack of timely coordination and guidance in the adoption of consistent approaches for presenting income and expenditure in the comprehensive income statement and valuing land under roads reported in the balance sheet.

## Findings

### Common internal control weaknesses

The audit of the design and effectiveness of the control environment at local government entities includes a review of controls over those financial systems that provide information for the annual financial statements.

Our interim audits found instances where internal controls should be strengthened and were reported to the audit committee and management of each entity. Three common control weaknesses were identified:

- masterfile changes at 31 councils (39 per cent) for the payroll and accounts payable systems were not verified
- poor bank reconciliation controls at 14 councils (18 per cent), including not completing reconciliations promptly, leaving reconciliations with unresolved variances, and inadequately segregating the duties of preparing and reviewing reconciliations
- inadequate information technology (IT) disaster recovery planning at 12 councils (15 per cent), including councils without plans, or with untested plans.

No common control weaknesses were identified through our audits of the RLCs and other local government entities.

### Controls over declarations of interest

We use a cyclical approach to reviewing internal controls relating to significant annual financial report balances and disclosures consistent with Australian Auditing Standards. This year we reviewed key controls over declarations of interests and gifts.

These controls are important as:

- one of councils' primary roles is to provide governance and leadership for the local community through advocacy, decision making and action
- councillors and council employees should act, and be seen to act, honestly and impartially at all times.

### Declarations of interests

Amendments to the *Local Government Act 1989* (the Act), which took effect in December 2008, introduced revised requirements for councillors.

It is pleasing to note in 2009–10, councillors at 76 of the 79 councils completed all the required returns in line with the Act; however, councillors at three councils did not complete all required returns in line with the Act.

Fifty-seven councils (72 per cent) did not have a council approved policy covering the completion of declarations of interest by councillors.

Of the 22 councils with an approved policy, three could be further improved by including the time frames required for the completion of ordinary and primary returns.

### Declarations of gifts

The December 2008 amendments to the Act also requires councillors and staff to declare gifts, as part of the declaration of interest, when they receive gifts with a cumulative value of more than \$200 over five years.

Eleven councils (14 per cent) do not have an approved gifts policy that builds on the Act, with guidelines for when gifts are received.

Analysis of the 68 councils with an approved gift policy shows that 54 councils (68 per cent) had specified a dollar threshold for declaring gifts, up to \$220. However, specifying a dollar threshold in this way can result in councillors and staff not complying with the Act's requirement to declare all gifts with a cumulative value of more than \$200 over five years.

### Controls over information technology change management

IT change management policies assist councils to reliably plan, authorise and test changes to their IT infrastructure before implementation.

Fifty-one councils (65 per cent) did not have an approved IT change management policy. Eleven of which outsourced all or part of their IT services without having a policy for in-house IT services. These councils had not reviewed and accepted their providers' IT change management policies.

The 28 with an approved policy could be further improved given:

- five (18 per cent) did not require that requested changes be supported by a risk/ benefit assessment
- ten (36 per cent) did not address the authorisation and implementation of emergency changes.

### Financial reporting framework

During the 2009–10 financial year there was a significant change to the financial reporting framework in local government, which was the revision of Australian Accounting Standard AASB 101 *Presentation of Financial Statements*. The presentation of the financial statements has changed, with a new format for the income statement and greater disclosure required when comparative information for previous periods is restated.

Different approaches were adopted for presenting income and expenditure and valuing land under roads in 2008–09. It is evident that this will continue in 2009–10. Without timely guidance, which requires the adoption of consistent approaches, the utility and consistency of financial reporting across the local government sector is reduced.

The Australian Accounting Standards Board (AASB) and the New Zealand Financial Reporting Standards Board (FRSB) issued a joint exposure draft, ED 180 *Income from Non-exchange Transactions* (Taxes and Transfers) in June 2009, to replace AASB 1004 *Contributions*. AASB 1004, requires that funds from non-exchange transactions, such as grants and developer contributions are recognised on receipt rather than as expended. This has introduced volatility in operating results at councils and reduces the usefulness of financial statements for users making decisions about resource allocation and management accountability. The proposals in the exposure draft are likely to result in the deferral of the recognition of income, which will reduce year-on-year volatility in entities' net results.

## Recommendations

Number	Recommendation	Page
1.	Local government entities should assess their policies and procedures against the commonly identified internal control weaknesses to assess if they are operating in a reliable, efficient and cost-effective manner.	9
2.	Local government entities should have a comprehensive declarations of interest policy that builds on the requirements of the <i>Local Government Act 1989</i> , including disclosure of conflicts of interests and the maintenance of the register of interests.	14
3.	Local government entities should have a comprehensive gifts policy that builds on the requirements of the <i>Local Government Act 1989</i> .	15
4.	Local government entities should have a comprehensive information technology change management policy.	20
5.	The Department of Planning and Community Development should facilitate provision of timely guidance to local government entities to achieve consistency and comparability in financial reporting across the sector.	24

## Submissions and comments received

In addition to progressive engagement during the course of the audit, in accordance with section 16(3) of the *Audit Act 1994* a copy of this report, or relevant extracts from the report, was provided to the Department of Planning and Community Development with a request for comments or submissions.

Agency views have been considered in reaching our audit conclusions and are represented to the extent relevant and warranted in preparing this report. Their full Section 16(3) comments and submissions; however, are included in Appendix B.

## Audit conduct

The interim audit of the 79 councils, the 13 entities they control and the 12 RLCs were undertaken in accordance with the Australian Auditing Standards.

The total cost of preparing and printing this report was \$125 000.