

## **AUDIT AND RISK MANAGEMENT SUBCOMMITTEE**

### **AGENDA**

**WEDNESDAY 29 MAY 2013**

**AT 1PM**

**COMMITTEE ROOM 1, SECOND FLOOR, CIVIC OFFICES, 53 HEREFORD STREET**

**Subcommittee:** Councillor Tim Carter (Chairperson)  
Councillors Helen Broughton, Sally Buck, Ngaire Button, Jimmy Chen and Jamie Gough  
and Messrs John Hooper and Michael Rondel

**General Manager  
Corporate Services**  
Paul Anderson  
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**1. APOLOGIES**

Nil.

**2. DEPUTATIONS BY APPOINTMENT**

Nil.



## AUDIT AND RISK MANAGEMENT SUBCOMMITTEE 29. 5. 2013

### 3. AUDIT NEW ZEALAND MANAGEMENT REPORT

<b>General Manager responsible:</b>	General Manager Corporate Services, DDI 941-8528
<b>Officer responsible:</b>	Corporate Finance Manager
<b>Author:</b>	Patricia Christie – External Reporting and Governance Manager

#### PURPOSE OF REPORT

1. This report tables the Audit New Zealand Management Report on the Council for the year ended 30 June 2012.

#### EXECUTIVE SUMMARY

2. The Management Report is in **Attachment 1**.
3. The key points noted in the Management Report are:
  - Audit New Zealand thanks Council staff for their work. It was noted that the financial statements for the Council Controlled Organisations (CCOs) were completed early and met their statutory reporting deadlines.
  - The continued issues regarding the valuation of assets and the quantification of asset impairment post-earthquakes are discussed in explaining the reasons for the disclaimer audit opinion on a number of sections of the annual report. It is noted that there will continue to be issues in this area for a number of years yet.
  - Additional detail is given on the work performed in validating the earthquake revenue and debtors balances.
  - There are a number of suggestions for the improvement of the annual report preparation process which are under action by staff.
  - It was suggested that the Council maintain an interests register to assess whether there are any related party transactions to be disclosed. It was noted that the Code of Conduct passed by the Council on 28 June 2012 made the declaration of Councillors' interests mandatory and this should be a positive step towards ensuring all interests are declared and disclosed.
  - It was noted that a number of the Council's CCOs did not meet the statutory timeframe for the provision of their Statement of Intent (SOI) to the Council. However, all had completed SOIs prior to the signing date of the annual report. This is not considered to be an issue for 2012/13 as the SOIs are already in hand.

In addition, the following Future Implications are noted:

- The Council is making progress in determining the quantum of earthquake related asset damage and that Audit New Zealand expects that the modified audit opinion issued in the last two years is the worst case scenario. It expects this to soften/improve over time as the Council is able to address these issues.
- That until the Council's valuers are able to value land, buildings and infrastructure assets some form of modification to the audit report will continue; as without an independent valuation of these assets there remains uncertainty over the fair value of the Council's property, plant and equipment.

#### FINANCIAL AND LEGAL CONSIDERATIONS

4. None.

#### STAFF RECOMMENDATION

That the Subcommittee receive the Audit New Zealand Management Report for the year ended 30 June 2012.

Management report on the audit of  
**Christchurch City Council**  
for the year ended 30 June 2012

# **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 of Christchurch City Council (the Council) and reporting that opinion to you. This responsibility arises from section 15 of the Public Audit Act 2001.

We carried 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 Council and management are responsible for implementing and maintaining your systems of controls for detecting these matters.

**Statement of auditor independence**

We confirm that, for the audit of the Council's financial statements for the year ended 30 June 2012 we have maintained our independence in accordance with the requirements of the Auditor-General, which incorporate the independence requirements of the New Zealand Institute of Chartered Accountants.

In addition to the audit of the annual report, we carried out other assurance engagements for the Council's subsidiaries. These involved issuing reports pursuant to the Electricity Distribution Services Default Price-Quality Path Determination 2010 and the Commerce Act (Specified Airport Services Information Disclosure) Determination 2010. These engagements are compatible with those independence requirements.

Other than the audit and the engagements detailed above, we have no relationship with or interests in the 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 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 Council during or since the end of the financial year.



Julian Tan  
Audit Director  
26 November 2012

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# Report to the Council

on the audit for the year ended 30 June 2012.

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We have completed the audit for the year ended 30 June 2012. This report complements our interim management report issued to the Council on 5 June 2012. The report sets out our findings from the final audit and draws attention to areas where the Council is doing well or where we have made recommendations for improvement.

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## Key messages

### Impact of earthquakes on the financial statements and audit opinion

The impact of the Christchurch earthquakes has continued to have a significant effect on the Council's 2011/12 annual report and our annual audit. The Council has faced the same asset related issues this year as those that led to a disclaimer of opinion last year.

These ongoing issues meant that we were unable to obtain appropriate audit evidence that property, plant and equipment related balances were fairly stated. Consequently, we issued a disclaimer of opinion on this year's financial statements. However, we have also provided positive assurance over those statements and balances that were not affected by the asset related issues.

We have also qualified aspects of the non-financial performance information in our audit report on the 'what did it cost' sections as these included asset related information that we were unable to verify. Additionally, there are modified audit opinion issues in the Council group entities that have impacted on the audit opinion for the Council group financial statements. These are also due to asset related issues arising from the effects of the earthquakes.

### Statements of intent

The other significant issue in this year's audit relates to most of the Council's CCOs not meeting statutory requirements in respect of their statement of intent. Most of the CCOs did not provide a draft statement of intent to the Council within the statutory timeframe. As a result some consequential legislative requirements for the statements of intent were also not met.

We made no mention of these legislative breaches in our audit opinion because the CCOs delivered the final completed statements of intent to the Council before the signing date of the annual report and the breaches were disclosed in the financial statements.

### Thank you

We would like to thank the Council, management and staff for the cooperation and assistance provided to the audit team during the audit.

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## **1 Our audit opinion**

### **1.1 We issued a modified audit opinion**

We issued a modified audit opinion on the Council and group's annual report on 25 October 2012.

The modified opinion related to the following matters:

- The impact of the Canterbury earthquakes which significantly damaged Council's property, plant and equipment. We issued a disclaimer of opinion due to the Council not being able to account for the financial effect of the damage to these assets nor being able to revalue its infrastructural assets and land and building assets in accordance with the standards.

We comment further on this in section **2.1** below.

- We also included in the audit report a qualification in respect of Council's non-financial performance reporting. Council was required to include non-financial performance information in its 2012 annual report (after being exempted from this requirement in 2011). However, we were unable to obtain sufficient appropriate audit evidence to support the 'what did it cost' sections and variance explanations as these were affected by the asset related issues identified above.
- Modified audit opinions within the Council group. In particular, the effect of Vbase Limited's asset related modified audit opinion is material to the Council group. Consequently, we referred to this impact in the Council's group opinion.

### **1.2 Uncorrected misstatements**

Other than the earthquake and property, plant and equipment issues noted above that impacted on the audit opinion, the financial statements are free from material misstatements, including omissions. However, in the course of the audit, we have found certain misstatements that are individually and collectively not material to the financial statements.

We have discussed these misstatements that we found with management. The significant misstatements that the Council has not corrected are listed in Appendix 1 along with management's reasons for not adjusting these misstatements. These only relate to the group financial statements. We are satisfied that these misstatements are individually and collectively immaterial.

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## 2 Matters arising from the audit

### 2.1 Property, plant and equipment related matters

As a result of the impact of the 2010 and 2011 Canterbury earthquakes, we issued a disclaimer of opinion last year on the Council's 2010/11 financial statements (other than the statement of cashflows and account balances not affected by the property, plant and equipment issues).

The reasons for the disclaimer of opinion were due to the impact of the earthquakes on the Council's property, plant and equipment and the Council's inability to account for the financial effect of the earthquake damage to these assets within its financial statements. The balances impacted included:

- the carrying amount of property, plant, and equipment, asset revaluation reserves, and retained earnings in the balance sheet;
- the related impairment losses, loss on disposals, and depreciation charged to the profit/loss in the statement of comprehensive income; and
- the related property, plant, and equipment valuation gains/losses and the impairment losses charged to other comprehensive income in the statement of comprehensive income.

This matter applied to the 2011/12 financial statements. Although there has been some progress made in 2011/12, the Council did not have sufficiently reliable information available to account for the earthquake damage to assets. In summary, the same issues that resulted in the disclaimer of opinion in 2011 continue to exist, and are considered material to Council's 2011/12 financial statements. The key issues were:

- Continued uncertainty over the cost estimates to repair damaged infrastructure assets.
- Inability to obtain valuations for asset classes carried at fair value, due to:
  - a lack of market evidence to perform a revaluation of land and buildings at 30 June 2012; and
  - uncertainty over the appropriate replacement cost rates for infrastructural assets valued using depreciated replacement cost.
- Insufficient information to allow Council to determine the correct accounting treatment for earthquake damaged assets (e.g. write-off of irreparable assets and impairment of damaged but repairable assets).
- Council's subsidiaries Vbase Limited and Tuam Limited have received modified audit reports on their 2012 financial statements due to the effects of the earthquakes.

We acknowledge that the Council has made some progress in 2011/12. The Council has recognised an impairment of \$191.2 million for its underground assets. This was calculated based on SCIRT's estimate of the length of underground pipes that will need to be replaced.

Whilst an impairment cost has been estimated for underground assets, there has been no estimate of impairment for other property, plant and equipment such as some of the above ground assets. Apart from \$44 million recognised last year for significantly damaged buildings, there have been no other impairment costs recognised.

The impairment estimate has also been calculated based on unit replacement cost rates used at the last valuation instead of current replacement cost rates. Consequently, we do not consider that the impairment recognised in 2011/12 fairly reflects the quantum of the estimated repair costs and therefore the carrying value of the associated assets are considered to be materially misstated.

The Council has derecognised a number of assets that have been demolished or where decisions regarding their future use have been made, for example, where CERA has issued a demolition. The majority of the assets derecognised in 2011/12 are building assets (mainly QEII stadium).

In conclusion, a disclaimer of opinion on the financial statements has been issued because we continued to assess the impact of the above matters as pervasive and material, due to their size and fundamental impact. Because of these matters, we were unable to obtain sufficient audit evidence to form an opinion over the financial statements as a whole.

As for last year, the Council has made extensive disclosure of the impact of the earthquakes in its financial statements.

### **Management comment**

*Agreed; with the ongoing work to determine asset conditions we expect to be in a position at June 2013 to write off further building assets and, subject to there being a robust market, will have commenced the revaluation process. Realistically though, it will still take several years to reach a position which satisfies both Audit New Zealand and ourselves.*

## **2.2 Other earthquake related matters**

### **2.2.1 Earthquake revenue/debtors**

There are five main sources of insurance/funding for earthquake damage to Council assets. These are LAPP (being the insurers of the Council's underground assets and also the above ground buildings (the latter through Civic Assurance)), CERA (funding the Crown's share of the rebuild costs), Department of Internal Affairs (funding the Crown's share of emergency response costs and temporary repairs), New Zealand Transport Agency (funding the Crown's share of the roading network), and EQC (funding the repairs to the Council's social housing stock).

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These different sources and types of earthquake revenue meant that it was difficult to confirm earthquake related revenue. As for last year, Council recognised a significant amount of earthquake revenue this year based on the premise that claimable costs have been incurred, captured, and are claimable from various parties. We performed testing of this expenditure to invoices and are satisfied that these costs are valid and claimable based on insurance policies or other documentation in place (for example, the National Civil Defence Emergency Management Plan).

We considered the revenue and year-end debtor separately for each source.

- LAPP underground assets. LAPP has exhausted its funds and could only cover damage up to and including the February 2011 earthquake. Therefore, the damage resulting from the June 2011 earthquake was not covered by LAPP. Much of the damaged underground assets are still to be repaired. The repair process could take up to 5 years to complete.

In the meantime, Council has reached a settlement with LAPP for a full and final payout of \$201 million to cover all damage. As a result, we have been able to confirm this revenue and debtor. Note that \$36 million of the \$201 million had been accrued in the 2010/11 year. The receivable at balance date was \$41 million of which \$21 million has been received subsequent to balance date.

- LAPP buildings insurance. The two major components of this are:
  - Council has previously reached a settlement with LAPP over payment of the indemnity value of significantly damaged buildings that have been demolished or are to be demolished. This settlement was for \$47 million, which was recognised as revenue in 2010/11. In 2011/12, Council has recognised the difference between this indemnity value and the reinstatement value that these buildings are insured for. We have confirmed to the insurance policy that these buildings are insured for reinstatement value.
  - Council has incurred costs in repairing buildings. These costs are claimable under the buildings insurance policy. At balance date an accrual of \$40 million has been recognised on the basis that the expenditure incurred is reimbursable. We have reviewed this expenditure for reasonableness.

The total receivable from LAPP in respect of buildings at balance date is \$100 million. There have not been any payments subsequent to balance date. We have discussed this debtor amount with Council finance staff who explained that the delay in payment is because LAPP is waiting for its re-insurers to pay. We are comfortable with this because we have seen evidence of payments coming through from the re-insurers for the payment of the indemnity value.

- Revenue from CERA for funding of rebuild is \$104 million. This amount is an accrual for rebuild work reimbursable from the Crown. As noted above, we

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have performed testing of earthquake expenditure back to invoices. \$24 million was received from CERA prior to balance date, and \$42 million subsequent to balance date.

- Revenue from the Department of Internal Affairs for funding of emergency response costs and temporary repair costs is \$95 million. This is an accrual based on costs incurred reimbursable from the Crown. The receivable at balance date is \$89 million. This has not been received subsequent to balance date.

However, since balance date, the Department of Internal Affairs appointed an external consultant (Deloitte) to review Council's claimable expenditure to invoices. It was pleasing to note that Deloitte identified only minor errors. The low rate of errors identified provides us with some comfort over the accuracy of the claims made. In addition, we have confirmed the amount owing by the Department of Internal Affairs in its financial statements to the amount included in Council's financial statements.

- NZTA revenue is \$103 million relating to roading repairs. Most of this was claimed for and paid by NZTA. At balance date, only \$15 million remained receivable.
- EQC is covering damage to the Council's social housing stock. Revenue for 2011/12 is \$15 million. There is no amount outstanding at balance date.

In conclusion, much of the revenue recognised is still in receivable. The total earthquake receivable at balance date is \$345 million, an increase from the \$212 million last year. Although LAPP, Department of Internal Affairs and CERA have been slow in paying, we are satisfied that the amount owing is collectable.

#### **Management comment**

*We continue to work with each of the parties above to reduce the outstanding balances, and improve the overall process for future receivables. \$62 million of the \$89 million owing by DIA was received in early November 2012.*

### **2.2.2 Implications for the future**

#### **Audit opinion**

As noted above, Council is making some progress in determining the quantum of asset damage. The modified audit opinion we have issued in the last two years is the worst case scenario. We would expect this to soften/improve over time as Council are able to address the issues impacting on the opinion.

We note that SCIRT staff are currently preparing an updated estimate of costs to repair and rebuild the horizontal infrastructure assets and this is due out towards the end of the year. These estimates are expected to be more robust as Council has been performing a lot of work in the meantime to identify asset damage. We will assess

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the degree of robustness of these estimates, and the impact on property, plant and equipment balances in next year's audit.

#### **Revaluation of assets**

An aspect of the modified opinion relates to Council's assets that are carried at fair value and subject to revaluation. In all likelihood, until Council's valuers are able to value the land, buildings and infrastructure assets some form of modification to the audit report will continue. Without an independent valuation of these assets, there is likely to be continuing uncertainty over the fair value of Council's property, plant and equipment.

#### **Upcoming 2013-22 Long Term Plan**

In preparing the upcoming long term plan (LTP), Council will need to consider how it will identify and distinguish between infrastructure and other asset repairs from rebuild (capital) work. This is important in determining the accounting for the work to be performed. The revised cost estimates will also be an important ingredient that will feed into Council's next LTP covering the period 2013/2022. We understand that Council will not have updated asset management plans for its infrastructure assets ready until the following 2015/25 LTP.

A number of important decisions are still to be made by Council in respect of existing and replacement facilities. For example, Council has not made any firm decisions on the QEII Park land or its replacement facility. These decisions could impact on the accounting treatment for existing assets and the next LTP.

#### **Accounting matters**

A number of Council buildings and facilities have been demolished, or will be demolished, due to earthquake damage. These properties are held for service delivery objectives. However, with the demolition of the building, the use of the land could change. NZ IAS 40, Investment Property, states that land held for a currently undetermined future use is "investment property". Council needs to consider this treatment in the future as the demolition may mean that properties may no longer be held for service delivery objectives.

Our view is that property with an uncertain future use shall not be reclassified to investment property unless a formal decision has been made by Council to change its future use. Council has not reclassified any such land to investment property in 2011/12.

#### **Management comment**

*Management acknowledges that there is still significant uncertainty as to the extent of damage to many of Councils assets as SCIRT and other contractors revise estimates. Similarly, we acknowledge the uncertainty around the use of some of the land. Management will continue to assess the information available and reassess the appropriate accounting treatment for assets and keep Audit New Zealand updated of any significant changes.*

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*We are confident that our existing processes will enable us to distinguish between infrastructure and other asset repairs and ensure the correct accounting treatment.*

### **2.3 Annual report preparation process**

From an audit perspective the preparation of the annual report went relatively smoothly this year. Council's finance team involved in the preparation this year was bolstered by new staff, and this increased capacity allowed the workload to be spread amongst staff. A notable success was that the financial statements for the Council Controlled Organisations were completed early and met their statutory reporting deadlines.

The finance team were proactive in identifying and addressing significant matters prior to the audit and promptly as they arose during the audit, and kept us informed of issues through the weekly meetings. There was good open communication between management and audit during these meetings.

We experienced some minor delays during the audit mainly in the areas of performance information and matters arising from accounting for earthquakes, insurance and property, plant and equipment matters. We have commented on the performance information separately in this report and will work with management to streamline the collection and dissemination of performance information for the 2013 audit.

In regards to the insurance issues (insurance proceeds, receivables etc), as this is a 'live' and constantly developing situation, we continued with our enquiries regarding receipts from insurers, the situation with the pool of reinsurers, etc, right up to the date of our audit report. Ultimately we were satisfied that receivables are fairly stated and collectable based on the information available.

### **2.4 Council's governance role in completion of statements of intent (SOIs) for Council Controlled Organisations (CCOs)**

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

We found that many of Council's CCOs did not comply with the legislative requirements for completion of their SOI. Under the Local Government Act 2002, there are a number of procedural requirements for the preparation of the annual SOIs which were not met in respect of the 2012/13 SOIs.

Each CCO is required to deliver a draft SOI to Council by 1 March each year. Other consequential requirements include the CCOs considering comments provided by Council within two months of 1 March 2012, and to deliver the final completed SOI to Council by 30 June 2012.

We understand that that this situation arose because a restructuring of Council committees meant that the process of, and responsibility for, reviewing SOIs, was disrupted.

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As the final completed SOI were delivered to Council before the signing date of the annual report, and the breach has been disclosed in the financial statements, we made no mention of the legislative breach in the audit report.

**Management comment**

*This has been addressed with the boards and trustees of the CCOs, and we anticipate having the SOIs before Council by the due date in 2013.*

**2.5 Capitalisation of work in progress**

Total capital work in progress at 30 June 2012 was \$440 million. This is an increase of \$300 million compared to 30 June 2011. Although an increase is expected due to the rebuild phase of the earthquake recovery, the main reason for the large amount of capital work in progress is that Council do not have sufficient information available from SCIRT to enable it to capitalise projects that are completed.

We understand that Council has entered into discussions with SCIRT for the provision of appropriate information on completed projects to enable them to be capitalised in a timely manner. This information, which will generally be provided by Council staff seconded to SCIRT, will allow Council to update their fixed asset registers.

In our review of capital work in progress, we also noted a minor item for \$36,231 relating to bus exchange fit-out costs incurred in a prior year that should have been capitalised.

**Recommendation**

Council capitalise completed projects into the fixed asset register in a timely manner.

**Management comment**

*We agree that this is a problem and continue to work with SCIRT and CERA to resolve it.*

**2.6 Interests register**

Council maintains an interests register for its members to declare their interests. However, we noted that during 2011/12, only three members had declared their interests. Although the declaration of interests is voluntary, Council is required to disclose related party transactions within its financial statements.

Therefore, it needs this information to assess whether there are any related party transactions to be disclosed. We understand that the provision of this information will be mandatory going forward. Council passed a Charter on 17 May 2012 and a new Code of Conduct on 28 June 2012 which will make the declaration of interests mandatory. This is a positive step towards ensuring all interests are declared and disclosed. It will also allow Council to proactively manage or avoid potential conflicts of interest situations as they arise.

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**Management comment**

*Noted, and agreed.*

**2.7 Accounting policies**

We reviewed Council's accounting policies. We noted the following areas where Council may want to consider developing and adopting an appropriate accounting policy.

- traffic and parking infringement revenue;
- grant expenditure; and
- accounting treatment for Kiwisaver.

Examples of these policies can be found in the Audit New Zealand Te Motu District Council model financial statements available on the following URL:

<http://www.auditnz.govt.nz/publications-resources/public-sector-auditing/model-financial-statements/local-authorities>

**Management comment**

*An accounting policy for Traffic and parking infringement revenue was not included as the revenue received in the current year was considered immaterial – this will be reviewed in 2012/13.*

*The need for a policy on Grant Expenditure and Kiwisaver will be reviewed in 2012/13.*

**2.8 Hurt and humiliation payments**

In last year's management report, we commented on the potential PAYE exposure that Council could face if Inland Revenue investigated payments made for hurt and humiliation.

During 2011/12, Council has made a number of payments to former employees for hurt and humiliation, including one payment for \$25,000. We understand that these payments have been treated as non-taxable.

In an investigation, any payments over \$10,000 are likely to attract attention from Inland Revenue. In general, it would be very difficult to convince Inland Revenue that any payments over \$20,000 were not at least partially taxable. Tax liabilities may also exist in relation to smaller payments. In cases where there is no evidence of a genuine personal grievance, Inland Revenue could consider the entire payment to be taxable.

Where there is no genuine personal grievance or the payment is considered to be excessive, Inland Revenue will often seek to "gross-up" the payment to calculate the

PAYE liability. As a result, the total liability for the employer, including interest and penalties, can be as much as the payment made to the employee.

Over the last few years, payments for hurt and humiliation have become an area of focus for Inland Revenue, with many public sector entities receiving amended PAYE assessments.

**Management comment**

*Noted. The extreme situation relating to the \$25,000 payment arose out of the unique circumstances of the Canterbury Earthquakes.*

**2.9 Accounting for non-current assets held for sale**

NZ IFRS 5, *Non-current assets held for sale and discontinued activities*, requires non-current assets held for sale or discontinued use to be measured at balance date at the lower of its carrying amount and fair value less costs to sell.

In the financial statements, Council measures its non-current assets held for sale at their carrying amount. Although non-current assets held for sale are minimal, we recommend that Council complies with NZ IFRS 5 in accounting for these assets and that these be carried at the lower of their carrying amount and fair value (less costs to sell).

**Management comment**

*Comment is noted and management will review and revise the accounting policy.*

**2.10 Interest rate swaps**

In our review of interest rate swaps which are hedge accounted, we noted one hedge where the date of the swap differed from the date it was designated as a hedge (VR3112). Although there is no requirement for the two dates to be the same, different dates will result in hedging ineffectiveness and will mean that the hedge relationship will likely become ineffective before maturity.

We recommend that swaps be designated for hedge accounting on the same date as the swaps are entered into

**Management comment**

*Agree, and this is our normal practice. We have amended our controls to prevent further errors.*

**3 Sector-wide areas of audit focus**

We completed reviews on our areas of interest across all local authorities. Our comments on the issues not previously discussed in this report or in our interim management report are as follows:

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### 3.1 Asset management plans

We will review the status of Council's asset management plans in our audit of the 2013-22 LTP that will commence soon. Given the damage to Council's assets from the earthquakes, the previous plans are effectively redundant and will need to be revised in alignment with the infrastructure rebuild.

We understand that the plans are not likely to be updated in time to be incorporated into the 2013-22 LTP and that a high level summary will be used to support the asset management information within the LTP while the detailed asset management plans are being reworked.

#### Management comment

*During the 2013-22 LTP process we did include a high level statement relating to the Council's strategy for assets in each appropriate Activity Management Plans. Within the Internal Activity Management Plan for our Infrastructure Asset Management Service we highlighted the programme of works required to review and update our asset management plans so that they are consistent with all of the recovery plans. This schedule of work is predicted to take a couple of years so that they are available to inform the 2015/25 LTP.*

### 3.2 Weather tightness

We considered the adequacy and appropriateness of the Council accounting treatment and related disclosures in the financial statements.

Council has formally opted into the financial assistance package (FAP) established by Government to help homeowners repair their leaky homes faster. We considered the adequacy of the assessment of the financial impact of the decision and whether this was appropriately accounted for and adequately disclosed.

We identified no issues for your attention.

### 3.3 Development Contributions

As part of the audit, we reviewed Council's controls to ensure development contributions were charged in accordance with the policy and the use and application of funds received was appropriate and correctly accounted for.

We did not identify any issues. We will review the development contributions policy as part of the LTP audit.

### 3.4 Audit of service performance

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 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).

When we performed the audit of Council's 2009-19 Long Term Council Community Plan (LTCCP), we concluded that the performance framework provided an appropriate basis for meaningfully assessing Council's actual performance. We have updated our assessment to take into account any changes in Council's business and activity since the LTCCP was adopted. 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. We are mindful that a number of performance measures were "suspended" this year, due to the impact of the earthquakes on infrastructure assets. For these measures, we are satisfied with the narrative contextual disclosures provided.

We make the following comments on other aspects of the service performance information.

#### **3.4.1 Process for preparing the service performance information**

In regards to the preparation of the service performance part of the annual report, we believe that the process could be improved by having one person responsible for the co-ordination of the entirety of the service performance information. This would entail having responsibility for coordinating and collecting both the information required to report against performance measures for the year and the narrative relating to performance for each activity.

In auditing the service performance information, we found that we were required to deal with a number of staff who provided information for various parts of the service performance statement. Although they were cooperative, we encountered delays in some cases in obtaining information or in requesting changes be made to the information reported.

Having one person with overall responsibility coordinating the service performance information would mean that there is one person who, at all times, is aware of the status of all of the service performance information. This person would know what information is outstanding, what information needs to be changed or updated, and is able to follow up any queries relating to this information in a timely manner.

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### **Management comment**

*This suggestion makes sense, assuming that the term 'service performance' applies to levels of service (and not to the total package of financial and non-financial information for a group of activity).*

*The Planning & Performance Unit is the point of contact for all non-financial service delivery data. This unit manages the databases concerned and generates the information used in the Annual Report. It also holds the experience and expertise around measures and targets.*

*Please ensure that all information on service delivery is co-ordinated by the Manager, Planning & Performance as he is our central point of contact.*

### **3.4.2 Comparative and trend information**

Comparative and trend information is not provided for service performance information. However, it is provided for financial information within the financial statements.

We encourage Council to include comparative and trend information, where appropriate, in the service performance information, particularly the performance targets. This would provide the reader with more information to analyse Council's performance over a longer period.

### **Management comment**

*Information on trends against service delivery targets is maintained by the Planning & Performance Unit. As noted a minority of measures were suspended during the earthquake events and this has created gaps in some instances.*

*While using trend line data against every measure in the Annual Report would perhaps be unwieldy, it would be quite easy to provide trends against the key indicators in each group of activity. This would simply require a minor modification of the report's format.*

### **3.4.3 Comments on specific measures**

We provide the following comments on specific measures included in Council's 2011/12 service performance information. We believe that consideration of these would enhance the quality of the service performance information provided to the reader in the future.

- City Planning and Development – District Plan. The Level of Service is "The Christchurch City Plan is fully operative" and the target was "Both territorial sections of the District Plan are fully operative by 31 March 2012".

Although the Council reported that there are two minor outstanding issues which stopped the two sections of the District Plan being made fully operative, it made no disclosure on when it was likely to become operative.

- City Planning and Development – Energy Conservation. The Level of Service is “A programme is developed to contain increase in the amount of energy used in Christchurch (to reduce increase in energy use to +12.0% per year by 2014)”.

The Council could enhance the reported result by including the comparative for the prior year and disclosing progress made to achieve this by 2014.

- City Planning and Development – Energy Conservation. The Level of Service is “Programme developed to encourage an increase in the proportion of renewable energy used in the City (to 23% by 2014)”.

The reported result could have included comment on how high it was, and what has it dropped to currently. Also it could comment on how Council is progressing to achieve 23% by 2014.

- Community Support – Early Learning Centres. There is a target of “Provide 113,520 hours of childcare per annum Pioneer ELC”. The reported result was “Actual achieved 84,480 hours, 5.30am – 4.30pm Monday – Friday (except snow days)”.

The reported result could be enhanced with information as to why the target was not achieved and what is being done to rectify this.

- Community Support – Civil Defence Emergency Management. The reported result is “Recovery Plan needs review. All other plans are up to date.”

Comment could be included on when the Recovery Plan will be reviewed by.

- Community Support – Civil Defence Emergency Management. The target “Hazards and risks framework maintained at all times” was not achieved. However, there was no explanation provided to explain why it was not achieved, and what Council is doing to achieve it in the future.

- Parks, open spaces and waterways. The actual results for some targets state “contract specification met”.

We believe that such a comment does not provide the reader with sufficient information because the reader does not have any information on what the contract specifications are. It is important that comments are provided that tell a performance story.

In order to avoid meaningless measures, we recommend that in developing the next LTP, Council reduces the number of targets but make them meaningful and specific so that actual performance can be reported.

### **Management comment**

*The 2011/12 Annual Report contains targets that were largely built and approved in June of 2011. At that time a great many earthquake-related issues were still unknown –*

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*as examples, there was no knowledge of which Council facilities would be closed due to unseen EQ damage, or what the programme of work for the central city activity should contain (the CCDU blueprint did not exist at the time.)*

*Most, if not all of the issues cited above stem from this. However it is acknowledged that some areas did not provide an adequate response explaining the change of circumstances around their target.*

*This feedback will be provided to each manager concerned, along with a reminder that this is not an appropriate level of response for future reports.*

*Fortunately this list makes up a very small percentage of all CCC measures and targets.*

### **3.5 Possible LTCCP amendments**

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

No amendments were identified. We had discussions with Council staff during the 2012/13 annual plan process and identified that there were some major capital building projects being considered, and for which some consultation and engagement was held with the community. Although these were not considered amendments, they will be a key component of the next LTP.

### **3.6 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.

Council has an active and effective internal audit function that considers significant fraud risk as part of the development of the audit plan. Work performed in 2011/12 included a review of transactions, activities and locations. This included a review of cash collection points which is performed annually.

### **3.7 Severance payments**

We reviewed a number of severance payments that occurred during the year with a focus on settlements which could be seen to be excessive or unusual.

We found that payments made were reasonable and appropriately approved.

### **3.8 Conflicts of interest**

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

We noted no instances for your attention.

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### **3.9 Treaty settlements and co-management**

We have not been made aware of any new treaty settlements or co-management arrangements that impact on the Council.

### **3.10 Funding arrangements and procurement**

Council has drafted a comprehensive Procurement Policy. Once ratified, a Procurement Strategy and set of Guidelines will be developed by March 2013. We will review this in our 2012/13 audit.

### **3.11 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.

We noted no issues.

### **3.12 Public Private Partnerships (PPPs)**

We ascertained if Council has, or is planning to enter into, any PPPs. We are not aware of any such intentions.

## **4 Details of reviews on behalf of the Auditor-General**

We completed the reviews required by the Auditor-General, as set out in our audit arrangements letter, and cleared them with appropriate members of your management team. Appendix 3 sets out the results of the reviews. There are no issues that need to be brought to your attention.

## Appendix 1: Uncorrected misstatements

### Parent

There were no parent uncorrected misstatements.

### Group

Current year misstatements	Assets	Liabilities	Equity	Statement of Financial Performance
	\$(000)	\$(000)	\$(000)	\$(000)
	Dr (Cr)	Dr (Cr)	Dr (Cr)	Dr (Cr)
Estimated impact on CCC group of non-consolidation of Gardens Event Trust.	70	(70)	0	0
Estimated impact on CCC group of non-consolidation of Canterbury Development Corporation.	3,533	(1,056)	(3,604)	(1,127)
<b>Total group</b>	<b>3,603</b>	<b>(1,126)</b>	<b>(3,604)</b>	<b>(1,127)</b>

These misstatements were not corrected as they are considered to be immaterial to the financial statements.

## Appendix 2: Status of recommendations made last year

### Outstanding matters

Matter	Recommendation	Outcome and status
Funding arrangements and procurement	Consideration is given to develop a more formalised procurement strategy and contract management system to ensure that value-for-money and cost efficiencies within procurement are maximised.	<p><i>In progress.</i></p> <p>Council has drafted a comprehensive Procurement Policy. Once ratified, a Procurement Strategy and set of Guidelines will be developed by March 2013.</p> <p><b>Management comment</b></p> <p><i>Council has ratified a comprehensive Procurement Policy. A set of guidelines will be developed by June 2013.</i></p>
Sensitive expenditure policies	<p>Council give consideration to developing additional sensitive expenditure policies outlined in the Auditor-General's good practice guidance:</p> <ul style="list-style-type: none"> <li>• tipping</li> <li>• sale of surplus assets to staff;</li> <li>• farewell and retirement gifts; and</li> <li>• sponsorship of staff and others.</li> </ul>	<p><i>Partly addressed</i></p> <p>Tipping – considered not significant as this is not common in New Zealand.</p> <p>Sale of surplus assets to staff – no policy has been developed for this.</p> <p>Farewell and retirement gifts – development of this policy was put on hold due to the earthquakes. This policy is expected to be completed by December 2012.</p> <p>Sponsorship of staff and others – considered not significant.</p>
Payroll – independent review of masterfile changes	Independently review all masterfile changes and retain evidence of the review.	<p><i>Outstanding</i></p> <p>This remains outstanding. We will follow this up in our 2012/13 audit.</p>

<b>Matter</b>	<b>Recommendation</b>	<b>Outcome and status</b>
Expenditure – masterfile changes	A masterfile changes report be produced and independently reviewed periodically.	<p><i>Outstanding.</i></p> <p>This remains outstanding. We will follow this up in our 2012/13 audit.</p> <p><b>Management comment</b></p> <p><i>The changes report is produced and updated for bank account changes only. A report on the remaining masterfile changes is not available.</i></p>
Bonds payable account	Monitor and clear out the bonds payable account on a regular basis.	<p><i>Outstanding</i></p> <p>Council has a process for reviewing private work bonds over 10 years old.</p> <p>However, in discussions for the year-end balance, we identified that there has not been a review performed of all bonds over ten years old. We understand this is something Council will look to undertake in the future.</p> <p><b>Management comment</b></p> <p><i>It is our understanding that all bonds were reviewed, but that there are several where we are waiting for the Subdivision and Consenting team to provide answers. These will be followed up again early in 2013.</i></p>

Matter	Recommendation	Outcome and status
<p>IS – Procurement policy</p>	<p>Once the Council's procurement policies are in place, a review of all existing IMCT procurement practices and contracts with vendors and contractors should be performed to ensure that they comply with the Council's procurement practices.</p> <p>The current procurement process for IMCT is that all projects over the IMCT financial delegated amounts are subject to the CCC procurement process. The absence of an approved procurement policy has been raised in previous year, and the current status is that the Council has a draft procurement policy that is due to be tabled with the Council by the end of May 2012.</p> <p>There is no vendor management policy within IMCT, and no formalised procedures for procurement of services below \$50,000.</p> <p>Without formal procurement procedures being followed, the Council may be at risk of inappropriate expenditure or paying for services which do not meet the best interest of the Council.</p>	<p><i>Partly addressed</i></p> <p>IMCT has now appointed a permanent Assets &amp; Contracts Specialist who is working through and monitoring procurement practices and will also take notice of the outputs from the Comprehensive Procurement Policy to ensure a pan-Council consistency to procurement policy/guidance/practices.</p> <p>This recommendation remains outstanding and will be reviewed as of part of the IS audit in 2012/13.</p> <p><b>Management comment</b></p> <p><i>All IS procurement is performed in line with the Council procurement policy.</i></p>

<b>Matter</b>	<b>Recommendation</b>	<b>Outcome and status</b>
<p>IS – SAP elevated user access account</p>	<p>The Council should review the current 'SAPALL' user needs as this is the most powerful ID with the user having full unrestricted access to the entire application. Use of such access rights should be restricted as much as possible or alternatively only granted when required and the Council needs to ensure that staff that have access require this level of access in order to perform their job.</p> <p>We noted in the previous year that there is one user with SAPALL access. This is the ultimate level of access allowed within SAP and we recommended a review was completed to determine if this level of access was still required. In our recent review we noted that this has not been actioned and the account is still active.</p>	<p><i>Outstanding</i></p> <p>This remains outstanding and will be reviewed as of part of the IS audit in 2012/13.</p> <p><b>Management comment</b></p> <p><i>All SAP access has been removed and is granted only as required.</i></p>

Matter	Recommendation	Outcome and status
<p>IS – data classification</p>	<p>The Council should establish a data classification scheme that would be applicable both to data stored in IT systems, data distributed as electronic reports and paper documents. The scheme should also describe the guidelines for handling and distribution of data depending on its classification.</p> <p>We noted in the previous year that IMCT's current policy on the distribution and retention of data is in line with the Council's Retention and Disposal Policy that was agreed in 2009. Currently IMCT has not implemented any data classification scheme that would consider data confidentiality. Additionally, no guidelines are established that would regulate distribution of data based on its confidentiality. In our recent review we were unable to see any progress on this.</p>	<p><i>Outstanding</i></p> <p>This remains outstanding and will be reviewed as of part of the IS audit in 2012/13.</p> <p><b>Management comment</b></p> <p><i>IM governance framework is currently being developed, and is due for completion by the end of March 2013.</i></p>
<p>Accounting for retirement gratuities</p>	<p>An independent actuarial valuation of the unvested retiring gratuities and long service leave liability be performed next year.</p>	<p><i>Outstanding</i></p> <p>An independent valuation was not obtained in 2011/12.</p> <p><b>Management comment</b></p> <p><i>We do not intend to seek an independent actuarial valuation. It is our view that the sum involved is not material, and is becoming less so each year.</i></p>

## Cleared matters

Matter	Recommendation	Outcome and status
P-Card expenditure	<p>The P-Card policies around the timely coding, verification and approval of P-Card expenditure prior to payment are met.</p> <p>Supporting documentation or narration is provided on what the business purpose of the expenditure was.</p>	<p><i>Cleared</i></p> <p>The Payments and Payroll Team Leader who administers P-Cards, follows up the coding and approval of P-Card expenditure within one month.</p> <p>This will be reviewed as part of our audit testing in 2012/13.</p>
GRNI (Goods received but not invoiced) account	<p>Monitor and clear out the GRNI (GL 20500) account on a regular basis.</p>	<p><i>Cleared</i></p> <p>The GRNI account has been reconciled in September and November 2011, and February, March, April, May and June of 2012.</p> <p>All amounts over three months old were reviewed. At year end only \$19,684 of \$7,248,615.32 related to GRNI older than three months.</p> <p>We noted that not all of the reconciliations had been signed off as prepared and/or reviewed.</p>
Review of credit notes	<p>Perform a regular independent review of credit notes raised in the system.</p>	<p><i>Cleared</i></p> <p>Since July 2012 the review is being undertaken by the Receivables and Banking Team Leader who has a folder in which credit notes are stored and she reviews all significant credit notes issued.</p>

<b>Matter</b>	<b>Recommendation</b>	<b>Outcome and status</b>
<p>IS - Lack of security incident process</p>	<p>The Council should develop a security incident process that is available to all staff. All security incidents should be reported in a consistent manner and registered. The list of open security incidents should be regularly reviewed and employees participating in the resolution should be reminded to update the status once it is resolved. Additionally, the Council should ensure all security incidents are registered to enable statistics and trend analysis.</p>	<p><i>Cleared</i></p> <p>A Security Group has been set up with the first meeting held on 17 July 2012. The group meets on a monthly basis. The group has established a charter which includes as its deliverables:</p> <ul style="list-style-type: none"> <li>• Recommendations on what security policies the organisation should have and the order in which they need to be delivered.</li> <li>• Recommendations around how the organisation can meet its operational and statutory obligations with reference to IT security.</li> <li>• Recommendations around managing IT security risk and issues.</li> </ul>

## Appendix 3: Details of reviews on behalf of the Auditor-General

Issue	Status/findings
Annual Report adoption and public release dates	We have advised the OAG of the dates that the Council adopted its annual report and made the full and summary annual reports available to the public.
Local Authority exemptions for Council Controlled Organisations (CCOs)	<p>The OAG asked us to advise on the 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>We found that during 2011/12, the Council did not issue any exemptions, or renew any existing exemptions, for small dormant CCOs.</p>
Local Authorities emissions and measurement and reduction	<p>We gathered information about the activities of local authorities in the area of emissions measurement and reduction. We confirmed that Council is measuring its gas emissions and considers the impact on Council. Council measures direct energy emissions and has various plans in place to reduce greenhouse gas emissions. These include the Climate Smart Strategy, and Sustainable Energy Strategy.</p> <p>We will forward this information to the OAG.</p> <p>We also noted that Council earns carbon credits from the Burwood landfill. As at balance date, Council had carbon credits to the value of \$975,000 on its balance sheet.</p>
Insurance of assets by public entities	We collected information on behalf of the Auditor-General relating to insurance within the public sector. Specifically this information related to the extent of insurance cover in place for property, plant and equipment assets and the extent of changes in managing insurance risks for those assets in recent years.
Management of significant assets by public entities	<p>We collected information on Council's management of significant physical assets. This included the condition of significant assets, how well maintained they are, whether or not enough is being spent on them to renew them and the adequacy of checking and reporting on them.</p> <p>Clearly, in the Council's case, the information collected has had to consider the significant impact of the earthquakes on Council's assets.</p>

**4. RESOLUTION TO EXCLUDE THE PUBLIC**

Attached.

29. 5. 2013

**AUDIT AND RISK MANAGEMENT SUBCOMMITTEE**  
**RESOLUTION TO EXCLUDE THE PUBLIC**

*Section 48, Local Government Official Information and Meetings Act 1987.*

I move that the public be excluded from the following parts of the proceedings of this meeting, namely items 5 to 9.

The general subject of each matter to be considered while the public is excluded, the reason for passing this resolution in relation to each matter, and the specific grounds under Section 48(1) of the Local Government Official Information and Meetings Act 1987, for the passing of this resolution are as follows:

GENERAL SUBJECT OF EACH MATTER TO BE CONSIDERED	REASON FOR PASSING THIS RESOLUTION IN RELATION TO EACH MATTER	GROUND(S) UNDER SECTION 48(1) FOR THE PASSING OF THIS RESOLUTION
5. INTERNAL AUDIT ACTIVITY REPORT	) GOOD REASON TO ) WITHHOLD EXISTS ) UNDER SECTION 7	SECTION 48(1)(a)
6. QUARTERLY PROCUREMENT REPORT - QUARTER THREE, 2012/13	) ) ) )	
7. LEGAL ADVICE ON EARTHQUAKE RELATED MATTERS	) ) ) )	
8. BUILDING CONSENTS – EARTHQUAKE RELATED CLAIMS	) ) ) )	
9. VERBAL UPDATE ON LEGAL ISSUES	) ) ) )	

This resolution is made in reliance on Section 48(1)(a) of the Local Government Official Information and Meetings Act 1987, and the particular interest or interests protected by Section 6 or Section 7 of that Act which would be prejudiced by the holding of the whole or relevant part of the proceedings of the meeting in public are as follows:

ITEM	REASON UNDER ACT	SECTION	PLAIN ENGLISH REASON	WHEN REPORT CAN BE RELEASED
5.	Prevent improper advantage	7(2)(j)	Prevent the disclosure or use of information for improper gain or advantage	Once the report has been signed off or updated as advised by the Subcommittee
6.	Prejudice commercial position	7(2)(b)(ii)	Would be likely to unreasonably prejudice the commercial position of the supplier	Never
6.	Commercial Activities	7(2)(h)	Enable Council to carry out commercial activities without prejudice or disadvantage	
6.	Conduct of negotiations	7(2)(i)	Enable Council to carry on negotiations without prejudice or disadvantage	

ITEM	REASON UNDER ACT	SECTION	PLAIN ENGLISH REASON	WHEN REPORT CAN BE RELEASED
6.	Prevent improper advantage	7(2)(j)	Prevent disclosure for improper gain or advantage	
7.	Maintain legal privilege	7(2)(g)	The report provides legal advice on potential legal risks arising as a result of the collapse of the CTV building.	Following the conclusion of legal proceedings (if any) relating to the collapse of the CTV building.
8.	Maintain legal privilege	7(2)(g)	The report provides legal advice relating to the risk of earthquake related claims by building owners/insurers against the Council as the building consent authority.	Cannot be released while there remains a potential for claims to be made against the Council in relation to its role as building consent authority for earthquake damaged / demolished buildings.
9.	Maintain legal privilege	7(2)(g)	Legal advice to be provided in confidence to the Subcommittee	

**Chairperson's**

**Recommendation:** That the foregoing motion be adopted.

**Note**

Section 48(4) of the Local Government Official Information and Meetings Act 1987 provides as follows:

- “(4) Every resolution to exclude the public shall be put at a time when the meeting is open to the public, and the text of that resolution (or copies thereof):
- (a) Shall be available to any member of the public who is present; and
  - (b) Shall form part of the minutes of the local authority.”