

Report on Local Government 2017

20 APRIL 2018



NEW SOUTH WALES AUDITOR-GENERAL'S REPORT

FINANCIAL AUDIT

THE ROLE OF THE AUDITOR-GENERAL

The roles and responsibilities of the Auditor-General, and hence the Audit Office, are set out in the *Public Finance and Audit Act 1983* and the *Local Government Act 1993*.

We conduct financial or 'attest' audits of State public sector and local government entities' financial statements. We also audit the Total State Sector Accounts, a consolidation of all agencies' accounts.

Financial audits are designed to add credibility to financial statements, enhancing their value to end-users. Also, the existence of such audits provides a constant stimulus to entities to ensure sound financial management.

Following a financial audit the Audit Office issues a variety of reports to entities and reports periodically to parliament. In combination these reports give opinions on the truth and fairness of financial statements, and comment on entity compliance with certain laws, regulations and government directives. They may comment on financial prudence, probity and waste, and recommend operational improvements.

We also conduct performance audits. These examine whether an entity is carrying out its activities effectively and doing so economically and efficiently and in compliance with relevant laws. Audits may cover all or parts of an entity's operations, or consider particular issues across a number of entities.

As well as financial and performance audits, the Auditor-General carries out special reviews and compliance engagements.

Performance audits are reported separately, with all other audits included in one of the regular volumes of the Auditor-General's Reports to Parliament – Financial Audits.



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In accordance with section 421C of the *Local Government Act 1993*, I present a report titled
'Report on Local Government 2017'.

A handwritten signature in black ink, appearing to read 'Margaret Crawford'.

Margaret Crawford

Auditor-General
20 April 2018

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Report on Local Government 2017

This report analyses the results of the financial statement audits of NSW councils in 2016–17.



Auditor-General's foreword

Under section 421C of the *Local Government Act 1993*, I am pleased to present our first report on the statutory financial audits of councils, to NSW Parliament.

My appointment as the auditor of local government in New South Wales is the most significant change to the Auditor-General's mandate in nearly three decades.

Moving to the new audit arrangements over the past 18 months has been challenging but rewarding. It has confirmed my appreciation of local government – a sector passionate about the community and focused on delivering local services.

The unique relationship each council has with its community differentiates it from other tiers of government.



Our audits

I am pleased to report that we completed 139 out of 140 financial statement audits for the 2016–17 audit cycle. The remaining council received an extension to lodge its financial statements.

We have also released a performance audit report on council reporting on service delivery. We will soon release another report on fraud controls in local councils and a report on council shared services later this year.

While the new audit mandate brings immense responsibility, my office has embraced the challenges involved and the objectives that NSW Parliament gave us:

- strengthening governance and financial oversight in local government
- providing greater consistency in external audit
- ensuring reliable financial information is available to assess council performance
- improving financial management, fiscal responsibility and public accountability in how councils use citizens' funds.

This report

This report is rich in data extracted from the results of the 2016–17 financial audits. For the first time, it presents a consistent view of financial performance across the New South Wales local government landscape. The report also provides guidance and includes recommendations to councils and the Office of Local Government aimed at strengthening financial reporting, asset management, governance and internal controls.

The report will help NSW Parliament understand the common challenges that councils face. It provides points of comparison for councils and signposts matters that will be the focus of future audits. Importantly, this report and the data visualisation that accompanies it, provides comprehensive and accessible information to citizens regarding the management and performance of their councils.

I would like to acknowledge the cooperation of councils throughout the audit process and our partnerships with the contract audit firms that helped us to deliver the audits. Together we can learn from each other and work towards improving outcomes for the community.



Executive summary



1. Introduction

Local government sector

NSW has 140 councils: 128 local councils serving a geographic area and 12 county councils formed for a specific purpose.

We completed audits of 139 councils' 2016–17 financial statements and eight councils' 2015–16 financial statements. Bayside Council received a lodgement extension from the Office of Local Government (OLG) and has not yet presented their 2016–17 financial statements for audit.

Service delivery

Each council provides a range of services, influenced by population density, demographics, the local economy, geographic and climatic characteristics. These differences influence the financial profile of councils.



2. Financial reporting

Quality of financial reporting

The overall quality of financial reporting needs to improve:

- we issued modified (qualified) audit opinions on the financial statements of three councils in 2016–17 and one council and one water authority in 2015–16
- we reported 39 significant matters to 29 councils. They related to material accounting issues and significant deficiencies in internal controls
- twenty-two councils required material adjustments to correct errors in previous audited financial statements
- moderate risk issues were identified in financial statement preparation processes for 43 councils.

OLG guidance for council year-end financial reporting needs to align with Australian Accounting Standards and be issued earlier.

Timeliness of financial reporting

Timeliness of financial reporting needs to improve. Forty councils required lodgement extensions past the 31 October 2017 statutory reporting deadline.



3. Financial performance and sustainability

Operating revenue

Eighteen councils operating expenses exceed current operating revenue.

Fifty-nine councils do not meet OLG's target of 60 per cent for own source operating revenue.

Liquidity and working capital

Most councils have sufficient liquidity and working capital. However, there are indicators that:

- three councils may not have the ability to meet short-term obligations as measured by the unrestricted current ratio
- two councils may not have sufficient operating cash available to service debt as measured by the debt service cover ratio
- eighteen councils do not meet the OLG benchmark for the collection of rates and annual charges
- five councils may not have sufficient cash to continue paying expenses without additional cash inflows as measured by the cash expense cover ratio.

Asset management measures

Reporting against OLG's asset management performance measures highlights that councils need to consider whether spending on existing infrastructure assets is sufficient to ensure they continue to meet service delivery standards:

- seventy councils are not renewing assets in line with the rate of their depreciation
- eighty-four councils did not meet OLG's benchmark for managing the infrastructure maintenance backlog
- seventy-one councils are not maintaining their assets in accordance with their asset management plans.



4. Asset management

High risk issues

We reported ten high risk issues relating to councils' asset management and accounting practices.

Asset reporting

The accuracy of asset registers requires improvement and all assets need to be reported in the financial statements.

At 30 June 2017, 62 councils did not record all rural fire-fighting equipment in their financial statements. A large proportion of rural fire-fighting equipment is not reported in either State government or local government financial statements.

Asset valuation

We reported seven high risk matters related to asset valuations, including two that resulted in qualified audit opinions.

Asset useful life estimates

We identified that accounting for the useful lives of similar assets varied across councils, resulting in variable depreciation expense for these assets.

In addition, the useful lives of assets need to be reviewed annually. This review should be supported by current condition assessments.

Asset policy and planning

Thirteen councils do not have an asset management strategy, policy and plan, as required by the Office of Local Government's Integrated Planning and Reporting Framework.



5. Governance and internal controls

High risk issues

We reported 17 high risk issues relating to governance, financial accounting, purchasing and payables and payroll matters.

Governance

There is currently no requirement for councils to have an audit, risk and improvement committee and internal audit function. Consequently, 53 councils do not have an audit committee and 52 councils do not have an internal audit function.

The Office of Local Government has incomplete information on the number of entities established by councils. There is no financial reporting framework for the variety of entities established by councils.

Councils can strengthen policies and procedures to support critical business processes, practices for risk management and compliance with key laws and regulations.

Internal controls

Councils can improve internal controls over manual journals, reconciliations, purchasing and payables and payroll.



6. Information technology

High risk issues

We reported nine high risk issues relating to information technology.

Access to IT systems

Controls over user access to IT systems need to be strengthened.

Information Technology governance

IT governance benefits from appropriate policies, standards and guidelines across all critical IT processes. We identified that:

- around one in four councils do not have an IT strategy or operational plan
- half of NSW councils have an IT security policy
- seventeen councils do not have a documented plan to recover from a disaster.



1. Introduction

The Auditor-General has the mandate under the *Local Government Act 1993* to audit the NSW local government sector. One-hundred and thirty-nine councils presented their 2016–17 financial statements and eight councils also presented their 2015–16¹ financial statements for audit. These audits have been completed. The Office of Local Government (OLG) granted Bayside Council an extension until 31 May 2018 to lodge their 2016–17 financial statements and Bayside Council has not yet presented them for audit.

We also tabled a performance audit report on ‘Council reporting on service delivery’ on 1 February 2018. We will soon release a report on ‘Fraud controls in local councils’ and a report on ‘Council shared services’ later this year.

This report focuses on the results of our financial audits, highlights issues that were common across the local government sector and provides guidance that councils should consider. This will help Parliament understand the challenges that councils face and the measures that can improve their financial management and reporting.

Each council provides a range of services to meet its communities’ needs

New South Wales has 128 local councils servicing a geographic area, and 12 county councils formed for specific purposes, such as supplying water, managing flood plains or eradicating noxious weeds. Each council provides a range of services, influenced by population density, demographics, the local economy, geographic and climatic characteristics. These differences also influence the spending profile of metropolitan, regional and rural councils.



2. Financial reporting

Each year, councils lodge their audited financial statements with OLG and publish them on their website. Council financial statements capture their financial activities, performance and position.

We issued five modified (qualified) audit opinions and identified a range of material financial reporting errors and significant accounting and control issues

We issued unmodified audit opinions on the financial statements of:

- one-hundred and thirty-six out of 139 councils for 2016–17
- two water authorities for 2016–17
- seven out of eight councils for 2015–16
- two out of three water authorities for 2015–16.

An unmodified audit opinion means that the financial statements present fairly the financial position and performance of the council. The Hills Shire Council, Junee Shire Council and Yass Valley Council received modified (qualified) audit opinions for 2016–17. We also issued disclaimers of opinion for the City of Botany Bay Council and Gosford Water Authority for 2015–16.

Our audits identified a further 33 material errors in the previous years’ audited financial statements of 22 councils that have been corrected. Eighty-eight per cent of these errors related to the way councils account for and value assets.

We also reported 39 significant matters to 29 councils. These related to material accounting issues and internal control weaknesses, of which 77 per cent related to assets. Councils should improve the way they account for their assets as a priority.

¹ The Auditor-General was appointed statutory auditor of eight councils for the 2015–16 reporting period due to the following reasons:

- specific request of councils
- failure by councils to appoint an auditor
- inability of the previous auditor to complete the audit due to external investigation
- auditor retirement.

Chapter 4 of this report further discusses the asset accounting issues identified during our audits.

Councils can improve their financial reporting processes

Our audits found that 43 councils need to improve the way they prepare their financial statements. A more robust review of the financial statements by councils prior to submitting them for audit would improve both quality and timeliness.

Recommendation

Councils can improve the quality of financial reporting by reviewing their financial statements close processes to identify areas for improvements.

Our experience at the State level shows that the preparation of annual financial statements benefits from review by independent audit committees.

Councils are not currently required to have an audit, risk and improvement committee and consequently 53 councils do not have an audit committee. For those councils with an audit committee, 55 per cent play no role in the review of financial statements.

Amendments made to the *Local Government Act 1993* by the *Local Government Amendment (Governance and Planning) Act 2016* will require all councils to appoint an audit, risk and improvement committee. Under transitional provisions, councils will not be required to comply until March 2021, six months after the next ordinary election.

Recommendation

Councils can improve the quality of financial reporting by involving an audit, risk and improvement committee in the review of financial statements.

OLG can improve the quality and timeliness of guidance provided to councils each year

The Office of Local Government (OLG) needs to release key guidance documents, such as the Local Government Code of Accounting Practice and Financial Reporting (Code) and end of year financial reporting circular, to councils earlier.

Councils are required to prepare financial statements in accordance with Australian Accounting Standards and the Code. The Code applicable for 2016–17 financial reporting provided options and guidance that in some instances did not align with Australian Accounting Standards.

Recommendation

The Office of Local Government should release the Local Government Code of Accounting Practice and Financial Reporting and the End of Year Financial Reporting Circular earlier in the audit cycle, ideally by 30 April each year.

The Local Government Code of Accounting Practice and Financial Reporting should align with Australian Accounting Standards.

Seventy-one per cent of councils lodged audited financial statements by the statutory deadline

Councils must lodge audited financial statements with OLG by 31 October each year, that is, within four months after the end of their financial year. Forty councils did not meet this deadline for their 2016–17 financial statements and required an extension from OLG. Bayside Council received a lodgement extension for their 2016–17 financial statements to 31 May 2018 and has not yet presented them for audit.

Early close procedures help to improve the quality and timeliness of financial reporting

Early close procedures can identify issues and key risk areas that councils need to consider and resolve before the year-end process. Asset valuation issues affected the quality and timeliness of many councils' financial statements in 2016–17. Completing infrastructure, property plant and equipment valuations is a key early close procedure that can improve the quality and timeliness of financial reporting.

Recommendation

The Office of Local Government should introduce early close procedures with an emphasis on asset valuations.



3. Financial performance and sustainability

Our next chapter reviews the financial performance of councils using indicators that the OLG prescribe. Councils must report against these in their audited financial statements:

- operating performance
- own source operating revenue
- unrestricted current ratio
- debt service cover ratio
- rates and annual charges outstanding percentage
- cash expense cover ratio.

Councils' annual reports also include the unaudited Special Schedule 7 'Report on Infrastructure Assets', in which councils report performance against four further measures:

- building and infrastructure renewals ratio
- infrastructure backlog ratio
- asset maintenance ratio
- cost to bring assets to agreed service level.

Three rural councils did not meet OLG benchmarks for three audited performance measures

Most councils met OLG benchmarks for at least five or all of the six audited performance measures. Eight rural, four regional, four metropolitan and two county councils did not meet OLG's benchmarks for two out of the six audited performance measures. Three rural councils did not meet OLG's benchmarks for three out of the six audited performance measures.

Eighteen councils operating expenses exceed their revenue base

The first measure of financial sustainability looks at the operating revenue that councils raise to cover their operating expenses. Eighteen councils operating expenses exceed their revenue base. For 11 councils, this has been the case for the past three years. Another 20 councils would not have met the operating performance benchmark without the advance receipt of their 2017–18 financial assistance grant, which was recorded as revenue during 2016–17.

Fifty-nine councils did not meet the OLG benchmark for generating own source revenue

Councils are also expected to generate 60 per cent of their revenue from their own sources. Fifty-nine councils did not meet this OLG benchmark, and 42 of these were rural councils. Rural councils have high-value infrastructure assets that cover large areas, with smaller populations and less capacity to raise revenue from alternative sources compared with metropolitan councils.

Most councils have sufficient liquidity and working capital

All but three councils met OLG's benchmark for the unrestricted current ratio, meaning the councils can meet short-term obligations as they fall due.

Most councils also have the capacity to cover more than three months of operating expenditure as measured by the cash expense cover ratio. However, some of the funds held by councils are restricted and should only be used for specific purposes.

A council with a high proportion of restricted funds may have limited flexibility to pay operating expenses. While a council can resolve to lift internal restrictions on funds to use them for a different purpose, the Minister for Local Government's approval is required to use externally restricted funds for another purpose.

All but two councils met OLG's debt service cover ratio benchmark

The debt service cover ratio measures the operating cash available to service debt. All but two councils met OLG's benchmark of greater than two times. This was due to these two councils repaying borrowings early.

One-hundred and twenty-three councils reported borrowings at 30 June 2017. Councils utilise borrowings to fund capital projects and to address backlog maintenance. Regional councils accounted for 56 per cent of the value of total council borrowings because they also borrow to manage water and sewerage infrastructure.

Eighteen councils did not meet OLG's benchmark for collecting rates and annual charges

Most councils are collecting rates and annual charges levied. However, eight rural, five regional, three metropolitan and two county councils did not meet the benchmark of having less than five per cent (metropolitan) or ten per cent (regional, rural and county) of rates and charges outstanding. These eighteen councils also did not meet the infrastructure backlog ratio.

Many councils did not meet OLG's benchmarks for renewing and maintaining infrastructure assets

The infrastructure asset indicators reported by councils suggest that many need to examine their asset management plans and consider whether investment in infrastructure assets is sufficient. Thirty-one councils reported they do not meet the OLG benchmarks for either the buildings and infrastructure renewals ratio, the infrastructure backlog ratio or the asset maintenance ratio. Individually:

- seventy councils reported that they are not renewing infrastructure assets at the same rate they are depreciating them
- eighty-four councils reported that they have not kept the infrastructure maintenance backlog below OLG's benchmark
- seventy-one councils reported actual asset maintenance lower than planned asset maintenance.



4. Asset management

NSW councils own and manage a significant range of assets, including infrastructure, property, plant and equipment with a value of \$136 billion. Many of our audit report qualifications, significant matters, prior-period errors and high risk issues related to assets.

Councils need to strengthen their asset registers

Our audits identified \$145 million worth of land and infrastructure assets at 24 councils that were not recorded in asset registers or the financial statements. This is in addition to the rural fire-fighting equipment not recorded by councils that is discussed in the following sections. We also found examples of multiple asset registers with conflicting information, inaccurate or incomplete registers and unreconciled registers.

Effective asset management requires accurate records of the assets that councils control. Council asset registers should accurately capture all assets to improve the quality and timeliness of financial statements. It is important that councils regularly update registers and reconcile them with asset management systems. Where manual spreadsheets are used to record asset details, suitable controls must be in place.

A large part of rural fire-fighting equipment is not reported in government financial statements

Our 2016–17 audits of the NSW local government sector noted that 46 councils did record vested rural fire-fighting equipment in their financial statements. However, 62 councils do not record similar rural fire-fighting assets in their financial statements. These councils are of the view that they do not control these rural fire-fighting assets used by the NSW Rural Fire Service.

NSW Treasury and the NSW Rural Fire Service are of the view that the NSW Rural Fire Service does not control rural fire-fighting equipment which has been vested in councils under the *Rural Fires Act 1997*. NSW Treasury and NSW Rural Fire Service consider that these assets are controlled by councils. The financial statements of the NSW Total State Sector and the NSW Rural Fire Service do not include these assets. Consequently, a large portion of rural fire-fighting assets are not reported in either State government or local government financial statements.

Recommendation

The Office of Local Government should address the different practices across the local government sector in accounting for rural fire-fighting equipment before 30 June 2018.

In doing so, the Office of Local Government should work with NSW Treasury to ensure there is a whole-of-government approach.

Asset valuation methods are not capturing asset values effectively

The Code requires that council assets reflect the fair value principles in Australian Accounting Standards.

Many significant issues arose in our audits because council asset revaluation processes were not robust. This affected both the quality and timeliness of the financial statements.

Our audits identified that ten councils overstated the fair value of land assets as their valuations did not take into account external restrictions on community land or land under roads as required by the Code and Australian Accounting Standards. This was the reason for one-third of the material errors that needed to be corrected in councils' previous years' audited financial statements and for the qualified audit opinion issued on The Hills Shire Council's 2016–17 financial statements.

We also found multiple cases where councils did not adequately review valuation results, comply with applicable codes or obtain accurate valuations. This was the reason for the qualified audit opinion issued on Junee Shire Council's 2016–17 financial statements.

Councils need to improve their asset valuation processes by strengthening reviews, supporting valuations with robust documentation and commencing the revaluation process earlier in the financial year.

Considerable variability in the way councils report the useful lives of similar assets

We found considerable variability in the way councils reported the useful lives of similar assets in their financial statements. This in turn affects the depreciation expense recognised in councils' financial statements and the key performance indicators that councils report. The useful lives of all assets need to be reviewed annually using current asset condition assessments.

All councils should comply with OLG asset planning requirements

Sound asset management requires effective planning. All councils should meet the asset management planning requirements in OLG's Integrated Planning and Reporting Framework to help ensure they have a plan to manage assets efficiently over their life.

We found that 13 councils did not have an asset management policy, strategy and plan.



5. Governance and internal controls

Councils should prioritise high risk governance and control deficiencies

Our audits reported 17 high risk issues relating to policies and procedures, risk management, manual journals, reconciliations, purchasing and payables, and payroll processes. It is important to address high risk matters as a priority.

Councils can improve management oversight and governance structures

We found that councils can strengthen governance measures, by having audit committees and internal audit functions, policies and procedures for critical business processes, legislative compliance frameworks and risk management practices.

Councils are not currently required to have an audit, risk and improvement committee and consequently 53 councils do not have an audit committee. Proposed legislative changes will require all councils to appoint an audit, risk and improvement committee by March 2021.

Recommendation

Councils should early adopt the proposed requirement to establish an audit, risk and improvement committee.

An internal audit function is currently not a requirement for councils, and consequently, 52 councils do not have this function. In addition, the Office of Local Government (OLG) has not updated its Internal Audit Guidelines since they were issued in 2010.

Recommendation

The Office of Local Government should introduce the requirement for councils to establish internal audit functions and update its 2010 Internal Audit Guidelines.

The Office of Local Government's register of council entities is not complete

The *Local Government Act 1993* requires councils to obtain the consent of the Minister for Local Government before forming a corporation or any other entity², as defined under section 358(4) of the Act (referred to as a 'council entity'). OLG maintains a register of council entities for which ministerial approval has been sought. Our audit work concluded that the register that OLG maintains is not complete.

Recommendation

The Office of Local Government should maintain an accurate register of entities approved under section 358 of the *Local Government Act 1993*.

² Section 358(4) of the *Local Government Act 1993* defines entity as 'any partnership, trust, joint venture, syndicate or other body (whether or not incorporated), but does not include any such entity that is of a class prescribed by the regulations as not being within this definition'.

We also found that the *Local Government Act 1993* does not stipulate a financial reporting framework for council entities. As a result, there are disparate reporting and auditing practices for entities established across the sector.

Recommendation

The Office of Local Government should consider establishing a financial reporting framework for council entities.

Councils can strengthen policies and procedures to support business processes

Our audits identified two high risk instances in two councils where business and IT policies and procedures did not exist to support critical business and information technology processes. It is important that critical policies, standards and guidelines are available to staff and contractors to provide direction for the day-to-day operations of a council, promote consistency in processes, clarify roles and responsibilities and support compliance with laws, regulations and codes.

Councils can improve internal controls in business processes

Effective internal controls are important to help councils operate efficiently and effectively, to meet service delivery objectives, and to enable accurate and timely reporting.

We identified two high risk issues where councils had weak controls over manual journals. In one instance, this resulted in significant errors in the financial statements. Councils should independently review manual journals and prepare and review account reconciliations earlier.

We identified five high risk internal control deficiencies in the purchasing function relating to unauthorised expenditure, non-compliance with tendering guidelines and a significant breakdown of purchasing controls.

We noted one high risk internal control deficiency in the payroll function related to payroll staff having unrestricted access to amend sensitive payroll data in the system.



6. Information technology

Like many organisations, councils increasingly rely on information technology (IT) to deliver services and manage sensitive information.

Our audits reported nine high risk issues, predominantly related to inappropriate user access. Information technology deficiencies represented the highest number of issues we reported.

Controls over user access to IT systems need to be strengthened

User access controls reduce the risk of users having excessive access to critical financial systems and sensitive information. Our audits found many instances where user access controls were insufficient. These controls should ensure that individuals only have access to financial systems and data necessary to undertake their job responsibilities.

Our audits also found examples of users with inappropriate privileged access. In addition, we found instances of inadequate review and insufficient retention of access logs to monitor the activities of privileged system users. Privileged access occurs when a person can change key system configurations and has wide access to system data, files and accounts. We also identified external IT service providers with unrestricted privileged access to council systems and data.

It is important that councils strengthen user access administration to prevent inappropriate access. They should update user access roles in line with the responsibilities of a position and review the level of user access regularly. Councils also need to ensure their existing risk management framework provides assurance for controls over IT outsourcing, and strengthen controls where required.

We identified weaknesses in user developed applications (UDAs), which are developed or managed outside IT administration. This increases the risk of errors that may adversely affect the integrity and quality of information produced. Councils need to adequately control UDAs where they continue to use them and back up business-critical information.

Councils need to strengthen information technology governance

IT governance should be founded on:

- a fit-for-purpose IT strategy and operational plan
- appropriate policies, standards and guidelines across all critical IT processes.

We found that one in four councils do not have an IT strategy or IT operational plan and some need to develop or improve IT policies and procedures. Sixty-six councils do not have an adequate information security policy.

Seventeen councils also do not have a documented plan to recover from a disaster. Councils need to develop a plan and periodically review it. They also need to periodically test that they can restore backed-up data to ensure business continuity in the face of a system disaster.



1. Introduction

1.1 The local government sector

Local government is the third tier of government. It is established under State legislation, which defines the powers and geographical areas each council is responsible for.

Each council is a statutory corporation. Elected councillors form the governing body that directs council affairs in line with the *Local Government Act 1993* and Local Government (General) Regulations 2005.

Local councils deliver services and infrastructure to a geographic area. County councils are formed for specific purposes such as to supply water, manage flood plains or eradicate noxious weeds.

During 2016, the NSW local government sector was reduced from 166 to 140 councils, resulting in 128 local councils and 12 county councils. This was due to council amalgamations that formed 19 new councils on 12 May 2016 and one new council on 9 September 2016. Appendix four lists the former councils that were amalgamated into 20 new councils.

The table below shows the number of councils before and after amalgamations.

Council categories	Number of councils before amalgamations	Number of councils after amalgamations (as at 30 June 2017)
Metropolitan	38	34
Regional	48	37
Rural	66	57
County	14	12
Total	166	140

From 1 July 2017, two more county councils were dissolved. The functions of:

- Mid-Coast County Council were transferred into the newly formed Mid-Coast Council
- Southern Slopes County Council were transferred into the Yass Valley Council and the newly formed Hilltops Council.

This report includes the audit results of the 139 councils that have lodged their 2016–17 audited financial statements with the Office of Local Government, plus two water authorities. Bayside Council received a lodgement extension for their 2016–17 financial statements to 31 May 2018 and has not yet presented them for audit.

This report also includes the audit results of the 2015–16 financial statements of eight councils and three water authorities.

In preparing this report, the comments and analysis are drawn from:

- audited financial statements
- data collected from councils
- audit findings reported to councils
- data from external sources, including population, kilometres of roads, and council area data obtained from the Australian Bureau of Statistics and the Office of Local Government.

We have also classified councils into four groups – metropolitan, regional, rural and county. Further details are provided in Appendix three.

1.2 Service delivery

Councils invest significant resources each year to deliver a wide range of services to the community. These include waste collection, planning, child and family day care, and recreational services. Councils also build and maintain infrastructure, including roads, footpaths and drains, and enforce various laws.

Council services vary depending on community needs

While core functions, such as waste collection, are similar across councils, the range of services that each council provides varies greatly. The mix is influenced by population density, demographics, the local economy, geographic and climatic characteristics.

Spending on services

The following graphic shows the councils' expenditure by function in 2016–17.



a Categories are based on the Local Government Purpose Classifications issued by the Australian Bureau of Statistics.

b Appendix six provides further information on council expenditure by function.

Source: Audited financial statements for 2016–17. Excludes county councils.

In 2016–17, councils collectively reported expenditure of \$11.4 billion, of which:

- \$2.1 billion was for governance and administration, including corporate and support services, engineering works, council elections, meetings and policy-making committees, members' fees and expenses, subscriptions, public disclosures and legislative compliance.
- \$2.1 billion was for transport and communications, including sealed and unsealed roads, bridges, footpaths, parking areas and aerodromes.
- \$2.0 billion was spent on the environment, including waste management, sanitation and garbage, street cleaning, drainage and stormwater management, and environmental protection.
- \$1.7 billion was spent on recreation and culture, including public libraries, museums, art galleries, community centres, public halls and performing arts venues, sporting grounds and venues, swimming pools, parks, gardens and lakes.

Metropolitan councils service sixty-five per cent of the State's population in an area of 12,135 square kilometres (1.7 per cent of the total State area). Regional and rural councils provide water and sewerage services to communities outside areas covered by metropolitan water utilities. Rural councils maintain almost 60 per cent of all roads controlled by local government authorities.

Twelve county councils perform activities that typically span across a number of council areas, such as supplying water, managing flood plains and eradicating noxious weeds.

Audit Office performance audit report on how councils report on service delivery

On 1 February 2018, the Auditor-General tabled a performance audit report on 'Council reporting on service delivery'. It concluded that councils reported well on their outputs, but there are opportunities to improve reporting on outcomes, efficiencies and results against targets.

1.3 Council data visualisation

To aid access, transparency, and comparison of councils' financial statement data, we have created a data visualisation as part of this report, which is available on the Audit Office of New South Wales website. The visualisation presents revenue, expense, operating surplus, asset and liability data, along with key financial performance and sustainability indicators for each council. The 2016–17 financial statement data used in the data visualisation tool is summarised in Appendix nine and ten of this report.

The data visualisation also presents minimum, median and maximum values within selected council groupings. While these values aid in comparison and assist further inquiry, a good or bad performance conclusion cannot be drawn from this data alone.

The visualisation excludes financial statement data for four councils due to either an incomplete audit, or where our audit opinion on the councils' financial statements was modified (qualified).

The background of the image is a blurred financial document. The top half shows a spreadsheet with columns of numbers, some of which are formatted with commas as thousands separators. The bottom half shows a 3D bar chart with several bars of varying heights. Overlaid on the bottom right of the image is a white circle with a thin orange border.

Financial reporting



2. Financial reporting

Accurate and timely financial statements are an important element of sound financial management. They bring accountability and transparency to the way councils use public resources. Our financial audits assessed the following aspects of councils' financial reporting:

- quality of financial reporting
- timeliness of financial reporting.

Observation

Conclusion or recommendation

2.1 Quality of financial reporting

Qualified audit opinions

We issued unmodified audit opinions on the:

- 2016–17 financial statements of 136 councils and two water authorities
- 2015–16³ financial statements for seven councils and two water authorities.

The councils that received unmodified audit opinions prepared financial statements that fairly present their financial position and results.

We issued modified (qualified) opinions on the:

- 2016–17 financial statements of three councils
- 2015–16 financial statement of one council and one water authority.

Councils with modified opinions should address the issues that give rise to the audit qualification.

Significant audit matters

We reported 39 significant matters in 29 councils. They included material accounting issues and significant deficiencies in internal controls. Seventy-seven per cent of the matters related to assets.

Significant issues with the quality of financial reporting delayed the completion of a number of audits. Improving the reporting on assets should be a priority.

Prior period errors

We found 33 material errors worth \$9.1 billion in the previous audited financial statements of 22 councils. These all required prior-year audited balances to be corrected. Eighty-eight per cent of these were asset-related.

The high number of asset-related prior-period errors reinforces the need for councils to improve the way they value and account for assets.

Financial statements

We reported 43 moderate risk findings where councils can improve the way they complete their financial statements.

Of the councils that had an audit, risk and improvement committee, 55 per cent of these did not review the financial statements before audit.

Recommendation

Councils can improve the quality of financial reporting by reviewing their financial statements close processes to identify areas for improvements.

Recommendation

Councils can improve the quality of financial reporting by involving an audit, risk and improvement committee in the review of financial statements.

³ The Auditor-General was appointed statutory auditor of eight councils for the 2015–16 reporting period at the specific request of councils, due to the failure by councils to appoint an auditor, or the inability of the previous auditor to complete the audit due to external investigation or auditor retirement.

Observation	Conclusion or recommendation
<p>OLG guidance</p> <p>To support councils in preparing 30 June 2017 financial statements, OLG issued guidance documents in June 2017 and September 2017. This limited the time councils had to prepare financial statements in the prescribed form and resolve financial reporting and audit issues.</p> <p>The Code applicable for the 2016–17 financial reporting period provided options and guidance that in some instances did not fully align with Australian Accounting Standards.</p>	<p>Recommendation</p> <p>The Office of Local Government should release the Local Government Code of Accounting Practice and Financial Reporting and the End of Year Financial Reporting Circular earlier in the audit cycle, ideally by 30 April each year.</p> <p>Recommendation</p> <p>The Local Government Code of Accounting Practice and Financial Reporting should align with Australian Accounting Standards.</p>
<p>2.2 Timeliness of financial reporting</p>	
<p>Statutory deadlines</p> <p>One hundred councils submitted audited financial statements to OLG by the statutory deadline of 31 October 2017.</p> <p>Thirty-nine councils received reporting extensions up to 28 February, including 16 of the 20 newly amalgamated councils.</p> <p>Bayside Council received a reporting extension to 31 May 2018 and has not yet presented their financial statements for audit.</p>	<p>Councils need to improve their financial reporting processes in order to lodge their financial statements by the statutory reporting deadline.</p>
<p>Early close procedures</p> <p>Councils currently do not use early close procedures to resolve accounting issues before the end of the financial year.</p>	<p>Recommendation</p> <p>The Office of Local Government should introduce early close procedures with an emphasis on asset valuations.</p>

2.1 Quality of financial reporting

Three indicators help to assess the quality of councils' financial statements:

- modified and unmodified audit opinions
- significant matters reported to management and those responsible for the governance of a council
- prior-period errors.

While we issued unmodified audit opinions for most councils, the number of significant matters and prior period errors indicate that the overall quality of financial reporting requires improvement.

Asset valuation issues affected the quality of many councils' financial statements in 2016–17, and were the reason for:

- two modified (qualified) audit opinions
- most of the prior-period errors, significant matters and high risk matters reported.

Audit opinions

The key outcome of our audits is an independent audit report on the financial statements that councils must produce each year. We issue either a modified or unmodified opinion on these reports, which indicates whether councils' financial statements fairly present their financial position and performance.

We issued five modified (qualified) audit opinions

We issued modified audit opinions on the:

- 2016–17 financial statements of three councils
- 2015–16⁴ financial statements of one council and one water authority.

The following tables explain the reasons for our modified audit opinions.

Council	Reason for modified audit opinion on the financial statements
2016–17 financial statements	
The Hills Shire Council	The method used by council to value land under roads did not appropriately reflect external restrictions on the use of this land as required by Australian Accounting Standards.
Junee Shire Council	Council could not demonstrate that roads, bridges, footpaths and bulk earthworks were reported at fair value, as it did not value these asset classes during the year. The last valuation was conducted in 2012.
Yass Valley Council	Council did not record the receipt of financial assistance grants from the Australian Government as revenue in the year received, as required by Australian Accounting Standards.
2015–16 financial statements	
City of Botany Bay Council	Significant breakdowns in administrative, financial and governance internal controls affected the reliability of financial reporting of the former Council. A significant fraud involving former management was also identified in the reporting period. Consequently, councillors and management were unable to provide written representation that the financial statements present fairly the financial performance and position of the Council. As a result, Australian Auditing Standards require a disclaimer of opinion to be issued.
Gosford Water Authority	Management could not confirm it had recorded all transactions in the financial statements due to control weaknesses in the Authority's finance system.

In addition, one council received an unmodified audit opinion on its 2016–17 financial statements, that also emphasised an important matter.

Council	Reason for the emphasis of matter in the unmodified audit opinion
2016–17 financial statements	
Central Darling Shire Council	It was uncertain if the council could continue operating without using restricted water and sewer funds. Using externally restricted funds for other purposes requires Ministerial approval under the <i>Local Government Act 1993</i> . Ministerial approval was not obtained.

We issued unmodified audit opinions for the remaining:

- 136 councils and two water authorities on the 2016–17 financial statements
- seven councils and two water authorities on the 2015–16 financial statements.

⁴ The Auditor-General was appointed statutory auditor of eight councils for the 2015–16 reporting period at the specific request of councils due to the failure by councils to appoint an auditor, or the inability of the previous auditor to complete the audit due to external investigation or auditor retirement.

We are yet to issue an audit opinion on Bayside Council's 2016–17 financial statements.

Council	Approved lodgement extension date	Reason for extension
Bayside Council	31 May 2018	The Office of Local Government approved a reporting extension for this council until 31 May 2018 due to incomplete financial records of the former City of Botany Bay Council.

The outcome of this incomplete audit will be reported in next year's report to Parliament.

Councils received unqualified audit opinions on special purpose financial information

Councils must also prepare two further documents that are audited:

- special purpose financial statements for declared business activities
- special schedule 8 'Permissible Income'.

The special purpose financial statements are required when councils provide services that compete in the marketplace. Special schedule 8 details the amount that councils can levy from rates for the next financial year. This amount is capped by the rate-peg limit set by the Independent Pricing and Regulatory Tribunal NSW.

The City of Botany Bay Council's 2015–16 special purpose financial statements were modified for the reason noted above. The Council did not prepare Special Schedule 8 'Permissible Income' in 2015–16.

Significant matters

Australian Auditing Standards require that we report significant matters identified during the audit to those responsible for the governance of a council. This includes the mayor or administrator, councillors and general manager. We also report significant matters to existing audit, risk and improvement committees, given their role in overseeing the financial reporting process.

Significant matters can include material accounting issues and internal control weaknesses.

The 2016–17 audits reported 39 significant matters

Our 2016–17 audits reported 39 significant matters in 29 councils. Most related to asset valuation and accounting issues, including:

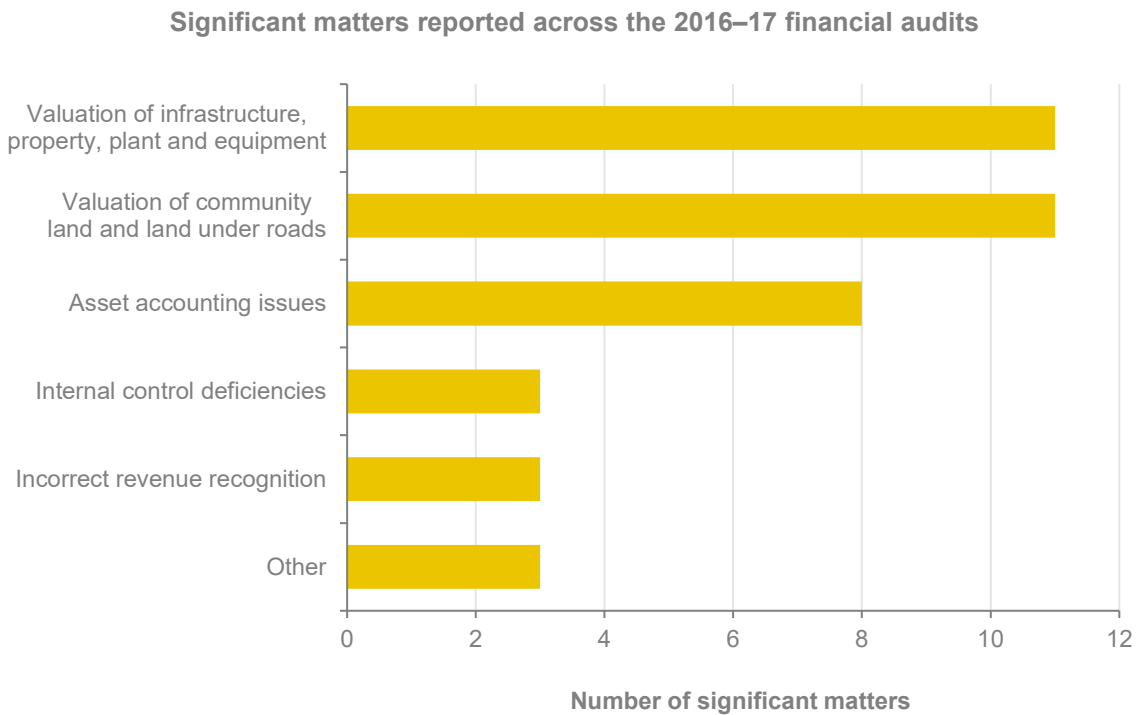
- ineffective controls and procedures to support asset valuations
- not appropriately considering external restrictions on the use of community land and land under roads when determining the fair value of assets
- incorrect accounting for Crown reserves and investment properties.

We discuss the asset-related issues further in Chapter 4.

The non asset-related significant matters included:

- internal control deficiencies over IT security
- incorrect recognition of revenue from government grants
- inappropriate use of corporate credit cards
- restricted funds used inappropriately.

The following graph below captures the range of significant matters we reported.



Source: Audited financial statements for 2016–17.

Prior-period errors

A prior-period error is an error identified in the current year that relates to the previous year's audited financial statements.

We found 33 material prior period financial reporting errors relating to 22 councils

Eighty-eight per cent of material prior-period errors related to assets, including:

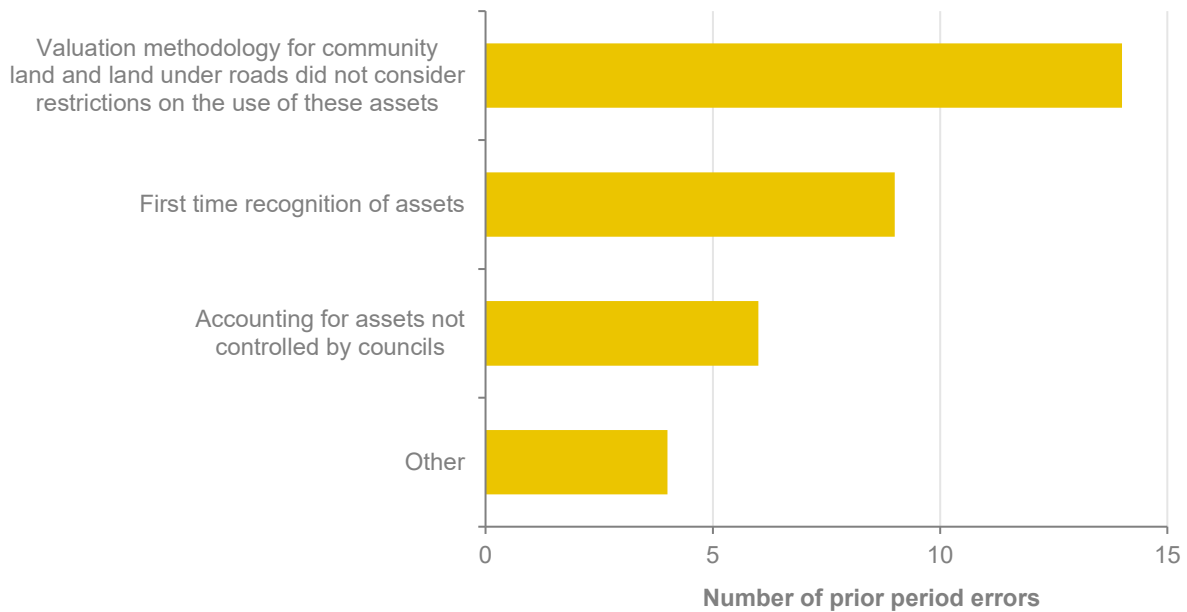
- failure to account for external restrictions on the use of community land and land under roads
- assets that were not recorded in the financial statements
- incorrect accounting for Crown reserves and investment properties.

We discuss the asset-related issues further in Chapter 4.

The remaining errors related to applying Australian Accounting Standards incorrectly, such as recognising the revenue from government grants.

The graph below illustrates the nature of the prior-period errors we found, which had a total value of \$9.1 billion. These errors meant that previous financial statements had to be corrected.

Material prior period errors identified across the 2016–17 financial audits



Source: Audited financial statements for 2016–17.

Financial statements

Councils need to improve the way they prepare financial statements

Recommendation

Councils can improve the quality of financial reporting by reviewing their financial statements close processes to identify areas for improvement.






The lack of robust quality assurance processes resulted in errors and disclosure deficiencies in councils' financial statements. At 43 councils, we considered these issues were significant enough to report as moderate risk findings in our management letters. Common issues include:

- incomplete note disclosures required by the Code, such as for related parties, commitments, fair value measurement, financial instruments, accounting policies and subsequent events
- incorrect classification of balances, such as employee provisions
- incorrect reporting of council entities, ownership percentages for interests in other entities and assets transferred on amalgamation
- errors in the cash flow statement and statement of changes in equity.

Better practice guides, such as the Australian National Audit Office's 'Public Sector Financial Statements: High quality reporting through good governance and processes' provide useful guidance, as the following checklist shows.

Better practice: Financial statements preparation process

A better practice financial statements preparation process has the following attributes:

- | | | | |
|---|--|---|---|
|  | Has the visible commitment and support of the council and management. |  | Invests in a skilled and knowledgeable finance team. |
|  | Applies the concept of materiality to the preparation of the financial statements, including in deciding the level of disclosure required. |  | Applies good practice project management including the development of a detailed work plan and a focus on meeting agreed deadlines. |
|  | Maintains a strong and effective internal control framework. |  | Applies robust risk management practices. |
|  | Maintains effective, open and constructive relationships with key stakeholders. |  | Identifies technical accounting issues and ensures there is consultation with stakeholders at an early stage. |
|  | Adopts good financial reporting practices throughout the year. | | |

Source: Australian National Audit Office, 'Public Sector Financial Statements: High quality reporting through good governance and processes'.

An audit, risk and improvement committee can support councils' financial management

Recommendation

Councils can improve the quality of financial reporting by involving an audit, risk and improvement committee in the review of financial statements.

Councils are not currently required to have an audit, risk and improvement committee and consequently 53 councils do not have an audit committee. Changes to the *Local Government Act 1993* made by the *Local Government Amendment (Governance and Planning) Act 2016* will require councils to establish an audit, risk and improvement committee (ARIC). This is expected to be a requirement by March 2021.

Of the 85 councils (60 per cent) that already have an ARIC in some form, only 45 per cent reviewed financial statements before they were submitted for external audit.

Councils can make better use of the ARIC, where it does exist, to oversee the council's financial information including the process to prepare the annual financial statements. The ARIC can support quality financial reporting by:

- ensuring key risk areas (such as asset revaluations) have been addressed
- tracking the resolution of audit findings from prior years
- confirming that key estimates and judgements in financial statements are reasonable
- recommending to the council whether the financial statements are appropriate to sign.

Office of Local Government guidance

The Office of Local Government needs to release key guidance documents earlier

Recommendation

The Office of Local Government should release the Local Government Code of Accounting Practice and Financial Reporting and the End of Year Financial Reporting Circular earlier in the audit cycle, ideally by 30 April each year.

The Office of Local Government (OLG) released two key documents to guide councils in preparing their 2016–17 financial statements:

- June 2017: Local Government Code of Accounting Practice and Financial Reporting (the Code)
- September 2017: End of year financial reporting 2016–17 Circular.

This timing meant there was limited scope for councils to apply the guidance in these documents when preparing financial statements by the statutory deadline of 31 October 2017. This also reduced the capacity of councils to resolve financial reporting, audit and compliance issues.

The Office of Local Government released the Code for the 2017-18 financial reporting year on 18 April 2018.

Local Government Code of Accounting Practice should align with Australian Accounting Standards

Recommendation

The Local Government Code of Accounting Practice and Financial Reporting should align with Australian Accounting Standards.

The Office of Local Government's Code of Accounting Practice and Financial Reporting (Code) sets the financial reporting requirements for councils. The Code requires councils to prepare financial statements in accordance with Australian Accounting Standards.

The Code applicable for 2016–17 financial reporting provided options and guidance that in some instances did not fully align with Australian Accounting Standards. For example, the Code:

- allowed councils the option to either recognise, or to not recognise rural fire-fighting equipment assets. This resulted in varying accounting practices across the sector and a significant portion of these assets not being reported in any government financial statements
- provided three methods for the valuation of land under roads and one of them did not specify that the restricted use of these assets needed to be considered as required by Australian Accounting Standards. This resulted in overstated asset values for this asset class for some councils.

2.2 Timeliness of financial reporting

Statutory deadlines

Councils had a statutory requirement to lodge their audited financial statements with OLG by 31 October 2017.

Seventy-one per cent of councils lodged audited financial statements by the statutory deadline

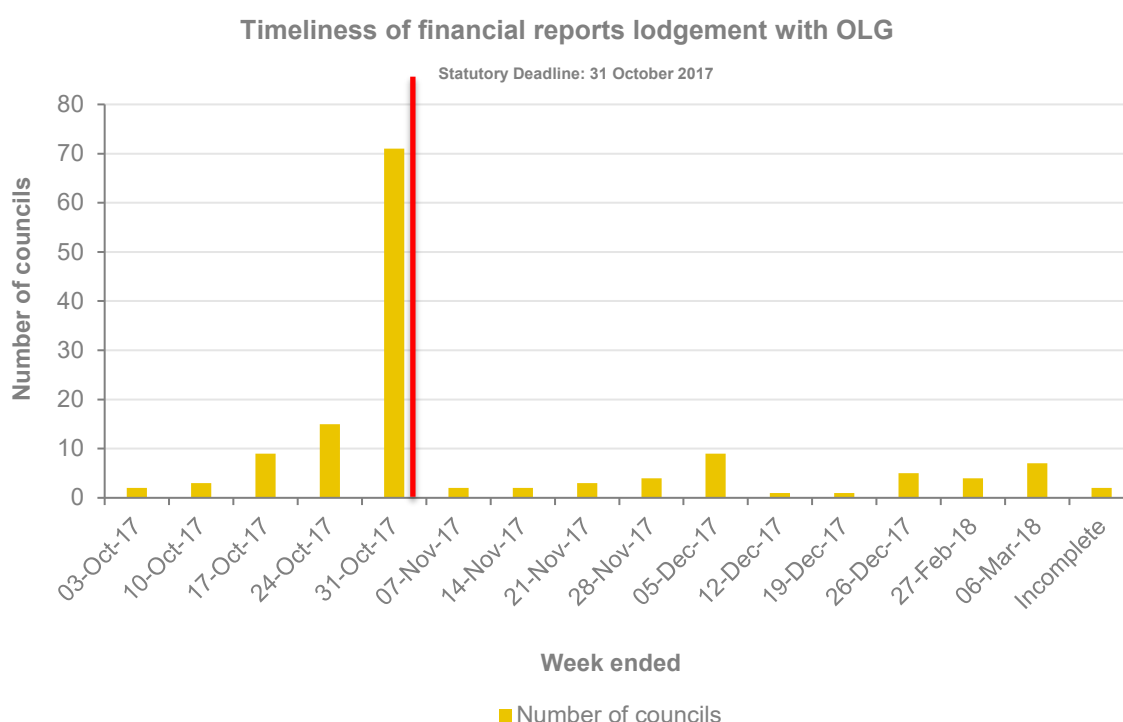
One hundred councils (71 per cent) met this requirement for the 2016–17 financial reporting period. However, of these, 71 councils submitted their audited financial statements to OLG during the last week of October 2017.

In many cases, councils provided multiple versions of the financial statements during the audit, including one council where 15 versions of the financial statements were presented for audit. This significantly delayed the audit and the lodgement of audited financial statements with OLG.

Under the *Local Government Act 1993*, a council may apply to OLG for an extension to the statutory reporting deadline. Forty councils received extensions for their 2016–17 financial statements including 16 newly amalgamated councils. These councils experienced challenges in harmonising accounting policies and practices and combining separate and distinct information technology and reporting systems.

Other reasons that councils put forward to support an extension were council resourcing issues and lack of financial records (particularly poor asset records). These issues had implications on audit resourcing and the timely completion of some audits by the Audit Office.

The graph below maps the lodgement dates of councils' financial statements.



Note: No council(s) lodged audited financial statements with OLG in January 2018.

2.3 Early close procedures

Early close procedures help to improve the quality and timeliness of financial reporting

Recommendation

The Office of Local Government should introduce early close procedures with an emphasis on asset valuations.

Early close procedures are those done before the end of a financial year, usually at the end of a month, such as 30 April. These procedures help to improve the timeliness and quality of financial reporting. They can identify issues and key risk areas that councils need to resolve before the year-end process. The table provides examples of early close procedures.

Asset valuation issues affected the quality of many councils' 2016–17 financial statements and were the reason for two modified (qualified) audit opinions and the majority of high risk and significant matters reported.

Preparing proforma financial statements at an early close date is a good test of a council's processes and controls.

The audit, risk and improvement committee could support the early close process by ensuring that audit findings are addressed before the year-end financial statements are prepared.

Early close procedures

- ✓ Complete infrastructure, property plant and equipment valuations.
- ✓ Prepare proforma financial statements and associated disclosures.
- ✓ Prepare variance analysis and meaningful explanations for movements in financial balances.
- ✓ Perform key account reconciliations.
- ✓ Assess the impact of material, complex and one-off significant transactions.
- ✓ Explain any unresolved prior year audit issues including the proposed action plan to resolve them.
- ✓ Assess the impact of new and revised accounting standards effective in the current and future years.
- ✓ Review of financial statements and processes by management and the audit, risk and improvement committee.

A person with short brown hair and glasses is seen from the side, looking at a laptop screen. The screen displays a dashboard with various financial charts, including a pie chart, a bar chart, and a line graph. The person is wearing a grey sweater. The background is blurred, showing a desk and some papers.

Financial
performance and
sustainability



3. Financial performance and sustainability

Strong and sustainable financial performance provides the platform for councils to deliver services and respond to the needs of their community. This chapter outlines our audit observations on the performance of councils against the Office of Local Government's (OLG) performance indicators, grouped in three areas:

- operating revenue performance measures
- liquidity and working capital performance measures
- asset management performance measures.

Our analysis indicates that some councils face challenges in meeting these performance and sustainability measures.

Observation	Conclusions	
3.1 Operating revenue performance measures		
Operating performance		
Operating expenses for 18 councils exceeded their operating revenue.	It is important that councils have financial management strategies that support their financial sustainability and ability to meet OLG's operating performance benchmark over the long term.	
Another 20 councils would not have met OLG's operating performance benchmark without the receipt of 2017–18 financial assistance grants which was recorded as revenue during 2016–17.		
Eleven councils have not met OLG's operating performance benchmark for the last three years.		
Operating performance measures how well councils contain operating expenses within operating revenue. OLG has prescribed a benchmark of greater than zero.		
Own source operating revenue		
Fifty-nine councils did not meet OLG's benchmark, and 42 of those were rural councils.	Rural councils have high-value infrastructure assets that cover large areas with smaller populations and less capacity to raise revenue from alternative sources compared with metropolitan councils.	
Own source operating revenue measures a council's fiscal flexibility and the degree to which it can generate revenue from own sources compared with total revenue from all sources. OLG has prescribed a benchmark of more than 60 per cent of total revenue.		

Observation

Conclusions

3.2 Liquidity and working capital performance measures

Unrestricted current ratio

All but three councils met OLG's benchmark.

The unrestricted current ratio represents a council's ability to meet its short-term obligations as they fall due. OLG has prescribed a benchmark of greater than 1.5 times.

Most councils can meet short-term obligations as they fall due.

Debt service cover ratio

All but two councils met OLG's benchmark. These two councils did not meet OLG's benchmark due to the early repayment of borrowings.

Regional councils have 56 per cent of the value of all borrowings in the sector.

The debt service cover ratio measures the operating cash available to service debt including interest, principal and lease payments. OLG has prescribed a benchmark of greater than two times.

Most councils have sufficient operating cash available to service their borrowings.

Regional councils borrow more heavily than metropolitan councils to deliver water and sewerage infrastructure. Metropolitan councils do not have the responsibility to provide water and sewerage infrastructure.

Rates and annual charges outstanding

Eight rural, five regional, three metropolitan and two county councils did not meet OLG's benchmark.

These councils also did not meet the infrastructure backlog ratio.

The rates and annual charges outstanding measure assesses the impact of uncollected rates and annual charges on a council's liquidity and the adequacy of debt recovery efforts. OLG has prescribed a benchmark of less than five per cent for metropolitan and less than ten per cent for other councils.

Most councils are collecting rates and annual charges levied. Councils with higher levels of uncollected rates and charges can experience increased pressure on the working capital available to fund operations.

Cash expense cover ratio

Three rural and two county councils did not meet OLG's benchmark.

The cash expense cover ratio indicates the number of months a council can continue paying its expenses without additional cash inflows. OLG has prescribed a benchmark of greater than three months.

This measure does not exclude externally and internally restricted funds. If externally restricted funds are excluded, all councils would still meet OLG's benchmark. If both externally and internally restricted funds are excluded:

- an additional 32 councils would have a cash expense cover ratio of less than three months
- a further nine councils are left without any unrestricted funds for general operations.

Most councils have the capacity to cover more than three months of operating expenses.

Councils with a higher proportion of restricted funds may have less flexibility to pay operational expenses than the cash expense cover ratio suggests. However, councils can resolve to lift internal restriction if required.

Observation

Conclusions

3.3 Asset management performance measures (not audited)

Building and infrastructure renewals ratio

Seventy councils reported to OLG they do not meet the benchmark for this ratio.

Most councils included expenditure related to work-in-progress in calculating this ratio. OLG are of the view that work-in-progress should be excluded and as a result identified that a further 23 councils do not meet the benchmark.

The building and infrastructure renewals ratio represents the rate at which assets are being renewed relative to the rate at which they are depreciating. OLG has prescribed a benchmark of greater than 100 per cent.

These councils appear to not be renewing assets in line with the rate they are depreciating them. This raises questions as to whether council asset management plans are adequate to determine whether assets are being kept up to agreed standards.

Uncertainty on the inclusion of work-in-progress assets does need to be clarified in order to ensure consistency in determining whether councils are adequately renewing their assets.

Infrastructure backlog ratio

Eighty-four councils reported to OLG that they do not meet the benchmark for this ratio.

The infrastructure backlog ratio represents the proportion of infrastructure backlog relative to the total net book value of a council's infrastructure assets. OLG has prescribed a benchmark of less than two per cent.

These councils may not be maintaining their infrastructure backlog at a manageable level.

Asset maintenance ratio

Seventy-one councils reported to OLG they do not meet the benchmark for this ratio.

The asset maintenance ratio represents the rate at which assets are being maintained relative to the rate at which they are required to be maintained. OLG has prescribed a benchmark of greater than 100 per cent.

These councils' maintenance expenditure may be insufficient to sustain their assets in a functional state so they reach their predicted useful life.

Cost to bring assets to agreed service level

One-hundred and two councils reported results against this indicator to OLG. The reported results ranged from 0.1 per cent to 19.8 per cent.

This ratio represents the estimated cost to renew or rehabilitate existing infrastructure assets that have reached the condition-based interval level adopted by a council, relative to the gross replacement cost of all infrastructure assets. OLG has not prescribed a benchmark for this performance measure.

There is variability between councils in the amount of outstanding renewal works to be completed.

OLG's benchmarks for financial performance and sustainability

Each local council has unique characteristics such as its size, location and services provided to their communities. These differences affect the nature of each council's assets and liabilities, revenue and expenses, and in turn the financial performance measures against which it reports.

The Office of Local Government prescribes performance indicators for council reporting

The analysis in this chapter is based on performance measures prescribed in OLG's Code of Accounting Practice and Financial Reporting (the Code). Councils report against these measures in their annual report, which includes the audited financial statements and other unaudited information. In the audited financial statements, councils report performance against six financial sustainability measures:

- operating performance
- own source operating revenue
- unrestricted current ratio
- debt service cover ratio
- rates and annual charges outstanding percentage
- cash expense cover ratio.

Councils also include the unaudited Special Schedule 7 'Report on Infrastructure Assets' in their annual reports. In this schedule, councils report to OLG on performance against four further measures:

- building and infrastructure renewals ratio
- infrastructure backlog ratio
- asset maintenance ratio
- cost to bring assets to agreed service level.

Each audited measure and three of the four unaudited measures has a prescribed benchmark. OLG's benchmarks are the same for metropolitan, regional, rural and county councils, with the exception of the rates and annual charges outstanding percentage. Regional, rural and county councils have a different benchmark to metropolitan councils for this measure.

Three rural councils did not meet three of the audited OLG benchmarks

Most councils met OLG's benchmarks for at least five or all of the six audited performance measures. Eight rural, four regional, four metropolitan and two county councils did not meet OLG's benchmarks for two out of the six audited performance measures. Three rural councils did not meet OLG's benchmarks for three out of the six audited performance measures.

The following table summarises how the councils performed across the six audited performance measures.

Number of OLG benchmarks met by councils	Number of councils			
	Metropolitan	Regional	Rural	County
6	12	12	29	5
5	17	21	17	5
4	4	4	8	2
3	--	--	3	--
Not available*	1	--	--	--
Total	34	37	57	12

* The financial statements for Bayside Council are not yet presented for audit.

Source: Audited Financial Statements for 2016–17.

Appendix ten lists the performance of each council against all performance measures.

3.1 Operating revenue performance measures

The first pair of performance indicators relate to the revenue that councils raise to deliver services:

- operating performance
- own source operating revenue.

Operating performance measures how well councils keep operating expenses within operating revenue. Own source operating revenue measures the degree to which a council can generate its own source revenue compared with the total revenue from all sources.

Operating performance

Operating revenue in this measure includes rates and annual charges, user charges and fees, interest, investment and other revenue. It excludes capital grants, capital contributions and changes in the fair value of assets.

OLG sets a benchmark of greater than zero per cent for this measure. Achieving this benchmark means councils are raising enough operating revenue to fund their operating expenses.

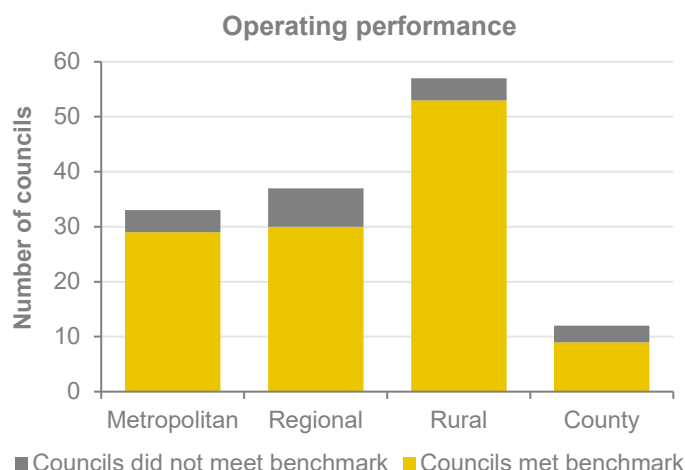
This measure assesses performance annually, so the result can be affected by short-term or one-off events and transactions, such as the profit or loss on disposal of assets and the cost of natural disasters.

Eighteen councils reported negative operating performance

Seven regional, four metropolitan, four rural and three county councils reported negative operating performance in 2016–17.

Of these 18 councils:

- five regional, two metropolitan, two rural and two county councils had reported a negative operating performance for the past three years
- fourteen councils also did not meet the infrastructure backlog ratio and twelve councils also did not meet the buildings and infrastructure renewals ratio.



Source: Audited financial statements for 2016–17.

Councils need to have financial management strategies that support their financial sustainability and meeting OLG's operating performance benchmark over the long term.

Five councils reported a net operating deficit

Yass Valley Council

In Chapter 2 Financial Reporting, we note that the audit opinion issued on the Yass Valley Council's 2016–17 financial statements was modified because Yass Valley Council did not record the receipt of financial assistance grants from the Australian Government as revenue in the year received, as required by Australian Accounting Standards.

The application of Australian Accounting Standards and the Code, with additional disclosure when appropriate, is necessary for financial statements to be presented fairly.

This resulted in an understatement of the net operating result for the year ended 30 June 2017 by \$1.48 million and overstatement of a liability recorded as 'income received in advance' by the same amount. It also affected the OLG indicators reported in the Council's financial statements.

In our audit report, we recalculated affected indicators and noted that if Council had correctly recognised this grant, its operating performance measure would have improved from negative 2.32 per cent to positive 2.48 per cent and met OLG's benchmark.

A council's net result is its operating surplus or deficit after expenses are deducted from revenue. The net result includes revenue from grants and contributions intended for capital purposes, but excludes the impact of extraordinary events such as amalgamations and boundary adjustments.

In 2016–17, one metropolitan, two regional and two county councils reported operating deficits. The remaining councils, including all rural councils, reported operating surpluses.

However, these results are affected by the timing of government grants. In 2016–17, councils received \$365 million of 2017–18 financial assistance grants from the Australian Government, which was recorded as revenue during 2016–17, consistent with the requirements of Australian Accounting Standards.

A council's financial statements present fairly their financial position and performance when transactions are recorded in accordance with the requirements of Australian Accounting Standards and the Code.

This grant income, received in advance, helped the 2016–17 operating performance of councils that had a net result close to break-even. Without these advance grant payments, a further 20 councils (four metropolitan, six regional and ten rural councils) would have reported negative operating performance and not met OLG's benchmark.

Own source operating revenue

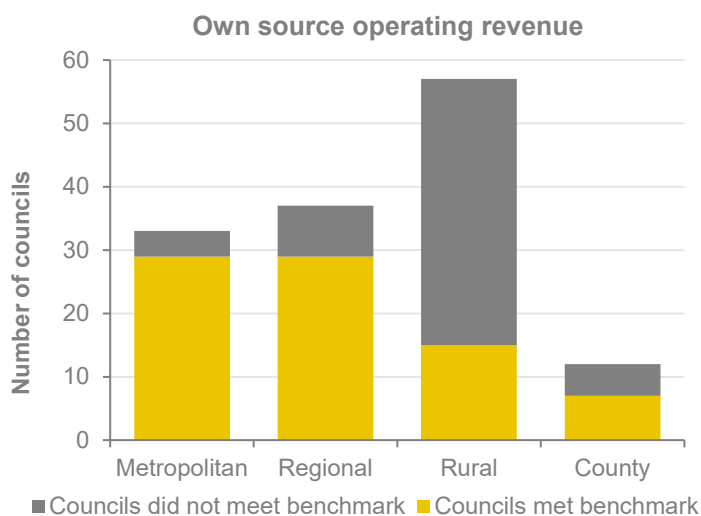
The second operating revenue measure helps to assess a council's fiscal flexibility and the degree to which it can generate own source revenue compared with the total revenue from all sources. The OLG benchmark is for own source operating revenue to be more than 60 per cent of total revenue.

This measure is sensitive to revenue from capital grants and developer contributions, and the percentage will fall where these revenue sources are significant.

Rural councils face challenges generating own source revenue

In 2016–17, forty-two rural, eight regional, five county and four metropolitan councils did not meet OLG's benchmark for own source operating revenue. This may result in councils not generating enough operating revenue to cover operating expenses.

Rural councils report challenges in generating their own revenue from rates, annual charges, user charges and fees. This is because they can have smaller populations and rating bases and lower economic activity. This reduces their capacity to generate revenue from alternative sources such as parking fees, infringement notices and rental income.



Source: Audited financial statements for 2016–17.

Seven of these 59 councils were also unable to meet the benchmark for OLG's performance measure for the collection of rates and annual charges, which is discussed later in the chapter. It is important for these councils to collect rates and annual charges on time given their challenges in generating this type of own source operating revenue.

Rural councils are responsible for maintaining infrastructure over large geographical areas. Thirteen of the 42 rural councils that did not meet OLG's benchmark for own source operating revenue also did not meet OLG's benchmarks for the buildings and infrastructure renewals ratio and infrastructure backlog ratio. These asset management performance measures are discussed later in this chapter.

Council revenue and expenses

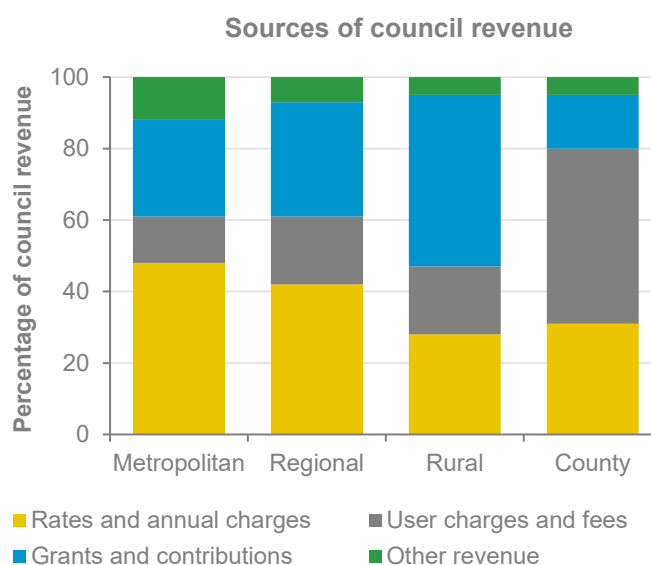
The following section details the main sources of council revenue, including special rate variations approved by the Independent Pricing and Regulatory Tribunal NSW, and the major categories of council expenditure. These are key drivers underlying several performance measures.

Revenue sources can vary significantly between councils

A council's total revenue comes from rates and annual charges, user charges and fees, operating and capital grants and contributions, and other revenue (such as interest, investments and asset disposals).

The graph illustrates the proportion of revenues from these sources for metropolitan, regional, rural and county councils.

Councils in metropolitan areas have the greatest capacity to generate other revenue, such as from childcare, parking fees, rental income and infringement notices. Rural councils rely more on grant funding to deliver their services.



Source: Audited financial statements for 2016–17.

County councils do not receive rates but do levy annual charges. They receive the highest proportion of user charges and fees, which they use to provide services such as water supply, management of flood plains, and eradication of noxious weeds.

Forty councils received revenue from special rate variations

In 2016–17, the Independent Pricing and Regulatory Tribunal NSW (IPART) set the allowable percentage increase in a council's annual rates income (the rate peg) at 1.8 per cent. However, IPART can approve special rate variations above the rate peg for things such as:

- extra services
- capital expenditure
- financial sustainability
- infrastructure such as roads, bridges and stormwater drainage.

Forty councils received additional revenue from special rate variations in 2016–17. Seventeen regional, 12 rural and ten metropolitan councils received revenue from special rate variations, ranging from three per cent to 11 per cent of their rates revenue. One rural council received approval to levy a special rate of 30 per cent.

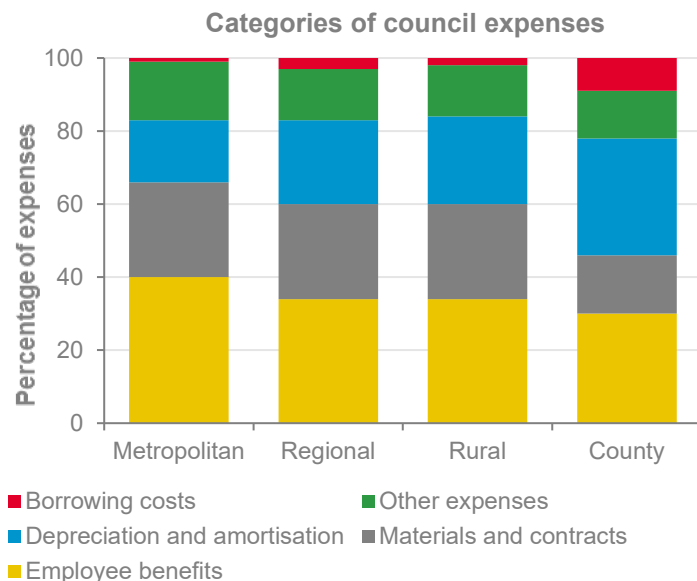
However, even with this extra revenue, four regional, one rural and one metropolitan council reported negative operating performance in 2016–17.

Employee benefits expense is the largest expense category for most councils

The largest overall expense categories for metropolitan, regional and rural councils are employee benefits, materials and contracts, and depreciation and amortisation.

The graph illustrates the proportion of expenses from various sources for metropolitan, regional, rural and county councils.

Regional, rural and county councils have a relatively larger proportion of depreciation and amortisation expenses compared to metropolitan councils because they have extensive infrastructure asset bases over large areas. This includes water supply and sewage infrastructure, which State agencies provide in metropolitan areas.



Source: Audited financial statements for 2016–17.

3.2 Liquidity and working capital performance measures

The next group of indicators help to assess the way councils can:

- meet short term obligations
- service their debt
- collect outstanding rates and annual charges
- meet their future expenses.

Unrestricted current ratio

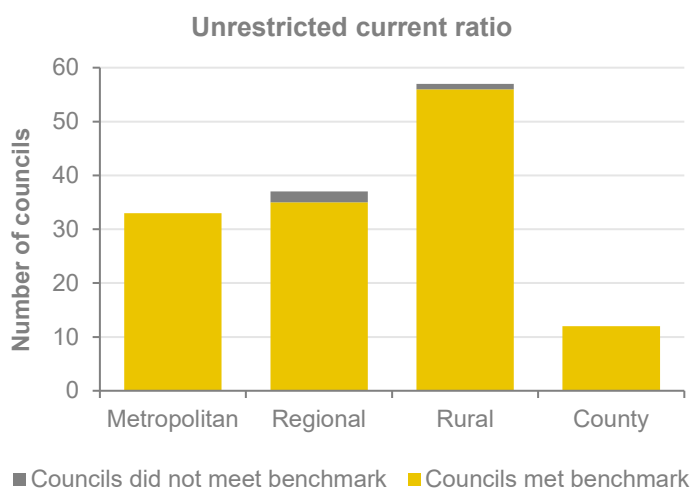
The unrestricted current ratio captures a council's ability to meet its short-term obligations as they fall due. The ratio excludes externally restricted assets and liabilities. OLG sets a benchmark of having available in unrestricted current assets more than 1.5 times the value of unrestricted current liabilities.

Two regional and one rural council did not meet OLG's benchmark for unrestricted current ratio.

The assets and liabilities of a council can fall into three categories:

- externally restricted
- internally restricted
- unrestricted.

Externally restricted assets are those affected by legislation or other externally imposed requirements. Internally restricted assets are affected by council resolution or policy, usually for an identified future works program. All other assets are unrestricted. Liabilities are restricted (specific purpose) if they relate to externally restricted assets.



Source: Audited financial statements for 2016–17.

Ninety-six councils had twice OLG's minimum benchmark for working capital

Forty-six rural, 21 metropolitan, 19 regional and ten county councils reported an unrestricted current ratio exceeding twice the OLG benchmark.

Two regional and one rural council did not meet OLG's benchmark for the unrestricted current ratio. One of these regional councils also did not meet OLG's benchmark for the collection of rates and annual charges. To meet operational needs, councils with a low unrestricted current ratio may need to:

- consider the availability of borrowings
- seek the Minister for Local Government's approval to use externally restricted funds
- look at ways to reduce expenditure or seek extra revenue from other sources.

Debt service cover ratio

One metropolitan and county council did not meet OLG's benchmark for the debt service cover ratio

The debt service cover ratio measures the operating cash available to service a council's debt, including interest, principal and lease payments. The benchmark OLG sets is to have available greater than twice the amount required to service debt.

The debt service cover ratio compares the operating result (before capital grants, capital contributions, depreciation and amortisation) with the repayment of borrowings and borrowing costs.

Fifty-seven rural, 37 regional, 27 metropolitan and five county councils reported borrowings at 30 June 2017. Councils utilise borrowings to fund capital projects and to address backlog maintenance. Regional councils accounted for 56 per cent of the value of total council borrowings because they also borrow to manage water and sewerage infrastructure.

One metropolitan and one county council did not meet this ratio as they repaid significant borrowings during 2016–17. One of these councils was newly amalgamated and the other was winding up.

Rates and annual charges outstanding percentage

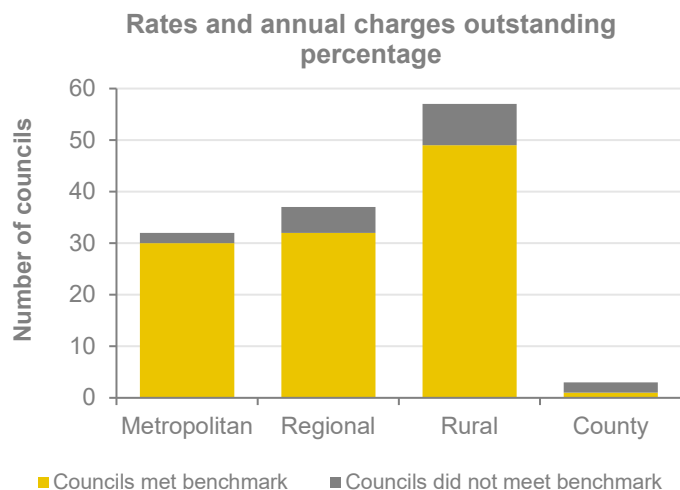
The rates and annual charges outstanding percentage assesses how successful councils are in collecting rates and annual charges. The indicator measures the percentage of rates and annual charges levied throughout the year that remain unpaid as at 30 June.

The OLG benchmark is that unpaid rates and annual charges for metropolitan councils should be less than five per cent and less than ten per cent for regional, rural and county councils.

Eighteen councils did not meet OLG's benchmark for outstanding rates and annual charges

Eight rural, five regional, three metropolitan and two county councils did not meet OLG's benchmark for the rates and annual charges outstanding percentage. Nine county councils do not levy rates and annual charges.

Councils with high levels of outstanding rates and annual charges may have less working capital available to fund operations. These eighteen councils also did not meet the infrastructure backlog ratio, which is discussed later in this chapter.



Source: Audited financial statements for 2016–17.

One rural council reported a rates and annual charges outstanding percentage of 36 per cent. Its inability to collect rates and charges resulted in less cash available for operations. This council also reported a cash expense cover ratio of 1.6 months, which is short of OLG's benchmark of more than three months. Unpaid rates are a debt on property. In certain circumstances, councils can assume ownership of land to recover a debt.

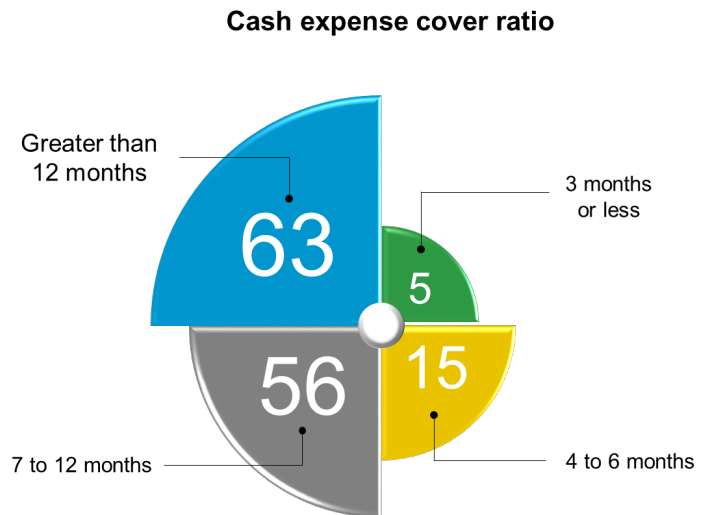
Cash expense cover ratio

The cash expense cover ratio estimates the number of months a council can continue paying its expenses without extra cash. It compares the total cash, cash equivalents and term deposit balances against the total payments for operating and financing activities from the cash flow statement. OLG sets a benchmark of greater than three months for this ratio.

Most councils met the cash expense cover ratio benchmark of more than three months

All but three rural and two county councils were able to cover more than three months of expenditure without extra cash inflows.

Sixty-three councils (45 per cent) had enough cash on hand to fund more than 12 months of expenditure. Another 56 councils (40 per cent) had enough cash to fund between seven and 12 months of expenditure, and 15 councils (11 per cent) had enough cash to cover four to six months of expenditure.



Source: Audited financial statements for 2016–17.

Cash expense cover ratio is lower when restricted funds are excluded

Central Darling Shire Council

In Section 1.1 of Chapter 2 Financial Reporting, we note that the audit opinion issued on the 2016–17 general purpose financial statements of Central Darling Shire Council referred to uncertainty over the council's ability to continue operating without using restricted water and sewer funds. This council used externally restricted funds for daily operations without ministerial approval.

On 2 March 2018, the council's administrator sought approval from the Minister for Local Government to continue using restricted cash as necessary.

Councils are not required to exclude externally and internally restricted funds when calculating the cash expense cover ratio. Restricted and unrestricted funds are held in accounts that councils control.

Section 409(3) of the *Local Government Act 1993* does not permit the use of externally restricted funds for general operations. A council with a high proportion of restricted funds may have a positive cash expense cover ratio, but limited flexibility to pay its operating expenses.

Section 410(3) of the *Local Government Act 1993* requires a council to obtain the Minister for Local Government's approval before using externally restricted funds collected from levying special rates and charges for another purpose. A council must pass a resolution to use internally restricted funds for another purpose.

If externally restricted funds are excluded from the cash expense cover ratio, all councils would still meet OLG's benchmark. However, if both internally and externally restricted funds are excluded:

- six regional, one rural and two county councils are left without any unrestricted funds, meaning there are no available funds for general operations, such as to pay salaries and suppliers
- seventeen rural, nine regional, four metropolitan and two county councils would have a cash expense cover ratio of three months or less.

Of these councils, 18 did not meet OLG's benchmark for own source operating revenue.

3.3 Asset management performance measures

The Office of Local Government (OLG) has prescribed four indicators to assess councils' asset management:

- buildings and infrastructure renewals ratio
- infrastructure backlog ratio
- asset maintenance ratio
- cost to bring assets to agreed service level.

Appendix ten lists the results of each indicator reported by councils to OLG.

Councils report to OLG against these indicators in the Special Schedule 7 'Report on Infrastructure Assets'. Special Schedule 7 is not required to be externally audited and does not form part of a council's independently audited financial statements. It provides information in addition to that available in the audited financial statements related to the maintenance, renewal, condition and costs of infrastructure assets. The Code requires that the information in Special Schedule 7 is consistent with the council's asset management plans.

Data reported against OLG's benchmarks is an indicator of whether councils' spending on renewing and maintaining their infrastructure assets is sufficient

Thirty-one councils reported they do not meet the OLG benchmarks for either the buildings and infrastructure renewals ratio, the infrastructure backlog ratio or the asset maintenance ratio. These councils may need to examine their asset management plans and consider if their investment in maintaining and renewing infrastructure assets is sufficient.

Councils are required to have asset management plans that consider community needs, available funds, the council's risk appetite, and the whole-of-life costs of owning and/or managing the infrastructure assets under their control.

The asset management indicators reported in Special Schedule 7 provide a snapshot of data at a point in time. While they may assist with further inquiry, a good or bad performance conclusion cannot be drawn from this data alone.

Buildings and infrastructure renewals ratio

Seventy councils do not meet OLG's buildings and infrastructure renewals ratio benchmark

The buildings and infrastructure renewals ratio is used to assess the rate at which infrastructure assets are being renewed against the rate at which they are depreciating. OLG sets a benchmark of greater than 100 per cent. The underlying information used to calculate this indicator is derived from a council's audited financial statements.

Achievement of the OLG benchmark indicates that a council is renewing its assets at the same rate it is depreciating them. Twenty-six rural, 24 regional, 16 metropolitan and four county councils reported to OLG they do not meet the prescribed benchmark for the buildings and infrastructure renewals ratio.

OLG's Code requires that the buildings and infrastructure renewals ratio is calculated based on a council's renewal expenditure on specific infrastructure assets listed in Special Schedule 7. OLG has informed the Audit Office that work-in-progress assets are not infrastructure assets for the purposes of reporting in Special Schedule 7. Eighty per cent of councils included work-in-progress assets in calculating the ratio. If work-in-progress assets are excluded from the calculation, a further 23 councils would not meet OLG's benchmark. This means that 93 councils, or 69 per cent of those that reported this indicator, did not meet the OLG benchmark for renewing their assets.

OLG will need to clarify the requirements for calculating the buildings and infrastructure renewals ratio with councils.

Infrastructure backlog ratio

Eighty-four councils do not meet OLG's infrastructure backlog ratio benchmark

The infrastructure backlog ratio shows the amount of infrastructure backlog expenditure relative to the total net book value of a council's infrastructure assets. OLG sets the benchmark for this ratio at less than two per cent. Achievement of the OLG benchmark indicates that infrastructure backlog is kept at a manageable level. The underlying information used to calculate this indicator is derived from a council's audited financial statements and other unaudited sources.

Infrastructure backlog is defined in Special Schedule 7 as the estimated cost to bring a council's infrastructure, buildings, other structures and depreciable land improvements back to a condition determined to be satisfactory by the council and the community.

Thirty-seven rural, 28 regional, 15 metropolitan and four county councils reported to OLG they do not meet the prescribed benchmark for the infrastructure backlog ratio. This means that 60 per cent of councils that reported this indicator did not meet OLG's benchmark for maintaining their infrastructure backlog.

Asset maintenance ratio

Seventy-one councils do not meet OLG's asset maintenance ratio benchmark

The asset maintenance ratio compares a council's actual asset maintenance expenditure to the amount planned in their asset management plans. OLG sets a benchmark of greater than 100 per cent. Achievement of the OLG benchmark indicates that a council is investing enough funds to sustain their assets in a functional state so they reach their predicted useful life. The underlying information used to calculate this indicator is derived from a council's unaudited asset management plans and other unaudited sources.

Twenty-nine rural, 26 regional, 13 metropolitan and three county councils reported to OLG that they do not meet the prescribed benchmark for the asset maintenance ratio. This means that 54 per cent of councils that reported this indicator did not maintain their assets in accordance with their asset management plans.

Cost to bring assets to agreed service level

The cost to bring assets to agreed service level compares the estimated cost to renew or rehabilitate existing infrastructure assets, that have reached the condition-based intervention level adopted by a council, to the gross replacement cost of all infrastructure assets. OLG has not prescribed a benchmark for this indicator. The underlying information used to calculate this indicator is derived from unaudited sources.

One-hundred and two councils reported results against this indicator to OLG, expressed as a percentage. The reported results ranged from 0.1 per cent to 19.8 per cent. This reflects significant variability between councils in the proportion of outstanding renewal works compared to the total replacement cost of infrastructure assets under their care and stewardship.

A scenic landscape at sunset. The sun is low on the horizon, casting a warm orange glow across the sky and the scene. A paved road curves through the foreground, flanked by green fields and trees. In the background, a line of trees separates the foreground from a distant town. Power lines and poles are visible on the right side of the road. A large white circle with an orange border is overlaid on the bottom right of the image, containing the text "Asset Management".

Asset Management



4. Asset management

NSW councils own and manage a significant range of assets, including infrastructure, property, plant and equipment with a total value of \$136 billion.

Many of the issues that our local government audits identified related to asset management. This chapter discusses some of the asset accounting issues we found, focusing on five areas:

- overall asset management issues
- asset registers
- asset valuation
- recognition and asset useful life estimates
- asset policy and planning.

Observation

Conclusion or recommendation

4.1 High risk issues

Significant matters reported to those charged with council governance

Our 2016–17 audits identified ten high risk issues related to the accuracy of asset registers, restricted assets and asset revaluations.

High risk issues affect council's ability to maintain their assets in the condition required to deliver essential services.

4.2 Asset reporting

Accuracy of asset registers

Our audits identified instances where councils had multiple asset registers, inaccurate or incomplete registers, unreconciled registers, or uncontrolled manual spreadsheets.

Maintaining accurate asset records is important as it enables councils to manage their assets effectively and report on finances appropriately.

Unrecorded land and infrastructure assets

Twenty-four councils had not recorded \$145 million worth of assets, mainly land and infrastructure assets.

Assets not captured in council records is at risk of not being subject to their care and control, nor recorded in the financial statements.

Rural fire-fighting equipment

At 30 June 2017, forty-six councils did report vested rural fire-fighting equipment in their financial statements. However, 62 councils did not record vested fire-fighting equipment in their financial statements. These rural fire-fighting equipment assets are not reported in either State government or local government financial statements.

Recommendation

The Office of Local Government should address the different practices across the local government sector in accounting for rural fire-fighting equipment before 30 June 2018.

In doing so, the Office of Local Government should work with NSW Treasury to ensure there is a whole-of-government approach.

Observation	Conclusion or recommendation
4.3 Asset valuation	
Restricted assets	
Our audits found that ten councils did not appropriately consider restrictions on the use of community land and land under roads when determining asset fair values in accordance with Australian Accounting Standards.	The valuation of community land and land under roads should reflect the physical and legislative restrictions on these assets as required by Australian Accounting Standards. The impact of restrictions can be significant.
Nine councils corrected the land values in their 2016–17 financial statements, reducing the reported value of community land and land under roads by \$12.1 billion.	Councils should consider engaging experts to assist with the determination of asset fair values, as necessary.
Asset revaluations	
Our audits found many cases where councils did not review valuation results, comply with applicable codes, or work effectively with valuers to obtain accurate asset valuations.	Valuing large infrastructure assets is a complex process. Councils would benefit if the process is started earlier and there is a clear plan to ensure valuations are appropriately managed and documented.
4.4 Asset useful life estimates	
Asset useful life estimates	
We found considerable variability in councils' useful lives for similar assets.	Depreciation is a significant expense for councils and therefore impacts on reported financial results and key performance indicators.
In some cases, the useful lives of assets are not reviewed annually or supported by regular condition assessment.	To comply with Australian Accounting Standards, councils need to reassess the useful lives of all assets annually. Regular condition assessments are essential to identify maintenance requirements and maintain service delivery.
4.5 Asset policy and planning	
Asset management strategy	
Thirteen councils do not have an asset management policy, strategy and plan, as required by OLG's Integrated Planning and Reporting Framework. Newly amalgamated councils have until 30 June 2018 to implement this.	An effective asset management strategy, policy and plan helps councils to manage their assets appropriately over their life cycle and to make informed decisions on the allocation of resources.

Assets overview

NSW councils own and manage a significant range of assets, including infrastructure, property, plant and equipment.

At 30 June 2017, the combined carrying value of NSW council assets was as follows.



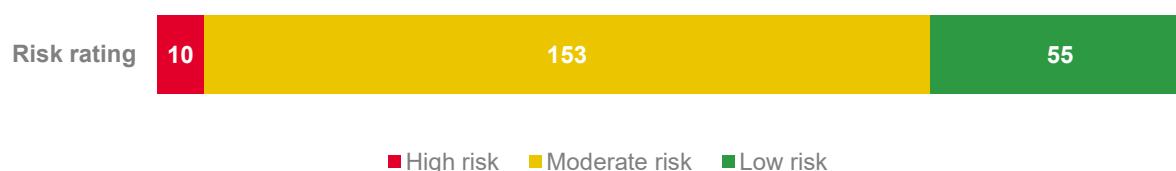
Source: Audited financial statements for 2016–17.

4.1 High risk issues

Significant matters reported to those charged with council governance

We reported ten high risk asset management issues

Our audits identified ten high risk issues related to asset practices.



Councils should address high risk issues as a priority because they can affect their ability to maintain their assets in the condition required to deliver essential services.

The high risk issues were in three areas:

- accuracy of asset registers
- restricted assets
- asset revaluations.

This chapter also discusses the need to strengthen asset depreciation practices and asset management strategies.

4.2 Asset reporting

Accuracy of asset registers

Effective asset management calls for accurate records of the assets that councils control. Our audits found that council asset registers and systems need to improve. Councils should regularly update asset registers and reconcile them with asset management systems. Suitable controls must be in place to ensure the integrity of manual spreadsheets.

Councils should improve how they manage asset registers

Asset registers record key data on the infrastructure, property, plant and equipment that a council holds. Our 2016–17 audits found:

- twenty-two examples where manual spreadsheets stored asset data without any controls to protect their integrity (discussed further in chapter 6)
- sixteen cases of multiple fixed-asset registers with inconsistent content and formats
- nine instances of inaccurate and incomplete asset registers without supporting documents
- six examples of asset registers that do not, or are not, reconciled with the asset management system used for operational activities
- five instances of completed works-in-progress not capitalised as assets on a timely basis.

Three high risk issues related to councils where multiple fixed asset registers were not reconciled and incomplete. This resulted in numerous errors identified during the audits.

Multiple and decentralised asset registers limit council's ability to manage and maintain the asset base and report on finances accurately. Manual spreadsheets increase the risk of errors in more complex asset data.

Unrecorded land and infrastructure assets

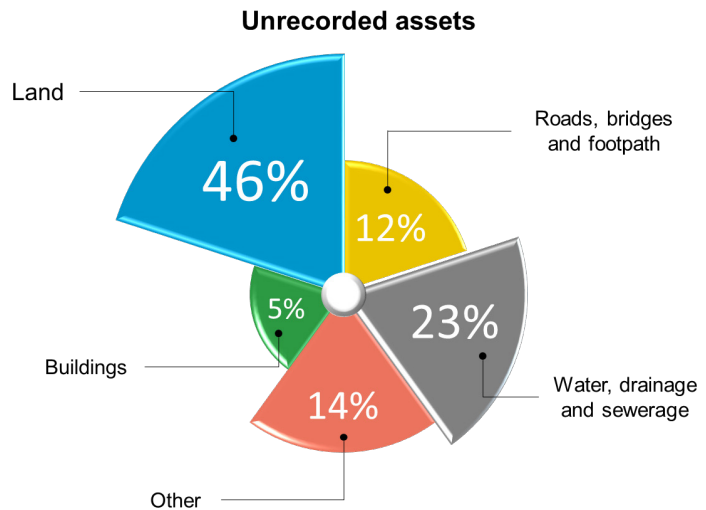
Councils had \$145 million in unrecorded land and infrastructure assets

Our 2016–17 audits identified \$145 million of unrecorded land and infrastructure assets at 24 councils. This is in addition to rural fire-fighting equipment not recorded by councils as discussed below.

The assets were mostly identified:

- during asset revaluations
- when reconciling asset registers and operational asset management systems
- during asset count processes to support the amalgamation of certain councils.

These assets are now recorded in the councils' 2016–17 financial statements. In eight councils, this also meant correcting the previous year's audited financial statements.



Source: Audited financial statements for 2016–17.

Rural fire-fighting equipment

A significant portion of rural fire-fighting equipment is not reported in either State government or local government financial statements

Recommendation

The Office of Local Government should address the different practices across the local government sector in accounting for rural fire-fighting equipment before 30 June 2018.

In doing so, the Office of Local Government should work with NSW Treasury to ensure there is a whole-of-government approach.

The 2016–17 Local Government Code of Accounting Practice and Financial Reporting required that council financial statements are prepared in accordance with Australian Accounting Standards. Forty-six councils did record vested rural fire-fighting equipment in their 2016–17 financial statements. However, sixty-two councils did not record these assets and, consequently, they are not reported in the financial statements of the State government or the local government.

Rural fire-fighting equipment is vested in councils under the *Rural Fires Act 1997*. This includes buildings, vehicles and other equipment used in connection with the prevention or suppression of fire. Service agreements govern the way the NSW Rural Fire Service can use these assets for fire mitigation and safety works in a council area.

NSW Treasury and the NSW Rural Fire Service are of the view that the NSW Rural Fire Service does not control rural fire-fighting equipment vested in councils. The financial statements of the NSW Total State Sector and the NSW Rural Fire Service do not include these assets.

The following factors suggest that councils control rural fire-fighting equipment:

- councils have responsibilities for fire mitigation and safety works in their area
- assets are vested in councils giving them legal ownership and title
- a council allows the NSW Rural Fire Service the use and occupancy of these assets within its council area through a service agreement
- councils are responsible for maintenance and insurance of the assets, although insurance of the vested vehicles is managed by the NSW Rural Fire Service.

4.3 Asset valuation

Seven high risk matters related to asset valuations, including two that resulted in qualified audit opinions

While having accurate asset registers is important, councils must also review the carrying value of their assets regularly so they reflect fair value.

Valuing large infrastructure assets is a complex process that needs to be well planned, managed and documented. The process should commence early in the financial year and, where used, instructions to external valuers need to clearly define the scope of work.

We found that councils need to improve their processes and controls over asset revaluations. Where experts are engaged, council management need to critically review the results to ensure they are robust.

The Office of Local Government (OLG) requires that councils comprehensively revalue each asset class on a five-year cycle. For those asset classes not subject to a comprehensive revaluation in a given year, councils must still satisfy themselves that asset values materially reflect fair value at the reporting date.

Restricted assets

Valuation methods need to consider restrictions that may affect asset values

At 30 June 2017, councils owned and managed \$33.5 billion worth of land, including \$17.8 billion (53 per cent) of community land and \$4.1 billion (12 per cent) of land under roads.

OLG's Local Government Code of Accounting Practice and Financial Reporting (Code) sets the financial reporting requirements for councils. The Code requires councils to report assets, such as land under roads and community land, at 'fair value'.

The Hills Shire Council

The method used by the Hills Shire Council to value land under roads did not appropriately reflect restrictions on the use of this land as required by Australian Accounting Standards.

This resulted in a modified (qualified) audit opinion on its 2016–17 financial statements.

Australian Accounting Standards define 'fair value' as the current exit price to sell or transfer an asset. They require that 'fair value' measurement considers an asset's characteristics, including its condition, location and any restrictions on its sale or use. Such restrictions may be imposed by legislation, regulation or planning instrument.

Most council community land is subject to legislative zoning restrictions through a Local Environment Plan. Land under public roadways is subject to physical restrictions and legislative restrictions under the *Roads Act 1993*. Councils cannot lift these restrictions without the approval of external bodies.

Our 2016–17 audits found ten councils where the 2015–16 audited financial statements had overstated the value of land assets because the valuation of community land and land under roads did not reflect the physical and legislative restrictions on these assets. Of these, nine corrected the land values in their 2016–17 financial statements.

As a result, the reported value of community land and land under roads at these nine councils reduced by \$12.1 billion from the previous years' audited financial statements. Over 90 per cent of

the reduction occurred in metropolitan councils, where the value of community land decreased by \$7.8 billion and land under roads decreased by \$3.5 billion.

Asset revaluations

Asset valuation processes can improve

Councils should have effective controls and procedures to support their asset valuations. Our 2016–17 audits found:

- twelve instances where council management did not sufficiently review valuation results, requiring adjustments in the financial statements
- seven cases where councils did not comprehensively revalue assets in line with the five-year cycle set by the Local Government Code of Accounting Practice and Financial Reporting
- five examples where council management did not agree on the scope and method of the required valuation with the external valuer before work was completed
- four instances where councils gave the valuer incomplete asset records, resulting in some assets being excluded
- four cases where there were no policies and procedures to support asset valuation processes
- four instances where the revaluation process did not start early enough to update the asset register and general ledger in time for year-end financial reporting
- four examples where supporting papers did not give enough detail of management's accounting treatments, judgements and assumptions underlying asset valuation.

Junee Shire Council

Junee Shire Council could not demonstrate that roads, bridges, footpaths and bulk earthworks were reported at fair value, as it did not value these asset classes during the year. The last valuation was conducted in 2012.

This led to a modified audit opinion on its 2016–17 financial statements.

4.4 Asset useful life estimates

The useful lives of road assets vary across councils

The useful life of an asset is the length of time it should be available for use. The remaining useful life is the period remaining that a council intends to use an asset, largely influenced by its physical condition. The useful life estimates determine the amount of depreciation expense reported in councils' financial statements.

Our audits reviewed the range of useful lives that councils reported for roads. We found considerable variability in the way councils reported the useful lives of similar road assets.

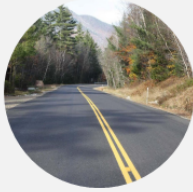


Sealed roads: Surface

Metropolitan Councils - from 19 to 41 years

Regional Councils - from 16 to 40 years

Rural Councils - from 19 to 28 years



Sealed roads: Structure

Metropolitan Councils - from 97 to 116 years

Regional Councils - from 45 to 192 years

Rural Councils - from 104 to 141 years



Unsealed roads

Metropolitan Councils - approximately 12 years

Regional Councils - from 19 to 88 years

Rural Councils - from 25 to 63 years

Source: Audited financial statements for 2016–17.

Some variability in the useful lives of roads can be expected due to different soil types, methods of construction, geography and the environment. However, these differences do not fully explain the large variation in the useful lives of similar assets across councils. This variability impacts the depreciation expense calculated by councils for similar assets and reported in the financial statements. This in turn may affect the key sustainability indicators that councils report.

Useful lives of assets need to be reviewed annually considering condition assessments

Australian Accounting Standards require that councils reassess the useful lives of all assets annually. Our 2016–17 audits identified six instances where there was no annual review of assets' remaining useful lives or regular condition assessment of assets. In three instances, the useful lives of assets were not adjusted to align with the physical condition assessments.

4.5 Asset policy and planning

Effective asset management should be tied together by an effective policy and planning processes. This helps to mitigate risk, support decision-making and ensure that councils manage assets efficiently and effectively over their life cycle. It also helps councils to determine future funding needs in maintaining, renewing and extending their asset base.

Asset management strategy

Thirteen councils do not have an asset management strategy, policy and plan

In 2013, OLG released an Integrated Planning and Reporting Framework (IP&R framework). This helps councils to integrate its plans and policies and align them with its strategic goals.

A key element of the IP&R framework is that all councils have an integrated asset management strategy, policy and plan. Newly amalgamated councils have until 30 June 2018 to finalise these.

Thirteen councils do not have the required asset management strategy, policy and plan. Eleven of these are regional and rural councils.



Governance and Internal Controls



5. Governance and internal controls

Good governance systems help councils to operate effectively and comply with relevant laws and standards. Internal controls assist councils to operate reliably and produce effective financial statements.

This chapter highlights the high risk issues we found and reports on a range of governance and control areas. Governance and control issues relating to asset management and information technology are covered in separate chapters.

Observation	Conclusion or recommendation
5.1 High risk issues	
Significant matters reported to those charged with council governance	
<p>Our 2016–17 audits identified 36 high risk governance and internal control deficiencies across 17 councils.</p> <p>We reported:</p> <ul style="list-style-type: none"> seventeen high risk issues relating to governance, purchase-to-pay, financial accounting and payroll processes ten high risk issues relating to asset practices nine high risk issues related to information technology management. 	<p>Asset practices accounted for the highest number of high risk issues and information technology accounted for the largest overall number of control deficiencies. These matters are covered in chapters four and six respectively.</p> <p>High risk issues affect council's ability to achieve their objectives and increase the risk of fraud and error.</p>
5.2 Governance	
Audit committees	
<p>Councils are currently not required to have an audit, risk and improvement committee. Consequently, 53 councils do not have an audit committee.</p>	<p>Proposed legislative changes will require councils to establish an audit, risk and improvement committee by March 2021.</p> <p>Recommendation</p> <p>Councils should early adopt the proposed requirement to establish an audit, risk and improvement committee.</p>
Internal audit	
<p>Councils are currently not required to have an internal audit function. Consequently, 52 councils do not have this function.</p>	<p>Recommendation</p> <p>The Office of Local Government should introduce the requirement for councils to establish internal audit functions and update its 2010 Internal Audit Guidelines.</p>
Council entities	
<p>The Office of Local Government's register of entities approved under section 358 of the <i>Local Government Act 1993</i> is incomplete.</p>	<p>Recommendation</p> <p>The Office of Local Government should maintain an accurate register of council entities approved under section 358 of the <i>Local Government Act 1993</i>.</p>
<p>The <i>Local Government Act 1993</i> does not stipulate a financial reporting framework for council entities.</p>	<p>Recommendation</p> <p>The Office of Local Government should establish a financial reporting framework for council entities.</p>

Observation	Conclusion or recommendation
<p>Policies and procedures</p> <p>We identified 50 high and moderate risk issues across 33 councils where policies and procedures over critical business processes did not exist or had not been updated.</p>	<p>It is important there are current policies, standards and guidelines available to staff and contractors across all critical business processes.</p>
<p>Legislative compliance frameworks</p> <p>Our audits found that 45 councils do not have sufficient processes to show they are complying with legislative requirements.</p>	<p>Councils can improve practices in monitoring compliance with key laws and regulations. This includes implementing a legislative compliance framework, register and policy.</p>
<p>Risk management</p> <p>We identified 15 high and moderate risk issues across 15 councils where risk management practices could be strengthened.</p>	<p>Council risk management practices are enhanced when there is a fit-for-purpose risk management framework, register and policy to outline how risks are identified, managed and monitored.</p>

5.3 Internal controls

Financial accounting

We identified 45 high and moderate risk control deficiencies across 41 councils concerning the use of manual journals to adjust council financial records. This can increase the risk of fraud and error.

We identified 51 high and moderate risk issues across 39 councils where reconciliation processes need to improve to support the preparation of accurate financial statements.

Sound financial accounting processes include controls to ensure:

- a person other than the preparer authorises manual journals
- key account reconciliations are prepared and reviewed.

Purchasing and payables

We found 102 high and moderate risk deficiencies in purchasing and payable controls across 64 councils. Sound purchasing controls are important to minimise error, unauthorised purchases, fraud and waste.

As councils spend a substantial amount each year to procure goods and services, strong controls over purchasing and payment practices are critical. These include:

- a review of changes to vendor master file data by an appropriate independent officer
- an independent review and approval of purchases, including credit card transactions
- compliance with Tendering Guidelines for NSW Local Government.

Payroll

We identified 71 high and moderate risk deficiencies in payroll controls across 48 councils. Weaknesses in payroll controls could result in incorrect payments being made to employees, due to error or fraud.

Managing excess annual leave balances was a challenge for 32 councils.

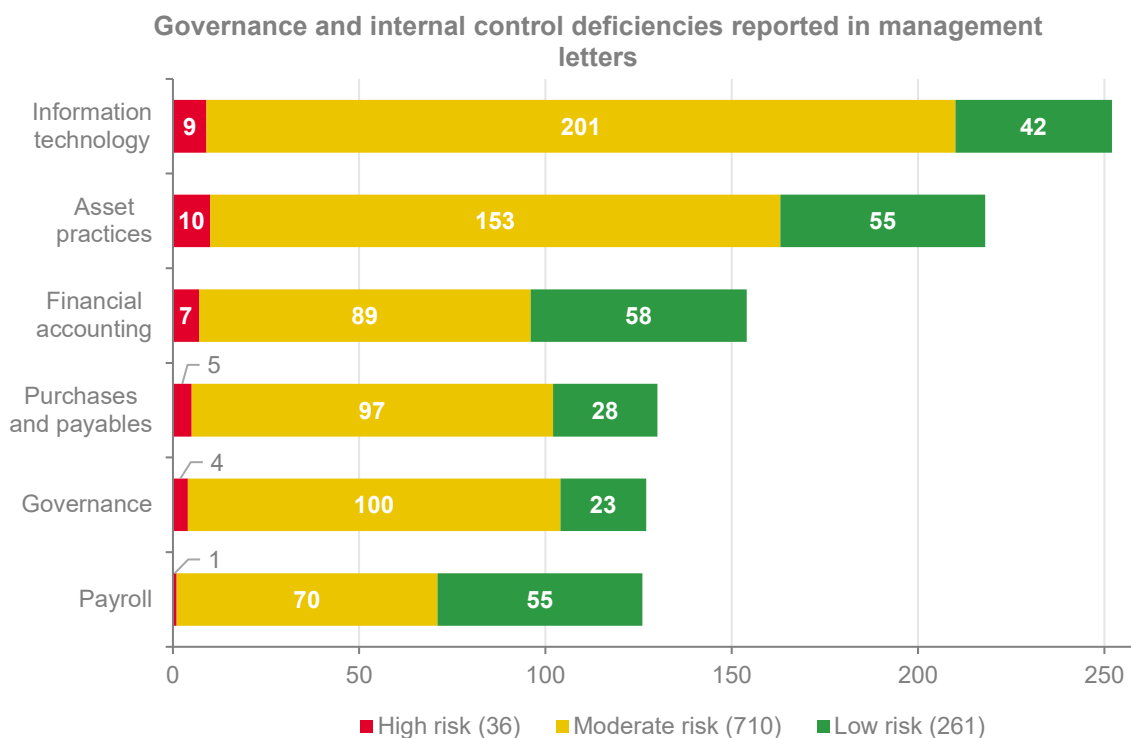
Effective payroll controls are important because employee expenses represent a large portion of council expenditure. These controls include segregation of duties in the review of payroll master file data, timesheets, leave forms, payroll exception reports and termination payments.

Excessive annual leave balances can have implications on employee costs, disrupts service delivery and affect work, health and safety. Excess annual leave balances should be continuously monitored and managed.

5.1 High risk issues

Significant matters reported to those charged with council governance

During our 2016–17 audits, we identified 36 high risk governance and internal control deficiencies.



The high risk issues fell across six areas. We discuss four of these in this chapter and the remaining two in other chapters:

- information technology (see chapter 6)
- asset management (see chapter 4)
- governance
- purchasing and payables
- financial accounting
- payroll.

Councils should address high risk issues as a priority as these can increase the risk of fraud and error.

5.2 Governance

Governance refers to the frameworks, processes and behaviours that help a council achieve its objectives, comply with legislative and other requirements, and meet standards of probity, accountability and transparency.

Effective governance builds community confidence and enables the effective and efficient use of public resources. Governance models need to be fit for purpose and tailored to the needs of each council.

In 2015, the Audit Office released its Governance Lighthouse to provide a best practice model of public sector governance for entities to follow. This covers eight principles and 17 key elements of good governance. Councils may find it useful to assess existing governance practices against the key principles in the lighthouse and address any gaps they find.

While this year's financial audit did not assess every aspect of governance in councils, this report highlights our findings and observations related to:

- audit committees and internal audit
- council entities
- policies and procedures
- legislative compliance frameworks
- risk-management.

Audit committees and internal audit

The combined benefit of an audit committee and internal audit function is that councillors can obtain general assurance that internal controls and risk management are working effectively. The 36 councils that do not have an audit committee and internal audit function are operating without important safeguards and generally accepted checks and balances.

Fifty-three councils have not established an audit, risk and improvement committee

Recommendation

Councils should early adopt the proposed requirement to establish an audit, risk and improvement committee.

An effective audit, risk and improvement committee is an important part of good governance.

Councils are not currently required to have an audit, risk and improvement committee. At present, 53 councils do not have a functioning audit committee.

Changes outlined in section 428A of the *Local Government Amendment (Governance and Planning) Act 2016* will require councils to establish an audit, risk and improvement committee. This is expected to be a requirement by March 2021.

Council type	Number of councils with an audit, risk and improvement committee	Number of councils without an audit, risk and improvement committee	% without
Metropolitan	32	2	5.9
Regional	29	8	21.6
Rural	23	34	59.6
County	1	9	90.0
Total	85	53	38.4

Note: Mid-Coast and Southern Slopes county councils were dissolved on 1 July 2017. They have been excluded from the table.

Section 428B of the *Local Government Amendment (Governance and Planning) Act 2016* specifies that councils may jointly appoint an audit, risk and improvement committee to exercise functions for more than one council.

Fifty-two councils do not have an internal audit function

Recommendation

The Office of Local Government should introduce the requirement for councils to establish internal audit functions and update its 2010 Internal Audit Guidelines.

Internal audit is another important element of an effective governance framework as it supports a risk and compliance culture. Internal audit provides assurance that a council's governance practices and internal control environment are effective, and identifies where performance can improve.

Councils are not currently required to have an internal audit function. As the following table shows, 33 rural councils, eight county councils, eight regional councils and three metropolitan councils do not have an internal audit function. Of these councils, nine are newly amalgamated.

Council type	Number of councils with an internal audit function	Number of councils without an internal audit function	% without
Metropolitan	31	3	8.8
Regional	29	8	21.6
Rural	24	33	57.9
County	2	8	80.0
Total	86	52	37.7

Note: Mid-Coast and Southern Slopes county councils were dissolved on 1 July 2017 and have therefore been excluded from the table.

There are 13 councils with an internal audit function but without an audit, risk and improvement committee. An effective audit committee would complement the internal audit function and provide it with a separate reporting line independent of management.

The Office of Local Government (OLG) has not updated the Internal Audit Guidelines it released in 2010. The OLG should, at a minimum, introduce the requirement for councils to establish internal audit functions and update its 2010 Internal Audit Guidelines.

An internal audit function is mandatory for all State government agencies. A useful reference point for councils is available in TPP 15-03 Internal Audit and Risk Management Policy for the NSW Public Sector, issued by NSW Treasury.

Council entities

The Office of Local Government does not have complete information on council entities

Recommendation

The Office of Local Government should maintain an accurate register of entities approved under section 358 of the *Local Government Act 1993*.

Section 358 of the *Local Government Act 1993* (Act) specifies that councils must not form or participate in forming a corporation or other entity, or acquire a controlling interest in a corporation or other entity, except with the consent of the Minister for Local Government. These entities are referred to as 'council entities'.

Section 415 of the Act deals with auditing of the financial statements of council entities. The definition of a council entity in section 415 includes a wide and diverse range of bodies and is consistent with the definition of entities under section 358 of the Act. Our initial audit work identified 261 entities that met the definition of a council entity.

OLG maintains a register of entities where a council has sought approval from the Minister under section 358 of the Act. The register maintained by OLG was not complete and accurate. It also did not identify what entities had been approved by the Minister.

The legislation does not clarify the financial reporting obligations of council entities

Recommendation

The Office of Local Government should consider establishing a financial reporting framework for council entities.

We found uncertainty in the legislative framework governing the oversight of council entities⁵ and their financial reporting and auditing requirements. This can result in a lack of transparency and accountability over the activities of council entities.

The *Local Government Act 1993* does not require council entities to keep records or prepare financial statements. Some council entities prepare financial statements, while others do not. The financial statements of some entities are audited, where others remain unaudited.

Given this uncertainty, we sought advice from the NSW Crown Solicitor about the Auditor-General's obligations under the Act. This confirmed that arrangements for council entities under the Act need clarification. Appendix 11 attaches this advice.

Policies and procedures

Formal policies and procedures support effective governance and internal control as they:

- provide direction for the day-to-day operations of a council
- promote consistency
- clarify accountability and other issues to staff and management
- support compliance with laws, regulations and codes.

Policies and procedures are not always in place or kept up to date

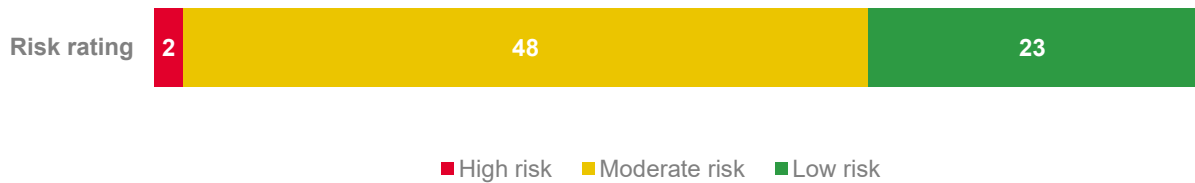
Councils need to ensure that policies, standards and guidelines are available to staff and contractors across all critical business processes, and that they are reviewed and updated regularly, including when significant changes occur.

Our financial audits did not review all council policies and procedures, but looked at whether policies and procedures for critical business processes exist and are updated. We found 73 cases across 47 councils where policies and procedures did not exist or had not been updated for:

- financial management
- information technology
- procurement
- contract management.

⁵ Section 358(4) of the *Local Government Act 1993* defines entity as 'any partnership, trust, joint venture, syndicate or other body (whether or not incorporated), but does not include any such entity that is of a class prescribed by the regulations as not being within this definition'.

Of the 73 issues, two were high risk, 48 were moderate risk and 23 were rated low risk.



The two high risk issues were:

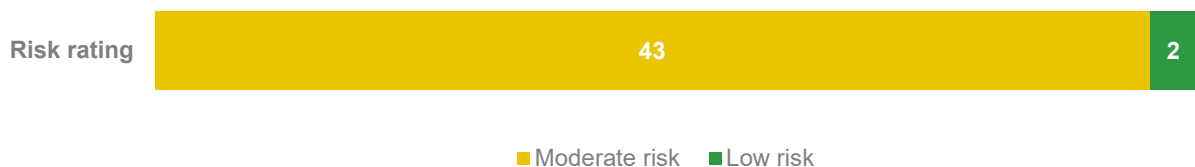
- one council without any policies for numerous critical business processes, including payroll, purchases, property, plant and equipment and revenue
- one council with no IT strategic plan, disaster recovery plan, business continuity plan and only limited IT operating procedures.

Legislative compliance frameworks

Councils need to improve practices to comply with key laws and regulations

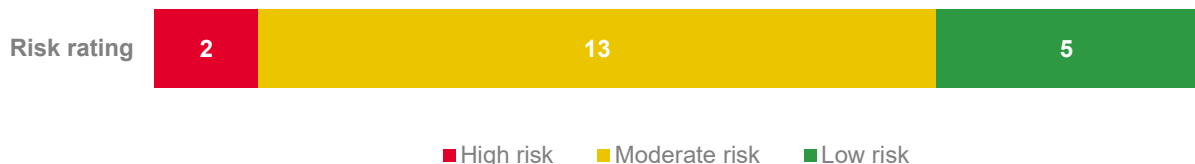
Our audits found 45 councils do not have a legislative compliance framework, which would include a compliance policy and compliance register. Without these, there is an increased risk that councils may breach legislative requirements. This can attract penalties, affect service delivery and cause significant reputational damage.

A compliance framework needs to be suited to the size of a council, but sufficient to help it comply with key legislative obligations. We reported this as a moderate risk at 43 councils and a low risk at two councils.



Risk management

While our financial audits are not designed to assess every aspect of risk management, we did identify 20 instances in 17 councils where risk management practices could be strengthened. Two of these were high risk, 13 were moderate risk and five were low risk.



Councils should address the high risk issues as a priority because they may affect their ability to achieve their objectives or comply with relevant legislation.

The high risk issues related to:

- one council where high-rated risks were identified on the risk register but there was no indication of how the risks were being managed. In addition, roles and responsibilities for risk management were not clearly defined
- one council where fraud-related risks identified by management were not being addressed.

The remaining moderate and low risk issues related to the lack of, or out-dated, risk management frameworks, risk registers and/or policies and procedures. Of the 20 issues identified in risk management practices, 14 related to rural councils.

Councils may find it useful to assess their risk management practices using the Audit Office's Risk Maturity Toolkit. The toolkit is based on the principles and guidance of International Standards on Risk Management AS/NZS ISO 31000:2009 Risk Management and NSW Treasury Policy Guidelines TPP 12-03 and TPP 15-03. The risk management toolkit needs to be applied in a way that is fit for purpose, considering the size and complexity of each council.

5.3 Internal controls

Our financial audits focus on key internal controls that underpin the financial statements that councils prepare each year. Our audits assess whether key internal controls are designed, implemented and operating effectively to manage the risk of material error in the financial statements.

We report any control deficiencies we find to management and those charged with governance of a council through our audit management letters.

Financial accounting

The two main financial control weaknesses we found related to manual journals and reconciliations. A high proportion of these weaknesses were of moderate risk.

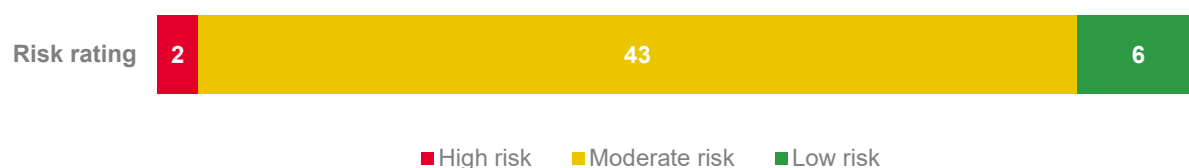
Councils can improve internal controls for manual journals

Staff use manual journals to make changes directly to the general ledger, which supports the preparation of council financial statements. Unlike IT controls, which are typically automated, most manual journals rely on human intervention and oversight. Using manual journal entries without appropriate controls and oversight can increase the risk of error and fraud.

Our audits found 51 cases in 43 councils where there were control weaknesses around manual journals. These included:

- manual journals not reviewed by an independent officer
- the finance system not preventing the same officer from posting and approving manual journals
- inadequate supporting documentation for manual journals posted
- staff with access to process manual journals beyond their job requirements.

Of the 51 cases, two were considered high risk, 43 of moderate risk and six low risk.



The high risk issues related to:

- one case where journals were posted to incorrect accounts and this had a significant impact on the financial statements. It could have been prevented if there was an appropriate review of the journals
- one case where journals could be posted without review by another officer. This was classified high risk, as fraud had been committed at this council in the past.

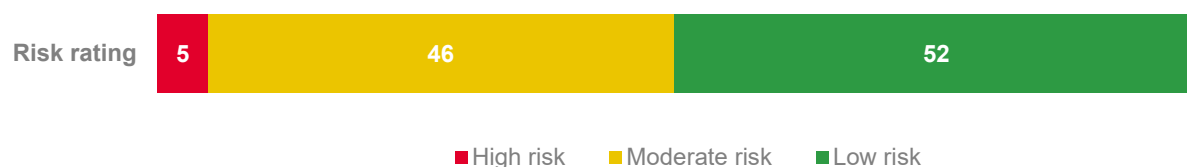
Councils should reconcile their accounts timely and review them independently

Councils need to improve processes in preparing and reviewing account reconciliations.

Council financial statements are based on information in the general ledger. Balances are often supported by information in subsidiary ledgers, such as for:

- accounts payable
- accounts receivable
- fixed assets
- payroll.

It is important that councils periodically reconcile the general ledger with these subsidiary ledgers to confirm that data is accurate and complete. Our audits found 103 deficiencies across 61 councils relating to key account reconciliations. Five were high-risk, 46 of moderate risk and 52 low risk.



The issues included:

- reconciliations not prepared for key account balances
- reconciliations not reviewed in a timely manner by an appropriate officer
- long-outstanding reconciling items remaining unresolved for long periods.

The deficiencies were assessed as high risk if they could significantly affect the councils' financial statements.

If key account reconciliations are not prepared and reviewed promptly, management's ability to identify and resolve issues is affected. That could result in misstatements in financial reporting.

Purchasing and payables

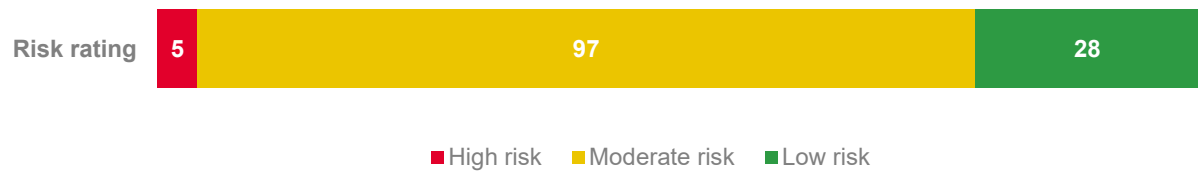
Councils purchase significant amounts of goods and services each year. In 2016–17, for example, councils collectively spent:

- \$3.5 billion to acquire property, plant and equipment
- \$3.9 billion on supplies, services and other general expenditure.

Seventy-six councils need to improve purchasing and payables controls

Sound controls for purchasing and payment functions are important to minimise the risk of unauthorised purchases, fraudulent activity and waste. For example, the report from the recent Independent Commission Against Corruption (ICAC) investigation into the conduct of employees at the former City of Botany Bay Council highlighted serious, systemic failures in procurement practices and internal controls. This led to financial loss and reputational damage.

Our audits identified 130 internal control weaknesses related to the purchasing and payables process across 76 councils. Five were high risk, 97 of moderate-risk, and 28 rated low risk.



The high risk issues related to:

- unauthorised expenditure, or expenditure approved by an officer without the necessary delegation
- non-compliance with Tendering Guidelines for NSW Local Government.

The moderate and low risk matters span these same issues but also included:

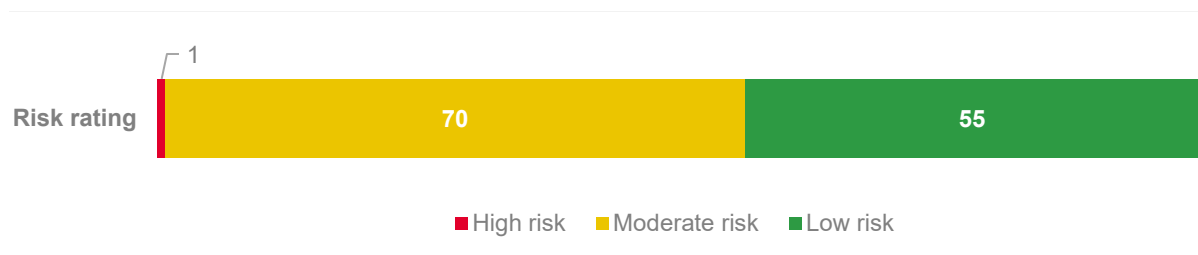
- purchase orders raised only after the goods or services were received and paid for
- reports designed to detect irregular or unusual changes that were not reviewed
- inadequate segregation of duties in the purchases and payables function
- inadequate review of credit card transactions and retention of supporting documents
- lack of review of changes to vendor master file data
- purchase orders not raised at all.

Payroll

Councils need to have effective payroll controls because employee expenses represent a large portion of their total expenditure. Weaknesses in payroll controls could result in incorrect payments to employees due to either error or fraud.

Seventy-two councils need to improve payroll controls

Our audits identified 126 internal control weaknesses related to payroll processes at 72 councils. One was assessed as high risk, 70 moderate risk and 55 rated low risk.



The high risk issue involved a council where payroll staff had unrestricted access to amend sensitive payroll data in the system. There were no mitigating controls as:

- system logs detailing changes to employee details were not generated
- exception reports which can be used to identify unusual changes in pay details were not reviewed by an officer independent of the payroll team.

Common issues from the remaining moderate and low risk deficiencies included:

- no review of changes to details in the payroll master file
- unapproved staff timesheets
- unapproved staff leave forms
- payroll exception reports not reviewed
- termination payments not reviewed.

Managing excess annual leave is a challenge for some councils

Under the Local Government Award, council employees should have less than eight weeks of annual leave accrued at any time.

We identified staff with annual leave balances greater than eight weeks at 32 councils.

There are several implications of excessive leave balances, including:

- higher employee costs in the future due to salary increases
- work, health and safety implications
- disruptions to service delivery when employees eventually take lengthy periods of leave
- employee fraud remaining undetected.



Information Technology



6. Information technology

Like most public sector agencies, councils increasingly rely on information technology (IT) to deliver services and manage sensitive information. While IT delivers considerable benefits, it also presents risks that councils need to address.

Our review of council IT systems focused on understanding the processes and controls that support the integrity, availability and security of the data used to prepare financial statements. This chapter outlines issues in three broad areas:

- high risk issues
- access to IT systems
- IT governance.

Observation

Conclusion

6.1 High risk issues

Significant matters reported to those charged with council governance

Our 2016–17 audits identified nine high risk IT control deficiencies across seven councils. The issues related to user access controls, privileged access controls and user developed applications.

High risk issues affect council's ability to achieve their objectives and increase the risk of fraud and error.

6.2 Access to IT systems

User access controls

We identified 107 issues across 56 councils where user access controls could be strengthened.

Inadequate IT policies and controls around user access, including privileged access, increases the risk of individuals having excessive or unauthorised access to critical financial systems and data.

Privileged access

We identified 86 examples across 64 councils of inappropriate privileged access, inadequate review of access and insufficient retention and review of access logs.

User developed applications

User developed applications (UDAs) are computing applications, tools and processes developed or managed outside IT administration. UDAs may allow users to bypass formal user access controls.

Our audits found 22 councils using spreadsheets for business operations, decision making and financial reporting that were not adequately secured, with changes that were not tracked, tested or reviewed.

We also identified five councils where finance staff and senior management use database query tools to directly modify financial data, circumventing system-based business process controls.

It is important councils are aware of all circumstances they are relying on UDAs to limit the risk of errors and potential misuse. This allows councils to:

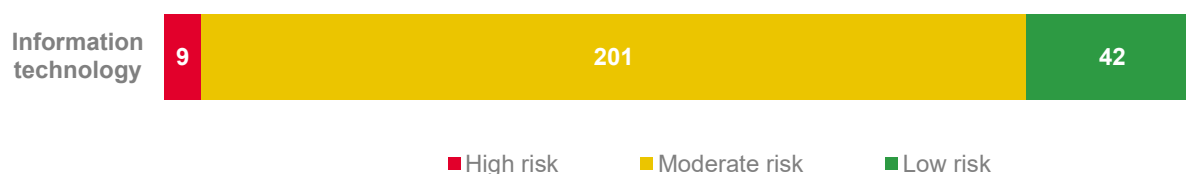
- transition UDA functions to internal systems where possible
- ensure UDAs are adequately controlled where they continue to use them
- regularly review access rights to UDAs and back-up business-critical information.

Observation	Conclusion
6.3 IT governance	
Strategy, policies and procedures	
Around one in four councils do not have an IT strategy or operational plan. Some councils also need to develop or improve IT policies and procedures.	IT governance is enhanced where there is: <ul style="list-style-type: none"> a fit-for-purpose IT strategy and operational plan appropriate policies, standards and guidelines across all critical IT processes a formally defined process to support security and access to all systems.
Sixty-six councils do not have an adequate information security policy.	
Disaster recovery and business continuity	
Our audits identified that 17 councils do not have a documented plan to recover critical business functions in the event of a disaster.	Sound management of disaster recovery and business continuity includes: <ul style="list-style-type: none"> a documented plan for how critical business functions will be recovered in the event of a disaster, which is periodically reviewed and tested the ability to restore backed-up data, which is periodically tested.
The ability to restore data from backups is critical to ensure business continuity in the face of a system disaster.	
We also found that 15 councils do not periodically test their ability to restore backups of data relevant to financial reporting.	We expect to focus on these areas in our future audits.

6.1 High risk issues

Our audits reported nine high risk information technology control issues in our audit management letters to councils.

Internal control deficiencies reported in management letters



Councils should address high risk issues as a priority as these can increase the risk of fraud and error. The high risk issues fell into three areas:

- user access controls
- privileged access controls
- user developed applications.

The chapter rounds out with some findings on IT governance.

6.2 Access to IT systems

User access controls

Access controls are informally documented and inconsistently applied

Our audit found that controls over user access at 38 councils were insufficient, or the councils could not provide evidence that their controls were operating effectively.

User access controls should ensure that individuals only have access to financial systems and data necessary to undertake their job responsibilities.

Councils need to have effective policies and procedures to create, modify and deactivate user access to minimise the risk of individuals having excessive or unauthorised access.

Our audits sought to confirm the effectiveness of user access administration over key financial systems against these principles. Where we found issues, these were mostly moderate rather than high risk because councils had mitigating controls in place.

Effective user access control involves the following good practice:



Clear policies and procedures



Formal approval to establish and modify user accounts



Removal of access when no longer required



Regular review of user access



Password parameters in line with good practice



Clear records of user access.

We identified staff at 35 councils with access to systems beyond what their job requires.

In three councils, the risks were high because there were only limited mitigating controls. In each case, we were required to perform extra audit procedures. These three councils have remediation plans in place, which we will review during our next audit.

We also found that 30 councils need to strengthen their password parameters for financial reporting systems.

Privileged access

Privileged access occurs when a person can change key system configurations and has wide access to system data, files and accounts. Our audits found examples of inappropriate privileged access, inadequate review and insufficient retention of access logs to monitor the activities of privileged system users.

To minimise the risk of individuals having inappropriate access to IT systems, councils need to strengthen their policies and procedures over privileged user access.

Staff and third-party contractors had unmonitored access to some council systems

Privileged access controls should follow the same good practice principles as general access controls discussed above. However, the impact of poor administration of privileged access controls can be greater than general access controls, because privileged access enables greater control over key IT systems.

Access to IT systems should be granted using the principle of 'least privilege'. This means that system users should only have the system access privileges needed to perform their job, and no-one should have ongoing access to highly privileged functions unless their job demands it.

Where individuals have privileged access, independent oversight should detect and rectify any inappropriate activity. Activity logs of users with privileged access should be reported to someone in a position of authority who is independent of the IT team.

Our audits found:

- IT staff, finance staff and senior management at 22 councils with inappropriate access to privileged finance applications and council data. They could bypass system-based controls or make direct changes to financial data
- fifty-six councils where there is no review of access and usage for users with highly privileged system access
- eleven councils where highly privileged generic user accounts were shared between staff and third-party contractors, limiting the effectiveness of any audit logs
- nine councils with no audit logs detailing the activity of privileged users
- two councils where audit logs were not reviewed or secured
- one council where IT staff could develop and implement changes to financial systems without any authorisation and oversight.

At five councils, these observations were high risk due to a combination of weaknesses. As a result, we were required to perform extra audit procedures to address the risk. These councils also have remediation plans in place, which we will review during our next audit.

Access controls over third-party service providers needs to be strengthened

Most councils rely on third-party service providers for IT administration support. This can be from the vendor of key council systems or an independent IT contractor. Councils need to ensure their existing risk management framework provides assurance for controls over IT outsourcing.

Our audits identified:

- nine councils where there were third parties with unrestricted and unmonitored access to council systems and data
- three councils that had cloud-based financial reporting systems where the council has no assurance that key controls at the service provider are operating effectively
- one council where there was significant reliance on the systems, knowledge and expertise of third parties with no plan should these services be withdrawn.

These examples presented a moderate risk given mitigating controls in place.

User developed applications

User developed applications (UDAs) are computing applications, tools and processes that are developed or managed outside IT administration. These pose extra risks because controls used by internal IT systems may be absent.

User developed applications allow users to bypass user access controls

Councils commonly use UDAs such as spreadsheets, databases and reporting tools in day-to-day operations. There may be internally developed workarounds when a vendor-supplied solution is absent or too expensive to implement.

Reasons why councils might use UDA tools include that they can:

- allow users to interact with council data directly and independently
- be developed cheaply and quickly compared to system enhancements that use a more traditional system development lifecycle.

At the same time, UDAs can pose significant risks. They can lack the traditional controls of a formally deployed business application, and often sit outside the defined control environment. Over time, their original purpose can be lost and their use and complexity can expand. This increases the risk of errors or intentional misuse.

Because of these risks, councils should consider migrating from UDAs to internal IT systems wherever possible. Where this is not feasible, they should implement mitigating controls such as:

- ensuring that UDAs are subject to the council's software development lifecycle requirements for specification, design, building, testing and maintenance
- reviewing and updating policies for user access controls and ensuring assigned access rights to UDAs are appropriate and periodically reviewed
- ensuring all business-critical UDAs are backed up regularly and their recoverability tested.

Our audits found:

- twenty-two councils where spreadsheets were used for business operations, decision making and financial reporting that were not adequately secured, with changes that were not tracked, tested or reviewed. Examples included the calculation of development application fees and depreciation
- five councils where finance staff and senior management had inappropriate access, using database query tools to directly modify financial data in database tables, circumventing system-based business process controls.

These observations were mostly classed as moderate risk as there were mitigating controls in place. However, it was a high risk issue at one council because of the importance of the data maintained in spreadsheets and the lack of access and version controls.

6.3 Information technology governance

IT governance refers to the strategies and frameworks, policies and processes that councils use to oversee and manage IT risks.

Strategy, policies and procedures

One in four councils do not have an IT strategy or operational plan

An IT strategy and an operational plan are important for achieving the best use of IT resources.

An IT strategy links technology use to the wider objectives of a council. It needs to be fit for purpose and take into account the size and complexity of a particular council.

An IT operational plan sets out the day-to-day tasks, time frames, responsibilities and resources needed to realise the goals of an IT strategy.

Thirty-one councils did not have an IT strategy or operational plan.

Effective IT governance is strengthened when:



There is an IT strategy and operational plan in place that is fit for purpose and suits the size and complexity of the council



Appropriate policies (such as an information security policy), standards and guidelines are available to staff and contractors across all critical IT processes. These are reviewed and updated periodically, including when significant system or process changes occur



There are processes to consider, capture and monitor IT risks that would affect operations.

We also found that 16 councils had an IT operational plan but not an IT strategy. Without an IT strategy, there is a risk that IT investment is not aligned with council priorities. Some councils need to develop or improve IT policies and procedures.

Clear and well-defined IT policies and procedures help organisations to implement their strategies and plans. Our audits found the following issues across 33 councils:

- twenty-four councils without formal IT policies and procedures over IT security, change management, disaster recovery and/or business continuity
- seventeen councils without a formal and defined process to appropriately support access management for financial reporting systems
- seventeen councils that need to strengthen existing policies and procedures for IT security, change management or disaster recovery
- two councils that had not reviewed or updated IT policies and procedures in several years.

Over half of councils do not have an information security policy

We identified that 66 councils do not have a formal information security policy. Without this, councils are likely to rely on the knowledge, risk appetite and diligence of individual staff to maintain the security of key IT systems. All councils should have a formally defined process to support the security of and access to all systems.

On 2 March 2018, the Audit Office tabled a performance audit report on 'Detecting and responding to cyber security incidents'. Cyber security incidents can harm government service delivery and may include theft of personal information, denial of access to critical technology, or even the hijacking of systems for profit or malicious intent. Recent global and national security incidents highlight the importance for councils to have systems and processes for detecting and responding effectively to security incidents.

Disaster recovery and business continuity

Councils can improve backup, disaster recovery and business continuity controls

The ability to restore data from valid backups is critical to ensure business continuity. Without it, councils may be unable to continue providing essential public services in the face of a system disaster.

Councils need to thoroughly assess their business systems and documented plan outlining how critical business functions will be recovered in the event of a disaster. Once plans are in place, they then need to be reviewed and tested regularly. The ability to restore backed-up data should also be periodically tested.

We found that 17 councils do not have a documented plan to recover from a disaster. We also found that 15 councils do not periodically test their ability to restore backups of data relevant to financial reporting.

Without these measures, there may not be a clear process to minimise the impact of a significant incident interrupting critical business functions to ensure the continued delivery of services.

We expect to focus on these areas in our future audits.



Appendices



Appendix one – Response from the Office of Local Government

Strengthening local government



**Office of
Local Government**

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Ms Margaret Crawford
Auditor-General of New South Wales
Audit Office of New South Wales
GPO Box 12
SYDNEY NSW 2001

Dear Ms Crawford

Thank you for your letter dated 23 March 2018 and for the opportunity to respond to your proposed Local Government 2017 report to Parliament.

The Office of Local Government welcomes the contribution from the Audit Office towards strengthening governance, financial management and reporting in the local government sector and notes your findings and recommendations.

We look forward to continuing work with the Audit Office in the future.

Yours sincerely

Tim Hurst
Acting Chief Executive
Office of Local Government

19/4/18

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Appendix two – List of recommendations

The table below lists the recommendations made in this report.



Financial reporting

Quality of financial reporting

Councils can improve the quality of financial reporting by reviewing their financial statements close processes to identify areas for improvements.

Councils can improve the quality of financial reporting by involving an audit, risk and improvement committee in the review of financial statements.

The Office of Local Government should release the Local Government Code of Accounting Practice and Financial Reporting and the End of Year Financial Reporting Circular earlier in the audit cycle, ideally by 30 April each year.

The Local Government Code of Accounting Practice and Financial Reporting should align with Australian Accounting Standards.

Timeliness of financial reporting

The Office of Local Government should introduce early close procedures with an emphasis on asset valuations.



Asset management

Recognition and asset useful life estimates

The Office of Local Government should address the different practices across the local government sector in accounting for rural fire-fighting equipment before 30 June 2018. In doing so, the Office of Local Government should work with NSW Treasury to ensure there is a whole-of-government approach.



Governance and internal controls

Governance

Councils should early adopt the proposed requirement to establish an audit, risk and improvement committee.

The Office of Local Government should introduce the requirement for councils to establish internal audit functions and update its 2010 Internal Audit Guidelines.

The Office of Local Government should maintain an accurate register of entities approved under section 358 of the *Local Government Act 1993*.

The Office of Local Government should consider establishing a financial reporting framework for council entities.



Appendix three – Sources of information and council classifications

Sources of information

This report comments on the results of audits completed on the 2016–17 financial statements of 139 councils and two water authorities and the completed audits of eight councils' and three water authorities' 2015–16 financial statements. The audit of one council's 2016–17 financial statements is ongoing as the council received a lodgement extension from the Office of Local Government.

In addition to the audited financial statements, the comments and analysis in this report has been drawn from:

- data collected from councils
- audit findings reported to councils
- data from external sources, including population, kilometres of roads, and council area data from the Australian Bureau of Statistics and the Office of Local Government.

Council classifications

We adopted the following methodology when classifying councils in our report.

OLG classification	Audit Office grouping
Metropolitan	Metropolitan
Regional Town/City	Regional
Metropolitan Fringe	Metropolitan
Rural	Rural
Large Rural	Rural

Source: OLG classifications and Audit Office of New South Wales.

Below is a list of councils and county councils by classification.

Council classifications

Local councils	OLG classification	Classification in this report
Albury City Council	Regional Town/City	Regional
Armidale Regional Council	Regional Town/City	Regional
Ballina Shire Council	Regional Town/City	Regional
Balranald Shire Council	Rural	Rural
Bathurst Regional Council	Regional Town/City	Regional
Bayside Council	Metropolitan	Metropolitan
Bega Valley Shire Council	Regional Town/City	Regional
Bellingen Shire Council	Large Rural	Rural
Berrigan Shire Council	Large Rural	Rural
Blacktown City Council	Metropolitan	Metropolitan
Bland Shire Council	Large Rural	Rural
Blayney Shire Council	Large Rural	Rural
Blue Mountains City Council	Metropolitan Fringe	Metropolitan

Local councils	OLG classification	Classification in this report
Bogan Shire Council	Rural	Rural
Bourke Shire Council	Rural	Rural
Brewarrina Shire Council	Rural	Rural
Broken Hill City Council	Regional Town/City	Regional
Burwood Council	Metropolitan	Metropolitan
Byron Shire Council	Regional Town/City	Regional
Cabonne Council	Large Rural	Rural
Camden Council	Metropolitan Fringe	Metropolitan
Campbelltown City Council	Metropolitan Fringe	Metropolitan
City of Canada Bay Council	Metropolitan	Metropolitan
Canterbury Bankstown Council	Metropolitan	Metropolitan
Carrathool Shire Council	Rural	Rural
Central Coast Council	Metropolitan Fringe	Metropolitan
Central Darling Shire Council	Rural	Rural
Cessnock City Council	Regional Town/City	Regional
Clarence Valley Council	Regional Town/City	Regional
Cobar Shire Council	Large Rural	Rural
Coffs Harbour City Council	Regional Town/City	Regional
Coolamon Shire Council	Rural	Rural
Coonamble Shire Council	Rural	Rural
Cootamundra-Gundagai Regional Council	Large Rural	Rural
Cowra Shire Council	Large Rural	Rural
Cumberland Council	Metropolitan	Metropolitan
Dubbo Regional Council	Regional Town/City	Regional
Dungog Shire Council	Large Rural	Rural
Edward River Council	Large Rural	Rural
Eurobodalla Shire Council	Regional Town/City	Regional
Fairfield City Council	Metropolitan	Metropolitan
Federation Council	Large Rural	Rural
Forbes Shire Council	Large Rural	Rural
Georges River Council	Metropolitan	Metropolitan
Gilgandra Shire Council	Rural	Rural
Glen Innes Severn Council	Large Rural	Rural
Goulburn Mulwaree Council	Regional Town/City	Regional
Greater Hume Shire Council	Large Rural	Rural
Griffith City Council	Regional Town/City	Regional
Gunnedah Shire Council	Large Rural	Rural
Gwydir Shire Council	Large Rural	Rural
Hawkesbury City Council	Metropolitan Fringe	Metropolitan

Local councils	OLG classification	Classification in this report
Hay Shire Council	Rural	Rural
Hills Shire Council, The	Metropolitan Fringe	Metropolitan
Hilltops Council	Large Rural	Rural
Hornsby, The Council of the Shire of	Metropolitan Fringe	Metropolitan
Hunters Hill, The Council of the Municipality of	Metropolitan	Metropolitan
Inner West Council	Metropolitan	Metropolitan
Inverell Shire Council	Large Rural	Rural
Junee Shire Council	Large Rural	Rural
Kempsey Shire Council	Regional Town/City	Regional
Kiama, the Council of the Municipality of	Regional Town/City	Regional
Ku-ring-gai Council	Metropolitan	Metropolitan
Kyogle Council	Large Rural	Rural
Lachlan Shire Council	Large Rural	Rural
Lake Macquarie City Council	Regional Town/City	Regional
Lane Cove Municipal Council	Metropolitan	Metropolitan
Leeton Shire Council	Large Rural	Rural
Lismore City Council	Regional Town/City	Regional
Lithgow Council, City of	Regional Town/City	Regional
Liverpool City Council	Metropolitan	Metropolitan
Liverpool Plains Shire Council	Large Rural	Rural
Lockhart Shire Council	Rural	Rural
Maitland City Council	Regional Town/City	Regional
Mid-Coast Council	Regional Town/City	Regional
Mid-Western Regional Council	Regional Town/City	Regional
Moree Plains Shire Council	Large Rural	Rural
Mosman Municipal Council	Metropolitan	Metropolitan
Murray River Council	Large Rural	Rural
Murrumbidgee Council	Rural	Rural
Muswellbrook Shire Council	Large Rural	Rural
Nambucca Shire Council	Large Rural	Rural
Narrabri Shire Council	Large Rural	Rural
Narrandera Shire Council	Large Rural	Rural
Narromine Shire Council	Large Rural	Rural
Newcastle City Council	Regional Town/City	Regional
North Sydney Council	Metropolitan	Metropolitan
Northern Beaches Council	Metropolitan	Metropolitan
Oberon Council	Large Rural	Rural
Orange City Council	Regional Town/City	Regional

Local councils	OLG classification	Classification in this report
Parkes Shire Council	Large Rural	Rural
Parramatta Council, City of	Metropolitan	Metropolitan
Penrith City Council	Metropolitan Fringe	Metropolitan
Port Macquarie-Hastings Council	Regional Town/City	Regional
Port Stephens Council	Regional Town/City	Regional
Queanbeyan-Palerang Regional Council	Regional Town/City	Regional
Randwick City Council	Metropolitan	Metropolitan
Richmond Valley Council	Regional Town/City	Regional
Ryde City Council	Metropolitan	Metropolitan
Shellharbour City Council	Regional Town/City	Regional
Shoalhaven City Council	Regional Town/City	Regional
Singleton Council	Regional Town/City	Regional
Snowy Monaro Regional Council	Regional Town/City	Regional
Snowy Valleys Council	Large Rural	Rural
Strathfield Municipal Council	Metropolitan	Metropolitan
Sutherland Shire Council	Metropolitan	Metropolitan
Sydney, Council of the City of	Metropolitan	Metropolitan
Tamworth Regional Council	Regional Town/City	Regional
Temora Shire Council	Large Rural	Rural
Tenterfield Shire Council	Large Rural	Rural
Tweed Shire Council	Regional Town/City	Regional
Upper Hunter Shire Council	Large Rural	Rural
Upper Lachlan Shire Council	Large Rural	Rural
Uralla Shire Council	Large Rural	Rural
Wagga Wagga City Council	Regional Town/City	Regional
Walcha Council	Rural	Rural
Walgett Shire Council	Large Rural	Rural
Warren Shire Council	Rural	Rural
Warrumbungle Shire Council	Large Rural	Rural
Waverley Council	Metropolitan	Metropolitan
Weddin Shire Council	Rural	Rural
Wentworth Shire Council	Large Rural	Rural
Willoughby City Council	Metropolitan	Metropolitan
Wingecarribee Shire Council	Regional Town/City	Regional
Wollondilly Shire Council	Metropolitan Fringe	Metropolitan
Wollongong City Council	Regional Town/City	Regional
Woollahra Municipal Council	Metropolitan	Metropolitan
Yass Valley Council	Large Rural	Rural

Source: OLG classifications and Audit Office of New South Wales.

County councils

County council	Geographical region	Classification in this report
Castlereagh-Macquarie County Council	Far West	County
Central Murray County Council	Riverina Murray	County
Central Tablelands County Council	Central West and Orana	County
Goldenfields Water County Council	Riverina Murray	County
Hawkesbury River County Council	Metropolitan Sydney	County
Mid-Coast County Council*	Hunter	County
New England Tablelands County Council	New England North West	County
Riverina Water County Council	Riverina Murray	County
Rous County Council	North Coast	County
Southern Slopes County Council*	South East and Tablelands	County
Upper Hunter County Council	Hunter	County
Upper Macquarie County Council	Central West and Orana	County

* Mid-Coast and Southern Slopes county councils were dissolved on 1 July 2017.

Source: OLG classifications and Audit Office of New South Wales.



Appendix four – Councils amalgamated in 2016

Newly amalgamated council	Former councils	Date of amalgamation
Armidale Regional Council	Armidale Dumaresq Council Guyra Shire Council	12 May 2016 ¹
Bayside Council	City of Botany Bay Council Rockdale City Council	9 September 2016 ³
Canterbury-Bankstown Council	Bankstown City Council Canterbury City Council	12 May 2016 ¹
Central Coast Council	Gosford City Council Wyong Shire Council	12 May 2016 ¹
City of Parramatta Council	Parramatta City Council The Hills Shire Council Auburn City Council Holroyd City Council Hornsby Shire Council	12 May 2016 ²
Cootamundra-Gundagai Council	Cootamundra Shire Council Gundagai Shire Council	12 May 2016 ¹
Cumberland Council	Parramatta City Council Auburn City Council Holroyd City Council	12 May 2016 ²
Dubbo Regional Council	Dubbo City Council Wellington Council	12 May 2016 ¹
Edward River Council	Conargo Shire Council Deniliquin Council	12 May 2016 ¹
Federation Council	Corowa Shire Council Urana Shire Council	12 May 2016 ¹

Newly amalgamated council	Former councils	Date of amalgamation
Georges River Council	Hurstville City Council Kogarah City Council	12 May 2016 ¹
Hilltops Council	Boorowa Council Harden Shire Council Young Shire Council	12 May 2016 ¹
Inner West Council	Ashfield Council Leichhardt Municipal Council Marrickville Council	12 May 2016 ¹
Mid-Coast Council	Gloucester Shire Council Great Lakes Council Greater Taree City Council	12 May 2016 ¹
Murray River Council	Murray Shire Council Wakool Shire Council	12 May 2016 ¹
Murrumbidgee Council	Jerilderie Shire Council Murrumbidgee Shire Council	12 May 2016 ¹
Northern Beaches Council	Manly Council Pittwater Council Warringah Council	12 May 2016 ¹
Queanbeyan-Palerang Regional Council	Palerang Council Queanbeyan City Council	12 May 2016 ¹
Snowy Monaro Regional Council	Bombala Council Cooma-Monaro Shire Council Snowy River Shire Council	12 May 2016 ¹
Snowy Valleys Council	Tumbarumba Shire Council Tumut Shire Council	12 May 2016 ¹

1 Local Government (Council Amalgamations) Proclamation 2016 dated 12 May 2016.

2 Local Government (City of Parramatta and Cumberland) Proclamation 2016 dated 12 May 2016.

3 Local Government (Bayside) Proclamation 2016 dated 9 September 2016.



Appendix five – Status of audits

Below is a summary of the status of the 2016–17 and 2015–16 financial statement audits, including the type of audit opinion and the date it was issued.

2016–17 audits

Key

Type of audit opinion		Date of audit opinion	
Unmodified opinion.		Financial statements were lodged by the statutory deadline of 31 October 2017.	
Unmodified opinion with emphasis of matter.		Extensions to the statutory deadline (and met).	
Modified opinion: Qualified opinion, an adverse opinion, or a disclaimer of opinion. Audit report not yet issued.		Financial statements not submitted as at tabling date.	

Local council	Type of audit opinion		Date of audit opinion	
Albury City Council	Unmodified		23 October 2017	
Armidale Regional Council	Unmodified		7 December 2017	
Ballina Shire Council	Unmodified		26 October 2017	
Balranald Shire Council	Unmodified		31 October 2017	
Bathurst Regional Council	Unmodified		23 October 2017	
Bayside Council ⁶	Not yet issued		Not yet issued	
Bega Valley Shire Council	Unmodified		31 October 2017	
Bellingen Shire Council	Unmodified		25 October 2017	
Berrigan Shire Council	Unmodified		18 October 2017	
Blacktown City Council	Unmodified		26 October 2017	
Bland Shire Council	Unmodified		28 February 2018	
Blayney Shire Council	Unmodified		24 October 2017	
Blue Mountains City Council	Unmodified		31 October 2017	
Bogan Shire Council	Unmodified		25 October 2017	
Bourke Shire Council	Unmodified		27 October 2017	
Brewarrina Shire Council	Unmodified		28 February 2018	
Broken Hill City Council	Unmodified		19 October 2017	
Burwood Council	Unmodified		18 October 2017	
Byron Shire Council	Unmodified		26 October 2017	
Cabonne Council	Unmodified		23 October 2017	

⁶ The Office of Local Government granted Bayside City Council with an extension until 31 May 2018. The council has not yet presented their 2016–17 financial statements for audit as the financial records were not ready. The outcome of this incomplete audit will be reported in next year's report.

Local council	Type of audit opinion		Date of audit opinion	
Camden Council	Unmodified	✓	27 October 2017	✓
Campbelltown City Council	Unmodified	✓	15 September 2017	✓
City of Canada Bay Council	Unmodified	✓	12 October 2017	✓
Canterbury Bankstown Council	Unmodified	✓	30 November 2017	✓
Carrathool Shire Council	Unmodified	✓	30 October 2017	✓
Central Coast Council	Unmodified	✓	9 March 2018	✓
Central Darling Shire Council	Unmodified (with Emphasis of Matter)	⚠	28 February 2018	✓
Cessnock City Council	Unmodified	✓	11 October 2017	✓
Clarence Valley Council	Unmodified	✓	6 November 2017	✓
Cobar Shire Council	Unmodified	✓	30 November 2017	✓
Coffs Harbour City Council	Unmodified	✓	26 October 2017	✓
Coolamon Shire Council	Unmodified	✓	23 October 2017	✓
Coonamble Shire Council	Unmodified	✓	10 November 2017	✓
Cootamundra-Gundagai Regional Council	Unmodified	✓	30 October 2017	✓
Cowra Shire Council	Unmodified	✓	26 October 2017	✓
Cumberland Council	Unmodified	✓	21 December 2017	✓
Dubbo Regional Council	Unmodified	✓	27 February 2018	✓
Dungog Shire Council	Unmodified	✓	28 February 2018	✓
Edward River Council	Unmodified	✓	15 December 2017	✓
Eurobodalla Shire Council	Unmodified	✓	27 October 2017	✓
Fairfield City Council	Unmodified	✓	25 October 2017	✓
Federation Council	Unmodified	✓	30 October 2017	✓
Forbes Shire Council	Unmodified	✓	30 October 2017	✓
Georges River Council	Unmodified	✓	14 November 2017	✓
Gilgandra Shire Council	Unmodified	✓	22 November 2017	✓
Glen Innes Severn Council	Unmodified	✓	19 December 2017	✓
Goulburn Mulwaree Council	Unmodified	✓	4 December 2017	✓
Greater Hume Shire Council	Unmodified	✓	23 October 2017	✓
Griffith City Council	Unmodified	✓	23 October 2017	✓
Gunnedah Shire Council	Unmodified	✓	20 October 2017	✓
Gwydir Shire Council	Unmodified	✓	31 October 2017	✓
Hawkesbury City Council	Unmodified	✓	27 October 2017	✓
Hay Shire Council	Unmodified	✓	30 October 2017	✓
Hills Shire Council, The	Qualified opinion	!	29 September 2017	✓

Local council	Type of audit opinion		Date of audit opinion	
Hilltops Council	Unmodified	✓	29 November 2017	✓
Hornsby, The Council of the Shire of	Unmodified	✓	20 October 2017	✓
Hunters Hill, The Council of the Municipality of	Unmodified	✓	31 October 2017	✓
Inner West Council	Unmodified	✓	27 October 2017	✓
Inverell Shire Council	Unmodified	✓	26 October 2017	✓
Junee Shire Council	Qualified opinion	!	30 October 2017	✓
Kempsey Shire Council	Unmodified	✓	9 November 2017	✓
Kiama, The Council of the Municipality of	Unmodified	✓	20 November 2017	✓
Ku-ring-gai Council	Unmodified	✓	12 October 2017	✓
Kyogle Council	Unmodified	✓	31 October 2017	✓
Lachlan Shire Council	Unmodified	✓	30 November 2017	✓
Lake Macquarie City Council	Unmodified	✓	24 October 2017	✓
Lane Cove Municipal Council	Unmodified	✓	30 October 2017	✓
Leeton Shire Council	Unmodified	✓	19 October 2017	✓
Lismore City Council	Unmodified	✓	17 October 2017	✓
Lithgow Council, City of	Unmodified	✓	21 November 2017	✓
Liverpool City Council	Unmodified	✓	27 October 2017	✓
Liverpool Plains Shire Council	Unmodified	✓	30 November 2017	✓
Lockhart Shire Council	Unmodified	✓	20 October 2017	✓
Maitland City Council	Unmodified	✓	13 October 2017	✓
Mid-Coast Council	Unmodified	✓	20 December 2017	✓
Mid-Western Regional Council	Unmodified	✓	3 October 2017	✓
Moree Plains Shire Council	Unmodified	✓	27 February 2018	✓
Mosman Municipal Council	Unmodified	✓	25 October 2017	✓
Murray River Council	Unmodified	✓	23 February 2018	✓
Murrumbidgee Council	Unmodified	✓	29 November 2017	✓
Muswellbrook Shire Council	Unmodified	✓	30 October 2017	✓
Nambucca Shire Council	Unmodified	✓	27 October 2017	✓
Narrabri Shire Council	Unmodified	✓	31 October 2017	✓
Narrandera Shire Council	Unmodified	✓	20 October 2017	✓
Narromine Shire Council	Unmodified	✓	26 October 2017	✓
Newcastle City Council	Unmodified	✓	13 October 2017	✓
North Sydney Council	Unmodified	✓	31 October 2017	✓
Northern Beaches Council	Unmodified	✓	20 December 2017	✓

Local council	Type of audit opinion		Date of audit opinion	
Oberon Council	Unmodified	✓	18 October 2017	✓
Orange City Council	Unmodified	✓	30 October 2017	✓
Parkes Shire Council	Unmodified	✓	5 October 2017	✓
Parramatta Council, City of	Unmodified	✓	13 December 2017	✓
Penrith City Council	Unmodified	✓	26 September 2017	✓
Port Macquarie-Hastings Council	Unmodified	✓	31 October 2017	✓
Port Stephens Council	Unmodified	✓	26 October 2017	✓
Queanbeyan-Palerang Regional Council	Unmodified	✓	27 February 2018	✓
Randwick City Council	Unmodified	✓	13 October 2017	✓
Richmond Valley Council	Unmodified	✓	19 October 2017	✓
Ryde City Council	Unmodified	✓	25 October 2017	✓
Shellharbour City Council	Unmodified	✓	20 October 2017	✓
Shoalhaven City Council	Unmodified	✓	31 October 2017	✓
Singleton Council	Unmodified	✓	27 October 2017	✓
Snowy Monaro Regional Council	Unmodified	✓	22 November 2017	✓
Snowy Valleys Council	Unmodified	✓	27 October 2017	✓
Strathfield Municipal Council	Unmodified	✓	30 October 2017	✓
Sutherland Shire Council	Unmodified	✓	24 October 2017	✓
Sydney, Council of the City of	Unmodified	✓	24 October 2017	✓
Tamworth Regional Council	Unmodified	✓	26 October 2017	✓
Temora Shire Council	Unmodified	✓	23 October 2017	✓
Tenterfield Shire Council	Unmodified	✓	28 November 2017	✓
Tweed Shire Council	Unmodified	✓	27 October 2017	✓
Upper Hunter Shire Council	Unmodified	✓	31 October 2017	✓
Upper Lachlan Shire Council	Unmodified	✓	10 October 2017	✓
Uralla Shire Council	Unmodified	✓	31 October 2017	✓
Wagga Wagga City Council	Unmodified	✓	23 October 2017	✓
Walcha Council	Unmodified	✓	25 October 2017	✓
Walgett Shire Council	Unmodified	✓	23 February 2018	✓
Warren Shire Council	Unmodified	✓	17 October 2017	✓
Warrumbungle Shire Council	Unmodified	✓	16 November 2017	✓
Waverley Council	Unmodified	✓	31 October 2017	✓
Weddin Shire Council	Unmodified	✓	31 October 2017	✓
Wentworth Shire Council	Unmodified	✓	31 October 2017	✓






Local council	Type of audit opinion		Date of audit opinion	
Willoughby City Council	Unmodified	✓	30 October 2017	✓
Wingecarribee Shire Council	Unmodified	✓	16 October 2017	✓
Wollondilly Shire Council	Unmodified	✓	16 October 2017	✓
Wollongong City Council	Unmodified	✓	10 October 2017	✓
Woollahra Municipal Council	Unmodified	✓	31 October 2017	✓
Yass Valley Council	Qualified opinion	!	30 October 2017	✓















County council	Type of audit opinion		Date of audit opinion	
Castlereagh Macquarie County Council	Unmodified	✓	28 February 2018	✓
Central Murray County Council	Unmodified	✓	31 October 2017	✓
Central Tablelands County Council	Unmodified	✓	20 November 2017	✓
Former MidCoast Water	Unmodified	✓	22 February 2018	✓
Goldenfields Water County Council	Unmodified	✓	11 October 2017	✓
Hawkesbury River County Council	Unmodified	✓	30 November 2017	✓
New England Tablelands County Council	Unmodified	✓	10 October 2017	✓
Riverina Water County Council	Unmodified	✓	11 October 2017	✓
Rous County Council	Unmodified	✓	18 October 2017	✓
Southern Slopes County Council	Unmodified	✓	31 October 2017	✓
Upper Hunter County Council	Unmodified	✓	30 October 2017	✓
Upper Macquarie County Council	Unmodified	✓	27 October 2017	✓



Water authority	Type of audit opinion		Date of audit opinion	
Central Coast Council Water Supply Authority	Unmodified	✓	9 March 2018	✓
Cobar Water Board	Unmodified	✓	22 September 2017	✓







2015–16 audits

Key

Type of audit opinion		Date of audit opinion	
Unmodified opinion.		Financial statements were lodged by the statutory deadline of 31 October 2017.	
Unmodified opinion with emphasis of matter.		Extensions to the statutory deadline (and met).	
Modified opinion: Qualified opinion, an adverse opinion, or a disclaimer of opinion.			
Audit report not yet issued.			

Local council	Type of audit opinion		Date of audit opinion	
Armidale Dumaresq Council, The former	Unmodified		14 February 2017	
City of Botany Bay Council, The former	Disclaimer of opinion		9 April 2018	
Conargo Shire Council, The former	Unmodified		21 December 2016	
Deniliquin Council, The former	Unmodified		3 February 2017	
Guyra Shire Council, The former	Unmodified		20 December 2016	
Liverpool City Council	Unmodified		26 October 2016	
MidCoast Water	Unmodified		27 October 2016	

County council	Type of audit opinion		Date of audit opinion	
New England Tablelands County Council	Unmodified		5 September 2016	

Water authority	Type of audit opinion		Date of audit opinion	
Cobar Water Board	Unmodified		4 October 2016	
Gosford Water Supply Water Authority, The former	Disclaimer of opinion		25 May 2017	
Wyong Shire Council Water Authority, The former	Unmodified		14 December 2016	



Appendix six – Council spending by function – Definitions from the Local Government Code of Accounting Practice and Financial Reporting

Category	Council expenditure on:
Governance	Costs relating to council's role as a component of democratic government, including elections, councillors' fees and expenses, subscriptions to local authority associations, meetings of Council and policy-making committees, public disclosure and legislative compliance.
Administration	Corporate support and other support services, engineering works and council policy compliance.
Public order and safety	Delivery of fire protection, emergency services, beach control, enforcement of regulations and animal control services.
Health	Immunisation, food control and health centres.
Environment	Noxious plants and insect/vermin control, other environmental protection, solid waste management including domestic and other waste, other sanitation, garbage, street cleaning, drainage and stormwater management.
Community services and education	Administration and education, social protection (welfare), migrant, Aboriginal and other community services and administration, youth services, aged and disabled persons services, children's services including family day care, child care and other family and child services.
Housing and community amenities	Public cemeteries, public conveniences, street lighting, town planning, other community amenities including housing development, accommodation for families, children, aged persons, disabled persons, migrants and Indigenous persons.
Water	Water services.
Sewerage	Sewer services.
Recreation and culture	Public libraries, museums, art galleries, community centres and halls including public halls and performing arts venues, sporting grounds and venues, swimming pools, parks, gardens, lakes and other sporting, recreational and cultural services.
Agriculture	Administration of agricultural services, supervision and regulation of the agricultural industry, operation of flood control and irrigation systems, operation of support services to farmers including vet services, pest control services, crop inspection and crop grading services.
Fuel and energy	Gas supplies.
Mining, manufacturing and construction	Building control, quarries and pits, mineral resources and abattoirs.
Transport and communication	Sealed and unsealed roads, bridges, footpaths, parking areas and aerodromes.
Economic affairs	Camping areas and caravan parks, tourism and area promotion, industrial development promotion, sale yards and markets, real estate development, commercial nurseries and other business undertakings.

Source: Local Government Code of Accounting Practice and Financial Reporting.



Appendix seven – OLG's performance indicators from the audited financial statement - Descriptions

Audited performance indicator	Formula	Description
Operating performance	Total continuing operating revenue [#] excluding capital grants and contributions less operating expenses	The 'operating performances ratio' measures how well local councils contained expenses within revenue.
	Total continuing operating revenue [#] excluding capital grants and contributions	The benchmark set by the Office of Local Government (OLG) for the ratio is greater than zero per cent.
Own source operating revenue	Total continuing operating revenue [#] excluding all grants and contributions	The 'own source operating revenue ratio' measures a council's fiscal flexibility and the degree to which it relies on external funding sources such as operating grants and contributions.
	Total continuing operating revenue [#] inclusive of all grants and contributions	The benchmark set by OLG for the ratio is greater than 60 per cent.
Unrestricted current ratio	Current assets less all external restrictions	The 'unrestricted current ratio' is specific to the local government sector and represents a council's ability to meet its short-term obligations as they fall due.
	Current liabilities less specific-purpose liabilities	The benchmark set by OLG for the ratio is greater than 1.5 times.
Debt service cover ratio	Operating result [#] before capital excluding interest and impairment, depreciation and amortisation	The 'debt service cover ratio' measures the operating cash available to service debt including interest, principal and lease payments.
	Principal repayments plus borrowing costs	The benchmark set by OLG for the ratio is greater than two times.
Rates and annual charges outstanding percentage	Rates and annual charges outstanding	The 'rates and annual charges outstanding ratio' assesses the impact of uncollected rates and annual charges on a council's liquidity and the adequacy of debt recovery efforts.
	Rates and annual charges collectible	The benchmark set by OLG for the ratio is less than five per cent for metropolitan and less than ten per cent for rural councils.
Cash expense cover ratio	Current year cash and cash equivalents, and term deposits *12	The 'cash expense cover ratio' indicates the number of months a council can continue paying its expenses without additional cash inflows.
	Payments from cash flow of operating and financing activities	The benchmark set by OLG for the ratio is greater than three months.

Excludes fair value adjustments, reversal of revaluation decrements, net gain/loss on sale of assets, and net share/loss of interests in joint ventures.

Source: Local Government Code of Accounting Practice and Financial Reporting.



Appendix eight – OLG's performance indicators from the unaudited special schedule 7 - Descriptions


Unaudited performance indicator	Formula	Description
Buildings and infrastructure renewals ratio	Asset renewals	The 'building and infrastructure renewals ratio' assesses the rate at which assets are being renewed against the rate at which they are depreciating. The benchmark set by OLG for the ratio is greater than 100 per cent.
	Depreciation, amortisation and impairment	
Infrastructure backlog ratio	Estimated cost to bring assets to a satisfactory condition	The 'infrastructure backlog ratio' represents the proportion of infrastructure backlog to the total net book value of a council's infrastructure assets. The benchmark set by OLG for the ratio is less than two per cent.
	Carrying value of infrastructure, building, other structures and depreciable land improvement assets	
Asset maintenance ratio	Actual asset maintenance	The 'asset maintenance ratio' compares actual versus required annual asset maintenance. The benchmark set by OLG for the ratio is greater than 100 per cent.
	Required asset maintenance	
Cost to bring assets to agreed service level	Estimated cost to bring assets to an agreed level of service set by council	The 'cost to bring assets to agreed service level' reflects the actual value of identified renewal works to be delivered in the future, compared to the total replacement cost of assets. OLG has not prescribed a benchmark for this performance indicator.
	Gross replacement cost	

Source: Local Government Code of Accounting Practice and Financial Reporting.




Appendix nine – Financial information

We have included a summary of key financial information from the 2016–17 audited financial statements of councils.

2016–17					
Local council	Total revenue	Total expenses	Operating result ⁷	Total assets	Total liabilities
	\$m	\$m	\$m	\$m	\$m
Albury City Council	139	104	35	1,395	74
Armidale Regional Council	93	77	16	909	48
Ballina Shire Council	115	85	30	1,257	104
Balranald Shire Council	15	13	2	123	5
Bathurst Regional Council	129	93	36	1,325	48
Bayside Council 	--	--	--	--	--
Bega Valley Shire Council	96	93	3	1,002	53
Bellingen Shire Council	31	29	2	466	15
Berrigan Shire Council	26	19	7	254	5
Blacktown City Council	583	314	269	4,016	162
Bland Shire Council	29	19	10	400	10
Blayney Shire Council	23	18	5	237	7
Blue Mountains City Council	119	110	9	800	61
Bogan Shire Council	21	17	4	224	5
Bourke Shire Council	29	21	8	256	8
Brewarrina Shire Council	16	13	3	138	5
Broken Hill City Council	37	43	(6)	242	18
Burwood Council	49	42	7	421	23
Byron Shire Council	99	78	21	854	82
Cabonne Council	50	37	13	621	11
Camden Council	189	92	97	1,400	79
Campbelltown City Council	254	143	111	2,639	51
City of Canada Bay Council	110	81	29	1,629	31



⁷ Operating result represents the 'Net operating result for the year' in accordance with Australian Accounting Standards. Councils also report the 'Net operating result for the year before capital grants and contributions provided for capital purposes' in their financial statements.

 Bayside council received a lodgement extension for the 2016–17 financial statements to 31 May 2018 and has not yet presented them for audit.

2016–17

Local council	Total revenue	Total expenses	Operating result ⁷	Total assets	Total liabilities
	\$m	\$m	\$m	\$m	\$m
Canterbury Bankstown Council	355	314	41	3,707	101
Carrathool Shire Council	24	18	6	231	7
Central Coast Council	724	568	156	7,388	494
Central Darling Shire Council	25	19	6	174	4
Cessnock City Council	95	76	19	789	38
Clarence Valley Council	135	146	(11)	2,130	156
Cobar Shire Council	37	33	4	316	5
Coffs Harbour City Council	219	165	54	2,229	193
Coolamon Shire Council	17	13	4	187	10
Coonamble Shire Council	25	19	6	306	4
Cootamundra-Gundagai Regional Council	49	44	5	416	9
Cowra Shire Council	42	35	7	614	26
Cumberland Council	244	206	38	2,356	68
Dubbo Regional Council	202	141	61	2,549	98
Dungog Shire Council	22	20	2	319	7
Edward River Council	48	38	10	421	9
Eurobodalla Shire Council	129	106	23	1,382	82
Fairfield City Council	195	153	42	1,918	43
Federation Council	54	38	16	504	11
Forbes Shire Council	37	36	1	310	33
Georges River Council	180	140	40	1,412	36
Gilgandra Shire Council	36	28	8	309	20
Glen Innes Severn Council	32	27	5	268	25
Goulburn Mulwaree Council	82	63	19	1,012	55
Greater Hume Shire Council	38	31	7	504	14
Griffith City Council	64	50	14	757	32
Gunnedah Shire Council	47	36	11	463	30
Gwydir Shire Council	28	25	3	434	18
Hawkesbury City Council	94	76	18	1,032	27
Hay Shire Council	14	12	2	81	4

2016–17

Local council	Total revenue	Total expenses	Operating result ⁷	Total assets	Total liabilities
	\$m	\$m	\$m	\$m	\$m
The Hills Shire Council 	257	130	127	5,026	67
Hilltops Council	85	83	2	605	36
The Council of the Shire of Hornsby	162	118	44	1,660	54
The Council of the Municipality of Hunters Hill	16	16	--	219	6
Inner West Council	316	258	58	2,391	78
Inverell Shire Council	41	33	8	688	13
Junee Shire Council 	17	14	3	143	10
Kempsey Shire Council	73	73	--	1,065	59
The Council of the Municipality of Kiama	74	53	21	486	79
Ku-ring-gai Council	151	118	33	1,364	48
Kyogle Council	33	27	6	399	10
Lachlan Shire Council	39	36	3	383	14
Lake Macquarie City Council	288	218	70	2,689	183
Lane Cove Municipal Council	78	38	40	619	13
Leeton Shire Council	31	25	6	245	7
Lismore City Council	121	102	19	1,425	93
City of Lithgow Council	57	48	9	547	34
Liverpool City Council	284	179	105	2,540	86
Liverpool Plains Shire Council	30	26	4	571	10
Lockhart Shire Council	17	10	7	231	3
Maitland City Council	148	97	51	1,110	65
Mid-Coast Council	211	175	36	2,145	113
Mid-Western Regional Council	82	63	19	962	33
Moree Plains Shire Council	67	56	11	572	64
Mosman Municipal Council	52	44	8	507	25
Murray River Council	68	46	22	726	12
Murrumbidgee Council	37	23	14	288	5




The audit reports of these councils included an audit modification.

2016–17

Local council	Total revenue	Total expenses	Operating result ⁷	Total assets	Total liabilities
	\$m	\$m	\$m	\$m	\$m
Muswellbrook Shire Council	52	42	10	650	40
Nambucca Shire Council	47	36	11	482	52
Narrabri Shire Council	57	42	15	517	16
Narrandera Shire Council	23	18	5	246	4
Narromine Shire Council	25	19	6	326	6
Newcastle City Council	289	265	24	1,727	190
North Sydney Council	133	106	27	1,001	48
Northern Beaches Council	404	355	49	4,912	143
Oberon Council	19	15	4	295	7
Orange City Council	120	86	34	1,208	50
Parkes Shire Council	69	43	26	711	30
City of Parramatta Council	352	274	78	3,026	148
Penrith City Council	259	207	52	1,916	111
Port Macquarie-Hastings Council	248	149	99	2,204	114
Port Stephens Council	132	110	22	970	51
Queanbeyan-Palerang Regional Council	229	138	91	1,453	68
Randwick City Council	157	147	10	1,557	39
Richmond Valley Council	56	49	7	727	37
Ryde City Council	146	107	39	1,470	41
Shellharbour City Council	122	85	37	844	57
Shoalhaven City Council	258	222	36	2,817	169
Singleton Council	67	54	13	905	24
Snowy Monaro Regional Council	100	85	15	1,222	22
Snowy Valleys Council	72	63	9	626	20
Strathfield Municipal Council	43	34	9	361	15
Sutherland Shire Council	270	205	65	2,426	71
Council of the City of Sydney	722	578	144	12,087	184
Tamworth Regional Council	166	126	40	1,584	120
Temora Shire Council	23	18	5	212	6
Tenterfield Shire Council	26	18	8	366	10

2016–17

Local council	Total revenue	Total expenses	Operating result ⁷	Total assets	Total liabilities
	\$m	\$m	\$m	\$m	\$m
Tweed Shire Council	230	187	43	3,283	220
Upper Hunter Shire Council	45	39	6	702	26
Upper Lachlan Shire Council	38	26	12	426	10
Uralla Shire Council	21	19	2	248	10
Wagga Wagga City Council	154	121	33	1,485	82
Walcha Council	17	12	5	439	4
Walgett Shire Council	37	29	8	304	9
Warren Shire Council	17	13	4	188	3
Warrumbungle Shire Council	47	42	5	511	15
Waverley Council	138	127	11	1,259	41
Weddin Shire Council	16	12	4	187	8
Wentworth Shire Council	32	25	7	433	9
Willoughby City Council	119	98	21	1,570	75
Wingecarribee Shire Council	144	103	41	1,481	54
Wollondilly Shire Council	65	56	9	504	39
Wollongong City Council	324	255	69	2,536	178
Woollahra Municipal Council	105	90	15	961	110
Yass Valley Council 	36	30	6	374	27

Source: Audited financial statements 2016–17.



The audit reports of these councils included an audit modification.

2016–17

County council	Total revenue	Total expenses	Operating result	Total assets	Total liabilities
	\$m	\$m	\$m	\$m	\$m
Castlereagh-Macquarie County Council	1	1	--	1	--
Central Murray County Council	1	1	--	1	--
Central Tablelands County Council	6	5	1	76	3
Goldenfields Water County Council	21	17	4	308	3
Hawkesbury River County Council	2	2	--	3	1
MidCoast Water (MidCoast County Council)	88	81	7	969	191
New England Tablelands County Council	1	1	--	2	--
Riverina Water County Council	31	20	11	366	18
Rous County Council	27	23	4	506	33
Southern Slopes County Council	1	1	--	1	--
Upper Hunter County Council	2	2	--	1	--
Upper Macquarie County Council	2	2	--	1	--

Source: Audited financial statements 2016–17.



Appendix ten – OLG's performance indicators

We have included a summary of how each council has performed against the performance indicators prescribed by the Office of Local Government (OLG). The first six indicators are audited and reported in councils' financial statements. The remaining four asset-related measures are not audited and reported in councils' special schedule 7 'Report on Infrastructure Assets'.

We present these performance indicators on a consolidated basis. Councils with water and sewer activities present separate performance indicators for general, water and sewer activities.

	Audited						Unaudited			
	Operating performance (%)	Own source operating revenue (%)	Unrestricted current ratio (times)	Debt service cover ratio (times)	Rates and annual outstanding percentage (%)	Cash expense cover ratio (months)	Buildings and infrastructure renewals ratio (%)	Infrastructure backlog ratio (%)	Asset maintenance ratio (%)	Cost to bring assets to agreed service level (%)
OLG Benchmark	Greater than zero per cent	Greater than 60 per cent	Greater than 1.5 times	Greater than two times	Less than five per cent for metro and 10 per cent for other councils	Greater than three months	Greater than 100 per cent	Less than two per cent	Greater than 100 per cent	OLG has not set a benchmark
Albury City Council	16.8	79.5	3.3	7.1	10.3	16.2	63.3	3.1	80.7	1.9
Armidale Regional Council	12.3	59.5	2.2	6.0	6.8	14.4	44.1	10.6	96.3	4.3
Ballina Shire Council	8.9	64.6	4.9	2.7	3.6	12.0	84.2	1.9	82.9	0.9
Balranald Shire Council	6.8	31.9	6.2	15.3	10.5	9.4	54.6	2.6	84.7	1.7
Bathurst Regional Council	(5.4)	62.4	2.3	4.1	5.7	10.0	60.2	8.0	158.8	0.7
Bayside Council ¹¹	--	--	--	--	--	--	--	--	--	--
Bega Valley Shire Council	(2.9)	71.7	1.5	4.4	3.6	10.0	45.4	0.7	95.8	--
Bellingen Shire Council	0.7	68.1	2.5	6.3	5.8	17.7	88.0	11.6	89.3	--
Berrigan Shire Council	22.5	53.9	8.1	34.9	3.7	24.0	80.3	--	114.7	--
Blacktown City Council	3.5	47.5	2.6	--	4.1	19.0	82.9	2.4	99.3	1.6

¹¹ Bayside council received a lodgement extension for the 2016–17 financial statements to 31 May 2018 and has not yet presented them for audit.

Audited							Unaudited			
	Operating performance (%)	Own source operating revenue (%)	Unrestricted current ratio (times)	Debt service cover ratio (times)	Rates and annual outstanding percentage (%)	Cash expense cover ratio (months)	Buildings and infrastructure renewals ratio (%)	Infrastructure backlog ratio (%)	Asset maintenance ratio (%)	Cost to bring assets to agreed service level (%)
OLG Benchmark	Greater than zero per cent	Greater than 60 per cent	Greater than 1.5 times	Greater than two times	Less than five per cent for metro and 10 per cent for other councils	Greater than three months	Greater than 100 per cent	Less than two per cent	Greater than 100 per cent	OLG has not set a benchmark
Bland Shire Council	30.7	37.8	4.0	32.4	6.2	0.3	112.8	5.1	110.5	3.2
Blayney Shire Council	11.0	60.9	3.9	21.1	2.2	15.7	199.9	10.7	145.9	2.5
Blue Mountains City Council	5.4	80.1	2.3	2.6	3.4	4.4	35.1	2.0	99.1	1.2
Bogan Shire Council	14.0	46.2	6.4	52.2	6.8	8.5	67.7	1.9	93.5	2.2
Bourke Shire Council	21.3	40.8	4.3	8.6	14.9	12.9	114.3	3.2	99.9	1.6
Brewarrina Shire Council	19.2	43.5	3.9	24.0	6.8	9.7	87.3	1.9	47.7	--
Broken Hill City Council	(0.9)	62.6	1.8	3.8	11.7	9.9	112.8	25.5	121.6	13.1
Burwood Council	5.6	84.0	4.4	12.4	2.4	11.4	117.7	7.3	102.6	5.2
Byron Shire Council	6.0	69.7	3.2	3.3	3.4	14.3	108.0	7.9	90.7	4.8
Cabonne Council	15.4	56.5	7.8	46.0	5.6	18.4	136.0	3.6	117.8	2.0
Camden Council	0.0	43.0	2.7	3.2	3.4	14.9	38.2	1.2	100.0	1.0
Campbelltown City Council	10.6	64.0	4.8	8.2	3.3	18.0	94.8	1.6	104.9	1.3
Canterbury Bankstown Council	(1.2)	75.7	2.9	18.0	4.0	11.9	75.8	4.7	94.2	2.6
Carrathool Shire Council	19.3	40.7	6.8	30.9	6.1	17.0	79.9	1.3	104.9	--
Castlereagh-Macquarie County Council	9.1	16.5	3.6	2.3	0.0	5.6	--	--	--	--

Audited							Unaudited			
	Operating performance (%)	Own source operating revenue (%)	Unrestricted current ratio (times)	Debt service cover ratio (times)	Rates and annual outstanding percentage (%)	Cash expense cover ratio (months)	Buildings and infrastructure renewals ratio (%)	Infrastructure backlog ratio (%)	Asset maintenance ratio (%)	Cost to bring assets to agreed service level (%)
OLG Benchmark	Greater than zero per cent	Greater than 60 per cent	Greater than 1.5 times	Greater than two times	Less than five per cent for metro and 10 per cent for other councils	Greater than three months	Greater than 100 per cent	Less than two per cent	Greater than 100 per cent	OLG has not set a benchmark
Central Coast Council	10.7	76.4	2.7	4.5	5.9	9.0	142.2	2.6	104.9	1.7
Central Darling Shire Council	18.2	47.4	2.0	33.2	35.7	1.6	94.4	21.1	79.4	2.0
Central Murray County Council	(18.6)	81.2	3.3	--	--	4.4	--	--	--	--
Central Tablelands County Council	4.8	96.1	8.0	3.9	--	19.7	112.4	34.9	99.2	1.4
Cessnock City Council	4.0	63.4	2.4	8.1	2.0	6.3	158.5	3.4	102.2	9.6
City of Canada Bay Council	7.0	80.2	4.2	28.6	1.3	12.9	119.5	3.5	88.7	2.3
City of Lithgow Council	4.2	64.9	3.1	5.4	5.8	9.1	99.2	7.2	81.5	--
City of Parramatta Council	0.4	68.5	4.7	2.9	3.0	6.4	92.5	2.4	103.6	4.3
Clarence Valley Council	(3.8)	69.2	4.4	3.2	6.3	12.0	25.6	4.3	69.0	3.0
Cobar Shire Council	7.5	52.1	4.6	25.1	8.2	6.6	37.1	7.0	92.1	7.2
Coffs Harbour City Council	18.7	74.3	14.8	3.1	6.6	9.1	76.8	--	100.5	--
Coolamon Shire Council	18.9	43.4	8.4	81.6	4.9	19.7	107.4	1.8	139.2	0.9
Coonamble Shire Council	18.3	55.1	6.1	158.4	7.3	19.9	108.7	1.0	262.6	0.7
Cootamundra- Gundagai Regional Council	4.7	44.8	8.5	19.6	4.0	16.4	60.0	10.9	--	--

Audited							Unaudited			
	Operating performance (%)	Own source operating revenue (%)	Unrestricted current ratio (times)	Debt service cover ratio (times)	Rates and annual outstanding percentage (%)	Cash expense cover ratio (months)	Buildings and infrastructure renewals ratio (%)	Infrastructure backlog ratio (%)	Asset maintenance ratio (%)	Cost to bring assets to agreed service level (%)
OLG Benchmark	Greater than zero per cent	Greater than 60 per cent	Greater than 1.5 times	Greater than two times	Less than five per cent for metro and 10 per cent for other councils	Greater than three months	Greater than 100 per cent	Less than two per cent	Greater than 100 per cent	OLG has not set a benchmark
Council of the City of Sydney	4.9	79.7	2.7	--	1.2	6.5	62.6	3.5	100.1	1.3
Cowra Shire Council	11.2	71.3	4.0	4.8	9.0	8.9	78.4	1.9	105.4	0.8
Cumberland Council	(2.7)	66.1	3.5	11.4	2.8	7.9	106.1	9.8	125.9	7.2
Dubbo Regional Council	13.2	62.5	3.6	5.8	3.3	16.6	108.6	1.0	100.0	--
Dungog Shire Council	(17.5)	40.5	8.2	11.5	6.0	8.3	92.4	7.0	72.3	10.1
Edward River Council	16.7	39.1	8.6	25.6	5.5	21.9	117.8	1.5	88.6	0.8
Eurobodalla Shire Council	9.7	71.3	2.4	3.4	2.5	14.7	79.2	7.2	100.0	4.5
Fairfield City Council	11.4	77.0	3.1	146.3	3.1	4.9	170.5	1.9	100.8	1.4
Federation Council	6.3	40.0	2.7	27.9	5.5	18.7	108.5	5.8	95.8	3.7
Forbes Shire Council	(0.5)	68.3	7.4	3.4	10.3	15.4	36.2	3.7	94.0	1.7
Georges River Council	11.3	76.2	4.4	46.0	2.7	9.5	116.3	1.8	127.9	3.8
Gilgandra Shire Council	19.4	63.5	4.3	18.4	6.5	9.8	192.9	2.3	102.2	1.7
Glen Innes Severn Council	12.8	58.7	5.2	4.3	4.7	9.9	97.0	10.9	100.0	6.0
Goldenfields Water County Council	14.3	95.0	6.0	--	23.8	49.6	22.8	4.4	105.2	0.6
Goulburn Mulwaree Council	7.9	61.0	3.6	5.7	3.1	24.5	125.8	2.5	99.9	--

Audited							Unaudited			
	Operating performance (%)	Own source operating revenue (%)	Unrestricted current ratio (times)	Debt service cover ratio (times)	Rates and annual outstanding percentage (%)	Cash expense cover ratio (months)	Buildings and infrastructure renewals ratio (%)	Infrastructure backlog ratio (%)	Asset maintenance ratio (%)	Cost to bring assets to agreed service level (%)
OLG Benchmark	Greater than zero per cent	Greater than 60 per cent	Greater than 1.5 times	Greater than two times	Less than five per cent for metro and 10 per cent for other councils	Greater than three months	Greater than 100 per cent	Less than two per cent	Greater than 100 per cent	OLG has not set a benchmark
Greater Hume Shire Council	13.0	48.5	5.5	13.2	6.6	13.0	156.3	0.1	145.0	0.1
Griffith City Council	15.1	74.3	2.5	8.0	6.8	7.1	63.7	--	--	--
Gunnedah Shire Council	19.9	65.1	6.1	18.7	4.3	28.2	120.7	2.4	120.2	1.6
Gwydir Shire Council	16.5	52.0	2.0	6.8	4.4	4.8	113.5	3.1	100.0	--
Hawkesbury City Council	(6.6)	68.4	3.3	11.5	5.5	8.9	131.9	3.1	95.2	--
Hawkesbury River County Council	(11.6)	23.3	2.8	--	--	10.1	113.6	--	--	--
Hay Shire Council	11.3	39.1	5.0	15.8	13.3	12.2	76.0	3.1	72.4	1.4
The Hills Shire Council*	16.2	50.5	8.5	--	4.2	42.5	216.8	--	154.0	--
Hilltops Council	(6.6)	44.6	5.5	2.3	6.8	12.1	78.6	6.5	97.8	1.1
The Council of the Shire of Hornsby	6.9	79.3	3.9	10.7	1.9	20.7	90.7	0.9	94.0	0.7
The Council of the Municipality of Hunters Hill	(4.2)	90.7	7.3	23.0	3.0	16.5	76.6	1.6	105.8	1.7
Inner West Council	4.4	74.6	3.3	5.2	3.1	8.6	145.5	9.6	100.0	3.6
Inverell Shire Council	20.4	61.3	12.0	19.3	5.8	25.1	192.2	1.1	106.2	0.8
Junee Shire Council*	9.9	53.8	1.0	4.2	8.8	3.0	158.5	4.7	81.2	2.4
Kempsey Shire Council	1.9	72.6	2.6	3.8	6.7	9.3	38.9	10.6	107.3	5.4

Audited							Unaudited			
	Operating performance (%)	Own source operating revenue (%)	Unrestricted current ratio (times)	Debt service cover ratio (times)	Rates and annual outstanding percentage (%)	Cash expense cover ratio (months)	Buildings and infrastructure renewals ratio (%)	Infrastructure backlog ratio (%)	Asset maintenance ratio (%)	Cost to bring assets to agreed service level (%)
OLG Benchmark	Greater than zero per cent	Greater than 60 per cent	Greater than 1.5 times	Greater than two times	Less than five per cent for metro and 10 per cent for other councils	Greater than three months	Greater than 100 per cent	Less than two per cent	Greater than 100 per cent	OLG has not set a benchmark
The Council of the Municipality of Kiama	4.4	60.4	3.9	8.7	1.5	10.7	199.2	0.3	95.9	--
Ku-ring-gai Council	9.0	82.4	3.2	13.5	3.3	13.9	76.5	4.5	103.6	--
Kyogle Council	17.2	49.6	6.3	27.9	7.2	17.2	281.8	10.7	100.5	--
Lachlan Shire Council	11.3	38.3	4.6	137.9	7.5	16.8	42.0	6.4	93.5	4.1
Lake Macquarie City Council	9.0	65.6	2.9	10.3	3.7	10.9	112.8	2.5	92.2	1.7
Lane Cove Municipal Council	11.0	68.6	6.7	--	1.9	19.2	294.2	0.7	325.1	0.6
Leeton Shire Council	16.2	69.0	4.5	28.3	3.1	20.7	54.0	3.0	100.8	1.8
Lismore City Council	6.5	74.4	1.5	4.0	10.5	9.1	144.9	19.9	93.0	9.8
Liverpool City Council	2.4	54.5	1.9	4.7	4.3	8.5	115.8	3.3	104.5	2.5
Liverpool Plains Shire Council	4.5	55.3	4.5	12.9	9.9	15.3	140.3	2.4	--	1.8
Lockhart Shire Council	40.6	23.3	4.8	100.6	4.5	11.3	106.9	1.3	106.5	--
Maitland City Council	0.3	54.1	3.2	4.6	2.1	14.5	87.0	10.1	133.8	3.7
Mid-Coast Council	(0.3)	55.2	4.5	3.4	4.1	10.6	65.6	8.5	75.5	4.4
MidCoast Water (MidCoast County Council)	(2.2)	87.1	2.3	1.9	6.0	8.8	5.4	13.5	73.7	--

Audited							Unaudited			
	Operating performance (%)	Own source operating revenue (%)	Unrestricted current ratio (times)	Debt service cover ratio (times)	Rates and annual outstanding percentage (%)	Cash expense cover ratio (months)	Buildings and infrastructure renewals ratio (%)	Infrastructure backlog ratio (%)	Asset maintenance ratio (%)	Cost to bring assets to agreed service level (%)
OLG Benchmark	Greater than zero per cent	Greater than 60 per cent	Greater than 1.5 times	Greater than two times	Less than five per cent for metro and 10 per cent for other councils	Greater than three months	Greater than 100 per cent	Less than two per cent	Greater than 100 per cent	OLG has not set a benchmark
Mid-Western Regional Council	9.6	55.2	3.7	8.7	3.4	16.7	137.3	6.6	108.5	2.9
Moree Plains Shire Council	13.5	68.1	2.4	5.4	6.3	8.3	114.9	1.9	95.0	1.4
Mosman Municipal Council	6.2	87.7	1.7	4.1	2.6	4.7	138.0	1.1	115.7	0.7
Murray River Council	17.7	39.4	5.1	17.8	7.2	20.1	95.1	3.4	100.0	1.1
Murrumbidgee Council	5.5	27.1	4.2	45.5	7.1	22.1	41.0	0.5	128.0	--
Muswellbrook Shire Council	8.1	70.3	5.3	4.9	14.9	10.3	93.5	6.1	83.1	3.5
Nambucca Shire Council	17.8	68.1	2.5	3.4	5.1	10.9	62.6	3.9	97.9	--
Narrabri Shire Council	18.1	58.8	5.2	13.1	7.6	19.5	136.9	12.1	110.6	--
Narrandera Shire Council	17.4	52.2	7.6	806.7	7.5	23.3	96.2	9.7	98.0	3.8
Narromine Shire Council	18.7	47.9	5.4	20.0	9.2	19.9	93.4	11.6	60.4	6.1
New England Tablelands County Council	2.7	22.3	5.7	--	--	14.9	--	--	--	--
Newcastle City Council	3.5	84.3	2.5	7.4	4.2	8.7	94.9	11.1	117.6	6.1
North Sydney Council	7.7	80.3	3.5	84.3	1.1	7.8	269.0	--	99.5	--
Northern Beaches Council	1.3	81.1	2.7	1.0	2.8	5.9	92.2	0.3	103.7	0.3
Oberon Council	20.9	63.8	4.6	12.1	7.7	11.8	224.8	4.2	93.8	0.6

	Audited						Unaudited			
	Operating performance (%)	Own source operating revenue (%)	Unrestricted current ratio (times)	Debt service cover ratio (times)	Rates and annual outstanding percentage (%)	Cash expense cover ratio (months)	Buildings and infrastructure renewals ratio (%)	Infrastructure backlog ratio (%)	Asset maintenance ratio (%)	Cost to bring assets to agreed service level (%)
OLG Benchmark	Greater than zero per cent	Greater than 60 per cent	Greater than 1.5 times	Greater than two times	Less than five per cent for metro and 10 per cent for other councils	Greater than three months	Greater than 100 per cent	Less than two per cent	Greater than 100 per cent	OLG has not set a benchmark
Orange City Council	11.7	67.5	1.6	6.9	5.7	13.6	52.5	4.1	32.8	2.6
Parkes Shire Council	8.0	46.4	3.2	4.8	6.4	13.8	272.6	1.4	115.0	0.6
Penrith City Council	7.4	71.9	2.5	3.2	3.0	6.5	45.5	1.1	100.7	0.7
Port Macquarie-Hastings Council	7.3	56.2	2.0	4.3	4.9	25.3	82.2	5.3	87.8	--
Port Stephens Council	7.1	76.6	3.3	6.4	2.8	5.8	100.0	1.9	93.3	1.6
Queanbeyan-Palerang Regional Council	5.8	52.4	2.4	8.0	3.4	9.0	140.7	2.9	67.3	2.1
Randwick City Council	3.7	89.6	3.3	--	2.8	3.8	107.0	0.6	154.8	0.4
Richmond Valley Council	7.5	68.1	3.5	5.0	14.9	7.0	82.9	3.8	113.8	2.7
Riverina Water County Council	31.0	90.1	7.5	9.0	12.4	16.0	104.8	29.3	101.7	19.8
Rous County Council	4.8	81.3	6.1	2.5	0.0	21.0	62.2	1.3	89.4	1.0
Ryde City Council	11.5	75.8	3.4	27.7	3.6	15.9	193.6	2.7	92.9	2.0
Shellharbour City Council	9.0	70.4	2.5	19.6	4.6	11.1	232.7	2.0	112.6	2.8
Shoalhaven City Council	2.6	77.7	2.0	3.7	8.9	9.9	71.7	3.1	88.5	1.5
Singleton Council	(1.6)	64.0	2.9	6.3	3.2	13.4	107.1	2.1	62.7	1.3

Audited							Unaudited			
	Operating performance (%)	Own source operating revenue (%)	Unrestricted current ratio (times)	Debt service cover ratio (times)	Rates and annual outstanding percentage (%)	Cash expense cover ratio (months)	Buildings and infrastructure renewals ratio (%)	Infrastructure backlog ratio (%)	Asset maintenance ratio (%)	Cost to bring assets to agreed service level (%)
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Snowy Monaro Regional Council	1.5	49.8	3.7	14.2	14.3	15.3	55.1	11.9	96.9	3.3
Snowy Valleys Council	3.4	56.4	6.0	7.4	4.2	12.0	82.7	--	101.4	3.3
Southern Slopes County Council	5.1	75.3	8.6	--	--	9.0	--	--	--	--
Strathfield Municipal Council	4.9	73.4	3.6	--	3.0	22.1	127.8	1.5	115.3	1.0
Sutherland Shire Council	9.3	76.4	2.4	21.2	3.6	6.1	57.6	1.9	101.0	3.4
Tamworth Regional Council	12.4	68.7	4.4	5.2	5.2	19.4	39.0	0.6	97.4	--
Temora Shire Council	14.3	51.9	2.1	22.2	3.8	6.6	64.7	3.5	116.3	--
Tenterfield Shire Council	15.7	45.3	4.4	11.8	6.8	12.6	135.4	8.9	101.3	1.7
Tweed Shire Council	11.3	74.4	3.5	3.7	4.4	20.7	44.2	1.7	92.9	--
Upper Hunter County Council	13.7	4.1	3.9	--	--	2.3	--	--	--	--
Upper Hunter Shire Council	9.9	66.6	3.0	7.2	8.5	10.1	139.9	0.9	96.4	0.5
Upper Lachlan Shire Council	16.5	52.1	5.1	25.5	3.4	19.3	136.5	1.7	118.4	1.0
Upper Macquarie County Council	3.6	43.5	10.0	--	--	5.5	--	--	--	--
Uralla Shire Council	11.6	71.3	2.1	16.7	4.3	10.5	86.6	0.9	131.8	0.3

Audited							Unaudited			
	Operating performance (%)	Own source operating revenue (%)	Unrestricted current ratio (times)	Debt service cover ratio (times)	Rates and annual outstanding percentage (%)	Cash expense cover ratio (months)	Buildings and infrastructure renewals ratio (%)	Infrastructure backlog ratio (%)	Asset maintenance ratio (%)	Cost to bring assets to agreed service level (%)
OLG Benchmark	Greater than zero per cent	Greater than 60 per cent	Greater than 1.5 times	Greater than two times	Less than five per cent for metro and 10 per cent for other councils	Greater than three months	Greater than 100 per cent	Less than two per cent	Greater than 100 per cent	OLG has not set a benchmark
Wagga Wagga City Council	(6.4)	59.2	3.1	5.4	5.1	7.2	39.7	28.4	55.8	11.9
Walcha Council	16.7	50.3	4.5	38.3	3.4	10.6	309.2	7.3	105.5	2.9
Walgett Shire Council	20.2	52.0	5.7	17.8	10.4	16.3	142.1	8.9	73.0	4.6
Warren Shire Council	23.0	47.6	7.5	62.6	2.5	17.7	143.5	0.8	158.3	--
Warrumbungle Shire Council	2.0	46.5	4.3	9.9	7.9	6.5	64.4	0.1	117.6	1.8
Waverley Council	2.4	86.5	12.4	20.3	3.8	14.5	77.1	1.1	98.2	0.7
Weddin Shire Council	19.9	44.2	5.2	42.5	5.9	11.9	293.8	2.2	100.7	--
Wentworth Shire Council	13.4	48.0	6.9	42.3	10.2	18.0	100.7	12.7	119.3	4.3
Willoughby City Council	12.7	89.6	4.7	6.0	1.4	14.4	98.3	1.4	100.0	1.2
Wingecarribee Shire Council	9.0	67.0	4.9	6.0	2.2	18.8	60.9	2.1	105.7	1.2
Wollondilly Shire Council	0.9	69.7	3.0	4.2	5.2	10.4	99.4	15.3	123.9	8.4
Wollongong City Council	10.7	74.7	2.6	8.5	5.9	6.9	104.9	5.7	98.1	3.7
Woollahra Municipal Council	4.3	90.4	3.9	3.0	4.1	7.0	103.1	1.4	99.7	0.9
Yass Valley Council*	(2.3)	63.7	1.8	2.6	4.0	7.6	106.7	2.6	95.4	--

* The audit report of this council was subject to an audit qualification.

The council met the benchmark prescribed by OLG for the relevant performance measure.

The council did not meet the benchmark prescribed by OLG for the relevant performance measure.

Source: First six measures are obtained from the audited financial statements 2016–17. Last four measures are obtained from the unaudited Special Schedule 7 'Report on Infrastructure Assets' 2016–17.



Appendix 11 – NSW Crown Solicitor's advice



CROWN SOLICITOR
NEW SOUTH WALES

Advice

Audit of council entities

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Prepared for: AUD018 Auditor-General of NSW
Date: 31 August 2017
Client ref: Steven Martin
CSO ref: 201702268 T08 Sally Johnston/Lea Armstrong

1. Summary of advice

- 1.1 You seek my advice as to the Auditor-General's obligations with regard to auditing of "council entities" pursuant to the *Local Government Act 1993* ("the Act"). Pursuant to s. 415(4), a council's auditor (who is the Auditor-General: s 422) must, in auditing the financial reports of a council, audit the financial reports of any council entity and report on same as part of the report on the council. You have proposed an interpretation of this provision for my comment.
- 1.2 In my view, it is clear that the obligation to audit a council entity in s. 415(4) forms a part of the audit of the council. As to what such "audit" involves, the preferable interpretation must take account of both the lack of any obligation in the Act for council entities to prepare financial reports, and the functions and powers of the Auditor-General in relation to the audit of such entities in the Act. Whilst the Auditor-General's audit functions in relation to councils in Div. 3 of Pt. 3 of Ch. 13 are extended to council entities, the accounting and financial reporting obligations of councils generally in Divs. 1 and 2 of that Part are not so extended. Given the diverse range of bodies which may constitute a "council entity", whether or not such an entity has prepared a financial report will depend on statutory obligations elsewhere arising and, in my view, where no financial report of a council entity exists, the obligation to audit that entity in s. 415(4) does not arise. Where the obligation does arise, it may necessarily be limited by the nature of the council entity in question and the financial reports which it does prepare.
- 1.3 For those reasons, to the extent that your proposed construction of the duty in s. 415(4) is that the Auditor-General (as the council auditor) is required to perform "those audit procedures on a council entity considered necessary to form an opinion on the council's consolidated general purpose financial report", I think that is a reasonable and open interpretation of the duty, where it arises.
- 1.4 Insofar as your proposed construction of the duty in s. 415(4) also suggests that "any matters as appropriate in respect of a council entity are included in the report on the conduct of the audit of the council's financial report required pursuant to s. 417(1) of the Act", I agree to the extent that the duty in s. 415(4) is discharged by the auditor reporting on the council entity audit in the auditor's report on the council, which is a reference to the two reports to be issued under s. 417(1).
- 1.5 Please note this is a summary of the central issues and conclusions in my advice. Other relevant or significant matters may be contained in the advice, which should be read in full.

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2. Background

- 2.1 By operation of the *Local Government Amendment (Governance and Planning) Bill 2016*, the Act was amended and ss. 415(4) and (5) were inserted. Section 415(4) relates to auditing of a "council entity" and s. 415(5) defines such entities. Your request for advice arises in the context where this provision has come into effect but no audits have yet been completed pursuant to it.
- 2.2 I note that conferences to discuss the background, issues and question for advice have been conducted between your officers and my officers on 21 July 2017 and 11 August 2017.

3. Advice sought

- 3.1 By letter dated 26 July 2017, you seek my advice as to whether:

"In acquitting my responsibility under the Act, is it reasonable to interpret that I will satisfy my obligations under the Act if, when auditing the financial report of a council, I perform those audit procedures on any Council Entity considered necessary to form an opinion on the council's consolidated general purpose financial report and include any matters I consider appropriate in respect of Council Entities in my report on the conduct of the audit of the council's financial report required under s. 417(1) of the Act?"

4. Advice

- 4.1 Chapter 13 of the Act is entitled "How are councils made accountable for their actions?", with Pt. 3 addressing "Financial management" and Div. 2 of that Part "Accounting records, financial reports and auditing". Section 415 provides:

"415 Auditing of financial reports

- (1) A council's auditor must audit the council's financial reports as soon as practicable (having regard to the requirements of section 416 (1)) after they are referred for audit.
- (2) A council's financial reports must be audited in accordance with the requirements of:
 - (a) the publications issued by the Australian Accounting Research Foundation, on behalf of the Australian Society of Certified Practising Accountants and the Institute of Chartered Accountants in Australia, under the titles *Statements of Auditing Standards* and *Statements of Auditing Practice*, as in force for the time being, subject to the regulations, and
 - (b) such other standards as may be prescribed by the regulations.

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- (3) The regulations may prescribe matters that an auditor must consider and provide comment on in auditing a council's financial reports.
- (4) In auditing the financial reports of the council, a council's auditor must also audit the financial reports of any council entity and report on that audit as part of the report on the council by the auditor.
- (5) In this Part:
council entity means:
 - (a) a partnership, trust, corporation, joint venture, syndicate or other body (whether or not incorporated) that a council has formed or participated in forming or has acquired a controlling interest in, other than an entity of a class prescribed by the regulations, or
 - (b) any other entity of a class prescribed by the regulations."

"Council entity"

- 4.2 In considering the scope of the duty in s. 415(4), it is first necessary to understand the nature of a "council entity", to which that duty relates. A "council entity" is defined for purposes of Pt. 3 of Ch. 13 of the Act in s. 415(5), as extracted above. There are currently no regulations made pursuant to s. 415(5)(a) or (b). In my view, the ordinary meaning and effect of the definition in s. 415(5)(a) is that a wide and diverse range of bodies may constitute a "council entity".
- 4.3 The definition operates by reference to factual matters. First, whether the entity in question is a "partnership, trust, corporation, joint venture, syndicate" or other type of body, and second, whether the council has "formed or participated in forming" or acquired a "controlling interest" in that body, both of which are questions of fact. To that end, I note that the phrase "controlling interest" is used in other relevant statutory regimes, particularly taxation contexts¹. Whether a council has a "controlling interest" in relation to some other entity will usually be a factual test adapted to the particular type and nature of the entity in question. In the context of audit of financial statements, the Auditor-General would typically refer to Australian Accounting Standards AASB 10 'Consolidated Financial Statements' for guidance on what constitutes a "control".
- 4.4 It is clear that a "council entity" is potentially a very broad concept. There are a diverse range of entities which may constitute council entities, from unincorporated bodies or associations to large corporations. In turn, these bodies may be subject to different legislative regimes which impact upon their financial management, record keeping and

¹ See, for example, the *Payroll Tax Act 2007*. In the companies context, the phrase has a generally settled meaning of control of a majority of voting power at meetings of the board of management/meeting of directors, power to appoint more than 50% of the members of a board of management/directors, or direct or indirect exercise of control of more than 50% of the voting power attached to voting shares or a class of voting shares issued by a company (as applicable).

auditing. For example, no relevant statutory provisions may exist in relation to a small unincorporated body and such a body may not keep or generate financial statements etc. By contrast, a corporation may be subject to the provisions in the *Corporations Act 2001 (Cth)* which include record keeping and accounting obligations consistent with the standards made by the Australian Accounting Standards Board. This diversity in the potential range of bodies constituting "council entities" has implications for the practical operation of s. 415(4), as discussed below.

- 4.5 I also note that a comparable concept, although not expressly defined as a "council entity", is referred to in s. 358 of the Act. That section provides:

"358 Restrictions on formation of corporations and other entities

- (1) A council must not form or participate in the formation of a corporation or other entity, or acquire a controlling interest in a corporation or other entity, except:
- (a) with the consent of the Minister and subject to such conditions, if any, as the Minister may specify, or
 - (b) as provided by this Act.
- ...
- (4) In this section, *entity* means any partnership, trust, joint venture, syndicate or other body (whether or not incorporated), but does not include any such entity that is of a class prescribed by the regulations as not being within this definition."

- 4.6 In my view, s. 358 (particularly s. 358(1) and (4)), adopt the same concepts as those in s. 415(5), namely "formation or participation in formation" and acquiring a "controlling interest" in relation to a corporation or "entity". In that way, the sections are equivalent in material elements and should be understood as encompassing the same entities. Indeed, in my view, one practical way of identifying which entities constitute "council entities" for purposes of s. 415(5) would be to consider those entities which have been subject to Ministerial review pursuant to s. 358. Having said that, it is not my view that an entity does not constitute a "council entity" for purposes of s. 415 merely because it has not been subject to review pursuant to s. 358 (for example, in the situation where there has been non-compliance with the requirement for Ministerial approval in s. 358).

Nature of obligation in s. 415(4)

- 4.7 I note that the Auditor-General is the auditor for a council: s. 422(1). In that capacity, the duty imposed on the Auditor-General pursuant to s. 415(4) is that:

"In auditing the financial reports of the council, a council's auditor must also audit the financial reports of any council entity and report on that audit as part of the report on the council by the auditor."

- 4.8 The duty in s. 415(4) arises and falls upon the Auditor-General in her capacity as the council's auditor. The Act does not appoint the Auditor-General (or any other person) as the independent statutory auditor of a council entity. Indeed, a council entity may have its own auditor. Rather, a duty to "audit the financial reports" of the council entity arises in the Auditor-General in her capacity as the *council's* auditor.
- 4.9 That being said, a duty to "audit the financial reports" of a body, in this case a council entity, is ordinarily the duty of that body's auditor. So too I understand that an "audit of a financial report" usually entails an auditor issuing an opinion on that financial report, *qua* auditor of the body. There is a clear tension in s. 415(4) between the fact that the Auditor-General is not the auditor of the council entity and yet is required to "audit" its financial report.
- 4.10 As a result, the scope and nature of the duty to "audit" the financial reports of a council entity pursuant to s. 415(4) is open to doubt. Nonetheless, I think the following points can be made about the preferable interpretation of that duty.
- 4.11 I note that "audit" is not a defined term in the Act (although pursuant to s. 421A it "includes examination and inspection"), nor does it have a clearly settled meaning in law generally. Rather, legislation typically sets the framework for auditing in relation to particular bodies. For example, the Auditor-General's role in auditing councils is detailed in s. 417, which provides for matters such as inclusions in the auditor's financial report and matters on which the opinion or statement of the Auditor-General is required.
- 4.12 It is clear, from the introductory words of s. 415(4) "*in auditing* the financial reports of the *council...*" (emphasis added), that the "audit" of the financial reports of a council entity forms part of the process of, or is a corollary to, the audit of the council. However, it is presumably not equivalent to the audit of the council, which is addressed in ss. 415(1)-(3), or the terms of s. 415(4) would be rendered otiose. For example, it must presumably go beyond the audit of financial transactions between the council and council entity which would already be encompassed by the terms of the audit of the council pursuant to ss. 415(1)-(3).
- 4.13 The apparent purpose of s. 415(4) is to provide that council entities must be considered or examined in conducting the audit of a council. As noted in the second reading speech for the amending bill² which introduced the now s. 415(4) and (5):

"The bill... support(s) the financial transparency of councils... under the amendments introduced by the bill, councils will become subject to oversight by the Auditor-General for their general audits and those of their subsidiary entities..."³

² *Local Government Amendment (Governance and Planning) Bill 2016*.

³ NSW Legislative Assembly, *Hansard*, 22 June 2016, Second Reading speech, Mr Paul Toole (Minister for Local Government).

("Subsidiary entities" apparently being used to refer to "council entities".)

- 4.14 In that way, the provision mirrors the requirement in s. 358 for Ministerial approval for council establishment of, or involvement in, such entities, by providing for ongoing oversight of the relationship between the council and the council entity, at least in a financial sense. However, as noted above, exactly what the additional obligation introduced by s. 415(4) is, and how it is to be fulfilled, is unclear and beset with practical difficulties.
- 4.15 Significantly, ss. 423 and 424 support the audit obligation in s. 415(4) by extending to "council entities" as well as councils: see s. 423(6) and 424(3). Pursuant to s. 423, the Auditor-General (or a person authorised by the Auditor-General) is entitled at all reasonable times to full and free access to a council's (or council entity's) accounting records and other records necessary in order to carry out her functions. She may direct persons to produce books, record or other documents in their custody or control, to appear personally and produce such documents, to answer any relevant question, to provide any necessary authorities to gain access to such documents, and to make copies or take extracts from such documents for the purposes of an audit or inspection carried out under the Act.
- 4.16 Pursuant to s. 424, the Auditor-General (or a person authorised by the Auditor-General) may direct an authorised deposit-taking institution or the person in charge of a council (or council entity) account in such an institution to give her a statement of the account or certificate as to the balance of the account and produce to her any relevant book, record or other document in its custody or control. The effect of these provisions is that the Auditor-General's functions and powers under Div. 3 ("Auditors") of Pt. 3 of Ch. 13 of the Act are extended to apply to council entities in the same way they apply to councils. This may suggest an equivalent "audit" function is intended in relation to council entities, as applies to councils.
- 4.17 However, the provisions of Div. 1 ("Funds") and Div. 2 ("Accounting records, financial reports and auditing") of Pt. 3 of Ch. 13 of the Act are not uniformly extended to encompass council entities in the same way as they apply to councils. Of particular significance, ss. 412 and 413, which provide that a council must keep accounting records and prepare financial reports respectively, do not extend to council entities.
- 4.18 For this reason, there is no obligation pursuant to the Act for council entities to prepare financial reports, equivalent to that which applies to councils. To some extent, financial information about council entities may be included in the council's financial reports, which must be prepared in accordance with s. 413. That includes a requirement in s. 413(3)(a) that the financial statement be prepared in accordance with the publications in force issued by the Australian Accounting Standards Board, and would pick up controlled entities pursuant to those standards. Such controlled entities would

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presumably also be "council entities" for purposes of s. 415(5) (although only a subset of the range of entities which may be council entities). However, it is for the council to determine appropriate compliance with s. 413 (although the Auditor-General may review this as part of her audit and report under s. 417). Even if, by that means, financial information about council entities is captured in the council's financial report, in my view, this has little application in terms of the s. 415(4) obligation. That is because the s. 415(4) "audit" obligation applies to "financial reports *of the council entity*" (emphasis added) and not the council's financial reports *per se*.

- 4.19 As noted in my discussion above about the diverse range of bodies potentially encompassed by the definition of "council entity", whether or not a council entity has prepared such a financial report will depend upon the nature of the entity and whether it is required to do so pursuant to other statutory regimes. In my view, that necessarily limits the operation of s. 415(4) to only those council entities which have such obligations elsewhere arising or which voluntarily prepare such reports, given the plain words of s. 415(4), that the audit is of "...the *financial reports* of any council entity..." (emphasis added).
- 4.20 In addition, it may limit the Auditor-General's ability to perform audit functions in relation to those financial reports, even where they do exist, depending upon the framework in which they have been prepared. As there is no means to compel a council entity to prepare a financial report in a particular manner pursuant to the Act, in my view the obligation in s. 415(4) upon the Auditor-General to audit the financial reports of a council entity can only extend to that which is reasonably possible having regard to the particular entity. It may be that, in practice, the Auditor-General can only comment on the limitations which apply to her audit.
- 4.21 In summary, it is clear that, whilst there is a diverse range of bodies which may constitute a "council entity", the obligation in s. 415(4) only arises in relation to "financial reports" and so only applies in relation to council entities which do prepare such financial reports. As to the nature of the duty to audit those financial reports, there are indications that s. 415(4) was intended to impose a duty of auditing of council entities which goes beyond that which would flow from proper auditing of the council in accordance with s. 415(2), and yet the scope of that duty is necessarily limited by the statutory context, functions and powers which are available to support it. The statutory language of s. 415(4) in my view reveals an intention to impose a duty on the council auditor in his or her capacity as council auditor (not as auditor of the council entity), and in the context of performing his or her audit of the council. That is, it is not an equivalent duty to that imposed in relation to the council, for which the Auditor-General is the auditor. Rather, the audit of the financial reports of the council entity must form, in some way, a component or part of the audit of the council.

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- 4.22 It is, in a practical sense, difficult to articulate precisely what that "audit" duty involves in the context of s. 415(4), beyond noting these features which point to it being less than equivalent to the role of an external auditor of the council entity (or equivalent to the audit of the council itself) and yet more than what would already be encompassed by the audit of the council pursuant to s. 415(1)-(3). What can be said is that the audit of the financial reports of a council entity should be conducted to the fullest extent necessary and possible to provide a report on that audit in the council report, in light of the audit functions and powers which the Auditor-General acquires in relation to both councils and council entities pursuant to Div. 3 of Pt. 3 of Ch. 13, especially ss. 423 and 424, as outlined above.

Conclusion re: proposed interpretation

- 4.23 Given the uncertainties about the scope of the duty in s. 415(4), outlined above, in my view your proposed construction of the duty is both reasonable and open. That is, your suggestion that the duty in s. 415(4) is that the Auditor-General (as the council auditor) is required to perform "those audit procedures on a council entity considered necessary to form an opinion on the council's consolidated general purpose financial report", is a clearly arguable interpretation of the duty, where it arises. I note that, strictly, I would prefer to phrase it as "those audit procedures necessary to form an opinion on the council's financial reports", but given that the report required pursuant to s. 417(1) of the Act is a report as to the council's general purpose financial report, I do not disagree with your phrasing. I also observe that, whilst an "audit of the financial reports" of a body may in other contexts generally be understood to require the issuing of an opinion by the auditor, in my view, the statutory context and fact that the Auditor-General performs the function in s. 415(4) in her capacity as auditor of the council, make it arguable that the duty can be discharged through performing "audit procedures" rather than necessarily requiring the issuance of an opinion by the auditor.
- 4.24 To the extent that your proposed construction of the duty in s. 415(4) also suggests that "any matters as appropriate in respect of a council entity are included in the report on the conduct of the audit of the council's financial report required pursuant to s. 417(1) of the Act", I agree that the duty in s. 415(4) is discharged by the auditor reporting on the council entity audit in the report on the council. The reference in section s. 415(4) to "the report on the council by the auditor" is, in my view, a reference to either of the two reports made under s. 417(1).

Comment: possible means to resolve uncertainty

- 4.25 The relevant provisions of the Act contain several powers for matters to be prescribed by regulation, which could assist to resolve the uncertainty and practical difficulties surrounding the operation of s. 415(4). The preparation and promulgation of regulations is a matter on which Parliamentary Counsel's advice should be sought, but I note the powers of regulation contained in s. 415(5)(a) and (b) as a potential means to clarify or limit the scope of the definition of "council entity", and the power in s. 415(3)

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to regulate what matters an auditor must consider and provide comment on in auditing a council's financial reports, which could in turn assist to clarify the scope of the audit required pursuant to s. 415(4), given that such audit is performed as part of the audit of the council financial reports.

Signed:



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