

28 September 2007

Ian Buchanan
Chairman
Greater Wellington Regional Council
PO Box 11-646
WELLINGTON

Dear Ian

Management report for the year ended 30 June 2007

We have completed our audit of the Greater Wellington Regional Council for the year ended 30 June 2007 and are pleased to report to you the findings arising from the audit. This report provides a summary of:

- v the audit opinion;
- v our assessment of your management control environment;
- v the significant matters arising from the audit.

Acknowledgement

We wish to acknowledge the assistance provided by management and staff during the audit. Should you require clarification on any other matters raised in this letter please contact Karen Young or me on 496-3099.

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AUDIT NEW ZEALAND
Mana Aotake Aotearoa

Yours sincerely

Rudie Tomlinson
Director

cc Judith Aitken, Chair, Planning & Monitoring Sub-Committee
Dave Benham, Chief Executive
Barry Turfrey, Chief Financial Officer

Audit for the year ended 30 June 2007

1 Introduction

We have completed our audit of the Greater Wellington Regional Council (the Regional Council) for the year ended 30 June 2007 and are pleased to report to you the findings arising from the audit. This report provides a summary of:

- v the audit opinion;
- v our assessment of your management control environment;
- v the significant issues arising from the audit.

2 Audit opinion

An unqualified opinion was issued on the Regional Council's financial statements.

3 Management control environment

3.1 Background

The management control environment is determined by the attitude, awareness and actions of the governing body, management, and others (who have the ability to influence the reliability of control systems) concerning the importance of internal control.

The control environment encompasses the entity's control culture and values, organisation and governance structures and its commitment to designing and maintaining reliable accountability systems. It also includes its attitude and approach to planning, budgeting, performance monitoring and compliance with legislative requirements. These translate into internal control procedures that are established to provide reasonable assurance that specific entity objectives will be achieved.

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To be returned to Audit New Zealand after finalisation of the management letter.*

These internal controls are built into the following processes:

- v Governance structures and mechanisms
- v Risk management
- v Financial planning, reporting and monitoring
- v Operational financial controls
- v Quality assurance procedures

The stronger the management control environment, the greater the likelihood that these processes at different levels within the organisation will operate as designed and that the organisation's objectives will be achieved.

We have assessed the management control environment as "effective". We note that overall risk management and quality assurance would be strengthened by the introduction of an internal review function. Our understanding is that Council will consider this going forward.

3.2 Our approach

Our approach for the audit of the financial statements was, where possible, to place reliance on the Council's control environment and management systems, with a view to minimising the level of detailed transaction testing performed.

3.3 Our assessment

We found that, consistent with previous years the Council continues to operate a sound management control environment and there are effective financial management processes in place. We have identified the following as some of the key aspects of the management control environment:

- v The Council and management have demonstrated a commitment to appropriate management control systems being in place and operating effectively. This includes both the maintenance of essential transactional recording systems as well as detailed financial analysis and management reporting throughout relevant levels of the Council.

- v Budgeting and monitoring of financial performance is effective due to the systems and processes in place.
- v There is an experienced executive team who displays a consistent level of commitment to maintaining a strong control environment.
- v The Council's governance structure provides a clear division of responsibilities between the Council and management.
- v Council maintains an established annual planning process, which includes regular reviews of Council's long-term financial strategy, and a substantial public consultation process.
- v There are structures and processes in place through which financial performance against budgets is monitored on a monthly basis by both management and the Council.

4 Significant matters

The following significant matters are raised for your consideration together with the comments received from management. Minor matters arising from the audit have been discussed and will be reported separately to the Chief Executive.

There are no significant issues arising from the audit of the financial statements which remained unresolved at the conclusion of the audit.

4.1 Reassessment of fair value of assets

The Regional Council's policy is to revalue its classes of property, plant and equipment assets on a five yearly basis. Regional water supply assets were last revalued at 30 June 2004. NZ IAS 16 requires that when the fair value of a revalued asset differs materially from its carrying amount, a further revaluation is required.

The Regional Council undertook an assessment of the fair values of its Regional water supply against their carrying value. This was a high level review based on data from the Statistic New Zealand indices as an indicator of changes in values. We concur with this approach.

The combined impact of applying these indicators is a total increase in values of around \$49m for Regional water supply assets. The estimated impact of the revaluation of these assets of \$49 million represented approximately 9% of total net assets. We agree with the Council that the movement is not material and therefore a full revaluation was not required for the 2006/07 financial year. We would recommend that the Regional Council needs to continuously monitor asset values and adjust revaluation cycles to ensure fair value reporting is maintained.

Management comment

Background

In respect of the regional water supply assets for the year ended 30 June 2007, the Regional Council undertook a valuation in accordance with NZ IAS 16, specifically clause 35.3 which states:

“For plant and equipment, where there is an active market or readily available price indices that establish the items fair value with reasonable reliability, the valuation need not be conducted or reviewed by an independent valuer or experienced employee.”

The Regional Council obtained indices from Statistics New Zealand. An independent valuer then approved specific indices as appropriate to be used in respect of the regional water supply assets. The approved indices were then applied to the assets resulting in an increase in value of the regional water supply assets of \$49 million.

However, Audit New Zealand took the view that the Regional Council had not satisfied the requirements of NZ IAS 16 in that the indices used were not appropriate. In fact in Audit New Zealand's view there were no appropriate indices available.

For the valuation to be acceptable to Audit New Zealand the valuation had to be approved and signed off by an independent valuer.

If the change in valuation in respect of these assets was material, then the Council's financial statements would have been qualified by Audit New Zealand regardless of whether the change was included in the financial statements or not:

- If the Council had included the change in its financial statements as the valuation, then the qualifications would have been on the basis that they had not been prepared in accordance with NZ IAS 16 (in the opinion of Audit New Zealand); or
- If the Council did not include the change in the assets in the financial statements, then the financial statements would not be fairly valued.

Under both scenarios the qualification would be based on the indices, which in Audit New Zealand's opinion, were considered inappropriate.

The Council is of the firm view that:

- The indices used were appropriate
- This was confirmed by an independent valuer
- The process was in accordance with and permitted by NZ IAS 16
- The rationale of not accepting the indices as appropriate for use in the financial statements but using them as a basis for an audit qualification is illogical.
- Audit New Zealand would appear to take the position that they are more qualified to judge what indices are appropriate than an independent valuer.

4.2 Legal compliance

Our review of the Regional Council's legal compliance focussed primarily on how it had met its accountability obligations in respect of its annual report. These are contained in the Local Government Act 2002, specifically, and more generally in its obligation to comply with generally accepted accounting practice (GAAP). We also reviewed the Regional Council's compliance with key aspects of the Rating Act 2002 and maintained a watching brief for any possible non-compliance with any other legislation coming to our attention.

The Regional Council has been using the SOLGM Legal Compliance modules as a guide for formalising and improving its practices and processes. The Regional Council's systems are designed to ensure that employees comply with legislation. Where a new process is developed, the Regional Council engage with lawyers and any relevant bodies to make sure that they develop processes that will ensure compliance with legislative requirements. The Regional Council has an employee whose specific duty is to inform employees of all updates in legislation and that where necessary employees attend courses that ensure they are up-to-date with legislation. This process provides a

forum whereby awareness of legislative requirements and related issues can be highlighted, and through this becomes a mechanism to mitigate the risk of non-compliance.

Within the scope of our work performed, no instances of non-compliance with significant legislative requirements were identified during the course of the audit.

Management comment

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4.3 Fraud policy

It is the expectation of the Auditor-General that every public entity should formally address the matter of fraud, and formulate an appropriate policy on how to minimise it and (if it occurs) how it will be dealt with.

The Regional Council adopted a fraud policy during the year.

The next steps would be to operationalise the policy, including performing a fraud risk assessment for the Regional Council.

An internal fraud was notified in the year relating to the misappropriation of dual cards (ie, fuel cards). An internal investigation found that the controls over the dual cards could be strengthened. The matter is now with the Police.

Management comment

5 Follow-up of issues raised in the audit arrangements letter

5.1 Audit of Long Term Council Community Plan (LTCCP) amendments

During the year Council amended its LTCCP for the ten years commencing 1 July 2006 to:

- ✓ include governance and funding arrangements to facilitate the development and implementation of the Wellington Regional Strategy (WRS) as a significant new activity;
- ✓ establish a council controlled organisation to deliver the economic development initiatives outlined in the WRS; and
- ✓ allow the Regional Council to debt fund certain operating expenditure on rail infrastructure assets over a longer time period than the five years of the current policy, for up to 75% of the expected life of the asset. Debt funding allows Greater Wellington to spread the rates impact of the expenditure over the term of the loan.

An unqualified opinion was issued on 12 September 2006 and 13 March 2007 on these Statements of Proposal and the amendments were adopted on 12 June 2007.

5.2 Review of draft 2007/08 annual plan

Council prepared a comprehensive annual plan. We reviewed the draft document, prior to its adoption, for compliance with Council's obligations under the LGA 2002. Issues identified were discussed with Council officers at the time. All significant recommendations were implemented in the final document.

5.3 Audit of NZ IFRS financial statements

Council prepared its first NZ IFRS financial statements for the year ended 30 June 2007. As NZ IFRS require the same accounting policies to be used throughout all periods presented in the Regional Council's first NZ IFRS financial statements, the comparative figures for the year ended 30 June 2006 had to be restated in accordance with NZ IFRS. These comparative figures were audited. We have issued an assurance letter over the opening balance sheet and comparatives.

5.4 Audit of exempt CCOs

We have been asked by the Office of the Auditor-General to advise them on Council's use of Section 7 of the Local Government Act 2002 (the Act). Under section 7 of the LGA 2002, a local authority may exempt a "small" CCO from the accountability regime that applies to CCOs under that Act. The Regional Council has not exempted any CCOs. This return was completed and forwarded to the OAG.

5.5 Performance framework

The Council, when preparing its 2006/16 LTCCP, reviewed its performance measures. New performance measures were developed as part of the process.

A large number of the measures were being reported against for the first time in 2007. We found there were appropriate systems and processes in place to capture information for reporting purposes over the performance measures.

5.6 Summary annual report

In accordance with the requirements of the Local Government Act 2002, Council has produced a summary of the information in its Annual Report.

We liaised with Regional Council to ensure that the Summary Annual Report complied with FRS-43, which amongst other things required Council to provide a précis of the financial and non-financial statement included in the summary annual report and SOLGM's Good Practice for LTCCP Summary Documents. The Regional Council decided that the easiest way to meet requirements of FRS-43 was to extract the financial statements, statement of service performance and NZ IFRS reconciliation straight from the annual report document, along with the compliance with FRS-43 statements. We have accepted this on the basis that the document contains all of the disclosures required by FRS-43.

We issued an unqualified audit opinion on 27 September 2007 over the summary annual report.

6 Audit independence

We confirm that for the audit of the financial statements of the Regional Council and its controlled entities for the year ended 30 June 2007, we have maintained our independence in accordance with requirements of the Auditor-General, which incorporate the independence requirements of the Institute of Chartered Accountants of New Zealand (ICANZ).

During the year we reviewed the tendering processes over the Greater Wellington Rail Project for the Regional Council and group, which is compatible with those independence requirements.

Other than this assignment, the audit and in conducting the audits of the amendments to the Long Term Council Community Plan, we have no relationship with or interests in the Regional Council or any of its subsidiaries.

Unresolved disagreements

We have not had any unresolved disagreements with management about matters that individually or in aggregate could be significant to the financial statements. Furthermore, management has not sought to influence our views on matters relevant to our opinion.

Other relationships

We are not aware of any situations where a spouse or close relative of a staff member involved in the audit occupies a position with the Regional Council or its controlled entities that is significant to the audit.

We are not aware of any situations where a staff member of Audit New Zealand has accepted a position of employment with the Regional Council or its controlled entities during or since the end of the financial year.