



## Christchurch City Council

# AUDIT AND RISK MANAGEMENT SUBCOMMITTEE AGENDA

29 AUGUST 2007

AT 9AM

IN THE NO 3 COMMITTEE ROOM, CIVIC OFFICES

**Subcommittee:** Councillor Bob Shearing (Chairman), The Mayor, Mr Garry Moore, Councillors Graham Condon, David Cox and Gail Sheriff, Messrs John Hooper and Michael Rondel.

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**1. APOLOGIES**

Councillor Cox.

**2. MINUTES OF THE PREVIOUS MEETING OF 16 MAY 2007**

Attached.

**3. MATTERS ARISING**

**4. CORRESPONDENCE**

**5. REPORT ON INTERNAL AUDIT ACTIVITIES; 3 MONTHS ENDED 30 JUNE 2007**

<b>General Manager responsible:</b>	Roy Baker, General Manager Corporate Services, DDI 941- 8540
<b>Officer responsible:</b>	Senior Auditor
<b>Author:</b>	G Nicholas, Senior Auditor

**PURPOSE OF REPORT**

1. The purpose of this report is to provide a brief periodic update on the status of internal audit activities completed by Price Waterhouse Coopers (PWC) and Graeme Nicholas (Senior Auditor) within the Council and includes:
  - the status of audit projects in the current year's programme.
  - executive summaries for reports completed during the quarter ending 30 June 2007.
  - issues outstanding from previous quarters.

**EXECUTIVE SUMMARY****Programme Status**

2. The attached appendix B to this report is the detailed work plan listing the internal audit scopes to be completed as part of the three year programme. The programme for 2007/8 has been revised and approved by management, with the current years audits shown as shaded. The planning and plan approval process was very thorough, involving each of the general managers, their reports and teams, invitation for the Audit Committee to contribute and input from the CEO.
3. We have completed the audit plan as proposed for the year with the exception of several reviews which were postponed for operational reasons. The co-sourcing model continues to produce a good blend of Council in-house input and experience through Graeme Nicholas and wider expertise and presence through the involvement of PWC.
4. Currently, there are a number of reviews relating to the 2007/8 year in an 'in progress' state.

**Value to the Council**

5. With the assistance of management and an ability to bring a broader focus we are delivering reviews which have an increased focus on:
  - alignment with the Council policies and strategic planning documentation.
  - alignment with the cultural and ethical aspirations of the Council.
  - review of some of the key operational areas of the Council.
  - raising the awareness of the importance of control.
6. During the course of the reviews completed to date and specifically with in the most recent quarters activities, we have again observed and raised a number of recommendations related to formalising and monitoring compliance with processes which will improve elements of the Council's financial performance. A number of issues have been resolved during the quarter, which is pleasing to see.

5 Cont'd

THE 2006/07 PROGRAMME

Internal Audit Review Status

7. Summarised below is the status of each of the internal audit reviews for the 2006/07 year and those commenced in the 2007/08 year:

Completed	Review complete, management comments received and final report issued
Draft Report	The field work has been completed and the draft audit report is awaiting review
In progress	Review underway
Planned	Review planned, high level terms of reference drafted

Review and ref #	Comments	Status
Procurement review (06-1)	Final report has been issued	Completed
Mayor's Welfare (07-08)	Final report has been issued	Completed
Cash handling – various sites (07-23)	Final report has been issued	Completed
Internet Monitoring (07-22)	Final report has been issued	Completed
Inventory management (07-6)	Final report has been issued	Completed
Enforcement (Parking) (07-06)	Final report has been issued	Completed
City Solutions Capital Contracts (07-26)	Final report has been issued	Completed
Fixed assets (07-17)	Final report has been issued	Completed
Probity and discretionary expenditure review (07-13) *	Final report has been issued	Completed
LIMs Process (07-04)	Final report has been issued	Completed
Fraud Prevention Review (07-14) *	Action plan being developed	Completed
Business Continuity Planning (07-1) *	Action plan in conjunction with the Council's Risk Management strategy	Completed
Key accounting controls (07-10)	Final report has been issued	Completed
Licensing - health , liquor (07-07)	Final report has been issued	Completed
Rates (07-15)	Final report has been issued	Completed
Regulatory consents (07-05)	Final report has been issued	Completed
Cash handling (07-23) part 2	Final report has been issued	Completed
Internet Monitoring (07-22)	Final report has been issued	Completed
Revenue & Receivables (07-11)	Final report has been issued	Completed
Probity and discretionary expenditure review (07-13) * Phase 2	Final report has been issued	Completed
Enforcement -Environmental enforcement (07-06)	Final report has been issued	Completed

## 5 Cont'd

Review and ref #	Comments	Status
Payroll processes (07-25)	Final report has been issued	Completed
General IT / Governance (07-19)	Final report has been issued	Completed
City Environment Contracts (07-18)	Final report has been issued	Completed

## THE 2007/08 PROGRAMME

Heritage grants (08-28)	Awaiting review	Draft report
Engagement of Consultants (08-15)	Awaiting review	Draft report
Mayors Welfare Fund (08-32)	Final report has been issued	Completed
Management of Council leased stadium (08-31)	Audit progressing	In progress
Sensitive expenditure (08-12)	Awaiting review	Draft report
Recruitment & Exit processes (08-26)	Audit progressing	In progress
Building inspections (8-04)	T of R being finalised	Planning

## Risk Categories of Issues Reported This Quarter

8. In each review under the co-sourced arrangement, findings are classified according to the ratings outlined below.
9. Given the size of the Council and its relative complexity from an operational perspective, it is expected that a number of issues will be identified during the course of the year where further improvements can be made (both from an internal control and efficiency/effectiveness perspective). The ratings in the table below will be a combination of potential opportunities for improvement identified and control related issues.
10. In PWC's experience, it is normal practice to report summarised outcomes from the reviews in this fashion; with the focus of many Audit Committees turning to the status of key findings where agreed management actions may not have been taken within agreed timeframes. The Subcommittee should note that delays may occur due to shifting management priorities and/or resourcing issues.

Review	Number of recommendations by risk category			Total Number
	High *	Moderate	Low	
Totals carried forward from last Qtr	10	56	48	114
Payroll (07-25)		3	3	6
City Environment Contract (07-18)	1	2	3	6
General IT / Governance (07-19)		9	6	15
<b>Total issues to date</b>	<b>11</b>	<b>70</b>	<b>60</b>	<b>141</b>
Issues resolved to date	-5	-35	-27	-67
<b>Issues Outstanding to date</b>	<b>6</b>	<b>35</b>	<b>33</b>	<b>74</b>

\* See Appendix C for a description of items rated with a "high" priority

11. The findings relating to our reviews are broadly classified as being high, moderate or low priority.

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12. These ratings are defined as follows:

- **High:** Significant potential exposure or area of critical importance. Management action required.
- **Moderate:** Exposure exists but with some mitigating factors. Management action required within the next six months.
- **Low:** Low level of potential exposure to the organisation. Action required is only of a low priority or housekeeping nature.

**New Issues Reported**

13. Attached as Appendix A are the executive summaries of the reports prepared this quarter.
14. A detailed report for each review completed has been provided to management which sets out agreed management action plans as approved by the review sponsor.

**Outstanding Issues Reported**

15. A database of audit issues is maintained. These are reported to General Managers for regular follow up. A status report is included as an Appendix C to this report.

**6. 2007 ANNUAL REPORT**

<b>General Manager responsible:</b>	General Manager Corporate Services, DDI 941-8540
<b>Officer responsible:</b>	Corporate Finance Manager
<b>Author:</b>	Diane Brandish, Corporate Finance Manager

**PURPOSE OF REPORT**

1. The purpose of this report is to present for review by the Audit and Risk Management Subcommittee the draft financial statements forming part of the annual report of the Christchurch City Council (CCC) for the year ended 30 June 2007.
2. Under section 98 of the Local Government Act 2002 a local authority must prepare and adopt in respect of each financial year an annual report. Each annual report must be completed and adopted by resolution, and within one month after the adoption of its annual report, the local authority must make publicly available:
  - (a) its annual report; and
  - (b) a summary of the information contained in its annual report.
3. These are the first accounts presented under the New Zealand Equivalents to International Financial Reporting Standards, (NZ IFRS). The Council adopted NZ IFRS as at 1 July 2006. The main differences between NZ IFRS and the previous reporting standard, NZ GAAP are;
  - (a) deferred taxation; under NZ IFRS deferred tax balances are calculated on a balance sheet approach which recognises where there is difference between the carrying value of an asset or liability and its tax base.
  - (b) reclassification of cash and cash equivalents; under NZ IFRS cash and cash equivalents include short term investments with a maturity of less than 90 days, (previously less than one year).
  - (c) derivatives are recognised on the balance sheet.
  - (d) impairment testing, all assets including investments are now annually tested for impairment and where necessary their value adjusted.

**EXECUTIVE SUMMARY**

4. At the time of forwarding this draft report to the Subcommittee, Audit NZ has examined the financial statements of the parent but has not yet signed off on the report. The main outstanding issue is that the final revaluation data is not yet finalised and we have still not received the last of the related party information.
5. The financial statements of the group have been omitted from this report because of delays in receiving them from the subsidiaries. It is intended to hold a conference call later next week so that the committee can sign off on the group accounts.
6. A representative of Audit NZ will be in attendance at the committee meeting to answer any questions regarding the accounts.
7. Attached as Appendix 1 is a copy of the financial statements of the draft annual report for the year ended 30 June 2006. Parent numbers only are included, group results have been omitted as they are not complete.

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8. Council's operating surplus before asset contributions for the year was \$27.2m, \$19.6m ahead of plan. \$11m of the additional surplus is the result of higher than expected revenue and the balance from lower than expected costs. Contributions to this variance are outlined in note 35 of the detailed accounts and include:

- higher than budgeted development contributions of \$4.2m. This needs to be considered along with the vested asset receipts which were \$10.7m below budget. This net revenue shortfall is a timing difference. The Council's new development contributions policy was scheduled to come into effect on 1 July 2006 and many developers brought forward their applications in order to avoid the increased fees.
- higher than budgeted rates of \$1.6m.
- interest received of \$1.4m. This is due to higher interest rates.
- higher than budgeted LTNZ subsidy of \$1.5m.

The main cost savings were:

- lower than budgeted personnel costs of \$1.4m
- lower than budgeted professional and contract fees of \$3.3m,
- lower than budgeted interest expense of \$2.0m due to lower intergroup loans.

9. The net surplus for the year after vested assets is \$39.3m, \$9.1m over plan.

10. Much of the focus for the year was on cost control and efficiencies, and for 10 of the 13 Groups of Activities actual expenditure was less than plan. These savings were largely achieved through better contract management, although in some areas a difficulty in recruiting skilled staff led to projects being postponed. Of the remaining 3 groups, 2 were affected by unbudgeted costs including a \$2.3m write-off for Jellie Park buildings, and a \$0.8m provision for leaky home claims. In the Streets activity, expenses were \$5.6m over budget due to increased maintenance costs and unbudgeted costs associated with the replacement of the old parking meters.

11. Equity increased by \$155m, \$115m of which results from asset revaluations.

12. Amongst the many capital projects completed for the year are the Blenheim Road deviation, (\$5.7m), upgrade of the parking meters, (\$2.6m) and strategic land purchases of \$8.5m.

13. Projects progressed include the Ocean outfall pipeline at South New Brighton (\$30.7m), Gowerton Place housing development (\$2.4m), the Burwood Landfill gas project (\$2.6m), construction of the 5th and 6th digesters, (\$10.4m), the upgrade of pump station 11 (\$3.9m), and the redevelopment of the Jellie Park swimming complex, (\$1.3m).

14. Of the balance, most went on providing the Council's basic services including \$6.1m on carriageway resurfacing, \$3.9m on footpath resurfacing, \$14.3m on kerb and channel, \$6.3m on road networks \$4.9m on renewals and replacements of water reticulation, \$16.5m on parks and \$4.3m on library books.

15. The Council has four financial ratios which form a key part of its financial risk management strategy. For all four actual results fell well within policy limits.

**FINANCIAL AND LEGAL CONSIDERATIONS**

16. There are no legal implications.



**6 Cont'd**

**STAFF RECOMMENDATIONS**

It is recommended:

- (a) That the General Manager Corporate Services be authorised to make changes as required by Audit to complete the accounts once the revaluation and related party data is finalised, or to correct errors in preparation for presentation of the report to the Council on 20 September 2007.
- (b) That the Christchurch City Council 2007 Annual Report be forwarded to the Council for adoption.

**7. TREASURY MANAGEMENT REPORT FOR 2006-07 YEAR - PERIOD TO 30 JUNE 2007**

<b>General Manager responsible:</b>	General Manager Corporate Services, DDI 941-8540
<b>Officer responsible:</b>	Corporate Finance Manager
<b>Author:</b>	Geoff Barnes, Funds and Financial Policy Manager

**PURPOSE OF REPORT**

1. The purpose of this report is to report on the management of Council loan liabilities and investments during the 2006-07 financial year.

**EXECUTIVE SUMMARY**

2. The Local Government Act 2002 requires publication of a Liability Management Policy and an Investment Policy (Policies). These are included as part of the Long-Term Council Community Plan (LTCCP) adopted by Council.
3. The Council's policies require periodic reporting to Council. Council has delegated reporting requirements to Council through the Audit and Risk Management Subcommittee.
4. To provide a regular and ongoing review, a Treasury Review Team appointed by the Chief Executive Officer in terms of the Policies overviews this function. Bancorp Treasury Services Ltd provides independent treasury advice.
5. The attached schedules summarise the results of management of Council's loan debt and investments for the period ending 30 June 2007. The debt is below that expected due to the lower capital expenditure program. Debt repayments are higher than expected due to BPDC loans repaid, funded by cash transferred to the Council at the time of the merger. All of the policy limits and KPIs were met.

**STAFF RECOMMENDATIONS**

It is recommended that the Audit and Risk Management Subcommittee receive the Treasury Management Report.

**8. UPDATE ON TAX AUDIT POSITION**

<b>General Manager responsible:</b>	General Manager Corporate Services, DDI 941-8540
<b>Officer responsible:</b>	Corporate Finance Manager
<b>Author:</b>	Diane Brandish, Corporate Finance Manager

**PURPOSE OF REPORT**

1. The purpose of this report is to provide the Audit and Risk Committee with an update of the Inland Revenue Department's, (IRD) audit of the Council's tax position.

**EXECUTIVE SUMMARY**

2. The IRD conducted a risk assessment during 2005 of the Council's group of companies for the 2004 tax return period. Formal notification of a tax audit, following from the results of the risk review, was received 21 March 2006. This audit covered the 2004 tax year, and was focussed on the Council itself, but was extended to other group companies on some specific issues.
3. The IRD's review was comprehensive; income tax, GST, FBT, PAYE and withholding tax were considered, and 85 formal information requests were received.
4. On balance, the Council fared quite well under the audit. There are a few areas for improvement as detailed in the report attached as Appendix 1.
5. The outstanding issues remaining are the eligibility of donation deductions and hurt and humiliation payments.
6. The Council engaged Deloitte and Lindsay McKay, a top tax barrister, to assist with the donation deductions matter and its response was referred to the IRD's Adjudications Unit at the beginning of this month. The Council's exposure under the audit is up to \$6.8m income tax on \$20.6m of deductions, plus penalties and interest. In addition there is a further \$6m relating to the 2006 and 2007 financial years. .
7. The Council engaged Kensington Swan to assist with its response on hurt and humiliation and this is still being considered by the IRD.
8. The total proposed assessment on the settled issues is \$176k plus possible shortfall penalties. A detailed report on these issues is the attached report.

**FINANCIAL AND LEGAL CONSIDERATIONS**

9. There are no legal implications. If the Council is unsuccessful in its defence of the eligibility of donations there is a significant financial implication, however, both Deloitte and Lindsay McKay feel that the Council has a very strong case against the IRD.

**STAFF RECOMMENDATIONS**

It is recommended that the report be received.

**9. DEBTOR MANAGEMENT REPORT**

<b>General Manager responsible:</b>	General Manager Corporate Services, DDI 941-8540
<b>Officer responsible:</b>	Corporate Finance Manager
<b>Author:</b>	Diane Brandish, Corporate Finance Manager

**PURPOSE OF REPORT**

1. The purpose of this report is to provide the Audit and Risk Management Subcommittee with an update of the Council's outstanding debtors.

**EXECUTIVE SUMMARY**

2. The Audit and Risk Management Subcommittee has requested a quarterly report on the Council's debtors. This report is attached as Appendix 1.
3. The total of outstanding trade debtors is \$5.2m compared with \$5.4m in April. The amount outstanding at 183+ days overdue has reduced from \$1.2m to \$0.6m largely through the write off the \$0.5m Lyttelton Marina debt inherited from the Banks Peninsula District Council.
4. For the total rates debtors the amount outstanding in the previous years column has reduced from \$1.4m to \$0.4m. This is partly due to the write off of \$0.2m of rates on Maori freehold land.
5. The write off of both of these debts was discussed at the May meeting of this Subcommittee and it was agreed that they would be forwarded to Council for formal write off. Due to a misunderstanding this did not happen and the papers are now in the process of being formally submitted. Any tax treatment of the debts will be deferred to the current financial year.

**FINANCIAL AND LEGAL CONSIDERATIONS**

6. There are no legal implications.

**STAFF RECOMMENDATIONS**

It is recommended that the report be received.

**29. 8. 2007**

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**10. ISSUES FOR FURTHER MEETINGS**

**11. NEXT MEETING**