



## Christchurch City Council

# AUDIT AND RISK MANAGEMENT SUBCOMMITTEE AGENDA

TUESDAY 28 JUNE 2005

AT 3PM

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.

**Principal Adviser**  
Roy Baker  
Telephone: 941-8540  
Fax: 941-8572

**Committee Secretary**  
Julie Sadler  
Telephone: 941-8438  
Fax: 941-8696

### INDEX

1. APOLOGIES
2. INTERNAL AUDIT PROGRAMME - 2005/06
3. RISK MANAGEMENT
4. ACCOUNTING FOR ACCUMULATED SICK LEAVE
5. NEXT MEETING

1. **APOLOGIES**

Councillor Graham Condon.

2. **INTERNAL AUDIT PROGRAMME - 2005/06**

<b>General Manager responsible:</b>	Director Strategic Investment
<b>Officer responsible:</b>	Internal Audit Manager
<b>Author:</b>	G Nicholas, DDI 941- 8550

**PURPOSE OF REPORT**

1. The purpose of this report is to advise the Subcommittee of the draft programme of internal audits for the year commencing 1 July 2005.

**EXECUTIVE SUMMARY**

2. Internal Audit provides an independent review function of the performance and adequacy of risk management by the Council. This also incorporates investigative and monitoring activities for compliance and probity. The attached draft internal programme incorporates work in these areas as well as assistance to the external auditors in completion of year-end reviews.

**FINANCIAL AND LEGAL CONSIDERATIONS**

3. The budgeted cost of the Internal Audit and Risk Management activities for the 2005/06 year is \$156,000. This covers the internal costs of the function as well as the employment of external resource when required (normally to provide specialist advice or audit time.)

**STAFF RECOMMENDATION**

It is recommended that the Council note the proposed internal audit programme.

**BACKGROUND ON DRAFT INTERNAL AUDIT PROGRAMME**

**What is an Internal Audit Programme?**

4. It is normal practice for an organisation's Audit Committee to approve the programme of internal audits.
5. Internal Audit is an independent review function within the Council, with the objective of providing assurance to management, that Council objectives are likely to be achieved effectively and efficiently within an acceptable degree of risk.
6. It provides management with two perspectives on the organisation's performance:
  - **Past performance** – the required results or outcomes have been and are being achieved now i.e. financial and service targets are being achieved; policies and laws are being complied with.
  - **Future performance** – the achieving of the desired results in the future is reasonably assured by the application of appropriate risk management processes and management controls.

## 2 Cont'd

7. Particular aspects that audit reviews aim to provide assurance on are:

1. Results are consistent with established goals and objectives.
2. There is compliance with policies, plans, procedures, laws, regulations and standards.
3. Information for decision-making is reliable and has integrity.
4. Resources are being economically and efficiently used.
5. Assets are safeguarded.
6. Staff are competent and committed.

- IIA Australian control criteria

### Programme Components

8. The programme has been compiled based on the following factors:
- Management requests for investigation into various concerns.
  - Providing assistance to Audit New Zealand in terms of accounting system reviews and in completion of end of year audit procedures.
  - Monitoring of processes where there is some potential risk of fraud or there are compliance or probity issues.
  - Rolling performance and risk reviews of activities prioritised on a risk basis.
  - General maintenance of the Council's risk register database.

### Setting of Priorities

9. The programme is a mix of audit assistance to Audit NZ at year end, compliance monitoring, systems security, reviews of accounting processes, reviews of key risks and activities:
- The work for external financial audit has been agreed with Audit NZ. This is given priority to ensure that the overall audit of the Annual Report is not delayed. Some credit for the work performed is allowed in the audit fee charged.
  - Compliance monitoring is performed throughout the year to provide assurance around the consistency of processes performed. It is intended to review the scope of the current monitoring and expand to further accounting processes particularly for fraud indications. This may involve purchase of a software tool designed for this purpose.
  - Activity-based audits are audits of operational aspects of the activity as well as applying audit scrutiny to the information and assumptions presented in the LTCCP. Activities are chosen based on the overall level of risk impact of the activity to the organisation (based on the overall level of risk as shown by the risk register). The risk register is still being currently reviewed and updated so this is very approximate and consideration is also given to the time elapsed since the last audit as well as significant individual risks that are associated with an activity. As internal functions are not "activities" in the true sense, these are listed as separate processes or functions.

Activity audits examine the basis for the levels of service intended, the required standards and laws that apply and whether what is intended to be achieved is in fact happening. We also examine the key processes that deliver on these service levels, their efficiency and whether the risks to future achievement are managed to an acceptable level.

**2 Cont'd**

**The Past Year's Programme (2004/05)**

10. This table also outlines the audits performed during the past year:

Activity Audits:

- Wastewater collection and treatment
- Library lending services
- Library life learning skills development
- Greenspace parks, reserves and open spaces (in progress)
- Treasury internal controls
- Community grants and funding
- Community Board expenditure

Compliance/Risk Audits:

- Volunteers
- Staff warrants
- Catering costs
- Revenue - City Transport, Greenspace, Community and Recreation Units
- Fixed asset systems
- Internet usage
- Staff expenses
- Staff cell phones and telephone usage
-

### 3. RISK MANAGEMENT

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

#### PURPOSE OF REPORT

1. The recent paper considered by the Council regarding the terms of reference for this Subcommittee included receiving reports from management on the adequacy of risk management practices within the Council.

This paper is designed to update the Subcommittee on where we are at with our current monitoring and reporting process.

#### EXECUTIVE SUMMARY

2.
  - (a) The Council for a number of years has operated a risk management system. It has been based upon NZ Standard 4360 and also uses the "NZS 4360 Risk Management for Local Government" handbook for identifying risk types. A risk ERA software database tool is also used.
  - (b) The process adopted was a bottom-up approach, but it is fair to say that it failed to gain significant traction at a middle management level. Many saw it as a chore rather than an opportunity for process improvement.
  - (c) The process adopted by the old Internal Risk Management Committee has since been continued by the Internal Audit function.
  - (d) By way of example of how risk is currently reported, attached is the consolidated view of City Environment (Appendix 1).
  - (e) While the current system has used the risk activities within the handbook (refer to point (a) above), there are a number of risks that are not defined (e.g. reputation). In addition, the risk area defined as operational has tended to be a "catch all".
  - (f) In line with the objective of increasing compliance throughout the organisation, and improved monitoring by the Council, risk management has been looked at by the Executive Team and we have determined the following actions:

#### 4. ACCOUNTING FOR ACCUMULATED SICK LEAVE

<b>General Manager responsible:</b>	General Manager Corporate Services
<b>Officer responsible:</b>	Corporate Finance Services
<b>Author:</b>	Diane Brandish, DDI 941-8454

##### PURPOSE OF REPORT

1. The purpose of this report is to make recommendations with regard to the Council's approach to accounting for accumulated sick leave when it adopts New Zealand Equivalents to International Financial Reporting Standards ("NZ IFRS").

##### BACKGROUND/DISCUSSION

2. The requirements for accounting for accumulated sick leave under NZ IFRS are provided by NZ IAS 19: *Employee Benefits* ("NZ IAS 19"). The standard requires an entity to recognise:
  - (a) a liability when an employee has provided service in exchange for employee benefits to be paid in the future; and
  - (b) an expense when the entity consumes the economic benefit arising from service provided by an employee in exchange for employee benefits.
3. Council employees have an entitlement to ten days of paid sick leave per annum. Those employed under the collective agreement have an uncapped entitlement to accumulated sick leave; for those on an IEA accumulated sick leave is capped at 40 days.
4. The Council does not currently accrue for accumulated sick leave, but will be required to do so when it adopts NZ IFRS.
5. During the financial years ending June 2003 and June 2004 the Council paid \$360,000 and \$300,000 respectively for sick leave over and above the ten day entitlement. These payments were calculated in accordance with the requirements of NZ IAS 19 by reviewing sick leave payments made to each employee. The higher of these two figures represents 0.01% of equity and 0.14% of expenditure. Those employees that took sick leave in excess of their current year's entitlement could have used sick leave carried forward from the previous financial year or from earlier financial years.
6. NZ IAS 19 defines the following classes of benefit:
 

Short-term employee benefits are those (other than termination benefits) which fall due wholly within 12 months after the end of the period in which the employees render the related service.

Other long-term employee benefits are those (other than post-employment benefits and termination benefits) which do not fall due wholly within 12 months after the end of the period in which the employees render the related service.
7. The sick leave taken during the two years analysed falls into both the short-term and other long-term categories as some employees took more than 20 days in total.

##### ANALYSIS

8. Considering each in turn the key points are as follows:

##### Short-Term Employee Benefits

9. Paragraph 8 of NZ IAS 19 states: "*Short-term employee benefits include items such as:*

*(b) short-term compensated absences (such as paid sick leave) where the absences are expected to occur within twelve months after the end of the period in which the employees render the related employee service".*

#### 4 Cont'd

10. Paragraph 9 states *"Accounting for short-term benefits is generally straightforward because no actuarial assumptions are required to measure the obligation or the cost. Moreover, (they) are measured on an undiscounted basis"*.
11. Paragraph 12 states, *"Entitlement to compensated absences falls into two categories, accumulating and non-accumulating"*

*'Accumulating compensated absences' are defined in paragraph 13 as, 'those that are carried forward and can be used in future periods if the current period's entitlement is not used in full'. The paragraph goes on to say, "(they) may be either vesting or non-vesting" and that "the obligation (to pay future compensated absences) exists, and is recognised, even if the compensated absences are non-vesting, although the possibility that employees may leave before they use an accumulated non-vesting entitlement affects the measurement of that obligation"*.

12. Paragraph 14 states, *"An entity shall measure the expected cost of accumulating compensated absences as the additional amount that the entity expects to pay as a result of the unused entitlement that has accumulated at the balance sheet date"*.

#### Other Long-Term Employee Benefits

13. Paragraph 126 defines these as including *"deferred compensation paid twelve months or more after the end of the period in which it is earned"* which clearly applies to some portion of the sick leave which has actually been taken by Council employees in the two years of our sample period. Paragraph 129 requires such liabilities to be measured at the "present value of the defined benefit obligation at the balance sheet date" less "the fair value at the balance sheet date of plan assets (if any) out of which the obligations are to be settled directly" (the Council does not have any such assets).

#### CONCLUSION

14. Although the amounts involved are not material, the Council should adopt the practice of accounting for accumulated sick leave entitlements. The provision should be based on the most up to date data of the Council's actual exposure, including trends in total accumulated sick leave and the annual amount of paid sick leave in excess of the current year's entitlement. The provision should be calculated as the sum of the following amounts for each employee:
  - Accumulated sick leave that is likely to be used in the coming financial year. This amount will not be present valued, but will take into account the likelihood of the employee using sick leave in addition to the current entitlement and the employee's likely pay rate when additional sick leave is used.
  - Accumulated sick leave that is likely to be used after the end of the coming financial year. This amount will be present valued and will take into account the likelihood of the employee using sick leave in addition to the current entitlement and the employee's likely pay rate when additional sick leave is used.

#### STAFF RECOMMENDATION

It is recommended that the Council adopt the practice of accounting for accumulated sick leave entitlements.

#### 5. NEXT MEETING