
NARROMINE SHIRE COUNCIL
ORDINARY MEETING BUSINESS PAPER – 10 NOVEMBER 2021
SUPPLEMENTARY REPORTS TO COUNCIL – FINANCE AND CORPORATE STRATEGY

1. 2020-21 ANNUAL FINANCIAL STATEMENTS

Author Director Governance
Responsible Officer General Manager

Executive Summary

This report presents further information to Council in relation to Item No 2 of the Finance and Corporate Strategy Report – 2020-21 Annual Financial Statements.

Internal Audit Committee Meeting

Council's Internal and Audit Committee Meeting met on 8 November 2021 wherein the Audited Financial Statements were presented by management.

The Chair of the Internal Audit Committee raised his concerns that the RFS assets had now been brought to account after the Committee provided its conditional 'in principle consent' via circular resolution.

In summary the Chair considered that for the last 3 years the RFS assets had not been included and that the Committee had supported management's previous position to not include them. To include them now overstates Council's operating result and assets by \$2.6m. Inclusion of the assets provides no benefit to Council, impacts Council's cash flow statements, and impacts future results in terms of \$356,000 annual depreciation, adding a cost to the operations of Council.

The General Manager advised the committee that the RFS assets were brought to account in accordance with the guidance and recommendation by Office of Local Government. The Audit Office also advised that if Council continue to not to recognise RFS assets, this would result in a High Risk Management letter and Council would be named in the Auditor General's Report to Parliament focusing on Local Government.

The Chair of the Committee stated that he could not support acceptance of the audited financial reports as they were considerably different to the referred statements to audit and to include the RFS assets without fundamental reasons as to why they are now recognised is misleading to ratepayers.

The Internal Audit Committee subsequently recommended: -

1. That management immediately corrects the accounts presented to the Committee today, reversing the impact from the single transaction of recognising the RFS assets which is a significant and an unnecessary, and potentially unauthorised, change in Council's accounting policies and historical position.
2. That Council is duly notified of this matter and that the proposed 'authorisation for issue' of the current accounts be deferred from 10th November to a later meeting when corrected accounts are available.

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3. That the Audit Office of NSW works with management to fast-track the correction of this single transaction matter, including amending and reissuing their associated reports.
4. That due to the facts of the matter, the Audit Office of NSW will not charge Council for any additional audit fees.
5. That the Audit Office of NSW ensure that the Chair of this Committee is provided with all future documents where the Chair is listed in them as being cc'd.

Advice Sought

Following the Internal Audit Committee Meeting, further urgent advice was sought in relation to this matter, both with the NSW Audit Office and the Office of Local Government.

The Office of Local Government has provided its Policy on inclusion or exclusion of the RFS assets being: -

Rural Fire Services (RFS) assets

Under Section 119 of the Rural Fire Services Act 1997 (NSW), 'all firefighting equipment purchased or constructed wholly or from money to the credit of the Fund is to be vested in the council of the area for or on behalf of which the firefighting equipment has been purchased or constructed'.

The NSW Government has confirmed its view that these assets are not controlled by the NSW Rural Fire Services or the State, Councils need to assess whether they control any rural firefighting equipment in accordance with Australian Accounting Standards and recognise in their financial statements any material assets under their control and state the relevant accounting policy in relation to the treatment.

The NSW Audit Office's position on the matter is: -

Australian Accounting Standards – AASB-SAC 4

Definition of "assets" includes future economic benefits controlled by the entity as a result of past transactions or other past events;

"Control of assets" means the capacity of the entity to benefit from the asset in the pursuit of the entity's objectives and to deny or regulate the access of others to that benefit.

Criteria for recognition of assets is "an asset should be recognised in the statement of financial position when and only when: -

- (a) It is probable that the future economic benefits embodied in the asset will eventuate; and
- (b) The asset possesses a cost or other value that can be measured reliably.

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The Department of Planning, Industry and Environment, which includes OLG, has confirmed that the NSW Rural Fire Service does not control rural firefighting equipment. Determination of this is based on: -

- The Rural Fires Act 1997 vests rural fire-fighting equipment to councils.
- Service agreements govern the way the RFS can use these assets for fire mitigation and safety works in a council area.
- As a land owner, Council has a responsibility for mitigation and safety works under the Rural Fires Act 1997
- Council is responsible for maintaining the assets but has transferred this responsibility to RFS through the service agreement.
- In the event of the loss of an asset, the insurance proceeds are used to require or build a similar asset which is again vested in Council.

The NSW Audit Office has advised that based on their data collected in the year 2020, there are 27 councils that have recorded RFS assets of approximately \$109 million vs 68 councils that did not record the RFS assets in their financial statements worth \$119 million.

Materiality

Materiality is a judgmental decision and it is noted that RFS assets represent **0.4%** of the overall Infrastructure, Property, Plant and Equipment balance for the financial year 2019-20. Hence, the recognition of RFS assets was not considered significant for financial statements purposes.

As the Department confers that the assets are not controlled by the NSW Rural Fire Services or the State, and the NSW Audit Office requires that the RFS assets be recognised in Council's financial statements under Australian Accounting Standards, this inclusion is not considered to be material.

Rural Fire District Service Agreement

Under the Rural Fire District Service Agreement between Council and the Commissioner of the NSW Rural Fire Service, Council pays a contribution to RFS for district equipment and sheds etc. Under the agreement Council agrees to make available to and allow the Commissioner and RFS to use the district equipment which is owned by, vested in or under the control of Council.

The Commissioner agrees that they will maintain the district equipment on behalf of Council in accordance with applicable service standards.

In addition, the RFS will maintain a register of the district equipment.

In the same manner, the Commissioner and RFS are able to occupy and use buildings (being land and buildings) for use without interference. Council is to pay all rates, taxes, electricity etc where applicable, maintain the buildings, and insure them.

Prior to preparation of the 2020/21 Financial Statements, Council conferred with RFS to determine the fleet as at 30 June. A spreadsheet/register was provided by RFS with current fleet and value of these assets.

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Legal Implications

In accordance with the Local Government Act 1993, Council must present its audited financial reports, together with the auditor's reports, at a meeting held on the date fixed for the meeting (s.419).

Any person may make submissions to Council with respect to Council's audited financial reports or with respect to the auditor's reports.

A submission must be in writing and must be lodged within 7 days after the date on which those reports are presented to the public.

Council must ensure that copies of all submissions received by it are referred to the Audit Office.

The Council may take such action as it considers appropriate with respect to any such submission, including giving notice to the Departmental Chief Executive of any matter that appears to require amendment of Council's financial reports (s.420).

The Internal Audit Committee has requested their recommendation be considered by Council.

Internal Audit Committee roles and responsibility

Council's Internal Audit Committee is an advisory committee and has no executive powers.

Specifically the Committee is to satisfy itself that the annual financial reports comply with applicable Australian Accounting Standards and are supported by appropriate management sign-off on the statements and the adequacy of internal controls; review the External Audit opinion, including whether or not appropriate action has been taken in response to audit recommendations and adjustments; consider contentious financial reporting matters in conjunction with Council's management and external auditors.

Primary responsibility for management of Council rests with the Council and the General Manager. The Statement by Councillors and Management in accordance with Section 413(2)c is signed by the Mayor, a Councillor, the General Manager and Council Responsible Accounting Officer.

Risk Management Issues

It is the responsibility of the Councillors and Management to ensure that the general-purpose financial statements have been prepared in accordance with the Local Government Act, the regulations made thereunder, the Australian Accounting Standards and other pronouncements of the Australian Accounting Standards Board, the Local Government Code of Accounting Practice and Financial Reporting (s.413(2)).

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In addition, it is those charged with governance that should consider the impact of misstatements from previous years that have not been corrected in the period in which they occurred.

Previously the RFS assets were not recognised by Council as there was differing opinion as to the level of control Council had with the assets.

It is now the Department of Planning, Industry and Environment's (including OLG) determination that NSW Rural Fire Service and the State does not control rural firefighting equipment.

The Audit Office agrees with the Department's position and as such records a misstatement where a Council does not record this equipment.

Council has lodged its audited financial statements with the Office of Local Government prior to 31 October 2021 as per the Act (s. 417).

If Council is to amend its financial reports it risks non-compliance with the above section of the Act (verbally confirmed to the General Manager by the OLG). The Audit Office has confirmed that non-compliance with the LG Act would be included in the management letter, the Report on Conduct of the Audit and specifically raised in the Auditor-General's Report to Parliament.

In addition, the Audit Office advised that it would be exceptionally difficult to recall the statements now that they have been submitted to the OLG. If Council was to accept the Internal Audit's recommendation, Council would need to write to the Audit Office to request that the Auditor-General re-issue the audit opinion.

The Audit Office advised they would be required to advise the Minister as it is a significant matter, include a high-risk matter in the management letter and Report on Conduct of the Audit, and included specific commentary in the Report to Parliament.

In addition, there are other resourcing and staffing matters that should be considered should Council determine to recall its audited Financial Statements.

It should be noted that Council's Financial Data Return has already been submitted. Council will likely miss its Annual Report publication deadline under the Act, being 30 November.

The financial statements would also need to be amended to specifically explain why the statements were recalled, and a new certification issued. The Audit Office would draw reference to the additional note in the financial statements with an Emphasis of Matter in any revised audit opinion.

The Audit Office would be required to re-issue its Engagement Closing Report, Report on Conduct of the Audit, Management Letter, and Independent Auditor's Report. This would also involve undertaking additional audit procedures, such as subsequent events reviews, as the date of the signing of the financial statements would be amended.

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The underlying issue of non-recognition of the RFS assets would also be reported as a high-risk matter in the management letter, the Report on Conduct of the Audit, and the Report to Parliament.

The Audit Office advised that costs associated with recalling the submitted audit financial statements would be charged to Council.

Internal Audit Committee Meeting – 10 November 2021

The voting members of the committee were informed of Management's recommendation to Council to endorse the 2020/21 Finance Statements in their current form.

The following recommendation was made by the committee (unanimous).

1. That the Committee notes the additional information provided by management and the discussion that ensued in respect of their position to change the longstanding accounting policy of Council to not recognise RFS Assets.
2. That despite the additional information provided and the discussion that has ensued today, the Committee reaffirms their recommendations that were passed at their meeting of 8th November 2021.
3. That the Committee is unable to endorse, in good conscience or with any integrity, the current version of the financial statements and the associated audit reports, which in their view contains a significant error and creates unintended misstatements and confusion as a result of the unjustified change of accounting policy and the subsequent recognition of RFS Assets.
4. That Council be promptly advised of the outcomes from both of this week's Committee meetings, mindful that today's scheduled Council meeting includes the agenda item 'Annual Financial Statements' with the drafted intention being to 'authorise for issue' the financial statements and audit reports that this Committee is unable to endorse.
5. That Council requests the creation or amendment of a policy document to address [REDACTED] being able to change historical accounting policies without due notification or consideration.

Legal advice will be sought from the Office of Local Government as to any legal avenues available to Council in recalling submitted Audited Financial Statements.

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Despite the above and in view of the numerous risks associated with recalling the Financial Statements which are not considered by the Office of Local Government or the NSW Audit Office to be incorrect, it is recommended that Council endorse the 2020-21 Audited Financial Statements and Auditors report as presented.

RECOMMENDATION

1. That Council adopts the 2020-21 Audited Financial Statements and Auditors Report, as presented.
2. That Council inform the community that the RFS assets have been recognised in Council's current year financial statements and not in prior years.

Jane Redden
General Manager