

Item No: C11/21-882

NSW AUDIT OFFICE REVISION TO DRAFT ANNUAL FINANCIAL STATEMENTS 2020/21

Responsible Division: General Manager
Officer: Manager Finance
File Number: 9065055
Community Strategic Plan Goal: *Transparent and accountable leadership*

SUMMARY

The 2020/21 (FY21) Draft Annual Financial Statements were presented to the Audit, Risk and Improvement Committee (ARIC) for their review and discussion before being referred to the Auditors. The minutes of the ARIC meeting were reported at the Council Meeting held on 8 September 2021.

The Draft Statements were then adopted by Council at the Ordinary meeting held on 20 October 2021. After this meeting was held, Council's Auditors advised Finance and the General Manager of a \$71.6m negative adjustment required to the income statement.

This report is to readopt the recommendations given the late significant adjustment.

Following endorsement by Council, the signed Financial Statements will then be presented to the Audit Office to allow Council to receive the final Independent Auditor Report and the Report on Conduct of the Audit. This will then enable Council to lodge the Financial Statements to the Office of Local Government.

Council has requested the Office of Local Government (OLG) provide a one-month extension to the 31 October deadline, to 30 November 2021, to submit the authorised Financial Statements after readoption.

Council will then publicly advertise the final statements and a representative from the Audit Office will attend the Ordinary Council Meeting on 17 November 2021 to present the Financial Statements and discuss the audit for Cumberland City Council. The Financial Statements are attached to this report.

RECOMMENDATION

That Council:

- 1. Pursuant to the provisions of Section 413 of the *Local Government Act 1993*, hereby declares that it has prepared the Annual Financial Statements for the 2020/2021 financial year ending 30 June 2021, and has formed an opinion based on the advice of Council officers and reports**

attached, that the Annual Financial Statements for Cumberland City Council:

- a) Have been prepared in accordance with:
 - the *Local Government Act 1993* (as amended) and the Regulations made there under;
 - the Australian Accounting Standards and other pronouncements of the Australian Accounting Standards Board;
 - The Local Government Code of Accounting Practice and Financial Reporting.
 - b) Present fairly Council's operating results and financial position for the 2020/21 financial year.
 - c) Accord with Council's accounting and other records and that Council is not aware of any matters that would render these statements false or misleading in any way.
2. Pursuant with Section 413(2)(c) of the *Local Government Act*, authorise the Mayor, Deputy Mayor, General Manager and the responsible accounting officer to sign the 'Statements by Councillors and Management' for the General Purpose and Special Purpose Financial Statements which must then accompany these reports.
 3. Publish a public notice as soon as practicable after Council receives a copy of the auditor's reports to advise of the Presentation by the Audit Office of the 2020/21 Financial statements at the Ordinary Council meeting to be held on 17 November 2021, as per Section 418 (3) of the *Local Government Act*.

REPORT

Financial Summary

Council is reporting a deficit of \$59.48m compared to a budget of \$5.794m. Council had previously reported a \$12.2m surplus, however after the Council meeting held on 20 October, Council's was notified by its Auditors of an expense adjustment of \$71.6m.

A negative \$71.6m adjustment to the revaluation reserve was required to be reported through the Income Statement. While Council has an overall positive revaluation reserve of over \$310m in its balance sheet, a subsequent analysis was done by Councils Auditors, after the Council meeting on 20 October, on individual asset classes since amalgamation which showed the Roads and Stormwater asset classes had little or no positive reserve balances. Decrements as a result of revaluation are subsequently recognised in the Income Statement where existing surpluses are not held in respect of that asset class, and not through the balance sheet where the revaluation reserve balance is held.

The draft Financial result presented to ARIC on 9 August 2021, and at the Council meeting held on 20 October 2021 showed an Operating Result before capital of over

\$12m. As a result of this \$71.6m revaluation adjustment, Council is now reporting a \$59.48m deficit before Capital.

As a result of this late NSW Audit Office revision, an Extraordinary Audit, Risk and Improvement meeting is planned to be held on 1 November 2021 to present and discuss the revised statements. This is not a common adjustment for Councils, and may generally only impact amalgamated Councils whose historic revaluation reserves do not get carried over to the newly formed Council. The former Councils had an asset revaluation reserve of over \$1 billion dollars prior to amalgamation.

Income Statement	2021 Actual \$'000	2021 Budget \$'000	Variance \$'000
Operating Income	\$210,186	\$207,988	\$2,198
Capital Income	\$26,233	\$24,373	\$1,860
Total Income from Continuing Operations	\$236,419	\$232,360	\$4,059
Expenses	\$198,075	\$202,194	\$4,119
Revaluation decrements of IPPE	\$71,595	-	-\$71,595
Total Expenses from Continuing Operations	\$269,670	\$202,194	-\$67,476
Net Operating Result	-\$33,251	\$30,166	-\$63,417
Net Operating Result before Capital grants and Contributions	-\$59,484	\$5,794	-\$65,278
One off/non-recurring Income*	\$9,694	\$5,020	
Operating Result before Capital grants and Contributions Excluding One Offs	-\$69,178	\$774	-\$69,952
*One off/non-recurring Income			
Joint Associations		\$490	
Profit on Sale	\$421		
Fair Value Interest	\$246		
Fair Value Investment Property	\$4,527	\$4,530	
Federal Grant	\$4,500		
Total One Off/non Recurring Income	\$9,694	\$5,020	

The following is a summary of the results against the original budget:

- Total User Fees and Charges of \$28.1m, being \$3.3m less than the original budget. The major cause for the variance was a drop in childcare fees, pool income and hall hire, which were all impacted by COVID-19.
- Operational Grants of \$21.3m, which was \$4.21m more than the original budget. This is mainly due to the \$4.5m Financial Assistance Grant paid in advance.
- Capital Grants and Contributions increased \$7.319m due to additional grants for the Parramatta Road Urban Improvement Program and other road grants.
- Revaluation decrements of Infrastructure, Property Plant and Equipment saw a \$71.6m for the Roads and Stormwater asset classes. This cannot be budgeted for as revaluations are finalised towards the end of the Financial Year. This is a non-cash adjustment.

- Employee Costs had a favourable variance of \$6m due to additional leave reductions and increased scrutiny applied to the backfilling of positions.
- Materials/Other Expenses decreased \$4m with savings in waste tipping fees of \$1m, \$450k in functions and activities, \$600k in utilities costs and consumables, and \$200k in postage costs due to a reduction in mail notifications.

Statement Of Financial Position	2021 Actual \$'000	2020 Actual \$'000	Variance \$'000
Total Assets	\$2,742,715	\$2,685,295	\$57,420
Total Liabilities	\$103,440	\$94,165	\$9,275
Net Assets	\$2,639,275	\$2,591,130	\$48,145
Capital Expenditure (Note C1-6)	\$57,165	\$63,240	-\$6,075
Total Cash and Investments	\$163,503	\$135,695	\$27,808
Unrestricted Cash	\$9,634	-\$3,361	\$12,995

Total cash and investment were \$163.5m which includes external reserves of \$106.1m (up \$25.6m from prior year), \$47.7m internal reserves (down \$10.8m from prior year), and unrestricted cash \$9.6m (up \$12.995m from prior year).

There was an increase in external reserves of \$25.6m from prior year due to:

- The S711 reserve increased \$13.1m due to receipt of \$17.5m in 2020/21, interest received \$0.8m, low expenditure of \$7.1m, and a loan repayment \$1.9m.
- Unexpended Grants up \$11.9m due to an unexpected pre-payment of the Parramatta Road Urban Improvement Program Grant.
- Waste Reserve up \$2.5m. This is a required increase due to having one of the lowest balances in NSW.
- Stormwater down \$1.7m due to large expenditure on stormwater.

There was a decrease in internal reserves of \$15.6m from the prior year due to:

- Merrylands CBD Reserve down \$11.4m due to expenditure of \$30m loan for the project.
- Woodville Reserve down \$9.4m due to expenditure from money received in 2017.
- Property Reserve up \$3.2m – Net proceeds on sale of property.

The positive unrestricted cash position is a result of good financial management by Council throughout the COVID-19 crisis.

Key Ratios	Benchmark	2021	2020
Unrestricted current ratio (times)	>1.5x	2.61	2.14
Operating performance ratio (%)	>0%	3.77%	1.60%
Debt service cover ratio (times)	>2x	6.37	8.4
Rates and annual charges outstanding ratio (%)	<5%	6.37%	5.88%
Infrastructure renewals ratio (%)	>100%	113.30%	101.93%
Own source operating revenue ratio (%)	>60%	79.51%	78.71%
Cash expense cover ratio (months)	>3 months	7.54	6.39

Council's rates and annual charges outstanding ratio was 6.37%, which is slightly above the industry benchmark of 5%. The increase was a COVID related trend as Council was unable to enforce collection. Council offers payment plans through its *Rates Hardship Policy* to assist ratepayers with financial difficulty which also impacts this ratio.

The Financial Planning and Sustainability Policy requires Council to budget based on meeting the criterion. There has been an upward trend in all the ratios due to improvements in profit, unrestricted cash, and cash investments. This highlights the importance of carrying positive non-restricted cash.

The infrastructure renewal ratio is above the benchmark and measures the effectiveness of Council's ability to reinvest depreciation and to fund maintenance

Overall, there was a combination of strong financial management, efficiency programs, capital renewal reduction and government initiatives. Council needs to continue with good financial management to ensure it is prepared for future financial challenges.

The Audit of the FY21 Draft Annual Financial Statements

The FY21 Financial Statements were audited from 16 August 2021 to 8 October 2021 by Grant Thornton (GT) on behalf of the Audit Office (AO) of NSW. An audit clearance meeting was held with GT, the AO, and Finance management on 11 October 2021, after which a closing report was provided summarising the outcome of the audit as discussed in the meeting.

An updated closing report will be provided and is anticipated to reflect a "Corrected Monetary Misstatement" of \$71.6m, as a result of the revaluation decrements reported in the Income Statement

The AO have advised that they are likely to express an unmodified opinion on the Financial Statements which is a great outcome for Council and continues Council's excellent history of clean audits and unmodified audit opinions.

Some discussion points in the report were around

- COVID-19 pandemic and its impact on Council
- Information Technology controls and risk mitigation
- Cyber Security monitoring and controls

- Population growth risk and demands on services and infrastructure
- Timely capital works delivery
- Revaluation of asset timelines and methods

The AO was satisfied with how Council was progressing with these points and did not identify any reportable matters and advised there would be no material misstatements around these.

An immaterial misstatement of \$3m was identified around capitalisation of Council's TechnologyOne software under a Software as a Service (SaaS) arrangement. This was a result of the International Financial Reporting Standards Interpretations Committee (IFRIC) releasing an agenda decision in April 2021 clarifying its interpretation of how current accounting standards apply to SaaS arrangements. SaaS arrangements are service contracts providing the Council with the right to access a cloud provider's application software over the contract period. Costs incurred to configure or customise, and the ongoing fees to obtain access to the cloud provider's application software, are recognised as expenses when the services are received. Management assessed the impact of the decision to have an immaterial impact on the financial statements and the AO confirmed it is not significant as to modify the opinion in the final Independent Auditor's Report.

COMMUNITY ENGAGEMENT

There are no consultation processes for Council associated with this report.

POLICY IMPLICATIONS

There are no policy implications for Council associated with this report.

RISK IMPLICATIONS

There are no risk implications for Council associated with this report.

FINANCIAL IMPLICATIONS

Council reported a deficit of \$59.48m compared to budget of \$5.794m. Unrestricted cash increased \$12.995m from the prior year, which is a great result given the COVID climate. With COVID lockdown continuing into the 2021/22 Financial Year, Council needs to ensure it continues to manage its expenditure and available cash.

CONCLUSION

The Mayor, Deputy Mayor, General Manager and the responsible accounting officer sign the general purpose and special purpose financial statements for Cumberland City Council for the period ended 30 June 2021 to enable the Audit Office to provide Council with the final Independent Auditor Report and the Report on Conduct of the Audit.