

ANNUAL REPORT 2022 – AUDIT NEW ZEALAND MANAGEMENT REPORT

To: Risk and Assurance Committee

Meeting Date: Tuesday 23 May 2023

From: Patricia Christie – Acting Group Manager – Finance and Assurance

Approved: Michael Day - Chief Executive

Approved Date: Wednesday 17 May 2023

Open Agenda: No

Public Excluded Agenda: Yes

Reason(s) for the Public Excluded

Section of the Act	Subclause and Reason under the Act	"Plain English" Reason	When Report Can Be Released
7(2)(h)	(2)(h)	Enable any local authority holding the information to carry out, without prejudice or disadvantage, commercial activities	When the Chief Executive determines there are no longer any reason to withhold the information under the Act.

Purpose and Summary

The purpose of this report is to provide the Committee and Council with the Management Report provided by Audit New Zealand on issues noted during their completion of the audit of the June 2022 annual report for Council and its subsidiaries, which was completed in March 2023.

Recommendations

That the Risk and Assurance Committee:

1. Receive the report 'Annual Report 2022 – Audit New Zealand Management Report'.
2. Note the recommendations raised by Audit New Zealand and management's response to those issues.
3. Note the continued operational issues experienced during the audit and request that regular updates from both management and Audit New Zealand are provided to the Committee.

4. Thank the Chair and Independent member for the work which they did behind the scenes working through the complexities and issues associated with the 2022 Annual Report audit opinion.
5. Note that Audit New Zealand have requested additional fees in relation to the 2022 audit for items not included in the audit proposal letter (audit of asset revaluations), technical issues that arose during the audit (ICL valuation at group level) and additional time incurred in relation to operational issues.
6. **Recommend to Council** that it approve the payment of additional audit fees for the 2022 audit of \$95,000.

Background

At the completion of the interim and year end audits, Audit New Zealand provided the Council with a report which outlines issues of risk and non-compliance that were identified during the audit progress and recommends the action which management should take.

Management review the report prior to issue and provide comments on the issues identified.

Audit New Zealand manage audits on a three year cycle with audit fees set by the Office of Auditor General for a three year period.

Issues

Management Report

The purpose of the management report is to report back to both management and governors, the findings from the audit and also the areas which Audit New Zealand consider that improvements need to be made.

The key issues and recommendations identified in the report are:

- The issuing of an 'except for' opinion in relation to the 2021 comparatives as a result of the differing opinions regarding the need for a revaluation of Property Plant and Equipment in 2021.
- Seven new recommendations were made of which one was urgent and six considered necessary.
- There were two uncorrected misstatements noted, these were minor in nature and the decision not to correct them was done in conjunction with Audit New Zealand and being mindful of materiality limits.

The 2022 audit was complex and there were a number of difficulties that needed to be addressed.

The urgent recommendation identified by Audit New Zealand relates principally to the preparation process for the Annual Report document. These difficulties have been acknowledged by management and were in the main the result of a significant turnover in Council staff and the need for new staff to learn our annual report preparation and public sector audit processes. Both our preparation and audit processes are much more involved and complex than private sector organisations. While staff acknowledge that there were a number of versions of the annual report provided, the lack of clear direct feedback early in the audit process meant the extent of the issue was not fully understood by management initially and when it was necessary steps were taken.

Steps are well underway to update our annual report processes and in particular the consolidation process to achieve a better quality of deliverable.

As has been previously discussed with the committee there were a number of operational challenges associated with the audit. The key issues were:

- The methodology used for the 2022 audit was principally a remote audit with the team raising issues and requests by email or on the electronic dashboard and a large number of requests were misinterpreted by Council staff or the auditors receiving them. While some members of the team did visit Invercargill, this didn't necessarily result in more phone or face to face interactions.
- A large number of audit staff rolled on and off the audit, many only on the audit for a week so additional council staff time was needed to ensure that all issues were addressed prior to the auditor rolling off the job.
- Covid impacted the staffing from both Council and specialists (e.g. valuers and other independent experts) providing input into the annual report which resulted in some key deadlines not being met.
- The level of input required from Council finance and corporate planning staff (in particular) in answering audit requests for further information and then the questions and issued raised is significant, especially given the length of the audit. This continues to be a significant factor for the 2023 audit as the timing of the audit will also coincide with key LTP milestones and the citywide revaluation for rating.

Steps are underway to address the recommendations noted in the report however given the short period of time between management receiving the report and the 2023 interim audit beginning on 6 June 2023 few are expected to be closed.

Audit Fees

The management report noted that Audit New Zealand were going to seek to recover additional audit fees from Council.

An initial additional fee proposal was provided by Audit New Zealand to the Chief Executive and Acting Group Manager Finance and Assurance. Discussions regarding this proposal have been held with Audit New Zealand. The additional fee proposal is broken down into three areas:

Items not included within the Audit Fee Proposal Letter

The fee for the 2022 audit ICC Group annual report was set in an Audit Proposal letter dated 17 June 2021 at \$175,130.

When the 2022 audit plan was provided for presentation to this committee it was verbally noted that a fee estimate had not been included in the audit plan for the increased scope (valuation). Two options were provided:

- to charge a reasonable additional fee after the audit based on actual costs incurred; or
- request an amendment to the Audit Fee via the Office of the Audit General.

The first option was chosen by management.

For the 2022 audit Council revalued all classes of property plant and equipment which it holds at fair value (operational land and buildings, roading, water supply, sewerage and stormwater). This was the first revaluation for three years.

During the audit a number of technical issues were identified that required additional resource both within Council and by the Audit team these included:

- Investment in Invercargill Central Limited (ICL) and treatment of impairment at ICC group level together with the potential impairment of the Council loan to ICL.
- Settlement of the Sir Tim Shadbolt v ICC case
- Invercargill city Property Limited prior period error.
- How the 2021 qualification over property plant and equipment assets would be treated post revaluation.

The total additional fee for this aspect is \$55,000, with the bulk being in relation to the audit work associated with the revaluation of assets.

Shared Costs

As has been reported to the Committee, during the period between the completion of the 2021 and 2022 Annual Reports, monthly meetings were held between the audit team, key Council staff and the independent members of the Risk and Assurance Committee.

The cost of these meetings had not been factored into the overall cost of the audit and the additional fee for this aspect is \$10,000. This reflects a share of the cost of the audit director and manager attending these meetings.

Impact of delivery challenges

As discussed above and outlined extensively in the management report Council had some significant challenges in the delivery of the annual report and information for the audit. While some of these factors were beyond our control (Covid) there were certainly a number of areas which on reflection we could have done better, such as the number of drafts of the financial statements that were provided.

In discussions with Audit New Zealand an additional fee of \$30,000 has been allocated.

Overall

The total additional fee being sought is \$95,000. Officers acknowledge that this is a significant increase. Officers will seek to have asset revaluation fees and an allowance for new technical matters included within the audit fee proposal which is currently being prepared, or listed by asset class so budgets can be appropriately agreed.

Audit New Zealand have advised that its total write-off of cost in relation to this engagement is in excess of \$250,000.

Next Steps

Officers will continue with the detailed planning for the 2023 Audit and preparation for the interim audit in June 2023.

Attachments

1. Annual Report 2022 - Audit New Zealand Management Report (A4577930)