

Report to the Council on the audit of
Greater Wellington Regional Council
for the year ended 30 June 2014

Management report

Key messages

We have completed the audit for the year ended 30 June 2014. This report sets out our findings from the audit and draws attention to areas where the Greater Wellington Regional Council (the Regional Council) is doing well or where we have made recommendations for improvement.

As part of our assessment of the overall control environment we have considered the arrangements in place for some key Regional Council projects, and our key findings are that the Regional Council has:

- Established appropriate governance and monitoring processes to manage these risks involved in the purchase of tranche 2 of the Matangi trains.
- Appropriate measures in place to address governance requirement and manage the risks associated with the implementation of the Public Transport Operating Model.
- We followed up on the Regional Council's water supply asset management plans against our recommendations from the prior year. Overall, significant improvements have been made to the water supply asset management plans. We will be reviewing asset management planning across the Regional Council as part of the audit of the LTP.

Other areas of audit focus include:

- We considered the revaluation of the Regional Council's assets completed during the period. We are satisfied with the revaluation of the Regional Council's infrastructure assets has been accounted for in accordance with generally accepted accounting practice.
- The Regional Council has continued its strong commitment in the non-financial performance area. We noted no issues from our review on planning and reporting of service performance information, and associated systems and controls used.
- The audit of financial statements has gone much better this year. Finance has been committed to delivery and a significant improvement has been seen compared to last year. There will be opportunities on the part of both audit and the finance team to improve the process further next year, and we will continue to work closely with Finance to ensure an effective and efficient audit programme is established for the 2014/15 audit.

Thank you

We would like to thank members of the Council, management, and staff for their assistance during the audit.



Andy Burns
Audit Director
10 November 2014

Contents

1 Our audit opinion.....4

2 Control environment.....4

3 Our areas of focus for this year5

4 Future Audit Focus7

5 Status of previous recommendations8

Appendix 1: Status of previous recommendations9

1 Asset management plans.....9

2 Going concern and possible sale of the Regional Council Centre or Pringle House Limited.....9

3 Property, plant and equipment revaluation 10

4 Preparation of the financial statements..... 10

5 Centralised Contract Management System..... 11

6 High annual leave balances..... 12

7 Local Government Rating Act 2002 12

8 Funding of Greater Wellington Rail Limited through the issuance of share capital 13

9 Sale of Ganz Mavag train fleet..... 13

Appendix 2: Mandatory disclosures 14

1 Our audit opinion

1.1 We issued an unmodified audit opinion

We issued an unmodified audit opinion on 30 September 2014. This means that we were satisfied that the financial statements and non-financial performance information fairly reflected the Regional Council's activity for the year and its financial position at the end of the year.

In forming our audit opinion, we considered the following matters.

1.2 Uncorrected misstatements

The financial statements and non-financial performance information are free from material misstatements, including omissions. However, in the course of the audit, we have found:

- certain misstatements that are individually and collectively not material to the financial statements and the non-financial performance information; and
- certain immaterial disclosures, required by generally accepted accounting practice, that have been omitted from the financial statements.

We have discussed any misstatements that we found with management. We are satisfied that these misstatements are individually and collectively immaterial.

2 Control environment

We performed a high-level review of the control environment. It is not an assessment of management's overall performance or an assessment of how effective the Regional Council is in achieving its financial and non-financial objectives. We considered the overall attitude, awareness, and actions of members of the Council and management in establishing and maintaining effective management procedures and internal controls. Our assessment of these areas was based on regular discussions with key members of senior management, members of the Council, and our accumulated knowledge of the Regional Council's business.

In performing this assessment, we considered both the "design effectiveness"¹ and "operational effectiveness"² of internal control. The explanation of these terms is outlined below. However, it is not the purpose of our assessment to provide you with assurance on internal control in its own right. As such, we provide no assurance that our assessment will necessarily identify and detect all matters in relation to internal control.

2.1 Compliance with significant legislation

We did not identify any breach of legislative requirements during our audit.

¹ Control is effective to either prevent or detect a material error in either the financial statements and/or non-financial information. The control is "fit for purpose".

² Control has operated effectively throughout the period tested.

We reviewed the systems in place to ensure that significant legislation has been complied with. The Regional Council has a number of policies and business processes in place to ensure the appropriate management of legislative obligations.

There are no issues that require your attention.

2.2 Financial information systems and controls

We reviewed the internal controls in place for your key financial information systems. Internal controls are the policies and processes that are designed, implemented and maintained by members of the Council and management – to provide reasonable assurance as to reliability and accuracy of financial reporting, as well as compliance with significant legislative requirements. Both “design effective” and “operationally effective” internal control is important to minimising the risk of either fraud or misstatement occurring. The responsibility for the effective design, implementation and maintenance of internal control rests with members of the Council.

Apart from the matters mentioned below in Appendix 1 “*Status of previous recommendations*”, there were no other matters we wish to bring to your attention.

2.3 Service performance information and associated systems and controls

We reviewed the environment, processes, and controls for developing service performance objectives and targets, as well as monitoring and reporting on service performance. This included reviewing the Regional Council’s Annual Plan. We focused on obtaining an understanding of how the Regional Council:

- identifies its activities;
- develops its plans; and
- measures and monitors its performance.

The Regional Council has continued its strong commitment in this area. We noted no issues from our review on planning and reporting of service performance information, and associated systems and controls used.

3 Our areas of focus for this year

3.1 Purchase of tranche 2 of the Matangi trains and sale of Ganz Mavag train fleet

The Regional Council has entered into an agreement with the Matangi supplier Hyundai Rotem for the purchase of a further 35 Matangi trains to replace the ageing Ganz Mavag fleet, along with an agreement to sell the 42 Ganz Mavag units. This is a significant project for the Regional Council, which carries risks such as delays in delivery or units not delivered to the agreed specification.

The Regional Council has implemented processes and practices to manage build and delivery of tranche 2 of the Matangi trains. Notably, a governance board has been set up with the purpose of resolving issues, providing approvals, and maintaining a

live risk register. We noted that the Regional Council is carefully managing the relationship with the suppliers and receives regular progress updates.

We are satisfied that the Regional Council has considered the risk associated with this transaction, and have established appropriate governance and monitoring process to manage the risks.

We have commented in detail on the sale of the Ganz Mavag train fleet in Appendix 1 of this report.

3.2 Procurement - Public Transport Operating Model

The Regional Council has responsibility for the planning and funding of the Metlink public transportation network. Companies are contracted to provide these services, which includes trains, buses and the harbour ferry services. We noted that one of the key initiatives is the development of the new Public Transport Operating Model (PTOM).

The PTOM procurement strategy along with the Wellington Regional Transport Plan will ensure that the Regional Council is in compliance with New Zealand Transport Authority's (NZTA) procurement requirements that promote efficient delivery of services and value for money.

The Regional Council is applying this strategic change in the way public transport is planned and procured, and has completed its first market sounding for the delivery of rail and bus transportation within the region.

We note that the continued risk and challenges for the Regional Council is that PTOM was developed by Government to be applied to all other subsidised public transport models. While the model has its advantages, its application for the Wellington region, particularly transitioning from the current arrangement, will be relatively complex.

The Regional Council has appropriately established a team to manage the project, which is drawn from a range of professional competencies. It has also assigned a probity auditor. We are satisfied that the Regional Council has appropriate measures in place to address governance requirements and manage the risks associated with implementation.

3.3 Property, plant and equipment values - revaluation

The revaluation of the Regional Council's infrastructure assets has been accounted for in accordance with generally accepted accounting practice.

During the year, the Regional Council's subsidiary revalued its rail and infrastructure assets (rolling stock, rail infrastructure and other transport infrastructure assets). The net change in Regional Council and group's asset values resulting from the 2014 valuations was a decrease of \$2.15m. The decrease was primarily within the rolling stock and transport infrastructure, amounting to less than 1% of the total value of this asset class. From our review, we noted that the decrease in the rolling stock asset class was driven by a reduction in the replacement cost of the Matangi trains along with a further reduction in the old Ganz units after consideration of the remaining useful life.

We noted during our audit that the Regional Council has reflected on its 2013/14 financial statement revaluation adjustment for the parks and forest and water supply assets classes. These adjustments were driven by:

- A part of the asset in the parks and forest class was not revalued in the 2012/13 financial years. However, the valuation was completed and the asset values updated as at 1 July 2013.
- Adjustment to the water supply asset class to accurately reflect the useful lives of some categories of assets in this class.

The overall adjustments are not material in the context of the overall asset value. While we agree that the impact was not material, we continue to emphasise our prior year recommendation that improvements are required to documentation, controls and process used in the Regional Council's revaluations of assets.

4 Future Audit Focus

While not significantly impacting the 2013/14 year, some risks and issues have an ongoing audit focus:

4.1 Regional Governance changes

A number of applications for reorganisation of the Wellington region's local authorities are with the Local Government Commission. The Local Government Commission is currently considering these and is expected to issue a draft proposal, which will propose either one or two unitary authorities for the existing region.

4.2 Audit of the Council's Long Term Plan

The Local Government Act 2002 Amendment Act 2014 made a number of changes to the nature of the consultation processes related to the Long Term Plan (LTP). The Office of the Auditor-General is finalising the audit approach and methodology for the audit of the 2015-25 LTP under the revised legislation.

At this time, we expect our audit to focus on:

The consultation document

The consultation document is designed to be a flexible, short and relevant document for councils to more easily and appropriately consult with their communities. We will focus on whether the consultation document provides "an effective basis for public participation in local authority decision making processes" (s93b) and whether the content is supported by adequate underlying information.

Infrastructure strategy

The Infrastructure strategy is another new requirement for the 2014/15 LTP. Management has undertaken significant work to improve the Regional Council's knowledge of its asset base, and is developing Service plans for infrastructure related activities that will provide a basis for the LTP. We will consider the Regional

Council's ability to support its conclusions behind its infrastructure strategy, including consistency with the financial forecasts and levels of service.

Financial strategy

The Regional Council's financial strategy will outline the 10 year financial objectives and provide the settings for developing and utilisation of funding tools and service levels. We will consider the consistency of the strategy with financial and non-financial information, as well as alignment with the infrastructure strategy noted above.

4.3 Changes to the accounting standards framework for public benefit entities (PBEs)

As noted in last year's report the Regional Council and Group is required to transition to the new PBE standards after 1 July 2014. This means Regional Council and Group's first financial statements, including its forecast financial statements, under the new standards are for the year ending 30 June 2015.

To ensure a smooth transition to the new standards, the Regional Council and group will need to plan and prepare in a timely manner for the transition to the new PBE accounting standards.

We ask that the Regional Council and group provide us with a copy of their detailed transition plan with dates included as soon as this has been finalised. We intend to complete our work on the transition statements sometime in the first half of next calendar year. We will work closely with Regional Council and group to ensure a smooth transition.

5 Status of previous recommendations

The status of each matter that was outstanding in previous reports to members of the Council are summarised in Appendix 1.

We note in particular that:

- We followed up on the Regional Council's water supply asset management plans against our recommendations from the prior year. Overall, significant improvements have been made to the water supply asset management plans. Most of our recommendations have been resolved; however a number of matters are still in progress. We will be reviewing asset management planning across the Regional Council as part of the audit of the LTP.
- The audit of financial statements has gone much better this year. Finance has been committed to delivery and a significant improvement has been seen compared to last year. There will be opportunities on the part of both audit and the finance team to improve the process further next year, and we will continue to work closely with Finance to ensure an effective and efficient audit programme is established for the 2014/15 Long Term Plan and Annual audit.

Appendices

Appendix 1: Status of previous recommendations

In progress:

1 Asset management plans

Previous recommendation

Further progress has been made on asset management planning. In particular, the Regional Council has reviewed the way it does asset planning across its business groups, adopted a prioritisation framework for minor transport assets and maintenance and are finalising public transport and updating water supply asset management plans.

During our 2014 audit, we will follow up on the recommendations from our review of the draft water supply and transportation asset management plans provided to management when the plans were being developed.

Current status - *In progress*:

We followed up on the Regional Council's water supply asset management plans against our recommendations from the prior year. Overall, significant improvements have been made to the water supply asset management plans. Most of our recommendations have been resolved; however a number of matters are still in progress. We will continue to work with the Regional Council as it progresses to the adoption of this plan, which is not due until June 2015, in line with Long Term Plan agendas.

Likewise with the transportation asset management plan, we will continue to work with the Regional Council as it progresses to the adoption of this plan, which is not due until June 2015, in line with Long Term Plan agendas.

2 Going concern and possible sale of the Regional Council Centre or Pringle House Limited

Previous recommendation

It was determined by the Board of Pringle House Limited (PHL) that the building had minimal leasing potential. This and a significant write-down of the investment property, means that there were concerns as to whether the preparation of the financial statements on the going concern assumption is appropriate. In response, the Regional Council provided the Board with a letter of financial support (to the extent necessary to meet its on-going operational and capital expenditure obligations) for PHL, which will continue for at least one year from the date of the issuance of the audit opinion for PHL.

Current status - *In progress*:

The Regional Council has extended its financial support for PHL, which will now expire on 24 September 2015. We are satisfied that PHL has made the appropriate disclosures in its 2013/14 financial statements.

During the September 2014 we noted that the PHL Board reached the decision to test the market for the possible sale of the Regional Council Centre. We will keep up to date with developments and consider the impact on PHL future reporting.

3 Property, plant and equipment revaluation

Previous recommendation

Water infrastructure, and parks and forest assets were revalued at 30 June 2013. The Regional Council decided to defer the revaluation of rail assets until the next financial year.

Due to different valuer(s) being engaged not all of the assets in the parks and forest asset class were included in the revaluation as at 30 June 2013. Once it became known, management were of the view that, based on the value of the assets not valued any movement is unlikely to have a significant impact on the financial statements. While we agree that the impact was not material, we noted that significant improvements are required to the controls and process used for revaluing parks and forest assets.

Current status - *In progress*:

Please refer to Section 3.5 above.

4 Preparation of the financial statements

Previous recommendation

During the prior year final audit there were significant delays in the preparation of the financial statements.

We recommend in 2013/14 that management prepare pro-forma financial statements in the proposed reporting format and provide this for our review before the commencement of the final audit. This would enable us to provide comments to management early and agree on the proposed disclosures.

We also recommend that the Regional Council ensures that it allows time in the account preparation process to conduct a thorough quality assurance review over the financial statements (including the notes to the financial statements) before providing the draft for audit.

Current status - *In progress*:

We have worked closely with Finance to ensure audit timetables have been kept.

Finance has been committed to delivery and a significant improvement has been seen compared to last year.

However, due to the tighter timeline this year, a full and complete set of the Regional Council and its subsidiaries' WRC Holdings and Port Investments accounts were not made available for us prior to the commencement of final audit as agreed; these were received in full during the last week of the onsite audit visit. We did receive the Greater Wellington Rail and Pringle House Limited's accounts prior to the commencement of the audit.

In an effort to meet delivery timeline, there was also insufficient time for the Finance team to perform its quality assurance review over the sets of accounts. This in turn led to multiple sets of accounts provided for our review, which also impacted the timing of our comments on the final version. We note that the departure of the CFO prior to the start of the year end audit created a stretch on the finance team. Having a full time CFO could have provided that extra quality assurance oversight to the finance team.

While there have been challenges, in our view the audit has gone well this year, and we will continue to work closely with Finance to ensure an effective and efficient audit programme is established for the 2014/15 Long Term Plan and Annual audit.

Management Comment

Management acknowledge that receiving multiple accounts is not the most efficient process. However financial statements initially provided of each Parent entity were substantially completed subject to cashflow, tax and consolidation. These final items do take time to complete and often change through the audit process. It was the latter issue of the tax calculations that caused the most delay.

Management will be working with Audit on improvements to how the tax is reviewed and audited.

We enjoyed working with audit this year and wish to thank you for your assistance.

5 Centralised Contract Management System

To better manage the implementation of contracts, reconcile contract expenditure with other financial management systems, and provide strategic procurement management information, the Regional Council should consider the benefit of working towards implementing a centralised contract management system that is linked to its financial management systems.

Management notes our 2013/14 interim audit findings, "We are not fully convinced that the benefits from a centralised contract management system outweigh the cost saving and gains we might get from a council wide system. This is being looked at for further consideration."

Current status - In progress:

We will follow up on this matter during our 2014/15 interim audit.

6 High annual leave balances

High annual leave balances expose the Regional Council to risks and challenges including:

- increased liability as accumulated leave balances increase with any future wage increase; and
- the possibility of weakened internal control as “job rotation” is reduced. Rotation reduces the risk of fraud through potentially identifying internal anomalies/errors in an employee’s regular area of work.

We recommend the Regional Council consider what, if any, additional focus is needed to reduce the numbers of employees with high leave balances.

Management notes our 2013/14 interim audit findings, “confirm that we do monitor and manage staff leave balances. Balances are reported regularly to the CEO by the Group General Managers.”

Current status - In progress:

We will follow up on this matter during our 2014/15 interim audit.

Recommendation resolved:

7 Local Government Rating Act 2002

Previous recommendation

We recommended that the Regional Council may wish to review the processes it currently employs with a view to gaining a greater level of assurance that TAs are collecting the correct rates.

From time-to-time issues have been highlighted on a local authority’s compliance with the Local Government Rating Act 2002. The consequences of non-compliance can be serious.

As part of our review, we enquired into the systems and processes that the Regional Council has in place for overseeing the collection of rates by territorial local authorities (TAs). The Regional Council relies on the territorial authorities in the region to collect rates on their behalf under an agency arrangement. The TAs are collecting the amount of rates that the Regional Council expects: The Regional Council has an expectation from when the rates are struck as to how much rates (broken down to general rate, targeted transport rate, water levy etc) they are expecting to receive and the Regional Council receives monthly rates summaries from the TAs and reviews them.

Current status - resolved:

Management are of the view that their risk in this area is significantly reduced through the agreement with the TA’s and the regular reviews and reconciliations performed by the Regional Council’s finance team.

We have considered management views and accepted the view that the current practice of the Regional Council is adequate for the associate risk.

8 Funding of Greater Wellington Rail Limited through the issuance of share capital

Previous recommendation

The Regional Council proposes to fund its subsidiary, Greater Wellington Rail Limited (GW Rail), for the second tranche of Matangi trains through the issuance of share capital. GW Rail will call up that share capital when the funding is needed.

While we had no issues with the arrangement, we draw the Regional Council attention that if the funding from the Regional Council to WRC Holdings is provided to GW Rail as the trains are purchased then at each balance date, WRC Holdings (and therefore the Regional Council) will have to consider whether its investment in GW Rail is impaired.

Current status - resolved:

The funding of GW Rail through the issuance of share is correctly treated - no impairment has been recognised as the cost is lower than the fair value.

9 Sale of Ganz Mavag train fleet

Previous recommendation

The first tranche of the Trains were delivered during the current year and the second tranche not until 2016, we expect the following to be reflected in the financial statements as at 30 June 2014:

- proceed to be recognised as revenue for the units delivered in February 2014 and assets derecognised; and
- the remaining Ganz units will continue to be classified as property, plant and equipment in the financial statements.

Current status - resolved:

Revenue has been correctly recognised in the 2013/14 financial year for the Tranche 1 assets and the remaining units have been appropriately classified as Property, Plant and Equipment in the financial statements with accelerated depreciation until 2016.

Appendix 2: Mandatory disclosures

Area	Key messages
Our responsibilities in conducting the audit.	<p>We carried out this audit on behalf of the Controller and Auditor-General. We are responsible for expressing an independent opinion on the financial statements and reporting that opinion to you. This responsibility arises from section 15 of the Public Audit Act 2001.</p> <p>The audit of the financial statements does not relieve management or the Council of their responsibilities.</p> <p>Our audit engagement letter contains a detailed explanation of the respective responsibilities of the auditor and the Council.</p>
Auditing standards	<p>We carry out our audit in accordance with generally accepted audit standards. The audit cannot and should not be relied upon to detect every instance of misstatement, fraud, irregularity or inefficiency that are immaterial to your financial statements. The Council and management are responsible for implementing and maintaining your systems of controls for detecting these matters.</p>
Auditor independence	<p>We confirm that, for the audit of the Greater Wellington Regional Council's financial statements for the year ended 30 June 2014, we have maintained our independence in accordance with the requirements of the Auditor-General, which incorporate the independence requirements of the External Reporting Board.</p> <p>Other than the audit, we have not provided any engagements for the Greater Wellington Regional Council during the year ended 30 June 2014. In addition, we have no relationships with, or interests in, the Greater Wellington Regional Council.</p>
Other relationships	<p>We are not aware of any situations where a spouse or close relative of a staff member involved in the audit occupies a position with the Greater Wellington Regional Council that is significant to the audit.</p> <p>We are not aware of any situations where a staff member of Audit New Zealand has accepted a position of employment with the Greater Wellington Regional Council during or since the end of the financial year.</p>
Unresolved disagreements	<p>We have no unresolved disagreements with management about matters that individually or in aggregate could be significant to the financial statements. Management has not sought to influence our views on matters relevant to our audit opinion.</p>