



TOWN OF BASSENDEAN

Audit Closing Report

30 June 2020 Financial Statements



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1 EXECUTIVE SUMMARY

1.1 Purpose of the Closing Report

The primary purpose of this Audit Closing Report is to brief the Town of Bassendean (**Town**) on the results of our substantially completed audit of the 30 June 2020 financial statements. This report should be read in conjunction with our Audit Planning Memorandum (**APM**) provided to the Town on 21 April 2020.

1.2 Scope and approach

Except for additional audit procedures relating to the late changes to the *Local Government (Financial Management) Regulations 1996*, there were no other changes to the audit scope or approach set out in the APM.

1.3 Key deliverables

1.3.1 Annual financial statements audit report

The Auditor General is required to issue an opinion on the financial statements of the Town for the year ended 30 June 2020. In accordance with section 7.9(1) of the *Local Government Act 1995 (LG Act)*, the audit report will be addressed to the Town Mayor, with a copy being forwarded to the Chief Executive Officer (**CEO**) and the Minister for Local Government.

We will recommend to the Auditor General that an unqualified audit opinion is issued on the financial statements (refer section 2.1).

1.3.2 Report on other legal and regulatory requirements

The Auditor General is also required by regulation 10(3) of the *Local Government (Audit) Regulations 1996* to report:

- Any matters indicating non-compliance with Part 6 of the LG Act or the *Local Government (Financial Management) Regulations 1996 (Financial Management Regulations)* or applicable financial controls;
- Any material matters indicating significant adverse trends in the financial position or the financial management practices;
- Whether all required information and explanations were obtained during the audit;
- Whether audit procedures were satisfactorily completed; and
- Whether the Asset Consumption Ratio and the Asset Renewal Ratio, disclosed in the notes to the financial statements, were supported by verifiable information and reasonable assumptions.

During the audit we identified four matters that require reporting under regulation 10(3) of the *Local Government (Audit) Regulations 1996* (refer section 2.3). We will recommend to the Auditor General that these matters are mentioned in the audit report.

1.3.3 Management letters

Seven significant findings, seven moderate findings and four minor findings were identified during the 2019/20 preliminary audit and one significant finding and two moderate findings was identified during the 2019/20 final audit (refer section 2.4).

1.4 Matters of significance

In accordance with section 24(1) of the *Auditor General Act 2006*, the Auditor General is required to report to Parliament on matters arising out of the performance of the Auditor General's functions that are, in the opinion of the Auditor General, of such significance as to require reporting.

We confirm that no such matters came to our attention during our audit work.

1.5 COVID-19

We concur with the Town's assessment that there is no significant impact on the Town's financial statements or operations due to the COVID-19 pandemic (refer section 6).

1.6 Independence

The audit methodology of RSM Australia requires that we conduct a regular evaluation of our independence. We have fully satisfied ourselves that we do not have any actual or perceived conflict of interest.

1.7 Our appreciation

We wish to express our thanks for the co-operation shown by Town and Town staff during the audit.

2 AUDIT COMPLETION

2.1 Statutory financial statements and audit opinion

We have completed the audit fieldwork on the statutory financial statements of the Town for the year ended 30 June 2020.

The financial statements are general purpose financial report prepared in accordance with the LG Act, accompanying regulations and, to the extent that they are not inconsistent with the LG Act, Australian Accounting Standards.

We have discussed all significant auditing and accounting issues with management, and these have been satisfactorily resolved and are discussed in this report. The audit and assurance procedures are designed to support the audit and assurance opinions and they cannot be expected to identify all weaknesses or inefficiencies in the Town's systems and working practices.

Based on the evidence, which has been assessed during our audit, we expect to conclude that the financial statements of the Town:

- (i) Are based on proper accounts and records; and
- (ii) Fairly represent, in all material respects, the results of the operations of the Town for the year ended 30 June 2020 and its financial position at the end of that period in accordance with the LG Act and, to the extent that they are not inconsistent with the LG Act, Australian Accounting Standards.

We will recommend to the Auditor General that an unqualified opinion is issued on the financial statements.

2.2 Emphasis of matter – basis of accounting

During the audit we identified the following matters which, although they will not require any modification to the audit opinion, are of such importance to require additional communication in the auditors' report in the form of an Emphasis of Matter paragraph:

2.2.1 Vested improvements on vested land

Note 11 to the financial statements describes the basis of accounting for vested improvements on vested land. Regulation 17A of the Financial Management Regulations, requires the Town to measure vested improvements at fair value and the associated vested land at zero cost. This is a departure from AASB 16 *Leases*, which requires the Town to also measure vested improvements at zero cost.

2.2.2 Land under roads

Note 11 to the financial statements describes the basis of accounting for land under roads. In respect of the comparatives for the previous year ended 30 June 2019, the former regulation 16 of the Financial Management Regulations did not allow the Town to recognise some categories of land, including land under roads, as assets in the financial statements.

2.3 Report on other legal and regulatory requirements

As disclosed in Note 33 to the financial statements, the following material matters indicate significant adverse trends in the financial position of the Town:

- The Asset Sustainability Ratio has been below the Department of Local Government, Sport and Cultural Industries (DLGSCI) standard and OAG threshold of 0.8 for the last three years.
- The Operating Surplus Ratio has been below the DLGSCI standard and OAG threshold of Zero (0) for the last three years.

We will recommend to the Auditor General that these matters are communicated in the audit report.

2.4 Management letter – control weaknesses

Our audit approach involves the use of a rotation methodology when planning our test of controls. Consequently, not all control cycles are subject to testing and only certain transaction cycles are in audit scope each year. In accordance with the APM, we performed key management control testing over the revenue, payroll, payment and fixed assets transaction cycles. In addition, we tested general IT controls to the extent described in section 9.

Based on our testing, the following control weaknesses were identified during the preliminary and final audit stages:

2.4.1 Prior period audits

Two significant findings, five moderate findings and one minor finding were reported during the prior year audit:

Findings	Rating	Status
1. Assess unrestricted to payroll module	Significant	Resolved
2. No formal information technology security policy	Significant	Resolved
3. Purchasing policy	Moderate	Resolved
4. Purchasing approvals exceeding delegations	Moderate	Resolved
5. Overdue debtors accounts	Moderate	In progress
6. Employees with excessive annual leave	Moderate	In progress
7. No formal information technology security policy	Moderate	Resolved
8. Monthly bank and investment reconciliations are not dated by the preparer	Minor	Resolved

2.4.2 2019/20 preliminary audit

Seven significant findings, seven moderate findings and four minor findings were identified during the 2019/20 preliminary audit:

Findings	Rating
1. Assessment of new accounting standards 15, 1058 and 16	Significant
2. Backdating of purchase orders	Moderate
3. Review of payroll exception report	Moderate
4. Petty cash policies	Moderate
5. Journal entries to be timely reviewed	Minor
6. Regular review of policies and procedures	Minor
7. Primary Return	Minor
Information system specific findings	Rating
8. IT governance – policies and procedures	Significant
9. Network - user access management	Significant
10. Synergy finance application – user access management	Significant
11. Remote – user access management	Significant
12. Virus protection and security monitoring	Significant
13. Business continuity and incident management	Significant

14. IT risk management	Moderate
15. Cyber vulnerability management	Moderate
16. IT change management	Moderate
17. Physical and environmental security	Moderate
18. Network password management	Minor

2.4.3 2019/20 final audit

One significant finding and two moderate findings were identified during the 2019/20 final audit:

Findings	Rating
1. Revenue has not been recognised in accordance with AASB 15 or AASB 1058	Significant
2. Incorrect fixed assets capitalisation date	Moderate
3. Excess annual leave management	Moderate

The action taken by the Town to address the 2019/20 management letter findings will be reviewed during the 2020/21 audit.

2.5 Compliance with laws and regulations

We have reviewed the Town's controls to manage the risk of systemic failure to comply with relevant laws and regulations. We also reviewed Town and other relevant committee minutes of meetings throughout the year to identify any recorded non-compliance with relevant laws and regulations.

As a result of our procedures, nothing has come to our attention, within the scope of the audit, to indicate non-compliance with relevant laws and regulations.

2.6 Unadjusted audit differences

There were no unadjusted audit differences noted during the audit.

2.7 Summary of audit adjustments

Three audit adjustments were processed by the Town during the course of the final audit.

Entry	Account Description	Debit (\$)	Credit (\$)
1	Retained earnings (equity) Grants and subsidies (revenue) Contract liability/Deferred revenue (liability) <i>Being adoption of AASB 15 and 1058 in relation to grants</i>	1,163,967	93,000 1,171,393
2	Retained earnings (equity) Contract liability/Deferred revenue (liability) <i>Being adoption of new revenue standard in relation to rates</i>	284,237	284,237

3	Contract liability/Deferred revenue (liability)	93,000	
	Grants and subsidies (revenue)		93,000
	Grants and subsidies (revenue)	100,426	
	Contract liability/Deferred revenue (liability)		100,426
<i>Being recognition of revenue as per new revenue standard AASB 15 and 1058</i>			

2.8 Subsequent events

Management has represented that, other than those matters disclosed in the financial statements, there are no significant subsequent events between the end of the financial year and the date of this Audit Closing Report, which may significantly impact the results of the operations and the state of affairs of the Town for the financial year.

2.9 Contingent liabilities and commitments

Management has represented to us that, other than those matters disclosed in the financial statements and at section 2.10 below, there are no other outstanding or pending litigation, contingent liabilities or commitments.

We have received and reviewed the solicitors' confirmations and, except for those matters detailed in the notes to the financial statements, we have not become aware of any other material contingent liabilities, pending litigation or commitments.

2.10 Environmental matters

Currently the Town has six potential contaminated sites. We have reviewed the key controls used by the Town to manage the risk of failure to comply with *Contaminated Sites Act 2003*. We also reviewed Town and committee minutes of meetings throughout the year to identify any reported non-compliance with the relevant environmental laws and regulations.

The Town represented that all identified contaminated sites are reported to the Department of Water and Environmental Regulation (**DWER**) and recorded in the DWER Contaminated Sites Database.

The Town is unable to accurately quantify its clean-up liabilities for potentially contaminated sites as at 30 June 2020.

Based on our work within the scope of our engagement, nothing came to our attention to indicate the key controls around contaminated sites are ineffective.

2.11 Outstanding audit matters

The audit opinion is subject to the finalisation of our audit process. The key matters still outstanding are:

- a) Our final review of the financial statements;
- b) Our receipt of the signed management representation letter; and
- c) Our performance of subsequent events review up to date the audit report is issued.

3 NEW ACCOUNTING STANDARD ADOPTED IN THE CURRENT YEAR

3.1 AASB 15 Revenue from Contracts with Customers

The Town adopted AASB 15 *Revenue from Contracts with Customers* on 1 July 2019, which resulted in changes to accounting policies. In accordance with the transition provisions of AASB 15, the Town adopted the new rules retrospectively with the cumulative effect of initially applying AASB 15 recognised as at 1 July 2019. Comparative information for prior reporting periods was not restated in accordance with AASB 15 transition requirements.

As disclosed in the Note 29(a) to the financial statements and section 2.7 above, the impact of AASB 15 as at 1 July 2019 was not material.

We have audited the Town's application of the impact of adopting AASB 15 and we conclude that the Town has correctly applied the requirements and made appropriate disclosures in the notes to the financial statements.

3.2 AASB 1058 *Income of Not-for-Profit Entities*

The Town adopted AASB 1058 *Income for Not-for-Profit Entities* on 1 July 2019, which resulted in changes to accounting policies. In accordance with the transition provisions of AASB 1058, the Town adopted the new rules retrospectively with the cumulative effect of initially applying AASB 1058 recognised as at 1 July 2019. Comparative information for prior reporting periods were not restated in accordance with AASB 1058 transition requirements.

As disclosed in the Note 29(b) to the financial statements, the impact of AASB 1058 as at 1 July 2019 amounted to \$1,325,924.

We have audited the Town's application of the impact of the initial adoption of AASB 1058 and we conclude that the Town has correctly applied the requirements and made appropriate disclosures in the notes to the financial statements.

3.3 AASB 16 *Leases*

The Town adopted AASB 16 *Leases* on 1 July 2019, which resulted in changes to accounting policies. In accordance with the transition provisions of AASB 16, the Town has applied AASB 16 to its leases retrospectively, with effect from 1 July 2019. The Town applied the modified retrospective approach, which did not require the comparatives to be restated.

AASB 16 requires vested land and vested improvements to be accounted for as a single lease component. In accordance with the Financial Management Regulations, which take precedence over Australian Accounting Standards, the Town is required to measure vested improvements at fair value and the associated vested land at zero cost. This is a departure from AASB 16, which requires the Town to measure the vested improvements also at zero cost.

We have audited the Town's application of the impact of applying AASB 16 and we conclude that the Town has correctly applied the requirements and made appropriate disclosures in the notes to the financial statements. However, although the Town's departure from AASB16 will not result in a qualification to the audit report, there will be an Emphasis of Matter paragraph included in the audit report to draw users' attention to this matter (refer section 2.2).

4 AMENDMENTS TO LOCAL GOVERNMENT FINANCIAL MANAGEMENT REGULATIONS

Effective 6 November 2020, Financial Management Regulations were amended with regulation 16 being removed and regulation 17A being amended with effect from 1 July 2019.

4.1 Impact of removal of regulation 16

The Town is required to de-recognise the values attributable to certain vested crown land assets previously required to be recognised as assets, as well as the associated revaluation surplus from 1 July 2019. These assets have been measured as concessionary lease right-of-use assets at zero cost in accordance with AASB 16.

As disclosed in Note 29 to the financial statements, the impact of applying the amendment as at 1 July 2019 was the derecognition of vested land (golf course) was not material.

We have audited the Town's assessment of the impact of applying amended regulation 17A and we conclude that the Town has correctly addressed the requirements and made appropriate disclosures in the notes to the financial statements.

4.2 Impact of amendment of regulation 17A

Plant and equipment type assets (being plant and equipment and furniture and equipment) are to be measured under the cost model, rather than at fair value with effect from 1 July 2019. No revaluations were carried out during the year, it was deemed by the Town that fair value approximates the cost model value at the date of the change.

We concur with the Town's assessment that fair value of plant and equipment type assets approximates the cost model value.

5 AREAS OF AUDIT EMPHASIS

As mentioned in the APM, our audit focus was on those areas where we assessed there to be a significant risk of material misstatement in the financial statements. We designed and performed procedures to be able to conclude, with reasonable assurance, whether each significant risk area is free from material misstatement. The following is a summary of the significant risk balances for the past three financial years:

Significant risk area	30 June 2020 \$'000	30 June 2019 \$'000	30 June 2018 \$'000
Revenue recognition			
• Rates	13,376	13,126	13,184
• Fees and charges	5,970	6,221	5,893
• Trade and other receivables	1,706	1,022	1,103
Procurement			
• Materials and contracts	5,168	7,641	7,090
• Property, plant and equipment (additions)	1,190	200	659
• Infrastructure (additions)	816	1,158	1,615
Fixed assets			
• Property, plant and equipment	56,339	55,780	56,196
• Infrastructure	105,287	107,397	109,136

The outcome of our audit procedures for each significant risk area is summarised in the following table:

Significant risk area	Key risks	Free from material misstatement
Revenue recognition <ul style="list-style-type: none"> • Rates • Fees and charges • Trade and other receivables 	<p>Rates, fees and charges revenue are material and a significant risk due to the multifaceted method of calculation, the high dependency on information systems and the significant regulatory compliance regime.</p> <p>Compliance with AASB 15 and AASB 1058 can be complex and requires detailed analysis of contracts and appropriate application of revenue recognition policies.</p> <p>Calculation and recording of the expected credit loss provision in accordance with <i>AASB 9 Financial Instruments</i> can also be complex and is subject to estimation.</p>	✓
Procurement <ul style="list-style-type: none"> • Materials and contracts • Property, plant and equipment (additions) • Infrastructure (additions) 	<p>These expenditure items are a significant risk due to the materiality of the amounts, the different cost allocation methods, the strict and complex requirements of the Town's purchasing policy and the risk of management override of controls.</p>	✓

Significant risk area	Key risks	Free from material misstatement
Fixed assets <ul style="list-style-type: none"> Property, plant and equipment Infrastructure 	Property, plant and equipment and Infrastructure are material assets in the Statement of Financial Position. Removal of regulation 16 and compliance with amended regulation 17A of the Financial Management Regulations can be complex and require some material adjustments to the carrying value of assets and associated asset revaluation reserves.	✓

6 IMPACT OF COVID-19

As the COVID-19 pandemic continues to evolve, developments throughout 2020 have been causing great uncertainty for the global economy. Whilst the initial effects were being felt most by the travel industry and education providers, the impact is now considerably wider and is creating significant uncertainty for supply chains and the global economy. This uncertainty is creating additional risks that entities may not have encountered before.

The Town advised that the COVID-19 pandemic did not have any significant impacts during 2019/20. There were some minor impacts on operations, including:

- Temporary suspension of all bookings relating to Town venues and halls
- Various community services scaled back
- All scheduled events and programs cancelled
- Temporary suspension of various Town operated centers
- Suspend/wave various fees and charges charged in relation to Town owned buildings and infrastructure

We concur with the Town's assessment that the COVID-19 pandemic did not have any significant impact on the Town's operations or the 2019/20 financial statements.

7 OTHER CRITICAL DISCLOSURES IN THE FINANCIAL STATEMENTS

We also audited the following critical disclosures in the financial statements by verifying the underlying calculations and auditing the evidence to support the amounts disclosed:

Critical disclosure	Key risks	Comply with accounting standards
Related party	Disclosures of key management personnel remuneration and related party transactions are not in accordance with AASB 124 <i>Related Party Disclosures</i> .	✓
Financial ratios	The underlying data is incomplete or inaccurate and the calculations of the ratios are incorrect and not in accordance with Financial Management Regulations.	✓

8 FRAUD RISK

Under Australian Auditing Standard ASA 240 *The Auditor's Responsibilities Relating to Fraud in an Audit of a Financial Report*, when planning and performing audit procedures and evaluating the results, the auditor must consider the risk of material misstatement in the financial statements because of fraud and error. To address our responsibilities relating to fraud, we designed and implemented audit procedures to obtain sufficient appropriate audit evidence regarding the assessed risks of material misstatement due to fraud. Procedures and the results of our testing are detailed below:

8.1 Management override of control

Management is in a unique position to perpetrate fraud because of management's ability to manipulate accounting records and prepare fraudulent financial statements by overriding controls that otherwise appear to be operating effectively. Management override can occur in areas such as journal entries, accounting estimates and judgements.

Based on our work, nothing has come to our attention to indicate that the Town does not have proper processes and controls to manage the risk of management override of controls and that material key estimates and judgments are properly assessed and brought to account. Our audit did not detect any instances of fraud.

8.2 Element of unpredictability

We also incorporated an element of unpredictability in our audit procedures to address the risk of Town staff, who are familiar with the normal audit procedures, being more able to conceal fraudulent activity.

Due to the risks of unauthorised transactions that may be associated with the use of corporate credit cards, our unpredictable testing selected a sample of credit card transactions. We tested whether:

- The purchases are supported by appropriate documentation
- The purchases were proper
- The credit card transactions are reviewed and approved by management in a timely manner.

The elected members that make up the Town's Town cannot use these cards as the LG Act does not allow them to incur debts. Instead, local governments pay allowances or reimburse expenses to an elected member.

During our audit work, nothing came to our attention to suggest the fraudulent use of corporate credit cards.

8.3 Fraud incidences during the audit

We have made enquiries of Town, the CEO and management regarding whether they have knowledge of any incidences of material fraud during the financial year. Based on our enquiries and other audit procedures, we did not become aware of any incidences of misconduct or fraud, which would have a material impact on the financial statements.

9 INFORMATION SYSTEM AUDIT

The Town's financial management information system is classified by the audit team as 'complex'. Audit also determined that the information system general controls are critical to the processing of financial transactions and the preparation of the financial statements. Due to these circumstances, the audit team included an information system audit specialist (**ISAS**) to assess the risk of material misstatement imposed by the Information Technology (**IT**) environment.

The ISAS obtained an understanding of the information system, including the related business processes, relevant to financial reporting, including how the information system captures events and conditions, other than transactions, that are significant to the financial statements. The ISAS also tested general IT controls around system access and testing controls over computer operations within specific applications which are required to be operating correctly to mitigate the risk of misstatement in the financial statements.

As a result of the ISAS' procedures, we identified and reported a number of control weakness in the audit management letter (refer to section 2.4)

10 NEW ACCOUNTING STANDARDS APPLICABLE IN FUTURE YEARS

There are no new accounting standards, which would materially impact the Town's financial statements in future financial years. We reviewed and concur with the Town's disclosures in the notes to the financial statements regarding new accounting standards.

11 MATTERS RELATING TO FUTURE AUDIT

Based on our discussion with the Town's management, the following matters will be materially relevant for the 30 June 2021 financial statement audit:

- Adoption of AASB 16 and regulation 17A requires right-of-use assets (vested improvements) to be disclosed separately on the statement of financial position; and
- Adoption of regulation 17A requires plant and equipment to be held using the cost model and any revaluation reserve held in relation to plant and equipment in equity should be reversed out.

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