



**Tasmanian**  
Audit Office

# Audit Committee Information Session

## Welcome

Hobart  
27 June 2016



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## **Introduction**

Rod Whitehead  
Auditor-General

# Program

TIME	TOPIC	SPEAKER
1:10 - 1:15	Welcome	Rod Whitehead
1:15 – 1:45	Update on financial reporting, areas of interest, recent findings	Ric De Santi
1:45 – 2:30	Fair Value measurements	Darryl Dorfan and Carl Harris – Deloitte
2:30 - 3:00	Afternoon Tea	
3:00 - 4:00	Cyber Security	Stan Gallo, Heather Hicks- KPMG
4:00 – 5:00	Audit Quality - Panel Discussion	Rod Whitehead, Sarah Merridew, Nick Burrows, Dan Norton
5:00	Close	Rod Whitehead





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Update on financial reporting,  
recent findings, areas of interest

**Audit Committee Information  
Session**

Hobart 27 June 2016

**Ric De Santi**

*Deputy Auditor-General*

# Financial reporting update



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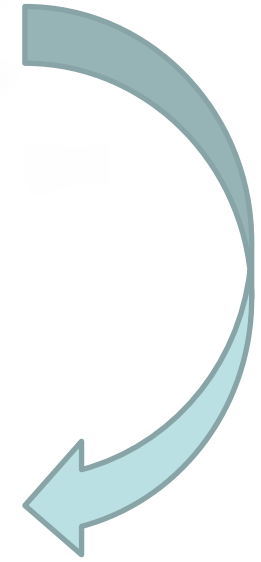
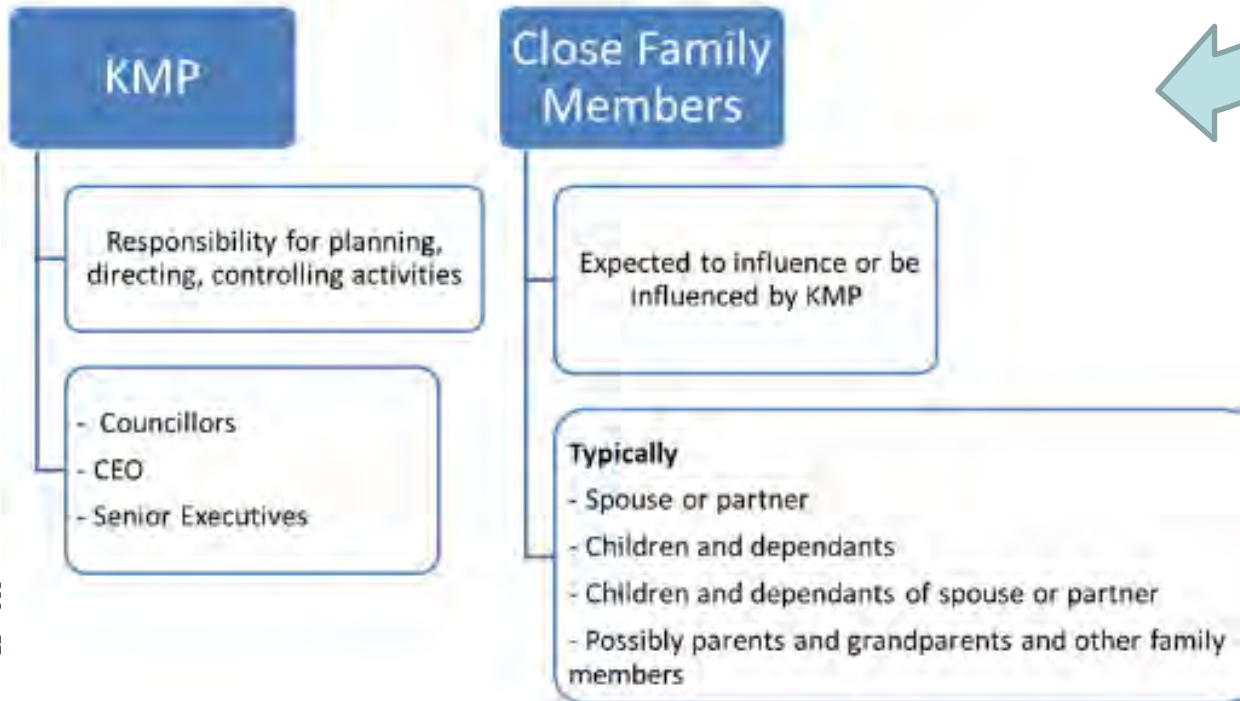
# Financial reporting update

Standard	Application date	Who is impacted	Comparatives required	Early adoption permitted
<i>AASB 124 Related Parties</i>	From 1 July 2016 (30 June 2017)	Not-for-profit public sector (could have some impact on for-profit entities)	No	Yes
<i>ED 260 Income of Not-for-Profit Entities</i>	On or after 1 January 2017 (30 June 2018)	Not-for-profit	Option	Yes (must also apply AASB 15)
<i>AASB 9 Financial Instruments</i>	On or after 1 January 2018 (30 June 2019)	All	Yes	Yes
<i>AASB 15 Revenue from Contracts with Customers</i>	On or after 1 January 2018 (30 June 2019)	All	Yes, some relief	Yes
<i>AASB 16 Leases</i>	On or after 1 January 2019 (30 June 2020)	All	Option	Yes

# AASB 124 *Related Parties*

- Main steps ....
  - Identify your related parties
  - Determine transactions that have occurred with your related parties
  - Disclose in financial statements

# Who are Related Parties



Source:  
Queensland  
Department of  
Infrastructure,  
Local Government  
and Planning



# AASB 124 - Related party transaction

“a transfer of resources, services or obligations between a reporting entity and a related party, **regardless of whether a price is charged**”

- Transactions and outstanding balances, including commitments
- KMP compensation

# AASB 124 - Disclosure

- Two main forms of disclosure:

Compensation  
Paid

Other  
Transactions

- Other transactions disclosure of:
  - Nature of relationships
  - Information about the transactions
  - Outstanding balances, including commitments.
- Items of a similar nature - disclosed in aggregate **except** when separate disclosure is necessary for an understanding of the effects of transactions on the financial statements
- Government-related entities – limited exemption from disclosure requirements

# AASB 124 - *Materiality*

- judgement required
- qualitative assessments about the nature of transactions
- appropriate criteria to be identified
- **ordinary citizen transactions** – generally not material
- transactions that have occurred at a different price or volume to that applying to the general public – likely material

# AASB 124 - Consider Points...

1. Who are the related parties?
2. Identify close family members of KMP
3. Educate and inform related parties of need to collect information
4. Identify transactions that have occurred (incl. outstanding balances)
5. Develop policy to determine the type of transactions and criteria around the disclosures:
  - 'everyday' or 'Citizen' transactions
  - close members of the family of the KMP
  - other related parties, joint ventures, subsidiaries etc.
6. Review systems and processes for capability to collect information
7. Review current disclosures i.e. Pecuniary Interest Registers, Annual Reports

# Common findings from 2015 audits

# Findings from 2015 Audits

YEAR  
**2015**

**>270 matters**

**63 entities**

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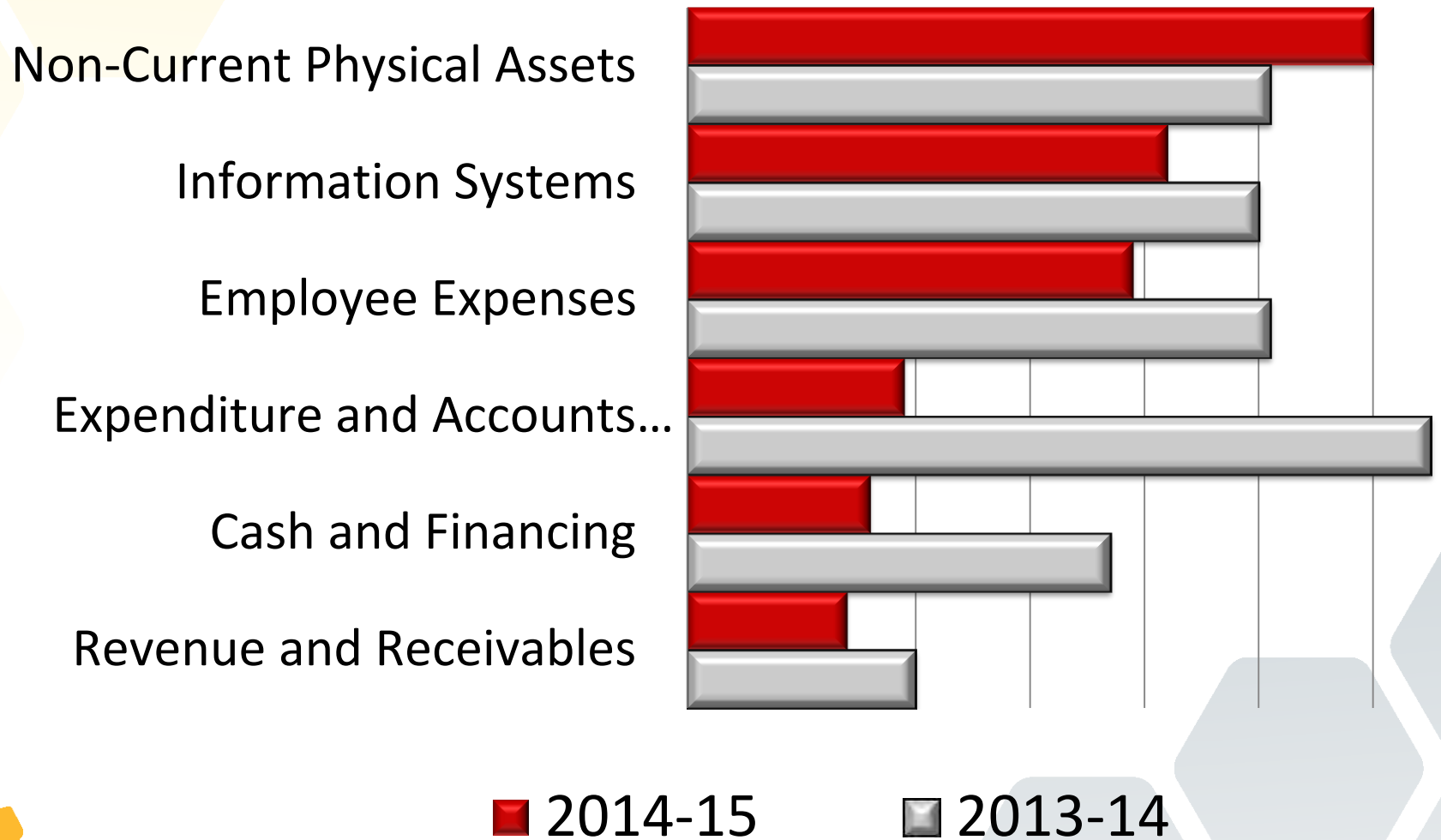
YEAR  
**2014**

**>350 matters**

**66 entities**



# Findings from 2015 Audits (continued)



# Non-current Physical Assets

- Majority of findings related to councils:
  - adoption of recommendations from our report on *Infrastructure Accounting in Local Government*
  - recognition of land under roads
  - reconciliation of asset registers to general ledger



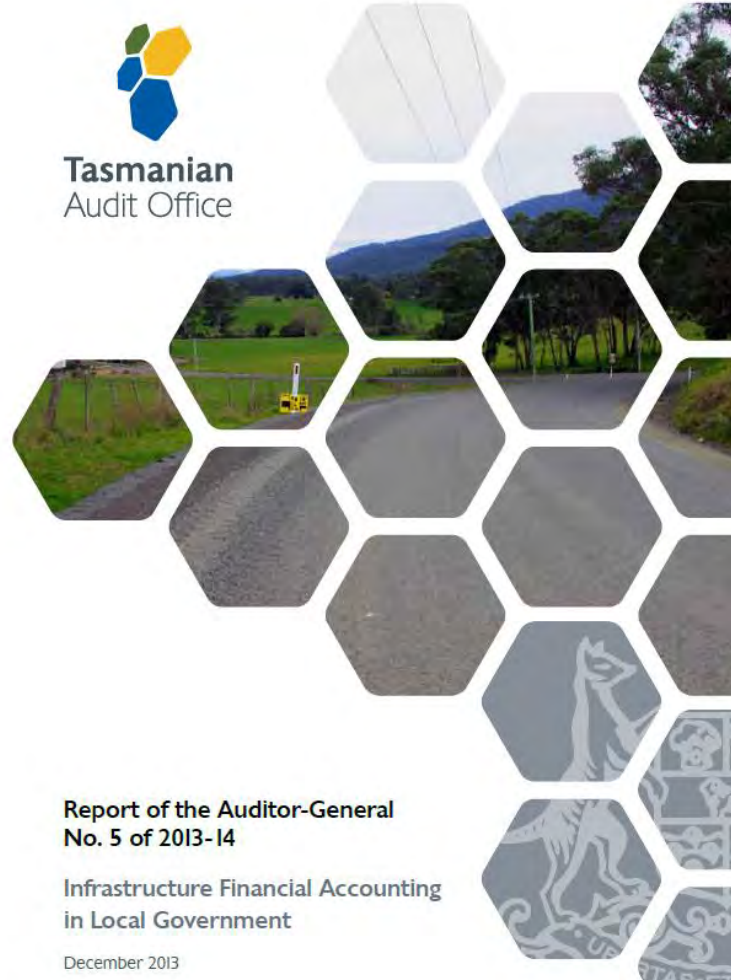
# Infrastructure Accounting

23 recommendations:

- 👉 Identification of assets
- 👉 Valuation
- 👉 Useful lives
- 👉 Depreciation
- 👉 Asset management
- 👉 Regulator compliance



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Report of the Auditor-General  
No. 5 of 2013-14

Infrastructure Financial Accounting  
in Local Government

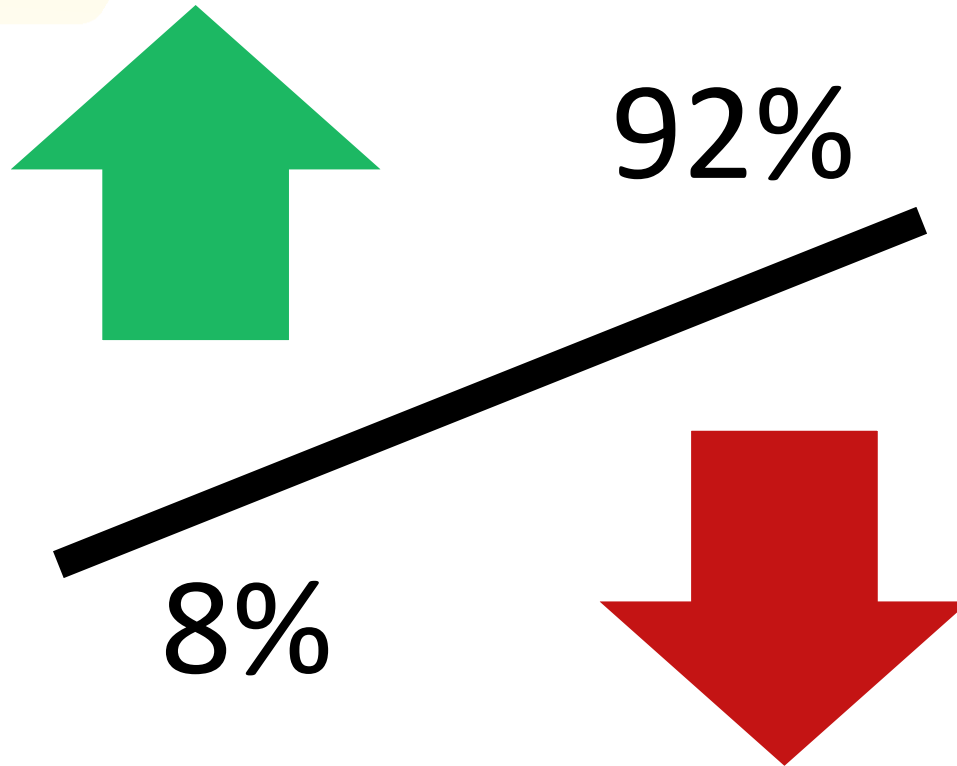
December 2013



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# Impact of the Report

*Recommendations Adopted*



# Follow-up of In-House Valuations

- Review of Road Valuations Performed by In-House Council Engineers
- Selected councils:
  - adequacy of componentisation
  - basis for values and useful lives
  - condition based valuation
  - residual values
  - earthworks
  - resheeting

# Condition Assessment



Condition used to indirectly or directly determine the value of assets

Condition is a good measure of physical wear and tear but...

... there are issues in using condition to measure value ...

# Condition Assessment (continued)

- Issues in using condition to measure value:
  - the coarseness of the condition scores (1-5, 1-6, etc.)
  - repeatability of subjective condition assessments
  - non-consideration of expected usage of the asset
  - non-consideration of technical or commercial obsolescence
  - non-consideration of legal or similar limits on use of the asset
  - non-consideration of changes in community preferences for services

# Infrastructure Report (Dec 2013)

## Recommendation 8

The condition of assets is only **one of several factors** that should be used to predict the remaining useful life of assets used for calculating depreciated replacement cost and depreciation.

Condition **should not on its own** be used to directly determine the value of depreciation or depreciated replacement cost.

# Land Under Roads

- Different valuation methods
- Preferred method:

*V-G's rates for property class category applied to land under roads, on an individual road basis, with the rate determined by the property class surrounding the road*

# Information Systems

- System security – password settings
- User access
- Business continuity and Disaster recovery planning



# Information Systems (continued)

Findings from ICT performance audit impacting financial audits:

- Physical security
- Information security
- Business Continuity/Disaster Recovery plans



# Employee Expenses

- Control weaknesses
  - inadequate segregation of payroll duties
  - employee terminations
  - timesheets not authorised
- Excessive leave balances

# Other areas of interest

# Valuation of Assets

- Statutory valuations suitable for financial reporting purposes for **non-specialised** assets, but ...
  - ... timing of valuations*
  - ... understanding of inputs and assumptions*
- Valuations of land and buildings be carried out, or overseen, by the Valuer-General

# Remuneration Disclosures

- Compulsory remuneration disclosures
  - GGS (Model Financial Statements)
  - Government businesses (*Director and Executive Remuneration Guidelines*)
- Transitional measures **no longer applicable**
  - termination payments were allowed to be disclosed in the aggregate
  - comparative information was not required

# Council Significant Business Activities (SBA)

- Business activities that involve production of goods and services
- Significant in terms of market share
- Inconsistent disclosures
- Revisit SBA assessments for 2015-16 having regard to:
  - Treasury guidelines
  - requirements of the *Local Government Act 1993*

# Authorisation of Credit Card Transactions

- Council General Managers' cards
- Often approved by the Mayor
- LGA only permits employees to authorise expenses
- We suggest GM credit card purchases are:
  - Authorised by a senior member of staff
  - Reviewed by an appropriate committee (eg audit panel) on a regular basis

# Enhanced auditor reporting





# The new standards



Financial reporting periods ending on or after 15 December 2016

## ASA 700 (revised) – Overarching Standard for Auditor Reporting



Key Audit Matter section  
ASA 701 (new)



Modifications to auditor's opinions  
ASA 705, 706 (revised)



Enhanced auditor reporting related to Going Concern  
ASA 570 (revised)



Other information section  
ASA 720 (revised)

# Auditor's Report Layout

Opinion

Basis of Opinion – *Incl. Independence Declaration*

Key Audit Matters

Other Information

Directors Responsibility for the Financial Statements

Auditor's Responsibility for the Audit of the Financial Report

Sign-off

# Key Audit Matters (KAM)

*“KAM” are those matters that, in the auditor’s professional judgment, were **of most significance** in the audit of the financial statements of the current period. Key audit matters are selected from matters communicated with those charged with governance.*



## Identify Key Audit Matters

## Describe Key Audit Matters

Matters communicated to those charged with governance

Matters that require significant auditor attention in performing the audit

Key audit matters (matters of most significance)

Description required to discuss

Why the matter was most significant

How the matter was addressed in the audit

Reference to relevant financial statement disclosures

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**Taxation**

*Refer to note A3 'Taxation'*

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The Company is subject to the National Tax Equivalent Regime and tax calculations are subject to complex legislation and rulings.

The Company has recognised a significant net deferred tax asset which represents the taxable temporary differences between the carrying amount of assets and liabilities in the financial statements and the corresponding tax bases used to calculate taxable profit.

Due to the significance of the net deferred tax asset, in the context of the financial statements as a whole and the level of judgement involved in the recognition of tax losses, the calculation and disclosure of tax related balances warrant particular audit attention.

Audit procedures included, amongst others:

- Evaluated and tested:
  - initial tax balances
  - tax effect accounting calculations
  - corresponding disclosure in the financial statements.
- Obtained a representation from the Company's tax expert.

## Defined benefits superannuation

*Refer to note '24 Employee benefits'*

The Company has employees who are members of defined benefit superannuation schemes. The Company's obligations under these schemes (less fair value of plan assets) are recognised in the statement of financial position.

The value of the superannuation liability and movements recognised in the financial statements are based on an annual valuation which is based upon a number of actuarial assumptions.

This is a key audit matter due to the size of the balance and the inherent judgement involved in determining the amount of the liability.

Audit procedures performed included:

- assessed the competence of the actuary that performed the valuation
- reviewed information provided to the actuary
- evaluated actuarial reports including the reasonableness of the assumptions used

# De-cluttering of financial statements



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# Cutting the clutter in financial reports

Financial reports must be clear, relevant and easy to understand. De-clutter your reports and gain deeper insights into the health of your business.



**Australian Government**  
**Australian Accounting Standards Board**

## Media releases

2 Feb. 2015

### AASB improves ability for companies to address disclosure overload in financial statements



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# De-cluttering of financial statements

- Removal of the irrelevant
- Only material disclosure
- Plain language
- Reordering
- Design features
- Inform the reader
- ✓ Average reduction in number of pages -> 6
- ✓ Average reduction in number of notes -> 10
- ✓ Average reduction in size of accounting policy note –  
> 30%



# Irrelevant

## (i) Financial assets

Council does not hold any financial assets

## (w) Investment property

Council does not hold any investment property.

## (x) Financial guarantees

Council has not issued any financial guarantees.

## *Finance leases as lessee*

Leases of assets where substantially all the risks and rewards incidental to ownership of the asset, are transferred to the Council are classified as finance leases. Finance leases are capitalised, recording an asset and a liability at the lower of the fair value of the asset and the present value of the minimum lease payments, including any guaranteed residual value. Lease payments are allocated between the reduction of the lease liability and the interest expense. Leased assets are depreciated on a straight line basis over their estimated useful lives to Council where it is likely that Council will obtain ownership of the asset or over the term of the lease, whichever is the shorter. Council does not currently have any finance leases.

## (v) Financial guarantees

Financial guarantee contracts are recognised as a liability at the time the guarantee is issued. The liability is initially measured at fair value, and if there is material increase in the likelihood that the guarantee may have to be exercised, at the higher of the amount determined in accordance with *AASB 137 Provisions, Contingent Liabilities and Contingent Assets* and the amount initially recognised less cumulative amortisation, where appropriate. In the determination of fair value, consideration is given to factors including the probability of default by the guaranteed party and the likely loss to Council in the event of default.

# Grouping

## Notes to the financial statements

### About this report

69–105

Our financial performance	Our asset platform	Our people	Our funding structure and management of our risks	Other information
A1 Segment information	B1 Receivables	C1 Employee provisions	D1 Capital management	E1 Our subsidiaries
A2 Revenue and other income	B2 Property, plant and equipment	C2 Senior executive and director remuneration and retirement benefits	D2 Managing our financial risk	E2 Leases
A3 Expenses	B3 Intangible assets	C3 Post employment benefits	D3 Using derivatives to hedge risk	E3 Australian Postal Corporation
A4 Taxation	B4 Impairment of non-financial assets		D4 Fair value measurement	E4 Auditors' remuneration
A5 Cash flows	B5 Investment property			E5 Contingencies
A6 Dividends	B6 Payables			E6 Other accounting policies
	B7 Other provisions			



# Reorder

## A2 REVENUE AND OTHER INCOME

### Revenue and other income for the year

The components of revenue and other income for the year ended 30 June are as follows:

Consolidated (\$m)	2015	2014
Rendering of services to:		
– Related entities <sup>1</sup>	178.0	173.5
– External entities <sup>2</sup>	5,790.6	5,747.8
	5,968.6	5,921.3
Sale of goods to external entities <sup>2</sup>	283.9	289.0
	6,252.5	6,210.3
Interest income from:		
– Cash and cash equivalents	5.3	9.1
– Loans and receivables	–	1.1
	5.3	10.2
<b>Total revenue</b>	<b>6,257.8</b>	<b>6,220.5</b>
Rents from operating leases	32.2	30.4
Income from investment property	10.3	8.3
	42.5	38.7
Net gain on disposal of land and buildings	43.3	86.0
Foreign exchange gains (net)	2.2	8.0
Change in fair value of investment property	7.4	14.1
Other services to entities	20.6	16.0
	73.5	124.1
<b>Total other income</b>	<b>116.0</b>	<b>162.8</b>
<b>Total income</b>	<b>6,373.8</b>	<b>6,383.3</b>

1 Related entities – related to the Commonwealth Government

2 External entities – not related to the Commonwealth Government

### Recognition and measurement

#### Sale of goods

Revenue from the sale of goods is recognised when the significant risks and rewards of ownership have passed to the buyer and the costs incurred or to be incurred can be measured reliably. Risks and rewards of ownership are considered passed to the buyer at the time of delivery of the goods to the customer.

#### Rendering of services

Revenue is recognised when the Group has the right to be compensated for services performed and the stage of completion can be reliably measured. It is recorded at the amount likely to be received for the provision of that service, usually set out on the invoice or contractually defined terms, excluding GST. Revenue is recognised on a commission basis where the Group acts as an agent rather than a principal in the transaction.

#### Interest revenue

Interest income is earned from the Group's financial assets that are measured at amortised cost, primarily cash within bank accounts. It is recorded using the effective interest rate, which is the rate that exactly discounts the estimated future cash payments or receipts through the expected life of the financial asset or a shorter period, where appropriate, to the net carrying amount of the financial asset.

#### Rental income

Income received from leasing Group-owned investment property to external parties under an operating lease arrangement is recorded on a straight-line basis over the lease term. Contingent rental income is recognised as income in the periods in which it is earned. Lease incentives granted are recognised as an integral part of the total rental income.

### Key Estimates: International mail revenue

The Group recognises an accrual for the amount of revenue earned from delivery of international mail where statements have not been received. Revenue is determined based on a number of factors including the volume of articles delivered, the international postal organisation for which we are delivering mail and with reference to the International Postal Union guidelines.

Source: Australia Post  
Annual Report 2014-15

## Our asset platform

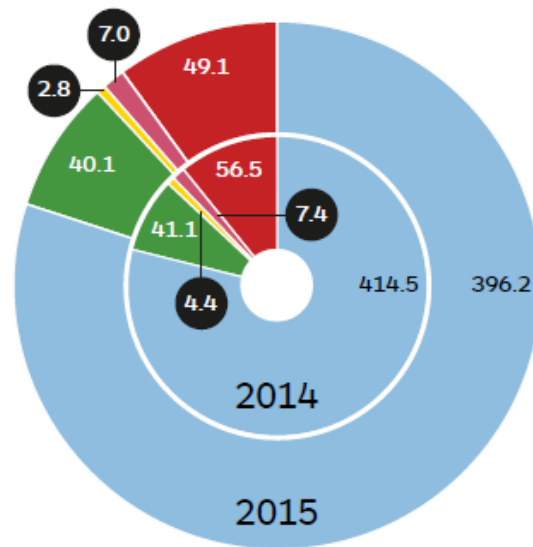
This section analyses the primary elements of our asset platform used to generate the Group's financial performance and operating liabilities incurred as a result. Employee related liabilities are discussed in note C1 and liabilities relating to financing activities are discussed in note D1. Deferred tax assets and liabilities are discussed in note A4.

### B1 RECEIVABLES

The composition of trade and other receivables at 30 June is:

Consolidated (\$m)	2015	2014
Trade receivables	486.6	507.4
Allowance for doubtful debts	(11.8)	(10.8)
	474.8	496.6
Other receivables	8.6	16.5
<b>Total current trade and other receivables</b>	<b>483.4</b>	<b>513.1</b>

Total current trade and other receivables are aged as follows (\$m):



### Recognition and measurement

Receivables for the sale of goods or performance of services (trade receivables) are recognised initially at the price on the invoice issued to the customer and subsequently at the amount considered receivable from the customer (amortised cost using the effective interest rate method) less any accumulated impairment.

These receivables are interest-free and for Australian customers, they normally have settlement terms of between 10 and 30 days, and for international customers, they are settled in accordance with Universal Postal Union (UPU) arrangements that may be longer than 30 days.

#### Analysis of ageing and recoverability

At 30 June 2015, no material receivables are individually determined to be impaired, with the total receivables determined to be impaired being \$11.8 million (2014: \$10.8 million). Overall, there have been no material movements in the allowance for doubtful debts during the year.

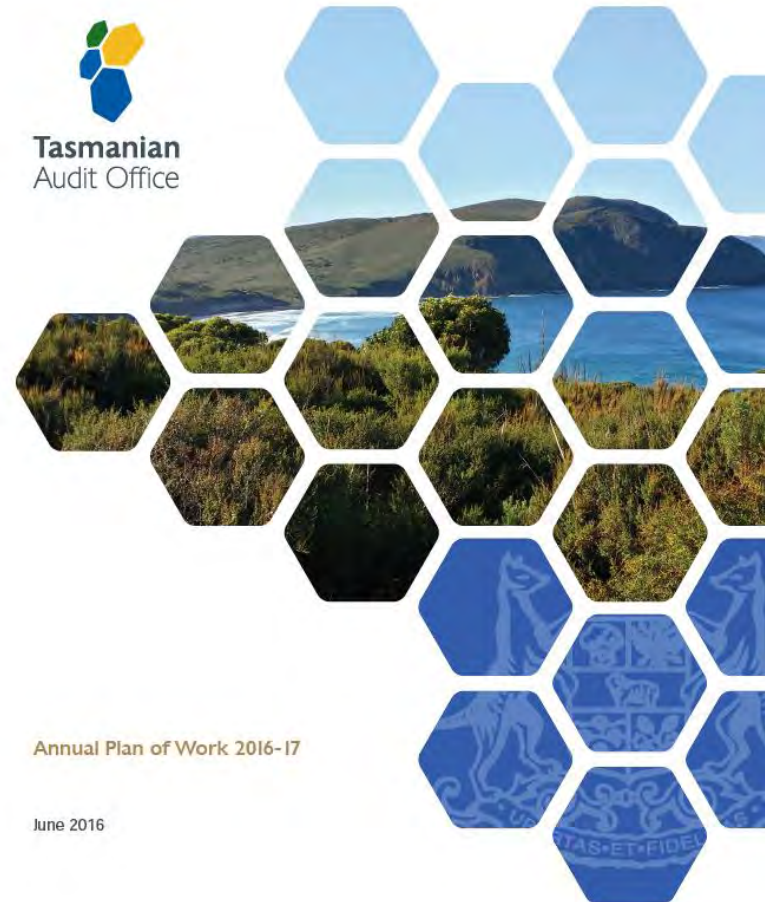
Refer to note D1 for further discussion on how the Group manages its credit risk and note A3 for the total write-down of receivables.

What  
we  
covered  
...

- Financial reporting update
  - Related Parties
  - Leases
  - Financial Instruments
- Common findings from 2015 audits
  - Assets
  - Information systems
  - Payroll
- Other matters
  - Valuation of assets
  - Remuneration and related parties disclosures
  - Significant business activities
  - Authorisation of credit card transactions
  - Enhanced auditor reporting
  - De-cluttering of financial statements

# Plan of Work 2016-17

- Financial, performance and employer audits
- Proposed projects for 2016-17 and beyond
- Available on our website before 30 June





*Thank you*

