

Our ref: W060 06P

23 November 2005

Mr Garry Poole
Chief Executive
Wellington City Council
Box 2199
WELLINGTON

Dear Garry

AUDIT ARRANGEMENTS LETTER: AUDIT OF LONG TERM COUNCIL COMMUNITY PLAN FOR THE PERIOD COMMENCING 1 JULY 2006

This letter outlines the following matters in relation to the audit of the Wellington City Council's Long Term Council Community Plan (LTCCP) Statement of Proposal (SOP) and adopted LTCCP (hereinafter referred to as the LTCCP SOP and the adopted LTCCP) including:

- σ arrangements for the audit of the LTCCP SOP and the adopted LTCCP for the period commencing 1 July 2006
- σ the areas of emphasis for the audit
- σ the terms of the engagement that apply specifically to the audit (Appendix 1) *and*
- σ our estimate of the audit fees associated with the audit (Appendix 2).

1 AUDIT SCOPE AND OBJECTIVES

The general terms of our audit engagement and our respective responsibilities are contained in our audit engagement letter of 31 March 2005 (which remains unchanged since that date), supplemented by the terms of the engagement that apply specifically to the audit of the LTCCP SOP and adopted LTCCP, which is set out in Appendix 1.

Our audit includes a review that the City Council has complied with significant legislation. The significant legislation associated with the LTCCP SOP and adopted LTCCP is contained within the Local Government Act 2002 (the Act).

2 AREAS OF AUDIT EMPHASIS

The Office of the Auditor-General (OAG) has taken the lead in developing our approach to the audit of LTCCP SOPs and adopted LTCCPs. Together with the

OAG, we have sought to be open about our approach, areas of emphasis and audit expectations. In considering the matters below we would refer you and the City Council to the OAG website (www.oag.govt.nz) and its LTCCP link for the OAG's newsletters updating the sector on our approach, as well as publishing key standard modules outlining our audit approach and process.

The focus of this work is to enable us to report within the context of Section 84(4) and Section 94(1) of the Act. Our approach will include a review of the Summary of the LTCCP SOP for its legislative compliance with sections 83(1)(a)(ii) and 89 of the Act. Subject to your approval, we can provide a separate opinion on the Summary of the LTCCP SOP if requested.

As a result of our planning to date, we have identified the following areas of audit emphasis. Additional areas may be highlighted during the course of the audit.

2.1 Project management, reporting deadlines and audit progress

The LTCCP draws together plans, policies, decisions and information from across the City Council's organisation and its community. The plan has complex and inter-related information needs. We recognise that the City Council will be undertaking its LTCCP preparation over an extended period and anticipate our audit approach will require a series of visits leading up to each reporting deadline.

Consequently we will discuss with you and your staff the City Council's approach to preparation and completion of the plan. We expect the City Council is approaching its preparation on a project basis and recognise our audit work should "shadow" that project timetable. As a result of this discussion we will agree dates for audit visits and deadlines with you and your staff.

2.2 Management control environment

Our primary approach is to identify, confirm and assess the City Council's key processes and controls over information gathering, budgeting, review of policies required by the Act and ultimate production of the LTCCP SOP and adopted LTCCP.

Our review of your self-assessment response and key controls relating to the underlying information and development of the LTCCP is critical to our initial assessment of audit risk and the nature and extent of our overall audit work.

2.2.1 Self assessment

Under separate cover, the OAG has forwarded to the City Council a "Self Assessment" form. The City Council completed the self assessment by the due date.

The purpose of the self-assessment is to assist us with gaining assurance about:

- the robustness of the processes (including compliance with statutory requirements) by which activities and decisions are brought into the LTCCP

- how the preparation and use of the LTCCP supports a framework for performance management.

The results of the self-assessment was confirmed in discussion with the City Council subsequent to its completion. There are no significant issues.

2.2.2 The review of key controls in the LTCCP development

The review will focus on the controls the City Council is using to ensure the LTCCP SOP and adopted LTCCP meet the objective of providing a long term plan in both financial and non-financial terms based on relevant policies and underlying information and assumptions which reflect the City Council's best knowledge of the future.

An early and high-level review of these key controls took place along with our review of the self-assessment. Subsequent to this, we will discuss with you our findings and the impact on the remainder of our audit work.

2.3 Audit approach

Where possible we plan to place reliance on the City Council systems and processes in approaching our audit.

The nature and extent of substantive tests to be performed will depend on our assessment of the key controls in operation. Where we decide that we can place reliance on controls or when substantive procedures alone would not provide sufficient appropriate audit evidence, we will perform tests of control to ensure that the controls are operating effectively at relevant times during the period under audit.

Where the controls over the planning systems and processes applied in the preparation of the LTCCP cannot be relied upon, the extent of our audit work is expected to increase significantly. This will add to the resource required to complete the audit and may potentially impact on overall timing.

We will also need to consider whether it is possible or practical to gain audit assurance to an acceptable level by performing solely substantive procedures. In circumstances where this is not possible, we will need to consider our reporting response.

We anticipate performing substantive tests on a selection of the City Council's Groups of Activities. The focus of this work is on disclosure including:

- activity based assumptions
- clarity of disclosure of financial information *and*
- specific disclosure requirements of the Act and, in particular, clause 2(1)(d) of Schedule 10 of the Act.

We will endeavour to keep you informed of our progress throughout the course of our audit.

2.4 Response to specific reporting requirements

In addition to our general approach of control and substantive testing, our specific reporting responsibilities require us to consider, in conducting our control and substantive testing work, the City Council's approach to:

2.4.1 Assumptions and underlying information

Good quality assumptions and underlying information are fundamental to development of relevant financial estimates and a meaningful performance management framework.

Our focus is aimed at gaining assurance that assumptions are reasonable, supportable, consistent with other assumptions, and consistently applied over the full period of the LTCCP and across all activities.

We expect Councils to consider the impact of price changes over the period of the LTCCP. The SOLGM Financial Management Working Party is actively researching this matter – including identifying sector relevant price changes. We will discuss the outcome of this work and its potential to impact on the City Council's LTCCP, once SOLGM has completed its work.

The quality of underlying information is the key base on which the financial estimates are prepared. We will consider the reasonableness of that information based on sources of information such as your asset management plans, with an expectation that the City Council will be using best estimates for the LTCCP SOP and adopted LTCCP forecasts.

2.4.2 Performance management

Our assessment of performance management focuses on the consideration by the City Council of the community outcomes as expressed through the outcomes process and the rationale for activities committed to by the City Council. Associated with the rationale for involvement in activities, is identification of service levels and a meaningful performance framework to assess the City Council's effectiveness in its achievements and in addressing its stated outcomes. The emphasis on the framework is that the resultant measures and targets are appropriate.

2.4.3 Legislative compliance and good practice

In meeting our responsibility to report on the City Council's LTCCP SOP and adopted LTCCP, we will assess the extent to which the LTCCP and the City Council's actions comply with the requirements of the Act. Our assessment of legislative compliance will occur throughout the various elements of our audit approach. We note that the Act in some instances sets specific compliance requirements. However, in many instances the City Council is to exercise judgement about how best to achieve compliance. Our approach includes understanding the

process used by the Council to facilitate the development of community outcomes. However, for the avoidance of doubt, we will not be “auditing” the outcomes.

Our approach will be to apply as appropriate:

- the requirements of the Act and (through the Act) of sustainable development principles
- the requirements of Generally Accepted Accounting Practice (GAAP)
- existing sector good practice (eg, NAMS asset management guidelines) *and*
- identified sector good practice emerging out of audit enquiries.

As part of compliance with the Act, our focus will also include:

- Section 100 – Balanced Budget

As part of the financial prudence regime outlined in the Act, section 100 requires the City Council’s budget to “balance” by setting operating revenue at a level sufficient to cover operating expenses. Our review of this statutory test encompasses a number of factors:

- That the test is met in each of the individual years of the LTCCP SOP and adopted LTCCP.
- That the result is financially prudent; being consistent with City Council’s financial management policies at both the operating level and in terms of its financial position.
- That the criteria of section 100(2) are met where a budget is “unbalanced”.

However, our primary focus will be to ensure that the City Council has a well developed rationale for the position that it has adopted in relation to its forecast operating surpluses/deficits across the period of the LTCCP SOP and adopted LTCCP.

We urge the City Council to consider this test as it develops the LTCCP. It can only be finally assessed at the conclusion of drawing together both the LTCCP SOP and adopted LTCCP when there are also statutory time constraints to be met. We encourage early discussion with us in relation to the City Council’s approach to the balanced budget requirements of the Act.

- Generally Accepted Accounting Practice and International Financial Reporting Standards

Section 111 of the Act requires the LTCCP to be prepared on a basis consistent with GAAP. Our review will encompass and specifically report on compliance with GAAP in the presentation of financial information.

We note the development in financial reporting standards which move New Zealand standards to align with International Financial Reporting Standards (IFRS). The sector recognises that under the options available to it, a local authority should elect to adopt IFRS (and its New Zealand equivalent – NZ IFRS) in the year ending 30 June 2007. The effect is the LTCCP will be prepared on a consistent basis throughout each of the 10 years within the plan.

The costs of the City Council’s conversion to NZ IFRS will be a separate engagement and are not part of our LTCCP audit work. Separately to this audit, we will discuss with your staff, their programme to adopt NZ IFRS and we will build this into our work programme.

- Summary of the Statement of Proposal

Our focus is on legislative compliance, which includes the provision of section 89 of the Act. This requires the Summary to fairly represent the “major matters” and to be suitable as “a basis for general consultation”.

We also note the good practice advice that the SOLGM Financial Management Working Party has recently promulgated.

- Adopted LTCCP

Consistent with section 94 of the Act, we are required to also report on the adopted LTCCP subsequent to your consultation on the LTCCP SOP. Our focus will be to assess the City Council’s consultation process on the LTCCP SOP. The extent of our work will be dependent on:

- the audit conclusions reached on the LTCCP SOP *and*
- the impact of consultation on the adopted LTCCP.

3 OTHER MATTERS

3.1 Publication of the LTCCP Statement of Proposal and Adopted LTCCP on the City Council’s web site

If you intend to publish the LTCCP SOP and/or adopted LTCCP electronically, the Office of the Auditor-General requires us to examine the final electronic file version of the audit report prior to its inclusion, and as soon as possible after its inclusion on

your web site to ensure consistency with the paper-based documents that have been subject to audit. Potential changes to parts of the audit opinion, for example for page number references, and the inclusion of additional information to readers of the electronic report will be required.

To ensure that we meet these obligations we would appreciate you advising us as soon as possible if you intend your financial statements to be published electronically.

4 AUDIT LOGISTICS

We have an electronic audit management system. This means that our auditors will complete the majority of their work on their laptops.

We would therefore appreciate it if the following could be made available during our audit:

- σ access to an analogue telephone line
- σ a suitable workspace for computer use *and*
- σ electronic copies of key documents where possible.

As noted in section 2.1, our audit work needs to be undertaken as the development of your LTCCP occurs to ensure the timely completion of our audit opinion. Hence we wish to discuss actual timing as specified in your project plan and agree timings for proposed audit visits and delivery.

To ensure we meet agreed deadlines, it is essential that the dates agreed are adhered to.

5 PROFESSIONAL FEES

Our audit fee, covering both the LTCCP SOP and the adopted LTCCP for the period commencing 1 July 2006, is \$79,400 (GST exclusive), including disbursements, as outlined in Attachment 2.

The fee assumes:

- σ the provision of information in a timely manner
- σ the appropriate level of assistance from your staff
- σ no significant change in the structure or level of operations of the City Council to the extent it impacts on the City Council
- σ we are able to place reliance on the key controls used in the development of the LTCCP (as set out in 2.2)

- σ that, as permitted by clause 8(2) of Schedule 10 of the Act, the Council is preparing LTCCP forecast financial statements for the 'Council parent' only rather than including consolidated forecast financial statements for the Council and any controlled entities.

If information is not available for the visits as agreed, we will seek to recover any additional costs incurred as a result. We will endeavour to inform you as soon as possible should such a situation arise.

This fee is exclusive of:

- σ the City Council's conversion to NZ-IFRS (as noted in section 2.4.4 under Generally Accepted Accounting Practice and International Financial Reporting Standards)
- σ any subsequent amendments, under section 84(2), the City Council may make to the adopted LTCCP
- σ the issuing of an audit opinion on the City Council's summary of the LTCCP SOP
- σ any additional audit work required where the controls over the planning systems and processes applied in the preparation of the LTCCP cannot be relied upon (as noted in section 2.3).

We wish to interim bill in equal instalments as work progresses. We propose the following billing arrangements:

	\$ (GST excl)
December 2005	10,000
January 2006	30,000
February 2006	20,000
March 2006	5,000
April 2006	5,000
May 2006	5,000
June 2006	4,400
	<u>\$79,400</u>

6 PERSONNEL

Our personnel involved in the management of the audit are:

Rudie Tomlinson	Director
Bede Kearney	Review Director
Karen Young	Manager
David Kidman	Audit Supervisor

We have endeavoured to maintain staff continuity as far as possible.

7 AUDIT TIMING

Audit Timetable key dates are as follows:

Planning controls assessment	August 2005
First interim visit	December 2005
Second interim visit	January 2006
Third interim visit	February 2006
Proposed LTCCP SOP available	24 February 2006
Summary available	20 March 2006
Audit Opinion on LTCCP SOP required	4 April 2006
Proposed LTCCP for adoption available	20 June 2006
Audit Opinion on adopted LTCCP required	28 June 2006

Should we encounter any significant problems or delays during the audit, we will inform you immediately.

8 AGREEMENT

Please sign and return the attached copy of this letter to indicate that:

- σ it is in accordance with your understanding of the arrangements for this audit of the LTCCP for the period commencing 1 July 2006 *and*
- σ you acknowledge the terms of the engagement (as set out on Appendix 1 to this letter) that apply specifically to the audit of the LTCCP SOP and adopted LTCCP and which supplements the existing audit engagement letter dated 31 March 2005.

If there are any matters requiring further clarification please do not hesitate to contact me.

Yours sincerely

Rudie Tomlinson
Director

cc Neil Cherry, Chief Financial Officer
John Scott, Director Risk and Assurance

I acknowledge that this letter is in accordance with my understanding of the arrangements of the audit engagement. I also acknowledge the terms of the engagement that apply specifically to the audit of the LTCCP, and which supplements the existing audit engagement letter dated 31 March 2005.

Signed: _____

Garry Poole
Chief Executive

Date: _____

Signed: _____

Kerry Prendergast
Mayor

Date: _____

APPENDIX 1

TERMS OF THE ENGAGEMENT THAT APPLY SPECIFICALLY TO THE AUDIT OF THE LTCCP

Background

This supplement to the existing engagement letter dated 31 March 2005 is issued on behalf of the Auditor-General. The Auditor-General is the statutory auditor of Wellington City Council. The Auditor-General has appointed me, Rudie Tomlinson, using the staff and resources of Audit New Zealand, to carry out the audit of the Long term Council Community Plan Statement of Proposal and adopted Long Term Council Community Plan (hereinafter referred as the LTCCP SOP and the adopted LTCCP) for the period commencing 1 July 2006.

The purpose of this supplement to the existing engagement letter is to outline the terms of the engagement that apply specifically to the audit of the Wellington City Council's LTCCP SOP and adopted LTCCP for the period commencing 1 July 2006. This supplement should be read in conjunction with the existing audit engagement letter dated 31 March 2005, which remains unchanged since that date.

Objectives

The objectives of the audit of the LTCCP SOP and adopted LTCCP are:

- σ to provide independent opinions on the LTCCP SOP (under s 84(4) of the Act) and on the adopted LTCCP (under s 94(1) of the Act) about the activities of the City Council in respect of:
 - the extent to which the LTCCP SOP and adopted LTCCP comply with the requirements of the Act
 - the quality of the information and assumptions underlying the forecast information provided in the LTCCP SOP and adopted LTCCP
 - the extent to which the forecast information and proposed performance measures will provide an appropriate framework for the meaningful assessment of the actual levels of service provision *and*
- σ to report on matters relevant to the City Council's planning systems, which come to our attention and are relevant to the City Council.

Our audit involves performing procedures that examine, on a test basis, evidence supporting assumptions, amounts and other disclosures in the LTCCP SOP and adopted LTCCP, determining compliance with the requirements of the Act, and evaluating the overall adequacy of the presentation of information.

We also review other accompanying information associated with the LTCCP SOP and adopted LTCCP to identify whether there are material inconsistencies with the audited LTCCP SOP and adopted LTCCP. In particular, we will need to review the Summary of the

LTCCP SOP for its representation of the *major matters* in the LTCCP SOP to enable general consultation with the community.

Reports arising from the audit of the LTCCP

Consistent with the objectives above, the reports arising from the audit of the LTCCP SOP and adopted LTCCP are:

- σ the audit report attached to the LTCCP SOP
- σ the audit report attached to the adopted LTCCP *and*
- σ a management report provided to the City Council.

The auditor's report on the LTCCP

We will be providing an overall report on whether the LTCCP SOP and adopted LTCCP provide a reasonable basis for long term integrated decision-making by the City Council and for participation in decision making by the public and subsequent accountability to the community. Each of the main audit reports arising from the audit of the LTCCP SOP and adopted LTCCP then provide an independent opinion to readers on specific matters required by sections 84(4) and 94(1) of the Act. These specific matters are:

- σ The extent of compliance with the requirements of the Act in respect of the plan, for a Council of City Council's size and scale within the context of its environment.
- σ The quality of the information used by the City Council to prepare the forecast information.
- σ The quality of the assumptions underlying the City Council's forecast information.
- σ The compliance of the LTCCP SOP and adopted LTCCP with Generally Accepted Accounting Practice in New Zealand.
- σ The extent to which the forecast information and proposed performance measures provide an appropriate framework for the meaningful assessment of actual levels of service provision reflects good practice for a Council of City Council's size and scale within the context of its environment.

The audit opinion does not:

- σ provide a guarantee of absolute accuracy in the LTCCP SOP and adopted LTCCP
- σ express an opinion on the merits of any policy content within the LTCCP SOP and adopted LTCCP
- σ include an opinion as to whether the forecasts will be achieved.

Provision of a management report to the City Council

Consistent with our objectives, we will report to the City Council on the conclusion of the engagement. The report communicates matters which come to our attention during the engagement and, which, in our opinion, are relevant to the City Council. For example we will report:

- σ any legislative breaches noted
- σ any weaknesses in the City Council's systems that come to our notice and we consider of relevance to the City Council *and*
- σ uncorrected misstatements noted during the audit.

Materiality

Consistent with the annual attest audit, the audit engagement for the LTCCP SOP and adopted LTCCP adheres to the principles and concepts of materiality across the 10-year period of the LTCCP.

Consequently, if we find material misstatements that are not corrected, we will refer to them in the audit opinion. Our preference is for any material misstatement to be corrected, avoiding the need to refer to misstatements in our opinion.

The auditing standards applied when conducting the audit of the LTCCP Statement of Proposal and Adopted LTCCP

We will ensure that the audit is carried out in accordance with the International Standard on Assurance Engagements 3000 (revised): Assurance Engagements Other Than Audits or Reviews of Historical Financial Information and the Auditor-General's Auditing Standards, which incorporate the New Zealand Auditing Standards. The financial forecast information is examined in accordance with the International Standard on Assurance Engagements 3400: The Examination of Prospective Financial Information.

Responsibilities

General responsibilities

The general responsibilities of the City Council with regards to the preparation and completion of the LTCCP SOP and adopted LTCCP are consistent with those existing for the annual report as set out in the audit engagement letter dated 31 March 2005 – with appropriate allowance for recognising that the LTCCP deals with forecast information.

Specific responsibilities

The City Council is responsible for preparing the LTCCP SOP and adopted LTCCP under the Act, by applying the City Council's assumptions and in accordance with generally accepted accounting practice in New Zealand. The City Council's responsibilities arise from section 93 of the Act. We assume that members of the City Council are familiar with those responsibilities and, where necessary, have obtained advice about them.

For clarity, we do note the following statutory responsibilities as set out in the Act:

- σ Section 93 of the Act requires Council to have a LTCCP, at all times. Part 1 of Schedule 10 governs the content of the LTCCP. S 111 aligns the financial information with *generally accepted accounting practice*.
- σ Section 84 sets out the special consultative procedures required to be followed by Council to adopt the LTCCP.
- σ Section 84(1) aligns the consultation for the adoption of the LTCCP with the special consultative procedure set out in section 83, which includes a requirement to produce a LTCCP SOP as well as a summary (consistent with section 89).
- σ Section 84(4) requires an auditor's report on the LTCCP SOP and section 94 requires a separate opinion on the adopted LTCCP.

Statutory reporting deadlines

We note that the *adoption deadline for the LTCCP is 30 June 2006*. It is imperative that we work together on a basis consistent with your project plan for the development of the LTCCP to ensure completion of all statutory requirements within the timeframes set by the City Council, consistent with this statutory deadline.

We envisage that the audit work for the LTCCP SOP and adopted LTCCP will be conducted as these are developed, rather than once the LTCCP SOP and adopted LTCCP are completed. While there is some audit work which can only be conducted on the conclusion of these reports, the majority of fieldwork will need to be completed as the LTCCP SOP and adopted LTCCP are developed.

APPENDIX 2**TEAM MIX AND HOURS FOR THE AUDIT OF THE LTCCP FOR THE 10-YEAR PERIOD COMMENCING ON 1 JULY 2006**

	Total hours
Director	66
Sector Specialists	24
Audit Manager	155
Other CA staff	241
Other Expert or Specialist Assistance	24
Totals	510

FEE CALCULATIONS

2006	\$
Net fee	79,060
OAG overhead contribution ¹	NIL
Estimated disbursements*	340
Total fee (including disbursements and overhead contribution)	79,400
GST	9,883
Audit fee for the LTCCP for the period commencing 1 July 2006	88,943

* Our estimate of disbursements, including travel, is \$340. Should actual and reasonable costs exceed that estimate for reasons beyond our control, we will, subject to the Auditor-General's approval, seek to recover those additional costs.

¹ No OAG overhead is charged in relation to the audit of the LTCCP