

14 November 2017

Hon Phil Goff  
Mayor of Auckland  
Auckland Council  
Private Bag 92300  
Victoria Street West  
Auckland 1142

Dear Hon Phil Goff

## **Audit Engagement Letter: Audit of the consultation document and Long-Term Plan for the period commencing 1 July 2018**

This letter outlines the following matters in relation to the audit of Auckland Council Group's consultation document and Long Term Plan:

- the terms of the audit engagement and the respective responsibilities of the governing body (the Council) and me;
- the audit scope and objectives;
- the approach taken to complete the audit;
- the areas of audit emphasis;
- the audit logistics; and
- the professional fees.

### **1 Specific responsibilities of the Auckland Council Group for preparing the consultation document and the Long-Term Plan**

Our audit will be carried out on the basis that the Auckland Council Group acknowledges that it has responsibility for preparing the consultation document (CD) and Long Term Plan (LTP), by applying its own assumptions, in accordance with the Local Government Act 2002 (the Act) (in particular, the requirements of Part 6 and Schedule 10), and in accordance with generally accepted accounting practice in New Zealand. We assume that elected members are familiar with those responsibilities and, where necessary, have obtained advice about them.

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

- Section 93 of the Act requires the Council to have an LTP at all times, and Part 1 of Schedule 10 governs the content of the LTP.
- Section 111 aligns the financial information with generally accepted accounting practice.

- Section 83 (with reference to section 93A) sets out the special consultative procedures that the Council is required to follow to adopt the CD and LTP.
- Section 93C(4) requires an auditor's report on the CD and section 94 requires a separate report on the LTP.

Please note that the audit does not relieve the Council of any of its responsibilities.

Other general terms are set out in the relevant sections of this letter and Appendix 1.

## **2 Our audit scope**

The Act requires us to provide two separate audit reports as follows:

- On the CD, a report on:
  - whether the CD gives effect to the purpose specified in section 93B; and
  - the quality of the information and assumptions underlying the information in the CD.
- On the LTP, a report on:
  - whether the LTP gives effect to the purpose in section 93(6); and
  - the quality of the information and assumptions underlying the forecast information provided in the LTP.

We expect our work to assess the quality of underlying information and assumptions to be a single, continuous process during the entire LTP preparation period, which includes the preparation of the CD.

Our focus for the first limb of each audit opinion will be to assess whether each document meets its statutory purpose. Given the different purposes of each document, we will assess the answers to different questions for each opinion.

Our focus for the second limb of each audit opinion will be to obtain evidence about the quality of the information and assumptions underlying the information contained in the CD and LTP. How we obtain this information depends on our judgement, including our assessment of the risks of material misstatement of the information and assumptions underlying the information contained in the CD and LTP, whether because of fraud or error.

Our audit opinions do not:

- provide a guarantee of absolute accuracy of the information in the relevant document;
- provide a guarantee that the Auckland Council Group has complied with all relevant legal obligations;
- express an opinion on the merits of any policy content; or

- include an opinion on whether the forecasts will be achieved.

### **3 Our approach to this audit**

#### **3.1 The content of the CD**

The Act emphasises the discretion of the Council to decide what is appropriate to include in the CD and the associated consultation process. In deciding what to include in the CD, the Council must have regard to its significance and engagement policy, and the importance of other matters to the region and its communities.

We will need to understand how the Council has approached the task of applying its significance and engagement policy, and how it has considered the importance of other matters in deciding what to include in the CD. This will help inform our assessment of whether the CD achieves its statutory purpose.

#### **3.2 Adopting and auditing the underlying information**

Before adopting the CD, section 93G of the Act requires the Council to prepare and adopt the information that:

- is relied on by the content of the CD;
- is necessary to enable the Auditor-General to issue an audit report under section 93C(4); and
- provides the basis for the preparation of the LTP.

The information to be prepared and adopted needs to be enough to enable the Auckland Council Group to prepare the CD.

We consider that local authorities will need to have thought comprehensively about how best to meet the requirements of the Act. Consistent with the guidance of the Society of Local Government Managers' (SOLGM), our view is that core building blocks of an LTP will be needed to support an effective CD. This will include, but not be limited to, draft financial and infrastructure strategies and the information that underlies them, including asset management information, assumptions, defined levels of service, funding and financial policies, and a complete set of financial forecasts.

We will work with management to understand the information proposed to be adopted and assess whether it will enable us to issue an audit report under section 93C(4).

In addition, the time frames to consider and adopt the LTP after the consultation process will be tight. From a practical perspective, it will be important that the Auckland Council Group is well advanced with the preparation of the full LTP when it issues the CD. Otherwise you may find it difficult to complete the work and adopt the full LTP before the statutory deadline. The same is true for the audit work. The more audit work that is able to be completed at the first stage of the process, the less pressure there will be on you and the audit team at the end of the process.

### **3.3 Control environment**

The Auckland Council Group is responsible for establishing and maintaining accounting and internal control systems (appropriate to the size of the Auckland Council Group), supported by written policies and procedures, designed to prepare the CD and LTP, and to provide reasonable quality information and assumptions underlying the information contained in these documents.

Our approach to the audit will be to identify, confirm and assess the Auckland Council Group's key processes and controls over the underlying information and the production of both the CD and the LTP. The purpose of this assessment is to enable us to plan the most effective and efficient approach to the audit work needed to provide our two audit opinions. Our assessment is not for the purpose of expressing an opinion on the effectiveness of the Auckland Council Group's internal controls.

We will carry out a review of the control environment to help us understand the approach taken to develop the CD and LTP, develop expectations of what should be included in the CD and LTP, and identify areas of potential audit risk. This will involve discussions with elected representatives and selected staff throughout the Auckland Council Group, review of publicly available information about the Auckland Council Group, updating our knowledge of the Auckland Council Group issues developed during recent years, and a review of Auckland Council Group minutes since the last audit review.

Our review of your self-assessment response (see below), and key controls relating to the underlying information and development of the LTP is useful for our initial assessment of audit risk which affects the nature and extent of our overall audit work.

### **3.4 Self-assessment**

To assist our audit planning we intend to request that you use a self-assessment process to assist with our risk assessment process. The self-assessment requires you to reflect on your most significant issues and risks, governance of the overall LTP project, and the systems and processes you have in place (particularly to meet the purposes in the Act for the CD and the LTP), asset management, performance management and reporting, and financial management.

We forwarded the self-assessment to you under a separate cover.

The self-assessment is similar to those used with our audit of previous LTPs. The information provided through the self-assessment will be confirmed with you through discussion after you have completed it and we have had an opportunity to analyse your responses.

## **4 Our particular areas of audit emphasis**

### **4.1 Project delivery**

The three-yearly task of preparing the Auckland Council Group's CD and LTP requires significant effort from the Mayor, elected members, and management and staff from across the group. In addition, the group approach to the CD and LTP also requires timely integration of Council and CCO planning activities, including financial forecasting and infrastructure planning.

The scale and complexity of the group's operations and planning activities increases the risk that the Council's project team will not be able to produce an LTP within legislative deadlines.

We expect the Council and its CCOs to actively engage with us as the project plan is developed and carried out. We also expect the Council to set realistic time frames for the delivery of key project milestones, and to actively monitor and manage work streams to meet these. If issues arise, or delivery problems are encountered, it is crucial that you talk to us early.

We expect the Council to ensure that formal planning inputs and outputs align across the group. As with the last LTP round, we expect this will involve:

- the implementation of formal controls to ensure the alignment of key underlying assumptions across the group;
- reconciliation of formally approved CCO plans and accountability documents with the final LTP forecasts; and
- formal sign off of budget inputs by CCO boards and management.

We also expect the Council to integrate appropriate project governance into the project plan, such as oversight by the Audit and Risk Committee and the Council, independent quality assurance processes, and legal sign off of key documents and process. The role of elected members in the project should be clearly agreed with them upfront and monitored along the way to ensure that their key responsibilities for governance and adoption are well understood and properly supported.

As in previous LTP audit rounds, Audit New Zealand, while completing the audit on my behalf, and my local government team are committed to helping the Council meet its obligations and statutory deadlines.

Within this audit engagement letter, we have included agreed timings for the delivery of key milestones. In order for us to meet Council's expectations it is important that the Council keep to these agreed timeframes and milestones.

Where relevant we will require evidence of formal CCO Board approval of budget inputs, asset management information and strategies, levels of service and the key assumptions that inform the CD and the LTP. We also need the inputs to reconcile to the Council and CCO's accountability agreements, including the draft Statements of Intent.

We will also review for evidence of appropriate Council governance processes over the entire LTP project including consultation processes.

## **4.2 Integration with Central Government**

Government policy and agreements with the Auckland Council Group are a significant determinant of the group's financial and infrastructure strategies. Due to the scale of the issues facing the region and the rapidly changing political landscape, it is highly unlikely that all issues will be resolved for CD or LTP purposes.

For the Council to include new funding sources from the Government in the CD or LTP budgets we would expect to see some form of formal signed agreement. However,

without this we expect that the Council will still be able to include a broad plan in the CD and LTP that outlines the status of the engagement with the government and the impact and options that could become available if such engagement results in a formal agreement that supports other sources of funding. This would enable readers to understand the existing parameters and limitations to the consultation process and resulting LTP.

We will review the Council's CD and LTP, including key assumptions and other underlying information supporting these documents, to ensure that these fairly reflect the most up-to-date outcomes of government policy decisions and agreements with the Council at the time of adoption.

### **4.3 Mayor's proposal**

The Mayor's proposal does not fall within our LTP audit engagement. However, it remains a key milestone in the LTP project as it sets the context for consultation and decision making and is expected to significantly inform the CD and LTP. We therefore expect that the information and assumptions supporting the Mayor's proposal are broadly consistent with those supporting the CD and LTP. As the project progresses there will be refinement of assumptions and underlying information along the way. However, given the timelines it is our expectation that the Mayor's proposal and LTP projects are joined up for this purpose.

### **4.4 Financial strategy and infrastructure strategy**

The Act requires a local authority to prepare two key strategies as part of the LTP: the financial strategy and the infrastructure strategy. The purpose of the financial strategy is to:

- facilitate prudent financial management by the local authority by providing a guide for the local authority to consider proposals for funding and expenditure against; and
- provide a context for consultation on the local authority's proposals for funding and expenditure by making transparent the overall effects of those proposals on the local authority's services, rates, debt, and investments

It is also critical that the Financial Strategy sets out a credible path that will keep the Council within its agreed financial parameters.

The purpose of the infrastructure strategy is to:

- identify significant infrastructure issues for the local authority during the period covered by the strategy; and
- identify the principal options for managing those issues and the implications of those options.

The Act expects close alignment between the two strategies and section 101B(5) allows for them to be combined into a single document.

Although the Act clearly sets the minimum requirements for these strategies, it does not define the only things that can be in a strategy. A good strategy should include what is needed to be a good quality strategic planning document. In the case of the

infrastructure strategy the principles of ISO55000 should be considered, particularly where the Auckland Council Group is seeking to prepare a best practice strategy.

Our focus when reviewing both strategies is to assess whether the Auckland Council Group has met the purpose outlined in the Act and presented the strategies in a coherent and easily readable manner. Specifically, we will:

- confirm that the two strategies are appropriately aligned; and
- understand the impact of the financial forecasts included in the infrastructure strategy on the prudence of the financial strategy; and
- assess the reasonableness of the prepared forecasts by:
  - understanding how the Auckland Council Group has applied the effect of its assumptions (for example, allowing for changing demographics) and levels of service on expenditure decisions, and outlined the implications of these decisions in the strategies;
  - reviewing the Auckland Council Group's relationship between its renewal capital expenditure and depreciation expenditure forecasts;
  - checking that the infrastructure strategy is appropriately inflated; and
  - checking that the Infrastructure Strategy is clearly aligned with the key information that underpins the CD and LTP (for example, forecast maintenance and renewals costs based on best information).

The Auckland Council Group's financial modelling is a significant component of the underlying information that supports both the financial strategy and infrastructure strategy. We will place particular emphasis on the integrity and effectiveness of the financial modelling of all local authorities.

An additional role played by these strategies is to facilitate accountability to the community. It is critical that these strategies are presented in such a way that they are engaging and informative, and support the presentation of issues, options and implications presented in the CD.

#### **4.5 Assumptions**

The quality of the Auckland Council Group financial forecasts is significantly affected by whether the assumptions on which they are based are defined, reasonable, and supportable. The Act recognises this by requiring all local authorities to clearly outline all significant forecasting assumptions and risks underlying the financial estimates in the LTP (Schedule 10, clause 17). *Prospective Financial Statements* (PBE FRS 42) also requires the disclosure of significant assumptions.

We will review the Auckland Council Group's list of significant forecasting assumptions and confirm that they are materially complete. We will also test the application of selected assumptions in the financial forecasts to check they have been reasonably applied and are supportable. Finally, we will confirm that:

- all significant forecasting assumptions disclose the level of uncertainty associated with the assumption; and
- for all significant forecasting assumptions that involve a high level of uncertainty, the uncertainty and an estimate of the potential effects of the uncertainty on the financial forecasts are appropriately disclosed in the LTP.

We consider that the significant forecasting assumptions are crucial to the underlying information for the CD and will complete our review during our audit of the CD.

## **4.6 Quality of asset-related forecasting information**

A significant portion of the Auckland Council Group's operations relates to the management of its infrastructure: the roading network, public transport network and the "three-waters" of water supply, wastewater, and stormwater drainage. These activities typically make up a significant part of Auckland Council Group's operational and capital expenditure.

To prepare reasonable quality asset information, the Auckland Council Group needs to have a comprehensive understanding of its critical assets and the cost of adequately maintaining and renewing them. An important consideration is how well the Auckland Council Group understands the condition of its assets and how the assets are performing.

In reviewing the reasonableness of the Auckland Council Group's asset-related forecasting information, we will:

- assess the Auckland Council Group's asset management planning systems and processes;
- understand what changes the Auckland Council Group proposes to its forecast levels of service;
- understand the Auckland Council Group's assessment of the reliability of the asset-related information;
- consider how accurate recently prepared budgets have been; and
- assess how matters such as affordability have been incorporated into the asset-related forecasts prepared.

Depending on what we identify in completing the above, we may have to complete further detailed testing on the Auckland Council Group's asset-related information.

## **5 Other matters**

### **5.1 Our independence**

It is essential that the audit team, including both the staff involved from my Office and those from Audit New Zealand, remain both economically and attitudinally independent of the Auckland Council Group (including being independent of management personnel and the Auckland Council Group). This involves being, and

appearing to be, free of any interest that might be regarded, whatever its actual effect, as being incompatible with integrity, objectivity and independence.

## **5.2 Publication of the CD and adopted LTP on the Council's website**

The Council is responsible for the electronic presentation of the CD and LTP on its website. This includes ensuring that there are enough security and controls over information on the website to maintain the integrity of the presented data. Please ensure that your project plan allows time for us to examine the final electronic file version of the respective documents, including our audit report, before their inclusion on the website.

We need to do this to ensure consistency with the paper-based documents that have been subject to audit.

## **6 Audit logistics**

### **6.1 Audit timing**

The key dates in the audit timetable are as follows:

Self-assessment provided to the Council	25 September 2017
Self-assessment returned to audit team for consideration	3 November 2017
Interim visit (including controls assessment and supporting information review).	From 13 November 2017 through to 22 December 2017*
Proposed CD available for audit	6 December 2017
Final CD visit (including completion of supporting information review)	8 January 2018 - February 2018*
Audit opinion on CD required	7 February 2018
Draft management report on CD engagement issued	7 February 2018
Final visit (including review of draft and final LTP)	May-June 2018
Proposed LTP for adoption available for audit	To be confirmed
Audit opinion on adopted LTP required	27 June 2018
Draft management report on LTP engagement issued	27 June 2018

\* These dates may need to move forward or backwards in response to unexpected delays in deliverables.

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

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

Therefore, we would appreciate it if the following could be made available during our audit:

- A suitable workspace for computer use (in keeping with the health and safety requirements discussed in **Appendix 1**).
- Electronic copies of key documents.

As noted in section 3.4, our audit work needs to be done as you develop your underlying information and prepare your CD and LTP, to ensure the timely completion of our audit.

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

## **7 Professional fees**

Our audit fee, covering both the CD and the LTP for the period commencing 1 July 2018, is \$685,000 (excluding GST and disbursements) as outlined in Appendix 2.

The proposed fee is based on the following assumptions:

- Information required to conduct the audit is complete and provided in accordance with the agreed timelines, including the draft CD and the full draft financial strategy and draft infrastructure strategy that supports it.
- There will be an appropriate level of assistance from your staff.
- All documentation (CD, LTP and all other underlying documentation) provided will be subject to appropriate levels of quality review before submission for audit.
- The CD and LTP will include all relevant disclosures.
- We will review, at most, two drafts of each of the CD and LTP during our audit.
- We will also review one printer's proof copy of the CD and LTP and one copy of the electronic version of the CD and LTP (for publication on your website).
- There are no significant changes in the structure or level of operations of the Auckland Council Group.

If the scope and/or amount of work changes significantly (such as a change in direction during the development of the CD or between the development of the CD and the LTP), we will discuss the issues with you at the time.

If information is not available for the visits as agreed, or the systems and controls the Auckland Council Group uses to prepare the underlying information and assumptions cannot be relied on, we will seek to recover all 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 any subsequent amendments the Auckland Council Group might make to the adopted LTP under section 93D.

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

<b>Month of billing</b>	<b>\$</b>
November 2017	137,000
December 2017	137,000
January 2018	137,000
February 2018	137,000
June 2018	137,000
<b>Total</b>	<b>\$685,000</b>

## **8 Personnel**

Our personnel involved in the management of the audit are:

### **Office of the Auditor-General**

Greg Schollum Deputy Auditor-General  
Sarah Markley Sector Manager – Local Government

### **Audit New Zealand**

Jo Smail Director  
Athol Graham Second Director  
Andy Burns Engagement Quality Control Director  
Robert Sutherland Audit Manager  
Lauren Clark Audit Supervisor  
Alan Clifford Information Systems Auditor  
John Mackey Tax Director  
Martin Richardson Specialist Audit and Assurance Services Director

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

## **9 Agreement**

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

- it is in accordance with your understanding of the arrangements for this audit of the CD and LTP for the period commencing 1 July 2018; and
- you accept the terms of the engagement set out in this letter that apply specifically to the audit of the CD and LTP and supplement the existing audit engagement letter dated 16 February 2017.

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

Yours sincerely

Greg Schollum  
Deputy Auditor-General

cc Stephen Town, Chief Executive  
Matthew Walker, Acting Chief Financial Officer

*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 CD and LTP, and which supplements the existing audit engagement letter dated 16 February 2017.*

Signed: \_\_\_\_\_ Date: \_\_\_\_\_  
Hon Phil Goff  
Mayor of Auckland

# Appendix 1: Terms of the engagement that apply specifically to the audit of the CD and LTP

## Objectives

The objectives of the audit of the CD and LTP are:

- to provide independent opinions on the CD (under section 93C(4) of the Act) and on the LTP (under section 94(1) of the Act) about:
  - whether each document gives effect to the relevant statutory purpose; and
  - the quality of the information and assumptions underlying the information included in each document; and
- to report on matters relevant to the Auckland Council Group's planning systems that come to our attention.

Our audit involves performing procedures that examine, on a test basis, evidence supporting assumptions, amounts and other disclosures in the CD and LTP, and evaluating the overall adequacy of the presentation of information.

We also review other information associated with the CD and LTP to identify whether there are material inconsistencies with the audited CD and LTP.

## Provision of a management report to the Council

At a minimum, we will report to the Council at the conclusion of the engagement. The management report communicates matters which come to our attention during the engagement and that we think are relevant to the Auckland Council Group. For example, we will report:

- any weaknesses in the Auckland Council Group's systems; and
- uncorrected misstatements noted during the audit.

Please note that the Auditor-General may refer to matters that are identified in the audit of CDs and LTPs in a report to Parliament if it is in the public interest, in keeping with section 20 of the Public Audit Act 2001.

## Materiality

Consistent with the annual audit, the audit engagement for the CD and LTP adheres to the principles and concepts of materiality during the 10-year period of the LTP and beyond (where relevant).

Materiality is one of the main factors affecting our judgement on the areas to be tested and the nature and extent of our tests and procedures performed during the audit. In planning and performing the audit, we aim to obtain assurance that the CD and LTP, and the information and assumptions underlying the information contained in these documents, do not have material misstatements caused by either fraud or error.

Material misstatements are differences or omissions of amounts and disclosures that, in our judgement, are likely to influence a reader's overall understanding of the forecast financial statements and performance information.

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 standards applied when conducting the audit of the CD and adopted LTP**

Our audit is carried out in accordance with International Standard on Assurance Engagements (New Zealand) 3000 (Revised): *Assurance Engagements Other Than Audits or Reviews of Historical Financial Information*. In meeting the requirements of this standard, we took into account particular elements of the Auditor-General's Auditing Standards and International Standard on Assurance Engagements 3400: *The Examination of Prospective Financial Information* that were consistent with those requirements.

## **Responsibilities**

### **General responsibilities**

The general responsibilities of the Council for preparing and completing the CD and LTP are consistent with those for the annual report, as set out in the audit engagement letter dated 16 February 2017 – but noting that the CD and LTP include forecast information.

These responsibilities include those set out in Appendices 1 and 2 of that audit engagement letter as detailed below:

- Appendix 1: Respective specific responsibilities of the Council and the Appointed Auditor:
  - Responsibilities for compliance with laws and regulations.
  - Responsibilities to establish and maintain appropriate standards of conduct and personal integrity.

### **Specific responsibilities**

The Council is responsible for:

- maintaining accounting and other records that:
  - correctly record and explain the forecast transactions of the Auckland Council Group;
  - enable the Auckland Council Group to monitor the resources, activities and entities under its control;
  - enable the Auckland Council Group's forecast financial position to be determined with reasonable accuracy at any time; and
  - enable the Auckland Council Group to prepare forecast financial statements and performance information that comply with legislation.

- providing us with:
  - access to all information and assumptions relevant to preparing the CD and LTP, such as records, documentation and other matters;
  - additional information that we may request from the Auckland Council Group for the purpose of the audit;
  - unrestricted access to Auckland Council Group members and employees that we consider necessary; and
  - written confirmation concerning representations made to us in connection with the audit.

### **Health and safety of audit staff**

The Auditor-General and Audit New Zealand take seriously their responsibility to provide a safe working environment for audit staff. Under the Health and Safety at Work Act 2015, we need to make arrangements with you to keep our audit staff safe while they are working at your premises. We expect you to provide a safe work environment for our audit staff. This includes providing adequate lighting and ventilation, suitable desks and chairs, and safety equipment, where required. We also expect you to provide them with all information or training necessary to protect them from any risks they may be exposed to at your premises. This includes advising them of emergency evacuation procedures and how to report any health and safety issues.

## Appendix 2: Team mix and hours for the audit of the CD and LTP for the 10-year period commencing on 1 July 2018

	Total hours
Audit Director	450
Engagement Quality Review Director	50
Sector Specialists	120
Audit Manager	650
Other CA staff	810
Staff not yet CA qualified	750
Other Expert or Specialist Assistance:	95
<b>Totals</b>	<b>2925</b>

### Fee calculations

	\$
Net fee	\$685,000
OAG overhead contribution*	<b>NIL</b>
<b>Total fee (including overhead contribution)</b>	<u>\$685,000</u>
GST	\$102,750
<b>Audit fee for the LTP for the period commencing 1 July 2018</b>	<b>\$787,750</b>

\* No OAG overhead is charged in relation to the audit of the LTP.

We will charge disbursements, including travel, on an actual and reasonable basis.