



Shire of Morawa

**Annual Financial Report Audit for Year Ended 30
June 2021**

**Report on Significant Matter (Section 7.12A (4a) of
the Local Government Act 1995)**

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Background

The Shire of Morawa (Shire) is required to prepare an audited Annual Financial Report each year under the Local Government Act 1995 (the Act). The Shire's auditor is the Office of the Auditor General (OAG).

The Shire's Annual Financial Report for the period ended 30 June 2021 was completed in December 2021 and signed Independent Auditors Report (**Appendix A**) was dated 21 December 2021.

Section 7.12A (4a) states that a Local Government must prepare a report addressing any matters identified as significant by the auditor in the audit report, stating what action the local government has taken or intends to take with respect to each of those matters.

The OAG Independent Auditor's Report shown in **Appendix A** identifies one matter identified as significant through the audit of the Shire's annual financial report.

As such this report has been prepared to meet the requirements of Section 7.12A and to address the significant adverse trend identified by the OAG.

Summary of Ratios

Regulation 50 of the Local Government (Financial Management) Regulations 1996 requires the inclusion of seven ratios in the Annual Financial Report.

Regulation 50: Financial ratios to be included in annual financial report

The annual financial report is to include, for the financial year covered by the annual financial report and the 2 preceding financial years –

1. the current ratio; and
2. the asset consumption ratio; and
3. the asset renewal funding ratio; and
4. the asset sustainability ratio; and
5. the debt service cover ratio, and
6. the operating surplus ratio; and
7. the own source revenue coverage ratio.

The OAG has identified that the Shire's Operating Surplus Ratio has been below the Department of Local Government, Sport and Cultural Industries' (DLGSCI) standard for the last three years. I would like to note that the 2019/2020 Audit Opinion also had the Asset Sustainability Ratio listed as having an adverse trend, which the Shire has managed to turnaround during 2020/2021.

Shire of Morawa's Position

The following ratio data has been taken from the Annual Financial Statements for the year ending 2019 & 2021.

	2017	2018	2019	2020	2021
Operating Surplus Ratio	0.19	-0.54	-0.32	-0.51	-0.28
Meets Benchmark?	Yes	No	No	No	No

Table 1: Colour coded ratio analysis 2017-2021 from Annual Financial Statements (Shire of Morawa)

This ratio has been in the negative for the last four (4) years with an improvement showing between 2020 and 2021. The results of this ratio are affected by Council's ability to raise own source revenue to cover its operational needs and shows that increases to rates and charges over time have not been adequate to cover the increases to expenditure. Covid-19 had a significant affect during the 2020 financial year as Council did not increase any of its fees or charges as the expected impact of the pandemic on the community was unknown.

The Shire typically takes a cautious and conscientious approach to expenditure and the use of rate payer funds, which is highlighted by the Shire's reserve management practices supported by associated policies.

For the financial year ended 30 June 2021 the Shire had a reserve fund balance of \$5.5m, \$300k higher than 2020 and around 2.8 times the Shire's annual rates income. The Shire is confident of its financial health even if the Operating Surplus Ratio indicates a significant adverse trend.

The Shire also monitors its use of borrowings very closely and will only borrow if necessary to carry out suitable capital investments. Council currently has borrowings to the value of \$473k. This indicates that the Shire is unlikely to face significant financial impacts from being unable to repay its debts and is evident by the Shire's positive current ratio of 4.59%.

Addressing the Significant Matter

The Shire plans to address the significant matter identified by the OAG in the following ways.

1. Undertake a review of its Long-Term Financial Plan/Strategic Resource Plan including Asset Management Plans
2. Review operational expenditure
3. Review operating income

1. Undertake a review of Long-Term Financial Plan

The Shire has instigated a review of its long-term financial plan which unfortunately has not yet been completed due to limited staff resources, and whilst this has been contracted to Moore Australia, staff input is still necessary.

A review of the Shire's long term financial plan may identify further areas where refinements can be made, but it should be noted that in previous versions of the Long-Term Financial Plan the Shire expected both the Operating Surplus Ratio and Asset

Sustainability Ratio ratios to be below the DLGSCI's standard/baseline, this was not seen as detrimental to the Shire's financial viability.

In terms of long-term financial planning the Shire will also be reviewing its depreciation rates. Since 2016 the Shire's total asset base has only increased by 3% but its annual depreciation has increased by 30%, indicating a higher depreciation for assets year on year or some newly purchased assets having short useful lives. The Shire's asset replacement and renewal expenditure has remained relatively consistent at around \$1.5m per year. Whilst depreciation and ratios may suggest a higher level of capital renewal and replacement is required this needs to be balanced against the level of usage of assets.

3. Review Operating Expenditure

It should be noted that the Shire's general operating expenditure is at a very similar position as it was when the Long-Term Financial Plan was last revised which demonstrates the Shire's prudent approach towards expenditure.

One of the Shire's biggest expenditure areas is transport, specifically road maintenance which is necessary to support the agricultural economy. As such it is unlikely many savings will be achievable in this area.

One area the Shire is looking to save funds is on utilities, given utility providers continue to increase charge rates year on year. The Shire has recently signed a new contract with Synergy which gives some relief on the cost of power on our high consumption facilities. We are also planning to complete asset upgrades on other Shire properties in the form of Solar Panels to reduce power consumption. Unfortunately to implement this type of installation will incur significant capital expenditure which will need to be spread over a few years to achieve.

The continuation of prudent financial management and cost rationalization should see improvement of the Shire's Operating Surplus Ratio over time.

4. Review Operating Income

One of the main factors affecting the Shire's ability to invest in asset renewal and improve its Operating Surplus Ratio is income.

Since 2016 the Shire's total income from rates has increased from \$1.3m to \$1.9m, with no increase in population. Although the Shire could impose significant rate increases to improve its ratios, this would not be in the best interest of the community. Rates will need to continue to increase by more than inflation and wage increases to maintain the Shire's ability to cover its operational expenditure and asset renewal needs but large increases are unlikely.

Another way to increase the potential income from rates is by substantially increasing the Shire's population and property development. The Shire's population has declined over several years and much of the land in the townsite is undeveloped. The Shire's strategic community plan and previously the Regeneration Morawa initiative has placed an emphasis on population growth and economic development. The Shire continues to invest in this area, but it is unlikely the Shire will see marked improvements

in the short term but over the longer term it is envisaged that growth will positively contribute to financial sustainability.

Other income components have been largely negative. Interest income from the Shire's reserve and bank accounts dropped from \$62k in 2019/2020 to \$27k in 2020/2021 a drop of 43% even though reserves increased by \$300k and is expected to be even lower in coming financial years.

Income from Fees and Charges is reviewed annually as part of the budget process, but whilst the Shire could consider implementing a significant increase it must consider the impact on the community when undertaking this course of action. Many of Shire's fees are legislated or have been set based on expenditure. Other areas are deemed to be a community service such as the swimming pool, so the charge does not cover costs.

Conclusion

The significant adverse trend in the Shire's financial position identified by the OAG in response to three consecutive years of below par performance for the Operating Surplus Ratio is not something that can be easily fixed during one financial year.

The Shire of Morawa is committed to exploring avenues to increase operating revenues and rationalize costs, however as an organization with a strategic vision to create a welcoming and inclusive community with a vibrant and growing economy, all operational changes must be reviewed in a strategic context in terms of the longer-term effects it might have on our community.

A review of long-term financial planning should highlight any areas of financial concern and allow the Shire to adapt its practices to maintain financial viability. Funds held in reserve are designed for strategic benefit but still provide the Shire with capacity to invest in asset renewal if necessary.

No obvious quick wins are evident to improve the Shire's financial ratios, however it is debated as to whether the Operating Surplus Ratio alone represent a significant adverse trend in the Shire's position. The Shire has very minimal debt and holds money in reserve and has limited chance of encountering financial hardship in the near future.

The Shire encourages the Minister for Local Government to engage with the OAG, WALGA and LG Professionals to review the Department's financial ratios and their relevance to regional/remote communities and the different operational environments in which they operate.



Auditor General

INDEPENDENT AUDITOR'S REPORT 2021 Shire of Morawa

To the Councillors of the Shire of Morawa

Report on the audit of the annual financial report

Opinion

I have audited the financial report of the Shire of Morawa (Shire) which comprises:

- the Statement of Financial Position at 30 June 2021, the Statement of Comprehensive Income by Nature or Type, Statement of Comprehensive Income by Program, Statement of Changes in Equity, Statement of Cash Flows and Rate Setting Statement for the year then ended
- Notes comprising a summary of significant accounting policies and other explanatory information
- the Statement by the Chief Executive Officer.

In my opinion the financial report of the Shire of Morawa:

- is based on proper accounts and records
- fairly represents, in all material respects, the results of the operations of the Shire for the year ended 30 June 2021 and its financial position at the end of that period in accordance with the *Local Government Act 1995* (the Act) and, to the extent that they are not inconsistent with the Act, Australian Accounting Standards.

Basis for opinion

I conducted my audit in accordance with Australian Auditing Standards. My responsibilities under those standards are further described in the Auditor's responsibilities section below. I am independent of the Shire in accordance with the *Auditor General Act 2006* and the relevant ethical requirements of the Accounting Professional & Ethical Standards Board's APES 110 *Code of Ethics for Professional Accountants (including Independence Standards)* (the Code) that are relevant to my audit of the financial report. I have also fulfilled my other ethical responsibilities in accordance with the Code. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my opinion.

Responsibilities of the Chief Executive Officer and Council for the financial report

The Chief Executive Officer (CEO) of the Shire is responsible for the preparation and fair presentation of the financial report in accordance with the requirements of the Act, the Regulations and Australian Accounting Standards. The CEO is also responsible for managing internal control (as required by the CEO) to ensure the financial report is free from material misstatement, whether due to fraud or error.

In preparing the financial report, the CEO is responsible for assessing the Shire's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the State Government has made decisions affecting the continued existence of the Shire.

The Council is responsible for overseeing the Shire's financial reporting process.

Auditor's responsibility for the audit of the financial report

As required by the *Auditor General Act 2006*, my responsibility is to express an opinion on the financial report. The objectives of my audit are to obtain reasonable assurance about whether the financial report as a whole is free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes my opinion. Reasonable assurance is a high level of assurance but is not a guarantee that an audit conducted in accordance with Australian Auditing Standards will always detect a material misstatement when it exists.

Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of the financial report. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations or the override of internal control.

A further description of my responsibilities for the audit of the financial report is located on the Auditing and Assurance Standards Board website. This description forms part of my auditor's report and can be found at https://www.auasb.gov.au/auditors_responsibilities/ar4.pdf.

Report on other legal and regulatory requirements

In accordance with the Local Government (Audit) Regulations 1996 I report that:

- (i) In my opinion, the following material matter indicates a significant adverse trend in the financial position of the Shire:
 - a) The Operating Surplus Ratio as reported in Note 31 of the annual financial report is below the Department of Local Government, Sport and Cultural Industries basic standard for all 3 years reported in the annual financial report.
- (ii) The following material matters indicating non-compliance with Part 6 of the Act, the Regulations or applicable financial controls of any other relevant written law were identified during the course of my audit:
 - a) A review of the appropriateness and effectiveness of the Shire's financial management systems and procedures was not completed by the CEO at least once every three financial years, as required by section 5(2)(c) of the Local Government (Financial Management) Regulations 1996. The last review took place for the financial year ended 30 June 2016.
 - b) Bank reconciliations for the municipal account was not reconciled until 17 August 2021, which resulted in 32 backdated payments totalling \$158,301 not being identified in a timely manner. These were subsequently corrected during the audit.
- (iii) All required information and explanations were obtained by me.
- (iv) All audit procedures were satisfactorily completed.
- (v) In my opinion, the Asset Consumption Ratio and the Asset Renewal Funding Ratio included in the financial report were supported by verifiable information and reasonable assumptions.

Other information

The other information is the information in the entity's annual report for the year ended 30 June 2021, but not the financial report and my auditor's report. The CEO is responsible for the preparation and the Council for overseeing the other information.

My opinion does not cover the other information and, accordingly, I do not express any form of assurance conclusion thereon.

Matters relating to the electronic publication of the audited financial report

This auditor's report relates to the financial report of the Shire of Morawa for the year ended 30 June 2021 included on the Shire's website. The Shire's management is responsible for the integrity of the Shire's website. This audit does not provide assurance on the integrity of the Shire's website. The auditor's report refers only to the financial report described above. It does not provide an opinion on any other information which may have been hyperlinked to/from this financial report. If users of the financial report are concerned with the inherent risks arising from publication on a website, they are advised to refer to the hard copy of the audited financial report to confirm the information contained in this website version of the financial report.

Grant Robinson
Assistant Auditor General Financial Audit
Delegate of the Auditor General for Western Australia
Perth, Western Australia
21 December 2021