

Sunshine Coast Regional Council

Interim management report to the Mayor
For the financial year ended 30 June 2016

Issued 9 June 2016





Summary



Understanding this report



Control and risk issues



Status update of prior year reported issues



Risk ratings used in this report

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1. Summary

In this report we detail the internal control and financial reporting issues we identified during our interim audit visit of Sunshine Coast Regional Council in respect of the 30 June 2016 financial statement audit. For each issue we have included the management responses we received. We have also provided a status update on report issues that were not resolved at the end of the prior year (refer to 4.1. and 4.2).

Internal control issues

Before testing

In our *External audit plan*, we set out our audit approach based on your overall internal control framework being assessed as effective. We based our assessment on our understanding of your council and including relevant controls. We planned to test the operating effectiveness of controls in the areas of information systems, expenditure and payroll reducing the expected level of other audit procedures to be performed in combination with a detailed substantive testing approach for all material financial statement components.

Results of testing

We have tested the operating effectiveness of information systems general controls, expenditure and payroll controls. We identified four internal control deficiencies in relation to information system general controls. Refer to 3.2 for details.

Approach after testing

Based on results of our testing we confirm our initial assessment of council's overall control framework as effective. Accordingly, we will rely on the operating effectiveness of your internal control environment to reduce the level of substantive procedures we will perform on the following financial statement areas of expenditure, payroll and cash and financing, with remaining financial statement areas of property, plant and equipment and revenue to have a detailed substantive testing approach.

Financial reporting issues

We identified a financial reporting issue that we assessed as low risk. Refer to 3.3 for details.

Other matters

We identified other matters that we consider represent business process improvement opportunities. Refer to 3.4 for details.

If we identify any further issues as the audit progresses, we will include them in our *Closing report* issued at the conclusion of our audit.

Based on the issues raised in this report, we will not make major changes to the audit approach as presented in our *External audit plan*.

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2. Understanding this report

2.1 Internal control issues

What is internal control?

'Internal control' is the processes, systems, records and activities that your entity designs, implements and maintains to provide you with reasonable assurance about the achievement of organisational objectives regarding:

- reliability of financial reporting
- effectiveness and efficiency of operations
- compliance with applicable laws and regulations.

Your elected council and executive management collectively are responsible for preparing reliable financial statements in accordance with generally accepted accounting principles; and they are similarly responsible for maintaining effective internal control over financial reporting.

Our assessments of your internal control framework

The auditing standards that we must comply with, require us to understand and assess those aspects of your internal control that relate to our financial statement audit objectives. In the planning phase of our audit we seek to understand and evaluate how controls are designed and implemented. We communicated to you the results of our analysis in our *External audit plan*.

If we decide that we can rely on your controls, we must then test them to confirm they operated effectively. The results of our testing may highlight deficiencies in your internal controls. We assess whether any identified deficiencies in internal control constitute, individually or in combination, a significant deficiency in internal control. This is based on their potential to cause a material misstatement (an error that could affect the judgement or opinion of readers) in the financial statements.

Limitations of our reporting on internal control deficiencies

No system of internal control can provide absolute assurance about the absence of error or compliance. Even in the absence of identified control weaknesses, the inherent limitations in your internal controls over financial reporting may not prevent or detect material misstatements.

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2.2 Financial reporting issues

Financial reporting issues relate to the reliability, accuracy and timeliness of your financial reporting and/or the effectiveness and efficiency of your council's operations, including probity, propriety and compliance with applicable laws and regulations. We have rated them based on their potential to impact on our auditor's report and/or for giving rise to material misstatement in the financial statements.

Where we have identified financial reporting issues not already included in our *External audit plan*, or where issues related to previously reported risks have significantly changed, we have included them in this report.

2.3 Auditor-General reporting to parliament

The *Auditor-General Act 2009* requires the Auditor-General to report to parliament on an issue raised during an audit if he considers it significant. This includes consideration of identified significant deficiencies in internal control and financial reporting issues. However, whether these issues are reported depends on a number of factors, including action taken to resolve the issues prior to the completion of the audit. If the Auditor-General intends to include an issue from this audit in a future report to parliament, you will be given an opportunity to comment on the issue raised and your comments, or a summary of them, will be reflected in the report.

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3. Issues

3.1 Significant internal control deficiencies

We did not identify any significant internal control deficiencies through our audit testing as at date of this report.

3.2 Internal control deficiencies

The following table summarises internal control deficiencies identified through our audit testing as at date of this report, and includes a response from management:

No.	Area	Issue	QAO recommendation	Management response
3.2.1	Information systems - Security	<p>Logging and monitoring critical database changes</p> <p>The council does not log and independently monitor security related transactions and critical changes to the databases of financial systems (e.g. direct data changes, changes to database configuration parameter settings, changes to executable code).</p> <p><i>Implication:</i> Detection of unauthorised changes in the financial systems production databases may not occur.</p>	<p>We recommend the council:</p> <ol style="list-style-type: none"> assess the risk, impact and criticality of: <ul style="list-style-type: none"> direct data changes to critical tables in the database changes to security configuration files for the database. Log, monitor and review critical security and direct data changes to databases in accordance with the result of the risk assessment. 	<p>Agree with QAO</p> <p><i>Action plan:</i></p> <ul style="list-style-type: none"> Relevant business areas have their own QA processes, including checks and balances, to ensure correctness of processes such as employee pay runs, council rate generation, and creditor payment runs etc. Therefore, with the history of audits and reviews of controls, we believe this risk is well managed. SCRC will action item 1 as requested above, and act on the findings of that analysis. It is noted that monitoring of direct data changes to the database is possible using T1 audit controls to add auditing to financial transactions (T1 Finance and T1 Property). This does, however, add a significant performance impact to the system, so the cost of implementation will need to be considered in this review. Critical security changes to the databases - The T1 Property and Finance databases - currently monitor for any database Add/Delete User operations which get alerted to our DBA.

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No.	Area	Issue	QAO recommendation	Management response
3.2.1 cont				<ul style="list-style-type: none"> Adequate controls are in place regarding executable changes as all go through TechOne (the provider), as well as SCC's change request process in ICTS. <p>SCRC will undertake the recommendations.</p> <p><i>Status:</i> Work in progress <i>Proposed action date:</i> 31 December 2016 <i>Responsible officer:</i> Chief Information Officer/Team Leader Corporate Systems.</p>
3.2.2	Information systems - Security	<p>Privileged user activities</p> <p>The council does not independently monitor and review key financial systems on security related transactions such as assignment of elevated privileges, changes to profile / role configurations, enabling and disabling user accounts with elevated privileges.</p> <p><i>Implication:</i></p> <p>There is an increased risk that unauthorised activities and transactions may not be timely detected.</p>	<p>We recommend that personnel, independent from system administration activities, monitor and review security related transactions for:</p> <ol style="list-style-type: none"> assigning of elevated privileges to users. changes to privileges allocated to a profile / role enabling and disabling user accounts with elevated privileges. 	<p>Agree with QAO</p> <p><i>Action plan:</i></p> <p>It has been the process that the appropriate business administrators maintain and monitor the users that have Application Admin privileges.</p> <p>It is understood that the Finance area perform periodical reviews of their administrators, however this will need to be reviewed for all of the T1 Property, and Payroll business areas. Reports are provided within each application which the business area could use to periodically review the admin users for each application.</p> <p>SCRC will undertake the recommendations.</p> <p><i>Status:</i> Work in progress <i>Proposed action date:</i> 31 December 2016 <i>Responsible officer:</i> Business Application Custodians.</p>

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No.	Area	Issue	QAO recommendation	Management response
3.2.3	Information systems - Security	<p>Resetting passwords over the phone</p> <p>There are no processes in place to verify the users' identity when they request password reset over the phone.</p> <p><i>Implication:</i></p> <p>There is a risk that password reset is requested by unauthorised user who intends to breach system security.</p>	We recommend the council implement processes and/or technology to verify users who request password reset over the phone.	<p>Agree with QAO</p> <p><i>Action plan:</i></p> <p>Most telephone assists are for unlocking the computer, and therefore still needs person to know password. However there are some people that do seek password reset. For system administrator users we require more information, and know the individuals, so any risk is associated only with those having lower access privileges. We could look at seeking DOB or payroll number as part of verification.</p> <p>We are introducing a new identity management solution that will provide improved validation, and also allow self-management that support multi-factor verification, and therefore will continue with the implementation and ensure it addresses this recommendation.</p> <p><i>Status:</i> Work in progress</p> <p><i>Proposed action date:</i> 31 December 2016</p> <p><i>Responsible officer:</i> Coordinator ICT Services.</p>
3.2.4	Information systems - Security	<p>User access for TechnologyOne Property system</p> <p>There is no periodic review of user access to the system to ensure that access privileges are commensurate with users' roles and responsibilities and segregated from incompatible functions.</p> <p><i>Implication:</i></p> <p>The council may not detect and correct unauthorised or incompatible access privileges and this may result in unauthorised or incorrect transactions being processed fraudulently or in error.</p>	We recommend that Council review user access on a regular basis (biannual or annually).	<p>Agree with QAO</p> <p><i>Action plan:</i></p> <p>The business area Application Administrators allocate access privileges to the applications. It is understood verification has occurred on processes, however we acknowledge the need to check with key personnel, e.g. applications administrators in the Rates Team, Waste, Development Service, and Community response, to understand and clarify their processes.</p> <p>It is important to note the business Quality Assurance processes also validate appropriate transactions, and controls in key areas around access privileges have been previously reviewed through audit processes.</p>

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No.	Area	Issue	QAO recommendation	Management response
3.2.4 cont				<i>Status:</i> Work in progress <i>Proposed action date:</i> 31 October 2016 <i>Responsible officer:</i> Business Application Custodians

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3.3 Financial reporting issues

This table summarises the one financial reporting issue (assessed as low risk), that we identified through our audit testing, and includes a response from management.

No.	Area	Details	QAO recommendation	Management response
3.3.1	Property, plant and equipment	<p>Capitalised costs for Maroochyore City Centre Priority Development Area includes operational expenses</p> <p>We commenced a review over capitalized costs relating to the Maroochyore City Development Area. We noted the capitalisation of advertising and promotional activity, totaling approximately \$212 500.</p> <p>In our judgment, the nature of these expenses do not meet the criteria for recognition of assets as set out in AASB 116 <i>Property, Plant & Equipment</i>.</p> <p>We will continue our review of capital works in progress during our year-end audit.</p> <p><i>Implication:</i> Costs that are not capital in nature are not being expensed in the period in which they are incurred and therefore operating expenditure may be understated and conversely Work-In-Progress overstated</p>	<p>We recommend the council undertake a review of capitalised costs assigned to the Maroochyore City Development jobs, to ensure they met the recognition criteria within AASB 16.</p>	<p><i>Agree with QAO</i></p> <p><i>Action plan:</i> Council accepts the recommendation provided by Queensland Audit Office. Council is aware that postings to capital jobs associated with MCC PDA require review with the expectation that some transfers to operating will be required.</p> <p>Comprehensive review and assessment of expenditure types for MCC PDA capital jobs will be conducted on a monthly basis by a key stakeholder review group. Key members:</p> <ul style="list-style-type: none"> • Project Manager • Financial Accounting Coordinator • Project Administrator (Senior Management Accountant) • Senior Capital Accountant • Senior Asset Accountant. <p>The monthly review group will ensure all costs posted to capital jobs satisfy recognition criteria and are directly attributable to assets being delivered. Where project costs are identified as not being capital in nature, such costs will be expensed in the period incurred. Comprehensive review will also ensure project costs are recorded in the appropriate capital job and project overhead costs are apportioned in the current period to the relevant stage or assets being delivered.</p> <p><i>Status:</i> Work in progress <i>Proposed action date:</i> 30 June 2016 <i>Responsible officer:</i> Key Stakeholder Review Group as detailed above.</p>

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3.4 Other matters

The following table summarises other matters related to business improvement opportunities we identified through our audit testing, and includes a response from management.

No.	Area	Opportunity	QAO recommendation	Management response
3.4.1	Property, plant and equipment	<p>Asset Management Plans awaiting adoption by Council.</p> <p>Management has completed seven Asset Management Plans (AMPs) during the 2015-16 financial year that are awaiting formally adoption by Council.</p> <p>The AMPs awaiting adoption are</p> <ul style="list-style-type: none"> • Buildings and Facilities; • Coastal & Environment; • Holiday Parks; • Parks & Gardens; • Stormwater; • Transportation; and • Waste and Resources Management. 	We recommend council's website reflect current Asset Management Plans.	<p>Agree with QAO</p> <p><i>Action plan:</i></p> <p>Council accepts the above recommendation and will commence tabling Annual Asset Management Plans at Council for endorsement.</p> <p><i>Status:</i> Work in progress</p> <p><i>Proposed action date:</i> 16 December 2016</p> <p><i>Responsible officer:</i> Coordinator Asset Management and Capital Planning</p>

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4. Status update of prior year reported issues

4.1 Internal control deficiencies

The following table provides an update on the status of an issue carried over from the prior year that was reported internal control deficiencies.

No.	Component	Prior year issue and recommendation	QAO	Status update
			assessed category	
4.1.2	Information systems	<p><i>Date issued raised:</i> 27 June 2013</p> <p>Issue: User Profile Maintenance and Financial Delegations Finance One user profile management processes identified control weaknesses over user profile matrix, system logging, and review and monitoring of financial delegations.</p> <p><i>Recommendation (summary only):</i> Council initiate action to address the control weaknesses identified.</p>	<p><i>Prior year:</i> Deficiency</p> <p><i>Current year:</i> Deficiency</p>	<p>Management comment: Agreed. It is proposed to maintain the profile matrix within Microsoft Excel.</p> <p>QAO update: Correction action is still being undertaken to address the issue. A FinanceOne upgrade is expected to go live by 17 June 2016. Council advised that a draft security matrix has been developed but not yet finalised. A review of delegations as set up in FinanceOne is also being conducted as part of the upgrade.</p> <p>Issue remains OPEN – We will follow-up during the 2015-16 final audit visit.</p>

Management has since resolved one issue the need for an additional audit committee prior to clearing the financial report for management certification.

4.2 Financial reporting issues

We also raised two financial reporting issues that have been resolved. These issues were about -

- erroneous duplicates in council's road spatial data and
- high Level of fully depreciated assets.

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5. Risk ratings used in this report

5.1 Our rating of internal control deficiencies

We have assessed all internal control deficiencies in this report based on their potential to cause a material misstatement in the financial statements. The risk assessment categories are as follows:

Assessed category	Potential effect on the financial statements	Prioritisation of remedial action
Significant deficiency	<p>This is a deficiency in internal control, or combination of deficiencies in internal control that, in our professional judgement, may lead to a material misstatement of the financial statements.</p> <p>Significant deficiencies are always of sufficient importance to merit the attention of those charged with governance.</p>	<p>This requires immediate management action to resolve.</p> <p>(This should be resolved before issuance of the current year audit opinion.)</p>
Deficiency	<p>We have assessed that the control:</p> <ul style="list-style-type: none"> (i) is designed, implemented or operated in such a way that it is unable to prevent, or detect and correct, misstatements in the financial statements component on a timely basis, or (ii) is necessary to prevent, or detect and correct, misstatements in the financial statements component on a timely basis, but is missing. 	<p>This requires management action to resolve within eight months of this report date.</p> <p>(This is not required to be resolved before the issuance of the current year audit opinion; however unless otherwise agreed it should be resolved before next year interim audit work is commenced.)</p>

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5.2 Our rating of financial reporting issues

We have assessed all financial reporting issues in this report based on their potential to cause a material misstatement in the financial statements. The assessed risk ratings are as follows:

Risk rating	Potential effect on the financial statements	Prioritisation of remedial action
High	We assess that there is a high likelihood of this causing a material misstatement, whether due to fraud or error, in one or more components (transactions, balances and disclosures) of the financial statements.	This requires immediate management action to resolve. (This must be resolved before we issue this year's audit opinion.)
Medium	We assess that there is a medium likelihood of this causing a material misstatement, whether due to fraud or error, in one or more components of the financial statements.	This requires management action to resolve within four months of this report date. (This is not required to be resolved before we issue this year's audit opinion.)
Low	We assess that there is a low likelihood of this causing a material misstatement, whether due to fraud or error, in one or more components of the financial statements.	We recommend management action to resolve; however, a decision on whether any action is taken is at management's discretion. (This is not required to be resolved before we issue this year's audit opinion.)

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