



Local Excellence

Councils Working Together for Communities

Financial Sustainability

Information Paper 4

Specifications for External Audit

Revised January 2012



Introduction

This Information Paper is one of a series of Information Papers about Financial Sustainability and Financial Governance in Local Government.

The series of Information Papers was originally published in 2006 to 2011 as part of the Financial Sustainability Program. The history of that program and a complete list of Information Papers and other resources, including a glossary of terms and abbreviations, is provided on the LGA's "Financial Sustainability" web page: <http://www.lga.sa.gov.au/goto/fsp>.

The entire series of Papers was revised in early 2012 to take account of legislative changes and other developments. These Papers are addressed to, and written primarily for the benefit of Council Members and staff, but they are also available as a resource for the general public and students of Local Government.

This Information Paper combines what were previously published as two separate Information Papers:

- No 4 – *Scope of External Audit - Audit Specification*; and
- No 24 – *Audit Management Letter*

The previous Information Paper No. 24 has been discontinued and its contents merged into this revised Information Paper. This Paper should be read in conjunction with relevant legislation, and all the other existing Information Papers, especially No. 23 – *Financial Governance* and No. 2 – *An Overview of Audit Mechanisms*.

What is an annual audit?

The general definition of the word "audit" is to examine or review and it is most commonly used in relation to verification of an organisation's financial statements. All Councils in South Australia must have annual audits of both:

- the Council's financial statements; and
- the internal financial controls exercised by the Council.¹

These twin audits must be carried out by a qualified auditor and be in accordance with [Australian Auditing Standards](#).² Auditors' reports form part of the annual financial statements and are included in Councils' Annual Reports which are available to communities and are provided to the South Australian Parliament.

During the first decade of the 21st century there were changes to the Corporations Law and [Australian Auditing Standards](#), as governments and the private sector increasingly sought

¹ Transitional provisions in the [Local Government \(Accountability Framework\) Amendment Act 2009](#) provide a period of grace before auditors have to comply with the requirements to audit, and to provide an opinion on, internal financial controls. For most Councils, the requirement to have an auditor provide an opinion on internal financial controls is not mandatory until the audit of the 2015-16 financial year. For 17 "prescribed" (i.e. metropolitan) Councils, the period of grace expires three years earlier, so that an auditor's opinion on internal financial controls must be provided no later than the audit of the 2012-13 financial year, unless the Council seeks and obtains a Ministerial exemption for a 12-month extension of time. Further information on internal financial controls is contained in LGA Financial Sustainability Information Paper 21 – *Internal Financial Controls* at <http://www.lga.sa.gov.au/goto/fsp>.

² [Local Government \(Financial Management\) Regulations 2011](#) – regulation 19. These standards are published by the [Auditing and Assurance Standards Board](#) established under the [Australian Securities and Investments Commission Act 2001](#) (Commonwealth).

additional forms of auditing to provide a greater level of independent analysis of finances and related issues. In part this was prompted by high-profile failures in the private sector but the changes also reflected some concerns about areas of the public sector.

Local Government should aspire to the highest standards and while significant problems have not been experienced by South Australian Councils, the 2005 [Independent Inquiry into the Financial Sustainability of Local Government](#) nevertheless raised questions about Councils' performance in financial areas and the consistency of financial audits for SA Councils. It made a number of recommendations including one that the LGA should develop, in liaison with auditors, a common specification for a traditional Local Government financial audit.

The publication of the audited financial statements is the primary measure used by a Council to provide financial accountability to its community.

Definitions

To ensure consistency across Councils, it is important that there is clarity in understanding the issues relating to the external audit of a Council. The following definitions are provided to assist.

'audit opinions' - at the conclusion of the two audits the auditor will provide two separate audit opinions:

- one on whether the financial statements are free from material mis-statements;³ and
- the other on whether the internal financial controls are "sufficient to provide reasonable assurance that the financial transactions of the council have been conducted properly and in accordance with law."⁴

These two opinions together satisfy the requirements of Section 129(3) of the [Local Government Act 1999](#) ("the Act").

'audit management letter' – Section 129(4) of [the Act](#) provides that an auditor must provide to a Council "written advice on particular matters arising from an audit." This "written advice" (provided either at the conclusion of an interim audit, or after the final audit, or both) is usually referred to as an audit management letter. The audit management letter will set out a range of matters that the auditor considers need to be drawn to the attention of the Council. If the auditor provides an audit management letter after an interim audit, this does not prevent the auditor providing a second audit management letter after the final audit. Audit management letters will become public documents, pursuant to section 129(5e) of [the Act](#), but only after the Council has had a chance to consider and respond to them.

'management representation letter' – [Auditing Standard ASA 580 \(Written Representations\)](#) requires auditors to obtain from management written representations in relation to the fairness and

³ Issued in accordance with [Australian Auditing Standard ASA 700 "Forming an Opinion and Reporting on a Financial Report"](#)

⁴ See footnote 1.

completeness of the financial statements and on other related matters. Management representations may also be required as audit evidence.⁵

'interim audit' – an audit of various aspects of a Council's operations, including the systems and procedures of internal control, prior to the end of the financial year. The interim audit does not result in the issue of an audit opinion on the truth and fairness of the financial report, nor an opinion on the adequacy of internal controls. However the interim audit may lead to provision of an audit management letter.

'final audit' – an audit which results in the issue of an audit opinion on the truth and fairness of the financial statements and a separate opinion on the adequacy of internal controls.

'internal control' – is defined in [ASA 315](#)⁶ (paragraph 4 c) as:

“...the process designed, implemented and maintained by those charged with governance, management and other personnel to provide reasonable assurance about the achievement of an entity's objectives with regard to reliability of financial reporting, effectiveness and efficiency of operations, and compliance with applicable laws and regulations. The term 'control' refers to any aspects of one or more of the components of internal control.”

'internal financial controls' – are the internal controls that are specifically related to financial activities, management and reporting.⁷

Legislative requirements

Some of the significant legislative provisions concerning the auditor include:

- the appointment of the auditor must be on the recommendation of a Council's Audit Committee,⁸
- measures directed at strengthening the independence of the auditor:
 - a Council is prohibited from engaging the auditor to provide any services outside the scope of the auditor's functions under the [Local Government Act 1999](#),⁹
 - a Council Chief Executive Officer and the Presiding Member of the Council's Audit Committee must sign a statement to certify the auditor's independence,¹⁰
 - the auditor himself/herself must sign a further declaration of independence consistent with industry standards;¹¹
- a requirement to include in a Council's annual report information on:
 - the remuneration payable to its auditor – distinguishing between remuneration payable for the annual audit and any other remuneration payable,¹²

⁵ This should not be confused with the 'certification statement' which the CEO and presiding member must sign in relation to the financial statements. See

[Local Government \(Financial Management\) Regulations 2011](#) – regulation 14.

⁶ *"Identifying and Assessing the Risks of Material Misstatement through Understanding the Entity and Its Environment"*

⁷ Further information on internal financial controls is contained in LGA Financial Sustainability Information Paper No. 21: *Internal Financial Controls* at <http://www.lga.sa.gov.au/goto/fsp>

⁸ [Local Government Act 1999](#)– section 128(2)

⁹ [Local Government \(Financial Management\) Regulations 2011](#)– regulation 22 (1)

¹⁰ [Local Government \(Financial Management\) Regulations 2011](#)– regulation 22 (3)

¹¹ [Local Government \(Financial Management\) Regulations 2011](#)– regulation 22 (5)

- the reason for early cessation of an auditor's appointment (if appropriate).¹³
- the auditor must provide:
 - both audit opinions; and
 - one or more audit management lettersto the principal member of the Council (the mayor or chairperson), who in turn must provide copies of the documents to the Chief Executive Officer, and must also ensure that copies are provided to the other Council Members for their consideration at the next available meeting.¹⁴

Auditor rotation

To maintain the independence of the role, [the Act](#) provides, at section 128, that a Council must rotate its auditor at least once each five years.

The effect of the auditor rotation provisions in section 128 of is that a sole financial practitioner who is qualified (i.e. is a registered company auditor) will be able to hold the office of auditor for a maximum 5 years before he or she is required to take an enforced break of at least 2 years from the position. By contrast, a *firm* which is appointed as a Council auditor may be continually reappointed to the office of auditor provided that the natural person within the firm who "plays a significant role in the audit"¹⁵ can be and is rotated so that no one natural person exceeds the 5 year limitation.

Audit Requirements

Councils should clearly articulate their requirements from the audit process and the information that they seek from prospective auditors and in doing so should be mindful that consistent specification of such requirements between Councils is a necessary pre-requisite to the achievement of effective and consistent audit outcomes in Local Government.

This paper includes, at Attachment 1, a model specification that could be adopted, or used by Councils as a basis for the conduct of annual external audits, including tendering for and managing the engagement of external auditors.

¹² The only permitted activities for a Council's auditor, additional to the annual audits of the financial statements and the internal financial controls, are:

- a possible role in conducting an efficiency and economy audit pursuant to section 130A of the [Local Government Act 1999](#). See Information Paper No. 5, *Efficiency and Economy Audits*; at <http://www.lga.sa.gov.au/goto/fsp>; and/or
- certifying that a grant or subsidy received by the council has been acquitted in accordance with any conditions required by the provider of the grant or subsidy. See sub regulation 22(2) of the [Local Government \(Financial Management\) Regulations 2011](#)

¹³ [Local Government Act 1999](#)– section 128(9)

¹⁴ [Local Government Act 1999](#)– section 129(5a)

¹⁵ This term "plays a significant role in the audit" is defined by Section 128(10) of the [Local Government Act 1999](#) and section 9 of the [Corporations Act 2001](#) (Commonwealth) to mean a registered company auditor who acts "on behalf of a firm or company, as a lead auditor, or review auditor, in relation to an audit." In practical terms, therefore, this provision requires only the rotation of the senior person within the firm, who takes final responsibility for signing off the Council's audits. It does not require the rotation of any other audit staff, although it is highly desirable that other audit staff be rotated to emphasize, in the public interest, the independence of their role and function.

The model specification not only addresses Councils' requirements under [the Act](#), but also provides guidance for good practice in Local Government auditing. It addresses the following areas:

- the objectives of the two audits;
- the term of audit appointment;
- scope of the audits;
- audit methodology and approach;
- critical matters to be audited;
- provision of one or two audit management letters;
- time, fees and other arrangements;
- terms and conditions of engagement;
- conditions for termination of appointment; and
- evidence of auditor independence.

The model specification is not designed to cover any *internal* audit requirements of management and Councils. Nor is the specification designed to cover any efficiency and economy audits of specific aspects of operations which the Council may seek an external auditor to undertake.

The model specification is not designed to be universally applicable to all Councils, as some are more advanced in their practices than others. However, the principles embodied in the specification are equally applicable to Councils of all sizes.

Audit management letter – for interim and final audit

For larger Councils, it is likely that the audit will be conducted in two sessions – an interim audit during the financial year and a final audit when the financial statements are available. [Australian Auditing Standard ASA 260](#)¹⁶ requires auditors to provide 'timely' communication. Therefore, where an auditor conducts an interim audit, a management letter will be provided to the Council at the conclusion of the interim audit to enable any required remedial action arising from the audit to be implemented as soon as possible. This also will ensure that any exposure to potential loss is minimised.

The auditor may then provide a second management letter at the completion of the final audit.

Alternatively, although undesirable, where the auditor does not conduct an interim audit, a single audit management letter will be provided at the conclusion of the final audit.

Audit management letter – timing and public release

Prior to handing over a final audit management letter, the auditor should first discuss the contents of the letter with senior management and thereafter at a meeting of the Council's Audit Committee or of the Council itself.

An audit management letter may be kept confidential prior to being considered at the next Council meeting (and for up to 60 days thereafter). However, it is intended to (and will) become a public document, under section 129(5e) of [the Act](#), after the Council has had up to 60 days to consider and act upon the letter.

¹⁶ "Communication with Those Charged with Governance"

This should give the Council sufficient time to clarify issues and instigate, where necessary, improved processes and procedures to ensure the soundness of the Council's internal control framework and the appropriateness of its policies and procedures.

Reports to the Minister

The [Local Government Act 1999](#) also provides that the auditor must report to the Minister in specific circumstances such as any serious financial irregularity, any unauthorised acts or omissions of a substantial nature, or any adverse, qualified or limited audit opinion.¹⁷

Acknowledgements

The contributions of:

- Mr Allen Bolaffi of UHY Haines Norton; and
 - David Hope, of Skilmar Systems Pty Ltd,
- in the preparation of this paper are acknowledged.

This project has been assisted by the [Local Government Research and Development Scheme](#).

¹⁷ [Local Government Act 1999](#) – section 129(6) and (7)

Attachment 1: Model draft specification for a Local Government Audit

Throughout the draft specification italicised comments have been included in text boxes to assist Councils' interpretation and use of the specification. These text boxes can be deleted to enable the specification to be included with a Council's tender request.

1. The Objectives of the Audit

The objective of Council's audit is to provide two independent audit opinions of the:

- accounts and annual financial reports; and
- internal financial controls;

of the [*insert name*] Council for each financial year covered by the term of the audit appointment. The audit must meet both statutory requirements and Australian audit standards.

2. Term of Audit Appointment

Council is seeking to make an appointment for a period of [*insert number (maximum of 5)*] years commencing 1 July [*insert year*] through to 30 June [*insert year*].

Section 128 (4a) and (6) of the [Local Government Act 1999](#) are aimed at ensuring that auditor independence is not compromised by the continuous use of the same natural person as the auditor for many years.

A natural person, who plays (or who has played) a significant role in the audit of the Council for at least 5 successive financial years or for 5 out of 6 successive financial years cannot be re-appointed at the end of a five year term. However if an audit firm is appointed as distinct from an individual, the audit firm may be re-appointed provided that an alternative audit engagement partner is available to be appointed as the lead auditor. A natural person may be re-appointed to the office of auditor if at least 2 years have passed since he or she last held the office.

A change in the natural person who actually undertakes the audit work is a healthy process that will assist in, not only the perceived independence, but also the actual independence of the auditor role.

3. Scope of the Audit

The auditor is to: –

- 3.1. carry out such work as is necessary to form opinions as to whether:
- a) the accounts are properly kept and the annual financial statements:
 - (i) are prepared in accordance with the financial records; and
 - (ii) represent fairly the results of the operations and cash flows for the financial year and the financial position of the Council at 30 June in accordance with the Australian Accounting Standards, the [Local Government Act 1999](#) (as amended) and other mandatory professional reporting requirements.
 - b) the controls exercised by the Council during the relevant financial year in relation to the receipt, expenditure and investment of money, the acquisition and disposal

of property and the incurring of liabilities are sufficient to provide reasonable assurance that the financial transactions of the council have been conducted properly and in accordance with law.

- 3.2. include in his or her audit report any matters identified during the normal audit procedures such as: –
- a) any significant adverse trends in the financial position or the financial management practices of the Council;
 - b) any material irregularities in the Council's accounting practices or in the management of the Council's financial affairs identified during the course of the audit;
 - c) any weaknesses in the Council's internal financial controls;
 - d) any factors impacting on the adequacy of the depreciation charge for the year. This is after due consideration of an assessment of the depreciation methodology principles adopted by Council and the consistency of the accounting principles applied.

This is an extension of the commonly accepted approach to audits in the private sector. Depreciation often is the largest expense line in the financial statements of Councils and the soundness of its methodology of determination, including its disclosure, is integral to the integrity of the financial statements.

The issue of internal financial controls is an important one, especially in smaller Councils where there may not be sufficient staff to maintain adequate segregation of duties. Councils should be conscious of this issue and regular reviews of their exposure to risks arising from inadequate segregation of duties are important. This also is an important aspect of any risk management strategy that Council may administer. This issue is more important where there is no internal audit function. Where there is an internal audit function any reviews of internal controls should have regard to the effectiveness and comprehensiveness of the internal audit activity.

4. Audit Methodology and Approach

- 4.1. The auditor is required to comply with the requirements of the [Local Government Act 1999](#) and the [Local Government \(Financial Management\) Regulations 2011](#).
- 4.2. An audit is to be carried out in accordance with in accordance with the [Auditing Standards and Auditing Guidance Statements](#) published (and amended from time to time) by the Auditing and Assurance Standards Board established under the [Australian Securities and Investments Commission Act 2001](#) of the Commonwealth.
- 4.3. The auditor is to provide the Council with a general outline of his or her methodology. This may include the proposed analysis and review of internal financial controls and the extent to which these controls lead to reliance on the Council's administration and financial systems to produce accurate reports.
- 4.4. The auditor is to provide the Council with a plan for the audit including:

- timing of interim audit visits;
 - final audit visit (within 60 days of being advised that the accounts and annual financial report are available for audit); and,
 - the method to be used to communicate with, and provide advice and information to, the Council.
- 4.5.** The auditor is required to produce two opinions in compliance with section 129(3) of the [Local Government Act 1999](#) and written advice on particular matters arising from the audit, in compliance with section 129(4).
- 4.6.** Prior to handing over a final audit management letter (see Section 6 below) the auditor is to discuss the proposed contents of the letter with senior management and thereafter at a meeting of the Council's Audit Committee or the Council itself.

The disclosure of methodology is to ensure that there are no gaps in expectations between the auditor and the Council as to the process. This will provide Council with an indication of the timing of the audit and an assurance that the work program, which should be agreed between Council and the auditor, is sufficient for Council's requirements.

When establishing the timetable for the audit, Council should note that in an election year it is suggested that, for practical purposes, the deadline for completion of an annual report by the Council should be one month earlier than required by [the Act](#).

5. Critical Matters to be Audited

Council is of the view that the following matters are important to the proper maintenance and reporting of its financial statements. They are also important to the auditor's responsibility for providing the audit opinions and the written advice required by subsections 129(3) and (4) of the [Local Government Act 1999](#). The auditor should include in his or her proposal the extent to which the matters outlined below will be examined in the course of forming his or her independent audit opinions of the annual financial reports and the internal financial controls of the [*insert name*] Council.

- 5.1. Governance and Control**
- a) Roles and Responsibilities
 - b) Delegated Authorities
 - c) Council/Committee Minutes and Directions
 - d) Strategic/Business/Risk Planning
 - e) Budget Management
 - f) Internal Controls including ICT Security
- 5.2. Financial Accounting and Reporting**
- a) Income
 - Rates revenue
 - Government grants
 - User pays revenue
 - Profit on sale of non-current assets
 - Other income

- b) Expenses
 - Salaries and wages
 - Depreciation
 - Materials and contracts
 - Loss on sale or revaluation of non-current assets
 - Insurances
 - Bad debts
 - Other expenses
- c) Current Assets
 - Cash at bank and short term investments
 - Receivables and prepayments
 - Inventories
- d) Non-Current Assets
 - Property, plant, furniture and equipment
 - Infrastructure and accumulated depreciation thereon
 - Other receivables
- e) Liabilities (current and non-current)
 - Creditors and accruals
 - Borrowings
 - Provisions for employee entitlements
- f) Other
 - Statement of changes in equity
 - Disclosure of contingent liabilities
 - Disclosure of capital commitments
 - Accounting policies and notes to the financial statements
 - Cash Flow Statement
 - Financial Indicators¹⁸ as set out in the Model Financial Statements

These are critical areas that would be the subject of review by the auditor. It would be expected that there would be a work program for each area and that sufficient time would be allowed in the audit fee to properly address each area. The areas should be reviewed with reference to the level of risk attached to each and the likelihood of errors and incorrect statements occurring. The consequences of any errors occurring should also be taken into consideration in the determination of the amount of work that is required for this activity.

6. Audit Management letter – reporting on the findings of an interim Audit and a final Audit

Without limiting the scope and application

[of ASA260 – “Communication of Audit Matters with Those Charged With Governance”](#)

Council requires that the auditor shall promptly after the conclusion of both the interim audit or a final audit (in compliance with section 129(4) of the [Local Government Act 1999](#)) provide to the Principal Member of the Council, the Council's Audit Committee and the Chief Executive Officer a management letter outlining the audit findings in relation to the following matters where such matters are material:

¹⁸ See Local Government Financial Sustainability Information Paper No. 9: *Financial Indicators* at <http://www.lga.sa.gov.au/goto/fsp>

- 6.1.** Any significant adverse trends in the financial performance, financial position or financial management practices of the Council and any material irregularities in the Council's accounting practices or in the management of the Council's financial affairs identified during the course of the audit. Where management has taken steps to correct or improve the financial performance, financial position, financial management practices, accounting practices or management of the Council's financial affairs, the auditor must comment on the efficacy of the correction or improvement.
- 6.2.** The appropriateness of the valuation and depreciation methodologies being used in respect of infrastructure assets. Depreciation is a significant component of a Council's operating expenses and any errors in the way in which depreciation is calculated can have a material impact on the calculation of a Council's operating surplus or deficit. The auditor also needs to ensure that useful lives and residual values of infrastructure are realistic.
- 6.3.** The extent to which the internal control environment has been assessed as set out in the audit plan and any material weaknesses in the control environment, based on the application of auditing standard [ASA 315](#) (*Identifying and Assessing the Risks of Material Misstatement through Understanding the Entity and Its Environment*) and other relevant auditing standards. Where weaknesses have been identified and management has proposed or adopted remedial action to rectify the weaknesses, the auditor must comment on the efficacy of the proposed or adopted course of action. Where weaknesses have not been addressed the auditor must make recommendations for addressing the weaknesses.
- 6.4.** Whether the Council, through its Audit Committee, is regularly monitoring and assessing the adequacy and effectiveness of its risk management framework and activities.
- 6.5.** Where the Council or management have requested that a specific activity, function or operation of the Council be reviewed during an audit, the auditor must report on the scope of the review, its findings and any recommendations in relation to the activity, function or operation of the Council.
- 6.6.** Where an Auditing Standard requires that the auditor must give consideration to the reporting of specific matters to those charged with governance, the auditor must comply with the Auditing Standard and report as necessary.
- 6.7.** The auditor must report on the outcome of any remedial action taken by the Council as a result of previous reports. Specific attention must be drawn to situations where the remedial action is not adequate, including the failure to implement remedial action.
- 6.8.** Where it becomes apparent to the auditor that the Council has failed to comply with relevant legislation, the auditor must report on significant failures and any remedial action proposed or adopted by management to rectify non-compliance.
- 6.9.** Where, during the course of an audit, it becomes apparent that management has failed to comply with Council policies, the auditor must report on significant non-compliance and any action proposed or adopted by management to rectify non-compliance with the Council's policies.

- 6.10.** The requirements set out above do not limit the scope of the auditor's report and the auditor must report on any other matter that in the auditor's judgment may have an impact on good governance and the sound management of the Council's affairs.

7. Hours, Fees and Expenditure

The auditor is to provide the following detail:

- a) an estimate of the hours to be spent on the audit;
- b) fees for completing the audit in accordance with this specification;
- c) the nominated auditor and registered company audit number; and,
- d) the experience of the nominated auditor in completing Local Government audits.

The auditor may be asked to provide a fee basis for any additional work permitted under section 130A of the [Local Government Act 1999](#), or under sub-regulation 22 (2) of the [Local Government \(Financial Management\) Regulations 2011](#). (See auditor independence below).

8. Terms and Conditions

The following conditions should be noted by auditors:

- a) The auditor shall not sub-contract to a third party without Council approval.
- b) The auditor shall not, and has no right to, assign the audit contract to third parties.
- c) The auditor shall not be engaged by the Council to undertake any financial and accounting work that results in financial information that will be the subject of the annual audit.
- d) The auditor shall confirm that he or she has, and will maintain during the duration of the audit term, professional indemnity insurance covering the legal liability arising out of any neglect, default, error, or omission of at least ***[insert amount (\$5m recommended)]*** in aggregate or ***[insert amount (\$1m - \$2m recommended)]*** on an "each and every claim" basis with a two year run-off, plus public liability insurance to a minimum of \$10m.

Council should consult with [Local Government Risk Services](#) on the amounts of professional indemnity and public liability insurance that are appropriate to its own circumstances.

The overriding requirement is that the auditor's independence is not compromised. Accordingly, regulation 22 of the [Local Government \(Financial Management\) Regulations 2011](#) prohibits the auditor providing services to the Council outside the scope of the auditor's functions under the Act. Thus, it is prohibited for the auditor to help prepare the financial statements and then audit them.

It is recommended that the audit tender canvass a wide field of candidates either by an advertisement in the press or a selective tender process.

9. Termination of Appointment

The appointment as auditor is terminated if:

- a) the auditor (being a natural person) dies;
- b) the auditor ceases to be a registered company auditor;
- c) the auditor is a disqualified person under Section 128 (6) of the [Local Government Act 1999](#);
- d) the auditor otherwise ceases to be eligible for appointment as auditor;
- e) the auditor accepts remunerated office or employment from the Council;
- f) the auditor resigns by notice in writing to Council;
- g) Council serves notice in writing to the auditor terminating the appointment for reasonable cause;
- h) the term of the appointment expires.

10. Auditor Independence

Pursuant to regulation 22(5) of the [Local Government \(Financial Management\) Regulations 2011](#), the auditor is required, annually, to provide a declaration that he/she is independent of Council and nothing has transpired that would compromise his or her independence during the conduct of the audit.

This is an important aspect of the auditor's role. Independence is key to the confidence with which the audit is undertaken. This certification provides positive assurance of independence. Regulation 22(5) of the [Local Government \(Financial Management\) Regulations 2011](#) sets out the format of the auditor's declaration of independence, which is in line with industry standards.

To comply with Regulation 22, the auditor is precluded from having any involvement in the preparation of the financial statements, or in advising on other issues such, employee recruitment, litigation support, internal audit or general or IT consulting.

The only permitted activities for a Council's auditor, additional to the annual audits of the financial statements and the internal financial controls, are:

- *a possible role in conducting an efficiency and economy audit pursuant to section 130A of the [Local Government Act 1999](#). See Information Paper No. 5, **Efficiency and Economy Audits**; at <http://www.lga.sa.gov.au/goto/fsp> and/or*
- *certifying that a grant or subsidy received by the council has been acquitted in accordance with any conditions required by the provider of the grant or subsidy. See sub regulation 22(2) of the [Local Government \(Financial Management\) Regulations 2011](#).*

In the past, Councils sometimes looked to their auditor for "value added" services in their audit tender specifications. This had the tendency to blur the auditor's role and risked compromising the auditor's function. Councils must look to other professional advisers for these additional services.