

12 May 2021

Mr. Ashley Lindsay
General Manager
Clarence Valley Council
Locked Bag 23
GRAFTON NSW 2460

Dear Ashley

REVIEW OF COUNCIL'S ELIGIBILITY TO PAY WATER FUNCTION DIVIDENDS

We have completed our review of your compliance with the eligibility criteria set out in the NSW Department of Planning, Industry and Environment - Water (DPIEW) "Best practice management of water supply and sewerage" Guidelines (Guidelines), to determine if Clarence Valley Council ("the Council") can declare a dividend from its water function for the year ended 30th June 2020.

Council's Responsibility

Council is responsible for ensuring compliance with the dividend eligibility criteria set out in the Guidelines for the year ended 30 June 2020.

Auditor's Responsibility

Our responsibility is to express a conclusion on whether anything has come to our attention that would indicate Council has not met the eligibility criteria to pay a dividend in accordance with the Guidelines for the year ended 30 June 2020.

We have conducted the review in accordance with Australian Assurance Standards (ASAE 3000 Assurance engagements other than the audit or review of historical financial information and ASAE 3100 Compliance Engagements) to provide limited assurance that Council has met the eligibility criteria set out in the Guidelines to pay a dividend from its water and sewer functions.

The core requirements of the compliance audit are to review whether Council has met the required outcomes set out on pages 22 to 26 of the Guidelines. The requirements include:

- That the Strategic Business Plan (SBP) met the criteria as set out in the Guidelines;
- That a 30-year financial plan (using DPIEW financial modelling – FINMOD) has been established and the forward cost estimates have been determined to assess whether the minimum water charges and other incomes meet future costs;
- That the documented pricing and developer charges comply with the Guidelines;
- That a Development Servicing Plan (DSP) has been established, including an assessment of water supply developer charges;
- That complying tariffs or dual water supplies (if applicable) have been established;
- That Council has implemented a water conservation and demand management process;
- That Council has created a drought management plan and related processes;
- That the level of annual performance reporting for the water fund over the past two years to ratepayers and the public, including Key Performance Indicators (KPI's) measured against the strategic business plan, has been adequate; and

- That Council has completed an Integrated Water Cycle Management (IWCM) evaluation and strategy.

The DPIEW also requires an opinion on whether the overhead allocation charge from Council's general fund to the Water funds is "fair and reasonable". Therefore, we have reviewed the methodology for the overhead allocation for the Water Fund. We have also reviewed the administration charge estimate to actual cost comparison to assess whether the actual expenses are in line with estimated activity.

The review involved performing procedures to obtain evidence about Council's compliance with the dividend eligibility criteria. The procedures selected depend on the auditor's judgement, including the assessment of assessing compliance with the dividend eligibility criteria, in all material respects. In making those assessments, the auditor considers internal controls relevant to the Council's compliance with dividends eligibility criteria, but not for the purpose of expressing an opinion on the effectiveness of the Council's internal control.

Consequently, this report only includes matters, which have come to our attention during testing as a result of these review procedures and, therefore, does not necessarily confirm the effectiveness of all the internal controls operated by Council for achieving all management objectives.

Conclusion

Based on our review, which is not an audit, except for the issues regarding the Integrated Water Cycle Management outlined in the attached report and below, we consider Council complies, in all material respects, with the dividend eligibility criteria of the Guidelines for the year ended 30 June 2020. Therefore, Council, after receiving formal approval, will be able to make payment of a dividend being the lesser of 50% of the fund's surplus for the 2020 financial year or \$27 per rateable assessment. Council has advised this would equate to approximately \$609,741 (\$27 per rateable assessments of 22,583) from the Water fund.

We attach audit report on your dividend eligibility that can be forwarded to the DPIEW.

Areas for Management Attention

From the conduct of the review, we note the following specific areas that provide an opportunity for management to improve the reliability of information, increase controls and reduce future risks that might cause Council to be ineligible for dividends in future years. These are referred to you for attention and appropriate action.

Integrated Water Cycle Management (IWCM)

We advise that the Integrated Water Cycle Management (IWCM) was adopted in the 2009 year and is presently outside of the eight-year period for renewal as recommended by the Guidelines. We have been informed and obtained correspondence that DPIEW is aware of the delay in the IWCM renewal and has recommended this is deferred until yield modelling is completed as outlined in the DPIEW North Coast Regional Water Strategy. Council has presently engaged external consultants to now commence demand assessments as one of the first stages of the revised IWCM as well as the secure

yield analysis. As a result, we understand DPIPEW will accept Council is entitled to a dividend for the year ended 30 June 2020 as it has materially complied with the Guidelines.

We have reported this in the attached audit report. Although we consider the DPIPEW will accept the delayed IWCM renewal, there is a risk Council maybe declined from declaring a dividend.

We also recommend that Council continues to keep DPIPEW fully informed on the progress of the renewed IWCM and seek formal agreement that the delay in renewal will not impact on dividend eligibility for the 2021 financial year.

Asset management processes (Repeat issue)

The SBP, Long Term Financial Plan (LTFP), Asset Management Plans (AMP's) and IWCM documents for the water and sewer functions rely heavily on Council's asset management process to identify future infrastructure needs including renewals, maintenance, and augmentation.

As reported previously, we found that Council's asset data is spread across various sources including hardcopy asset manuals (e.g. treatment works and pump stations), maintenance software, computer spreadsheets, GIS mapping and the Technology One asset register. It is therefore difficult to assess the critical asset issues including required maintenance, condition and age risks. Further, there is no clear audit trail between the SBP, WLFP, AMP and IWCM and underlying asset records.

WE understand that, Council plans to go live with a new fully integrated Corporate Enterprise System from 1 July 2021. This system includes a works order and project management system that will capture all expenditure on an individual asset whether it be of an operating or capital nature. There is also the ability to capture on-going condition data. Over time this will build data to better inform the strategic Asset Management Plan. In the meantime, a full review of the Asset Management Plan and Asset Register attributes is being carried out to develop a rolling capital works program.

Given Council's desire to obtain dividends each year it will be increasingly important for Council to refine and capture its asset data and improve its systems. This will allow improved audit trails and justification for estimating asset maintenance, renewal and augmentation needs in the future.

We recommend that Council continue to develop its asset management systems so that it can capture all the various data sources including maintenance work conducted, GIS, condition inspections, etc. The system should then provide "automated" asset risk assessed ranking regarding asset renewal and maintenance to flow into Council's IWCM, SBP, LTFP and AMPs.

Council's Long-Term Financial Plans (LTFP) (Repeat issue)

The forecast period in the Council LTFP (which includes water operations) is for a period of 10 years but the Guidelines advise the LTFP for water and sewer functions should have forecasts for a period of 30 years.

We have been advised that a future release of the LG Solutions LTFP product will allow Council's to model for more than 10 years. Therefore, we suggest that in the future, Council's LTFP forecast period should be extended to 30 years to allow Council to clearly demonstrate that the LTFP meets the Guidelines and aligns with FINMOD forecasts.

Water AMP (Repeat issue)

As reported previously, within the AMP for the water function, there is a section on required maintenance. The wording within this section includes examples of required maintenance related to roads and other infrastructure but not specific examples related to the water function.

We were informed, a full review of the Asset Management Plan and Asset Register attributes is being carried out by 30 June 2022.

We recommend the Water AMP is modified with specific examples of required maintenance for water infrastructure, to improve user understanding and relevance.

Update on risks identified in our previous report

- Water Access Licence – the current Nymboida headworks (weir and pipeline plus associated water access and works approval licences) are owned and maintained by Essential Energy and were previously utilised by them as part of their hydro-electricity operations. Electricity generation has not been undertaken since 2013. Council is currently in negotiations with Essential energy regarding future ownership, operation and maintenance of the water infrastructure.

Negotiation with Essential Energy and still in progress. This includes carrying out inspections and determining valuations.

- Improvement in infrastructure modelling of required maintenance, asset renewal and back log works requirements – Changes in modelling assumptions and improvement in asset data will continue to modify the definition and calculation of results associated with required maintenance, backlog and renewal works. This will then have impacts on the LTFP, AMPs, SBP and IWCM outcomes.

Council is making a significant long-term investment in a new Corporate Enterprise System and corporate structure to provide the necessary data and resources for prudent strategic asset planning and actions.

- Changes in expected service level due to government regulation – It is expected the Department of Health will continue to suggest and impose additional water treatment processes to reduce risks associated with water quality, including risks from micro-biological hazards.

In the 2020-21 financial year Council has been working on a masterplan which includes a future upgrade of the Rushforth Road water treatment plant. Council estimates the likely construction timeframe is within the next five years. This has been foreshadowed in various Council reports. Very preliminary financial modelling (FINMOD) has been undertaken to determine the impact on the pricing path (which was minimal) but until we have the ballpark budget estimate we have not refined the modelling.

Finalisation of dividend claim for the 2020 financial year

As per the DPIEW guidelines, Council will need to complete the following before transferring the funds from the water function to the general fund:

- Complete the submission forms to DPIEW and attach our audit review report and copy of signed Special Purpose Financial Statements;
- Prepare dividend declaration resolution and have this formally adopted by Council at a Council meeting; and

- Submit submission, including copy of council resolution, to DPIEW for approval.

Once DPIEW provides formal response, Council can then make the necessary dividend payment for the 2020 year.

Please note that the submission needs to be made before 30th June 2021. Therefore, your urgent attention is recommended.

If you have any questions regarding the matters raised above, please do not hesitate to contact me.

Yours sincerely



**Paul Cornall
Principal**

INDEPENDENT REVIEW REPORT TO CLARENCE VALLEY COUNCIL AND NSW DEPARTMENT OF PLANNING, INDUSTRY AND ENVIRONMENT- WATER

Report on the Clarence Valley Council compliance with the Dividend eligibility criteria set out in the NSW Department of Planning, Industry and Environment - Water "Best Practice Management of Water Supply and Sewage Guideline".

We have reviewed the Clarence Valley Council ("the Council") compliance with the Dividend eligibility criteria established by NSW Department of Planning, Industry and Environment- Water (DPIEW) for the year ended 30 June 2020 in relation to its Water function.

Council's Responsibility

Council is responsible for ensuring compliance with the dividend eligibility criteria set out in the DPIEW Water Best Practice Management of Water Supply and Sewerage Guidelines ("the Guidelines") for the year ended 30 June 2020.

Auditor's Responsibility

Our responsibility is to express a conclusion on whether anything has come to our attention that would indicate Council has not met the eligibility criteria to pay a dividend in accordance with the Guidelines for the year ended 30 June 2020.

We have conducted the review in accordance with Australian Assurance Standards (ASAE 3000 Assurance engagements other than the audit or review of historical financial information and ASAE 3100 Compliance Engagements) to provide limited assurance that Council has met the eligibility criteria set out in the Guidelines to pay a dividend from its water function.

The core requirements of the compliance audit whether that Council has met the required outcomes set out on pages 22 to 26 of the Guidelines. The requirements reviewed were:

- That the strategic business plan met the criteria as set out in the Guidelines;
- That a 30-year financial plan has been established and the forward cost estimates have been determined to assess whether the minimum water and sewer charges and other incomes meet future costs;
- That the documented pricing and developer charges comply with DPIEW requirements;
- That a Development Servicing Plan has been established, including an assessment of water supply and sewerage developer charges;
- That complying tariffs or dual water supplies (if applicable) have been established;
- That Council has implemented a water conservation and demand management process;
- That Council has created a drought management plan and related processes;
- That the level of annual performance reporting for water function over the past two years to ratepayers and the public, including Key Performance Indicators (KPI's) measured against the strategic business plan has been adequate; and
- That Council has completed an Integrated Water Cycle Management evaluation and strategy.

The DPIEW also requires an opinion on whether the overhead allocation charge from Council's general fund to the Water Fund are "fair and reasonable". Therefore, we have reviewed the methodology for the overhead allocation for the Water Funds. We have also reviewed the administration charge estimate to actual cost comparison to assess whether the actual expenses are in line with estimated activity.

Due to the inherent limitations of conducting the review of the dividend eligibility criteria, it is possible that fraud, error, or non-compliance may occur and not be detected. A review is not designed to detect all instances of non-compliance with the dividend eligibility criteria as the review is not performed continuously throughout the year ended 30 June 2020 and procedures performed to test compliance with the dividend eligibility criteria are undertaken on a test basis and involve enquires with management, observing documents provided and other review procedures. The review conclusion expressed in this report has been formed on the above basis.

Due to the inherent limitations of a review engagement, together with the inherent limitations of internal control, there is an unavoidable risk that some material non-compliance may not be detected, even though the review is properly planned and performed in accordance with Australian Assurance Standards.

This report has been prepared specifically for the DPIEW and for Council for their exclusive use in meeting their dividend eligibility requirements. Neither this report nor its contents may be referred to or quoted in any statement, without the express written approval of Forsyths Chartered Accountants. We disclaim any assumption of responsibility for any reliance on this report, or on Council's statement of compliance to which it relates, to any person or for any other purpose than that for which it was prepared.

We believe that the evidence we have obtained is sufficient and appropriate to provide a basis for our conclusion.

Conclusion

Based on our review, which is not an audit, except for the matter noted in the findings below, nothing has come to our attention that causes us to believe that Council has not complied, in all material respects, with the dividend eligibility criteria of the DPIEW Guidelines for the year ended 30 June 2020 in relation to dividends from the Water Function.

Findings – Integrated Water Cycle Management

We advise that the Integrated Water Cycle Management (IWCM) was adopted in the 2009 year and is presently outside of the eight-year period for renewal as recommended by the Guidelines. We have been informed and obtained correspondence that DPIEW is aware of the delay in the IWCM renewal and has recommended this is deferred until yield modelling is completed as outlined in the DPIEW North Coast Regional Water Strategy. Council has presently engaged external consultants to now commence demand assessments as one of the first stages of the revised IWCM as well as the secure yield analysis. As a result, we understand DPIEW will accept Council is entitled to a dividend for the year ended 30 June 2020 as it has materially complied with the Guidelines. Our opinion is not modified in respect of this matter.

Forsyths

Forsyths Business Services Pty Limited



Paul R Corriall
Principal

121 Rusden Street, Armidale

12 May 2021