# MINUTES

# AUDIT AND RISK COMMITTEE

## 25 MAY 2015

APPROVED FOR RELEASE

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GARY STEVENSON PSM
CHIEF EXECUTIVE OFFICER

CITY of PERTH

# MINUTES

# AUDIT AND RISK COMMITTEE

## 25 MAY 2015

**THESE MINUTES ARE HEREBY CERTIFIED AS CONFIRMED**

**PRESIDING MEMBER'S SIGNATURE**

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**DATE:** 22.2.2016

# AUDIT AND RISK COMMITTEE

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Minutes of the meeting of the City of Perth **Audit and Risk Committee** held in Committee Room 1, Ninth Floor, Council House, 27 St Georges Terrace, Perth on **Monday, 25 May 2015**.

## MEMBERS IN ATTENDANCE

| | | |
|---|---|---|
| Cr Davidson | - | Presiding Member |
| Cr Butler | | |
| Cr Harley | | |
| Mr Linden | - | Independent Member |

## OFFICERS

| | | |
|---|---|---|
| Mr Stevenson | - | Chief Executive Officer |
| Mr Mianich | - | Director Corporate Services |
| Mr Richards | - | Manager Finance |
| Mr White | - | Chief Accountant |
| Mr Cheldi | - | Internal Auditor |
| Ms Mendoza | - | Assistant Internal Auditor |
| Ms Honmon | - | Governance Officer |

## GUESTS AND DEPUTATIONS

Nil

## AR17/15 DECLARATION OF OPENING

**4.30pm** The Presiding Member declared the meeting open.

## AR18/15 APOLOGIES AND MEMBERS ON LEAVE OF ABSENCE

Nil

## AR19/15 QUESTION TIME FOR THE PUBLIC

Nil

## AR20/15 CONFIRMATION OF MINUTES

***Moved by Cr Butler, seconded by Cr Harley***

***That the minutes of the meeting of the Audit and Risk Committee held on Monday, 23 February 2015 be confirmed as a true and correct record.***

***The motion was put and carried***

**The votes were recorded as follows:**

**For: Crs Davidson, Butler, Harley and Mr Linden**

**Against: Nil**

## AR21/15 CORRESPONDENCE

Nil

## AR22/15 DISCLOSURE OF MEMBERS' INTERESTS

Nil

## AR23/15 MATTERS FOR WHICH THE MEETING MAY BE CLOSED

The Presiding Member advised that in accordance with Section 5.23(2) of the *Local Government Act 1995*, the meeting will be required to be closed to the public prior to discussion of the following:

| Confidential Item / Schedule No. | Item No. and Title. | Reason |
|---|---|---|
| Confidential Item AR24/15 and Schedule 1 | City of Perth Internal Audit Plan 2015/16 | Section 5.23(2)(f)(i) |
| Schedule 3 | Item AR26/15 – City of Perth Internal Audit – Outstanding Recommendations May 2015 | Section 5.23(2)(a) |
| Schedule 4 | Item AR27/15 – City of Perth Internal Audit – Cash Handling Review | Section 5.23(2)(a) |

| Confidential Item / Schedule No. | Item No. and Title. | Reason |
|---|---|---|
| Schedule 5 | Item AR28/15 – City of Perth Internal Audit 2014/15 – Human Resources Review | Section 5.23(2)(a) |

Confidential reports and schedules are distributed to Members under separate cover.

## MOTION TO CLOSE THE MEETING

***Moved by Cr Butler, seconded by Cr Harley***

***That the Audit and Risk Committee resolves to close the meeting to the public to consider Confidential Item AR24/15 in accordance with Section 5.23(2) of the Local Government Act 1995.***

***The motion was put and carried***

**The votes were recorded as follows:**

**For:** **Crs Davidson, Butler, Harley and Mr Linden**

**Against:** **Nil**

**4.33pm** The meeting was closed to the public with no members of the public in attendance.

## AR25/15 CONFIDENTIAL ITEM – CITY OF PERTH INTERNAL AUDIT PLAN 2015/16

**BACKGROUND:**

| | |
|---|---|
| FILE REFERENCE: | P102969-8 |
| REPORTING UNIT: | Internal Audit |
| RESPONSIBLE DIRECTORATE: | Corporate Services |
| DATE: | 14 May 2015 |
| MAP / SCHEDULE: | Confidential Schedule 1 – City of Perth Internal Audit Plan 2015/16 |

**In accordance with Section 5.23(2)(f)(i) of the *Local Government Act 1995*, this confidential item was distributed to the Members under separate cover.**

**Confidential Item AR24/15 and Confidential Schedule 1 is bound in Consolidated Committee Confidential Minute Book Volume 1 2015.**

***Moved by Mr Linden, seconded by Cr Butler***

***That Council approves the City of Perth Internal Audit Plan 2015/16 attached as Schedule 1.***

***The motion was put and carried***

**The votes were recorded as follows:**

**For:** **Crs Davidson, Butler, Harley and Mr Linden**

**Against:** **Nil**

## MOTION TO RE-OPEN THE MEETING

***Moved by Cr Butler, seconded by Cr Harley***

***That the Audit and Risk Committee resolves to re-open the meeting to the public.***

***The motion was put and carried***

**The votes were recorded as follows:**

**For:** **Crs Davidson, Butler, Harley and Mr Linden**

**Against:** **Nil**

**4.53pm** The meeting was re-opened to the public with no members of the public returning the meeting.

## AR26/15 CORRUPTION AND CRIME COMMISSION REPORT ON MISCONDUCT RISK IN LOCAL GOVERNMENT PROCUREMENT

**BACKGROUND:**

| | |
|---|---|
| FILE REFERENCE: | P1013788-5 |
| REPORTING UNIT: | Internal Audit |
| RESPONSIBLE DIRECTORATE: | Corporate Services |
| DATE: | 31 March 2015 |
| MAP / SCHEDULE: | Schedule 2 – Corruption and Crime Commission Report on Misconduct Risk in Local Government Procurement |

The Corruption and Crime Commission (CCC) Report on Misconduct Risk in Local Government Procurement was tabled in State Parliament on 26 February 2015.
This Council report serves as a summary of the key points of discussion within the CCC report.

**LEGISLATION / STRATEGIC PLAN / POLICY:**

| | |
|---|---|
| **Legislation** | *Local Government (Audit) Amendment Regulations 2013* |
| **Integrated Planning and Reporting Framework Implications** | **Corporate Business Plan**<br>Council Four Year Priorities: Community Outcome<br>Capable and Responsive Organisation<br>A capable, flexible and sustainable organisation with a strong effective governance system to provide leadership as a capital city and deliver efficient and effective community centred services. |
| **Policy**<br>Policy No and Name: | 19.1 – Enterprise Risk Management |

**DETAILS:**

An analysis of the CCC Report on Misconduct Risk in Local Government has been carried out. This analysis has identified that the key points of discussion within the report are as follows:

- Misconduct risks for local governments in Western Australia. A description is provided on the nature and extent of risks of misconduct arising from procurement.
- Specific CCC investigation case studies (six cases in total) on procurement activities involving local government (does not include the City of Perth) and lessons from these investigations.

- A summary of the RSM Bird Cameron Procurement Audits carried out at five local governments including the City of Perth.
- Recommendations for proper oversight of procurement by local governments.

The RSM Bird Cameron Procurement Audit is only discussed in pages 13 to 15 within the CCC report. This discussion is centred on the key finding of this audit being that the five local governments subjected to review had not undertaken an assessment to determine their specific fraud and misconduct risks. Discussion also comprised what the five local governments have done post-audit to address weaknesses in their financial governance systems.

It should be noted that the City of Perth has now completed a fraud and misconduct risk assessment which addresses the above mentioned key finding. This risk assessment was undertaken by the City's Risk Management Coordinator and presented to City of Perth Audit and Risk Committee meeting at its meeting held on 23 February 2015. The City has also addressed the majority of findings from the RSM Bird Cameron Procurement Audit. Two findings remain outstanding, however, it is considered that these findings are not significant and plans are in place to address the relevant issues.

Two recommendations for proper oversight of procurement by local governments have been made by the CCC in its report as follows:

**"*Section 5.1 [94]: The Commission recommends that the jurisdiction of the Auditor General be extended to include local governments.***

*In the Commission's view an appropriate way to ensure external oversight of financial governance in procurement by local governments would be to extend the jurisdiction of the Auditor General to specifically include local governments. This would align the local government sector with the State Government sector*." (Refer to page 21 of CCC report – Schedule 2[1]).

**"*Section 5.1 [100]: The Commission recommends that the Department of Local Government and Communities actively oversights risk management reviews prepared by local governments pursuant to the Local Government (Audit) Regulations 1996 to ensure that they include appropriate assessment of misconduct risks arising from procurement, and mechanisms for reducing those risks".***

*The Commission considers that the legislative and policy requirements for local governments to assess misconduct risks and develop a plan for mitigating those risks, should be subject of active oversight by the Department of Local Government and Communities, particularly in relation to the risks of misconduct arising from procurement*." (Refer to page 22 of CCC report – Schedule 2[2]).

[1] [2] Administrative correction: Incorrect references shown in the agenda of "Confidential Schedule 3" corrected to "Schedule 2".

**FINANCIAL IMPLICATIONS:**

There are no financial implications related to this report.

**COMMENTS:**

The CCC report has reiterated the risks associated with procurement in local government and the requirement for individual local governments to maintain adequate purchasing processes and controls.

If implemented above mentioned recommendations for external oversight will provide the State Government with a means for evaluating the adequacy of controls and risk management plans developed by local governments in relation to procurement.

***Moved by Cr Harley, seconded by Cr Butler***

***That Council receives the report titled "Corruption and Crime Commission Report on Misconduct Risk in Local Government Procurement".***

***The motion was put and carried***

**The votes were recorded as follows:**

**For: Crs Davidson, Butler, Harley and Mr Linden**

**Against: Nil**

## AR27/15 CITY OF PERTH INTERNAL AUDIT – OUTSTANDING RECOMMENDATIONS MAY 2015

**BACKGROUND:**

| | |
|---|---|
| FILE REFERENCE: | P1029698 |
| REPORTING UNIT: | Internal Audit |
| RESPONSIBLE DIRECTORATE: | Corporate Services |
| DATE: | 11 May 2015 |
| MAP / SCHEDULE: | Confidential Schedule 3 – Outstanding Recommendations – May 2015 |

**Confidential Schedule 3 is bound in Consolidated Committee Confidential Minute Book Volume 1 2015.**

**LEGISLATION / STRATEGIC PLAN / POLICY:**

| | |
|---|---|
| **Legislation** | *Local Government (Audit) Amendment Regulations 2013* |
| **Integrated Planning and Reporting Framework Implications** | **Corporate Business Plan**<br>Council Four Year Priorities: Community Outcome<br>Capable and Responsive Organisation<br>A capable, flexible and sustainable organisation with a strong effective governance system to provide leadership as a capital city and deliver efficient and effective community centred services. |
| **Policy**<br>Policy No and Name: | 19.1 – Enterprise Risk Management |

**DETAILS:**

Internal audit recommendations to improve controls are followed up with relevant staff to ensure agreed action is being taken to address identified control weaknesses. Where it is confirmed that agreed action has taken place the recommendation is considered to be closed. A recommendation is considered to be outstanding where agreed action has yet to be completed.

This report provides a summary on the status of outstanding internal audit recommendations as at May 2015.

As at May 2015 two internal audit recommendations remain outstanding as per the attached Confidential Schedule 3 which provides a summary of the recommendation, action plan to address the issue, person(s) responsible for implementing the action, target date for completion of action as well as current status of required action to address the issue.

**FINANCIAL IMPLICATIONS:**

There are no financial implications related to this report.

**COMMENTS:**

Provision of this report facilitates the monitoring of progress of action to address the outstanding internal audit recommendations from prior internal audits carried out.

Recommendations contained within internal audit reports presented in the May 2015 Audit and Risk Committee meeting will be followed up with relevant staff and the status of outstanding recommendations from these reports will be reported in the next Audit and Risk Committee meeting.

***Moved by Mr Linden, seconded by Cr Butler***

***That the Audit and Risk Committee receives the report titled "City of Perth Internal Audit – Outstanding Recommendations May 2015" and as detailed in Confidential Schedule 3.***

***The motion was put and carried***

**The votes were recorded as follows:**

**For: Crs Davidson, Butler, Harley and Mr Linden**

**Against: Nil**

## AR28/15 CITY OF PERTH INTERNAL AUDIT 2014/15 – CASH HANDLING REVIEW

**BACKGROUND:**

| | |
|---|---|
| FILE REFERENCE: | P102969-8 |
| REPORTING UNIT: | Internal Audit |
| RESPONSIBLE DIRECTORATE: | Corporate Services |
| DATE: | 4 May 2015 |
| MAP / SCHEDULE: | Confidential Schedule 4 – City of Perth Cash Handling Review |

**Confidential Schedule 4 is bound in Consolidated Committee Confidential Minute Book Volume 1 2015.**

The City of Perth Internal Audit Plan 2014/15 was approved by Council at its meeting held on **22 October 2014**.

As part of the City's 2014/15 Internal Audit Plan, a review of key controls and practices in regards to cash handling was carried out between March and April 2015. Confidential Schedule 4 details the findings of this audit.

**LEGISLATION / STRATEGIC PLAN / POLICY:**

| | |
|---|---|
| **Legislation** | *Local Government (Audit) Amendment Regulations 2013* |
| **Integrated Planning and Reporting Framework** | **Corporate Business Plan**<br>Council Four Year Priorities: Community Outcome<br>Capable and Responsive Organisation |

**Implications** A capable, flexible and sustainable organisation with a strong effective governance system to provide leadership as a capital city and deliver efficient and effective community centred services.

**Policy**
Policy No and Name: 19.1 – Enterprise Risk Management

**DETAILS:**

The findings of the internal audit are detailed in the attached Confidential Schedule 4[3].

**FINANCIAL IMPLICATIONS:**

There are no financial implications related to this report.

***Moved by Cr Harley, seconded by Cr Butler***

***That Council approves the review of key controls and practices in regards to cash handling as part of the Internal Audit Plan 2014/15 as detailed in Confidential Schedule 4.***

***The motion was put and carried***

**The votes were recorded as follows:**

**For: Crs Davidson, Butler, Harley and Mr Linden**

**Against: Nil**

## AR29/15 CITY OF PERTH INTERNAL AUDIT 2014/15 – HUMAN RESOURCES REVIEW

**BACKGROUND:**

| | |
|---|---|
| FILE REFERENCE: | P102969-8 |
| REPORTING UNIT: | Internal Audit |
| RESPONSIBLE DIRECTORATE: | Corporate Services |
| DATE: | 18 May 2015 |
| MAP / SCHEDULE: | Confidential Schedule 5 – Human Resources Review April 2015 |

[3] Administrative correction: Incorrect schedule number shown in the agenda corrected from “5” to “4”.

**Confidential Schedule 5 is bound in Consolidated Committee Confidential Minute Book Volume 1 2015.**

The City of Perth Internal Audit Plan 2014/15 was approved by Council at its meeting held on **22 October 2014**.

As part of the City's 2014/15 Internal Audit Plan, a review of key controls and practices for dealing with workplace issues was carried out between March and April 2015. Confidential Schedule 5 details the findings of this audit

**LEGISLATION / STRATEGIC PLAN / POLICY:**

| | | |
|---|---|---|
| **Legislation** | *Local Government (Audit) Amendment Regulations 2013* | |
| **Integrated Planning and Reporting Framework Implications** | **Corporate Business Plan**<br>Council Four Year Priorities:<br>**Capable and Responsive Organisation** | |
| | S18 | Strengthen the capacity of the organisation.<br>A capable, flexible and sustainable organisation with a strong and effective governance system to provide leadership as a capital city and deliver efficient and effective community centred services. |
| **Policy** | | |
| Policy No and Name: | 19.1 – Enterprise Risk Management | |

**DETAILS:**

The findings of the internal audit are detailed in the attached Confidential Schedule 5.

**FINANCIAL IMPLICATIONS:**

There are no financial implications related to this report.

***Moved by Cr Butler, seconded by Cr Harley***

***That Council approves the review of key controls and practices for dealing with workplace issues as part of the Internal Audit Plan 2014/15 as detailed in Confidential Schedule 5.***

***The motion was put and carried***

**The votes were recorded as follows:**

**For:** **Crs Davidson, Butler, Harley and Mr Linden**

**Against:** **Nil**

## AR30/15 MOTIONS OF WHICH PREVIOUS NOTICE HAS BEEN GIVEN

Nil

## AR31/15 GENERAL BUSINESS

### Responses to General Business from a Previous Meeting

Nil

### New General Business

Nil

## AR32/15 ITEMS FOR CONSIDERATION AT A FUTURE MEETING

### Outstanding Items:

Nil

## AR33/15 CLOSE OF MEETING

**5.22pm** There being no further business the Presiding Member declared the meeting closed.

# SCHEDULES

# FOR THE MINUTES OF THE

# AUDIT AND RISK

# COMMITTEE MEETING

# HELD ON

# 25 MAY 2015

Audit and Risk Committee
Confidential Schedule 1
(Minute AR24/15 refers)

Distributed to Elected Members under separate cover

Bound in Consolidated Committee

Confidential Minute Book

Volume 1 2015

SCHEDULE 2

# Corruption and Crime Commission

# Report on Misconduct Risk in Local Government Procurement

4 February 2015

# CORRUPTION AND CRIME COMMISSION

Hon. Tony Simpson, MLA
Minister for Local Government
Floor 8, Dumas House
2 Havelock Street
WEST PERTH WA 6005

Dear Minister

***REPORT ON MISCONDUCT RISK IN LOCAL GOVERNMENT PROCUREMENT***

The Corruption and Crime Commission ("the Commission") wishes to make a report to you as Minister pursuant to section 89 of the *Corruption and Crime Commission Act 2003* ("the CCC Act").

This course is available as an alternative to making a report to the Parliament of Western Australia "if, for any reason, the Commission considers it appropriate to do so".

In making this report to you I am seeking to finalise work not completed during the tenure of Commissioner Roger Macknay, QC. Mindful of the need to finalise the body of work which forms the basis of this report and the passage of time, the Commission has determined, after considering the benefits of publication, that this is the appropriate course of action.

The report sets out six case studies relating to Commission investigations, a post investigation review of financial governance at the City of Stirling, and the findings of procurement audits in five metropolitan local governments conducted by RSM Bird Cameron on behalf of the Commission.

The Commission notes that the local governments that were subject of the investigations and audits have taken steps to address identified shortcomings and system weaknesses in order to mitigate their misconduct risks in procurement.

Although some time has passed since the investigations and audits, the Commission has had considerable involvement in local government procurement matters over time and considers that the investigations and audits highlight ongoing misconduct risks for the local government sector. As a consequence the report concludes with two recommendations for action.

The CCC Act provides in section 87(2) that following the making of a report to a Minister, a matter in the report may be disclosed with the approval of the Minister, despite the restrictions on the disclosure of such material set out in section 151 of the CCC Act.

The Commission provides five numbered copies of the report to you, together with a disc containing both a Microsoft Word and PDF version of such.

Yours faithfully

Christopher Shanahan, SC
**ACTING COMMISSIONER**

4 February 2015

# ABBREVIATIONS AND ACRONYMS

| | |
|---|---|
| ABS | Australian Bureau of Statistics |
| (“the CCC Act”) | *Corruption and Crime Commission Act 2003* |
| CEO | Chief Executive Officer |
| ("the Cities") | Cities of Cockburn, Joondalup, Perth, Swan and Wanneroo |
| ("the City") | City of Stirling |
| (“the Commission”) | Corruption and Crime Commission |
| ("the Committee") | Public Accounts Committee, Legislative Assembly, Parliament of Western Australia |
| ICAC | Independent Commission Against Corruption (New South Wales) |
| OAG | Office of the Auditor General |
| OECD | Organisation for Economic Co-operation and Development |
| ("the Parliament") | Parliament of Western Australia |
| ("the Regulations") | *Local Government (Audit) Regulations 1996* |
| ("the report") | RSM Bird Cameron, *Local Government Authorities Procurement Audits, Consolidated Report* |
| SSC | State Supply Commission |
| ("the Town") | Town of Cottesloe |

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# CHAPTER ONE
# PURPOSE AND BACKGROUND

## 1.1 Purpose

[1] The purpose of this report is to:

- describe investigations by the Corruption and Crime Commission ("the Commission") into misconduct in procurement by local governments;
- describe audits carried out on behalf of the Commission into the capacity of five local governments to prevent, identify and deal with misconduct in procurement;
- describe a post-investigation review of financial governance at the City of Stirling;
- identify concerns arising from the investigations, audits and the review; and
- make recommendations about how these concerns may be mitigated.

[2] Broadly, the concerns identified by the Commission are that procurement and financial governance processes used by local governments in Western Australia can leave them vulnerable to fraud, corruption and other forms of misconduct. This is exacerbated by a lack of risk assessment by many local governments in their procurement processes, which in turn means there is a lack of planning about how those risks may be mitigated.

[3] This report is made to the Minister for Local Government pursuant to sections 84 and 89 of the *Corruption and Crime Commission Act 2003* ("the CCC Act").

## 1.2 Background

### 1.2.1 Procurement

[4] "Procurement" means buying goods and services. Goods and services bought by local governments can range from stationery to construction services to computer technology. Procurement can include outright purchase, lease and hire, and contracting for the delivery of goods and services.

### 1.2.2 Misconduct Risks for Local Governments in Western Australia

[5] There are 140 local governments in Western Australia. Thirty of these are located within the Perth metropolitan area. According to the Australian

Bureau of Statistics[1] at June 2013 Western Australia had a population of 2.52 million people of whom 1.97 million (78%) lived in the Greater Perth area.[2]

[6] The local government sector is a unique and diverse area of business activity with particular misconduct risks. Among other services local governments provide infrastructure, building services, health services, community services, waste collection and disposal services, and recreation and cultural facilities.

[7] The diverse functions performed by local governments can create misconduct risks. These include regulatory functions carried out by rangers, health inspectors and building inspectors, functions relating to procurement and tendering and functions relating to planning and building approvals. The misconduct risks associated with those functions include:

- improper influence;[3]
- conflicts of interest;
- abuse of power;
- bribery and corruption;[4]
- fraud; and
- theft.

[8] Research carried out in New South Wales by the Independent Commission Against Corruption (ICAC)[5] and by the Auditors General of Queensland[6] and Victoria[7] support the Commission's concerns about

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[1] Australian Bureau of Statistics (ABS), 1306.5, *Western Australia at a Glance 2014*, available on the ABS Website at http://www.abs.gov.au/ausstats/abs@.nsf/Lookup/1306.5main+features32014, viewed 20 December 2014. Figures for 2013-14 will be released by the ABS on 31 March 2015.

[2] The boundaries for "Greater Perth" used by the ABS are similar, but not identical, to those for "Metropolitan Perth" used by the Department of Local Government and Communities. Both extend from the north boundary of the City of Wanneroo to the south boundary of the City of Mandurah and to the east boundaries of the Cities of Swan, Belmont and Armadale.

[3] The term "improper influence" is used above generically to describe the actions and behaviours of customers intended to improperly affect the outcome of a business activity or process to gain a benefit which they would not otherwise have obtained. Put simply, to divert public officers from fidelity to the public interest because of other personal interests (that is, a way of corruptly influencing a public officer). Improper influence can manifest itself in a number of ways, including: offers of cash and other bribes; an offer of a gift or beneficial "arrangement"; emotional pressure related to personal needs or hardship; intimidation or threats; or a favour on the basis of assumed friendship or associations.

[4] Authorities with a regulatory function have increased risks of bribery and corruption of persons in positions of authority.

[5] Independent Commission Against Corruption (ICAC), *Profiling the NSW Public Sector II – Report 3: Differences Between Local and State Government*, April 2010, p.8.

[6] Auditor General of Queensland, *Results of Audits: Local Government Financial Statements for 2010-11*, Report 2, May 2012, pp.31-39.

misconduct risks in local government. Specifically the research suggests that local governments face a wider range of corruption risks than state government authorities, and many local governments have significant weaknesses in their internal controls, increasing their susceptibility to fraud and corruption.

[9] Local governments in Western Australia vary enormously in size, isolation and complexity. However, in terms of misconduct risk, there are similarities across the sector.

[10] In providing local government services, employees of all levels can exercise significant authority, often with considerable independence. Local government employees often act independently from their administrative centre, and without direct supervision.

[11] In addition, many local government services are delivered in partnership with state and Federal Governments and private sector organisations. Local governments around Western Australia regularly negotiate large scale business developments. These are typically commercial, residential and industrial developments driven by the interests of the private sector, or infrastructure developments driven by government and community needs and, increasingly, also by the private sector.

[12] The financial stakes can be extraordinarily high. Local governments are in the difficult position of engaging with companies that are simultaneously applicants seeking cooperation and approval, and are also good corporate citizens looking to invest in community facilities and infrastructure. There is a risk that the lines between these roles can become blurred, that impartiality is lost and that improper influence may occur.

[13] It is rarely a single weakness within a local government that creates an environment where misconduct can occur. More often, there are a range of factors such as lack of processes, inadequate record keeping, lack of supervision and training, failure to declare gifts and conflicts of interest, and lack of adequate audits and assurance.

[14] On 16 April 2013 the Commission tabled in the Parliament of Western Australia ("the Parliament") a report entitled *Report on the Review of the Capacity of Local Governments in the Pilbara to Prevent, Identify and Deal with Misconduct*. That report considered risks which affect local governments operating in regional and remote areas in addition to those which affect the local government sector as a whole. These include:

- difficulty in attracting and retaining suitable employees;
- a high cost of living;
- close working relationships that naturally develop between the people in local government, the community and private enterprise;

[7] Auditor General of Victoria, *Fraud Prevention Strategies in Local Government*, 2012.

- difficulty in keeping professional and private relationships separate in small towns;
- the increased potential for conflicts of interest in small towns;
- large geographic areas in which to provide services;
- a limited revenue base to provide services to meet diverse community needs; and
- demands from industry and government for infrastructure and services.

[15] In relation to local governments operating in the Perth metropolitan area, in its final report the Metropolitan Local Government Review Panel stated:

> *Collectively, the local governments of Perth are a big business. The 30 metropolitan local governments raised $1.9 billion in operating revenues, including over $957 million in rates in 2010/11, and incurred operating expenditures of $1.7 billion. They engaged over 9,000 full-time equivalent employees and controlled assets of nearly $11 billion. These local governments had borrowings of $295 million and had accumulated reserves of $791 million. The net assets of these communities was $10.3 billion*.[8]

[16] A significant amount of the public money managed by local governments is used to procure a range of goods and services. According to the Metropolitan Local Government Review Panel "materials and contracts" account for 32% of metropolitan local government operating expenditures.[9]

[17] It is recognised world-wide that procurement by government authorities, including local governments, is an activity with a high risk of serious misconduct. In its *Principles for Integrity in Public Procurement* report the Organisation for Economic Co-operation and Development (OECD) stated, “of all government activities, public procurement is also one of the most vulnerable to fraud and corruption”.[10]

[18] The findings of the PwC *Global Economic Crime Survey 2014* were that procurement fraud is the second most commonly reported type of economic crime, after asset misappropriation, and it is a growing threat. Procurement fraud was reported by 29% of respondents globally who had experienced an economic crime.[11] This percentage was 33% in Australia. The Australian report commented "[t]he procurement life cycle is a hotspot

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[8] *Metropolitan Local Government Review, Final Report of the Independent Panel*, by the Metropolitan Local Government Review Panel, July 2012, p.25.

[9] *Ibid*, p.81.

[10] Organisation for Economic Co-operation and Development (OECD), *Principles for Integrity in Public Procurement*, 2009, p.9.

[11] PwC, *Global Economic Crime Survey 2014*, available on the PwC website at http://www.pwc.com/gx/en/economic-crime-survey/, viewed 21 January 2015.

for fraudsters as it serves as one of the primary areas of expenditure for most organisations".[12]

[19] The PwC survey included government agencies as well as private organisations. It found that globally 41% of government respondents to the survey said they had been victims of economic crime.

[20] PwC found that globally overall "56% of fraudsters are on the inside". This was higher for Government enterprises, where it was 60%.

[21] The commentary on the survey in Australia noted that procurement fraud often involves an external and an internal party, and is collusive in nature. "The most effective and lucrative procurement fraud schemes require an internal employee to be involved".

[22] It also commented, in relation to internal employees, "that a focus on preventative measures is a key approach to combatting these fraudsters". It said that reactive measures often occurred too late to be effective.

[23] In relation to economic crimes which were detected "55% of instances were uncovered by internal controls, be they preventative or detective".

[12] *Ibid*, *Territory Insights*, *The Australian Story*, p.13.

# CHAPTER TWO
# COMMISSION INVESTIGATIONS

## 2.1 Commission Investigation Case Studies

[24] The following are summaries of six investigations by the Commission into procurement related misconduct in local governments. They demonstrate a variety of ways in which misconduct in procurement can cause a loss to a local government, to its ratepayers, and to honest suppliers of goods and services.[13]

### 2.1.1 Investigation 1

[25] A Building Coordinator at the City of Stirling colluded with up to seven building contractors over a seven-year period in order to fraudulently obtain financial gains.

[26] The Building Co-ordinator:

- awarded contracts to his uncle's business and conspired to ensure that the relationship was not detected by submitting quotes and invoices to the City of Stirling with incomplete, incorrect or false information;
- authorised payments to his uncle's company for work that was not done, or was done by the Building Coordinator himself during his work hours, or was subcontracted to another company which was also paid for the work;
- directly fabricated quotes himself, or requested contractors to submit fictional quotes; and
- arranged with contractors to submit invoices containing vague descriptions so that the City of Stirling was unable to verify whether work had been completed, and which allowed the contractors to charge for work not done, or to overcharge for work that was done.

[27] The Commission investigation determined that the value of known benefits received by the Building Coordinator from contractors involved in the frauds was in excess of $600,000. The benefits included a Mitsubishi Triton and Toyota Kluger, a bobcat, three tractors, overseas travel, security cameras, a generator, materials and work on an extension to his home and the payment of domestic fees and accounts. In its *Annual Report 2011-2012*, p.41, the City of Stirling reported that it had "successfully recovered $848,000 … [with the funds recovered including] monies associated with the investigation, CCC representation and costs incurred in pursuing the repayment of the misappropriated funds".

[13] All local governments considered in this report have taken steps to improve their financial governance systems relating to procurement.

### Commission Observations

[28] The Commission noted that the Building Coordinator had almost complete control of the procurement processes in relation to maintenance of City of Stirling buildings, including setting budgets, raising orders and approving invoices for payment. The Building Coordinator's supervisor allowed him to operate in an environment of unqualified trust, without commensurate internal controls. There was little scrutiny of tender documents by other employees.

[29] Arising from this investigation the Commission identified a number of issues relating to the City of Stirling's ability to prevent, identify and deal with misconduct during the relevant period. These included:

- inadequate financial management and supervision;
- failure to recognise risks relating to procurement in its Building Operations risk management plan;
- inadequate record keeping; and
- inadequate response to information received which should have aroused suspicions about the actions of the Building Coordinator.

### 2.1.2 Investigation 2

[30] The Commission's investigation found that over a 15-month period the Town of Cottesloe ("the Town") unknowingly awarded and paid contracts valued at $51,267 to a private company which was owned by the Town's Conservation and Maintenance Officer ("the Officer"). These were based on 24 purchase orders, and subsequent invoices prepared by the Officer. Of these, an audit by the Town found that $46,389 was falsely invoiced because the work was either:

- not done;
- carried out by the Officer during his work hours; or
- carried out by another contractor.

[31] The Officer also bought materials and tools using the Town's financial resources, but kept them for his personal use.

### Commission Observations

[32] The Officer presented contracts to his supervisor, who trusted him and signed them without checking supporting documentation to enable verification. Invoices were paid on the Officer's authorisation that work had been done. There was no independent verification of the work done.

### 2.1.3 Investigation 3

[33] The Chief Executive Officer (CEO) of the Shire of Murchison fraudulently obtained $41,689 worth of goods, services and money over a two-year period by:

- using his corporate credit card for private expenditure, including fuel, airfares, clothes, electronic equipment, tools, veterinary bills, vehicle parts, fines and other domestic bills;
- making payments to a fictitious business while directing funds to a personal account; and
- creating and paying false invoices.

**Commission Observations**

[34] The CEO was able to authorise payments without review or scrutiny by any other employee. He used this lack of separation of duties to misuse the Shire of Murchison's financial resources for his personal benefit.

### 2.1.4 Investigation 4

[35] Over a three-year period state and local government employees spent at least $620,000 purchasing toner cartridges from a group of related companies outside procurement policies and arrangements.[14] The companies provided many of these employees with gifts. They also used a variety of sales methods to pressure employees into purchasing from them, for example, faxing a contract to a junior employee and pretending the authority was already committed to the order and it only needed confirmation. Had the employees complied with relevant procurement policies and purchased toner through approved suppliers the cost would have been around $205,000, a saving to state and local government authorities of $415,000. Much of the toner purchased was excess to requirements and could not be used before the use-by date.

**Commission Observations**

[36] The Commission's investigation involved 24 local governments, 10 of which had employees who received gifts from the companies.

[37] The Commission noted that despite the existence of procurement policies, employees were found to have made substantial purchases of unnecessary toner cartridges, at prices higher than those of approved suppliers, often without supervisors or managers being aware.

[14] This investigation was the subject of the Commission's *Report on the Investigation of Alleged Public Sector Misconduct in Relation to the Purchase of Toner Cartridges in Exchange for Gifts Outside Government Procurement Policies and Arrangements*, tabled in the Parliament of Western Australia on 24 November 2011.

[38] The Commission found that generally the gift policies, gift registers and accountability mechanisms did not sufficiently address the misconduct risks associated with gifts connected to purchasing decisions.

### 2.1.5 Investigation 5

[39] The CEO of the Shire of Kalamunda purchased just over $1 million worth of software from a company, despite only having authorisation from the Council to spend $200,000.[15] While employed as CEO of another local government, the Shire of Augusta-Margaret River, he had also purchased $230,947 worth of software from the company despite only having authorisation from the Council to spend $60,000.

[40] The CEO received a range of gifts and benefits from the software company, including tickets to cricket and Australian Football League games. When the CEO attended a conference in London (and presented a paper) the software company paid for the business class flight and provided $2,000 travel allowance, tickets to the cricket at Lords in London, and golf admission in Dubai and Wales.

#### Commission Observations

[41] The CEO was able to contravene policy and legislation because there was no effective oversight of his work by either of the Councils for which he had worked. Information he presented to the Councils either lacked relevant details or was presented in an ambiguous manner.

### 2.1.6 Investigation 6

[42] An employee of the City of Bayswater awarded contracts to businesses owned by his personal associates and family members.[16] He provided information to them about other quotes so that they could quote slightly less. He also arranged for them to submit false higher quotes in the names of other businesses to make their own quotes appear reasonable.

[43] A second employee awarded work to a favoured contractor on 28 occasions, to a value of $56,762, without obtaining quotes.

#### Commission Observations

[44] Apart from the clear dishonesty identified during this investigation, the Commission also noted a systemic problem in the lack of interrelationship between the finance system then operating at the City of Bayswater and the management of tender contracts. This meant that once tenderers had

[15] This investigation was the subject of the Commission's *Report on the Investigation of Alleged Public Sector Misconduct by a Local Government Employee in Relation to the Purchase of Management Systems Software*, tabled in the Parliament of Western Australia on 19 December 2013.

[16] This investigation was the subject of the Commission's *Report on the Investigation into Allegations of Misconduct by Councillors or Employees of the City of Bayswater*, tabled in the Parliament of Western Australia on 13 November 2009.

successfully obtained a contract they were able to charge, and be paid, more than the amount they had quoted in their tenders.

## 2.2 Lessons from the Investigations

[45] Although the fraud, corruption and misconduct in the six investigations considered above came in a variety of forms, and involved employees at different levels of the organisation, they demonstrate how the processes of local governments can be exploited by employees, suppliers and contractors, to obtain benefits dishonestly.

[46] In the Commission's view these investigations indicate a systemic weakness across the local government sector. In 2013-2014 the Commission undertook 13 investigations into allegations of serious misconduct in local governments. Eight of those were into procurement related misconduct and/or revealed serious flaws in the management of procurement by a local government.

[47] The investigations summarised above demonstrate the necessity for local governments to have proper systems and procedures to mitigate misconduct risks. While it is difficult to prevent a determined person from committing fraud, the opportunities and temptations can be greatly reduced through an appropriate control framework.

[48] The type of risks noted by the Commission in the course of its investigations and reviews into misconduct related to procurement in local government include situations in which:

- one person is able to be involved in various stages of organising contracts and authorising payments, that is, there is no separation of duties;
- supervisors do not check tender and payment processes, and work actually done on contracts, with a view to preventing misconduct;
- audits are not carried out, or are superficial or ineffective, in relation to use of purchasing cards and contract administration;
- inadequate training is provided and/or the policies and procedures on purchasing are not provided to employees or enforced;
- records are inadequate, particularly in relation to documenting decisions, and the reasons for those decisions, about tenders and contracts;
- conflicts of interest are not declared by employees or recorded, for example, when contracts are awarded to family members, friends or associates;
- employees do not declare secondary employment or private business interests;
- receipt of gifts is permitted or gift registers are not used;

- a clear code of conduct is not brought to the attention of employees on a regular basis;
- allegations about misconduct made to the local government are not dealt with appropriately; and
- local governments do not report possible misconduct to the Commission.

# CHAPTER THREE
# COMMISSION AUDITS AND REVIEW

## 3.1 Introduction

[49] The Commission, in addition to its investigations, has commissioned audits of the capacity of five local governments to prevent, identify and deal with misconduct, especially in relation to procurement.

[50] The Commission has also conducted a review of the capacity of the City of Stirling to prevent, identify and deal with misconduct. This was subsequent to the Commission's investigation, considered above as Investigation 1.

[51] The audits and the review are considered below.

## 3.2 RSM Bird Cameron Procurement Audits of Five Cities

[52] The Commission engaged independent auditors RSM Bird Cameron to undertake procurement audits in five major metropolitan local governments, the Cities of Cockburn, Joondalup, Perth, Swan and Wanneroo ("the Cities").

[53] These local governments were chosen for the audits purely because of their size and the scale of their operations. With the City of Stirling, these are the six largest local government purchasers in Western Australia. Each of them is a large, complex organisation in its own right.

[54] The objective of the audits was "to evaluate the capacity of systems, policies, procedures and practices of five selected local government authorities to effectively prevent, identify and respond to misconduct in procurement practices".

[55] RSM Bird Cameron had three lines of inquiry. In summary, these questioned how the Cities:

- minimised opportunities for misconduct;
- were alerted to possible misconduct; and
- reported and dealt with suspected misconduct.

[56] In effect, RSM Bird Cameron conducted the type of procurement audits on local government authorities that the Office of the Auditor General undertakes for State Government authorities.

[57] RSM Bird Cameron's audit report[17] ("the report") noted that the five Cities spent $401 million on procurement in 2011- 2012.

[17] RSM Bird Cameron, *Local Government Authorities Procurement Audits, Consolidated Report*, October 2013.

### 3.2.1 Findings of Audits

[58] The report noted some positive findings. The Cities were found to generally have procurement policies and procedures which complied with legislation, and managed conflicts of interest; although instances of non-compliance and gaps in the internal control framework were found, including in the areas of stock, contracts and major works.

[59] The Cities were also found to have access to expertise, and to provide their employees with knowledge and training, and mechanisms for reporting misconduct.

[60] However, the first key observation by RSM Bird Cameron in the report, and one which impacted their conclusions on all lines of inquiry, was that "[t]he Cities have not undertaken an assessment to determine their specific fraud and misconduct risks".

[61] In this context, in relation to each of their lines of inquiry, RSM Bird Cameron found that the absence of a specific fraud and misconduct risk assessment indicated that:

- *… the Cities may not be managing procurement related misconduct risks effectively;*
- *… the Cities controls in identifying non-compliance with procurement policies and procedures are unlikely to be effective in detecting and managing misconduct and fraud risks*; and
- *… the Cities governance and frameworks can only provide limited assurance that they are managing these risks effectively*.

[62] RSM Bird Cameron pointed out that during the relevant period, although the Cities had audit processes, "… these audit activities may not be adequately directed towards key misconduct areas as specific risks have not been identified".

[63] The Commission accepts that the fact that misconduct risk assessments had not been conducted, and risk mitigation strategies had not been developed, does not mean that misconduct was occurring in the five Cities reviewed. However, in the Commission's view the absence of risk assessments suggests that the Cities had an increased level of exposure to misconduct risk, and that, if misconduct occurred, there was an increased probability that it would go undetected.

[64] In the Commission's view the lack of risk assessments for misconduct in procurement is a significant issue for the for the local government sector.

[65] The RSM Bird Cameron audits also identified specific financial governance weaknesses related to procurement, which existed in some Cities and not others. The main weaknesses identified during the relevant period were in the areas of:

- internal audit procedures relevant to misconduct risk;
- lack of separation of duties;
- tendering and quotation procedures;
- adherence to procedures, particularly in relation to authorisation to make decisions and justification of those decisions;
- education and training about misconduct; and
- dealing with conflicts of interest.

[66] These six areas of weakness in governance systems also featured in the investigations considered earlier in this report.

### 3.2.2 Capacity Building: Post-Audits

[67] Since the procurement audits all five local governments have conducted, or are in the process of conducting, assessments of their misconduct risks in procurement and have addressed weaknesses in their financial governance systems. Key features of actions undertaken include:

- developing and implementing a fraud prevention policy and fraud control plan;
- reviewing risk management policies and frameworks, including updating corporate risk registers;
- undertaking risk assessments which include fraud, corruption and misconduct risks in procurement;
- testing key controls;
- establishing strategies to mitigate identified risks;
- requiring independent review of tenders and sole supplier applications before they are approved, and improved record keeping for this process;
- reviewing segregation of purchasing duties;
- developing a corporate credit card policy;
- developing a statement of business ethics for suppliers and contractors; and
- expanding terms of reference for an Audit Committee to include risk management, internal control and legislative compliance, as required by the *Local Government (Audit) Regulations 1996*.

[68] All five local governments involved in the RSM Bird Cameron procurement audits have stated their commitment to ongoing improvements in this area.

## 3.3 City of Stirling Review

[69] The Commission's review of the City of Stirling ("the City") found that since the original Commission investigation in 2010 the City has addressed the identified financial governance weaknesses that had allowed serious fraud and corruption to occur. It had also taken steps to build its misconduct resistance across the whole organisation, which include the following.

- The CEO has taken a lead role in driving the City's misconduct resistance agenda, and has facilitated the investment of considerable City resources to better enable the organisation to manage its misconduct risks.

- The City has developed a comprehensive policy and procedures framework for dealing with misconduct. This includes an investigations procedure with a requirement to report suspected misconduct to the Commission.

- Responsibility for progressing the City’s misconduct resistance agenda is vested in senior executives. A centralised oversight and reporting mechanism exists to monitor progress. Senior executives demonstrate high levels of awareness of misconduct risk and how to deal with misconduct when it occurs.

- Education of employees is a corporate priority. The need to build understanding about misconduct and the importance of reporting suspected misconduct are consistent messages. Education programs clearly and consistently support workplace behaviour in line with the code of conduct and a "no tolerance" stand on misconduct.

- The City's *Misconduct, Corruption and Fraud Control Plan* reflects its wider consideration of its risk environment, and sets out a range of strategies. There is an appreciation of the misconduct risks in the City's functions, including procurement.

# CHAPTER FOUR
# ANALYSIS

## 4.1 Introduction

[70] The investigations, audits and review of individual local governments, as described in this report, are not, in the Commission's view, the most effective way to achieve sector-wide change. They are resource intensive, and investigations into fraud or corruption usually mean that a local government has already suffered a loss.

[71] In the Commission's view a whole-of-sector approach, with a focus on prevention, is needed.

[72] In this context it is worth noting the differences in procurement oversight arrangements between the state and local government sectors in Western Australia.

## 4.2 State Government Sector

[73] In the State Government sector procurement by authorities is overseen by the State Supply Commission (SSC) which is part of the Department of Finance. The SSC issues mandatory procurement policies and guidelines, including on "Probity and Accountability",[18] and offers support to agencies.

[74] State Government authorities are also required by *Treasurer's Instruction 825: Risk Management and Security*[19] to apply a risk management process, which includes identifying and analysing risks and developing policies and practices to deal with them. The areas listed in *Instruction 825* where an organisation can have exposure to risk include "human behaviour, including risk of misconduct and corruption".

[75] The Auditor General for Western Australia has a role "to audit the finances and activities of the West Australian public sector". This includes State Government authorities, but does not include local government (except in limited circumstances which are described below). In this role, among other things, the Auditor General is responsible for:

- conducting financial statement, KPI and control audits and issuing audit opinions for over 200 public sector agencies; and
- undertaking wide-ranging performance examinations to ensure that there are adequate controls within agencies.[20]

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[18] Department of Finance, *Procurement Practice Guide*, August 2014.

[19] Department of Treasury, *Financial Administration Bookcase, Treasurer's Instruction 825: Risk Management and Security*, 28 December 2007.

[20] Office of the Auditor General (OAG), *Our Role and Responsibility*, available on the OAG Website at https://audit.wa.gov.au/about-the-oag/our-role-responsibility, viewed 20 December 2014.

[76] In Queensland, South Australia, Tasmania and Victoria the respective Auditors General have jurisdiction to conduct performance audits of local governments. In Queensland, Tasmania and Victoria they also have jurisdiction to conduct financial statement audits of local governments.

[77] In a letter to the Commission, the Auditor General for Western Australia noted that he does have a limited capacity to audit local government in circumstances relating to the provision of State Government funding for a particular purpose. However, he advised that this has only been used on two occasions since the Auditor General's legislation was enacted in 2006. Furthermore, the Auditor General advised the Commission that the *Auditor General Act 2006* gives him the capacity to:

> *… enter into an arrangement with any person or body to carry out an audit. This means that a local government could for instance ask me to perform a performance audit of its procurement arrangements. I hasten to add that no such request has ever been made.*[21]

[78] The Commission accepts that local governments may be unaware that they are able to request a performance audit by the Auditor General. However, there are obvious weaknesses in a system which requires that an agency itself ask the Auditor General to become involved.

[79] The Commission's view is that individual local governments should not be left to themselves to determine whether they need an external performance audit of their procurement arrangements.[22]

## 4.3 Recommendations by the Public Accounts Committee

[80] In September 2006 the Public Accounts Committee ("the Committee") tabled in the Parliament a report entitled *Local Government Accountability in Western Australia: Report No. 4 in the 37th Parliament*.

[81] In this report the Committee identified as a problem that local government in Western Australia was not subject to a similar accountability framework as the rest of the public sector. It said "… provisions relating to audit in local government are largely limited to financial attestation, or 'tick and flick' audits".[23]

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[21] Letter to Commissioner Roger Macknay QC, 30 April 2014, from Mr Colin Murphy, Auditor General for Western Australia, in response to a draft of this report.

[22] It is significant to note that amendments to the *Local Government Act 1995*, Part 7, Division 1A, in 2004, with effect from May 2005, provides for the establishment of audit committees, whereby the audit committee of a local government is to be comprised of three or more persons, with the majority of members being council members. The Chief Executive Officer and employees are excluded from being members of the audit committee. A local government appoints a person (or persons) as its auditor on the recommendation of the audit committee to audit accounts and annual financial reports for each financial year, but does not undertake performance audits. The auditor is to be a registered company auditor or an approved auditor.

[23] Public Accounts Committee - Legislative Assembly, *Local Government Accountability in Western Australia: Report No. 4 in the 37th Parliament*, 2006, p.xiii.

[82] The Committee said that it "… strongly recommends that the audit of WA local governments should be brought under the authority of the Auditor General".[24] It made a series of recommendations to support this view.

## 4.4 Recent Amendments to Law and Policy Affecting Local Governments

[83] In February 2013 the *Local Government (Audit) Regulations 1996* ("the Regulations") were amended to, among other things, include at regulation 17(1) a requirement that for each local government:

> *(1)* [t]*he CEO is to review the appropriateness and effectiveness of a local government's systems and procedures in relation to –*
>
> *(a) risk management;*
>
> *(b) internal control; and*
>
> *(c) legislative compliance.*

[84] Regulation 17(2) states that the review is to be carried out at least once every two calendar years and regulation 17(3) states that the CEO is to report to the local government's audit committee the results of the review. The process to be followed in the review is not stipulated.

[85] In September 2013 the Department of Local Government and Communities issued Operational Guideline Number 09 relating to *Audit in Local Government*.[25] Appendix 3 of the Guideline relates specifically to "Issues that should be considered in the CEO's Review of Risk Management, Internal Control and Legislative Compliance". It is clear from the points listed under the heading "Risk Management" in Appendix 3 that risks relating to misconduct in procurement are specifically included. One of the issues to be considered under Risk Management is:

> [a]*scertaining whether fraud and misconduct risks have been identified, analysed, evaluated, have an appropriate treatment plan which has been implemented, communicated, monitored and there is regular reporting and ongoing management of fraud and misconduct risks.*

[86] In addition, Section 7.2 of the *Local Government Accounting Manual*[26] is entitled "Risk Management" and describes the process of risk management for local governments, although procurement is only one of many areas in which it states that risks may arise.

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[24] *Ibid*, p.xv.

[25] *Local Government Operational Guidelines*, Number 09, Revised September 2013, *Audit in Local Government, The Appointment, Function and Responsibilities of Audit Committees*.

[26] *WA Local Government Accounting Manual*, Edition 3, Section 7, Internal Control Framework.

[87] One local government which was the subject of a Commission investigation wrote to the Commission, well after the promulgation of the above guidelines, and, made the following comments.

- *The Local Government Act sets out roles and responsibilities of the Council and the CEO but the Council is constrained from delving too deep into 'operational' matters and the actual internal control systems which are in place.*
- *In this instance* [misuse of funds] *it is apparent that the audit system failed to identify either the actual fraud or the system failures or weaknesses.*
- *The Department of Local Government has statutory responsibility under part 8 of the Local Government Act to oversee local governments but does not conduct occasional visits and audit tests, or provide guidelines for small isolated shires where there are limited resources to provide checking and accountability.*[27]

[88] The Commission notes the developments in legislation and guidelines. However, the Commission also notes that these developments are based on internal compliance by individual local governments, especially by the CEO. Although the development of risk management strategies are valuable they cannot, by themselves, prevent, fraud, corruption or other forms of misconduct in procurement. This is especially the case where a CEO is himself or herself involved in misconduct, as was the case for the Shires of Murchison and Kalamunda (refer Investigations 3 and 5 above).

[89] In the Commission's view the concerns expressed by the Public Accounts Committee in 2006, and its recommendation that the audit of local governments be brought under the authority of the Auditor General, are still relevant. There is a need for external audit of local government procurement.

[90] In addition, in order to be effective in preventing and dealing with misconduct in procurement, the requirement for local governments to review their systems and procedures in relation to risk management and internal controls will require active oversight by the Department of Local Government and Communities.

[91] In this regard the Commission notes that the Strategic Plan for the Department of Local Government and Communities includes, as a priority strategy, to "[u]ndertake local government performance and risk management".[28]

[27] Letter to Commissioner Roger Macknay QC, of 7 May 2014, from a local government CEO in response to a draft of this report

[28] Department of Local Government and Communities, *Strategic Plan 2014-2018*.

# CHAPTER FIVE
# RECOMMENDATIONS

## 5.1 Oversight by the Auditor General

[92] Independent and external oversight of authorities is an effective means for identifying and preventing misconduct. In the Commission's view an appropriate way to ensure external oversight of financial governance in procurement by local governments would be to extend the jurisdiction of the Auditor General to specifically include local governments.

[93] Doing so would align the local government sector with the State Government sector. There seems to be no reason why local governments should have lower standards of accountability than State Government authorities.

[94] Accordingly, the Commission makes the following recommendation.

> **Recommendation One**
>
> The Commission recommends that the jurisdiction of the Auditor General be extended to include local governments.

[95] This recommendation is consistent with the recommendations of the Public Accounts Committee in 2006.[29]

[96] The Department of Local Government and Communities has advised the Commission that implementing this recommendation would require amendments to the *Auditor General Act 2006* and the *Local Government Act 1995*.[30]

## 5.2 Oversight by the Department of Local Government and Communities

[97] The Commission notes the amendment to the *Local Government (Audit) Regulations 1996*, and the guidelines issued by the Department of Local Government and Communities, as considered in the previous chapter of this report.

[98] The Commission also notes that effective risk assessments, and mechanisms for reducing identified risks, have been developed by the five local governments that were the subject of the procurement audits by RSM Bird Cameron considered in this report. In addition, following

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[29] Public Accounts Committee - Legislative Assembly, *Local Government Accountability in Western Australia: Report No. 4 in the 37th Parliament*, 2006, pp.xxi - xxii.

[30] Letter to Commissioner Roger Macknay QC, of 8 May 2014, from Ms Jennifer Mathews, Director General Department of Local Government and Communities, in response to a draft of this report.

Commission reviews misconduct resistance approaches have been developed by other local governments including the City of Stirling.

[99] Nonetheless, based on its investigations and reviews the Commission considers that the legislative and policy requirements for local governments to assess misconduct risks, and develop a plan for mitigating those risks, should be the subject of active oversight by the Department of Local Government and Communities, particularly in relation to the risks of misconduct arising from procurement.

[100] Accordingly, the Commission makes the following recommendation.

**Recommendation Two**

The Commission recommends that the Department of Local Government and Communities actively oversights risk management reviews prepared by local governments pursuant to the *Local Government (Audit) Regulations 1996* to ensure that they include appropriate assessment of misconduct risks arising from procurement, and mechanisms for reducing those risks.

Audit and Risk Committee
Confidential Schedule 3
(Minute AR26/15 refers)

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