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EXECUTIVE SUMMARY

Audit committees play a key role in assisting Local Government Entities to fulfil their governance and overseeing responsibilities, ethical practices and accountability requirements.

The best practice guidelines for Local Government Entity audit committees and internal audit apply to Councils, Regional Library Corporations and local government companies incorporated or set up under section 193 of the Local Government Act 1989. Therefore the term Local Government Entity (LGE) used throughout these Guidelines includes Councils, being the collective body of Councillors, the Board of a Regional Library Corporation and the Board of local government companies. A Regional Library Corporation is a statutory body corporate and its governing body is the Board as if they were the Councillors of a Council.

The main objectives, functions and potential benefits of an appropriately established and effective audit committee will include the following:

- the enhancement of the credibility and objectivity of internal and external financial reporting;
- effective management of financial and other risks and the protection of the LGE’s assets;
- compliance with laws and regulations as well as use of best practice guidelines;
- assisting the effectiveness of the internal audit function to add value in the interests of the LGE and its ratepayers or other constituents; and
- the provision of an effective means of communication between the external auditor, internal audit, management and the LGE.

The Audit Committee is a formally appointed committee of the LGE and is responsible to that body. The Audit Committee does not have executive powers or authority to implement actions in areas over which management has responsibility and does not have any delegated financial responsibility. The Audit Committee does not have any management functions and is therefore independent of management. The Audit Committee does not have any role in relation to issues normally addressed by a LGE Finance Committee which is a LGE/management subcommittee with delegated powers and financial management responsibilities in relation to budgets, financing decisions and expenditure priorities. The Audit Committee is a separate activity and acts independently of any Finance Committee, and does not have any role in relation to financial management issues or have an executory role or powers.

The Committee’s role is to report to the LGE and provide appropriate advice and recommendations on matters relevant to its Charter in order to facilitate decision-making by the LGE in relation to the discharge of its responsibilities.
The Audit Committee should comprise a minimum of three members – one member of the LGE and two external independent persons. The chairperson of the Audit Committee should be an independent person and the Committee should include a majority of external independent persons. All members shall have full voting rights.

The Chief Executive Officer and internal auditor (whether a member of staff or contractor) are required to attend all Audit Committee meetings, except when the Committee chooses to meet in camera. Other members of the LGE or Council/Library/Company staff may be invited to attend at the discretion of the Committee to advise and provide information as and when required.

The Council/Regional Library/Company shall provide secretarial and administrative support to the Committee.

The Committee should meet at least four times per annum preferably with a minimum of one meeting taking place in each quarter.

The Audit Committee shall after every meeting forward the minutes of that meeting to the next ordinary open meeting of the LGE, including a report explaining any specific recommendations and key outcomes.
INTRODUCTION

An audit committee plays a key role in assisting a Local Government Entity to fulfil its governance and overseeing responsibilities in relation to financial reporting, internal control structure, risk management systems, ethical accountability and the internal and external audit functions.

The best practice guidelines for Local Government Entity audit committees and internal audit apply to Councils, Regional Library Corporations and local government companies incorporated or set up under section 193 of the Local Government Act 1989. Therefore the term Local Government Entity (LGE) used throughout these Guidelines includes Councils, being the collective body of Councillors, the Board of a Regional Library Corporation and the board of local government companies. A Regional Library Corporation Library is a statutory body corporate and its governing body is the Board as if they were the Councillors of a Council.

The Victorian Government has recognised the importance of audit committees and is working further to develop the effectiveness of LGE audit committees in response to the challenges posed by the increasing complexity of operations and the greater accountability requirements placed on members of a LGE and Council/Regional Library Corporation staff.

An audit committee provides a forum where members of a LGE, management and auditors can address issues relating to the management of risk, transactions with external parties and financial reporting obligations. Audit Committees provide a mechanism to introduce independent oversight into the governance process and to co-ordinate the internal and external audit functions, as part of an overall system for financial reporting and the management of risk.

The Best Practice Guide is intended to assist LGEs establish and maintain an effective audit committee.

A local government sector working party (who developed this Guide) was established in response to concerns raised by the Auditor General at the operation of audit committees and internal audits within the local government sector. The local government sector working party comprised:

- Mr Greg Pound Director Auditing Standards, Australian Accounting Research Foundation
- Mr Rob Spence Municipal Association of Victoria
- Mr David Gibbs McInnes Graham & Gibbs – Chartered Accountants
- Cr John Lawless Moira Shire Council
- Mr Neil Armstrong LGPro
- Mr Ian Matthews LGPro
- Mr Craig Burke Victorian Auditor-Generals Office (Observer)
- Mr Evan Dukas former Director Commercial and Financial Services, DOI - Local Government Division
Whilst this Guide reflects recent developments and best practices identified in Australia and overseas for audit committees generally, it has been developed specifically for the local government sector in Victoria. It is based on the Best Practice Guide “Audit Committees” produced by the Auditing and Assurance Standards Board of the Australian Accounting Research Foundation (AARF), the Australian Institute of Company Directors (AICD), the Institute of Internal Auditors – Australia (IIA) and has been customised for Victorian local government entities to meet the objectives established by a local government sector working party. The Guide has been customised with the direct involvement of the Auditing & Assurance Standards Board of the AARF with the support of the AICD and IIA.

Following a two-month period of consultation with LGEs, the Guide was reviewed and amended in light of the submissions received by the working party.

The MAV, LGPro and the Department of Infrastructure endorse the best practices identified. A representative of the Auditor-General’s Office has acted as an observer during the development of the guidelines.

Some small LGEs with limited resources may find it impractical to meet all of the best practices outlined in these Guidelines. Where this is the case, it will still be important for the LGE to assess carefully the elements of best practice that are relevant to “corporate governance” which includes financial reporting, management and associated accountability, risk management, internal control, compliance with applicable laws, regulations and best practice guidelines. The Best Practice Guide will be a helpful basis for such an assessment. It should be recognised, however, that as the role of LGEs in the local community, their objectives and regulatory requirements are the same irrespective of size, the benefits to be derived from an appropriately structured audit committee are the same.

Audit committees should be an integral component of the “Code of Good Governance” issued by the Municipal Association of Victoria and the Victorian Local Governance Association. In this context, the role of the audit committee relates to the specific elements of “corporate governance” indicated above.
1. **Objectives of the Audit Committee**

The main objectives and the potential benefits of an appropriately established and effective audit committee would usually include the following:

- Improving the credibility and objectivity of the accountability process (including financial reporting) especially where the role of the audit committee is disclosed.

- Assisting the LGE to discharge its responsibility to exercise due care, diligence and skill in relation to the LGE’s:
  - reporting of financial information to users of financial reports;
  - application of accounting policies;
  - financial management;
  - internal control system;
  - policies and practices;
  - compliance with applicable laws, regulations and best practice guidelines; and
  - risk management systems, in particular monitoring and controlling of community and commercial risk.

- Providing an additional and independent formal forum for communication between the LGE and senior financial management.

- Improving the effectiveness of the internal and external audit functions and the communication between the LGE and the external and internal auditors.

- Improving the efficiency of the LGE by seeking advice (or delegating tasks) to the committee and thus facilitating the discussion of issues in sufficient depth.

- Providing an independent reporting line, in addition to the functional reporting line to the CEO, for internal audit, thereby facilitating the maintenance of the objectivity of the internal auditor.

- Improving the quality of internal reporting.

- Adding to the credibility of the LGE and the organisation through monitoring of ethical standards.

**Commentary**

*An audit committee is a sub-committee of the LGE and as such it assists members of the LGE to discharge the LGE’s responsibilities of oversight and governance.*

*Members of the LGE and auditors, both external and internal, therefore, have a vested interest in effective audit committees as an audit committee can help them to meet their legal and professional responsibilities.*
The role of a properly constituted audit committee is strengthened if all relevant participants have a clear understanding of the audit committee’s objectives. Disclosure of the existence and role of the audit committee in a LGE’s financial reports will also enhance the credibility of those reports.

2. Charter and Terms of Reference

The responsibility and authority of the audit committee should be made clear.

The charter and terms of reference of the audit committee should be included in a formal charter and supporting terms of reference, which should be formally approved by the LGE and periodically reviewed and updated. These documents should set out the following:

- The audit committee’s objectives.
- The committee’s duties and responsibilities and the scope of its activities, particularly in the areas of:
  - financial reporting, including review of significant accounting policies;
  - internal control and risk management;
  - the establishment and continuous monitoring of a framework and processes for compliance with laws, regulations and the LGE’s code of conduct;
  - reviewing financial, tendering and performance reports requiring the LGE’s approval;
  - reviewing related-party transactions, for example transactions with entities controlled by members of the LGE or council/library/company management;
  - management information systems;
  - the oversight of the process for the prevention and detection of fraud and irregularities,
  - performance management;
  - financial reporting by LGE business units; and
  - national competition policy.
- The extent of the authority delegated to the audit committee and its powers which should emphasise that the audit committee does not have an executory role or powers, and is not a finance committee and does not have financial management responsibilities.
- The number of members and the method of appointing and replacing them.
- The process for appointing the chairperson.
- The process for appointing a secretary and for gaining access to other resources (including external resources such as independent advice if necessary) for the committee to fulfil its responsibilities.
- The committee’s right of access to all levels of management.
• The committee’s right of access to the external and internal auditors and the oversight of their respective activities.

• The arrangements for meetings, including the power to call an audit committee meeting if required, and details of what constitutes a quorum.

• The LGE’s requirements regarding how the LGE is to be informed of the committee’s activities and the reports it is to receive.

• The process for monitoring the committee’s performance and compliance with its terms of reference.

**Commentary**

*For an audit committee to operate effectively, its mandate, structure and methods must be defined clearly. To achieve this the committee should be established by the LGE setting out its terms of reference.*

Committee members, management, internal and external auditors and all members of a LGE must understand the committee’s terms of reference.

*The terms of reference should include the committee’s scope of activities and the communication arrangements put in place.*

*The terms of reference should also provide the audit committee with the resources and authority necessary to meet its objectives. This provision will in part require the committee to have the right to seek independent professional advice when considered necessary and the power to obtain information from management and to consult directly with the auditors.*

### 3. Committee Membership

• The chairperson of the audit committee and the majority of committee members should be independent of the LGE and management.

• Members must have the appropriate skills and time to fulfil their role on the committee.

• At least one member should have significant experience and skills with financial matters.

• Members should be given the opportunity to attend technical or professional development courses to help them keep up to date with legislative, accounting, operational and other relevant issues.

**Commentary**

*As the audit committee members have been formally appointed by the LGE, any changes in membership should be subject to the LGE’s approval.*

*While an audit committee is a sub-committee of the LGE with the objective being to assist members of the LGE to discharge their responsibilities, it is important that the Audit*
Committee be, and be seen to be an independent element of the governance process. Independence brings with it the ability to approach a task objectively and to avoid potential conflicts of interest.

The chairperson of the audit committee and at least the majority of committee members should be independent with no operating responsibilities within the LGE management structure nor any association with the LGE. Associations refer to commitments and provision of paid services to the LGE, directly or indirectly, for example sporting clubs, regional committees etc. This exclusion does not include ratepayers, and appropriately skilled ratepayers are encouraged to participate. This will enable the committee to approach its tasks objectively, to maintain its independence, and also to be seen to be independent.

This structure recognises that the LGE is a policy making body that is accountable to its electorate or other constituents for its policies and in meeting its associated responsibilities, and that this process is strengthened by an independent (and appropriately skilled) review and advisory function. External members bring to the Audit Committee skills, knowledge and experience that may not otherwise be available from within the LGE, and a facility for checks and balances to the primarily internal focus of other members. In this regard, members of the LGE are not regarded as independent as they are part of the policy and decision-making process, and have responsibilities within the LGE’s internal processes which will be subject to review by the Audit Committee.

The qualifications for membership of the audit committee should reflect those appropriate to its responsibilities. While it is desirable that at least one member of the committee have a strong financial background, the overall composition of the committee should reflect a broad experience and knowledge base consistent with the LGE’s business activities. The number of members required will depend on the responsibilities assigned to the committee, the relative diversity and complexity of the LGE’s business activities and the knowledge and experience of the individual members.

The selection of the chairperson should be given careful consideration because this person will be pivotal in ensuring the overall effectiveness of the committee and the efficient planning and conduct of meetings. The need for independence applies particularly to the chairperson, as does the need for that person to have significant administrative and commercial experience, and be knowledgeable about the LGE’s responsibilities and financial reporting and auditing requirements. The chairperson has a significant role and must be capable of providing strong and effective leadership.

The Chief Executive Officer shall not be a member of the Committee but should attend all meetings, except when the Committee chooses to meet in camera.

The LGE will include independent members of the audit committee in its professional indemnity insurance coverage for the services they provide to the LGE, and advise those members accordingly.

Local government entities may also seek to appoint in the Audit Committee community members with the appropriate skills on an “honourary basis”.
4. **Induction of New Members**

- Any prospective new committee members should be provided with a copy of the audit committee’s terms of reference and with specific, tailored information about the LGE, particularly in the following areas:
  
  - current business plan;
  - day to day operations;
  - financial performance;
  - business and financial risks and the way they are managed;
  - the internal control system;
  - key financial reporting policies, including related-party issues;
  - legal and regulatory requirements, including external reporting and compliance responsibilities;
  - key performance and annual plan indicators;
  - code of ethical conduct; and
  - unusual transactions.

- New members should meet key management personnel, including the Mayor, Chairperson of the Regional Library Corporation or Company Chairperson and senior management, to listen to issues raised for attention by them.

- New members should meet the external and internal auditors and obtain background on key audit issues and risk areas.

**Commentary**

*The committee’s knowledge and proficiency are enhanced when new members are acquainted adequately with the committee’s objectives and practices. This is especially important when a new committee chairperson is appointed; however, all new members need to be well briefed. Audit committees can undertake training in many different ways ranging from formal orientation programs to informal discussions with new members.*

*A new member should understand the committee’s responsibilities and objectives, be familiar with its relationships with the LGE and management and the internal and external auditors, and have a sound knowledge of the LGE’s operations and the environment in which it operates.*

5. **Meetings**

- There should be a regular schedule of meetings with pre-arranged dates.

- Meetings should be structured with the use of an agenda and supporting papers.

- A process should be established for putting items on the agenda by those entitled to do so, and for special meetings to be arranged. Auditors should be invited to contribute to the agenda.
• Agenda and briefing papers (including any input from management) should be well documented and circulated in sufficient time to allow members to review the information well before the meeting.

• The internal and external auditors should have a right to attend audit committee meetings except in situations where there could be a perceived conflict of interest.

• Meetings should meet the requirements of a pre-established quorum. A quorum shall be two for a Committee with the minimum membership of three. For Committees with membership of greater than three, a quorum will be a majority of the Committee membership comprising at least equal representation of internal and external independent members.

• Progress reports on actions previously agreed between auditors and the LGE’s management should be presented to the Audit Committee until it is satisfied that the issues raised have been resolved.

• Meetings should be minuted and the minutes signed by the chairperson.

Commentary

The conduct of audit committee meetings will influence greatly the ability of committee members to achieve the audit committee’s objectives.

Normal administrative practices apply in relation to audit committee meetings in that there should be a well-structured agenda and minutes to record the proceedings. Meetings should be arranged in such a way that, as far as possible, all audit committee members could attend. Any briefing papers should be well documented and circulated in advance to all members and any other participants in the meeting.

Adequate time should be allowed for discussion and resolution of each agenda item.

The number and duration of audit committee meetings depends on the range and complexity of the committee’s responsibilities and are matters to be agreed by the committee.

A useful way of arranging the timing and content of meetings is to follow the financial reporting and external audit cycle. For example:

• at the planning stage of the audit, at which time the planned scope of the audit and the auditor’s recommendations on controls can be considered;

• before the LGE’s meeting approving the annual financial report, at which time significant matters arising during the audit can be considered.

The timing of meetings may also be influenced by factors such as the council’s budget, planning cycle and internal audit programme.
6. Systems of Reporting

The chairperson of the audit committee should report formally to the LGE to provide a summary of the audit committee’s work and results. The report should cover at least the following:

- the committee’s minutes;
- any formal resolutions of the committee;
- information about the audit process and any recommendations and results from the audit (both internal and external) including issues raised in the external audit report and any management letter issued by the external auditor; and
- other major issues of which the committee believes the LGE should be informed.

Commentary

As a sub-committee of the LGE, the audit committee must have a formal process for communicating with the LGE.

The role and status of the audit committee result in its decisions being, in effect, recommendations to the LGE rather than determinations in their own right.

Provision should be made by Councils for circumstances where it may be appropriate for the LGE to deal with the audit committee’s report in camera, such as where matters require further investigation or relate to matters that must remain confidential under the provisions of the Local Government Act.

7. Audit Committee’s Responsibilities

The audit committee’s main responsibilities can be divided into the following areas:

7.1 External Reporting

- Consider the appropriateness of the LGE’s accounting policies and principles and any changes to them, as well as the methods of applying them, ensuring that they are in accordance with the stated financial reporting framework. To do this the audit committee will need to request management to inform the committee of:
  - whether the methods chosen by management are consistent with Accounting Standards, Accounting Concepts and Urgent Issues Group (UIG) Consensus Views;
  - any changes in significant accounting policies or their application during the reporting period;
  - the methods used to account for significant unusual transactions or transactions in emerging areas for which there may be no specific accounting standard,
including management’s reasoning in determining the appropriateness of those methods;

and then request the internal and external auditors to inform the committee of their views in relation to these matters.

- Assess significant estimates and judgements in the financial reports by enquiring of management about the process used by management in making material accounting estimates and then enquire of the external auditor as to the basis for the auditor’s conclusions regarding the reasonableness of those estimates.

- Assess information from internal and external auditors, which affects the quality of financial reports (e.g. actual and potential material audit adjustments, financial report disclosures, non-compliance with the laws and regulations, and internal control issues).

- Ask the auditor for an independent judgement about the appropriateness, not just the acceptability, of the accounting principles used and the clarity of the financial disclosure practices used or proposed to be used by the entity as put forward by management.

- Review documents and reports on regulatory issues and make a recommendation to the LGE on their approval or amendment.

7.2 Related-party Transactions

- Review and monitor the propriety of all related-party transactions, being transactions with any entities or individuals associated with the LGE’s activities.

- Related party transactions are those defined in AAS 22 “Related Party Disclosures” as well as transactions between members of the LGE, Council/Regional Library Corporation/Company staff and third external parties involved with the operations of the LGE.

7.3 Internal Control and Risk Management

- Play a key role in establishing an appropriate culture in overall corporate control.

- Assess the internal processes for determining and managing key risk areas, particularly:
  - litigation and claims;
  - non-compliance with laws and regulations;
  - compliance with tendering agreements;
  - important judgements and accounting estimates;
  - risks other than those that are dealt with by other specific committees of the LGE; and
  - commercial risks associated with activities external to the LGE’s core functions.
• Discuss with management the adequacy of the organization’s risk management systems.

• Address the adequacy of the organization’s control structure with management and the internal auditor and seek advice from the external auditor on indications of control deficiencies identified during the course of their audit of the financial report.

• Evaluate the process the organization has in place for assessing and continuously improving internal controls, particularly those related to areas of significant risk.

• Assess whether management has controls in place for identifying and dealing with unusual types of transactions and/or any potential transactions that may carry more than an acceptable degree of risk.

• Recommend the issue of a code of ethical conduct, assist in its overseeing and review ongoing compliance with it.

7.4 External Audit

• Liaise with and monitor issues raised by the external auditor.

• While recognising that the appointment of the external auditor is controlled by the Victorian Auditor-General, consider the reasonableness of the external auditor’s fee and be satisfied that an effective, comprehensive and complete audit can be conducted for the set fee.

• At the start of each audit, discuss the engagement with the external auditor.

• Together with the external auditor, review the scope of the external audit (particularly the identified risk areas) and the scope of any additional agreed-upon procedures on a regular and timely basis.

• Invite the external auditor to attend audit committee meetings to, at least, review the audit plan, discuss audit results and consider the implications of the external audit findings for the control environment.

• Review representation letters, relevant to the committee’s charter, signed by management and assess, to the extent practicable based on committee members’ knowledge of the LGE’s activities, whether the information provided is complete and appropriate.

• Enquire of the auditor if there have been any significant disagreements with management irrespective of whether or not they have been resolved.

• Monitor and critique management’s responsiveness to the external auditor’s findings and recommendations. Review progress by management in implementing audit recommendations and assist the resolution of any issues where this is in disagreement.
7.5 **Internal Audit**

- Review the internal auditor’s mission, charter, qualifications and resources.
- Communicate the committee’s expectations to the internal auditor in writing or through the minutes of the meetings of the committee.
- Ensure that in addition to reporting directly to the Chief Executive Officer, who has functional responsibility for the internal audit function, the internal auditor also reports to the audit committee.
- Review and approve the scope of the internal audit plan and work programme.
- Monitor the progress of the internal audit work programme and consider the implications of the internal audit findings for the control environment.
- Enquire of the auditor if there have been significant disagreements with management irrespective of whether or not they have been resolved.
- Monitor and critique management’s responsiveness to internal audit’s findings and recommendations. Review progress by management in implementing audit recommendations and assist the resolution of any issues where there is disagreement.
- Evaluate the process the LGE has in place for monitoring and assessing the effectiveness of the internal auditor.
- In consultation with the CEO appoint an Internal Auditor and determine and secure appropriate budget approval for the LGE’s Internal Audit function.

7.6 **Co-ordination of Auditors**

- Oversee the work of the internal audit function to facilitate co-ordination with the external auditor.
- Meet periodically with key management staff, internal and external auditors, and compliance staff to understand and discuss the organisation’s control environment.

*Commentary*

The audit committee’s main responsibilities are to ensure that the audit process (both external and internal) is effective, that external reporting and other corporate governance responsibilities are addressed, including that the LGE’s internal control and risk management structures are appropriate.

The audit committee also has a responsibility to consider carefully issues raised by the external and internal auditors as those issues may have implications for the organisation’s control environment.
The audit committee can play a key role in strengthening an organisation's control environment and in establishing an appropriate ethical attitude and culture throughout the organisation.

While it is recognised that the appointment of the external auditor is controlled by the Victorian Auditor-General through a tendering system, the audit committee can assist the LGE in communicating with the external audit contractor appointed by the Victorian Auditor-General by discussing the appointment, remuneration and effectiveness of the external audit function.

Corporate governance can be strengthened if the audit committee’s independent members meet at least once a year with the external auditor and separately with the internal auditor without any management staff or executives present. There may be issues in which the audit committee is interested which involve management and executives; to be effective the committee needs to be able to discuss these issues with the auditor freely.

The committee should play a major role in ensuring that the organisation’s accounting policies and principles are in accordance with the stated financial reporting framework and that the LGE is informed of any significant issues raised by the auditors, management or the committee’s members.

8. Assessing the Audit Committee’s Performance

The audit committee should be subject to a periodic review, including a review by the LGE and the completion of a self-assessment programme. The reviews should include the following:

- Obtaining feedback on the committee’s performance and operations from key people such as the external auditor, the internal auditor, and senior financial and other management staff.

- Obtaining feedback from the LGE on the effectiveness of the committee.

- Assessing the performance of the audit committee against its terms of reference.

- Assessing the contribution of individual committee members (review to be completed by the committee’s chairperson) and the chairperson (review by committee members), for discussion with the Mayor/Shire President/Chairperson of the Regional Library Board/Chairperson of the Local Government Company.

Commentary

To ensure that an audit committee is operating effectively and fulfilling its objectives, a formal assessment process should be established. The assessment process could include interviews with key people outside the committee and the completion of self-assessment questionnaires by committee members regarding the committee’s effectiveness. The process of self-assessment can be facilitated by reference to published self-assessment models which are generally available.
9. Internal Auditor’s Responsibilities

Internal audit, whether internally staffed or outsourced, should provide the audit committee with the following:

- A copy of the formal audit plan, including internal audit’s objectives, work schedules, staffing requirements, budgets, and a description of any limitations placed on internal audit’s scope of work.

- Details of the internal audit staff structure, including staff skills, experience and qualifications.

- Activity reports highlighting significant findings and recommendations, particularly in relation to the LGE’s risk management, and identifying any lack of action by management.

- Major variances from the internal audit functions, goals, work schedules and budgets.

- Advice on the extent to which there is co-ordination of the internal audit plan, which is based on the potential risks faced by the LGE, with the external audit plan.

- Activity reports on any major fraud or conflict of interest.

- Any other information requested by the audit committee.

Commentary

The role of internal audit varies between different LGEs; it could include financial or compliance audits, or it could be used for specific one-off assignments. An effective internal audit function should, among other things, evaluate and monitor the adequacy and effectiveness of the internal control structure. Internal audit is an important component of an organisation’s control environment and can be instrumental in assisting with risk management. It is important for the internal auditor to have direct access to the audit committee and for the committee to monitor the scope of the work of internal audit and to review the reports issued. This can be achieved by having the internal auditor attend meetings of the audit committee.

The audit committee can play an important role in ensuring that the internal audit function is effective by addressing such issues as the level of resources allocated to internal audit, the scope of the authority of internal audit, the appropriateness of the internal audit programme and reporting line, the quality and timeliness of its reports, and the extent to which management reacts to the matters raised by internal audit.

The audit committee can also provide an effective means of formalising and co-ordinating the working relationship between internal and external auditors.
10. **Recommended Charters**

Attached at Appendix 1 and 2 are recommended Charters for the Audit Committee and internal Audit respectively which reflect the key principles from the guidelines. These are provided to assist LGEs implement these recommendations and achieve the objectives of an Audit Committee and Internal Audit function.
Appendix 1

AUDIT COMMITTEE CHARTER – LOCAL GOVERNMENT ENTITIES

1. Recommended Audit Committee Charter

The Audit Committee is an independent advisory Committee to Council. The primary objective of the Audit Committee is to assist Council in the effective conduct of its responsibilities for financial reporting, management of risk, maintaining a reliable system of internal controls and facilitating the organisation’s ethical development.

The Audit Committee is established to assist the co-ordination of relevant activities of management, the internal audit function and the external auditor to facilitate achieving overall organisational objectives in an efficient and effective manner.

As part of Council’s governance obligations to its community, Council has constituted an Audit Committee to facilitate:

- the enhancement of the credibility and objectivity of internal and external financial reporting;
- effective management of financial and other risks and the protection of Council assets;
- compliance with laws and regulations as well as use of best practice guidelines;
- the effectiveness of the internal audit function;
- the provision of an effective means of communication between the external auditor, internal audit, management and the Council.

2. Recommended Terms of Reference

2.1 General

(a) The Audit Committee is a formally appointed committee of the Council and is responsible to that body. The Audit Committee does not have executive powers or authority to implement actions in areas over which management has responsibility and does not have any delegated financial responsibility. The Audit Committee does not have any management functions and is therefore independent of management.

The Committee’s role is to report to Council and provide appropriate advice and recommendations on matters relevant to its Charter in order to facilitate decision-making by Council in relation to the discharge of its responsibilities.

2.2 Membership

(b) The Audit Committee will comprise a minimum of three members – one Councillor and two external independent persons. Committees with a membership greater than
three must include a majority of external independent persons. All members shall have full voting rights.

External independent persons will have senior business or financial management/reporting knowledge and experience, and be conversant with the financial and other reporting requirements. The evaluation of potential members will be undertaken by the Mayor and Chief Executive Officer taking account of the experience of candidates and their likely ability to apply appropriate analytical and strategic management skills, and a recommendation for appointment put to Council.

(d) Appointments of external persons shall be made by Council by way of a public advertisement and be for a maximum term of three years. The terms of the appointment should be arranged to ensure an orderly rotation and continuity of membership despite changes to Council’s elected representatives.

(e) If the Council proposes to remove a member of the Committee, it must give written notice to the member of its intention to do so and provide that member with the opportunity to be heard at a Council meeting which is open to the public, if that member so requests.

(f) Remuneration will be paid to each independent member of the Committee (the basis may be an annual fee, with an additional amount paid to the Chairperson or a set fee per meeting, or another basis as appropriate).

(g) The Chairperson shall be appointed from the external members of the Committee by the Audit Committee subject to Council’s approval. In the absence of the appointed Chairperson from a meeting, the meeting will appoint an acting Chairperson from the external members present.

(h) A quorum shall be two for a Committee with the minimum membership of three. For Committees with membership greater than three, a quorum will be a majority of the Committee membership comprising at least equal representation of internal and external independent members.

(i) The Chief Executive Officer and internal auditor (whether a member of staff or contractor) should attend all meetings, except when the Committee chooses to meet in camera. Other members of Council or Council staff may be invited to attend at the discretion of the Committee to advise and provide information when required.

(j) Representatives of the external auditor should be invited to attend at the discretion of the Committee but must attend meetings considering the draft annual financial report and results of the external audit.

(k) Council shall provide secretarial and administrative support to the Committee.

2.3 Meetings

(l) The Committee shall meet at least quarterly.
A schedule of meetings will be developed and agreed to by the members. As an indicative guide, meetings would be arranged to coincide with relevant Council reporting deadlines, for example in June to coincide with the approval of corporate plans, annual plans and budgets and in August to coincide with the finalisation of the financial statements and the draft annual report to the Minister.

Additional meetings shall be convened at the discretion of the Chairperson or at the written request of any member of the Committee, internal or external auditor.

2.4 Reporting

(m) The Audit Committee shall after every meeting forward the minutes of that meeting to the next ordinary meeting of the Council, including a report explaining any specific recommendations and key outcomes.

(n) The Committee shall report annually to the Council summarising the activities of the Committee during the previous financial year.

2.5 Duties and Responsibilities

(o) The following are the duties and responsibilities of the Audit Committee in pursuing its Charter:

(i) To review the scope of the internal audit plan and programme and the effectiveness of the function. This review should consider whether, over a period of years the internal audit plan systematically addresses:

- internal controls over significant areas of risk, including non-financial management control systems;
- internal controls over revenue, expenditure, assets and liability processes;
- the efficiency, effectiveness and economy of significant Council programmes; and
- compliance with regulations, policies, best practice guidelines, instructions and contractual arrangements.

(ii) Review the appropriateness of special internal audit assignments undertaken by internal audit at the request of Council or Chief Executive Officer.

(iii) Review the level of resources allocated to internal audit and the scope of its authority.

(iv) Review reports of internal audit and the extent to which Council and management react to matters raised by internal audit, by monitoring the implementation of recommendations made by internal audit.
(v) Facilitate liaison between the internal and external auditor to promote compatibility, to the extent appropriate, between their audit programmes.

(vi) Critically analyse and follow up any internal or external audit report that raises significant issues relating to risk management, internal control, financial reporting and other accountability or governance issues, and any other matters relevant under the Committee’s terms of reference. Review management’s response to, and actions taken as a result of the issues raised.

(vii) Monitor the risk exposure of Council by determining if management has appropriate risk management processes and adequate management information systems.

(viii) Monitor ethical standards and related party transactions by determining whether the systems of control are adequate.

(ix) Review Council’s draft annual financial report, focusing on:

- accounting policies and practices;
- changes to accounting policies and practices;
- the process used in making significant accounting estimates;
- significant adjustments to the financial report (if any) arising from the audit process;
- compliance with accounting standards and other reporting requirements;
- significant variances from prior years.

(x) Recommend adoption of the annual financial report to Council. Review any significant changes that may arise subsequent to any such recommendation but before the financial report is signed.

(xi) Discuss with the external auditor the scope of the audit and the planning of the audit.

(xii) Discuss with the external auditor issues arising from the audit, including any management letter issued by the auditor and the resolution of such matters.

(xiii) Review tendering arrangements and advise Council.

(xiv) Review the annual performance statement and recommend its adoption to Council.

(xv) Review issues relating to national competition policy, financial reporting by Council business units and comparative performance indicators.
(xvi) Identify and refer specific projects or investigations deemed necessary through the Chief Executive Officer, the internal auditor and the Council if appropriate. Oversee any subsequent investigation, including overseeing of the investigation of any suspected cases of fraud within the organisation.

(xvii) Monitor the progress of any major lawsuits facing the Council.

(xviii) Address issues brought to the attention of the Committee, including responding to requests from Council for advice that are within the parameters of the Committee’s terms of reference.

(xxiv) Report to Council after each meeting, in the form of minutes or otherwise, and as necessary and provide an annual report to Council summarising the activities undertaken during the year.

(xx) The Audit Committee in conjunction with Council and the Chief Executive Officer should develop the Committee’s performance indicators.

(p) The Audit Committee, through the Chief Executive Officer and following authorisation from the Council, and within the scope of its responsibilities, may seek information or obtain expert advice on matters of concern.
INTERNAL AUDIT CHARTER – LOCAL GOVERNMENT ENTITIES

1. Internal Audit

Internal audit is an independent appraisal activity within an organisation for the review of operations as a service to management. The internal audit function should remain independent of the operational activities; that is, it should not be involved in the day to day management; or administration. The function should have an advisory role in the development and implementation of new systems and procedures.

The objective of the internal audit function is to assist the Local Government Entity (LGE) and management in the effective discharge of their responsibilities. It is a control which functions by measuring and evaluating the effectiveness of other controls and reviewing key risk areas and issues of efficiency, economy and effectiveness. Internal audit is functionally responsible to the Chief Executive Officer for the efficient and effective use of its resources and in meeting its objectives.

The internal audit mandate should be specified as a combination of financial, compliance and performance audit work and other investigations.

2. Recommended Internal Audit Charter

2.1 Develop and maintain an Internal Audit Charter, which is to be approved by the Audit Committee.

2.2 Develop and implement a comprehensive risk based cyclical strategic Audit Plan which is to be approved by the Chief Executive Officer and which is to be reviewed and endorsed by the Audit Committee, and which may incorporate the following key functions:

(a) Reviewing, analysing and reporting on the efficiency and effectiveness of internal control systems and procedures and recommending changes.

(b) Reviewing the LGE’s activities and making assessments and recommendations in relation to risk management.

(c) Monitoring, evaluating and reporting on compliance and probity issues surrounding the management of tendering arrangements, including contract compliance, the annual performance statement, comparative performance indicators, the national competition policy compliance statement, financial reporting by business units of the LGE and competitively neutral pricing guidelines.

(d) Reviewing, assessing and reporting recommended changes to the LGE’s policies, practices and systems in respect to requirements for the highest standards of ethical behaviour and the impact on the LGE’s financial statements and performance.
(e) Providing strategic advice, conducting and completing corporate governance and compliance audits to assess performance against the LGE’s corporate, financial and strategic plans.

(f) Conducting investigations of any special cases of fraud within the organisation and monitoring the progress of any major law suits facing the LGE.

(g) Reviewing policies, procedures and controls having appropriate regard of information technology systems employed.

(h) Monitoring the implementation of all due diligence audit recommendations and recommendations of the Audit Committee as adopted by the LGE.

(i) Review of key performance indicators for the Committee and the monitoring and reporting of performance against the identified measures to the Chief Executive Officer, Audit Committee and LGE.

2.3 Develop and implement a detailed annual Internal Audit Work Programme, which is to be approved by the Chief Executive Officer and endorsed by the Audit Committee.

2.4 Provide advice to the LGE, Chief Executive Officer and management as requested, including the development of policies and procedures.

2.5 Undertake special assignments as requested by the Chief Executive Officer.

2.6 Liaise with the external auditor and co-ordinate audit coverage.

2.7 Report to the Chief Executive Officer and LGE Audit Committee.

2.8 Undertake internal audit work in accordance with the professional auditing standards, codes of conduct and ethics promulgated by organisations such as the Australian Society of Certified Practising Accountants, the Institute of Chartered Accountants in Australia and the Institute of Internal Auditors – Australia.

2.9 Financial audit work will take into consideration the extent to which the area concerned is already covered by the external auditor.