J. Our assessment of councils' financial governance

Auditing internal controls

Entities design, implement, and maintain internal controls (people, systems, and processes) to deliver reliable financial reporting, effective and efficient operations, and compliance with applicable laws and regulations.

In undertaking our audit, we are required under the Australian auditing standards to obtain an understanding of an entity's internal controls relevant to the preparation of the financial report.

We assess internal controls to ensure they are suitably designed to:

- prevent, or detect and correct, material misstatements in the financial report (which could influence a user's decision-making)

- achieve compliance with legislative requirements and make appropriate use of public resources.

Our assessment determines the nature, timing, and extent of the testing we perform to address the risk of significant mistakes in the financial statements.

If we believe the design and implementation of controls is effective, we select the controls we intend to test further. We do this by considering a balance of factors including:

- the significance of the related risks

- the characteristics of balances, transactions, or disclosures (volume, value, and complexity)

- the nature and complexity of the entity's information systems

- whether the design of the controls addresses the risk of material misstatement and facilitates an efficient audit.

If we identify deficiencies in internal controls, we determine the impact on our audit approach, considering whether additional audit procedures are necessary.

We design our audit procedures to address the risk of material misstatement so we can express an opinion on the financial report. We do not express an opinion on the effectiveness of internal controls.

Internal controls framework

We categorise internal controls using the Committee of Sponsoring Organizations of the Treadway Commission (COSO) internal controls framework, which is widely recognised as a benchmark for designing and evaluating internal controls.

The framework identifies 5 components for a successful internal control framework. These are explained in the following paragraphs.

Control environment

- Cultures and values
- Governance
- Organisational structure
- Policies
- Qualified and skilled people
- Management's integrity and operating style

The control environment is defined as the structures, policies, attitudes, and values that influence day-to-day operations. As the control environment is closely linked to an entity's overarching governance and culture, it is important that the control environment provides a strong foundation for the other components of internal control.

In assessing the design and implementation of the control environment, we consider whether:

- those charged with governance are independent, appropriately qualified, experienced, and active in challenging management

- policies and procedures are established and communicated so people with the right qualifications and experiences are recruited; they understand their role in the organisation; and they also understand management's expectations regarding internal controls, financial reporting, and misconduct, including fraud.

Risk assessment

- Strategic risk assessment
- Financial risk assessment
- Operational risk assessment

Risk assessment relates to management's processes for considering risks that may prevent an entity from achieving its objectives; and how management agrees risks should be identified, assessed, and managed.

To appropriately manage business risks, management can either accept the risk if it is minor or mitigate the risk to an acceptable level by implementing appropriately designed controls. Management can also eliminate risks entirely by choosing to exit from a risky business venture.

Control activities

- General information technology controls
- Automated controls
- Manual controls

Control activities are the actions taken to implement policies and procedures in accordance with management directives, and to ensure identified risks are addressed. These activities operate at all levels and in all functions. They can be designed to prevent or detect errors entering financial systems.

The mix of control activities can be categorised into general information technology controls, automated controls, and manual controls.

General information technology controls

General information technology controls form the basis of the automated systems control environment. They include controls over information systems security, user access, and system changes. These controls address the risk of unauthorised access and of changes to systems and data.

Automated control activities

Automated controls are embedded within information technology systems. These controls can improve timeliness, availability, and accuracy of information by consistently applying predefined business rules. They enable entities to perform complex calculations when processing large volumes of transactions. They also improve the effectiveness of financial delegations and the segregation of duties.

Manual control activities

Manual controls contain a human element, which can provide the opportunity to assess the reasonableness and appropriateness of transactions. However, these controls may be less reliable than automated elements, as they can be more easily bypassed or overridden. They include activities such as approvals, authorisations, verifications, reconciliations, reviews of operating performance, and segregation of incompatible duties. Manual controls may be performed with the assistance of information technology systems.

Information and communication

- Non-financial systems
- Financial systems
- Reporting systems

Information and communication controls are the systems used to provide information to employees, and the ways in which responsibilities are communicated.

This aspect of internal control also considers how management generates financial reports, and how these reports are communicated to internal and external parties to support the functioning of internal controls.

Monitoring activities

- Management supervision
- Self-assessment
- Internal audit

Monitoring activities are the methods management uses to oversee and assess whether internal controls are present and operating effectively. This may be achieved through ongoing supervision, periodic self-assessments, and separate evaluations. Monitoring activities also concern the evaluation and communication of control deficiencies in a timely manner to effect corrective action.

Typically, the internal audit function and an independent audit and risk committee are responsible for assessing and overseeing management's implementation of controls and their resolution of control deficiencies. These 2 functions work together to ensure that internal control deficiencies are identified and then resolved in a timely manner.

Assessment of internal controls

Our assessment of internal control effectiveness is based on the number of deficiencies and significant deficiencies we identified during our audit. We assess each of the 5 components of a successful internal control framework separately.

Assessment of internal controls	
Rating scale	Assessment criteria
● Effective	No significant (high-risk) deficiencies
● Partially effective	One significant deficiency
● Ineffective	More than one significant deficiency

The deficiencies detailed in this report were identified during our audit and may have been subsequently resolved by the entity.

They are reported here because they impacted on the overall system of control during 2021–22.

Financial statements preparation process

Until the 2019–20 financial year, we assessed the effectiveness of the financial statement preparation processes across 3 components:

- Year-end close processes – was based on early completion of 5 key elements of financial statements

- Timeliness of financial statements – compared the date the financial statements were certified against the legislative deadline of 31 October

- Quality of financial statements – was assessed based on the number of changes that are made between the draft of the financial statements submitted to audit and the final audited financial statements.

Each component was assigned a traffic light (red/amber/green), and this was reported to each council and in our annual reports to parliament.

In the 2020–21 financial year, we changed the way we assessed the financial statement preparation process to a maturity model (which is available on our website at www.qao.qld.gov.au/reports-resources/better-practice). The model is entity-driven and is scalable to each entity's size and complexity. It aims to bring flexibility in responding to the qualitative factors that influence entities' practices, which the previous assessment criteria did not take into account.

The model facilitates sharing of better practices across the public sector. It also brings focus to entities' areas of development to allow them to reach their targeted positioning.

For the 2020–21 financial year, we asked councils to self-assess their financial statement preparation processes using this model. In the 2022–23 financial year, we will work with councils to ensure that their self-assessed maturity levels reflect the reality of their strengths and weaknesses of their processes. We will report on the outcome of this assessment in our *Local government 2023* report.

Financial sustainability relative risk assessment

The detailed criteria for assessing a council's financial sustainability are explained in Appendix I – Figures I1 and I2. The overall assessment criteria are shown in Figure I3. Colours used for the overall risk levels are lower risk (green), moderate risk (amber), and higher risk (red).

Results summary

The following tables summarise the results of our assessment of the 77 councils' internal controls, by council segment.

Figure J1
Our assessment of the financial governance of councils by segment

Council	Internal controls						Financial sustainability	Days to complete from year end

Key:
CE = Control environment; RA = Risk assessment; CA = Control activities; IC = Information and communication;
MA = Monitoring activities.
OS = Number of significant deficiencies outstanding longer than 12 months at 30 June 2022
FS = Financial sustainability — relative risk assessment (refer Figure I4).
D = Number of days to have audit opinion certified from 30 June 2022 (number of days between 30 June and 31 October is 123)

Coastal councils	CE	RA	CA	IC	MA	OS	FS	D
Bundaberg Regional Council	🟢	🟢	🟢	🟢	🟢	-	🟡	99
Burdekin Shire Council	🟢	🟢	🟢	🟢	🟢	-	🟢	70
Cairns Regional Council	🟢	🟢	🟢	🟢	🟢	-	🟢	78
Cassowary Coast Regional Council	🟡	🟢	🟢	🟢	🟢	-	🟡	106
Douglas Shire Council	🟢	🟢	🟢	🟢	🟢	-	🟡	104
Fraser Coast Regional Council	🟢	🟢	🟡	🟢	🟢	1	🟢	91
Gladstone Regional Council	🟢	🟢	🟢	🟢	🟢	-	🟡	120
Gympie Regional Council	🟢	🟢	🔴	🟢	🟢	2	🟡	249
Hinchinbrook Shire Council	🟢	🟢	🟢	🟢	🟢	-	🔴	123
Livingstone Shire Council	🟢	🟢	🟡	🟢	🟢	1	🟢	123
Mackay Regional Council	🟢	🟢	🟢	🟢	🟢	-	🟢	102
Noosa Shire Council	🟢	🟢	🟡	🟢	🟢	1	🟢	118
Rockhampton Regional Council	🟢	🟢	🟢	🟢	🟢	-	🟢	105
Townsville City Council	🟢	🟢	🔴	🟢	🟢	1	🟡	97
Whitsunday Regional Council	🟢	🟢	🟢	🟢	🟢	-	🟢	48

Council	Internal controls						Financial sustainability	Days to complete from year end

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Indigenous	CE	RA	CA	IC	MA	OS	FS	D
Aurukun Shire Council	●green	●green	●green	●green	●green	-	●red	104
Cherbourg Aboriginal Shire Council	●green	●green	●green	●green	●yellow	1	●green	113
Doomadgee Aboriginal Shire Council	●green	●green	●green	●green	●green	-	●red	123
Hope Vale Aboriginal Shire Council	●green	●green	●green	●green	●green	-	●green	29
Kowanyama Aboriginal Shire Council	●green	●green	●red	●green	●green	-	●red	103
Lockhart River Aboriginal Shire Council	●green	●green	●green	●green	●green	-	●yellow	123
Mapoon Aboriginal Shire Council	●green	●green	●yellow	●green	●green	1	●red	123
Mornington Shire Council*	●green	●yellow	●red	●green	●green	4	●red	Not Complete
Napranum Aboriginal Shire Council	●green	●green	●red	●yellow	●green	2	●red	117
Northern Peninsula Area Regional Council*	●red	●green	●red	●red	●yellow	1	●red	Not Complete
Palm Island Aboriginal Shire Council*	●yellow	●green	●red	●yellow	●green	11	●red	Not Complete
Pormpuraaw Aboriginal Shire Council	●green	●green	●green	●green	●green	-	●green	70
Torres Shire Council	●green	●green	●green	●red	●green	-	●red	123
Torres Strait Island Regional Council	●green	●green	●green	●green	●green	-	●red	81
Woorabinda Aboriginal Shire Council*	●red	●green	●red	●yellow	●yellow	8	●red	Not Complete
Wujal Wujal Aboriginal Shire Council	●yellow	●yellow	●yellow	●green	●green	3	●red	118
Yarrabah Aboriginal Shire Council	●green	●green	●yellow	●green	●green	1	●red	105

Council	Internal controls						Financial sustainability	Days to complete from year end

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Resources councils	CE	RA	CA	IC	MA	OS	FS	D
Banana Shire Council	🟢	🟢	🟢	🟢	🟢	-	🟡	123
Bulloo Shire Council	🔴	🟢	🔴	🟢	🟢	1	🟡	123
Burke Shire Council	🟢	🟢	🟢	🟢	🟢	-	🔴	123
Central Highlands Regional Council	🟢	🟢	🔴	🟡	🟢	3	🟢	123
Charters Towers Regional Council	🟢	🟢	🟡	🟢	🟢	1	🟢	123
Cloncurry Shire Council	🟢	🟢	🔴	🟡	🟢	1	🟡	209
Cook Shire Council	🟢	🟢	🔴	🟢	🟢	2	🔴	105
Etheridge Shire Council	🟢	🟢	🔴	🟡	🟢	2	🟡	167
Isaac Regional Council	🟢	🟢	🟢	🟢	🟢	-	🟢	120
Maranoa Regional Council	🟢	🟢	🟢	🟢	🟢	-	🟢	110
McKinlay Shire Council	🟢	🟢	🟡	🟢	🟢	1	🟡	105
Mount Isa City Council	🔴	🟢	🔴	🟡	🟢	3	🟢	116
Quilpie Shire Council	🟢	🟢	🟡	🟢	🟢	-	🟡	123
Western Downs Regional Council	🟢	🟢	🟢	🟢	🟢	-	🟢	106

Council	Internal controls						Financial sustainability	Days to complete from year end

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Rural/Regional councils	CE	RA	CA	IC	MA	OS	FS	D
Goondiwindi Regional Council	● (green)	● (green)	● (green)	● (green)	● (green)	-	● (green)	83
Lockyer Valley Regional Council	● (green)	● (green)	● (green)	● (green)	● (green)	-	● (green)	169
Mareeba Shire Council	● (green)	● (green)	● (green)	● (green)	● (green)	-	● (green)	97
North Burnett Regional Council	● (green)	● (green)	● (red)	● (green)	● (green)	1	● (red)	259
Scenic Rim Regional Council	● (green)	● (green)	● (green)	● (green)	● (amber)	-	● (green)	99
Somerset Regional Council	● (green)	● (green)	● (green)	● (green)	● (green)	-	● (green)	103
South Burnett Regional Council	● (green)	● (green)	● (green)	● (green)	● (green)	-	● (green)	105
Southern Downs Regional Council	● (green)	● (green)	● (green)	● (green)	● (green)	-	● (green)	110
Tablelands Regional Council	● (green)	● (green)	● (amber)	● (green)	● (green)	1	● (green)	123

Council	Internal controls						Financial sustainability	Days to complete from year end

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Rural/Remote councils	CE	RA	CA	IC	MA	OS	FS	D
Balonne Shire Council	green	green	green	green	green	-	yellow	120
Barcaldine Regional Council	green	green	green	yellow	green	1	red	123
Barcoo Shire Council	green	green	green	red	green	2	red	111
Blackall-Tambo Regional Council	green	green	green	green	green	-	yellow	123
Boulia Shire Council	green	green	yellow	green	green	1	red	165
Carpentaria Shire Council	yellow	green	red	yellow	green	6	red	123
Croydon Shire Council	green	green	red	green	green	2	green	140
Diamantina Shire Council	green	green	green	green	green	-	yellow	123
Flinders Shire Council	green	green	green	green	green	-	green	119
Longreach Regional Council	green	green	green	green	green	-	red	119
Murweh Shire Council	green	green	yellow	green	green	-	red	116
Paroo Shire Council	yellow	green	green	yellow	green	1	red	120
Richmond Shire Council	green	green	red	green	green	2	red	249
Winton Shire Council	green	green	green	green	green	-	yellow	106

Council	Internal controls						Financial sustainability	Days to complete from year end

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MA = Monitoring activities.
OS = Number of significant deficiencies outstanding longer than 12 months at 30 June 2022
FS = Financial sustainability — relative risk assessment (refer Figure I4).
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South East Queensland councils	CE	RA	CA	IC	MA	OS	FS	D
Brisbane City Council	🟢	🟢	🟢	🟢	🟢	-	🟡	46
Council of the City of Gold Coast	🟢	🟢	🔴	🟡	🟢	3	🟡	91
Ipswich City Council	🟢	🟢	🟢	🟢	🟢	-	🟡	120
Logan City Council	🟢	🟢	🟡	🟢	🟢	1	🟢	76
Moreton Bay Regional Council	🟢	🟢	🟡	🟢	🟢	1	🟢	104
Redland City Council	🟢	🟢	🟢	🟢	🟢	-	🟡	81
Sunshine Coast Regional Council	🟢	🟢	🔴	🟢	🟢	-	🟢	102
Toowoomba Regional Council	🟢	🟢	🟡	🟢	🟡	1	🟢	92

Notes:
* The internal controls assessments are based on the previous year's results because the 2021–22 financial year audit has not yet been completed.

Source: Queensland Audit Office.