

**ITEM 3. PRESENTATION OF THE 2016/17 FINANCIAL STATEMENTS AND
AUDIT REPORTS TO COUNCIL**

FILE NO: X006437

SUMMARY

This report presents the City's 2016/17 Financial Statements to Council and seeks authorisation to issue the public notice of the intention to present the audited statements to the public at the Council meeting of 13 November 2017.

The City of Sydney's Income Statement for the year ended 30 June 2017 reports a Net Operating Result for the year of \$144.0M, in accordance with relevant accounting standards and reporting requirements, against a budget of \$30.6M. The increase above budget is mainly due to the higher than expected level of capital grants and contributions during the year, reflecting the dedication of land and works to the City through Voluntary Planning Agreements with developers, and revaluation of the City's Investment Properties.

In finalising the 2016/17 Financial Statements, some further adjustments were made to the results reported to Council within the 2016/17 Quarter 4 Review of the Delivery Program. These adjustments are summarised in the attached background information.

The Statement of Financial Position reports Net Assets of \$11.9B, an increase of \$1.6B over the year. This significant increase can largely be attributed to the Office of Local Government-mandated revaluation of certain fixed asset classes, in particular operational land, buildings and infrastructure assets.

The City of Sydney remains in a strong, stable financial position. The City is well placed to fund its operations on an ongoing basis, with sufficient financial resources to support its ongoing operations and programs, and the \$1.7B capital works program identified within the City's 2017/18 to 2026/27 Long Term Financial Plan.

The 2016/17 financial statements incorporate mandatory disclosures of financial performance ratios within the Statement of Performance Measurement (Note 13 of the General Purpose Financial Statements) and the Report on Infrastructure Assets (Special Schedule 7). The ratios include those mandated as part of the Fit for the Future benchmarks, as well as other relevant performance indicators.

Effective measurement and monitoring of a range of relevant performance indicators, particularly those related to asset management, remains an ongoing challenge. The City supports the ongoing effort to assess and report each council's financial and asset management sustainability, and will continue to work with the Office of Local Government (OLG) to refine the definition and appropriate benchmarks set for financial indicators. In the interim, the City has reported all mandatory indicators, and additional (supplementary) indicators where it believes these provide more relevant information for the readers of the financial statements.

The City's external auditor, the Audit Office of NSW, has completed its review and advised that it will be issuing an unqualified audit opinion on the 2016/17 Financial Statements.

RECOMMENDATION

It is resolved that Council:

- (A) receive the Financial Statements for City of Sydney for the year ended 30 June 2017, as shown at Attachment A to the subject report;
- (B) authorise the Lord Mayor, Councillor Scully (member – Audit, Risk and Compliance Committee), the Chief Executive Officer, and the Chief Financial Officer to sign the General Purpose Financial Statements;
- (C) authorise the Lord Mayor, Councillor Scully (member – Audit, Risk and Compliance Committee), the Chief Executive Officer, and the Chief Financial Officer to sign the Special Purpose Financial Statements;
- (D) receive the auditor's reports on the 2016/17 Annual Financial Statements; and
- (E) authorise that notice be given, by newspaper advertisement, of public presentation of the audited 2016/17 Financial Statements for the City of Sydney at the Council meeting on 13 November 2017.

ATTACHMENTS

Attachment A: 2016/17 Financial Statements

Attachment B: Auditor's Report on the 2016/17 Financial Statements

BACKGROUND

1. The 2016/17 Financial Statements have been prepared for the City of Sydney in accordance with applicable Australian Accounting Standards and Interpretations issued by the Australian Accounting Standards Board, the Local Government Act 1993 and Regulations and the Local Government Code of Accounting Practice and Financial Reporting (the Code).
2. The Annual Financial Statements comprise the:
 - (a) General Purpose Financial Statements**
 - (i) Income Statement
 - (ii) Statement of Comprehensive Income
 - (iii) Statement of Financial Position
 - (iv) Statement of Changes in Equity
 - (v) Statement of Cash Flows
 - (b) Special Purpose Financial Statements**
 - (i) Income Statement of Business Activities
 - (ii) Statement of Financial Position of Business Activities
 - (c) Special Schedules (note that these schedules are not subject to audit)**
 - (i) Special Schedule 1 – Net Cost of Services
 - (ii) Special Schedule 7 – Report on Infrastructure Assets
 - (iii) Special Schedule 8 – Permissible Income Calculation
3. Notes to the accounts provide supporting information, and these, together with the above Financial Statements, fulfil all related statutory financial reporting requirements and are included within the City's Annual Report.
4. The Audit Office of NSW, the City's external auditor, has reviewed the Financial Statements and has indicated that it will provide the City with an unqualified audit opinion.
5. The Office of Local Government requires councils to value non-current assets at fair value on a staged approach of valuing different asset classes in different years, and to continue the cycle on a rolling basis.
6. As a result, the valuation process comprises revaluations of each asset class on a maximum five year cycle basis. The City has the option to undertake valuations more frequently, if required.

7. For 2016/17, the following classes/asset types were revalued, in accordance with Office of Local Government requirements:
 - Operational Land resulting in a net revaluation increment of **\$937.1M**
 - Buildings (specialised and non-specialised) in a net revaluation increment of **\$669.1M**
 - Crown Land (Crown owned land controlled by the City and held in trust), resulting in a net revaluation decrement of **\$1,334.1M**
 - Infrastructure Assets: Roads, bridges, footpaths and kerbs resulting in a net revaluation decrement of **\$206.7M**
 - Infrastructure Assets: Stormwater Drainage, resulting in a net revaluation increment of **\$38.4M**
 - Trees resulting in a net revaluation increment of **\$26.1M**
8. The City is also seeking to work with the Office of Local Government to develop approaches to fixed asset valuation that meet Australian Accounting Standards and are consistently and applied across the local government sector. Valuation adjustments, which are notional book entries and non-cash in nature, can have a very significant impact on the financial position of a Council.
9. The draft Financial Statements were reviewed by the Audit Risk and Compliance Committee on 9 October 2017 for endorsement to Council for authorisation.
10. The 2016/17 financial statements incorporate mandatory disclosures of financial performance ratios within the Statement of Performance Measurement (Note 13 in the General Purpose Financial Statements) and the Report on Infrastructure Assets (Special Schedule 7).
11. While the City supports the ongoing measurement and monitoring of a range of relevant performance indicators, to assess and report each council's financial and asset management sustainability, there remain a number of reservations about the current definition and mandatory benchmarks for several of these indicators. The City's management and financial staff have provided submissions on these concerns, as have a number of other local government professionals and auditors, and we will continue to work with the Office of Local Government to refine the current suite of indicators.
12. In cases where the mandatory ratios provide an inadequate or misrepresentative measure of the City's underlying financial performance and/or position, the City has provided supplementary indicators that eliminate some or all of these inadequacies to present a more realistic and balanced view. The importance of providing this additional disclosure to the readers of the financial statements was brought into focus by the NSW Government's '*Fit for the Future*' program for local government reform. The City's submission to IPART in 2015 in respect of *Fit for the Future* articulated the inherent shortcomings of the key ratios and benchmarks, including Operating Performance, Debt Service (benchmark) and Asset Renewal.

FINANCIAL IMPLICATIONS

13. The Financial Statements reflect a Net Operating Result of \$144.0M (versus Budget \$30.6M) and a Net Operating Result excluding Capital Grants and Contributions of \$24.9M (versus Budget (\$34.2M)). The favourable result against budget is mainly due to the higher than expected level of capital grants and contributions during the year for the dedication of land and works to the City, at no cost, as a result of Voluntary Planning Agreements with developers, and a significant revaluation increment in respect of the City's Investment Properties.
14. The Q4 Report to Council on 7 August 2017 reflected a Net Surplus of \$96.1M (versus Budget \$30.6M). There is a difference of \$47.9M between the Q4 Net Surplus and the 2016/17 Financial Statements' Net Operating Result.

Movements from the Q4 Report to the Financial Statements comprised:

	\$M Fav/(Unfav)
Net Operating Result (reported at Q4 Review)	\$96.1
Revaluation of Investment Property Portfolio	\$44.7
Recognition of Capital Contributions Income (works in kind and land dedication recognition)	\$12.2
Finalise accounting treatment for expensing of non-capital items from capital works	(\$7.9)
Depreciation adjustments resulting from fixed asset finalisation	(\$0.9)
Asset disposals arising from finalisation of completed capital projects and asset revaluation process	(\$0.7)
Finalise Public Liability Provision balance - adjustment amount booked to Public Liability Expense	\$0.4
Minor year-end accrual adjustments	\$0.1
Net Operating Result (Final)	\$144.0

15. The significant variances to budget were explained in detail in the Q4 Report which was presented to Council on 7 August 2017.
16. Since that report, additional Capital Contributions of \$12.2M were recognised as a result of finalising the accounting treatment of land dedicated to the City from Voluntary Planning Agreements with developers, largely comprising land under roads.
17. The City's independent property valuers, undertook the revaluation of the City's investment properties' and the increase in the portfolio was significantly higher than in previous years (\$44.7M in 2016/17, compared to \$17.3M in 2015/16). This result reflected positive market conditions in areas where properties are held, particularly in the CBD.
18. The City of Sydney remains in a strong, stable financial position. The City is well placed to fund its operations on an ongoing basis, with sufficient financial resources to support the \$1.7B capital works program identified within the City's 2017/18 to 2026/27 Long Term Financial Plan.

RELEVANT LEGISLATION

19. The *Local Government Act (1993)* requires Council's annual financial statements to be prepared and audited within four months after the end of the year concerned (section 416(1)).
20. The *Local Government Act (1993)* further requires that, as soon as practicable after a Council receives a copy of the auditor's reports:
 - (a) it must fix a date for the meeting at which it proposes to present its audited financial statements, together with the auditor's reports, to the public; and
 - (b) it must give public notice of the date so fixed (section 419(1)).
21. This meeting must be held within five weeks of the receiving the audit opinion.

CRITICAL DATES / TIME FRAMES

22. The 2016/17 Financial Statements must be prepared, audited and submitted to the Office of Local Government by 31 October 2017.
23. A public notice must be placed to advise that the 2016/17 Financial Statements and the Auditor's Report will be presented to the public at the Council meeting of 13 November 2017. The Financial Statements will be included in the Annual Report which must be lodged with the Office of Local Government by 30 November 2017.

PUBLIC CONSULTATION

24. After the City's 2016/17 Financial Statements are endorsed by Council, a notice will be issued to present the audited statements to the public at the Council meeting of 13 November 2017.

BILL CARTER

Chief Financial Officer