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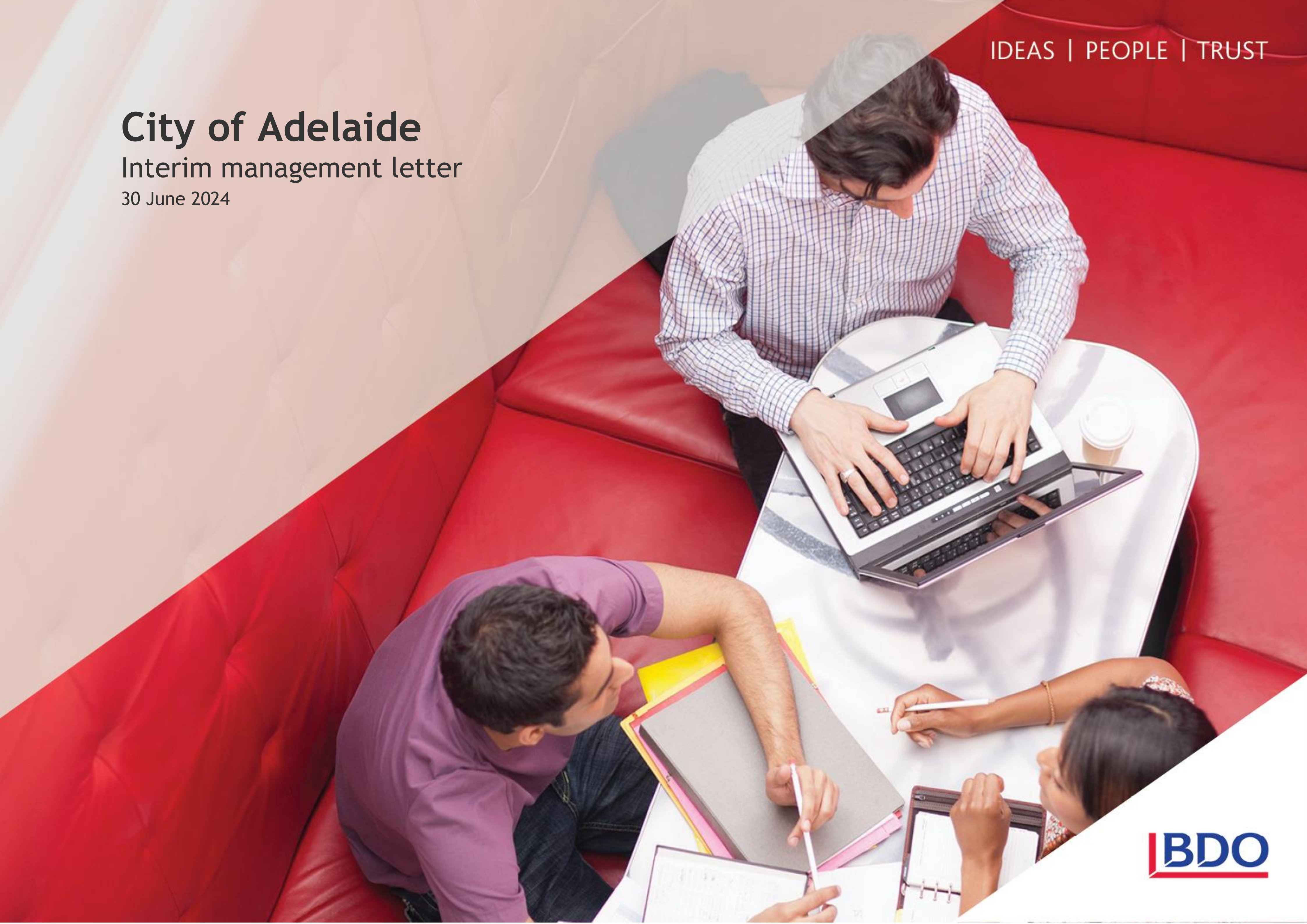
City of Adelaide

Interim management letter

30 June 2024



Contents

Dear Audit and Risk Committee Members

Thank you for the opportunity to present our interim management letter for City of Adelaide for the year ending 30 June 2024.

We have now completed our interim visit and finalised our audit plan for the audit. We acknowledge that there may be further business developments, circumstances may change and additional matters may arise. Our audit approach will be responsive to these changes and will maximise audit effectiveness so we can deliver the high-quality audit you expect.

This letter is intended solely for management and the Audit and Risk Committee and is not intended to be and should not be used by anyone other than these specified parties.

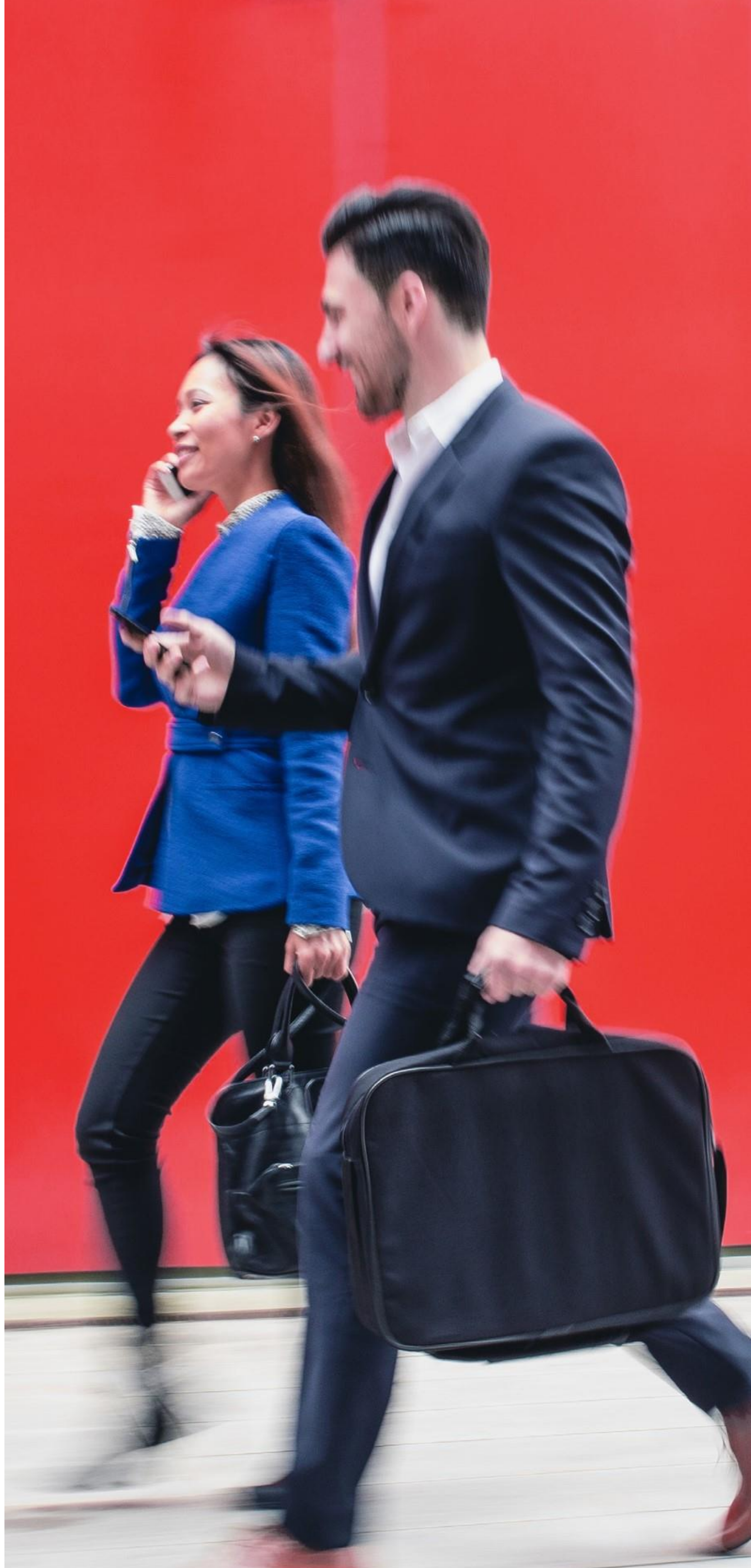
We welcome the opportunity to discuss this letter with you at the Committee meeting on 14 June 2024.

Please feel free to contact me on +61 8 7324 6147 if you have any questions or would like to discuss the content of this plan further.

Yours faithfully

Linh Dao
Lead audit partner

Adelaide, 30 May 2024

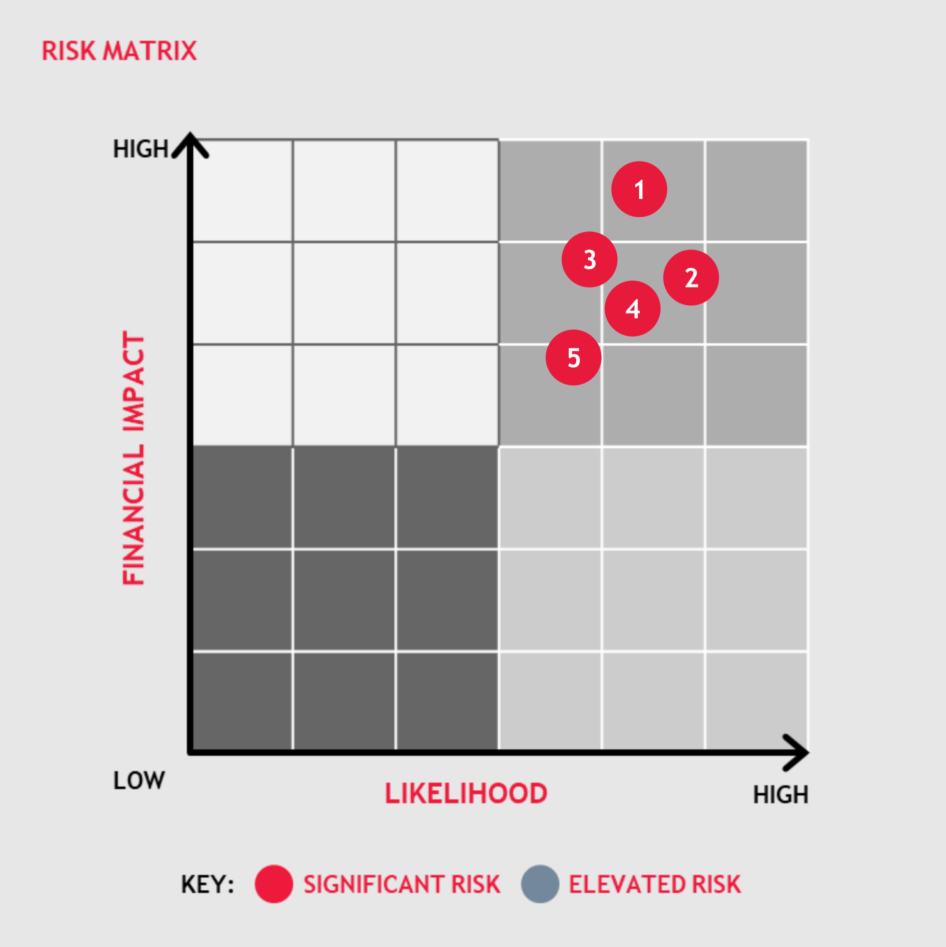


Risk assessment and areas of focus update

In line with our audit approach and based on our understanding of City of Adelaide, we have identified the risks of material misstatement (RMM) at both the engagement and assertion level. In assessing the RMMs, we use a spectrum of risk based on the likelihood of a misstatement occurring and the magnitude of the misstatement in the context of our materiality. We use inherent risk factors (complexity, subjectivity, change, uncertainty or susceptibility to misstatement due to management bias or fraud) to drive risk identification and assessment.

Our initial assessment is shown in the matrix for the risks identified at the upper end of our spectrum (Significant and Elevated).

On the subsequent page we have set out our perspective on the potential impact on the financial statements and the status update on these key issues. We will continue to be alert for risks during the course of the audit and update our assessment and responses as required.



Risk assessment and areas of focus *continued*

#	AREAS OF FOCUS	OUR PERSPECTIVE	STATUS UPDATE
1	Revaluation of infrastructure assets	Council’s infrastructure assets, land and buildings are carried at valuation. There is a risk that these balances are misstated as a result of the application of inappropriate valuation methodologies, or incorrect underlying assumptions.	We have been briefed by management that there will be revaluations of Road, Stormwater and Drainage, Bridge, Kerb & Water Table. We have had preliminary discussion with management on the proposed valuation methodologies for individual classes of assets. Management has also advised us that a decision was made to undertake indexation for certain material classes of assets in between formal revaluations to ensure the compliance with AASB 116 requirements. This year, indexation will be applied for the Footpath class of assets. We expect that the revaluation work will be completed before the commencement of our year-end visit.
2	Accounting treatment of Capital Work in Progress (WIP)	There is a risk that the accounting treatment of items captured within Capital WIP may not be in accordance with Australian Accounting Standards.	We have been briefed on the progress in relation to capital work in progress, in particular the capitalisation and/or expensing of items and the handover process of completed capital projects during the year. Similar to prior year, management does not intend to perform any manual capitalisation for assets that have reached practical completion before the reporting date as part of the year-end process and all capitalisation will happen in Assetic. Projects that have reached practical completion but not yet been capitalised to Assetic will remain in WIP and management has assessed that any depreciation impact on Council’s surplus or deficit would be clearly trivial to the financial statements. It is expected that the underlying asset records and associated reconciliations for Capital WIP will be completed before the commencement of our year-end visit.

Risk assessment and areas of focus *continued*

#	AREAS OF FOCUS	OUR PERSPECTIVE	STATUS UPDATE
3	Management override of internal controls	Australian Auditing Standards require that we presume there is a risk that management has the ability to manipulate accounting records and override control that otherwise appear to be operating effectively.	Our interim testing has not identified any evidence of management override of internal controls. We will revisit this during our year-end visit, complete our testing and report our findings accordingly.
4	Cut-off of grant funding and accuracy of any amounts deferred at 30 June 2024	There is a risk of error in the calculation of grant income recognised and deferred at the end of the year by reference to grant agreements and Australian Accounting Standards.	Council continued to be awarded a significant number of grants during the year. However, the ability to effectively spend these grants has been limited due to the shortage of contractors or internal resources. As a result, it is expected that there will be a significant portion of grant funding to be deferred as at 30 June 2024 and carried forward into following reporting period. We have been provided with Council's grant register and been briefed on management's assessment process to determine whether a grant is of capital or operating nature. We have made initial inquiries with management and will revisit this accounting during our year-end visit.

Risk assessment and areas of focus *continued*

#	AREAS OF FOCUS	OUR PERSPECTIVE	STATUS UPDATE
5	Assets held for sale & discontinued operations	In prior year, Council reported $26mil non-current assets held for sale relating to the former Franklin Street bus terminal. A contract for sale and purchase has been entered into with regard to this site during the year. Furthermore, Council and State Government entered into an agreement to develop a new Adelaide Aquatic Centre (AAC). Under this arrangement, the current AAC will cease operations from August 2024. These agreements are complex in nature involving various components that need accounting for separately under relevant Australian Accounting Standards.	Management's position papers have been provided to us for consideration for both transactions. Discussions have been had with management around the accounting treatment and requests for additional information/ audit supporting documents have been provided to management. We will revisit this during our year-end visit.

Risk assessment and areas of focus *continued*

Other matters

Lease accounting

Council has a number of lease arrangements in place both as a lessor and a lessee. Subsequent to the presentation of our annual audit plan, we identified one additional risk with regard to the ongoing reassessment of lease accounting for changes during the year. We had initial discussion with management with regard to overall changes to the lease portfolio during the year and will reassess the impact at the year-end visit.

Central Market Arcade Redevelopment (‘CMAR’)

We have been briefed by management on the progress of CMAR project to date. We have held discussion with management about their considerations with regard to the accounting for any potential changes in the project, including cash flows. We will revisit the matter during our year-end visit to assess the measurement and recognition of any contract balances associated with the projects, as well as disclosures made in the financial statements.

Internal Control Assessment

Update on our audit opinion in relation to internal controls

We have commenced planning and testing of internal controls for the purpose of providing an audit opinion on Council's internal controls. Specifically controls exercised by the Council in relation to the receipt, expenditure and investment of money, the acquisition and disposal of property and the incurring of liabilities are sufficient to provide reasonable assurance that the financial transactions of the Council have been conducted properly and in accordance with legislative requirements.

Our assessment of internal controls is based on the criteria in the *Better Practice Model – Financial Internal Control for South Australian Councils* as issued by the Local Government Association of South Australia.

At the time of this report, we have not completed all testing of core controls as some relate to annual processes and consequently will not occur until the end of the financial year, or others are more closely aligned to testing we would normally conduct after year end. The controls to be tested did not yield exceptions in the prior year nor does the current Promapp reporting indicate significant issues.

Based on the work to date, we have not noted any material exceptions that would lead to a qualification to the audit report on internal controls. We will continue our work on internal controls at the year-end visit and will report to Council accordingly.

Please contact me if you have any questions or need any further information.

Appendix 1 New developments

Changes in financial reporting for 30 June 2024

AASB 2021-2 *Amendments to Australian Accounting Standards - Disclosure of Accounting Policies and Definition of Accounting Estimates*

Effective for annual reporting periods beginning on or after 1 January 2023 (30 June 2024 year ends), these amendments clarify that accounting policies are only disclosed if they are material, and also introduce a definition of 'accounting estimate'. Similar changes apply if preparing financial statements using Simplified Disclosures.

Material accounting policies

Accounting policies are typically only material if they relate to transactions and balances where:

- There is an accounting policy choice (such as cost or fair value)
- Significant judgements are made in applying a policy
- The accounting is complex and users would not otherwise understand the transaction
- There has been a change in accounting policy during the period and the impact on the financial statements is material, or
- The entity has developed an accounting policy applying the hierarchy in AASB 108 *Accounting Policies, Changes in Accounting Estimates and Errors*.

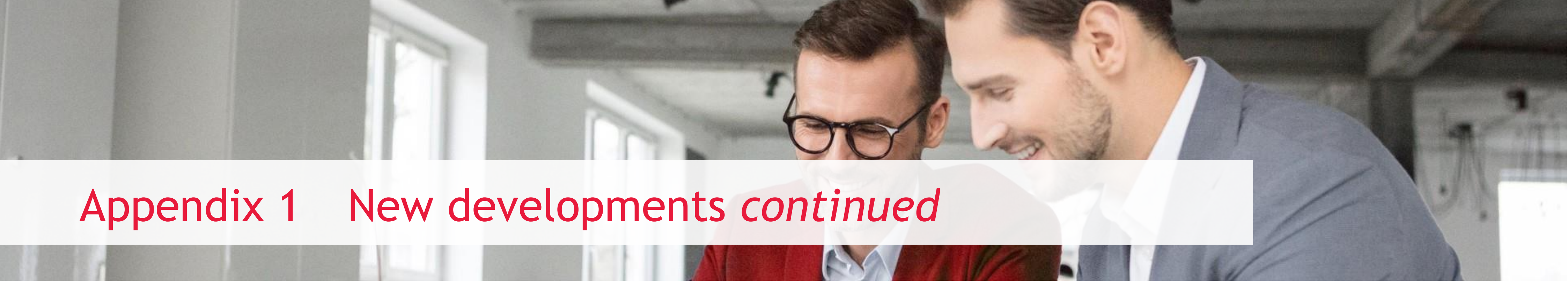
'Boilerplate' accounting policies should be removed from financial statements, including those that merely duplicate or summarise the accounting requirements of IFRS® Accounting Standards. Superfluous accounting policies for transactions and balances that don't exist should also be removed. This is likely to result in the majority of accounting policies being removed for 30 June 2024, with only those meeting the criteria for 'material' being retained. Streamlining accounting policies will result in efficiencies in the audit process. Refer to this article for further guidance.

Accounting estimates

An accounting estimate is a monetary amount in financial statements that is subject to estimation uncertainty, such as estimating expected credit losses for receivables, or estimating the fair value of an item recognised in the financial statements at fair value. Accounting estimates are developed using measurement techniques and inputs. Measurement techniques comprise estimation techniques (such as used to determine expected credit losses or value in use) and valuation techniques (such as the income approach to determine fair value). The amendments clarify that a change in an estimate occurs when there is either a change in a measurement technique or a change in an input.

There will be no impact on the financial statements when these amendments are first adopted for 30 June 2024 because they apply prospectively to changes in accounting estimates that occur on or after the beginning of the first annual reporting period to which these amendments apply, i.e. annual periods beginning on or after 1 July 2023.

For further guidance, refer to the 'Considerations for Management when determining accounting estimates and related disclosures' Briefing issued by IAASB. This Briefing provides an overview of matters for management to consider in preparing for and responding to the significant revisions in, and the auditor's requests pertaining to ASA 540 Revised *Auditing Accounting Estimates and Related Disclosures*.



Appendix 1 New developments *continued*

New developments in financial reporting

Amendments to AASB 101 for classifying liabilities as current or non-current

Effective for annual reporting periods beginning on or after 1 January 2024, there are three main changes to the classification requirements within AASB 101 *Presentation of Financial Statements*:

- The right to defer settlement must exist at the end of the reporting period. If the right to defer settlement is dependent upon the entity complying with specified conditions (covenants), the right to defer only exists at reporting date if the entity complies with those conditions at reporting date (paragraph 72B)
- Classification is based on the right to defer settlement, and not intention (paragraph 73), and
- If a liability could be settled by an entity transferring its own equity instruments prior to maturity (e.g. a convertible bond), classification is determined without considering the possibility of earlier settlement by conversion to equity, but only if the conversion feature is classified as equity under AASB 132 *Financial Instruments: Presentation* (paragraph 76B).

Classifying loans can be complicated where there has been a breach of a loan covenant, and can depend on whether and when the lender has provided a waiver or a period of grace. Our publication includes a flowchart and detailed examples to assist in this analysis.

Where a liability could be settled by an entity transferring its own equity instruments, such as for a convertible bond or note, this publication provides examples to assist with appropriate classification.

As these amendments apply for the first time to the 30 June 2025 balance sheet (and 30 June 2024 comparative balance sheet and 1 July 2023 opening balance sheet), at 30 June 2024, companies are in a position to assess the impacts regarding these changes. Entities must quantify the effect of any reclassification on current and non-current liabilities as part of disclosures about the effect of new standards issued that are not effective as at 30 June 2024.

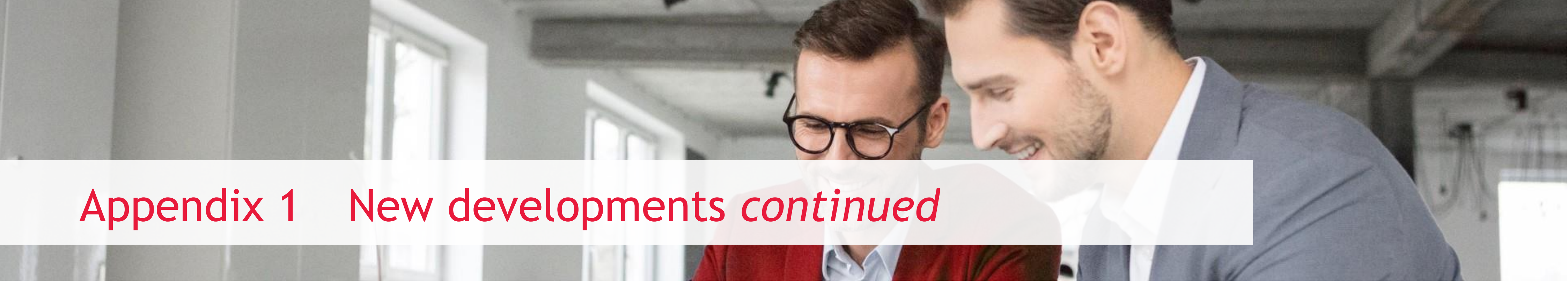
AASB 2022-5 *Amendments to Australian Accounting Standards - Lease Liability in a Sale and Leaseback*

The accounting approach taken by entities entering into sale and leaseback transactions may potentially change significantly as a result of these amendments, which are effective for annual reporting periods beginning on or after 1 January 2024.

The amendments clarify that where a sale and leaseback transaction qualifies to be recognised as a sales transaction under IFRS 15 *Revenue from Contracts with Customers*, the seller-lessee must subsequently measure its lease liability from the sale and leaseback transaction in such a way that it recognises no gain or loss related to the right of use it retains.

In practice, this means that:

- The lease liability initially recognised by a seller-lessee for a sale and leaseback transaction includes variable lease payments that are not dependent on an index or rate if they can be reasonably estimated. The difference between the actual variable lease payments made, and estimated variable lease payments recognised as part of the initial lease liability will be recognised in profit or loss in the period in which they are incurred.



Appendix 1 New developments *continued*

- If not part of a sale and leaseback transaction, lease liabilities do not include such variable payments, which are instead expensed in profit or loss in the period in which the event or condition that triggers those payments occurs.

This bulletin contains further information.

IFRS 18 *Presentation and Disclosure in Financial Statements*

On 9 April 2024, the International Accounting Standards Board issued IFRS 18 *Presentation and Disclosure in Financial Statements*, a new financial statements presentation standard to replace IAS 1 *Presentation of Financial Statements*. You can read more about this in our recent publication.

The changes require income and expenses to be classified into five categories – investing, financing, income taxes, discontinued operations and operating (which is the residual category). Classification follows an entity's 'main business activities' so may differ from one entity to another. The Statement of Profit or Loss also includes two mandatory subtotals:

- Operating profit or loss – this is a sub-total of all income and all expenses classified as operating
- Profit or loss before financing and income taxes – this is the sub-total of operating profit or loss, and all income and expenses classified as investing.

There are also changes to the Statement of Cash Flows, including how interest and dividend cash inflows and interest cash outflows are classified.

Lastly, the financial statements must include new disclosures in single note about 'management-defined performance measures' such as earnings before interest, taxes, depreciation and amortisation (EBITDA), 'adjusted profit', operating profit excluding recurring items, etc. The new disclosures apply to 'management-defined performance measures' if they are used in public communications outside the financial statements, to communicate to users of financial statements, management's view of an aspect of the entity's financial performance. They do not apply to certain specific sub-totals in the Statement of Profit or Loss such as gross profit. They also do not apply to social media posts and oral communications, and to non-IFRS information based on financial measures that are not performance-related (such as measures based only on the financial position of the entity). Also, they do not apply if an entity makes no public communications (as may be the case for private companies).

The changes are effective for annual periods beginning on or after 1 January 2027.

If you have any questions or require more information regarding these changes, please contact our IFRS & Corporate Reporting team.

Appendix 2 Climate reporting

Mandatory climate reporting Bill introduced into Parliament

On 27 March 2024, the Australian Government followed its promise to mandate climate reporting in Australia by introducing the *Treasury Laws Amendment (Financial Market Infrastructure and Other Measures) Bill* (Bill) into Parliament. The Bill mandates climate reporting for entities required to prepare and lodge financial reports with the Australian Securities and Investments Commission (ASIC) under Chapter 2M of the *Corporations Act 2001* if they meet certain criteria (refer to table below).

Climate-related financial disclosures will be included in a separate sustainability report, as part of the annual financial report. The disclosures required will be set by the Australian Accounting Standards Board. Entities will also be required to obtain an assurance report over the sustainability report from their financial statement auditors. The AUASB will make standards to provide for the audit or review of this information, and also specify how the level of assurance will phase-in over time.

Limited immunity

The Bill also contains limited immunity provisions for directors for the first three years covering statements about Scope 3 emissions, scenario analysis and statements about the entity's transition plans. Further immunity is provided for certain 'protected statements' made during the 12 months from the start date of the legislation for forward-looking climate statements.

Timing

The start date outlined in the Bill may vary depending on when the Bill passes through both Houses of Parliament. While the Government announced that the new climate reporting requirements will commence on 1 January 2025 rather than 1 July 2024, the Bill anticipates that the start date could be later. For example, if the necessary amendments proposed in the Bill:

a. Commence on or before 2 December 2024; the start date will be 1 January 2025

b. Commence between 3 December 2024 and 1 June 2025; the start date will be 1 July 2025

c. Commence on or after 2 June 2025; the start date will be the first 1 January or 1 July to occur 29 days or more after the day the amendments commence.

If the amendments don't pass by June 2025, mandating climate reporting will fall to the next government, as a Federal election is due no later than May 2025.

Appendix 2 Climate reporting *continued*

Criteria for reporting

The following table outlines the criteria and size thresholds for climate reporting, as well as the first mandatory reporting period end, assuming the entity has a 30 June reporting date and the start date for final legislation is 1 January 2025 or 1 July 2025:

	Large entities and their controlled entities meet at least two of three criteria			**National Greenhouse Energy Reporting (NGER) reporters**	**Asset owners**	**Start date - 1 January 2025 or 1 July 2025**
	Consolidated revenue	***End of financial year consolidated gross assets***	***End of financial year employees***			
Group 1	$500 million or more	$1 billion or more	500 or more	Above NGER publication threshold	N/A	30 June 2026
Group 2	$200 million or more	$500 million or more	250 or more	All other NGER reporters	$5 billion assets under management or more	30 June 2027
Group 3	$50 million or more	$25 million or more	100 or more	N/A	N/A	30 June 2028

There will be a materiality exemption for Group 3 entities. They will not have to make climate-related financial disclosures if they do not have any material climate-related risks and opportunities for the financial period.

More information

For the most up-to-date information regarding climate reporting, refer to the ‘Australian reporting’ Articles on BDO’s website.

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