



Hon John Carey BA(Hons) MLA
Minister for Housing, Lands, Homelessness & Local Government
7th Floor
Dumas House
2 Havelock Street
WEST PERTH WA 6005

Dear Minister

RE: 2020/21 ANNUAL FINANCIAL REPORT – SIGNIFICANT MATTER REPORTED BY AUDITOR

Please find attached the Shire of Gnowangerup 2020/21 Annual Financial Report, including the Independent Auditor's Report provided by the Auditor General. A copy of this document has also been provided to the Department of Local Government, Sport and Cultural Industries via the SmarHub lodgement process.

Pursuant to section 7.12A(4) of the Local Government Act 1995, I wish to report a matter identified as significant by the auditor in the audit report, and provide a response to that matter.

The Auditor General reported:

In accordance with the Local Government (Audit) Regulations 1996 I report that:

“(i) In my opinion, the following material matter indicates a significant adverse trend in the financial position of the Shire: a) The Operating Surplus Ratio is below the Department of Local Government, Sport and Cultural Industries standard for the past 3 years. The financial ratios are reported at Note 31 of the annual financial report”.

The Department of Local Government, Sport and Cultural Industries Operational Guideline No 18 outlines that:

‘A key indicator of a local government’s financial performance is measured by the “Operating Surplus Ratio”. If a local government consistently achieves a positive operating surplus ratio and has soundly based long term financial plans showing that it can continue to do so in future, having regard to asset management and the community’s service level needs, then it is considered financially sustainable.’

The ratio is subject to a number of one off influences such as prepaid financial assistance grants and abnormal operating expenditure. The biggest influence that a large number of local governments have experienced since 2013 is the revaluation of assets and the flow-on

effects this has had to depreciation, which is included as part of operating expenses. The increase in depreciation has affected the Shire of Gnowangerup significantly due to its relatively small budget, and therefore had an impact upon the operating surplus ratio. Depreciation has increased from \$1.2M in 2012/13 to \$2.3M in 2020/21 as a result of fair value asset revaluations.

The exclusion of Financial Assistance Grants (general purpose and local road grants) from the calculation also unfairly distorts the ratio calculation. Local governments use this funding to provide services and facilities to its community, mostly in the form of funding operational expenses. However, all grant funding is excluded to establish the local government's ability to cover its operational costs from its own sources of revenue.

It is worth noting that the Shire's current Long Term Financial Plan projects that, while depreciation expenses will continue to increase, the operating deficit will reduce over the next ten years.

The Shire of Gnowangerup, like many other local governments, believes that the operating surplus ratio does not truly reflect its financial position and the Department should consider whether it should remain as a measure of financial sustainability.

Do not hesitate to contact the undersigned should you have any queries relating to this matter.

Yours faithfully



Bob Jarvis
Chief Executive Officer

12 January 2022