



CORRUPTION AND CRIME COMMISSION

REPORT ON A MATTER OF GOVERNANCE AT THE SHIRE OF DOWERIN

10 OCTOBER 2016

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CORRUPTION AND CRIME COMMISSION

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Dear Mr Pratt
Dear Ms Robinson

As neither House of Parliament is presently sitting, in accordance with the *Corruption, Crime and Misconduct Act 2003* (CCM Act) s 93, the Commission hereby transmits to you a copy of its *Report on a Matter of Governance at the Shire of Dowerin*.

The Commission notes that under the CCM Act s 93 a copy of a report transmitted to a Clerk of a House is to be regarded as having been laid before that House.

Yours sincerely

A handwritten signature in blue ink that reads "John McKechnie".

John McKechnie, QC
COMMISSIONER

10 October 2016

TABLE OF CONTENTS

OVERVIEW	1
CHAPTER ONE	5
Council Responsibilities under the <i>Local Government Act 1995</i>	5
Regulation 9: A Source of Confusion: Nose in, Fingers out	6
The knowledge and understanding of councillors	8
The President	8
The relationship between Council and the CEO: The President's view	8
CEO performance review.....	9
Financial oversight by Council	10
The Deputy President	12
The relationship between the Council and the CEO: The Deputy President's view	13
CHAPTER TWO	15
Training for Councillors	15
Training and better practice reviews	15
President and Deputy President's opinion of training.....	16
Knowledge may deter councillors	17
CHAPTER THREE.....	19
Lack of Financial Controls at Dowerin	19
CHAPTER FOUR	23
The Role of the Audit and its Limitations	23
The Auditor: Byfields.....	24
Lack of an audit committee	25
Bank reconciliation.....	26
Fraud risk.....	27
Internal controls: strong or weak?	28
The audit process: Ms Leanne Oliver and Mr Paulo Cue.....	28
Audit and credit cards	32
The audit process: Mr Paulo Cue	34
The audit process and scope: The President's knowledge	35
The annual compliance report	36
The audit process: The Deputy President's knowledge	37

CHAPTER FIVE	39
The Forensic Audit	39
CHAPTER SIX	43
The role of the Department of Local Government and Communities.....	43
Intervention based on Risk Assessment.....	44
2014 Risk Profile Result.....	44
Intervention at Dowerin when Mr Alcock was CEO	44
Deeply embedded weaknesses	45
Independent review of the compliance audit reports.....	46
CHAPTER SEVEN	49
The Cost to Dowerin and the Steps to Recovery.....	49
The first steps	49
Appointment of Ms Selvey	49
Financial costs	49
Intangible costs	51
The way forward	51

OVERVIEW

- [1] On the morning of 6 October 2015, Ms Sonia King, Finance Manager for the Shire of Dowerin, received a disturbing telephone call from the fraud prevention unit of the National Australia Bank (NAB). The caller advised that a Shire credit card had been used to pay into gambling accounts. Ms King and the Deputy President, Mr Ralph, immediately notified the Commission that serious misconduct was suspected.
- [2] Dowerin is a small farming community of approximately 700 people in the eastern wheatbelt region of Western Australia. The annual budget for Dowerin records projected income for the 2015-16 financial year to be approximately \$2.9 million. Despite this, Dowerin is a mendicant Council. Its greatest source of funding is from grants.
- [3] In June 2008, the Shire of Dowerin employed Mr Dacre Alcock as CEO. He was CEO for seven years, and by all accounts, was an integral part of the Dowerin community. Great trust was placed in him to perform his duties.
- [4] For four years, from 2011 until he was arrested in October 2015, he stole almost \$600,000 over 665 occasions. His actions went unnoticed until the phone call.
- [5] On 28 October 2015, Commission officers travelled to Dowerin and arrested Mr Alcock for stealing as a servant.
- [6] The embezzlement occurred over four years. Successive audits had failed to discover anything wrong with the accounts.
- [7] After Mr Alcock's arrest, the Shire appointed Mr Gary Martin as Acting CEO pending the permanent appointment in March 2016 of Ms Andrea Selvey. One of Mr Martin's early tasks was to engage Mr Ron Back to conduct a forensic audit. Mr Back found many basic policies and procedures were lacking. Mr Alcock was able to steal with impunity. No one held him to account.
- [8] The Commission has previously reported on CEO malfeasance in local authorities.
- [9] In 2012, as a result of a Commission investigation, the former CEO of the Shire of Murchison was imprisoned for corruption and stealing. At the same time, Mr Alcock was stealing funds at Dowerin. This obviously did nothing to deter his conduct. Nor were there any changes made at Dowerin to strengthen controls over finances in light of the illustrated risks identified when there is inadequate governance of a CEO by a complacent council.
- [10] The Commission decided to investigate the circumstances in which Mr Alcock was able to steal so much money over such a long period without detection. As part of its investigation, the Commission travelled to Dowerin for two days in July 2016 and took evidence in a series of public examinations. It did this so that the ratepayers and residents could hear

for themselves what went wrong and, just as importantly, what has now been done by Council and Ms Selvey to fix the problem.

- [11] The evidence showed breathtaking levels of ignorance as to the role and responsibility of councillors over the governance of a CEO. If there had been proper policies in place, if the Council had complied with the *Local Government Act 1995* (LGA) and appointed an audit committee, if the auditors had asked for or simply glanced at the credit card statements which Mr Alcock kept to himself, the probabilities are that the embezzlement would have been discovered much sooner and the losses mitigated.
- [12] On 30 September 2016, Mr Alcock pleaded guilty in the District Court to three counts of stealing as a servant and was sentenced to a total of four years and six months imprisonment. A parole eligibility order was made, as was a compensation order for \$516,219. In the circumstances it is pointless to form any opinion of serious misconduct.
- [13] Corruption by public officers is insidious and damaging in its consequences. CEOs in local government control public moneys to enable them to perform functions for the broader public good of the community they serve. There is a significant element of trust that accompanies such responsibilities. Ratepayers have a right to expect that such trust will not be abused. Government bodies, including local authorities must be vigilant for signs of corrupt behaviour, and have policies and procedures in place to minimise such risks. Dowerin was not vigilant and had few policies. All the blame cannot be laid at the auditors' feet.
- [14] The Commission has formed no opinions of serious misconduct about officers and councillors of the Shire of Dowerin. It lacks jurisdiction to form any opinion of minor misconduct. Indeed, following amendments to the *Corruption, Crime and Misconduct Act 2003* in 2015, neither the Commission nor the Public Sector Commission has jurisdiction to investigate minor misconduct or form opinions in respect of any elected official including local government councillors and Members of Parliament.
- [15] The Commission has nevertheless decided to report to Parliament on the result of its investigation. Copies of the draft report were provided to parties who might be adversely affected¹. Where the Commission accepts the response given, the report has been amended accordingly. Extensive submissions were received from lawyers acting on behalf of the President and Deputy President of Dowerin arguing in essence:
- The LGA does not set out a duty on council to be a check and balance on the CEO or on financial reports presented to it; and
 - Council has no responsibility for close financial oversight.

¹ *Corruption, Crime and Misconduct Act 2003*, s 86.

- [16] These are matters of legal opinion with which the Commission fundamentally disagrees. The LGA provides a governance framework that mandates council's responsibility to govern the local government's affairs.
- [17] There are 137 local authorities in Western Australia. What happened in Dowerin over four years is a cautionary tale and a warning to other local authorities. Although painful, Dowerin has learned the lessons. Can the same be said for every local government?

CHAPTER ONE

Council Responsibilities under the *Local Government Act 1995*

- [18] Elected councillors have ultimate responsibility for the local government. Council is responsible for the appointment of and subsequent governance of the CEO. Council is also responsible for financial affairs.²
- [19] The general function of a local government is to provide for the good government of persons in its district, s 3.1. The role of council is set out in the LGA s 2.7. It is to govern the local government's affairs and is responsible for the performance of the local government's functions. The role of councillors is set out in the LGA s 2.10.
- [20] Submissions on behalf of Mr Metcalf and Mr Ralph draw attention to s 2.7(2):
- Without limiting subsection (1), the council is to -*
- (a) oversee the allocation of the local government's finances and resources; and*
- (b) determine the local government's policies.*
- [21] The submission on their behalf is that an examination of the LGA and regulations reveals that the legislation does not contemplate the council acting as a check and balance on the adequacy and accuracy of the financial reports presented to it by the CEO. Nor, it is said, does the legislation contemplate the council being a check and balance on the financial management of the local government generally including the appropriate governance framework and policies that the local government is to have in place. It is submitted that as locally elected representatives, the members of the council are (as a general rule) not qualified to perform that function.
- [22] The Commission has considered the submission and completely rejects it. It is at odds with council's function to govern the local government's affairs. Council is to ensure that there is an appropriate structure for administering the local government.³ Council is to employ a suitably qualified CEO⁴ and annually review the CEO's performance.⁵ The CEO must review the financial management systems and procedures regularly (not less than once every four years) and report the results of the review.⁶
- [23] The functions of a CEO are set out in the LGA s 5.41.

² *Local Government Act 1995*, s 2.7, s 6.2.

³ *Local Government Act 1995*, s 5.2.

⁴ *Local Government Act 1995*, s 5.36.

⁵ *Local Government Act 1995*, s 5.38.

⁶ *Local Government (Financial Management) Regulations 1996*, s 5(2).

[24] There is a limitation on council delegating some matters to a CEO including appointing an audit committee.⁷

[25] The CEO has duties in relation to financial records:

6.5. Accounts and records

The CEO has a duty —

- (a) *to ensure that there are kept, in accordance with regulations, proper accounts and records of the transactions and affairs of the local government; and*
- (b) *to keep the accounts and records up to date and ready for inspection at any time by persons authorised to do so under this Act or another written law.*⁸

[26] The Department of Local Government and Communities (DLGC) has published guidelines for the assistance of councils: *Local Government Operational Guidelines Number 9 - Revised September 2013; Audit in Local Government, The appointment, function and responsibilities of Audit Committees*; and *Local Government Operational Guidelines Number 11 - September 2006* which sets out the use of corporate credit cards. The guidelines could be very helpful but they are useless if no one bothers to read them.

[27] Councillors are volunteers. They often fit the description applied to Mr Metcalf and Mr Ralph as persons of standing within the community who may be successful at business, but may have little knowledge needed to provide proper oversight of the financial affairs of the local government. So it proved in Dowerin. Training courses are offered by Western Australian Local Government Association (WALGA) and the DLGC but are not mandatory.

Regulation 9: A Source of Confusion: Nose in, Fingers out

[28] The *Local Government (Rules of Conduct) Regulations 2007* (Local Government (Rules of Conduct) Regulations) prescribes limitations on councillors interfering with the operations of council, something described by Deputy President Ralph:

*As a councillor I feel since I've been on council, and my other councillors, we have been nose in and fingers out. There's been robust discussion the whole way through and I don't see there's been any downfall from the current or previous councils in not asking the right questions to try and cover this.*⁹

[29] The Local Government (Rules of Conduct) Regulations provides:

⁷ *Local Government Act 1995*, s 7.1A.

⁸ *Local Government Act 1995*, s 6.5.

⁹ Transcript of Public Examinations at Dowerin on Thursday, 28 July 2016, p59.

9. Prohibition against involvement in administration

- (1) *A person who is a council member must not undertake a task that contributes to the administration of the local government that unless authorised by the council or by the CEO to undertake that task.*
- (2) *Subregulation (1) does not apply to anything that a council member does as part of the deliberations at a council or committee meeting.*

10. Relations with local government employees

- (1) *A person who is a council member must not -*
 - (a) *direct or attempt to direct a person who is a local government employee to do or not to do anything in the person's capacity as a local government employee; or*
 - (b) *attempt to influence, by means of threat or the promise of a reward, the conduct of a person who is a local government employee in the person's capacity as a local government employee.*
- (2) *Subregulation (1) does not apply to anything that a council member does as part of the deliberations at a council or committee meeting.*

[30] This bifurcation of responsibility may cause confusion as to the extent to which a council can inquire into the operations of local government.

[31] Mr Martin was appointed acting CEO following Mr Alcock's resignation. He is very experienced and has acted as CEO in similar situations. He was asked about the difference between operational matters and councillors understanding:

This issue of operational, the separation of roles in the Act, is quite often used as a shield by CEOs. "Butt out; that's now operational," so some elected members, particularly those who haven't been to training or haven't any widespread knowledge of local government, they may have concerns, and don't know how to go about dealing with it.

... In my view where the issues of concern relate to the governance of the Shire, elected members have a legitimate right to be involved and ask questions. They've got the power but they don't know because they rely upon the CEO to tell them what they don't know or what they need to know.¹⁰

[32] The Commission is of the same opinion.

¹⁰ Transcript of Public Examinations at Dowerin on Friday, 29 July 2016, p70.

The knowledge and understanding of councillors

- [33] The Commission received evidence from the President, Mr Dale Metcalf, and Deputy President, Mr Graham Ralph in public examination. The Commission accepts that they are each persons of standing within the community who have given years of service to Dowerin. They of course are not responsible for Mr Alcock's embezzlement. But their knowledge and understanding is important in shedding light as to why the embezzlement was not discovered sooner.
- [34] Their general lack of knowledge of the LGA is disturbing. Their evidence also illustrates the tension many councillors must feel between their statutory responsibilities and those of the CEO.

The President

- [35] Mr Dale Metcalf was elected a member of Council in July 2003 and has been President since November 2007. There are eight councillors in Dowerin.

The relationship between Council and the CEO: The President's view

- [36] Mr Metcalf clarified his understanding of the LGA s 2.7 (the role of council):

*In broad terms, the clarification being: oversee the allocation of local government finances and resources as a result of reports brought to council by the CEO for us to debate and then accept or reject. The CEO has the position that he has to supply us with the necessary equipment to carry out those functions.*¹¹

...

*The budget is formed by the staff; by the CEO, the finance officers, by the staff. The works manager has input. They put together the budget. Then they bring it to council for review and we check the allocations. We check what extra funding that is required for any extra asset purchased or whatever, so the actual body of the budget is performed by the staff. That's operational.*¹²

- [37] The CEO attended Council meetings once a month along with the finance manager and the works manager.
- [38] Mr Metcalf agreed that every four years there should be a review of the financial systems. Mr Alcock provided a review to Council in December 2014 which Council relied on:

¹¹ Transcript of Public Examinations at Dowerin on Thursday, 28 July 2016, p12.

¹² Transcript of Public Examinations at Dowerin on Thursday, 28 July 2016, p13.

*In summary then, would you agree that it's fair to say that the CEO's role was to manage the financials and report to council?---The CEO has complete control over the operations of the Shire.*¹³

[39] Mr Metcalf made the point "We have the oversight on what is reported to us."¹⁴

[40] Mr Alcock was appointed CEO in June 2008. Mr Metcalf gave his opinion of Mr Alcock:

*When he first came, it was the typical new broom sweeps clean and it was quite remarkable how the council lifted and the activities seemed to improve and that was probably the case for four years and then there was – and I didn't personally notice because I'd see him all the time. Some of the other councillors on once a month contact were saying "The performance is going down" and it wasn't until after I'd been on this overseas trip and came back I realised that he was changing.*¹⁵

[41] Although it was reported that he was taking longer to do tasks or ignoring them, Mr Metcalf didn't have any concerns. His view was that he was competently performing the job. A lot of the matters were minor.

CEO performance review

[42] The performance of the CEO must be reviewed each year.¹⁶ Council did so. Mr Metcalf said the same form was always used. Nothing outside the form is used. There are no external consultants or interviews with staff. The form was provided to each councillor at usually the June meeting because the performance review was done in July: "... my request was that all councillors fill this in independently and then come to the July meeting with the completed assessment ..."¹⁷ Seven filled it in, one generally refused. It was filled in by the councillor at the July meeting.

[43] Mr Metcalf said there was concern about some areas where Council may not have direct knowledge of Mr Alcock's performance:

*That was always a concern, because when we did this it was quite robust discussion and that was a major concern because we could not honestly assess his communication skills with the staff, at what level or how involved he was with both inside and outside staff and we had to just make the best assessments on an individual basis.*¹⁸

[44] This passage reflects the dilemma both Mr Metcalf and Mr Ralph had in balancing their governance of the CEO against what they saw as the

¹³ Transcript of Public Examinations at Dowerin on Thursday, 28 July 2016, pp15-16.

¹⁴ Transcript of Public Examinations at Dowerin on Thursday, 28 July 2016, p16.

¹⁵ Transcript of Public Examinations at Dowerin on Thursday, 28 July 2016, p16.

¹⁶ *Local Government Act 1995* s 5.38.

¹⁷ Transcript of Public Examinations at Dowerin on Thursday, 28 July 2016, p18.

¹⁸ Transcript of Public Examinations at Dowerin on Thursday, 28 July 2016, p18.

restriction on councillors interfering with operational matters. Ms King had a similar dilemma.

- [45] Their view, according to Mr Bradley Jolly, Executive Director, Sector Regulation and Support at DLGC, may be widespread among councils.
- [46] Mr Metcalf tallied the forms and concluded there was no concern about Mr Alcock's ability to put correct financial information before Council.
- [47] Mr Martin was asked about performance reviews:

Certainly the performance reviews I think should involve an element of external assistance. Quite often the KPIs the CEOs are being assessed on are performance as far as achieving milestones or projects. There's very little emphasis in many Shires on actual performance of their core duties, and by core duties I mean their duties under section 541, the day-to-day operation, information as to council, etcetera. A lot of the CEO performance reviews are based on the big picture items and there's no scrutiny about actually doing the job, their statutory role.¹⁹

Financial oversight by Council

- [48] When Mr Alcock was appointed, Council had a combined finance and audit committee. It didn't actually discuss finance, only accounts and the payment of them. At the time of Mr Alcock's appointment, Mr Rex Adams was deputy CEO and finance manager. He retired, and for a time Mr Alcock carried out both tasks from September 2011, but in May 2012 advertised for a finance manager. Ms King was an administration officer. She was ultimately the successful applicant. Mr Metcalf was aware that Ms King had very limited financial management experience:

The CEO had a lot of faith in her ability and I have to say that his faith was correct, because her ability to pick up finances was extraordinary.

That was based on your interactions with her, that you found her ability to be very good?---Very good.²⁰

- [49] When Ms King went on maternity leave nobody took over her responsibilities. The perceived inability to have oversight over administrative matters continued. Mr Metcalf said:

The staff in general probably took up some of the slack: that's operational.

...

Well, the functions of the Shire is the management of the affairs of the community and the finances. That's all operational and that's not for council or councillors.

...

¹⁹ Transcript of Public Examinations at Dowerin on Friday, 29 July 2016, p69.

²⁰ Transcript of Public Examinations at Dowerin on Thursday, 28 July 2016, p20.

*We cannot be involved with the managerial. So as much as you might like to, you cannot be involved in the managerial side or the operational side of the outfit which is the Shire, the Shire part.*²¹

[50] Mr Metcalf was not aware that there were *Local Government (Financial Management) Regulations 1996*. How then could he know if the Council was compliant?

[51] The municipal fund is the Shire's working fund. Council delegated authority for the municipal fund to the CEO. The accounts would come before Council; the hard copy documents were available for Council with the invoices attached. Council would receive a monthly statement of financial activity:

... how did you develop the ability to read the financial statements and know what you were looking for?---Intuition.

*So no formal training in relation to them?---I've got limited mentality and no academic skills whatsoever.*²²

[52] Mr Metcalf said he ran his own business for 50 years and regarded himself as competent because he didn't go broke. He never felt he was incapable of performing well as a councillor. As to the division of responsibility: "We are not to interfere with the operational management role of the CEO and it's a grey area."²³

[53] Mr Metcalf was aware that Dowerin was required to have an audit committee. There was in fact a finance and audit committee. Mr Alcock would run the meetings if he was present. Ms King was on the committee. The LGA Part 7 specifies the requirements of audit. The CEO is not to be a member.²⁴

[54] Mr Metcalf was unaware that Dowerin was not compliant in relation to the audit committee. He knew there was a role for audit and finance, but didn't realise they had to be separate. Council was never told that an audit committee had to be set up separately. It never came up in the annual compliance audit.

[55] Mr Metcalf said that there was a stage where he wasn't comfortable with the finances, didn't know quite why, and sort of floundered. When asked whether he ran any financial statements for his farm he said: "Totally different."²⁵

[56] Mr Metcalf was shown bank statements that showed the electronic transfer number, although how that operated he had no idea. He looked at the numbers sometimes and admitted that he didn't know there was a missing

²¹ Transcript of Public Examinations at Dowerin on Thursday, 28 July 2016, p21.

²² Transcript of Public Examinations at Dowerin on Thursday, 28 July 2016, p25.

²³ Transcript of Public Examinations at Dowerin on Thursday, 28 July 2016, p38.

²⁴ *Local Government Act 1995* s 7.1A(3).

²⁵ Transcript of Public Examinations at Dowerin on Thursday, 28 July 2016, p25.

number on a couple of occasions. He just presumed it was a mistake: "Did you ask questions about that?---No. I'm not cynical enough."²⁶

- [57] Mr Metcalf knew that Mr Alcock and others at the Shire had corporate credit cards: "Did you understand that all of that expenditure would appear on the monthly statements that came before council?---Never gave it a thought."²⁷ Mr Metcalf did not know Dowerin lacked a credit card policy.

Did you know that Mr Alcock had complete control over the financial management system?---That was a concern.

...

It was a concern that the CEO has excessive power in everything.

...

Under the Act all CEOs have got excessive power.

...

The concern is that it's the CEO's role to bring a report to council with a recommendation, and that report could be on governance or finance or whatever, but it's the CEO's role to be the architect of a report, bring it to council for debate and then for council to ratify it, endorse it. It's not council's role to go and create the policy. So if the CEO doesn't come to council, doesn't bring the council the policies required for good governance, is it the role of council to follow up or to know or to have any idea of what is supposed to be done.²⁸

- [58] Mr Metcalf acknowledged his ignorance:

I really have to state that I was quite ignorant of the scope of procedures and government matters that were required; operate on common sense and logic. It doesn't always work.²⁹

The Deputy President

- [59] Mr Graham Benjamin Ralph has been Deputy President of the Shire of Dowerin since October 2011, having been elected to Council in August 2006. He worked with Mr Alcock for seven years. He was involved in reporting Mr Alcock's conduct to the Commission.

- [60] In all that time, Mr Ralph never acquainted himself with his basic responsibilities as set out in the LGA:

Can I just say one thing on this act. I've only seen the act twice. Once was when we met at Mr Metcalf's last Friday and one time in Shire. That's the only time as a councillor I've ever - - -

²⁶ Transcript of Public Examinations at Dowerin on Thursday, 28 July 2016, p26.

²⁷ Transcript of Public Examinations at Dowerin on Thursday, 28 July 2016, p27.

²⁸ Transcript of Public Examinations at Dowerin on Thursday, 28 July 2016, pp28-29.

²⁹ Transcript of Public Examinations at Dowerin on Thursday, 28 July 2016, p30.

...

At Mr Metcalf's house last Friday and one time, which I couldn't tell you, in Shire, which Mr Metcalf brought the act to council to show councillors what was involved. When I seen the size of the act, which is I don't know, a hundred-plus mil of small pages, I was surprised. I've never been told I had to read the act as a councillor. I've never been instructed that I should have a copy of the act. I've never read the act.

...

My understanding of the act was that that's why we have the CEO to inform us of a lot of that stuff and as I said, I've never been directed that it was my duty to follow the act as a councillor; like to read the act so when the CEO presents something, to go to the act to work out if it's done correctly or not.³⁰

The relationship between the Council and the CEO: The Deputy President's view

- [61] In his view: "The role of the Council is just to scrutinise the reports that are given from the CEO at Council meetings."³¹
- [62] As to the separation of power between Council and the CEO, Mr Ralph said: "Operations is all to do with everything that is done on a daily thing ..."³² So primarily Mr Alcock was in a reporting role: "... he'd engage in the day-to-day operations and then report on those to Council."³³
- [63] Mr Ralph knew there was a finance and audit committee. As to their work: "I never stuck my nose into that. It doesn't – finance and audit doesn't interest me. I never stuck my nose into it. That was theirs. I was focused on other stuff."³⁴
- [64] Mr Ralph was not aware that the LGA prohibits a CEO from sitting on an audit committee:

... relied entirely on the CEO to tell you what you needed to be doing ... ?--- Correct. That's why we employ him. As a councillor I don't feel it's the onus on us to do that sort of stuff. It's a worry as a councillor that if you go and start directing the CEO or finding out what to do, if I did know the act, where does that leave us from what's coming onto it now. It does leave me and other councillors in a fair bit of unknown with what's going on. There's a lot of onus coming back on the council. Yeah, now I'm reading the act and seen a bit of the act and hearing the act, a lot more than what a lot of council – I know it's a concern of council currently.

...

³⁰ Transcript of Public Examinations at Dowerin on Thursday, 28 July 2016, p47.

³¹ Transcript of Public Examinations at Dowerin on Thursday, 28 July 2016, p46.

³² Transcript of Public Examinations at Dowerin on Thursday, 28 July 2016, p48.

³³ Transcript of Public Examinations at Dowerin on Thursday, 28 July 2016, p48.

³⁴ Transcript of Public Examinations at Dowerin on Thursday, 28 July 2016, p48.

... I'd never been told or informed or read it anywhere else (councillors' responsibility).³⁵

[65] As to suggestions for the future, Mr Ralph said:

I think that ... senior management should be able to go to their Shire President with some concerns. I know CEOs aren't going to like that but I think that would have raised flags a long time ago and should have been uncovered and not been so untidy for the Shire of Dowerin.³⁶

[66] In view of the confusion expressed by councillors about their oversight role and the comments of Mr Martin and Mr Jolly, the Commission recommends that DLGC advise local governments the proper interpretation of regulation 9 and its interaction with a council's responsibility for governance.

³⁵ Transcript of Public Examinations at Dowerin on Thursday, 28 July 2016, p49.

³⁶ Transcript of Public Examinations at Dowerin on Thursday, 28 July 2016, p58.

CHAPTER TWO

Training for Councillors

- [67] The issue of training for councillors raises policy questions that are not the province of the Commission, but Parliament. A councillor is democratically elected, even allowing for local governments such as Dowerin where there may be a dearth of nominees. A councillor may be elected on a platform to advocate for particular issues.
- [68] Once elected however, a councillor is invested with responsibilities imposed by the LGA and regulations including responsibilities for good governance of the local government and the CEO. Council also has ultimate responsibilities for the finances.
- [69] It is difficult to see how these responsibilities can be fulfilled without some knowledge or training. At a minimum, reading the LGA and regulations does not seem an excessive burden to place on a person elected to a position of public trust.

Training and better practice reviews

- [70] When he gave evidence, Mr Jolly was the Acting Director General of DLGC. He gave evidence that as part of DLGC's capacity building function it provides targeted training in response to requests from local governments to address particular issues.³⁷ More broadly, DLGC has procured training for the local government sector through WALGA, funded by the Royalties for Regions Country Local Government Fund. Over four years \$1.52 million has been used to procure elected member training services outside the Perth metropolitan area. The funding for the training program is in its final year.
- [71] In relation to the uptake of the voluntary training program delivered in locations throughout country Western Australia, Mr Jolly stated that:
- Since 2014 the program has trained 326 councillors from 86 country local governments... and that's out of country 108 local governments.*³⁸

- [72] The training program has evolved to consist of two core units:

- 'understanding financial reports and budgets'; and
- 'sustainable asset management',

together with four out of six available elective modules.

- [73] The elective modules that are offered are:

- 'effective community leadership';

³⁷ Transcript of Public Examination on Friday, 2 September 2016, p3.

³⁸ Transcript of Public Examination on Friday, 2 September 2016, p7.

- 'CEO performance appraisals';
- 'understanding strategic policy';
- 'land use planning';
- 'better planning decisions'; and
- 'meeting procedures and debating'.³⁹

[74] The training is provided at a modest cost to the local government.⁴⁰

[75] DLGC is also funded through Royalties for Regions Country Local Government Fund until 30 June 2017 to undertake Better Practice Reviews. The purpose of that program is to help identify and promulgate good practice across the sector as well as identify opportunity for improvement. A Better Practice Review involves DLGC sending a team of officers to undertake a functional review of the local government and work through a range of functions that the local government performs. The local government's effectiveness or performance is measured against established criteria. That process results in the compilation of a report of findings that indicates where there are opportunities for improvement.⁴¹

[76] Between 2014 and 2015 during the second and third year of the DLGC training program, training was offered in the great eastern zone which includes Dowerin. None of the Dowerin councillors attended that training.⁴²

[77] Training is made available for interested councillors in Perth and the regions. It is not mandatory.

President and Deputy President's opinion of training

[78] Mr Metcalf said: "It's hard to believe that 35 or 40 hours of training for councillors is going to create a major change when a CEO has done four years of university or higher education and ongoing education."⁴³

[79] As to training and whether it would be of benefit, he said:

It's a fairly big Act, and when you're talking about additional training it's going to be skimpy.

...

We did a training session a fortnight ago for a day with WA Local Government Authority and the Department. The booklet that was given out at that training session is of tremendous benefit to a new councillor. I learnt a lot, although I've been 13 years on Council. That would make a huge

³⁹ Transcript of Public Examination on Friday, 2 September 2016, p8.

⁴⁰ Transcript of Public Examination on Friday, 2 September 2016, p9-10.

⁴¹ Transcript of Public Examination on Friday, 2 September 2016, p11.

⁴² Transcript of Public Examination on Friday, 2 September 2016, p9.

⁴³ Transcript of Public Examinations at Dowerin on Thursday, 28 July 2016, p30.

difference to the understanding of the role, and that was the point of the exercise. It was the role of a councillor, and that would highlight to councillors their responsibilities, that in conjunction with induction and some induction process. We then come to the point of do potential councillors nominating have to do it before they go on council or do you wait until they go on council, so they're actually running dry to start with.

...

When Mr Alcock was CEO were there any discussions about the need for training for councillors?---Often it was brought up but we always got a negative – generally got a negative.

...

What was the reason?---Not required. Councillors weren't really interested, and now that's changed. I would say the councillors are very aware that we need to be more skilled and aware.⁴⁴

Knowledge may deter councillors

- [80] Mr Ralph's views on training for councillors is illuminating: as to training: "... it's always been considered. ... is not compulsory"⁴⁵ Mr Ralph "... got on Council for strategies to make my community a better community. ... I'm not qualified in [accounting]. ... Mr Alcock was pretty negative on training. I never got a positive vibe from him on training."⁴⁶

- [81] Mr Ralph appeared to suggest that proper knowledge of the obligations of councillors could prove a deterrent to new councillors:

... because if you have a look at – if you do the training and have a look at the obligation underneath the act, I don't feel we will. It's not healthy as it is. In our last two elections we haven't actually had elections. We've only had just the right amount of people to nominate, so it's not as though there's 10 people nominating for one position.

...

... the problem is, as I say again, the more we get to know what we know now, I'm not too sure whether I would personally sit on council. I know other councillors are concerned since all this has gone on, and we are knowing parts of the act, why they have nominated, but personally myself, if I had known what I was getting myself into, no, I wouldn't get on council.⁴⁷

- [82] Mr Back commented:

These events highlight the need to ensure elected members are up to date with governance issues and the value of independent reviews of accounting processes. There was a lack of training provided to elected members which

⁴⁴ Transcript of Public Examinations at Dowerin on Thursday, 28 July 2016, pp33-34.

⁴⁵ Transcript of Public Examinations at Dowerin on Thursday, 28 July 2016, p50.

⁴⁶ Transcript of Public Examinations at Dowerin on Thursday, 28 July 2016, p50.

⁴⁷ Transcript of Public Examinations at Dowerin on Thursday, 28 July 2016, p51.

*created a knowledge gap and allowed the former CEO to control the events, information and conceal the misappropriation of Shire funds.*⁴⁸

- [83] If Mr Ralph's view is widespread, it reflects a significant issue for the State. Being a councillor enables a person to participate in decisions affecting their community but it comes with responsibility to understand the duties and requirements. The DLGC publishes extensive guidance for elected members. It funds WALGA through Royalties for Regions to undertake training courses in rural regions. Elected members represent the interests of electors, ratepayers, and residents of the district⁴⁹ but are also part of a council that governs the affairs of the local government and is responsible for its functions.⁵⁰
- [84] A primary duty of a council is governance. Councillors, for good reason, are prevented under regulation 9 from exercising direct control over administrative matters. That duty cannot be avoided by ignorance. It can be assisted by training.
- [85] There are policy issues for and against mandatory training for councillors. The policy issue is summarised by Ms Selvey:

*Democracy is about people being able to let someone represent them. How those people then become best skilled to represent the community is a subject for a great deal of debate and discussion and examination of how it could be delivered in a way that doesn't prevent or preclude people from participating in the democratic process.*⁵¹

- [86] The policy in favour of mandatory training by Mr Jolly:

*I think WALGA's argument, and I don't know that it's necessarily a view that the department agrees with, the department thinks that -- you know, our view is that there is scope, perhaps, for some level of mandated training. That's been the department's view fairly consistently throughout this debate for a lot of the reasons that we've discussed. I think the counterview is that by mandating training that you heighten the barriers to participation and so, as I understand it, you know, that's central to WALGA's participation -- sorry, to WALGA's views.*⁵²

⁴⁸ Shire of Dowerin Forensic Audit Report 2016, Vol 1, R J Back and Associates, 10 March 2016, p45.

⁴⁹ *Local Government Act 1995* s 2.10(a).

⁵⁰ *Local Government Act 1995* s 2.7(1).

⁵¹ Transcript of Public Examinations at Dowerin on Friday, 29 July 2016, p79.

⁵² Transcript of Public Examination on Friday, 2 September 2016, pp 59-60.

CHAPTER THREE

Lack of Financial Controls at Dowerin

- [87] There were few financial policies in place while Mr Alcock was CEO. Dowerin had no corporate credit card policy. Mr Alcock retained the credit card statements and did not provide them to the finance manager. The auditors never asked for them or inspected them. He made 567 payments to gambling companies using his Shire credit card.
- [88] Standard risk mitigation is to have checks and balances. A routine financial precaution is to require two people to authorise a payment. In times gone by, this was achieved by having two signatories on a cheque account. The modern equivalent is an electronic token with accompanying password. NAB supplied Dowerin with such tokens. One token was kept by Ms Howard in a box, with the password written inside the box, the user ID on the back of the token, and the box stored in an unlocked drawer. When Ms Howard retired, her token was not cancelled by Dowerin as it should have been. When Ms King went on leave, she emailed Mr Alcock the location of her token and where he could find stored passwords. So the supposed precaution was missing.
- [89] Ms King was employed at Dowerin in August 2010 as administration officer. In 2011 she was appointed Finance Manager although she had no formal qualifications. There is no evidence to suggest that she was other than diligent, and the present CEO, Ms Selvey, speaks well of her. However, she was vulnerable to influence from Mr Alcock, particularly when he told her certain financial tasks were beyond her competence, and therefore retained control over many aspects of the accounts, including credit card statements. It is a basic feature of good financial management that there should be separate checks and balances. One of these is separation of CEO and Chief Financial Officer responsibilities.
- [90] When Mr Adams, the Deputy CEO, left there was no immediate replacement: "I think the general idea was to not focus on the deputy CEO but more a finance manager or administration manager/finance."⁵³
- [91] After some months, the position of finance manager was advertised and Ms King applied for the position. She had no relevant qualifications. She had experience; she had undertaken some financial tasks assisting with payroll and creditors and debtors as needed.
- [92] Her salary and allowances were adjusted by Mr Alcock to recognise her lack of qualifications. The cash component of the role was up to \$90,000. She started on a cash salary of approximately \$60,000:

Communicated verbally to me from Dacre ... was that due to my lack of qualifications at that time and experience, I would be paid according to the duties that I would be able to fulfil; following that, that training would be

⁵³ Transcript of Public Examinations at Dowerin on Thursday, 28 July 2016, p63.

*provided and my salary would go up accordingly as I was better fit to take on more financial duties.*⁵⁴

[93] Ms King's appointment highlights a risk for local government. Ms King was living in Dowerin when she was first employed. It may be difficult for rural authorities to attract qualified staff. Employing an unqualified person may be necessary, but it carries the risk that a finance manager is beholden to a CEO.

[94] The separation between the two roles, part of a wider system of risk mitigation, is diminished.

[95] Ms King was excited over taking on extra responsibility and meeting the expectations of the community. She reported directly to the CEO. At first, she was lacking in confidence in financial reporting leading up to budgets and annual reports. She had an understanding of monthly reports but wanted to gain more knowledge. She had trained on enabling SynergySoft to speak to Excel so she could prepare monthly statements. Ms King took maternity leave between November 2014 and August 2015. Mr Alcock performed her duties while she was away.

[96] When she returned:

... everything was a bit of a mess. Bank reconciliations weren't being done. Monthly reporting I think was happening but the accounts were just – as far as I could see were just being balanced at the end of the month by making journals to make it look like it was balancing.

...

*I was questioning what I was seeing. So I didn't form that view completely at that time but I was seeing that things weren't really making sense. So I had questioned him and he didn't want me to be involved in the finances. He said I needed to take the time from August 15 ... to settle back in to my role and as a part-timer I would have to review my duties and that he would continue to oversee the finances.*⁵⁵

[97] Conversations about issues with bank reconciliations were held between them:

*I just saw that things were being put to bank fees when we wouldn't have had that many bank fees in the last month, so to me it looked like there was an amount that wasn't being reconciled ...*⁵⁶

[98] She suspected "... it was sloppy bookwork ... and lazy, like he generally was with everything."⁵⁷

⁵⁴ Transcript of Public Examinations at Dowerin on Thursday, 28 July 2016, p64.

⁵⁵ Transcript of Public Examinations at Dowerin on Thursday, 28 July 2016, pp66-67.

⁵⁶ Transcript of Public Examinations at Dowerin on Thursday, 28 July 2016, p67.

⁵⁷ Transcript of Public Examinations at Dowerin on Thursday, 28 July 2016, p67.

- [99] When asked if she worked closely with Mr Alcock when she was finance manager, Ms King said:

*As much as was possible. He wasn't really available a lot of the time. He was very distracted and he wasn't in the office a lot ...*⁵⁸

- [100] The relationship disintegrated over the years:

*When I first started I certainly looked to Dacre as a mentor, ... I had faith in his financial abilities and knowledge and past experience. ... when I did start to ask questions ... I found that ... our relationship probably started to fall down ... over time he became very difficult to communicate with, he would basically ignore me when I was in the office. ... and ... he would even be reasonably intimidating or aggressive at certain times in basically just telling me to mind my own business and that he is knowledgeable and skilled in finance, I am limited and he would take it over basically.*⁵⁹

- [101] She formed the view that Mr Alcock wasn't ably performing aspects of his job and gave an example of the integrated planning and reporting framework; he did a lot of work preparing it, but he wasn't very interested.

- [102] As to Mr Alcock's gambling:

*In a social community context certainly, and then generally his talk at morning tea or during the day quite often was about gambling and the horses he was betting on and then one instance I did see he accidentally had his laptop screen - because he was using two screens, the laptop screen was facing me while he was apparently discussing something about work but he was watching a horserace on his monitor, not really realising I could see it on the other screen ...*⁶⁰

- [103] Ms King was concerned about how Mr Alcock was performing in the job. She checked the legislation and concluded that she wasn't supposed to be talking to councillors; she didn't feel she had an avenue to raise her concerns. This reflects the misunderstanding that Mr Metcalf and Mr Ralph also shared concerning regulation 9.

- [104] During the time she was performing bank reconciliations, bank statements didn't match the general ledger. Ms King asked Mr Alcock for assistance and he said he would do it. From July 2013, he said: "... that he would take over ... made me feel that I was incompetent and probably not up to the job."⁶¹

- [105] Ms King did one credit card reconciliation. Then Mr Alcock said that he would do them from now on. In February 2013: "I asked where the credit card statements were. He leaned forward and became more direct in the

⁵⁸ Transcript of Public Examinations at Dowerin on Thursday, 28 July 2016, p67.

⁵⁹ Transcript of Public Examinations at Dowerin on Thursday, 28 July 2016, pp67-68.

⁶⁰ Transcript of Public Examinations at Dowerin on Thursday, 28 July 2016, p69.

⁶¹ Transcript of Public Examinations at Dowerin on Thursday, 28 July 2016, p70.

way that he was looking at me and said, 'You don't need to do that: I can'".⁶²

[106] Ms Shirley Anne Howard retired from the role of payroll officer at Dowerin in July 2015 having commenced work as a Shire clerk/secretary in 1990. In 2003 she became the payroll officer which continued on for 12 years. She reported to Mr Alcock and then to Ms King for some of her duties, mainly the creditors, and occasionally payroll. Credit cards were rarely used. At one point she stopped doing the reconciliations because "... we weren't getting the credit card statements".⁶³ She asked Ms King, but not Mr Alcock for the statements. She did not receive them.

[107] Despite being finance manager, Ms King had minimal involvement in the budget process and annual reports and financial reports.

[108] Requests from the auditors for documents came directly to Mr Alcock. She was never asked for credit card statements.

[109] Ms King was aware that the tokens and pin numbers were sometimes shared: "When people were on leave we had to process payroll or continue with the creditors."⁶⁴

[110] When she was going on leave she emailed Mr Alcock and said where her token was and where he could find stored passwords.

[111] On 6 October 2015, Ms King took a telephone call from the fraud department of the NAB:

... they had noticed some flags in transactions that they thought were unusual. I asked what they were and she said, "They look like they're betting transactions. Would that be something that your Shire would approve of?" and I said, "No, certainly not." Then I asked how much was it, thinking \$50 or something, and she said the last one had totalled 5000 for the month. Then I asked her to send through ...

...

*She said they had raised flags in the past ... it had obviously been happening for a period of time.*⁶⁵

[112] She told Deputy President Ralph and they reported it to the Commission.

[113] Until alerted by the NAB in October 2015, Ms King was not aware that Mr Alcock's behaviour was fraudulent. She did not suspect anything.

⁶² Transcript of Public Examinations at Dowerin on Thursday, 28 July 2016, p72.

⁶³ Transcript of Public Examinations at Dowerin on Thursday, 28 July 2016, p81.

⁶⁴ Transcript of Public Examinations at Dowerin on Thursday, 28 July 2016, p75.

⁶⁵ Transcript of Public Examinations at Dowerin on Thursday, 28 July 2016, pp75-76.

CHAPTER FOUR

The Role of the Audit and its Limitations

- [114] On 26 November 2015, the Public Accounts Committee of Parliament tabled a report "Improving Local Government Accountability" (Report No 12). In his foreword to the report, the Chairman of the Committee, Mr L'Estrange, MLA said:

*For the 2014-2015 financial year it has been estimated that Western Australia's 140 local governments will receive a combined total of \$1.9 billion from rate revenues, with a further 282 million coming into the sector via the Local Government Grants Commission. While it is important that elected councillors and local government employees are held sufficiently accountable for the manner in which these moneys are spent, the reality is that WA's local governments have tended to avoid the degree of scrutiny applied to agencies in other tiers of government.*⁶⁶

- [115] Other matters relevantly noted by the Public Accounts Committee in the 2015 report were:

- *A notable inconsistency in the level of detail and general quality of financial audit reports prepared for local governments. This issue was highlighted in 2006, but does not appear to have been the focus of any meaningful corrective action over the last nine years.*
- *A Compliance Audit Return process that is ultimately undermined by the fact that responses from individual local governments are not subject to verification or independent scrutiny.*
- *A lack of rigour and a seemingly inconsistent approach by the Department in its monitoring and follow-up of local governments regarding compliance with statutory requirements.*
- *A lack of transparency across the sector around the findings of financial audits.*
- *A lack of transparency on the non-compliance among local governments with regards to key statutory requirements of the Local Government Act 1995 (WA) and associated regulations.*⁶⁷

- [116] Inquiry panels, Parliamentary Committees, and the Commission have made recommendations about local government, many of which have yet to be acted upon. The conduct illustrated in this report may continue having a significant detrimental effect financially and in other ways on a local community. A Bill introduced to empower the Auditor General will go some way to resolving the issue, but the limitations of an audit to detect fraud will remain.⁶⁸

⁶⁶ Public Accounts Committee, Improving Local Government Accountability, Chairman's Foreword, Report No 12, November 2015.

⁶⁷ Ibid.

⁶⁸ Local Government Amendment (Auditing) Bill 2016.

- [117] As part of its oversight function, a council is required to form an audit committee.⁶⁹ This is an important role because auditors report to the audit committee not the CEO. Dowerin never established an audit committee. It had a nominal Finance and Audit Committee but it exercised no audit functions. The auditors knew Council was non-compliant but did nothing. They effectively reported to Mr Alcock.
- [118] The accounts and annual financial report must be audited and a copy provided to the Mayor or President, the CEO of the local government and the Minister.⁷⁰

The Auditor: Byfields

- [119] Auditors are not public officers and so it is inappropriate for the Commission to form any adverse opinion. It is, however, necessary to examine the audit process, what was its scope, and also what councillors and others believed its scope to be. Councils must be clear about the scope and purpose of an audit contained in the written contract.⁷¹ Council must know the limits of an audit in detecting fraud.
- [120] Byfields is a firm of accountants and financial advisors who have been engaged to conduct the audit of financial reports and accounts of Dowerin since at least 2011. The Director in charge of audit is Ms Leanne Oliver. The Audit Manager was Mr Paulo Cue. It was successful in a further contract with a supply of auditing services commencing 1 July 2013. The quote for supply of auditing services dated 10 March 2014 was presented to Mr Alcock. The quote was accepted and contained the following: "We understand we are to produce the audit report and management report as required by s 7.9 LGA (as amended)".⁷² The quote confirmed Byfields' understandings of the objective, scope and responsibilities for the proposed engagement. The approach, plan and commitment:

Methodology and Approach

The audit shall be conducted in accordance with the Australian Auditing Standards & Auditing Guidance Statements and the relevant requirements of the Local Government Act 1995 (as amended) & related regulations, the Local Government (Audit) Regulations 1996 in the following manner:

- ❖ *Develop a thorough understanding of the Council's business operations and internal control structure by performing walk through test.*
- ❖ *Assess audit risks and identify significant audit areas.*

⁶⁹ Local Government Act 1995 s 7.1A.

⁷⁰ Local Government Act 1995 s 7.2.

⁷¹ Local Government (Audit) Regulations 1996, Reg 7.

⁷² Byfields Accountants & Financial Advisers, Shire of Dowerin Quote for supply of Auditing Services dated 10 March 2014, Understanding Your Requirements.

- ❖ *Perform systems testing i.e. compliance test on all major risk areas.*
- ❖ *Review the existing system as well as the internal controls and procedures to suggest areas for improvement where appropriate.*
- ❖ *Verify material balance sheet and profit & loss account items by carrying out analytical review procedures and substantive tests.*
- ❖ *Review all aspects of the Council's operations for compliance with relevant legislations and regulations.*
- ❖ *Any items of a particularly critical nature should be forwarded via the Audit Committee and normal queries should be furnished via the administration.*

Our audit work will be cost-effective by concentrating most work on the major risk areas with minimum work on non-risk areas.

Our audit program will be designed to meet the audit objectives. At the actual fieldwork, standard programs will be tailored or improved further where appropriate to reflect the unique circumstance of Council's operations.⁷³

- [121] Byfields produced an Audit Strategy and Risk Assessment for the year ended 30 June 2014, dated 6 June 2014:

The strategy of the audit is to perform sufficient audit procedures to enable the auditor to obtain reasonable assurance as to whether the financial report of the Shire, when taken as a whole, is free from material misstatement, whether due to fraud or error, and or whether the organisation has, in all material respects, complied with the specific requirement of funding agreements and or external parties.⁷⁴

Lack of an audit committee

- [122] Byfields produced a series of independent audit reports to the Shire of Dowerin dated 19 December 2011, 4 December 2012, 12 December 2013, and 4 December 2014. Each report contained the following:

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial report. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial report, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial report in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes

⁷³ Byfields Quote for supply of Auditing Services for the Shire of Dowerin, dated 10 March 2014, Our Approach, Plan and Commitment.

⁷⁴ Byfields Audit Strategy and Risk Assessment for the Shire of Dowerin for the year ended 30 June 2014, dated 6 June 2014.

*evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by the committee, as well as evaluating the overall presentation of the financial report.*⁷⁵

[123] Although each report refers to "the committee" which must mean the audit committee, the evidence of the audit manager, Mr Paulo Cue was that there was no audit committee and he knew that Council was non-compliant in this regard but never informed them.

[124] The management report for each year submitted with the audit reports highlighted a number of issues but did not draw Council's attention to the need for an audit committee.

[125] Mr Cue said that Dowerin is one of a number of councils that don't have a formalised audit committee. He was aware of the requirements for an audit committee to be established, and responded:

*Not so much that it's properly established but experience from other councils states that basically we discuss audit issues as part of a committee meeting, so it could be a finance committee which could ... be a representative of a number of people in the council ...*⁷⁶

[126] To his understanding, nobody from Byfields ever met directly with the finance and audit committee. He acknowledged being non-compliant with legislation as something that fell within the scope of the audit. Information about the finance committee came from discussions with Mr Alcock.

[127] Mr Cue agreed he knew at the time he was conducting the audit that the CEO cannot be part of the audit committee. He agreed that the Dowerin Shire should have been formally notified that they were non-compliant in failing to have an audit committee.

Bank reconciliation

[128] Mr Cue said he obtained a bank certificate for the year-end audit. He agreed that the standard of information provided is dependent on who the conduit is. He did not find Mr Alcock prompt, dealing with information: "He was always able to deliver, whether it be an invoice or a statement or a reconciliation ..."⁷⁷

[129] The Management Report for 4 December 2014 drew the attention of the President to bank reconciliations:

It was noted from our review of the shires bank accounts during the year that there were a number of months when bank reconciliation was not performed.

⁷⁵ Byfields Independent Audit Report to the Shire of Dowerin, 19 December 2011, 4 December 2012, 12 December 2013 and 4 December 2014.

⁷⁶ Transcript of Public Examinations at Dowerin on Friday, 29 July 2016, p41.

⁷⁷ Transcript of Public Examinations at Dowerin on Friday, 29 July 2016, p47.

It is a recommendation by the department as outlined in section 5.3.6 of the Local Government Accounting Manual that as part of the local governments general systems of internal controls that a reconciliation of all restricted and non-restricted bank accounts be performed at the very least once a month.

*We recommend that as part of the shires end of month processing that all of the shires bank accounts be reconciled and any anomalies be investigated.*⁷⁸

[130] It does not appear that any action was taken by Council in relation to bank reconciliations.

[131] Ms Oliver agreed that the auditors would check bank reconciliations up until the time of the audit and she agreed with Mr Back that this was really paramount in accounting.

Fraud risk

[132] The critical matters to be audited in the interim audit included statements of financial activity. Identification of the risk of fraud is nowhere mentioned.

[133] As part of the audit process, Byfields required a fraud representation from Dowerin for the year ended 30 June 2014. Question "a) To the best of your knowledge has there been any fraud?"⁷⁹ was answered "No" by Mr Alcock.

[134] The fraud risk was assessed:

An assessment is required to be made of whether or not fraud and/or error exists and if financial information is likely to be materially misstated as a result of fraud and/or error.

All members involved in the audit, discussed the susceptibility of the Shire's financial reports to material misstatements due to fraud at the beginning and during the audit process. Given the nature of the organisation, its staff and their responsibilities and our understanding of the organisation and its internal controls it is considered that the fraud risk is no greater or no less than that of any similar organisation in the industry.

*That is given our review of the environment of the organisation and its internal controls we consider that the information obtained does not indicate the presence of one or more fraud risk factors other than those associated with any similar organisation. Certain procedures will be conducted in the analytical review of the organisation's financial reports to determine if there are inconsistencies or unusual relationships that may indicate the existence of fraud. If this is the case then management will be informed and appropriate additional tests will be performed.*⁸⁰

⁷⁸ Byfields Letter to The President, Shire of Dowerin, dated 4 December 2014.

⁷⁹ Byfields Planning and Fraud Representation Shire of Dowerin for the year ended 30 June 2014.

⁸⁰ Byfields Audit Strategy and Risk Assessment for the Shire of Dowerin for the year ended 30 June 2014, dated 6 June 2014, Fraud Risk.

Internal controls: strong or weak?

[135] The audit examined internal control in respect of:

- Revenue and Receivables
- Purchases and Payables
- Cash/bank/deposits
- Payroll

The evaluations were undertaken by verbal enquiry with management and examination of documents. These discussions and enquiry reveal a Shire with a relatively small accounting function and limited capacity for segregation of duties, however have over riding controls that mitigate the lack of segregation of duties (i.e. review and approval process performed by someone else).

We established that the Shire has a relatively strong control environment, therefore we have assessed the control risk as low - medium.⁸¹

[136] This auditor's opinion of the control environment may be contrasted with Mr Back's summary which the Commission accepts states the true position:

*There was a substantial breakdown of internal controls associated with the accounting processes regarding the payment of accounts and credit cards over a prolonged period of time. The former CEO had complete control of the accounting systems and processes and in addition was able to access security devices that would allow him to effect transactions through electronic funds transfer direct to his own bank account. The former CEO's control over the composition and presentation of financial reports allowed for these transactions to be suppressed from payment listings presented to Council. In addition he took the step to falsify records so that these transactions were not readily identified. **There was a breakdown in the checks and balances that should have detected these unauthorised transactions at an earlier time and not be allowed to go undetected for four years.***⁸²

The audit process: Ms Leanne Oliver and Mr Paulo Cue

[137] Ms Leanne Oliver is a registered company auditor and Director of Byfields Business Advisers since 2007.

[138] Ms Oliver was questioned about the findings of the audit for the periods 2011 to 2014:

*The scope can vary from ... a standard or a baseline audit ... the wider the scope ... the greater the cost ... Most councils ... select ... a standard audit which ticked off with their compliance with local government reporting.*⁸³

⁸¹ Byfields Audit Strategy and Risk Assessment for the Shire of Dowerin for the year ended 30 June 2014, dated 6 June 2014, Internal Control.

⁸² Shire of Dowerin Forensic Audit Report 2016, Volume 1, R J Back and Associates, 10 March 2016, p44.

⁸³ Transcript of Public Examinations at Dowerin on Friday, 29 July 2016, p18.

- [139] The methodology and approach outlines the audit. Firstly, in May or June there was an interim audit, then there is an end of year audit:

*The purpose of the interim audit is to do more of the planning side of the audit, so to look at the risk, how we would tackle the risk. We usually look at internal control testing at that time, different transaction testing if possible and looking at the compliance aspects that have been completed up till that point in time.*⁸⁴

- [140] As previously noted, Byfields sent Dowerin a fraud questionnaire which was completed by Mr Alcock indicating that there was no fraud.

*The purpose is to get a representation from the organisation that are they aware that fraud is taking place. It doesn't then stop there. We don't then say, "Okay, everything's good" because there are organisations which have had fraud and then they disclose those, so we audit differently. We would take this on face value, I guess, and trust that the CEO is saying the right things, but throughout our testing we would still be aware and looking for stuff that was not right.*⁸⁵

- [141] There is a step before the visit, usually conducted in the office before going to site, setting materiality:

... so what threshold we think that above will make the financial statement incorrect ...Materiality is an assessment ... if there was an error in the financial statements above a certain number, a user of those accounts may be misled, if that error remains there.

...

*We assess fraud as a risk to the organisation as a whole. It doesn't have necessarily a direct link to materiality but we would certainly sit and assess for any organisation how fraud may occur in this audit. Our aim in the audit, in accordance with the accounting auditing standards – we aren't there to necessarily just find fraud but we are required to be aware and looking out for it as we do our testing.*⁸⁶

- [142] Ms Oliver said that: "We don't go out of our way looking for [fraud] ... Because that is not what is required of an auditor under the auditing standards."⁸⁷ The relevant auditing standard is ASA 240 which relevantly provides:

Responsibility for the Prevention and Detection of Fraud

4. The primary responsibility for the prevention and detection of fraud rests with both those charged with governance of the entity and management. It is important that management, with the oversight of those charged with governance, place a strong emphasis on fraud prevention, which may reduce opportunities for fraud to take place, and fraud deterrence, which

⁸⁴ Transcript of Public Examinations at Dowerin on Friday, 29 July 2016, p19.

⁸⁵ Transcript of Public Examinations at Dowerin on Friday, 29 July 2016, p26.

⁸⁶ Transcript of Public Examinations at Dowerin on Friday, 29 July 2016, pp19-20.

⁸⁷ Transcript of Public Examinations at Dowerin on Friday, 29 July 2016, p20.

could persuade individuals not to commit fraud because of the likelihood of detection and punishment. This involves a commitment to creating a culture of honesty and ethical behaviour which can be reinforced by an active oversight by those charged with governance. Oversight by those charged with governance includes considering the potential for override of controls or other inappropriate influence over the financial reporting process, such as efforts by management to manage earnings in order to influence the perceptions of analysts as to the entity's performance and profitability.

Responsibilities of the Auditor

5. An auditor conducting an audit in accordance with Australian Auditing Standards is responsible for obtaining reasonable assurance that the financial report taken as a whole is free from material misstatement, whether caused by fraud or error. Owing to the inherent limitations of an audit, there is an unavoidable risk that some material misstatements of the financial report may not be detected, even though the audit is properly planned and performed in accordance with Australian Auditing Standards.

...

8. When obtaining reasonable assurance, the auditor is responsible for maintaining professional scepticism throughout the audit, considering the potential for management override of controls and recognising the fact that audit procedures that are effective for detecting error may not be effective in detecting fraud. The requirements in this Auditing Standard are designed to assist the auditor in identifying and assessing the risks of material misstatement due to fraud and in designing procedures to detect such misstatement.⁸⁸

[143] The final materiality threshold amount was calculated at \$30,000.⁸⁹ Ms Oliver regarded the materiality threshold of \$30,000 as being a conservative amount.

[144] Dowerin was considered by Byfields to be low to medium risk. That generally accords with DLGC assessment as medium risk. The assessment impacts on the sample tested: "The higher the risk the more work you would do to become comfortable."⁹⁰ Testing is done on site:

Practically speaking ...we contact the CEO prior to the event ... provide them with a list of documentation they need to have ready. We arrive and start working through our work papers based around these sorts of areas. While this is split into interim and final, it's not always done that way. If for some reason there was something unavailable when we are out there in interim, we make a note of it and make sure it was attended to at final.

...

An interim audit is usually two staff for a day.

⁸⁸ Compiled Auditing Standard ASA 240 *The Auditor's Responsibilities Relating to Fraud in an Audit of a Financial Report* (June 2011)

⁸⁹ Byfields File Note - Materiality, dated 2 October 2014.

⁹⁰ Transcript of Public Examinations at Dowerin on Friday, 29 July 2016, p21.

...

*As part of the control testing of the purchases and procurement process we would select a sample of invoices and follow it through their system.*⁹¹

- [145] In relation to a possible adverse comment by the Commission on the audits undertaken by Byfields, Ms Oliver said:

*The way that Mr Alcock perpetrated the fraud I don't feel in general would have been picked up. Certainly sitting here today and going well, you know, if we'd looked at the credit card closer, if we pushed harder to get them if they weren't supplied, then that may be a failing on our part; but I think in terms of certainly in the later years when it became larger, we would have picked that up if we'd got to the 15. The way that Mr Alcock was using the dongles of other members of staff to transact, there's no way we would have picked that up and the testing of control showed that, you know, the following – the proper procedure was being followed; there was dual authorisations on payments, on ordering of supplies and all things of that nature.*⁹²

- [146] Ms Oliver was asked about possible improvements:

*... rotation of audit is always a good thing. ... Outside of that, we could push to widen the scope of what we look at, keeping in mind the cost of effectiveness of doing that for Shires and clients in general are very sensitive to the fees that they pay.*⁹³

- [147] Ms Oliver said that in shires the CEO is "usually your key point of contact. It's not very often that you will have councillors come and visit."⁹⁴

- [148] As part of the quote, there was a requirement to produce a Management Report which Ms Oliver described as the "interim audit management letter. There is only one audit. The interim and final audit are not two audits ... The main management letter is recorded at the end of the audit process."⁹⁵ The interim letter is "usually sent addressed to the President but to the Shire offices"⁹⁶.

*The purpose of the end of year audit is more to look at the financial statements and the closing balances and finalisation of transactions.*⁹⁷

- [149] The financial audit has two staff onsite for two days. Specific transactions and balances are tested and randomly sampled: "what we would send the council at the end would be the management letter, the financials, the

⁹¹ Transcript of Public Examinations at Dowerin on Friday, 29 July 2016, p21.

⁹² Transcript of Public Examinations at Dowerin on Friday, 29 July 2016, p34.

⁹³ Transcript of Public Examinations at Dowerin on Friday, 29 July 2016, p35.

⁹⁴ Transcript of Public Examinations at Dowerin on Friday, 29 July 2016, p23.

⁹⁵ Transcript of Public Examinations at Dowerin on Friday, 29 July 2016, p23.

⁹⁶ Transcript of Public Examinations at Dowerin on Friday, 29 July 2016, p24.

⁹⁷ Transcript of Public Examinations at Dowerin on Friday, 29 July 2016, p24.

audit report, and that would come to the Shire addressed to the President."⁹⁸ The audit report also goes to DLGC.

[150] Ms Oliver was asked whether Byfields met with the Council or any committee: "That process is usually coordinated through the CEO and we talked to the CEOs and there are a number of them who say, 'Oh, it's not necessary.'"⁹⁹

[151] Ms Oliver said she didn't manage the audit process.¹⁰⁰ The audit manager was Mr Paulo Cue.

[152] Ms Oliver was asked about the perception that the next general audit would or should provide local government with some assurance that large amounts of money aren't going missing. Her response:

*That we don't audit – because we audit by sample to represent a population, we do not look at every transaction that goes past. We trust the documentation. It's reasonable to trust the documentation provided to us as part of that audit, so our purpose is not to conduct a forensic audit as Mr Back did but to keep our eyes open.*¹⁰¹

[153] The guide used by Byfields was published by the Institute of Chartered Accountants.

Audit and credit cards

[154] Ms Oliver was asked about credit cards:

What about credit card statements? Would they be looked at as part of the interim audit stage?---Possibly.

*Do you think they should be?---I was out doing interim audits this year and I certainly looked at credit cards up until the time of our visit.*¹⁰²

[155] Ms Oliver agreed with Mr Back that it is paramount in the area of local government to check credit cards during an audit because they are a high risk area. She agreed Dowerin's credit card policy or lack of it should have been noted.

[156] Ms Oliver said: "If the internal control is found to be failing, then we rely less on controls and do more substantive testing."¹⁰³ There was no formal credit card policy but no substantive testing was ever done.

[157] In relation to the credit card statement:

⁹⁸ Transcript of Public Examinations at Dowerin on Friday, 29 July 2016, p25.

⁹⁹ Transcript of Public Examinations at Dowerin on Friday, 29 July 2016, p25.

¹⁰⁰ Transcript of Public Examinations at Dowerin on Friday, 29 July 2016, p25.

¹⁰¹ Transcript of Public Examinations at Dowerin on Friday, 29 July 2016, p27.

¹⁰² Transcript of Public Examinations at Dowerin on Friday, 29 July 2016, p22.

¹⁰³ Transcript of Public Examinations at Dowerin on Friday, 29 July 2016, p28.

There was evidence on the file that there was a balance as at year end, therefore we requested the statements to verify those balances and those statements were on the file.

...

*Reviewing it last night there was the voucher showing the breakdown and the summary top page; because as they've said before they were all accumulated onto one header credit card ... Whether the individual credit card statements for each cardholder were viewed, I couldn't confirm.*¹⁰⁴

[158] There were no notes on the file about analysing the credit card statements. The year end balances were checked for correctness.

[159] Her attention was drawn to the fact that Mr Alcock made many credit card transactions through the general journal and not through the creditor's system:

The general journals would run to a number of pages, so to sit there and scroll through them in great detail would take a long time and usually outside the time allowed to prepare the audit.

...

*On review of the file, it indicated that general journals had been reviewed.*¹⁰⁵

[160] Ms Oliver agreed it would have been unusual if general journals were used for everyday transactions and that it should have created some suspicion. It may have been reported in the management letter.

[161] Anecdotal evidence about the SynergySoft financial software used by Dowerin is that "it's very difficult to use and of the five Shires I visited I think four of them do manual reconciliations."¹⁰⁶ This may explain why the manual reconciliations at Dowerin did not raise an alarm with the auditors.

[162] Ms Oliver thought the credit card statements were not provided. She was unaware that the auditor has the ability to request those directly from the bank.

[163] Mr Cue did not regard credit cards as a significant risk area although he acknowledged it was a risk area.

[164] Mr Cue was asked to comment on Mr Back's report: "98 direct transfers of money from the municipal funds and also from trust funds ... with no supporting documentation whatsoever."¹⁰⁷ He agreed that the auditing process did not pick these up: "... otherwise we would have raised an issue clearly."¹⁰⁸

¹⁰⁴ Transcript of Public Examinations at Dowerin on Friday, 29 July 2016, p29.

¹⁰⁵ Transcript of Public Examinations at Dowerin on Friday, 29 July 2016, p31.

¹⁰⁶ Transcript of Public Examinations at Dowerin on Friday, 29 July 2016, p32.

¹⁰⁷ Transcript of Public Examinations at Dowerin on Friday, 29 July 2016, p55.

¹⁰⁸ Transcript of Public Examinations at Dowerin on Friday, 29 July 2016, p55.

- [165] In relation to credit cards, Mr Cue did not look at the controls, he just made a reconciliation, and checked that balances aligned. The auditors didn't obtain credit card statements during the audit.

Would you agree that a councillor or the people of Dowerin seeing the audited financial statements and seeing that note at 14, which indicated zero credit limit and zero outstanding expenditure on the credit card, might be led to believe that there are no credit cards in use at the Shire?---Yes. I mean, you would, unless you were in the industry and know that there's no such thing as – it would be highly unlikely that it wouldn't have a credit card, but, yes, if you looked at that and you were just an outside observer, you would have thought perhaps there wasn't a credit card.¹⁰⁹

- [166] Mr Cue was unaware that the credit card expenditure wasn't in the creditor system in the general ledger system; it was separately journalled by Mr Alcock.

- [167] He was asked why he didn't think the auditor had uncovered the fraud:

I suppose the level of testing ... how we performed that testing. Maybe perhaps it was some form of familiarity ... and on that basis whatever we have documented on file ... would be comfortable enough to say that if my colleague has tested 20 transactions and he said he's agreed it to an invoice or has agreed it to a bank, I'm going to ... be comfortable with that ... whether or not we hit on those fraudulent transactions ... whether an invoice was fictitiously made ... it was unreasonable for any auditor to think that it was not at all genuine. ... But as far as the scope over the period of years that we're discussing ... it all comes back to what you're signing off on and the level of testing methodologies, the sample you've chosen, it all forms part of that.¹¹⁰

- [168] Mr Metcalf was aware that Dowerin had corporate credit cards. It never occurred to him as a councillor about overseeing credit card expenditure; it was an operational matter. Mr Ralph said:

You hope that they had procedures in place in operations, and that was getting done through the auditor.¹¹¹

- [169] The credit card statements were simply hidden. There was no source documentation for most of the 567 transactions. If any credit card statements had been identified for examination, auditors should have discovered there were no source documents to verify the expenditure.

The audit process: Mr Paulo Cue

- [170] Mr Paulo Enrico Cue was the Byfields Audit Manager for Dowerin. He was manager of the audit team and supervised graduates in the team.

- [171] When Mr Cue joined Byfields in 2011 he had over eight years' experience auditing large organisations. At the time he conducted audits of Dowerin,

¹⁰⁹ Transcript of Public Examinations at Dowerin on Friday, 29 July 2016, p59.

¹¹⁰ Transcript of Public Examinations at Dowerin on Friday, 29 July 2016, p62.

¹¹¹ Transcript of Public Examinations at Dowerin on Thursday, 28 July 2016, p54.

he had never overseen an audit of local government as manager, but had done parts of local government audit.

... what's noted in the audit report is whether or not the financial position at that moment- of the local government is true and fair and whether or not they have complied on a reasonable basis of the Local Government Act and specific financial regulations.¹¹²

[172] When asked whether he looks for fraud, Mr Cue said:

You do but it doesn't form the entire basis for what we do. As Leanne [Oliver] says, you don't go in there looking for fraud. It's not what the auditing standards say you must do. You need to consider it as part of providing your opinion, so, yes, you certainly – you know about it. You consider it as a risk but you don't go out there looking for it to some extent.¹¹³

[173] He was asked to comment on the risk assessment: " ... we are of the view that the risk that material misstatement might not be prevented or detected by internal procedures is low."¹¹⁴

[174] That opinion was based on verbal inquiry as well as examination of documents. When asked how he justified his view, Mr Cue responded:

First of all this is a planning document so it's a document that forms the basis of what we have seen to date and from experience. So it's not an overriding document that says because they have a strong or a weak environment it then doesn't allow us to do other forms of testing to get to an end result, which is the audit opinion we provide.¹¹⁵

The audit process and scope: The President's knowledge

[175] Mr Metcalf was unaware of the scope of the audit:

I was never aware that there was such a thing as scope for auditors. To my understanding an audit was an audit and they had a certain task to do, and I think that was the general understanding of our Council ... that the scope was a fixed – automatically the auditors did this. We've got two new councillors who have accounting background and one of those said to me one day after this happened, "The scope wasn't there" and that was the first time I was made aware there was such a thing that we could ask the auditors to do this whatever. I am now well aware, but also reading the Act ... the auditors have got untold power to move in, and I can't imagine that they would need any more direction from a council to do their job because it's all listed.

...

¹¹² Transcript of Public Examinations at Dowerin on Friday, 29 July 2016, p38.

¹¹³ Transcript of Public Examinations at Dowerin on Friday, 29 July 2016, p39.

¹¹⁴ Transcript of Public Examinations at Dowerin on Friday, 29 July 2016, p48.

¹¹⁵ Byfields Audit Strategy and Risk Assessment, Shire of Dowerin 6 June 2014, p7.

*Mr Alcock was the primary conduit ... we had no contact with the auditors.*¹¹⁶

...

Did you understand that it would detect this type of conduct?---I presumed it would.

*Did you know that the Council were required to give the auditors assurance that the material that was being provided to them was free from fraud?---I had no idea that we had that capacity to even judge that it was not fraudulent.*¹¹⁷

The annual compliance report

- [176] Mr Metcalf never saw the compliance report signed by Mr Alcock. He did not recall receiving a copy of the financial report. They were presented to Council. Council did not discuss the outcome of the audit.

... it was a mechanical thing because I was not aware of the scope and the intent of the compliance report. I now know what the scope and the intent of the compliance report is. ... reading up and checking and talking with Gary Martin ... he was absolutely scathing regards our compliance return, which was done by our CEO, and ... we did accept what he said.

...

*If you had been aware of all of these legislative requirements in relation to what an audit committee was meant to be doing, would you have ensured that they were followed?---I'm pretty sure I would.*¹¹⁸

- [177] He was not aware that any other councillor had been qualified as an accountant during the time of the fraud.
- [178] Mr Metcalf displayed ignorance of the role of the audit committee "The audit role in the old committee was very marginal. ... ignorance created this thing that we didn't realise the extent of what we were supposed to do."¹¹⁹
- [179] The auditor has the responsibility of checking, in his view. "... we have no powers at all."¹²⁰ "I would expect the auditors would be far more cynical than me."¹²¹

¹¹⁶ Transcript of Public Examinations at Dowerin on Thursday, 28 July 2016, p32.

¹¹⁷ Transcript of Public Examinations at Dowerin on Thursday, 28 July 2016, p34.

¹¹⁸ Transcript of Public Examinations at Dowerin on Thursday, 28 July 2016, pp32-33.

¹¹⁹ Transcript of Public Examinations at Dowerin on Thursday, 28 July 2016, p40.

¹²⁰ Transcript of Public Examinations at Dowerin on Thursday, 28 July 2016, p41

¹²¹ Transcript of Public Examinations at Dowerin on Thursday, 28 July 2016, p43.

The audit process: The Deputy President's knowledge

[180] Mr Ralph said he would be surprised if he knew that an audit of this kind was not designed to check for fraud: "An audit is there to pick the shortcomings in whatever organisation. Fraud is a major shortcoming."¹²²

[181] Having read Mr Back's report, Mr Ralph said:

*I was never aware of what checking mechanisms we should have had as a Council. I never ever got told. I never received documentation from anywhere. It comes back to training. Did I do the right training course to – if I had've done the right training course, yes; if I had gone the other path and done the wrong training course, I still wouldn't know. At the end of the day the duty of the Council is to employ the CEO. We employ the CEO through a reputable company that went through the process of getting him for us. We didn't employ himself ourselves. We would have hoped that the background checks were done. As a councillor I would expect the CEO is in a position of trust and he should be doing everything right, so I would have expected that that should have all been done from the CEO.*¹²³

[182] The Commission recommends that all local governments be reminded:

- An audit committee is compulsory.
- Attention be paid to the scope of work contracted with the auditor.
- An audit may not detect fraud.
- It is council's responsibility to have robust policies and procedures to mitigate the risk of fraud.

¹²² Transcript of Public Examinations at Dowerin on Thursday, 28 July 2016, p56.

¹²³ Transcript of Public Examinations at Dowerin on Thursday, 28 July 2016, pp57-58.

CHAPTER FIVE

The Forensic Audit

- [183] Mr Ron Back has many years' experience in local government as a consultant. He was engaged by the acting CEO, Mr Martin, to conduct a forensic audit. The Commission found his expert evidence helpful and accepts his conclusions.
- [184] Mr Back gave evidence that policies and procedures were lacking. There was a lack of training for staff about accounting systems, and councillors, about their financial responsibilities. Council failed to establish an audit committee. The separation of duties and internal control was non-existent for many of the accounting and compliance functions. Bank reconciliations had not been consistently undertaken (this was a task that Mr Alcock declined to give Ms King). Internal controls such as the segregation of duties were non-existent with regard to the CEO's corporate credit card transactions.
- [185] Dowerin had a direct debit arrangement with NAB so that each month the balance owing on the credit card would automatically be paid by direct debit. While this had the advantage of keeping down bank interest charges, it rendered more difficult the detection of fraud. Each month the fund Mr Alcock could illegally draw from was automatically refreshed.
- [186] Mr Back reported in detail but it is convenient to reproduce only his executive summary:

The Shire of Dowerin is located in the Wheatbelt regional development area of the State of Western Australia and is 156 kilometres from the Perth CBD. The Shire's population is 680 (ABS 2015) and the municipal district covers an area of 1,867 square kilometres.

The Shire has rate revenue of \$1.144 million and the other major source of revenues is from operating grants of \$1.9 million (after adjustment of the advance paid in 2014/15 of 50% of the Federal Government Assistance grant).

...

This report was commissioned by the Shire of Dowerin to determine the extent and impact of alleged misconduct by Mr Dacre Alcock, on the financial position of the Shire. The terms of reference stated that "Initially the period should focus on the current 2015 year and the 2014/2015 financial year and with test checking of problems identified for the 2013/2014 financial year."

It became apparent that the misuse of the Shire's credit card and bank transfers covered a much wider period. For the purpose of this investigation the credit cards for the five financial years 2010/11 to 2014/15 and the period to 1 July 2015 to 28 October 2015 were scrutinised.

The misappropriation of funds has been classified under two headings; direct misappropriations and gaining entitlements not provided for under terms of employment.

Direct Misappropriation of funds

The misappropriation of funds took place between October 2011 and October 2015. Unauthorised activity was made via the Shire's credit card, direct transfers from the Shire's bank accounts and fraudulent invoices.

Some 665 transactions relating to credit card betting and direct fund transfers, totalling \$599,879.92, have been identified as being unauthorised. On 21 occasions Mr Alcock made payments to the credit card from his personal NAB account totalling \$28,710.00 (net loss of \$571,169.92).

Period 1 July 2011 to December 2015		
	Number	Amount
Payments made to betting agencies	567	\$164,039.25
Direct bank transfers	98	435,840.67
	665	\$599,879.92
Payment made to credit card	21	(28,710.00)
		<u>\$571,169.92</u>

The first instance of a betting transaction was recorded on the former CEO's Shire credit card on 7 November 2011. Some 567, totalling \$164,039.25, payments were made to betting agencies from the Shire's National Australia Bank credit card of Mr Dacre Alcock for the period 7 November 2011 to 19 October 2015.

There were 83 transactions totalling \$363,052.67 from the Shire's Municipal Bank account and 15 transactions totalling \$72,788.00 from the Trust Bank account (total \$435,840.67) were made by Mr Alcock to his own bank accounts. Mr Alcock established different methods of transferring Shire funds into his own bank accounts, these included direct bank transfers, redirecting bank transfer by changing BSB details for creditors and falsifying invoices.

There was a complete breakdown of internal controls associated with the payment of these accounts and credit cards over a prolonged period of time. The former CEO had complete control of the accounting systems and processes and was able to access security devices that would allow him to make electronic funds transfers to his bank account. The former CEO's control over the composition and presentation of financial reports allowed for these transactions to be concealed or omitted within payment listings presented to Council. In cases where items were listed or included in supporting documents, invoices and statements were altered or falsified to remove any reference to the unauthorised transactions. This process commenced in 2011 and continued to October 2015.

Other entitlements

There exists doubt over the benefits obtained by the former CEO from the use of the Shire's credit card for private purposes, private expenses at

conferences attended and benefits greater than the contract of employment authorised.

	Number	Amount
Other Transactions		
Private use of Credit Card	12	\$2,664.21
Payment made to credit card	1	(251.00)
		2,413.21
Employee benefits		
Communications	4	5,371.76
Housing	52	27,519.71
Conferences	13	4,711.00
		37,602.47
		<u>\$40,015.68</u>

It would appear the former CEO changed the structure of his employment package without the agreement of the Council. This is included the payment of leave loading, \$2,000 increase in the communications allowance and the provision of a rent free house including all outgoings of electricity, gas, water and telephone. In addition the former CEO "cashed out" his long service leave entitlements commencing in 2013. There are no entitlements to "cash out" long service leave except on termination.

The actions of Mr Alcock in the misuse of the Shire's credit card and the direct transfer of funds from Shire bank accounts to his own personal account and the fraudulent transactions associated with masking these misappropriation of funds would warrant action under the Criminal Code Act for corruption under sections 83 and 85.

The Council had little to no effective checking mechanism that protected the assets of the Shire. The Council was reliant on its CEO to provide advice, information and guidance in undertaking its responsibilities under the Local Government Act. He was in a position to prepare, control and conceal information about the processes he used to misappropriate funds.

The Council had failed to establish an audit committee under section 7.1A of the Local Government Act. That Committee was not formally established until December 2015. Consequently, reports required under Audit Regulation 17 for risk management, internal control and legislative compliance have not been prepared.

The Shire was reliant on its auditors, Byfield's to provide the only external and independent review of the financial transactions and reports.

...

Clearly the objectives and scope of the audit failed in their application to detect any misappropriation over such a long period.

There was a substantial breakdown of internal controls associated with the accounting processes regarding the payment of accounts and credit cards over a prolonged period of time. The former CEO had complete control of the accounting systems and processes and in addition was able to access security devices that would allow him to effect transactions through

electronic funds transfer direct to his bank account. The former CEO's control over the composition and presentation of financial reports allowed for these transactions to be suppressed within payment listings presented to Council. In addition he took the step to falsify records so that these transactions were not readily identified.

...

The Council placed its trust in the former CEO to provide the necessary governance processes, controls and information that would ensure the Shire was operating within the law and the community's assets were protected. That trust was misplaced and the former CEO used his position so that the Council was not aware of the processes in operation in the administration. The total net loss of his actions is estimated to be at least \$611,185.60.

The Shire will incur more expenses in undertaking reviews, seeking recovery through insurance, organisations or individuals, new appointments, correcting prior year records, changing systems and processes and re-establishing governance processes. This will take additional resources beyond the Shire's current resourcing capacity.¹²⁴

¹²⁴ Shire of Dowerin Forensic Audit Report, Vol 1, R J Back & Associates 10 March 2016, pp1-3.

CHAPTER SIX

The role of the Department of Local Government and Communities

- [187] The DLGC is responsible for the administration of the LGA by monitoring local governments' compliance with their requirements under the LGA. DLGC carries out that function through the application of a compliance framework. Mr Jolly stated that the DLGC:

... takes a risk based approach to monitoring compliance across the local government sector

...

*Alongside the compliance activities are some capacity building programs that the department administers, things like better practice reviews and elected member training programs.*¹²⁵

- [188] Mr Jolly gave evidence that a risk based approach is taken by the DLGC in order to apply its resources to effectively monitor compliance within the sector. The approach involves the Department annually undertaking:

*... an exercise where we compile a risk profile of each local government within the State, which is based on a range of criteria that includes their financial position, the extent to which they've complied with some key statutory regulations, the number of complaints that have been made and a range of other criteria, and we assess all of that to form a view as to whether or not one or more of those local governments might be at risk. We then go through a process of categorising those according to some criteria that have been established within the organisation. From there, we would then take remedial action, depending on the perceived level of risk.*¹²⁶

- [189] A local government's annual compliance audit returns, audit reports, management letters, annual financial statement, mid-year review and budget are all considered by DLGC as part of its risk assessment process.¹²⁷

- [190] The Department identifies local governments as being either at low, medium or high risk. Local governments typically receive a letter from the Department setting out any specific concerns that led to their particular risk assessment.¹²⁸

¹²⁵ Transcript of Public Examination on Friday, 2 September 2016, p3.

¹²⁶ Transcript of Public Examination on Friday, 2 September 2016, p3.

¹²⁷ Transcript of Public Examination on Friday, 2 September 2016, pp13, 16.

¹²⁸ Transcript of Public Examination on Friday, 2 September 2016 p15.

Intervention based on Risk Assessment

- [191] Mr Jolly gave evidence that the DLGC's level of intervention in a local government's affairs varies according to the level of assessed risk.¹²⁹ If a local government is of low risk, a letter might be sent that identifies any issues that are of concern and ask that they be brought to the attention of the council for corrective action.
- [192] The medium risk local governments might have a letter in similar terms with the addition of a request to the council to respond to DLGC outlining the remedial action proposed to be taken to address those issues.
- [193] If the DLGC identifies that a local government is at high risk, that may trigger an intervention in the form of a probity audit. A probity audit assesses the local government's compliance with a range of legislative obligations.¹³⁰ A probity audit is not a statutory intervention so it relies on the cooperation of the local government. However, Mr Jolly noted that in the DLGC's experience it tends to receive cooperation because the local government understands that the alternative may be for DLGC to exercise its compulsive powers of inquiry under Part 8 of the LGA.¹³¹

2014 Risk Profile Result

- [194] The risk profile assessments identified 55 out of 138 local governments as showing an element of risk. These have been classified as high, medium and low risk affected local governments. All at high risk are country local governments. Sixteen out of the 18 local governments assessed at medium risk are country local governments.

Intervention at Dowerin when Mr Alcock was CEO

- [195] The DLGC identified the Shire of Dowerin as being at medium risk.¹³²
- [196] Mr Jolly stated that during the years that Mr Alcock was CEO, the DLGC received the documentation required to be provided under the LGA, but not always within the required timeframe.¹³³
- [197] During the time that Mr Alcock was CEO, as part of its compliance framework and monitoring role, the DLGC sent two letters to the Shire.
- [198] The first was to Shire President Mr Metcalf on 22 July 2015. This is the letter Mr Metcalf did not receive. The letter was sent in response to concerns that were raised as a result of financial management and compliance issues identified by the auditor. The letter requested that by

¹²⁹ Transcript of Public Examination on Friday, 2 September 2016 p15.

¹³⁰ Transcript of Public Examination on Friday, 2 September 2016, p17.

¹³¹ Transcript of Public Examination on Friday, 2 September 2016, p11.

¹³² Transcript of Public Examination on Friday, 2 September 2016, p21.

¹³³ Transcript of Public Examination on Friday, 2 September 2016, p17.

31 August 2015 the Council review the matters identified and advise DLGC what remedial action was proposed to be taken.

[199] Because of non-receipt, Dowerin did not consider the issues as requested and did not respond by 31 August 2015. DLGC did not follow up the Shire's lack of response until November 2015.

[200] In relation to the timing of the follow up by the DLGC, Mr Jolly stated that:

I'm not aware that there was a follow up in-between the time that that letter was sent and, then, the subsequent contact in November. Clearly, that was a breakdown in that process because there probably should have been a follow-up

...

*That system has subsequently been tightened, as you would expect, and so now it receives -- those follow-ups now are subject to closer oversight by the manager of that particular area on a regular basis with the director of the branch.*¹³⁴

[201] The second letter sent by the DLGC to Dowerin is dated 18 September 2015. The purpose of that letter was to request assistance to ensure Byfields met their obligations under the LGA by submitting the 2014 audit report and management report. Action was requested within 14 days. The letter was not actioned and there was no follow-up by the Department prior to November 2015. Mr Jolly stated that there should have been.¹³⁵

[202] In 2013 and 2014 the audit reports for the Shire received by the DLGC identified that the review of the Shire's financial management systems that the CEO is required to conduct not less than once every four years, had not been done. There was no follow-up in either year from the Department with Dowerin about the CEO's failure to conduct the review.¹³⁶

Deeply embedded weaknesses

[203] While Mr Jolly noted that had there been a timelier follow-up the Department would have been in a better position to be able to ascertain the extent to which Dowerin's response satisfactorily addressed the issues:

We need to keep in mind, of course, that dealing with rural shires, and as I think has already been identified in the evidence that's been provided to the Commission at previous hearings, there are some deeply imbedded weaknesses in the structure of local government in Western Australia. Part of those go to size and scale and capability. The sorts of issues that you are seeing at Dowerin in terms of their performance -- Dowerin is, in fact, a mendicant council. Its greatest source of revenue is from grant funding,

¹³⁴ Transcript of Public Examination on Friday, 2 September 2016, p24-25.

¹³⁵ Transcript of Public Examination on Friday, 2 September 2016, p32.

¹³⁶ Transcript of Public Examination on Friday, 2 September 2016, p26.

*and that is similar to a lot of other rural local governments. There are some significant capacity issues across the sector generally.*¹³⁷

- [204] When asked about concerns raised by repeated non-compliance with the financial management review requirement, Mr Jolly said:

Look, I think if there is a pattern of non-compliance then, yes, that should heighten our concerns. I would make the point again that the type of behaviour that you're describing in terms of timeliness with compliance obligations clearly wasn't met by Dowerin. As I think some of the data that's been provided by the Department and the risk profile will show, you know, there are certainly a number of local governments who are in the -- rural local governments, in particular, who are resource challenged, who routinely fail to meet their statutory obligations in relation to the reporting requirements, and the like.

...

*Many of these smaller local governments fundamentally lack the capacity, in my view, to properly discharge all of their statutory obligations. What that tends to manifest itself in is either non-compliance or delays with compliance. We've, I guess, effectively designed the system which is intended, to the best extent possible, to be able to capture those non-compliances and then provide the feedback to those local governments in order for them to take the appropriate remedial action.*¹³⁸

- [205] Mr Jolly noted that as a result of the Commission's inquiry there are lessons to be learnt by the DLGC in terms of how the Department might improve.¹³⁹

Independent review of compliance audit reports

- [206] Mr Jolly stated that whilst not required by the legislation, Mr Jolly would favour independent preparation of a local government's mandatory annual compliance audit report.¹⁴⁰ Mr Jolly noted that independent verification would improve confidence and rigour around the process. Mr Jolly gave evidence that the scope of the compliance audit return has been substantially reduced and significantly streamlined. The cost to a local government to have their compliance audit report independently verified would be unlikely to send even a mendicant local government 'broke'.¹⁴¹
- [207] DLGC's risk assessment criteria seems appropriate. It continues to evolve. Having regard to finite resources, DLGC concentrates on the high risk profile local governments.

¹³⁷ Transcript of Public Examination on Friday, 2 September 2016, p26.

¹³⁸ Transcript of Public Examination on Friday, 2 September 2016, p36-37.

¹³⁹ Transcript of Public Examination on Friday, 2 September 2016, p43.

¹⁴⁰ Transcript of Public Examination on Friday, 2 September 2016, p49.

¹⁴¹ Transcript of Public Examination on Friday, 2 September 2016, p45.

- [208] Some witnesses criticized DLGC for its perceived lack of action, Mr Metcalf for example said:

*We sent correspondence to the Department, so that the Minister was aware. ... Jenni Law is here today. I think it's the fourth time she's been up here in a very short while giving us a tremendous amount of direction but it was disappointing that we went so long and had nothing.*¹⁴²

- [209] On Mr Martin's first day he received a phone call from the DLGC about the letter sent to the Shire President on 22 July 2015 regarding non-compliance.

This monitoring process has identified financial management and compliance issues as well as issues identified by the auditor in his audit report and audit management report which we draw to your attention. The matters identified are detailed in the schedule attached to this letter.

*The purpose of this letter is to request that the Council review the various matters identified and to consider strategies to ensure that the Shire returns to a strong financial position and improves its statutory compliance practices.*¹⁴³

- [210] This letter was never received by Mr Metcalf. The probabilities are that Mr Alcock abstracted it before it reached Mr Metcalf. Attached to the letter was a schedule of matters to be addressed. There was no follow up after 31 August 2015.

- [211] Mr Martin saw no evidence of other oversight by DLGC:

*I had one further contact. I read through my work diary in the last couple of days and I had one further contact in about March this year, 2016. It was a Departmental officer just checking the progress of the 2014-15 audit.*¹⁴⁴

- [212] Mr Martin sent a series of emails to the DLGC seeking assistance asking whether they would consider conducting an inquiry under the LGA part 8. Mr Martin made this request because a person authorised to conduct an inquiry under the LGA part 8 has wide ranging powers, including the authority to compel the production of documents from banks or other financial institutions.¹⁴⁵ He received no response.

*I followed up about a week later because I was very keen to get the forensic audit under way. ... I contacted them and I was advised that the executive were going to be discussing it. I never heard any more about it.*¹⁴⁶

¹⁴² Transcript of Public Examinations at Dowerin on Thursday, 28 July 2016, p37.

¹⁴³ Letter from DLGC to Clr Dale Metcalf, Shire President, 22 July 2015.

¹⁴⁴ Transcript of Public Examinations at Dowerin on Friday, 29 July 2016, p68.

¹⁴⁵ *Local Government Act 1995* s 8.5.

¹⁴⁶ Transcript of Public Examinations at Dowerin on Friday, 29 July 2016, p69.

- [213] Mr Jolly later acknowledged that the response was "a bit abrupt".¹⁴⁷ The response to Mr Martin's request may have been influenced by knowledge that other investigations (including the Commission's) were occurring.
- [214] Mr Jolly has acknowledged lessons to be learned and some things to be improved.
- [215] Although DLGC has an important role to play, the LGA clearly places responsibility on the council to govern the local government's affairs and for the performance of its functions.¹⁴⁸

¹⁴⁷ Transcript of Public Examinations on Friday, 2 September 2016, p52.

¹⁴⁸ *Local Government Act 1995* s 2.7.

CHAPTER SEVEN

The Cost to Dowerin and the Steps to Recovery

The first steps

- [216] Mr Martin was engaged as Acting CEO at the Shire of Dowerin from November 2015 to March 2016 until a new substantive CEO was appointed. He is a consultant with wide experience of local government who has regularly acted as CEO. At the time of his appointment, there was a level of disruption:

*Probably a bit shaky; you know, quite clearly the events had upset the staff. There was certainly an element of self-doubt as to whether they should have or could have done more. There was an element of feeling in the community that there must have been collusion. So the environment was not all that helpful.*¹⁴⁹

- [217] A high priority was to have a forensic audit to ascertain the true position. Mr Back was engaged. Mr Martin realised there was no audit committee. There was a finance committee but it wasn't properly constituted. It was in name only. There were no minutes. He put in steps to get a proper audit committee and a separate finance committee. He introduced a number of policies including a policy that credit cards would be reconciled and signed off and scanned into the documents that went to Council. Dowerin had significant non-compliance. As to reviews:

*... they are better done externally rather than a self-assessment ... some CEOs see that as a positive, particularly in larger organisations.*¹⁵⁰

- [218] There were a number of other records missing. There was no maintenance of a register of complaints. There was no current register of disclosure of financial interests. The last entry was 2003.

Appointment of Ms Selvey

- [219] Ms Andrea Selvey was appointed CEO on 14 March 2016 having worked in local government for about 30 years. This is her first CEO position. The Commission acknowledges with thanks the full assistance Ms Selvey and the staff provided to the Commission during the investigation.

Financial costs

- [220] She commented on the financial and other costs of the embezzlement:

*The amount ... stolen \$599,879. ... It's approximately 50 per cent of the annual rate income for this Shire. ... In round terms around 700 residents, so about \$850 per person.*¹⁵¹

¹⁴⁹ Transcript of Public Examinations at Dowerin on Friday, 29 July 2016, p64.

¹⁵⁰ Transcript of Public Examinations at Dowerin on Friday, 29 July 2016, p67.

¹⁵¹ Transcript of Public Examinations at Dowerin on Friday, 29 July 2016, p71.

[221] When asked what \$600,000 would mean to Dowerin's priorities, short-term accommodation was identified:

*... a high priority to get quality holiday accommodation within the Shire. The project has had to be scaled back. There isn't the funds to progress a full-scale project as was originally planned so the project has been scaled back, but even so Council is borrowing about \$800,000 to progress the project. An extra \$600,000 would have reduced our borrowing to 200 or perhaps allowed us to incorporate a greater element of the initial master plan into the current phase.*¹⁵²

[222] There have been a number of indirect financial costs which were unbudgeted including quite a lot of re-auditing:

*... in addition to the forensic audit that was done by Mr Back and the financial management review ... there's been a lot of work ... correcting the general ledger and correcting the budget for the last few financial years ... over and above normal operations ... looking at a quantum of around \$60,000.*¹⁵³

[223] Insurers advised: "that our crime liability insurance will increase by ... exactly \$1650 this year."¹⁵⁴ And there's a form of fidelity insurance:

*We've had a payment of \$99,000 made to the Shire ... just ... got access to the ATO so there's an awful lot of work now that has to go into analysing the accounts that relate to the BAS, so we're still working through that.*¹⁵⁵

[224] There have been delays in complying with statutory reporting:

*A significant source of revenue for the Council is our federal roads funding and that had been frozen and that put a serious impact on our cash flow. ... It will take the Council some time to replenish reserves ...*¹⁵⁶

[225] As part of his report Mr Back noted:

With the reconstruction, finalisation and audit of the 2014/15 financial report of the Shire there will be a correction of the Trust accounts for AROC by \$38,870 and the Recreation Steering Committee (Dowerin Community Club) of \$23,359.11. In addition adjustments will be required to the Shire's BAS with the Australian Taxation Office.

Until the Shire has access to the ATO portal, and can properly reconstruct BAS statements since 2011, the full impact of the funds owed back to the Australian Tax Office is unclear. The known value at the time of writing this report is \$144,514.85 (\$43,723.20 pertains to 2015/16) excluding credit card transactions. This reconstruction process is likely to be time consuming and will require resourcing.

¹⁵² Transcript of Public Examinations at Dowerin on Friday, 29 July 2016, p71.

¹⁵³ Transcript of Public Examinations at Dowerin on Friday, 29 July 2016, p72.

¹⁵⁴ Transcript of Public Examinations at Dowerin on Friday, 29 July 2016, p72.

¹⁵⁵ Transcript of Public Examinations at Dowerin on Friday, 29 July 2016, p72.

¹⁵⁶ Transcript of Public Examinations at Dowerin on Friday, 29 July 2016, p73.

*The Shire will incur more expenses in undertaking reviews, seeking recovery through insurance, organisations or individuals, new appointments, correcting prior year records, changing administration systems and processes and re-establishing governance processes. This will take additional resources beyond the Shire's current resourcing capacity.*¹⁵⁷

Intangible costs

[226] As to intangible costs Ms Selvey said:

*When I first started here I don't think I appreciated the hurt and damage that had been done, but it became more and more evident that staff had suffered a great deal of hurt. They'd had their trust betrayed. Most people like to feel pride in their work and in the organisation they work for, and of course with what had happened it was very difficult for staff in a small community to feel that pride for the organisation when the trust of the community had been betrayed so badly.*¹⁵⁸

[227] One of the biggest areas of reputational damage is what is on the DLGC website: "... it's listed as being noncompliant in a number of areas on that very public platform."¹⁵⁹

The way forward

[228] Mr Back's report included 51 recommendations and an action plan was developed to put those recommendations into practice. (Tokens and the username and password are no longer kept together.)

[229] As to credit cards: "If any transactions are conducted on the credit card the documentation goes to the accounts payable officer."¹⁶⁰ The statements are reconciled. All credit card statements go to Council.

[230] There's a positive impact:

*Councillors on a whole are taking a much greater interest ... in what's happening; they ask questions, they are expecting a greater level of compliance and are willing to resource it. ... last week Council approved a restructure for the organisation which provides us with a governance officer, a governance coordinator to ensure compliance requirements are met.*¹⁶¹

[231] The audit committee now has an independent member, the CEO from the Shire of Northam who has experience with a financial background. There are plans to have the compliance audit done externally. They have new templates which are more accessible but councillors have also been asked about further training:

¹⁵⁷ Shire of Dowerin Forensic Audit Report 2016, Vol 1, R J Back and Associates, 10 March 2016, pp44-45

¹⁵⁸ Transcript of Public Examinations at Dowerin on Friday, 29 July 2016, p73.

¹⁵⁹ Transcript of Public Examinations at Dowerin on Friday, 29 July 2016, p73.

¹⁶⁰ Transcript of Public Examinations at Dowerin on Friday, 29 July 2016, p76.

¹⁶¹ Transcript of Public Examinations at Dowerin on Friday, 29 July 2016, p74.

The elected member training: we have been very fortunate to get some support from WALGA and from the Department of Local Government and Communities, to offer training in Dowerin for elected members. Elected members have done the first module of a series of four that are planned.

...

*I have entered into a formal mentoring program ... and I've arranged ... mentoring for ... staff.*¹⁶²

[232] The Commission is content to leave the last word on Dowerin to Ms Selvey:

*It's a great community with a great future and we've got some amazing projects that we're delivering at the moment and we're looking forward to being able to get on and deliver services to this community as an organisation and as a Council.*¹⁶³

¹⁶² Transcript of Public Examinations at Dowerin on Friday, 29 July 2016, pp78-79.

¹⁶³ Transcript of Public Examinations at Dowerin on Friday, 29 July 2016, pp79-80.

