

Meeting of the Risk and Audit Committee

Date: 7 May 2025
Time: 9.00am
Venue: Council Chamber
Hawke's Bay Regional Council
159 Dalton Street
NAPIER

Attachments excluded from the Agenda
available online only

Item	Title	Page
4.	Audit Plan for the 2024-2025 Annual Report	
	Attachment 1: HBRC Audit Plan for year ending 30 June 2025	2



WELCOME

Dear Risk and Audit Committee Members



We are pleased to present our Audit Plan ("Plan") for the audit of the financial statements and service performance information of Hawke's Bay Regional Council ("HBRC") and its controlled entities ("the Group") for the year ending 30 June 2025. This Plan outlines the scope of our work, your current expectations and ensures that our efforts are aligned with your expectations.

We conduct our audit in accordance with the Auditor General's auditing standards which incorporate International Standards on Auditing (New Zealand). Our audit will be conducted to provide reasonable assurance that the financial statements and service performance information for the year ending 30 June 2025 are free of material misstatement.


Our Plan has been prepared based on our understanding of HBRC and the local government sector. We have considered, and will continue to consider, HBRC's current and emerging operating risks and assess those that could materially affect the financial statements and performance reporting and align our procedures accordingly. The Plan will be responsive to your needs and will maximise audit effectiveness so we can deliver the high-quality audit you expect.

Should you have any questions or comments, please do not hesitate to contact me on 021 923 431.

Yours faithfully

David Borrie
Appointed Auditor




Charlie Cramond
Manager

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Shape the future
with confidence

EXECUTIVE SUMMARY

Hawke's Bay Regional Council


For the year ending 30 June 2025

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AREAS OF
AUDIT FOCUS

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key focus areas identified that remain broadly consistent with the prior year




Our areas of audit focus have been summarised below and explained in detail in the [Areas of Audit Focus](#) section. The level of complexity or management judgement applied has been rated as high, medium or low.

<ul style="list-style-type: none"> ▪ Infrastructure assets & PPE HIGH ▪ Cyclone Recovery and Other Grants MEDIUM ▪ Investment Property Valuation MEDIUM ▪ Integrity of rates set, rates invoicing and collection MEDIUM 	<ul style="list-style-type: none"> ▪ Performance Reporting MEDIUM ▪ Financial Assets LOW ▪ Borrowing & Derivatives LOW ▪ Expenditure, procurement and tendering LOW
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AUDIT
APPROACH

We continue to invest in transforming to an increasingly data-driven audit, leveraging our technology through data analytics and automation. We will look to further expand this where appropriate, focusing on opportunities that will provide audit efficiencies and insights.




PLANNING
MATERIALITY

\$4.1M


Our planning materiality has been set at \$6.9m, calculated at 3% of forecast operating expenses. The basis for calculating planning materiality is consistent with the prior year.

We will report all audit differences over \$205k.




INDEPENDENCE


We will confirm our independence throughout the audit and remain in compliance with [For AU: the Corporations Act 2001 OR; For NZ: NZICA Code of Ethics and the Professional and Ethical Standard 1: International Code of Ethics for Assurance Practitioners (Including International Independence Standards)(New Zealand)] independence requirements.



FEES

We agreed the fees for the 2024 and 2025 Annual Report Audits with you through the 2024 / 2025 Audit Proposal Letter process. Our current engagement letter with Council covers the same two-year period as the Audit Proposal Letter.





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Item 4 Audit Plan for the 2024-2025 Annual Report

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Infrastructure assets & PPE

Background

- Infrastructure assets and PPE represent a significant component of the Council's balance sheet with carrying values of \$436m and \$38m at 30 June 2024.
- Infrastructure assets primarily comprise of land, stopbanks, and drainage networks and are valued at Optimised Depreciated Replacement Cost (ODRC).
- A full valuation of infrastructure assets was undertaken by PDP as at 30 June 2024. Management intend to consider whether there has been a material movement in the value of these assets since 30 June 2024 and, if not, won't undertake another valuation of infrastructure assets at 30 June 2025.
- Misclassification of maintenance and/or capital expenditure given nature and useful life of work completed can be a risk.
- PPE assets are revalued triennially, with a full valuation of Land and Buildings scheduled for 30 June 2025. This will be completed by an independent third party.
- The valuation of PPE is judgmental and there are key assumptions that the valuer is required to make based on their experience. Each of these judgements have the potential to materially impact the resulting valuation and future depreciation.
- Valuation adjustments arising from significant movements in market values or replacement costs may be material. There is a risk that the useful life assumptions used in the valuations are not reflective of up-to-date information maintained in the Council's Asset Management Plans.

Planned Audit Approach

- ▶ For assets planned to be revalued this year, we will review the respective valuations for appropriateness. In particular, we will review key inputs to the valuations and consider valuation techniques for appropriateness as well as appropriateness of data used in valuation.
- ▶ For any asset classes that are not being revalued in the current year, we will examine the assumptions underlying the historical valuation against current asset management plans to assess whether the value remains materially correct.
- ▶ We will examine management's assessment for significant asset impairments and the resultant write-down of Council assets.
- ▶ We will consider management's assessment of possible material changes in asset classes where a revaluation is not planned for the current financial period in light of other available evidence.
- ▶ We will review the fixed asset reconciliation of underlying data to the general ledger with a focus on significant additions and disposals during the year.
- ▶ We will examine the appropriateness of depreciation against the estimated useful lives in the Council's accounting policies. We will also consider the useful lives included in the most recent valuations.
- ▶ We will test on a sample basis the classification procedures relating to capital, renewal and maintenance work as well as cut off at year end for capital works to check it is consistent with work completed at that point.
- ▶ We will test, on a sample basis, the accounting for significant additions and disposals of assets during the year.
- ▶ We will check the appropriateness of disclosures in the financial statements.

Relevant accounting standards: PBE IPSAS 17 Properties, Plant and Equipment

Level of complexity or management judgement: **HIGH**





Cyclone Recovery and Other Grants

Background

- ▶ Cyclone Gabrielle caused significant damage to the region's infrastructure, economy and community. Council plays an important role in the coordination of central government initiatives and funding to support local government and businesses in the region. Council is also responsible for repairing damaged flood protection assets and improving future resilience and flood mitigations.
- ▶ In May 2023 Government allocated \$133.2m of funding for removal of sediment and debris on residential and commercial properties in the region and entered into two agreements for this to be distributed through HBRC. By 30 June 2024, this funding had increased to \$193.2m consisting of \$142.6m for local and regional councils and \$50.6m for commercial entities. As at 30 June 2025, we expect all funding relating to these projects to have been utilised and any small residual amounts will be reflected in the balance sheet as awaiting distribution.
- ▶ HBRC is responsible for allocating and ensuring funds provided to other entities are spent on approved purpose and in line with the contractual agreements with government agencies. Therefore, it is important that focus is placed on the contractual clauses included within contracts with fund recipients for funds that require return to Central Government agencies if not spent on approved purpose.
- ▶ HBRC also needs to be vigilant that funds recognised as revenue meet the funding conditions and where there is no return obligation for funds revenue should be recognised upon receipt.
- ▶ In addition to the above, Council receives payments from NEMA and insurers with respect to damaged infrastructure assets.
- ▶ Council also continues to receive ongoing Waka Kotahi funding for bus services and road safety projects. For the year ended 30 June 2024, grant and subsidies from Waka Kotahi amounted to \$5.5m. Financial reporting standards require NZTA subsidies to be recognised as revenue, while a portion of the associated expenditure is capitalised.

Planned Audit Approach

We will perform the following audit procedures to validate the revenue and emergency works costs recognised during the year:

- ▶ Inquire updates with the Council on any progress related to these grants
- ▶ Obtain any new agreements, amendments or correspondence between HBRC and central government (and other providers) in respect of funding approved.
- ▶ Review HBRC's procedures for revenue recognition and monitoring the conditions of the various grants.
- ▶ Review HBRC's approach to filing insurance claims for physical damage or lost earnings.
- ▶ Check on a sample basis, that revenue is being recognised in line with obligations/undertakings being satisfied.
- ▶ For a sample of revenue recognised in the year across all grants, we will vouch receipt of funds to cash received.
- ▶ Examine costs claims from Waka Kotahi , on a sample basis, to check the expenditure is allowed to be claimed and the funding assistance rate applied was appropriate.
- ▶ Carry out an assessment of the reasonability of Waka Kotahi income and its completeness in consideration of the level of costs incurred for the period.
- ▶ Assess the disclosures in the annual report in relation to each funding agreement is in line with relevant accounting standards.

Relevant accounting standards: *PBE IPSAS 23 Revenue from Non-Exchange Transactions*

Level of complexity or management judgement: HIGH

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Investment Property Valuation

Background

- ▶ HBRC properties in Napier and Wellington are recorded as investment property (IP) at fair value. As at 30 June 2024 the portfolio of investment property was valued at \$66.7m (2023: \$67.2m).

Components	Fair value (\$m)
Napier Endowment properties	42.0
Wellington properties	24.1
Other	0.6
Total value	66.7

- ▶ The Napier leasehold endowment portfolio comprises of 134 individual properties, all being residential and 1 commercial lease. These are all perpetual renewal ground leases with all but 1 being subject to a 21-year review. Many leases have the rents at prescribed 5% of land value on review. Under the Hawke's Bay Endowment Land Empowering Act 2002, freeholding is only allowed to the current lessee under a specified valuation methodology.
- ▶ The Wellington portfolio comprises of 11 properties located in inner residential and commercial areas of Wellington.
- ▶ IP is revalued annually in line with accounting policies by registered independent valuer, Telfer Young. The valuation requires significant judgement as fluctuation in assumptions including yield can materially impact the valuation outcome.

Planned Audit Approach

Our audit procedures will include:

- ▶ Reviewing key assumptions used in the valuations and assessing whether they are reasonable, in accordance with accounting standards.
- ▶ Discussing the valuation reports with Telfer Young to understand the changes to significant judgements and assumptions they have applied in the valuation.
- ▶ Testing, on a sample basis, property specific information supplied to the valuer by management to the underlying records held by the Council.
- ▶ Understanding the changes to the market and the portfolio which would result in movements in assumed discount rates and tenure periods.
- ▶ Obtaining assurance as to the valuers' independence and objectivity.
- ▶ Considering the appropriateness of management's disclosures of the key estimates and judgements for investment property within the financial statements.

Key Judgements: *Forecasted cashflows, average occupancy period, capitalisation rates, market rental yields*

Relevant accounting standards: [PBE IPSAS 16 Investment Property](#)

Level of complexity or management judgement: MEDIUM



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Integrity of Rates set, Rates Invoicing and Collection

Background

- ▶ Rates income levied represents the Council's primary revenue source. There is specific legislation in place which must be adhered to for the rates set to be lawful. In the local authority context, failure to comply with rating law and the associated consultation requirements can create significant risks to the integrity of rates revenue.
- ▶ The requirement for there to be consistency between the rates resolution, Funding Impact Statement and the Finance Policy in the LTP is fundamental because this is the thread that links community consultation to the rates levied by HBRC forming the core of the Council's revenue.
- ▶ The accuracy of a rates set is dependent on the integrity of the rates database. The reliability of the rates billing system should ensure rates are billed appropriately.
- ▶ Legal challenges against certain local authorities have identified a range of issues relating to the legislative compliance, and therefore legality of rates sought.
- ▶ Management have a history of consulting with external legal counsel to check compliance with rating legislation is maintained.



Planned Audit Approach

Our work in relation to rates revenue and debtors will include:

- ▶ Testing Council's controls over the rate setting processes including testing the accuracy of the underlying valuation information.
- ▶ Reviewing Council's procedures for ensuring the rates set is compliant with the Local Government Rating Act.
- ▶ Examining the application of the rates set to the rating database.
- ▶ Reviewing the billing to specific ratepayers and subsequent collection on a sample basis.
- ▶ Reviewing the provision for doubtful rates debtors to consider whether it is appropriate in the circumstances.

Key Judgements: *Compliance with the Local Government (Rating) Act and provisioning for outstanding rates debtors.*

Relevant accounting standards: [PBE IPSAS 23 Revenue from Non-Exchange Transactions](#)

Level of complexity or management judgement: MEDIUM



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Performance Reporting

Background

- ▶ Council is required to report its performance against performance measures included in the Long-Term Plan (LTP). These measures are key to the Council providing a 'performance story' to the community.
- ▶ Our audit opinion on the service performance reporting covers compliance with generally accepted accounting practice, and whether the service performance report fairly reflects the Council's actual service performance for the period.
- ▶ The performance framework set as part of the Three Year Plan 2024/27 is applicable to the current financial year.
- ▶ We will select measures we deem significant across the group of activities for detailed testing in the context of our audit of the 2024/25 annual report. However, we will consider the entire performance report as part of our feedback to management. Council is required to report on mandatory measures in relation to flood protection, as governed by DIA. Our selected measures include these mandatory measures.
- ▶ HBRC performance framework includes a measure to assesses HBRC's greenhouse gas (GHG) emissions with a target of reducing emissions over time. HBRC will continue to engage the services of EKOS to prepare a GHG inventory report for the year ending 30 June 2025 which will be verified by independent auditors. The quantification of GHG emissions is subject to inherent uncertainty because scientific knowledge and methodologies to determine the emission factors and processes to calculate and estimate quantities of GHG sources are still evolving.
- ▶ There is a risk of inadequacy of reporting systems to monitor performance and hence the potential failure to adequately report the provisions of core utility services to the public.

Planned Audit Approach

Our audit procedures will include:

- ▶ Obtaining an understanding of key performance reporting processes and reviewing the collation methodologies applied by Council.
- ▶ Examining, on a sample basis, the Statement of Service Performance to determine that the measures have been reported on and outputs have been achieved where stipulated. For the selected measures this will include obtaining the underlying supporting documentation and re-performing the calculations.
- ▶ Assessing the completeness and effectiveness of the performance framework utilised.
- ▶ Checking whether all mandatory performance measures stipulated by the Non-Financial Performance Measures rules 2013 have been included in Council's reporting.
- ▶ Providing feedback on the overall annual report and the summary annual report.
- ▶ Our audit procedures on the Greenhouse gas (GHG) emissions measure will include:
 - ▶ Obtaining and reviewing the EKOS inventory reports for the year ending 30 June 2025.
 - ▶ Assessing whether the report covers adequately factors that are normally included in GHG inventory report.
 - ▶ On a sample basis testing the accuracy of the GHG activities and related emission factors applied to externally sourced documentation.
 - ▶ Assessing the adequacy of the disclosures in the annual report that describe the judgements involved in determining the reported results.

Key judgements: Selection of measures relevant to reporting non-financial performance

Level of complexity or management judgement: **Medium**

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Low Risk Focus Areas



Audit Approach



Areas of Audit Focus



Background



Planned Audit Approach



Financial Assets

Low

- ▶ Council has a managed investments portfolio which amounted to \$119m at 30 June 2024. The administration of investments is outsourced to Harbour Asset Management.
- ▶ Council's investments in Hawke's Bay Regional Investment Company (HBRIC) amounted to \$352m as at 30 June 2024. This investment is eliminated at group level as Council consolidate its subsidiaries in line with accounting standards.
- ▶ HBRC has community loans receivable which amounted to \$19.8m at 30 June 2024. This is designed to support ratepayers transition to energy efficient homes. The loans are repayable by a targeted rates over 10-year period.

- ▶ Examining key investment reconciliations.
- ▶ Confirming the existence and valuation of all investments with investment managers at balance date through external confirmations.
- ▶ Obtaining and evaluating the ISAE 3402 reports of the investment managers and custodians to place reliance over the external confirmations regarding existence and valuation.
- ▶ On a sample basis assessed the valuation of direct investments to externally sourced prices.
- ▶ On a sample basis verifying the community loans movement during the year to agreements with ratepayers and the levy of rates to repay the loans.
- ▶ Investments in the Port through HBRIC, our procedure will include reperforming the fair value calculation based on an externally sourced share price and verification of shares held.
- ▶ Assessing the appropriateness of disclosures in accordance with financial reporting standards.



Borrowing & Derivatives

Low

- ▶ Borrowing represents one of the main sources of funding for HBRC's capital projects and debt levels change with the timing of planned capital projects and the repayment profile. The total value of debt at 30 June 2024 was \$130m. Majority of the outstanding borrowing is through LGFA (\$110m), and Westpac (\$2.1m). HBRC also has borrowing amounting to \$16.7m from HBRIC and \$1.5m provincial growth fund lending.
- ▶ HBRC continues to maintain interest rate swaps to manage the Council's exposure to interest rate fluctuations arising from borrowing activities. The mark to market value of swaps as at 30 June 2024 amounted to an asset of \$1.9m.
- ▶ Apart from the LGFA borrowing, there are no financial covenants relating to the either borrowing from the banks or HBRIC. HBRC is also a guarantor of LGFA total debt, and financial reporting standards require the Council to recognise the fair value of the guarantee liability if it is material.
- ▶ The Council is also responsible for preparing Reporting Certificates to the Trustee in accordance with the requirements of the Trust Deed and we are required to report to the Trustee with respect to the accuracy of the reporting certificates.

- We will carry out the following audit procedures regarding the Council's public debt and interest rates swaps:
- ▶ Obtain an understanding of debt facility agreements maintained in the year and reviewing the relevant debt facility agreements including the process for managing drawdowns.
 - ▶ Consider the term and classification of debt.
 - ▶ Obtain an LGFA confirmation of the outstanding debt position at year end.
 - ▶ Confirm derivative positions in place at year end and independently value a sample of derivative contracts.
 - ▶ Review disclosures associated with the debt and derivative positions.
 - ▶ Review the prudence benchmark measures relating to debt, interest levels and sustainability as required by legislation.
 - ▶ We will also complete procedures required of us by the debenture trust deed.



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Low Risk Focus Areas



Audit Approach



Areas of Audit Focus



Background



Planned Audit Approach



Expenditure, Procurement and Tendering

LOW

- ▶ Appropriateness of Councillor and management expenditure is an area of interest to ratepayers.
- ▶ Council's capital works procurement programme involves significant cash flows and complex long term contract management.
- ▶ Areas of expenditure such as travel, accommodation, training and catering can present opportunities for personal benefit (or perceived personal benefit).

In considering expenditure and procurement, we will perform the following:

- ▶ reviewing Council's policies and procedures are adequate regarding the procedures for handling sensitive expenditure and conflicts of interest within the organisation and policies are consistent with best practice guidelines issued by the OAG in 2020.
- ▶ Updating our understanding of Council's procurement and contract tendering processes and testing on a sample basis contracts procured during the year follow policies appropriately.
- ▶ Reviewing, on a sample basis, expenditure and credit card statements of councillors and management and checking expenditure is appropriate and in line with Council Policies.



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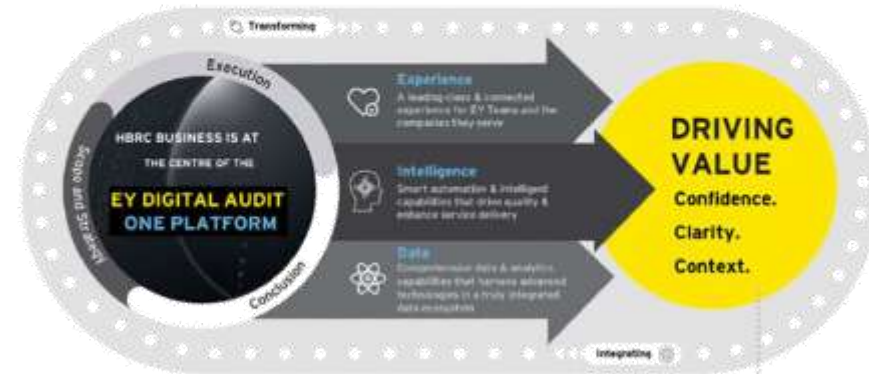
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Digital Audit Approach

Delivering a digital audit is standard to the way we execute. What is personalised is the journey.

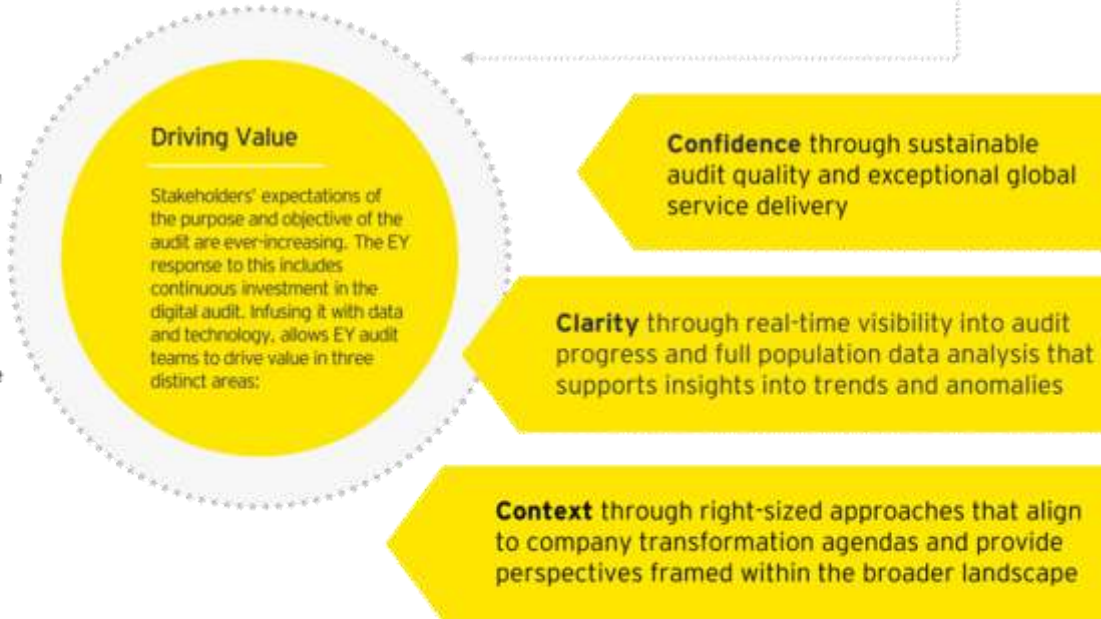
Digitalisation continues to be one of the most important drivers of transformation, especially in these changing times. The evolving business landscape has challenged the usual accounting and reporting cycles for many companies, prompting a faster transition to digital work environments. It is even more critical now for companies to share trustworthy and readily available financial information for stakeholders.



Data-driven Audit

The latest EY Assurance technology releases include the launch of additional AI-powered capabilities, such as supporting EY teams with financial statement tie-out procedures globally. EY also introduced pilots of generative AI (GenAI) technologies - driving toward the integration of the award winning EY.ai.EYQ ecosystem of GenAI capabilities with EY's next-generation Assurance technology platform.

The EY Digital Audit improves the way our auditors look at risk, reduces management burden in supporting the audit and provides recommendations to improve Hawke's Bay Regional Council's finance processes.



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Internal Control Environment

The primary responsibility for the design and operating effectiveness of the internal control environment, including the prevention and detection of fraud and error, rests with those charged with governance and management.

We obtain an understanding of internal control sufficient to plan our audit and determine the nature, timing and extent of testing performed. Although our audit is not designed to express an opinion on the effectiveness of internal control we are required to communicate significant deficiencies in internal control to you.

Our assessment of internal controls covers:

- ▶ The control environment including entity level controls
- ▶ Council's risk assessment procedures
- ▶ The design and operating effectiveness of internal controls
- ▶ Monitoring of controls

Set out below is the level of control reliance we expect to achieve over key financial statement processes. Substantive audit approach is more efficient or effective in most areas. We provide management with a report, outlining our findings and our recommendations on where improvements in internal controls can be made. Where significant deficiencies come to our attention, we will communicate these to the RAC Committee.

Process	Reliance On Internal Controls
Financial statement close	
Expenditure and accounts payable / Payroll and related employee entitlements	
Rates setting and collection	
Infrastructure, PPE and Investment Property assets management	
Non-financial performance reporting	
Other revenue - fees and subsidies	

Assessing the Risk of Fraud

Our responsibility as the external auditor is to consider the risk of fraud and the factors that are associated with it so as to provide reasonable assurance that the financial statements and performance information are free from material misstatement resulting from fraud. However, it is important to note that while our external audit work is not primarily directed towards the detection of fraud or other irregularities, we will report any matters identified during the course of our work.

When developing our Audit Plan we use professional judgement in determining whether a fraud risk factor is present. We determine fraud risk factors in the context of the three conditions generally present when fraud occurs (i.e., incentive/pressure, opportunity and attitude/rationalisation).

Our approach to fraud risks are outlined below:

Understanding the business and the control environment - We will enhance this understanding to provide a foundation for our risk assessment. Our understanding includes the business model as well as external factors and internal factors, including the governance and monitoring structures in place.

Identification of risks of material misstatement due to fraud - we will challenge risk assessments in line with the current environment, applying the fraud triangle when making these risk assessments, focusing on sources of fraud risk factors.

Responding to risks of material misstatements due to fraud - we will take into account our understanding of the entity's business and its control environment, designing tailored responses to identified risks of fraud and evaluating the reliability of audit evidence obtained

Identifying and responding to fraud risks in an audit - We will apply data analytics to enhance identification of and response to identified fraud risks.

Communicating our audit approach to fraud risks - We will discuss fraud risks with the audit committee including our approach to addressing those risks.

Communicating identified or suspected fraud - We will report any instances of suspected fraud to management and the audit committee in accordance with obligations under both auditing and ethics standards.



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Your EY Team

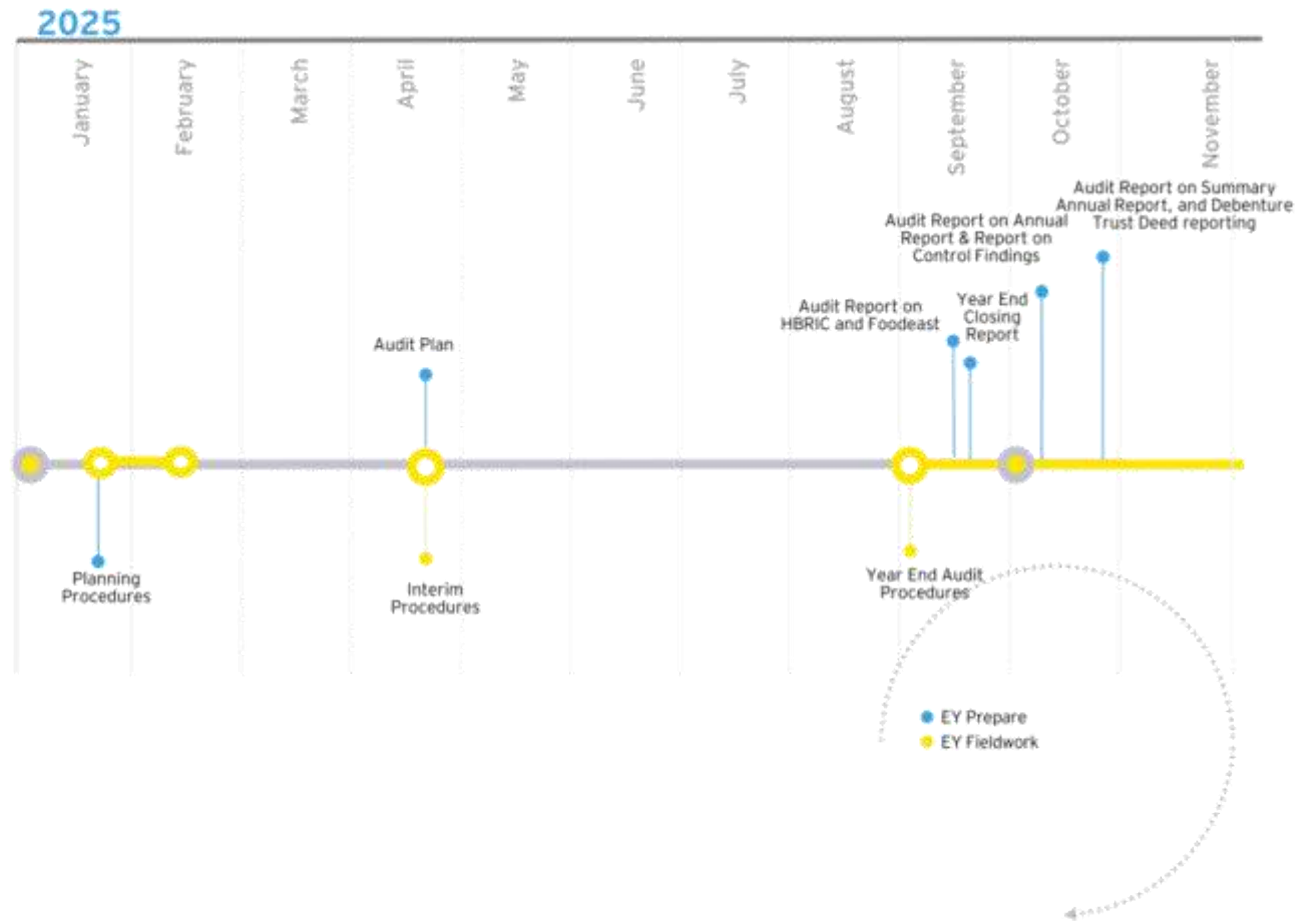
We understand that our team is the most important element of your relationship with us.

Our team has been involved in the audit of Hawke's Bay Regional Council for a number of years. This stability provides HBRC with continuity, historical knowledge of your business and industry expertise. These combined factors enable us to focus on the significant matters relevant to your business. Further we have incorporated experts to assist us in addressing the financial risks relevant to HBRC.



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Engagement Execution





A. Independence

Independence is fundamental to EY as our ongoing reputation and success is connected to our ability to meet both the Council's and broader regulatory independence requirements.

We have consistently complied with all professional regulations relating to auditor independence including those outlined in:

- ▶ PES 1 International Code of Ethics for Assurance Practitioners (including International Independence Standards) (New Zealand)
- ▶ Auditor General's (OAG) independence standards.

Accordingly, we ensure that there are controls in place and actions taken on a regular basis that mitigate any risks to our independence.

There are no matters that, in our professional judgement, bear on our independence which need to be disclosed to the Committee.

We identify in the table the threats to our independence from the services we provide or relationships with the entity and the safeguards adopted to reduce or eliminate those threats. We consider that our independence in this context is a matter that should be reviewed by both you and ourselves. It is therefore important that you and your Council consider the facts of which you are aware and come to a view. Should you have any specific matters that you wish to discuss, please contact us.

	Fees (\$'000)	Independence threats	Actions taken to eliminate or address the threat and safeguards adopted
FEES PAID TO EY FOR NON AUDIT WORK:			
Debenture Trust Deed Reporting	3	Self interest threat	Permitted service. Independent assurance services. Work required to be completed by the entity's auditor.

Because HBRC is a Public Interest Entity those charged with governance are required to approve the provision of non-assurance services by HBRC's auditor. We have agreed with those charged with governance that such services will be approved on a case by case basis.



Appendices

B. System of Quality Management

The annual evaluation conclusion for EY New Zealand is that the objectives of the System of Quality Management are being achieved as of 30 June 2024 and that they support the consistent performance of quality audits and related engagements.

EY's approach to quality management

Professional and Ethical Standard 3 ("PES 3", which is the NZ version of ISQM 1) is applicable to all firms that perform audits and other similar engagements. As a result, we are required to design, implement and operate a system of quality management ("SQM") to provide reasonable assurance that:

- The member firm and its personnel fulfil their responsibilities in accordance with professional standards and applicable legal and regulatory requirements, and conduct engagements in accordance with such standards and requirements
- Engagement reports issued by the member firm or engagement partners are appropriate in the circumstances.

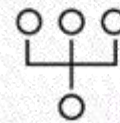
We are also required to monitor, remediate and annually evaluate the SQM as well as communicate to those charged with governance how the SQM supports the consistent performance of quality engagements. The following slides explain our approach and the results of our most recent assessment.

Individuals with SQM roles have the appropriate experience, knowledge, influence and authority, and sufficient time to fulfil their System of Quality Management roles and are accountable for fulfilling their responsibilities.

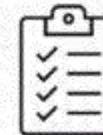
Note: In the context of the annual evaluation of the SQM, EY New Zealand refers to the following member firms performing audits or reviews of financial statements or other assurance or related services engagements: Ernst & Young (partnership), Ernst & Young Limited and Ernst & Young Strategy and Transactions Limited.

EY is dedicated to delivering high-quality audits and assurance engagements and serving the public interest.

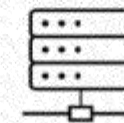
Key elements of EY's SQM



Common processes, policies, programs and technologies



Consistent quality objectives, quality risks and responses



Commitment to conduct high-quality audits across the EY organisation

EY member firms, which include the relevant New Zealand firms, are ultimately responsible for the design, implementation, and operation of their SQM, and have the responsibility to:

- Evaluate policies, technologies, strategies, programs and baseline elements provided to them
- Determine if they need to be supplemented by the member firm to be appropriate for use.



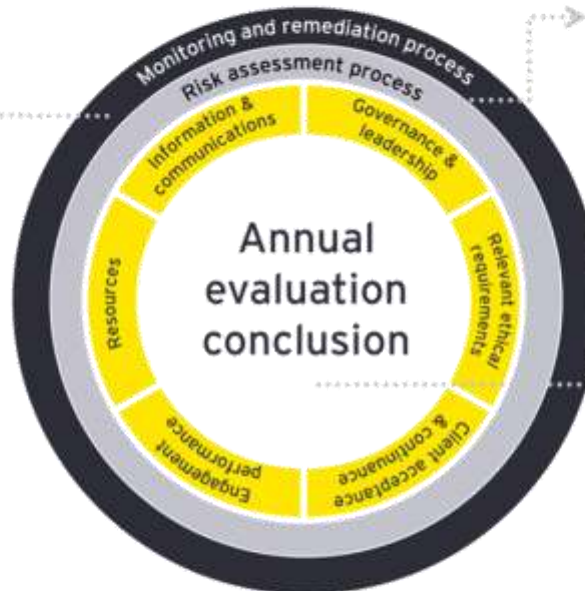
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B. System of Quality Management (cont.)

SQM processes to support quality audits

Monitoring and remediation process

- Provide relevant, reliable and timely information about the design, implementation and operation of the SQM and a basis for the identification of deficiencies in the SQM.
- Monitoring activities include monitoring the entire SQM (e.g., testing SQM controls, internal inspections of completed engagements, assessing member firm and personnel’s compliance with ethical requirements related to independence).
- If deficiencies are identified, they are corrected on a timely basis and an action plan is designed, implemented and evaluated for effectiveness.



Risk assessment process

- Establishing quality objectives (based on PES 3 requirements).
- Identifying and assessing quality risks.
- Designing and implementing responses (including policies, technologies and key controls).

Annual evaluation conclusion

- The annual evaluation conclusion:
- Is as of 30 June for all EY Member Firms performing engagements in the scope of PES 3
 - Considers the results of monitoring activities.

Key roles within the SQM include:

- The Country Managing Partner: assigned ultimate responsibility and accountability for the SQM by concluding on its effectiveness.
- The Country Assurance Managing Partner: assigned operational responsibility for the System of Quality Management. This includes recommending the System of Quality Management annual evaluation conclusion to the Country Managing Partner.
- The Country Independence leader: assigned operational responsibility for compliance with independence requirements.
- The Country Professional Practice Director: assigned operational responsibility for monitoring the SQM including concurring with or proposing changes to the recommended SQM annual evaluation conclusion.



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