



LOCAL GOVERNMENT CODE OF ACCOUNTING PRACTICE & FINANCIAL REPORTING

SUBMISSION RELATING TO DRAFT CODE UPDATE # 9

We set out below our submission in relation to the draft of update #9 to the Local Government Code of Accounting Practice and Financial Reporting.

1 Timing

We submit that, as a general policy, a Code Update should not be issued any later than the end of February of the year in which the changes are to commence to take effect.

2 Section 2 - Definitions - “Fee”

We suggest that confusion exists within the industry as to the proper differentiation between “Regulatory Fees” and “Discretionary Fees”. We suggest that it would be useful to differentiate the examples given in this definition between the two types of fees.

3 Section 2 - Definitions - “Legal costs - other”

We submit that conveyancing costs relating to the sale of land held for resale is more appropriately treated as deduction in determining the net sales proceeds, and should not be included within “Legal costs - other”. Accordingly, we believe that a notation to this effect should be made within this definition.

4 Section 2 - Definitions - “Ordinary Activities”

We agree that this is an accurate quotation from the accounting standard. However, the range of activities in which a Council may engage is so wide that additional guidance may well be appropriate. We are of the view that flood repair and other disaster relief activities are within the purview of “ordinary activities” for local government, but the events giving rise to such activities are certainly not “ordinary”.



Similarly, the “objectives” of local government are so wide that almost any activity may be said to be “a related activit(y) in which the entity engages in furtherance of, or incidental to, or arising from activities undertaken to meet its objectives.”

5 Section 2 - Definitions - “Outside Equity Interest”

We submit that this definition would be clearer to Local Government accountants, and more appropriate to a *Local Government Code of Accounting Practice* by adding “i.e. the ratepayers of the reporting Council” to the end of the definition as printed.

6 Section 4.3 - Submission of Financial Statements - last paragraph

We submit that the last sentence should read “as long as the minimum information provided in the general purpose financial reports in Appendix A1 of Section 10 of this Code, *and any additional information required by the Australian Accounting Standards*, are met,...”. We suggest that such an amendment would be appropriate to cover any situations where the Code does not make specific provision for additional disclosure that may be required by the standards.

7 Section 4.5 - Statement of Financial Performance - first paragraph

We submit that the cross-reference to paragraph 31 of the old AAS 1 is now out of date. (Paragraph 31 of the previous standard referred to transfers to and from reserves, which is not referred to in the new standard. We anticipate an amendment to AAS 27.)

8 Section 4.5 - Statement of Financial Performance - (f)

We recognise that the wording of this paragraph replicates that of the Standard. However, we would be interested to know the number of Councils who need to recognise an actual taxation expense in relation to their principal activities.

9 Section 4.5 - Statement of Financial Performance - paragraph commencing “borrowing costs expense”

We draw to your attention that AAS 27 specifically requires that expenses and revenues be classified both by nature and by classification (paragraphs 76 & 86). We submit that it would be appropriate to refer to this over-riding requirement here.

10 Section 4.5 - Statement of Financial Performance - Discussion (c)

We submit that it would be appropriate to refer to *material* errors rather than retain the current implication of *all* errors.



11 Section 4.5 - Statement of Financial Performance - Disclosure of Expenses before Revenues

We oppose the proposed disclosure of expenses before revenues, and find the purported explanation to be unconvincing.

One of the stated aims of local government reporting is to adopt disclosure procedures common to those of commerce - where revenues always precede expenses.

In some other jurisdictions, local governments are required to budget for all anticipated expenditures and incomes other than rates, and to strike a rate sufficient to result in a “balanced” budget. In NSW, under a rate-pegging regime, this argument does not exist.

In order to comply with AAS 37 paragraph 4.5 a number of the notes to the accounts should be re-numbered.

For consistency, the presentation in the Statement of Cash Flows should show Payments before Receipts.

12 Section 4.5 - Statement of Financial Performance - Joint Ventures not “Ordinary Activities”

Unlike commerce, where joint venture vehicles are most commonly used for activities not directly related to the core activities of the principal corporation, local government tends to use joint venture vehicles as a means of delivering ordinary services on a shared basis with other Councils in order to achieve appropriate economies of scale. We concur with the example presentation in AAS 1 where the results of joint venture operations are treated as “ordinary activities”.

13 Section 4.6 - Statement of Financial Position - 2nd, 3rd & 4th paragraphs

We recognise that these are correct transcripts from the accounting standard. However, we submit that NSW local government has a clearly identifiable operating cycle of 12 months exactly, and that this is an area where it is appropriate for the Code to prescribe

- * the use or current/non-current presentation (in effect policy 4.6.1 and Appendix 1 do this in any case)
- * that a twelve month period must be used as the basis for identifying current assets and current liabilities.

We note that policy statement 6.2.3 is to the above effect and suggest that it is appropriate to make a similar reference in this section.

14 Section 4.6 - Statement of Financial Position - reference AAS 36, para 4.5 - Discussion

The accounting standard refers to an entity having “agreed to finance the obligation on a long term basis”. We suggest that it frequently happens in local government that formal agreement (ie. by resolution of Council) may only occur when the renewal of the loan is imminent, and submit that the requirement of the standard should be regarded as having been met if (in the absence of formal Council resolution to renew the loan) the adopted management plan provides for its renewal, and that wording to that effect should be inserted here.



15 Section 5.3 - Functions/Business Activities - Policy 5.3.1

It is in the nature of this type of submission that it is only matters where changes are sought that are listed - the many matters with which we agree, or at least have no argument, receive no mention. However, we support the proposed disclosure of "governance costs".

We submit that the description included in Section 9.5 should also form part of the discussion in this section. It would also be appropriate to indicate the separate components that should be allocated to "Council", "Executive Support" and "Other" in Special Schedule 1. Is it intended that "Council" relate only to elected members fees, allowances, expenses and election costs, or does this include all costs associated with the Council as a body in meetings (including staff time)?

16 Section 5.4 - Revenue from ordinary activities - Discussion - last paragraph

We have noted that some Councils disclose gains from the sale of assets separately from losses from the sale of assets, although by far the majority disclose only the net gains or losses. We suggest that this paragraph should nominate the disclosure to be adopted by reference to policy 5.6.2 (and similarly in section 5.5).

17 Section 5.5 - Expenses from ordinary activities - Discussion - paragraph 3

Although not a change in this draft, the wording of this paragraph relates more appropriately to the classification of asset types, and its connection with the disclosure of depreciation and amortisation expense is not clear. We suggest that the paragraph could be replaced with "depreciation and amortisation expense should be sub-classified in accordance with asset classifications disclosed in Example Note 9".

18 Section 5.5 - Expenses from ordinary activities - Discussion - Other Expenses

Our recent inspection of the annual statements of a number of Councils shows that there is a very wide range of interpretations of "Other Expenses", and it is probably now appropriate to provide more comprehensive guidance.

We recommend that examples of other expenses could be given, and would include the following in our list:-

Advertising, Auditor's Remuneration (dissected as required by the Standards), Bank Charges, Consultancies, Donations and Contributions to Local & Regional Bodies, Election Expenses, Insurances, Legal Expenses separately disclosing planning & development and other), Light, Power & Heating, Mayoral Allowance, Members' Fees & Allowances, Members' Expenses, Operating Lease Rentals (dissected as required by the Standards), Payments to other levels of government, Revaluation Decrements, Street Lighting (if not otherwise included under Power, Light & Heating), Subscriptions & Publications, Telephone & Communications

We submit that there are certain items in the above list that should always be disclosed and draw your attention to the wording in paragraph 1.3 of AAS 37.



19 Section 5.10 - Cash Flows - last paragraph

We understand that the previous calculation of legal limit of overdraft is no longer applicable, in which case amendment to this wording would be necessary.

We also understand that, under Loan Council arrangements, any authorised borrowings not drawn at the end of the financial year lapse, in which case the amount of borrowings still available would be NIL in every case.

20 Section 5.14 - Performance Indicators

Unrestricted Current Ratio

For the reasons we gave in our email to Mr Portelli dated 10/11/2000 we oppose the inclusion of special rate fund overdrafts in the calculation of this ratio.

Rates & Annual Charges Outstanding Percentage

With the clarification of Interest & Extra Charges in Note 7, we submit that the inclusion of these amounts should be specifically referred to in this section.

21 Section 5.16 - Extraordinary Items

The discussion section quotes paragraph 5.5.3 (b) from the Standard.

We refer to our comments in paragraph 4 on page 1 above and repeat our view that the recovery from natural disasters is an **ordinary activity** for local government organisations. We therefore suggest that a different example be selected.

22 Section 6.4 - Measurement of Assets - Revaluations

We suggest that policy 6.4.3 would be clarified by the addition of the words “in relation to the assets used in those business entities” to the end of the policy.

23 Section 7.1 - Recognition of Liabilities - Commitments Which Do Not Qualify

We suggest that the the words “but note that disclosure of future commitments is required” be added to the last three dot points.

24 Section 7.1 - Recognition of Liabilities - Definition of Current Assets

We suggest that the first heading on page 7004 be amended to read “Current Liabilities”.

We have some concern with the last sentence of the last paragraph on this page. In relation to unexpended loans, we would assume that the classification between current and non-current would be based on the characteristics of the loan itself, and be independent of whether the loan has been expended or not. In our view, the non-expenditure of the loan would merely affect the restriction, if any, remaining in relation to those funds.



As a general rule, grants are required to be treated as revenue upon receipt and would therefore not appear as a liability. Again, the non-expenditure of the grant would merely affect the amount of the restriction recorded in relation to those funds. (On 16/9/2000 we submitted a paper in relation to GST on Grants that may possibly affect the above treatment, but to date have received no response.)

May we suggest an alternative example that may be given would be in relation to building bonds and deposits that are not expected to be repaid within 12 months.

25 Section 7.3 - Accounting for Employees' Leave Entitlements - page 7013

We suggest that the section "Accounting for Initial Adjustments" could now be entirely omitted.

We suggest that the last sentence of the sub-heading "Investments" should be re-worded to refer to "Section 6 of this Code".

26 Section 8 - Accounting for Equity - Revenue Reserves

Some jurisdictions permit the disclosure of revenue reserves in the Statement of Equity while also separately requiring that restricted cash amounts be retained to fund those reserves. As the NSW practice is not to disclose revenue reserves in the Statement of Equity, this should be stated in policy 8.1.2 and in the discussion relating thereto.

27 Section 9.4 - Rates, Charges, Fees & Fines

In the course of our recent inspection of a number of Council's Annual Statements we noted instances of Councils classifying the total amount of pensioner rate rebate granted to pensioners as an expense, rather than netting the amount against the rates revenues raised. There was also a wide range of classifications of *ex gratia payments in lieu of rates*. We submit that specific reference to both should be made within this section, and specific provision be made in Note 3(a) for the *ex gratia* amounts (as they stand in place of, and are usually calculated with reference to, rates).

We also noted that the definition of "user charges" contained in section 2 of the Code is not being uniformly applied, and we suggest that the discussion under this item be expanded to clarify the matter.

We suggest that specific reference should also be made to revenues related to the Companion Animals Act. In receiving registration monies, is Council merely acting as "bare trustee" for the Department? in which case amounts collected but not forwarded should be recorded as a liability.

28 Section 9.5 - Allocation of Overheads

We feel that there is a conflict between the second sentence of the paragraph commencing "Other overheads" on page 9012, and policy 9.5.3. We suggest that the words "(where a reliable basis exists)" to that sentence would remove the conflict.

Similarly, revision would also be appropriate for the last paragraph under heading "Indirect Costs" on page 9014.



29 Appendix 1 - Table of Contents

We strongly support the relocation of the Auditors Reports.

30 Appendix 1 - Statement of Financial Performance

We refer to our comments in paragraph 11 on page 3.

We submit that the proposed display of the Statement of Financial Performance will encourage and develop confusion and submit the following for consideration. We have not amended the draft format to give effect to our recommendations in paragraph 35 on page 9 below)

Expenses from Ordinary Activities

Materials & Contracts
Employee Costs
Borrowing Costs
Depreciation & Amortisation
Other Expenses
Loss on Disposal of Assets

Revenue from Ordinary Activities

Rates & Annual Charges
User Charges & Fees
Interest & Dividends Received
Grants & Contributions - non-capital
Other Revenues
Gain on Disposal of Assets

Surplus/deficit from non-capital ordinary activities

Grants & contributions for capital purposes
Share of result of associates and joint ventures accounted for using the equity method
Correction of fundamental error

Surplus/(deficit) from ordinary activities

Extraordinary Items

Surplus/(deficit) after extraordinary items

Surplus/(deficit) attributable to outside equity interests

Surplus/(deficit) attributable to Council

The above presentation would need amendment if our comments in paragraph 35 on page 9 below are accepted.



31 Appendix A1 - Statement of Changes in Equity

May we suggest the following as a revised presentation?

	Notes Ref	2001 \$ '000				2000 \$ '000					
		Retained Profits	Asset Revaluation Reserve	Council Equity Interests	Outside Equity Interests	Total Equity	Retained Profits	Asset Revaluation Reserve	Council Equity Interests	Outside Equity Interests	Total Equity
Balance at beginning of the reporting period											
Changes in equity recognised in the statement of financial performance											
Adjustment due to compliance with revised Accounting Standards	*										
Transfers to Asset Revaluation Reserve	*										
Transfers from Asset Revaluation Reserve	*										
Balance at end of the reporting period											



32 Appendix A1 - Statement of Cash Flows

We draw to your attention the similarity in definitions of *cash*, *cash on hand* and *cash equivalents* in AAS 28 and *cash-equivalent assets* in AAS 36. We submit that reference should be made to this in this section, and that the “cash” to which the Statement of Cash Flows should be reconciled is the amount shown in the first sub-heading in Note 6 (subject to any bank overdraft).

As referred to in paragraph 11 on page 3 above, the presentation of the Statement of Cash Flows should be consistent with that of the Statement of Financial Performance, and internally consistent within itself (refer Investing Activities).

There is a further minor inconsistency in that Note 5 differentiates between Property, Plant & Equipment and Real Estate Assets as three items while the Statement of Cash Flows groups Property with Plant & Equipment.

33 Appendix A2 - Note 1 - Significant Accounting Policies

We submit that an appropriate sequence for disclosure of accounting policies would be:

- * the nature of the statements and policies fundamental to their basic understanding.
- * policies relating to specific revenue, expense, asset and liability classifications, broadly in order of their appearance in the principal statements and subsequent notes.
- * other policy matters and references to Standards that may otherwise be thought to have some application (eg. AAS 35).

34 Appendix A2 - Note 2 - Functions

One of the fundamental concepts underlying AAS 27 is the requirement that local governments are required to report their activities by nature (type) **and** by function. The interleaving of separate items at the foot of the draft Note are tending toward a situation where some items are reported by type twice.

We have been unable to identify any reference to the location for disclosure of financial assistance grants and pensioner concession subsidy - items previously included as general purpose revenues. It is also not clear whether special rates (water, sewer) and annual charges for DWM, etc are to be reported under the relevant functions or under “Rates & Annual Charges” at the foot of the Note.

When compared with the very terse descriptions of the nature of all other functions, that of “Governance” tends towards being prolix. “Costs relating to the Council’s role as a component of democratic government, including elections, meetings and associated activities, area representation, and public disclosure and compliance, together with related administration costs” could be a suitable description.

35 Appendix A2 - Note 3 - Revenues

Investment Income

Many Councils, by virtue of their memberships of NRMA, will have received dividend income relating to their share ownerships. The same applies to a number of other Councils who have previously been involved in share-farming arrangements, and who have received issues of shares in newly privatised marketing authorities.



Other Revenues

The item “Equity interest in joint venture operating result” also appears on the face of the Statement of Financial Performance, and should be removed from Note 3(d).

Grants & Contributions

During the course of our inspection of Council annual statements we noted a large variation in interpretations in this section, particularly in relation to apportionment between capital and non-capital, but also generally. Some types of receipts by Councils are treated by most as “grants”, but by others as “contributions”.

In fact, we believe that a “capital/non-capital” disclosure is of less benefit than a “recurrent¹/non-recurrent” disclosure would be. Accordingly, we suggest the following display:

Payments from other levels of Government - Recurrent

Financial Assistance Grants
Pensioner Rates Subsidies
State, Regional & Local Roads & Bridges
Employment & Training Programs
Community Care Services
Bushfire & Emergency Services

Payments from other levels of Government - Non-recurrent

Water & Sewer Construction
National Disaster Funding
Construction Grants - Community Care Facilities
Other

Contributions & Donations from Other Sources

Developer Contributions
etc
etc

If this suggestion is adopted there would need to be consequential amendment to the Statement of Financial Performance.

We suggest the use of “Subdivider Dedications” in lieu of “Land & other material public benefits” as an appropriate description of works and land transferred to Council. Strictly, these may physically be roadworks, drainage, water, sewer etc and the existing wording could be interpreted as requiring dedications to be split between each type, to which any cash Section 94 contributions would be added. We submit that the wording “Subdivider Dedications” covers all of the above, leaving the subsequent descriptions to apply only to cash contributions received under the various plans.

1. We would define a “recurrent” payment from another level of government as one which the Council has a reasonable expectation that a payment, similar in amount and for similar purposes, would be made in each of the 3 succeeding reporting periods (ie. the life of the current Management Plan).



36 Appendix A2 - Note 4 - Expenses

We are of the opinion that the disclosure requirements of AAS 17 in relation to non-cancellable operating leases are quite onerous, and failure to make provision for all of the various possibilities in Note 4(d) in the Code may lead some officers to wrongly assume that the Standard need not be complied with.

We have listed our recommended schedule of “other expenses” in paragraph 18 on page 4 above.

37 Appendix A2 - Note 5 - Gain or Loss on Disposal of Assets

During the course of our inspection of some annual statements we noted some instances where a fourth item, “Gain/(Loss) on Disposal of Infrastructure” was inserted. We have no information relating to the circumstances that applied, but suggest that a policy be formulated and included in the Code.

38 Appendix A2 - Note 6 - Cash Assets & Investment Securities

We suggest that the line “Short Term Money Market” is effectively made redundant by the new line inserted “Deposits at Call”. We also refer to our comments relating to “cash” for the purposes of the Statement of Cash Flows in paragraph 32 on page 9 above.

We refer to our comments in paragraph 35 on page 9 above in relation to shares (listed and unlisted) allotted to Councils during privatisation of formerly public enterprises. Appropriate provision needs to be made for disclosure of these amounts.

Restrictions - 1

We have come to the view that the accounting policies relating to the nature of restrictions on Council assets (currently included in Note 6) more properly belongs in Note 1, particularly as some of those descriptions also relate to Notes 7, 8 & 9.

Restrictions - 2

We suggest that the segregation of restrictions between current and non-current on page 2 of this Note may be misleading. It is perfectly valid for a Council to hold Section 94 contributions that are not expected to be spent for (say) 24 months in the form of relatively short term cash securities but the arithmetic of the note format means that the restriction must be shown as “current”. In general, the existing design of this Note means that there is an implied shortening of the period of all restrictions.

See also our comments in paragraph 43 on page 13 below.

Restrictions - 3

Although it is not NSW policy to include revenue reserves in the Statement of Changes in Equity (see paragraph 26 on page 6 above), we are inclined to the view that these amounts are equity reserves within the meaning of AAS 36 and that a reconciliation of movements should therefore be provided. An alternative treatment would be to segregate all information concerning all restrictions for all assets and liabilities to a separate Note.



39 Appendix A2 - Note 7 - Receivables

The separate disclosure of “Interest & Extra Charges” will eliminate much confusion that has existed on whether these form part of “Rates & Annual Charges” or “Accrued Revenues”. We would prefer to combine the first two lines into a single item “Ratepayers - Secured” covering all amounts that are commonly held in a Council’s subsidiary rates ledger.

We suggest the replacement of “Government Grants & Subsidies” with “Other Levels of Government” as a more comprehensive term. We note the removal of the line “Private Works” but believe that a line to similar effect will be required by most Councils. Indeed, we would prefer to add two items described “Ratepayers & Residents - Unsecured” and “Other Persons - Unsecured”.

Financial Instruments Disclosures

We submit that government grants and subsidies are guaranteed only to the extent of compliance with the specific terms and conditions of the relevant agreement, some of which exceed 25 pages. The implication of absolute guarantee, we believe, is incorrect.

Debtors resulting from land development and resale exposes council only to the level of risk associated with the failure of a debtor to settle as set out in the contract. Council’s exposure to the instability of the real estate market affects the value of the inventory of unsold land, which is not a financial instrument.

Bills of Exchange are an investment security, not a receivable, and this notation should form part of Note 6. We question whether the information given in the draft note conforms to the Minister’s Order (Appendix A9).

40 Appendix A2 - Note 9 - Property, Plant & Equipment

We believe that this note would read more naturally if read from left to right, rather than from right to left as shown. The current year’s information could be highlighted by the use of **bold type**. Please note the clerical errors in the headings of the third and fourth columns from the right.

41 Appendix A2 - Note 10 - Payables, Provisions and Interest Bearing Liabilities

We suggest the addition of the description “Deposits & Retentions” within the group “Payables”.

Should “Payables”, “Interest Bearing Liabilities” and “Provisions” be set out in the same order that they appear in the Statement of Financial Position?

42 Appendix A2 - Note 11 - Statement of Cash Flows”

We submit that provision should be made within the relevant sections of the reconciliation for decreases and increases in equity shares in associates.

We refer to our comments in paragraph 19 on page 5 above, and suggest that the current presentation may be made clearer.



43 Appendix A2 - Note 14 - Conditions over Grants & Contributions

Further to part of our comments in paragraph 38 on page 11 above, we suggest the inclusion of a further section at the foot of this Note disclosing the amounts expected to be expended within 12 months and later than 12 months. This information would have particular applicability to the expenditures of Section 94 contributions.

44 Appendix A2 - Note 19 - Joint Venture

Perhaps this Note should be entitled “Equity Accounted Investments”? In our copy, the withdrawn Note covered pages A242, A243 & A244.

Please note that in our copy, the graphical illustration in Appendix A3 did not print correctly.

45 Appendix A5 - Special Purpose Financial Reports

Our comments relating to each item are similar to the General Purpose Financial Reports and are not repeated here. We understand that the Business Activities of some Councils included equity accounted associates, and recommend that the standard format make appropriate provision as has been done in the GPFs. The line “Other” under Non-Current Liabilities seems to be superfluous.

We doubt the accuracy of the statement in Note 1 that “no other applicable Accounting Standards ...”. Because the SPFRs are usually prepared by modifying information contained in the GPFs, we submit that it would be more accurate to state that all Accounting Standards have been applied except where directed to the contrary.

46 Appendix A7 - Special Schedules

We question the last sentence of the second last paragraph on page A701. We suggest that schedule 1 must also include the net effect of the proceeds and book values on disposals of assets. In our opinion, inclusion of capital purchases would make it impossible to obtain the necessary agreements with the Statement of Financial Performance.

We understand that the totals of the revenues and expenditure columns should be reconcilable to the appropriate amounts shown in the Statement of Financial Performance. A clear statement of the correlations would be an advantage.

47 Appendix A8 - Special Schedule 1

These Schedules are designed to meet the specific purposes of the relevant departments and, being unaware of specific departmental requirements, some of our comments may be inappropriate, for which we apologise.

We have referred above to dispensing with the capital/non-capital revenue split (paragraph 35 on page 9), to the fact that many equity accounted associates are dispensing ordinary Council services which should therefore be disclosed before any surplus/deficit calculation (paragraph 12 on page 3) and seeking clarification for the inclusion of financial assistance grants (paragraph 34 on page 9); all of which would impact on the drafting of this schedule.



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48 Appendix A8 - Special Schedule 7

We recommend that the supply of the schedule be voluntary for the 2000/2001 year, and mandatory from the 2001/2002 financial year.

We submit that many Councils will find it extremely difficult and time consuming to assemble the information in the format required. For example, a Council may have listed all components in their sewerage reticulation system based on the sewer line, and sub-totalled accordingly. This sub-total for a particular line would include pipes, manholes, pump stations & sewerage connections. To assemble the information required, every item will need to be sub-totalled according to type, necessitating the review of every single item.

For a change with the potential workload that is inherent in this new schedule, at least 12 months notice should be given.

We shall be pleased to supply any further information and explanations that you may require.

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