Matters arising from the 2006-16 Long-Term Council Community Plans
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Long-term planning is not new for local authorities. They have been required to prepare long-term financial strategies since 1996, and they are now required to prepare Long-Term Council Community Plans (LTCCPs) under the Local Government Act 2002 (the Act).

The emphasis on long-term planning in the Act\(^1\) reflects the concerns of Parliament and the public that the governing and accountability framework for local government should give it incentives to plan for sustainable long-term service delivery, informed by an understanding of community needs and views.

I am required to audit the LTCCPs under sections 84(4) and 94(1) of the Act. While other countries have adopted long-term planning requirements for local government, auditing the reasonableness of the LTCCP and issuing an audit opinion is unique to New Zealand.

This report outlines the results of, and matters arising from, our audits of Long-Term Council Community Plans (LTCCPs). This includes specific stages of the LTCCP development process, including the LTCCP Statement of Proposal and its Summary (which is used for community consultation) and the final LTCCP adopted by the local authority. My auditors issue audit opinions on the LTCCP Statement of Proposal as well as the final LTCCP.

As preparation of LTCCPs is a relatively new and complex process, there is room for improvement. My report is intended to assist with improvements for the next round of LTCCPs for 2009-19.

I also commissioned an external review by four experts\(^2\) in four areas that are central to preparing an LTCCP – sustainable development, performance information, asset management information, and financial management and strategies.

I considered that this external review would help to stimulate debate in the local government sector about the effect of the requirements to prepare LTCCPs and about the direction of future change to address the requirements and intentions of the legislation relating to LTCCPs.

Planning, preparation, and auditing of LTCCPs

The results of this external review show that, overall, the 2006-16 LTCCPs have improved compared to the 2004-14 LTCCPs.

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1. Section 93(7) of the Act requires an LTCCP to be adopted for a period of not less than 10 consecutive years. In one instance, Kapiti Coast District Council adopted an LTCCP covering 20 years.

2. The reviewers were selected for their knowledge in their specific field of review and of the local government sector.
After the 2006-16 LTCCP audits, my auditors assessed asset management planning against benchmark information collected in 2003. The results show an improvement in the quality of asset management planning.

These results from the external review and our audits show that local authorities are making progress in addressing the intentions as well as the specific content and process requirements of the LTCCP.

Despite these improvements, the expert reviewers concluded that LTCCPs have a significant way to go to become strategic and user-centric planning documents that are a strong expression of the purpose of local government.3

My auditors’ observations support this view of the expert reviewers that there is still a need for improvement. Indeed, a frequent observation made during our audit work was that, while an LTCCP may contain the required statutory content, information was not integrated in a way that gave a clear indication of important issues or the local authority’s strategic direction for these issues.

**Communicating the “right debate” and the LTCCP Summary**

A particular concern was that many LTCCP Statements of Proposal did not appear to encapsulate the “right debate” – they did not focus on the crucial issues facing each local authority and how the authority was addressing these issues.

Further, one of the disappointing features of the 2006-16 LTCCPs was the low priority given to preparing the LTCCP Summary. The Act states that the purpose of the LTCCP Summary is to serve as a basis for general consultation.4

I am aware that the size of an LTCCP and the complexity of the information it covers were the main reasons Parliament provided for the LTCCPs to be audited. The intention was that an audit would provide assurance of the quality of the underlying information and assumptions in the LTCCP, and that the processes for preparing an LTCCP had been complied with. This assurance would, in turn, allow communities to focus on the major matters and choices required – both in the LTCCP Statement of Proposal and its related LTCCP Summary.

Despite this, I note that many LTCCP Summaries were prepared late, almost as an afterthought, and without a focus on the important issues that needed to be addressed – a consequence of not having identified the “right debate” in the first instance.

I am reminded of the comment by a senior manager of one of the local authorities that prepared an LTCCP early in 2003 that, if he had had another month to spend

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3 Section 10 of the Act.
4 Section 89(c) of the Act.
on improving the LTCCP, he would have spent it on the LTCCP Summary. Improving the preparation and presentation of the LTCCP Summary is an important way in which the LTCCP can become more user-centric.

The role of the LTCCP and areas for improvement

I am aware from anecdotal reports that some local authorities perceive a contradiction between the potential roles of an LTCCP as:

- a high-level articulation of strategy; and
- a document to record detailed management intentions.

They view one role as resulting in a strategic plan that would omit the more detailed LTCCP content required by Schedule 10 of the Act, and the other as being simply a work plan that would not need the same amount of community engagement and audit.

My own observation, as a result of conducting the 2006-16 LTCCP audits, is that there is a middle ground between these views. This would be where the LTCCP articulates a local authority’s strategy (informed by both community desires and the reality of the community’s circumstances) and also provides an integrated view of the policies and actions required to support the strategy.

Using this approach, the LTCCP is a process that bridges high-level strategic planning and detailed work planning. Although there were few LTCCPs that ultimately received a qualified audit opinion for being fundamentally unfit for their intended purpose, there are differences in the usability of LTCCPs and the extent to which the “right debate” has been encapsulated (see the Appendix for a summary of our non-standard audit opinions).

My auditors have advised me that more usable LTCCPs tended to result where local authorities embedded the preparation of the LTCCP as a process, rather than treating the LTCCP as a document that was prepared as a one-off compliance exercise.

This is also a view that was reached by our expert reviewers. Their report notes that it generally appeared:

…”that councils focused on complying with the requirements of the Act, and have improved the quality of the underlying information to ensure that they meet audit expectations, but are still at an early stage in effectively using the integrated information to enhance their own decision-making processes and the quality of the planning process for all stakeholders.”
The importance of project management and the sequence for developing information

Local authorities need to better understand the sequence for obtaining and developing information from different parts of the organisation, and the relationship between sets of information. They also need to better understand how to integrate this information through good project management disciplines.

When my auditors began to ask local authorities in mid-2005 about their project management intentions for preparing their LTCCPs, most local authorities had started updating asset management plans. However, my auditors were surprised to find that many had not prepared much of the underlying information on which future planning for asset management is based. This included not identifying and reviewing their relevant policy and strategic objectives, and not reviewing current and intended levels of service.

This concern was confirmed in the period of audit work carried out before the issuing of audit opinions on the LTCCP Statements of Proposal. During this work, my auditors frequently observed that changes to capital expenditure budgets did not result in changes to forecast levels of service, suggesting weak relationships between financial and service performance forecasts for infrastructure assets. In my view, clear understanding is vital in this area of local authority activity.

Many local authorities were therefore preparing asset management forecasts without having formed deliberate objectives in terms of the nature and condition of assets required to deliver the intended services.

In saying this, I am not suggesting that the LTCCP needs to be prepared entirely from a zero base every three years. Rather, what I had expected was that, before starting asset management planning and making financial estimates, local authorities would have completed the community outcomes process and confirmed that their existing information continued to be relevant.

This would have included identifying gaps and areas to update in:
- crucial local authority service strategies and policies;
- revenue, financing, and treasury management policies; and
- current and desired levels of service.

Performance frameworks and financial management strategy need improvement

The development of performance frameworks also clearly needs further work. Indeed, despite the expert reviewers reporting that the performance framework
area showed the strongest improvement from the 2004-14 to the 2006-16 LTCCPs, it is also where the reviewers and my auditors reported the greatest deficiencies in 2006-16 LTCCP Statements of Proposal.

The LTCCP should reflect a local authority’s synthesis of its community feedback and of its policies and strategies, including its financial management strategies, culminating in the prospective financial statements. Through the LTCCP process, financial estimates and implications become the main ingredients to inform decision-making.

Local authorities appear to be more experienced at assembling financial statements than other sets of LTCCP information. However, as is common with the other review areas, there is a range of financial management areas, primarily relating to financial strategy at both a whole-of-council level and at a service level, that we consider requires further development.

In particular, I would emphasise the importance of a local authority explaining the financial prudence of its annual forecast surplus or deficit position in the light of its future service intentions and the funding of these.

This report also provides an analysis of, and comments on, the major financial trends among local authorities. Overall, although the trends highlight an increased use of debt and other revenue as funding sources, rates continue to increase and are forecast to be proportionately higher as a source of funding in 2016 than in 2006.

Long-term management of local authority finances remains a crucial issue. The changes between the draft LTCCP Statements of Proposal and the final adopted LTCCPs pushed rates increases out beyond 2006/07. This indicated that local authorities had a shorter-term focus in financial planning.

The quality of the financial forecasts for the earlier years of the 2006-16 LTCCPs appears to have improved compared to the 2004-14 LTCCPs. However, financial forecasts in the later years of the 2006-16 LTCCPs again show similar weaknesses to the 2004-14 LTCCPs. Investment and cash balances significantly increase in later years, while capital expenditure substantially reduces. This suggests that capital expenditure forecasts may not be complete, and that local authorities need to reconsider whether their current approaches to capital planning remain appropriate.

**Information management must continue to improve**

It is unsurprising that so many in the sector found preparing the 2006-16 LTCCP, including the audit, a challenge. Identifying community outcomes and preparing an LTCCP require cost and effort. However, I have been surprised at the extent of
Auditor-General’s overview

the difficulty reported to me by local government representatives. I have asked why it is so difficult to pull together information that should already exist to support good future planning and management of a local authority’s services. I have been troubled to be frequently told that the information did not exist before a local authority was required to produce the 2006-16 LTCCP.

There is no question that, in the future, there will be changes to local government legislation and to the structure and environment of local government. However, I cannot emphasise enough to those who are the guardians of important resources and services – the management of our waste, water, roading, and community service infrastructure, and our precious environmental resources – how important it is to ensure that they get and maintain quality information so they can perform the role entrusted to them by communities.

My focus for 2009

The combination of project management and sequencing issues, information gaps, and the still developing familiarity of many in the sector with the requirements of the Act produced a result for my auditors that I had not wanted.

In my 2003/04 report to Parliament on the results of local government audits, I reported that the audit of the 2006-16 LTCCPs would focus on systems.7 Initially, we looked at the following systems and controls, to assess whether they produced reasonable information that served the intentions and requirements of the Act, ensured that that information was integrated, and ensured that it was reflected in the LTCCP:

- community outcomes and decision-making processes;
- performance measures and monitoring procedures;
- determining and measuring levels of service;
- identifying and applying assumptions;
- asset management plans;
- information systems and related business processes (in particular, the financial planning processes and financial modelling systems);
- funding and financing policies and accounting policies; and
- project management and monitoring controls over preparing the LTCCP.

However, in many instances, the absence or weaknesses of systems and controls forced my auditors into what I would describe as a “compliance mode”.

By this, I mean that we were obliged to give greater emphasis to successive drafts of LTCCP documents (with my auditors on some occasions seeing as many as 10 drafts) and checking the reasonableness of figures and that content requirements

7 Local Government – Results of the 2003-04 Audits, parliamentary paper B.29[05b], paragraph 3.207.
had been addressed. This style of working created high costs for local authorities and auditors but, more critically, meant that our own work could not always focus as much as I would have wanted on whether the “right debate” had been conducted.

We are carrying out internal work to review our LTCCP audit methodology and will be working with the sector in the lead-up to the 2009-19 LTCCPs to try to help address the issues identified in this report. I would emphasise again that, for our audit work to be more effective, local authorities will need to become more practised at managing the preparation of LTCCPs in the areas I have outlined.

My intention is to revise and re-issue our LTCCP audit methodology, building on our 2006 experience, to enhance our contribution to the preparation of LTCCPs that plan for sustainable long-term service delivery, informed by community needs and views.

Kevin Brady
Controller and Auditor-General
22 June 2007
Part 1
Introduction

1.1 This is our report arising from the audits of the 2006-16 Long-Term Council Community Plans (LTCCPs) prepared by local authorities.

1.2 An LTCCP is a 10-year plan. Section 93(6) of the Local Government Act 2002 (the Act) sets out its purposes, which are to:

• describe the activities of the local authority;
• describe the community outcomes of the local authority’s district or region;
• provide integrated decision-making and co-ordination of the use of the local authority’s resources;
• provide a long-term focus for the decisions and activities of the local authority;
• provide a basis for the local authority to be accountable to the community; and
• provide an opportunity for the public to participate in decision-making processes on activities to be carried out by the local authority.

1.3 There are a number of steps that a local authority must take to meet the requirements of the Act in preparing the LTCCP. These steps include consultation with the community, development of key policies and plans, and putting in place financial strategies and performance measures. Figure 1 outlines the process for preparing an LTCCP.
1.4 Two key documents in the LTCCP process are the LTCCP Statement of Proposal (which includes the draft LTCCP) and the final LTCCP. Local authorities are also required to prepare a Summary of the Statement of Proposal (the LTCCP Summary) for use as a public consultation document.

1.5 Section 84(4) of the Act requires the draft LTCCP to include a report from the Auditor-General. Local authorities are also required to consult with the public on the LTCCP Statement of Proposal using the special consultative procedure outlined in sections 84(1) and 83.
1.6 Section 94(1) requires the final LTCCP (adopted after the local authority has considered the results from the consultation) to include the Auditor-General’s report.

1.7 For both the LTCCP Statement of Proposal and the final LTCCP, the Auditor-General is required to report on:
   • the extent to which statutory requirements have been complied with;
   • the quality of information and assumptions underlying the forecast information provided; and
   • the extent to which the forecast information and proposed performance measures will provide an appropriate framework for the actual levels of service provision to be meaningfully addressed.

1.8 Under the provisions of the Act, all local authorities are required to prepare an LTCCP every three years. The full provisions of the Act on preparing LTCCPs, including their audit, came into effect for the first time for LTCCPs adopted for the period starting 1 July 2006.¹

1.9 The next LTCCP audits will be required in 2009. However, the Auditor-General is also required to report on amendments that are proposed to the LTCCPs during the intervening three years for which the existing LTCCP is in force.

Purpose of this report

1.10 The purpose of this report is:
   • to tell Parliament and the local government sector about matters arising from our audit of local authorities’ LTCCPs; and
   • to provide comparative information on changes in the quality of information in crucial areas since the Act was passed, to allow Parliament and the local government sector to assess the effect of the LTCCP on local authority planning.

Scope of this report

1.11 This report includes:
   • a separate report by external reviewers of the changes between the 2004-14 and 2006-16 LTCCPs in each of the areas of sustainable development, performance information, asset management information, and financial management strategies;
   • an analysis of financial trends and issues in the 2006-16 LTCCPs;
   • an analysis of common issues relating to the preparation of 2006-16 LTCCPs, including the performance management framework, asset management planning, and the financial management framework; and

¹ Local authorities also prepared LTCCPs for the period 2003-14 or 2004-14, which allowed analysis of changes between these and the 2006-16 LTCCPs.
• commentary on our audit opinions on the 2006-16 LTCCP Statements of Proposals and final LTCCPs.

**Our auditing methodology and reporting approach**

1.12 In developing our approach to the LTCCP audits, we aimed to adhere to relevant professional standards and good auditing practice. However, we recognised that preparing an LTCCP requires making informed and reasonable judgements about the future that cannot always be solely supported by facts or evidence.

1.13 We therefore took a flexible approach that attempted to recognise the reality of the context and constraints in which local authorities operate, while allowing for good practice to emerge over time within the general framework of the Act. To this extent, our methodology relied on local authorities applying, as appropriate:

- the requirements and principles of the Act (including the sustainable development principle);
- the requirements of generally accepted accounting practice (GAAP);
- existing sector good practice (for example, National Asset Management Steering Group asset management guidelines); and
- good practice identified in the sector during our audit enquiries.

1.14 Our audit work focused initially on systems because we consider that a local authority’s planning systems are vital to preparing an effective LTCCP. We also doubted whether there would be enough time to complete our audit work once a LTCCP Statement of Proposal had been drafted if we were not able to rely on a local authority’s planning systems.

1.15 We considered that, by focusing on systems rather than on specific decisions or forecast amounts, we would encourage good practice and that, over time, this would give communities greater confidence in the reliability and quality of LTCCPs.

1.16 We wanted our local government sector audit service providers – Audit New Zealand, Deloitte, and Ernst & Young – to achieve maximum consistency in their approach and to minimise the effect of their audit work on local authorities’ time and resources. To achieve this:

- We moved away from competitive contracting for audits to an allocation model. This gave local authorities certainty and consistency in their audit

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2 See section 14(1)(h) of the Act, which states that, in taking a sustainable development approach, a local authority should take into account (i) the social, economic, and cultural well-being of people and communities, and (ii) the need to maintain and enhance the quality of the environment, and (iii) the reasonably foreseeable needs of future generations.

3 The National Asset Management Steering Group is a non-profit industry organisation set up in 1995 to promote asset management by developing best practice guidelines and training.
arrangements and allowed auditors to develop expertise in the field of LTCCP and local government audits.

- We prepared a range of standard audit documentation to provide consistency and minimise duplication of audit work. This applied to our LTCCP audit methodology, as well as standard engagement arrangements and reporting documents. We also provided support and training that was shared among all our auditors.
- We provided several “checkpoints” at which audit work was centrally reviewed to confirm the consistency and fairness of our approach to each local authority.

1.17 We recognise that the LTCCP is a plan and that plans, of necessity, are not based on information that is certain. Therefore, we were not seeking to second-guess the financial and performance estimates provided by local authorities. Rather, we were seeking confidence that estimates were reasonably based.

1.18 We expected that both the draft and final LTCCPs would be based on a local authority’s best available information and best estimates. This would provide a good basis for consultation and decision-making during the preparation of the LTCCP and for subsequent decision-making and accountability to the community.

1.19 Our major focus was on the LTCCP Statement of Proposal, as this is the most important document for public consultation. Our interest in the final adopted LTCCP was primarily to ensure that changes (made through consultation) and final decisions had been appropriately reflected.

1.20 Figure 2 sets out our audit approach, which was based on the International Standard on Assurance Engagements (ISAE 3000) and adapted as appropriate to reflect the intentions and specific requirements of the Act. A full diagram of this methodology and an outline of our approach are available on our website at www.oag.govt.nz.
Part 1 Introduction

Figure 2
Summary of our LTCCP audit approach

PRELIMINARY PLANNING AND RISK IDENTIFICATION

Understand the local authority’s business environment and the LTCCP development process, including the local authority’s self-assessment of consultation, outcomes, decision-making, governance, and performance management. *

Commence assessment of the local authority’s approach to:
• significant assumptions;
• accounting policies; and
• prudent financial management and balanced budget.

Understand, document, and assess control risks in the internal control environment for the financial and performance planning systems and processes to be applied in the preparation of the LTCCP.

Perform preliminary analytical review procedures of available information to help identify unexpected balances and relationships.

Determine planning materiality.

DEVELOP THE AUDIT PLAN

Perform risk assessment and assess the reliance that can be placed on the local authority’s controls, focusing on:
• significant account balances;
• groups of activities; and
• disclosures.

Where controls cannot be relied on, plan level of substantive tests to address risks.

Where controls can be relied on, identify the controls that mitigate risk and plan substantive tests to address residual risk.

Summarise and communicate the audit plan.

PERFORM THE AUDIT PLAN

Perform tests of controls and substantive tests, and evaluate results.

Complete review of:
• the local authority’s self-assessment,
• significant assumptions;
• accounting policies; and
• prudent financial management and balanced budget.

Review:
• groups of activities;
• council-controlled organisations;
• funding impact statement;
• LTCCP Statement of Proposal content and integration; and
• summary report.

CONCLUDE AND REPORT ON THE LTCCP STATEMENT OF PROPOSAL

* The self-assessment was an audit tool developed for local authorities to describe and analyse their processes and controls in the described areas.
Part 2

Summary of the report of expert reviewers on changes in LTCCPs

2.1 In this Part, we present a summary of an external review we commissioned of the changes between the 2004-14 and 2006-16 LTCCPs.

2.2 We considered that this external review would help to stimulate debate in the local government sector about the effect of the requirements to prepare LTCCPs and about the direction of future change to address the requirements and intentions of the legislation relating to LTCCPs.

2.3 The review was carried out by four expert reviewers with experience in specialist fields as well as overall local government experience and expertise. They were:
   - Leanne Holdsworth, Director, Holistic Business Solutions Ltd;
   - Robyn Wells, Research and Assurance Specialist, Audit New Zealand;
   - Malcolm Morrison, Director, Morrison Low & Associates Ltd; and
   - Kevin Simpkins, Director, Kevin Simpkins Advisory Services Limited.

2.4 We asked them to review a selection of LTCCPs to identify changes that may be discernible to users of LTCCPs (being either improvements or deteriorations) between each selected local authority’s 2004-14 LTCCP and its 2006-16 LTCCP. We also asked the reviewers to use this work to make recommendations for future improvements.

2.5 The review was carried out on the understanding that the reviewers’ findings and recommendations would be included in a report to Parliament, be used to inform our advice in the context of any review of the legislation, and enhance the audits of LTCCPs in 2009 and subsequent years.

2.6 We asked the reviewers, when seeking to identify changes that may be discernible to the users of LTCCPs, to take the perspective of moderately interested and informed individuals and groups, such as media commentators, academics and analysts, members of relevant professional disciplines working with local authorities, and community groups such as ratepayer groups and associations.

Scope of the review

2.7 The review involved 30 final adopted LTCCP documents, comprising the 2006-16 LTCCP and the immediately preceding LTCCP for each of 15 local authorities. Of these 15, three pairs of LTCCP documents were reviewed in common by all four reviewers and three additional pairs of LTCCP documents were reviewed by each reviewer.

2.8 We requested the reviewers to focus their individual reviews in their particular fields of expertise:
Part 2 Summary of the report of expert reviewers on changes in LTCCPs

• sustainable development;
• performance information;
• asset management information; and
• financial management and strategies.

2.9 We also requested the reviewers to take account of:
• the statutory purpose of the LTCCP (outlined in section 93(6) of the Act); and
• the need to consider their individual fields of expertise within the context of the whole LTCCP document.

2.10 The 15 local authorities selected for review represent a spread of local authorities of different size and scale:
• Gore District Council;
• Environment Canterbury;
• Hauraki District Council;
• Kapiti Coast District Council;
• Mackenzie District Council;
• New Plymouth District Council;
• North Shore City Council;
• Queenstown Lakes District Council;
• Rotorua District Council;
• South Taranaki District Council;
• South Wairarapa District Council;
• Stratford District Council;
• Tasman District Council;
• Thames-Coromandel District Council; and
• Wellington City Council.

2.11 The expert reviewers’ summary and four individual reports are provided in a separate report attached to this report. The reports are:
• “Reviewer’s Report 1: Sustainable development – findings and recommendations”, by Leanne Holdsworth;
• “Reviewer’s Report 2: Performance information – findings and recommendations”, by Robyn Wells;
• “Reviewer’s Report 3: Asset management information – findings and recommendations”, by Malcolm Morrison; and
Report of expert reviewers – summary

Our reviews have been based solely on each final adopted LTCCP, and we have not considered the systems and information which underlie the LTCCPs. Specifically, we have assumed that the underlying financial and asset information in the LTCCP itself is consistent with planned levels of service, and we have not considered any other documents referred to in the LTCCPs (such as detailed asset management plans).

Limitations of the review

The scope of this review results in certain limitations in the findings and recommendations we have made. Specifically each reviewer’s findings are based solely on the 12 LTCCPs they have reviewed and, in particular, on comparisons between the 2004-14 and 2006-16 LTCCPs of the local authorities selected. Care therefore needs to be taken in extrapolating our findings across other local authorities.

Reviewers’ recommendations are based on the review they have undertaken, although they have also taken account of other knowledge they have about LTCCPs generally and about the accountability and reporting environment of local authorities in seeking to make appropriate recommendations. Our review does not include any assessment of the actual level of assets and services provided by the council, but focuses on the information disclosed about the activities provided by the council in the LTCCPs.

Approaches, findings, and recommendations

We report separately about each of the particular fields of expertise – sustainable development, performance information, asset management information, and financial management and strategy. Within each review report, our approaches, findings, and the recommendations arising from our reviews are set out in five parts:

- Approach taken by the reviewer.
- An assessment of the change (either improvement or deterioration) between the 2004-14 and 2006-16 LTCCPs based on the review of the six councils selected.
- Observations on patterns discernible in relation to how well the information is presented over the six councils reviewed (such as whether the presentation and quality changes with size and scale of council).
- Observations on the overall state of the information in 2006-16 LTCCPs, including strengths and weaknesses, and suggestions as to where future improvement work would best be focused.
- Issues in relation to the legislation applicable to LTCCPs.

Summary of key findings and recommendations from all reviews

In this summary, we outline common and main findings from each of our reviews in respect of the change (either improvement or deterioration) between the 2004-14 and 2006-16 LTCCPs, patterns discernible in relation to how well the information is presented, the overall state of the information in 2006-16 LTCCPs, and suggestions for future improvement work.

Overall, there are discernible improvements between the 2004-14 and 2006-16 LTCCPs, although the extent of the improvement and the number of councils showing improvement vary across the areas reviewed and, within these, across the matters considered by each reviewer.

Despite these improvements, in our view LTCCPs have a significant way to go to move from compliance-focused documents that set out the contents required by statute to strategic and user-centric planning documents that are a strong expression of the purpose of local government (as set out in section 10 of the Act).
It may be that councils have focused on complying with the requirements of the Act and have improved the quality of the underlying information, but are still at an early stage in effectively using the integrated information to enhance their own decision-making processes and the quality of the planning process for all stakeholders. There is the capacity to significantly improve the integrated “story” about the challenges, options, and the long-term plans of the council. We encourage local authorities to view the legislative requirements as the starting point to be addressed within a wider more strategic integrated context.

Sustainable development

Overall, there has been improvement in the adequacy and presentation of information about sustainable development and community outcomes between the reviewed 2004-14 and 2006-16 LTCCPs. However, the review of the LTCCPs showed that:

- the relationship between well-beings, community outcomes, and sustainable development within LTCCPs is often not clear, and there is limited evidence within current LTCCPs of sustainable development infusing the thinking of local authorities; and
- there appears to be uneven understanding of the scope of sustainable development.

While improvements were more readily identified in larger councils, improvements are more closely related to the timing of a community outcomes process. Large councils were found to have undertaken a community outcomes process more recently.

While all councils refer to the four well-beings (social, economic, environmental, and cultural) in their LTCCPs, to a greater or lesser extent there are a number of areas requiring improvement to infuse council thinking on sustainable development into LTCCPs:

- expressing how sustainable development is localised, owned, and defined at a council and community level;
- ensuring that community outcomes are expressed at a level of specificity that is meaningful, and that it is clear how the council contributes to the outcomes;
- reflecting consideration given to the needs of future generations’ well-being in decision making;
- integrating thinking (across the well-beings) to express how activities (including the means by which they are delivered) satisfy the four elements of the section 14 sustainable development principle;*
- using the sustainable development principle and the community outcomes as a framework for performance planning and management;
- using a current and future wellbeing context to address statutory content areas, such as assumptions and negative effects, as well as to develop information about intended benefits and associated risks and key issues; and
- “walking the talk” in outlining how sustainable development relates to councils’ internal functioning.

A stronger articulation of sustainable development and how it relates to and affects the intentions and operations of councils would be required to in turn improve the usefulness of LTCCPs both as a public articulation of strategy and objectives and as a management framework for councils.

* Section 14(1)(h) of the Act, principles relating to local authorities, states that:

1. In performing its role, a local authority must act in accordance with the following principles: ...
2. In taking a sustainable development approach, a local authority should take into account —
   (i) the social, economic, and cultural well-being of people and communities; and
   (ii) the need to maintain and enhance the quality of the environment; and
   (iii) the reasonably foreseeable needs of future generations.
Part 2 Summary of the report of expert reviewers on changes in LTCCPs

Performance information

We found that there was a discernible improvement in the performance framework in the 2006-16 LTCCPs for all the councils, from a 2004 baseline that required significant improvement. There was no consistent pattern, but the main improvements related to:

- specification and completeness of the performance measures;
- provision of more background narrative to support the levels of service and performance measures;
- direct connection of the levels of service and performance measures; and
- specification of performance measures for the full 10-year period.

Larger councils tended to have more complete and sophisticated performance frameworks and information. Therefore there was less improvement in performance frameworks for larger councils compared to medium and small, as the larger councils started from a stronger base.

However, there were examples of good practice spread across all councils and also room for improvement across all councils.

Overall, we found that there was room for improvement in how well the LTCCP expressed the council’s strategic focus and how it flowed through to its activity statements, including the performance information. We consider that there is real scope for development in the performance information, particularly in further connecting the objectives, levels of service and performance measures with a clear context of the “big picture”, including:

- clear articulation within the activity statements of the planned levels of service and performance measures relative to previous years;
- an appropriate focus on levels of service and performance measures to provide a meaningful picture of key aspects of the activity; and
- appropriate and relevant performance measures that include at least some indication of the intended impacts of planned services. We note that it is the quality of performance measures that matters, not the quantity (that is, how the performance measures work individually and, more importantly, in combination).

Asset management information

Councils have made some improvements from the first LTCCP information, by expanding the detail of the information. For example, while 2004-14 LTCCPs tended to focus on key infrastructure assets, in the 2006-16 versions, other community assets such as parks, halls, and libraries were analysed to a similar extent as network infrastructure assets. However, the focus continues to be on the management of the currently held assets, rather than planning for the next 10 years for new assets.

Overall, the medium-sized councils provided the most useful information and could identify changes to existing or new assets and the rationale for the changes. While generally larger city councils produced larger LTCCPs for 2006-16 than did small and medium-sized councils, these plans contained a lot of detailed asset information that did not always link into other parts of the LTCCP.

Users, as defined for the purposes of this review, are not yet provided a transparent and complete assessment of the planning decisions used to determine the current and future services and asset requirements. In particular, the following areas were not well covered by any of the LTCCPs that we reviewed:

- The Act’s Schedule 10 requirement that group of activities information outlines the additional capacity requirements, how the capacity will be delivered, and a discussion on the options considered.
- Defining the future service level and capacity, and the linkage of the service level and capacity with the identified capital projects and ongoing expenditure.
Financial management and strategies

The forecast financial statements, accounting policies, and significant forecasting assumptions are all strong aspects of the 2006-16 LTCCPs. The funding impact statements are reasonable, as are most of the funding and financial policies examined.

However, there are two areas where improvement work would have the greatest capacity to enhance the value of the LTCCPs for users – explanation of the overall fiscal strategy, and enhancing the quality of the financial information about groups of activities.

How councils have addressed the balanced budget requirement is a demonstration of the weaknesses in articulating fiscal strategy, in that councils have not provided further comment where the operating revenues exceed the operating expenses. That is, where the balanced budget test has been met at a whole-of-council level, councils have not discussed whether the surplus is prudent or not.

The financial information about groups of activities represents an opportunity for a sector-wide effort to improve consistency in the manner of presentation of this information, as well as to improve the clarity of the information and the underlying logic. Separation of operating expenses from capital expenditure in the 2006-16 LTCCPs has led to some improvement. However, the funding part of these statements remains weak. In fact, the divergent underlying logic of funding approaches (including the confusion of real financial resources with accounting balances in some cases), and the terminology used by many councils, makes it very difficult for even an informed reader to understand the information.

Based on the selected local authorities, it appears that, in general, the larger the authority the better the information which has been presented. However, this observation is not valid across all of the financial management and strategy aspects examined in this review.
Part 3
Trends, issues, and observations from the 2006-16 LTCCPs

3.1 In this Part, we discuss our analysis of the main financial trends projected in the 2006-16 LTCCPs. This includes:
• the effect of including price change in the 2006-16 LTCCPs;
• analysing forecasts made in the 2006-16 LTCCPs;
• comparing the 2006-16 LTCCP Statements of Proposal to the final LTCCPs;
• comparing the 2004-14 LTCCPs to the 2006-16 LTCCPs; and
• our conclusions.

3.2 LTCCPs include forecast financial statements for the next 10 years. These are forecasts only and therefore will differ from the actual financial results achieved in those years. However, in aggregate, the forecasts provide a useful picture of the size of, and trends occurring in, local government finances and their implications for planning. Given our role, we were in an ideal position to aggregate this information to provide a snapshot of the future from the combined LTCCPs.

3.3 We note that there is scope for further substantial and detailed analysis of this information. This Part seeks only to highlight the main trends, issues, and observations about LTCCPs.

3.4 For our analysis, we collated local authorities’ financial data from:
• 2004-14 final LTCCPs\(^1\) (sourced from the Treasury);
• 2006-16 LTCCP Statements of Proposal issued for consultation;
• 2006-16 final LTCCPs; and
• 2005/06 annual plans.

The effect of including price change in the 2006-16 LTCCPs

3.5 When reviewing the financial information included in the 2006-16 LTCCPs, readers need to consider the effect of price change,\(^2\) which estimates the real increase in the cost of local authorities’ operations during the planning period and which will also have a real effect on rating levels.

3.6 Financial Reporting Standard 42: Prospective Financial Statements (FRS-42) requires prospective financial information and the assumptions used to prepare it to be based on the best and reasonable information available to the entity. The assumptions and resulting information must be reasonable and supportable.

\(^1\) Seventy-seven local authorities completed 2004-14 LTCCPs, and all 85 local authorities completed the 2006-16 LTCCPs.

\(^2\) Generally, the term “price change” or “cost change” is used interchangeably with “inflation”. It is important to note that it is an assumption of future price change at rates specific to the individual local authority. This often is different from the rate known as the Consumer Price Index (CPI). For further discussion about price change, see paragraphs 3.64-3.67.
Local authorities prepared the financial projections included in the 2004-14 LTCCPs on the assumption that the value of money would not change over time. Under FRS-42, this assumption was considered unsupportable as historical evidence and current forecasts suggested that cost increases were probable in the future. Local authorities were therefore required to include price change in their financial projections in the 2006-16 LTCCPs to meet the reasonable and supportable test in FRS-42.

To help local authorities prepare their 2006-16 forecasts, the Society of Local Government Managers (SOLGM) engaged the Bureau of Economic Research Limited (BERL) to provide a forecast of probable price change for the 10 years covered by the LTCCP. As an example, the cumulative effect of BERL’s indices suggested that staffing costs would be 19.5% higher in 2016 than in 2006, and water activity costs would be 35% higher.

Local authorities generally used the BERL forecasts to prepare their financial information. Some used their own forecasts of price change. Irrespective of the source of the price change assumptions, including price change had a substantial effect on the financial forecasts in the 2006-16 LTCCPs.

FRS-42 also requires local authorities to apply their accounting policies to the financial forecasts. Because of this requirement and the assumption that prices change over time, local authorities were required to forecast the change in asset values and resulting depreciation from the periodic revaluation of property, plant, and equipment, such as land and buildings, roads, water, and stormwater and wastewater infrastructure assets.

While revaluations substantially affect the Statement of Financial Position, the most significant implication is for depreciation. Depreciation represents the extent to which the service potential of a local authority’s assets has been consumed. The balanced budget test in section 100 of the Act requires that operating revenues be set to cover operating expenses, which includes asset consumption represented by depreciation.3

Revaluing assets results in a depreciation figure based on current replacement costs rather than historic costs. In an inflationary environment, this results in increases in depreciation expenses.

If assets are not revalued, depreciation is calculated on a historic cost basis, and it is arguable that the current community does not pay the full cost of the consumption of the asset. This approach leaves a significant shortfall that a later generation must fund when the asset requires replacement.

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3 See paragraphs 7.18-7.25 for further discussion of the balanced budget requirement.
Analysis of forecasts made in the 2006-16 LTCCPs

3.14 The 2006-16 LTCCPs forecast a substantial increase in cumulative local authority size by 2016. The main financial forecasts are:

- Rates increase from $3,100 million in 2006 to $5,300 million in 2016 (up 71%).
- Local authority surpluses double from $667 million in 2006 to $1,300 million in 2016. Cumulatively, surpluses total $12,000 million during the 2006-16 period.
- Overall, equity increases by more than 40% to $101,000 million.
- Local authorities’ investment in property, plant, and equipment increases to $98,000 million in 2016, up from the $56,000 million estimated in 2005/06 annual plans.
- Public debt increases from $3,200 million estimated in the 2005/06 annual plans to $8,200 million (up 154%) in 2016 forecast in the LTCCPs.
- Capital expenditure of $29,500 million for the 10 years of the LTCCPs.
- Local authority cash investments (including bank balances) increase by $900 million during the 10 years of the LTCCPs.

Operating expenditure

3.15 Figure 3 shows that operating expenditure is forecast to increase by 44% overall. The overall increase in operating revenues (including rates) is 82% (see Figure 4).

4 The 2006 information was collated from the 2005/06 annual plans of all local authorities. The 2006-16 LTCCPs were not required to include comparative information for the 2006 year, so this was not included in many instances.

5 Balances for equity and property, plant, and equipment are both affected by the revaluation of property, plant, and equipment.

6 Overall, investments are estimated to increase by $3,400 million compared to the 2005/06 annual plans. However, this includes Manukau City Council’s reclassification of property, plant, and equipment to investments, and changes in investment values (including revaluations made by other local authorities between the publication of their annual plan and their LTCCP) that affect this figure.
Part 3  Trends, issues, and observations from the 2006-16 LTCCPs

Figure 3
Forecast operating expenditure from 2006 to 2016

<table>
<thead>
<tr>
<th>Year</th>
<th>Interest expense</th>
<th>Depreciation</th>
<th>Other operating expenses</th>
</tr>
</thead>
<tbody>
<tr>
<td>2006</td>
<td>2000</td>
<td>5000</td>
<td>3000</td>
</tr>
<tr>
<td>2007</td>
<td>2100</td>
<td>5500</td>
<td>3500</td>
</tr>
<tr>
<td>2008</td>
<td>2300</td>
<td>6000</td>
<td>4000</td>
</tr>
<tr>
<td>2009</td>
<td>2500</td>
<td>6500</td>
<td>4500</td>
</tr>
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<td>2010</td>
<td>2700</td>
<td>7000</td>
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</tr>
<tr>
<td>2011</td>
<td>2900</td>
<td>7500</td>
<td>5500</td>
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<td>2012</td>
<td>3100</td>
<td>8000</td>
<td>6000</td>
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<tr>
<td>2013</td>
<td>3300</td>
<td>8500</td>
<td>6500</td>
</tr>
<tr>
<td>2014</td>
<td>3500</td>
<td>9000</td>
<td>7000</td>
</tr>
<tr>
<td>2015</td>
<td>3700</td>
<td>9500</td>
<td>7500</td>
</tr>
<tr>
<td>2016</td>
<td>3900</td>
<td>10000</td>
<td>8000</td>
</tr>
</tbody>
</table>

Note: The 2006 amount comes from 2005/06 annual plans.

3.16 By component, other operating expenses are forecast to increase by 30%, depreciation by 113%, and interest expense by 327%.

3.17 Depreciation more than doubles as a result of revaluations and asset additions during the 10 years covered by the LTCCPs.

3.18 Interest expense is forecast to increase substantially as local authorities take on more debt to finance the purchase of assets. The interest increase appears disproportionate to the increase in debt, but this is because of the significant increase in debt in the early years of the LTCCPs.

Operating revenues

3.19 The 2006-16 LTCCPs forecast a substantial increase in rates and an increasing use of some of the other funding sources available to local authorities. For example, development contributions revenue (used to finance growth-related capital expenditure) is forecast to nearly double from $216 million in 2006 to $423 million in 2016.

3.20 While, on average, development contributions are expected to form about 5% of revenue for the overall sector, they represent up to 20% of all revenues for local authorities in high growth areas.
3.21 Despite increases from other revenue sources during the 10 years covered by the LTCCPs, rates are anticipated to increase by 6% relative to other operating revenue sources – that is, from 53% to 59% of all operating revenue. Figure 4 summarises the forecast operating revenues from the 2006-16 LTCCPs.

**Figure 4**
Forecast operating revenues from 2006 to 2016

Note: User-pays charges are included as “other revenue”. The 2006 amount comes from 2005/06 annual plans.

3.22 The proportionate increase in rates revenues may reflect that rates are a primary funding source for capital expenditure as well as operating expenditure. This increases the sensitivity of rating figures to increases in size and cost (including price change) within the operating and capital expenditure programmes.

3.23 It should also be noted that the sizeable “other revenue” stream, which is primarily user-pays charges, is typically linked to operating expenditure and not capital expenditure (for example, resource consent charges). On the other hand, to meet critical non-financial objectives in providing a service (for example, libraries or other sporting, leisure, or cultural facilities), “other revenue” might not be set to recover total operating costs, including depreciation. This may contribute to rates increasing proportionately more than other revenue sources.

3.24 It is also possible that there may be an element of conservatism in the forecasts for “other revenue” streams, or that local authorities have given limited
consideration to the appropriateness of non-rates revenue requirements in the later years of the LTCCP given the cost increases forecast.

**Surpluses**

3.25 The total of the surpluses forecast in local authorities’ 2005/06 annual plans was $667 million. The total forecast surplus is $883 million for 2006/07, the first year of the LTCCP, and exceeds $1,000 million for both 2007/08 and 2008/09. After that, the total surpluses forecast by the sector drop below $1,200 million only once in the seven remaining years of the LTCCP.

3.26 Figure 5 shows that the surpluses forecast in the first three years of the LTCCPs are comparatively lower than the remaining years of the plans.

**Figure 5**
Forecast surpluses from 2006 to 2016

Note: The 2006 amount comes from 2005/06 annual plans.

3.27 Analysing the surpluses further, fewer than 10% of local authorities had surpluses that generally decreased during the 10 years covered by the LTCCPs. The majority of local authorities forecast surplus levels that were generally constant between years or that increased during the 10 years of the plan.\(^7\)

**Capital expenditure and non-rate financing mechanisms**

3.28 To understand the overall local authority financial forecasts in the LTCCP, operating revenues and surpluses should not be viewed in isolation. Surpluses include non-cash items, such as vested assets. They also include revenue sources – such as development and financial contributions, some grants and subsidies, and (in some instances) rates – that are to be used to purchase capital items. In addition, local

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\(^7\) For further discussion about surpluses, particularly in relation to the balanced budget concept and prudent financial management, see Part 7.
Part 3  Trends, issues, and observations from the 2006-16 LTCCPs

authorities need to consider using other funding sources – such as debt, reserves, and investments or cash balances – to fund capital expenditure.

3.29 The LTCCPs forecast a total of $29,500 million of capital expenditure for the 2006-16 period. There is a marked decrease in capital expenditure forecast for the later years of the plan. Figure 6 shows the capital expenditure forecast for each year of that period.

Figure 6
Forecast capital expenditure from 2006 to 2016

Note: The 2006 amount comes from 2005/06 annual plans.

3.30 The 2006-16 LTCCPs forecast an increase in the use of external debt to fund capital expenditure. The net movement in debt shown in the Statements of Financial Position is $5,000 million. Of the overall increase in debt, Auckland City Council accounts for $1,200 million.

3.31 External debt levels are forecast to increase in the early years of the LTCCPs, with net local authority external debt increasing by more than $1,000 million a year for the three years from 2007 to 2009 and then levelling out. External debt decreases in the later years of the LTCCPs.

3.32 Typically, the increased use of debt went hand in hand with increased surpluses, which is not unexpected given that both are used to finance capital expenditure. The increased surpluses and debt were especially prevalent in larger city and district councils.

3.33 Of the nine local authorities that showed no or minimal debt balances (less than $300,000) in their LTCCPs, six had forecast reasonably constant and relatively small surpluses. Of those local authorities, two were regional councils and four were small district councils. Figure 7 shows forecast external debt from 2006 to 2016.

8 The cumulative cash flows indicate net borrowing of $5,500 million. It is likely that this is because the 2006 comparative information used to prepare the LTCCPs differed from the 2005/06 annual plan debt figures.
3.34 Many local authorities include a threshold of interest expense as a proportion of rates revenue or total revenue within their liability management policy. These thresholds provide a boundary within which local authorities manage their debt levels – in this instance, by determining the level of debt-servicing costs that the local authority is willing to incur.

3.35 Interest expense was forecast to increase from 7.0% to 11.2% as a proportion of rates and to increase from 3.6% to 6.6% as a proportion of total revenue.9

3.36 However, overall, debt remains at a relatively modest level considering the level of investments and cash held. During each year of the 2006-16 LTCCPs, investments and cash exceed the level of external debt forecast. At the end of the LTCCP period, local authority investments – including cash – are forecast to exceed debt by $1,500 million (investments and cash are forecast to be $9,700 million).

Overall funding – Statement of Cash Flows

3.37 The Statement of Cash Flows reflects the cumulative effect of local authority funding decisions and therefore the use of surpluses.

3.38 Figure 8 shows the cumulative local authority funding forecast in the 2006-16 LTCCPs.

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9 It is important to note that this is from an analysis of external debt only and does not reflect local authorities’ internal debt programmes, in which funds are lent between activities. The receiving activity is charged interest, which is recovered from that activity’s revenues. This practice efficiently uses cash balances to avoid incurring external financing costs.
3.39 Figure 8 shows that about 81% of the capital expenditure included in LTCCPs is funded from operating cash flows and asset sales, and 19% is funded from external debt. It also shows that, by the end of 2016, the local government sector will have increased its cash and cash investments by $900 million.

3.40 It should be noted that operating cash flows include development contributions and capital-expenditure-related Land Transport New Zealand subsidies. However, as noted earlier, development contributions amount to only 5% or $3,700 million of forecast revenue in the LTCCPs. Even if all development contributions revenue was excluded from local authority surpluses, there would be a remaining surplus of $8,300 million.

3.41 Analysed on a year-by-year basis, the cash flow information reflects an even more dramatic picture. Figure 9 shows that, in the early years of the LTCCPs, local authorities are funding a significantly higher proportion of their proposed capital programmes from debt and are also using investments and bank balances. In later years, investment and bank balances increase annually and the proportion of debt used as a funding source decreases. Local authorities forecast that, in 2015, they will have enough cash surpluses to cover capital expenditure for the year, repay a portion of debt, and also increase bank and investment balances.
3.42 In analysing net capital expenditure, it would have been desirable to know what portion of capital expenditure was attributable to renewals expenditure. Renewals costs are often paid from funded revenue and are set to cover non-cash expenses such as depreciation – the excess cash resulting from a “balanced budget”\textsuperscript{10} position – with new capital financed by surpluses, reserves, and debt. Nevertheless, forecasts for the later years suggest that all capital expenditure could be financed from operations (that is, surpluses and funded depreciation) regardless of its nature. Local authorities need to consider the intergenerational equity (each generation paying its own way) of such an approach.

**Overall summary**

3.43 The 2006-16 LTCCPs reflect an increased use of other funding sources, such as development contributions, and intergenerational funding sources, such as debt. However, the forecast rates and operating surpluses continue to increase at significantly higher levels than overall operating costs. There is no clear reason for rates and surpluses of this level. This reflects our broader concern that the financial strategies of local authorities are not necessarily apparent.

3.44 Although debt increases, the levels of debt held by local authorities remain relatively small compared with their asset base, especially considering that investments and cash are forecast to exceed debt in each year of the LTCCP.

3.45 The forecasts reveal a marked change in funding strategies in different years of the LTCCPs. In the first three years, debt funds at least 36% of total capital expenditure. In the later years, the percentage of debt funding decreases substantially, to the extent that it is being repaid rather than borrowed. The rationale for the change in approach – that is, funding capital expenditure from operating cash flows (surpluses and funded depreciation) rather than debt – is unclear.

3.46 The overall position is that 81% of the capital in the LTCCPs is funded from operating sources. This suggests that the costs of new assets, which have benefits over a long term, are being funded by current revenues. This raises questions about the intergenerational equity of the adopted funding approach.
3.47 Given the points identified above, the situation warrants further analysis. Each local authority needs to consider whether its LTCCP adequately reflects its financial strategies, including the rationale for the proposed levels of rates increases and surpluses – in particular, for the later years of the plan.

Comparing the 2006-16 LTCCP Statements of Proposal to the final LTCCPs

3.48 We compared the financial forecasts in the 2006-16 LTCCP Statements of Proposal with the final LTCCPs to see the nature of changes made after the draft plan had been subject to public consultation. This would highlight the effect of decisions made by local authorities between publication of the LTCCP Statements of Proposal and the final LTCCPs.

3.49 The changes occurring to the 2006/07 year’s forecasts in the Statements of Financial Performance between the LTCCP Statements of Proposal and the final LTCCPs were:

- rates decreased by $51 million (down 1.7%);^11
- other income increased by $53 million (up 3.6%);
- development contributions, interest, and vested assets increased by $16 million;
- subsidies increased by $27 million (up 3.8%);
- total operating expenditure (including depreciation and interest) increased by $58 million (up 1.1%); and
- the cumulative operating surplus decreased by $15 million (down 1.7%).

3.50 It is unclear why local authorities collectively believed that more “other revenue” would be available after consultation than before consultation (“other revenue” excludes interest, subsidies, and development contributions). This is an area that requires further consideration when we review LTCCP Statements of Proposal in future years.

3.51 The changes occurring to the 2006/07 forecasts in the Statements of Financial Position between the LTCCP Statements of Proposal and the final LTCCPs were:

- property, plant, and equipment (including infrastructure) increased by $57 million;
- investments decreased by $77 million (down 1.1%); and
- debt increased by $41.6 million (up 1.2%).

3.52 In Figure 10, we isolate Auckland City Council forecasts from the changes made by other local authorities between the LTCCP Statements of Proposal and the final

^11 If Auckland City Council is excluded, rates in the remaining 84 local authorities’ final LTCCPs were 2.1% lower than those in the LTCCP Statements of Proposal.
LTCCPs. This is because the council’s LTCCP Statement of Proposal included various options for consultation that had significant effects on the proposed capital programme and resulting funding sources, including rates and debt. The option adopted by Auckland City Council for its final LTCCP was a capital expenditure and operating programme of 29 projects at a cost of $2,200 million over the 10 years.

3.53 Although the changes noted in paragraph 3.52 were relatively insignificant in the 2007 year, the Auckland City Council’s LTCCP showed that, by 2016, rates were $171 million more than in the LTCCP Statement of Proposal. In addition, the surplus was up $85 million, assets increased by $2,200 million, and debt rose by $1,200 million. Changes of this size need to be excluded to highlight the changes for the other 84 local authorities.

**Figure 10**

Changes to the 2016 year of the 2006-16 LTCCPs after consultation on the draft LTCCP Statements of Proposal and over the term of the LTCCPs

<table>
<thead>
<tr>
<th></th>
<th>2016 Including Auckland City Council</th>
<th>2016 Excluding Auckland City Council</th>
<th>2006-16 Including Auckland City Council</th>
<th>2006-16 Excluding Auckland City Council</th>
</tr>
</thead>
<tbody>
<tr>
<td>Rates</td>
<td>$105m 2.0%</td>
<td>($66m) 1.4%</td>
<td>$202m 0.5%</td>
<td>($592m) 1.5%</td>
</tr>
<tr>
<td>Other income</td>
<td>$119m 6.4%</td>
<td>$81m 4.8%</td>
<td>$822m 4.8%</td>
<td>$669m 4.3%</td>
</tr>
<tr>
<td>Total operating expenditure</td>
<td>$286m 3.8%</td>
<td>$91m 1.3%</td>
<td>$1,600m 2.5%</td>
<td>$626m 1.0%</td>
</tr>
<tr>
<td>Change in operating surplus</td>
<td>$38m 2.9%</td>
<td>($47m) 4.1%</td>
<td>$841m 7.6%</td>
<td>($61m) 0.6%</td>
</tr>
<tr>
<td>Property, plant, and equipment (including infrastructure assets)</td>
<td>$3,005m 3.1%</td>
<td>$781m 0.9%</td>
<td>N/A</td>
<td>N/A</td>
</tr>
<tr>
<td>External debt</td>
<td>$1,840m 29.0%</td>
<td>$617m 9.9%</td>
<td>N/A</td>
<td>N/A</td>
</tr>
</tbody>
</table>

3.54 Excluding Auckland City Council, the 2016 year information and the cumulative information continues a trend established from the changes to the 2007 information, of an overall lower level of rating offset by increased operating revenues and more infrastructure assets financed by external debt.
Our analysis

3.55 The changes made by local authorities after consultation on the LTCCP Statements of Proposal indicated a focus primarily on the first year of the plan, with the remaining years of the LTCCPs reflecting this trend – that is, lower rates combined with more use of other revenue sources and debt to fund an increased level of asset investment.

3.56 In the context of the overall sector, the changes for the 84 local authorities (that is, excluding Auckland City Council) are individually relatively insignificant. What is interesting to note is that the changes resulted in more operating and capital expenditure, while rates were also reduced.

3.57 A review of the changes between the LTCCP Statements of Proposal and the final LTCCPs suggests that the majority of the changes were made in the first year of the plans, with only minor changes made in later years.

3.58 In addition to reducing the overall amount of rates sought, the changes made to rates in 2006/07 lowered the percentage increase in rates for that year from 8.0% to 6.3% (8.1% to 6.0% if Auckland City Council is excluded). The forecast increase in rates for 2008 increased from 8.3% to 8.8% (8.5% to 8.8% excluding Auckland City Council), and a similar small percentage increase was forecast for future years.

3.59 The percentage increase in rates is a typical area of focus for local authorities and ratepayers. The decrease in the first year and no percentage decreases in subsequent years may be the result of taking a short-term view on the LTCCPs. However, this cannot be said with any certainty.

3.60 We will be interested to see whether local authorities seek to change the comparatively high level of rates increases forecast for 2008 through their annual planning processes. If this occurs, it would provide a stronger indication that local authorities are viewing their LTCCPs and decision-making on a short-term basis.

3.61 Figure 11 shows the comparison of forecast rate changes between the LTCCP Statements of Proposal and the final LTCCPs.
Part 3 Trends, issues, and observations from the 2006-16 LTCCPs

Figure 11
Comparison of rates changes forecast in the LTCCP Statements of Proposal with the final LTCCPs

Note: Includes Auckland City Council forecasts.

Comparing the 2004-14 and 2006-16 LTCCPs

3.62 We were aware that the sector acknowledged that it had issues with the completeness of the 2004-14 LTCCPs (and their predecessors, the 10-year long-term financial strategies), especially in the forecasts for the later years of the planning period. While the audits considered the quality of the financial projections at an individual LTCCP level, we also wanted to find out whether some of the issues with the earlier projections remained at a sector-wide level.

3.63 The ideal way to perform this analysis and to see whether the financial forecasts had improved would be to directly compare the information in the 2004-14 and 2006-16 LTCCPs. However, one effect of including price change in the 2006-16 LTCCPs is that a direct comparison of the forecasts between the two LTCCPs is difficult to perform with any accuracy.

Price change

3.64 Failure to include price change was one of the main deficiencies noted in the 2004-14 LTCCPs. It meant that forecast costs in the later years of the LTCCPs were significantly lower than the probable costs that a local authority was going to incur in that year. This made the resulting funding sources, such as rate and debt levels, less meaningful. It also meant that the LTCCPs could not be relied on as
a tool for long-term planning or, at least, made them less relevant to decision-making.

3.65 For the 2006-16 LTCCPs, all but one local authority included price change in forecasts of operating and capital expenditure. Another local authority did not include forecasts for the revaluation of infrastructure assets.

3.66 Including the effect of price change does not make the forecasts "correct", since actual costs will inevitably vary from the predicted costs. However, including price change means the forecasts will be closer to the actual costs than if price change had been excluded, enhancing the reliability and relevance of the information contained within the LTCCPs. This gives local authorities a clearer basis on which to determine their approach to managing their finances.

3.67 Figure 12 highlights differences between the forecasts included in the 2004-14 and 2006-16 LTCCPs, and shows the significant effect price change had on the forecasts.

**Figure 12**
Comparison of Statements of Financial Performance in the 2004-14 and 2006-16 LTCCPs
Reliability of forecasts

3.68 One of the main concerns raised about the 2004-14 LTCCPs was the reliability of the financial forecasts in the plans – in particular, an apparent focus on the first year of the plan or at least the first three years of the plan compared to years 4-10. For the 2006-16 LTCCPs, this was overcome in part by including price change.

3.69 Capital expenditure was the most obvious area where the forecasts in the 2004-14 LTCCPs could be questioned. The aggregation of all local authorities’ 2004-14 LTCCP cash flow information showed an increase in capital expenditure between 2003 and 2004 from $1,400 million to $2,100 million. However, capital expenditure decreased from $2,100 million in 2004 to $1,200 million in 2014, which is a reduction of $900 million or 43%.

3.70 Our expectation for the 2006-16 LTCCPs was that we would not see such a decrease in the later years of the plans and that the integrity of capital expenditure forecasts in the later years would have improved. Superficially, however, this does not appear to have been the case. Figures 13 and 14 show the comparisons for capital expenditure and for debt and investment in the 2004-14 and 2006-16 LTCCPs.

Figure 13
Comparison of capital expenditure in the 2004-14 and 2006-16 LTCCPs
3.71 As shown in Figure 13, there is a large increase in capital expenditure from $2,500 million (as shown in the 2005/06 annual plans) to $3,200 million in 2006/07 (year 1) of the 2006-16 LTCCPs. In the 2004-14 LTCCPs, capital expenditure decreased from the high point in the first year. The 2006-16 capital expenditure is forecast at a relatively constant level for the first three years of the plan. This suggests that the forecasts in the early years at least may be more reliable than the previous LTCCPs.

3.72 In the 2006-16 LTCCPs, the capital expenditure forecast decreases significantly after the 2008/09 year. The forecast capital expenditure for 2016 is $2,500 million – a decrease of 21% from 2006/07. It must also be noted that the 2006-16 forecasts include the effects of price change, which if excluded would likely result in the decrease being about equivalent to the 43% decrease noted in the 2004-14 LTCCPs.

3.73 Many LTCCPs included significant capital expenditure in the early years to enhance the treatment of wastewater in anticipation of future resource consents relating to the introduction of the New Zealand Drinking Water Standards.

3.74 Local authorities with high growth also appear to be constructing assets earlier in the planning period. All these factors may account for an element of the peak
in capital expenditure in the early years of the LTCCPs and, therefore, affect the overall decrease shown in Figure 13. However, history suggests that local authority capital expenditure does not decrease on a year-to-year basis.

3.75 In our view, the reasons for the significant decrease in the later years are counter-intuitive and need more research and understanding.

3.76 During the LTCCP audits, we became aware of the difficulties local authorities faced in forecasting capital expenditure. Local authorities typically adopted the approach that they would include forecasts only for actual “known” projects. Consequently, in non-infrastructure asset areas that may be more discretionary in nature or where there is no equivalent to an asset management plan, it is less likely that this expenditure will be included in the LTCCP in the later years. Examples in this area include expenditure related to economic development, such as convention centres, or other community facilities such as pools, libraries, and parks.

3.77 An alternative approach to capital expenditure forecasting would have been to include general assessments of other capital expenditure in addition to known projects. This assessment could have considered historical levels of capital expenditure or a capital expenditure envelope defining the probable and affordable level of capital expenditure for the local authority. In developing future LTCCPs, the sector and auditors need to explore this option to assess whether it would be more appropriate.

3.78 Linked to the drop-off in capital expenditure and potentially indicative of the focus on the first three years of the LTCCPs is the cash flows forecast for the 10 years of the plan and the resultant cash and investment balances. Figure 4, earlier in this Part, highlights an apparent change in the financial management strategy indicated by increased funding of capital expenditure from operating revenues in the later part of the LTCCPs, rather than from debt.

3.79 It is possible this is because local authorities focus primarily on the first three years of the LTCCPs, giving less consideration to the forecasts for the rest of the plan. Possible contributing factors to those forecasts include an understatement of capital expenditure, which would mean that cash and investments would be spent on acquiring assets not shown in the LTCCPs.

3.80 Alternatively, for some local authorities, this could represent the build-up of reserves for the future replacement of assets beyond the period covered by the LTCCPs. In this second situation, the local authorities concerned need to consider why they appear to have increases in both cash and debt balances. Efficient financial management would suggest that a local authority would not borrow externally when the expenditure could be financed internally.
Our conclusions

3.81 Overall, there is evidence to suggest that the reliability of financial forecasts has improved – in particular, for the first three years of the 2006-16 LTCCP. Including price change has also resulted in a better representation of the financial future of the local government sector.

3.82 However, we have some doubts about the integrity of the forecasts in the later years of the LTCCPs, with improvements in forecasting required for the 2009-19 LTCCPs. The doubts are primarily about the integrity of capital expenditure forecasts in the later years of the plan and also how clearly LTCCP forecasts reflect local authorities’ financial strategies in those years – or at least in how those strategies are applied to preparing all of the financial information included in the LTCCPs.

3.83 The LTCCPs forecast that rates will continue to increase and will become a proportionately greater funding source in 2016 than in 2006. Rates are an important element in the doubling of surpluses during the 10 years of the plan. However, without further explanation by local authorities of their financial strategy, there is no apparent need for surpluses of this level.

3.84 The surpluses appear to be primarily used for funding capital expenditure, with 81% of total capital expenditure forecast in the LTCCPs to be funded from operating cash flows (which includes surpluses and depreciation). This raises questions around the prudence of the proposed approach, especially in terms of intergenerational equity.

3.85 The significant reliance on operating cash flow in the later years of the LTCCPs differs from the approach used in the first three years of the plans, where debt is a substantial funding source. Possible reasons for such a substantial change include capital expenditure in these years being incomplete and/or that the LTCCPs do not accurately reflect the financial strategy of local authorities for these years. Neither scenario is ideal and suggests that local authorities need to consider whether the LTCCPs appropriately reflect their financing strategies and capital expenditure intentions for the whole 10 years.

3.86 The changes between the LTCCP Statements of Proposal and the final LTCCPs occurred primarily in the first year of the plans, possibly indicating a short-term focus by local authorities. This cannot be substantiated, but we will compare rating levels proposed for local authorities’ 2007/08 annual plans to those proposed in the LTCCPs to see if this theory is correct.

3.87 The financial analysis and aggregation of the financial data included in this Part highlights some trends and possible issues within the local government sector’s financial approach. The sector needs to analyse the financial information in the LTCCPs and consider the issues further.
Part 4
Common issues arising during preparation of the 2006-16 LTCCPs

4.1 In this Part, we discuss the common issues about the preparation of the 2006-16 LTCCPs that emerged during our audits.

What is the LTCCP intended to provide?

4.2 The LTCCP is intended to provide the basis for an integrated long-term focus for a local authority to make decisions, select activities, and co-ordinate the use of its resources.¹

4.3 The three main individual content areas of the LTCCP – the performance framework, asset management planning, and the financial management framework – are integrated to form the Group of Activities Statements² within the LTCCP. We discuss the three content areas in detail separately in Parts 5, 6, and 7.

4.4 Clause 2 of Schedule 10 of the Act requires an LTCCP to include information about:

- the activities within the group of activities, the rationale for carrying out these activities, and any significant negative effects that the activities may have on the well-being of the community; and
- the assets required by the group of activities, including:
  - how a local authority will assess and manage the asset management implications of changes to demand for, or consumption of, relevant services, and service provision levels and standards;
  - what additional asset capacity is estimated to be required as a result;
  - how additional asset capacity will be provided, including the estimated costs and how these costs will be met; and
  - how the maintenance, renewal, and replacement of assets will be carried out and the associated costs met.

4.5 Clause 2 of Schedule 10 of the Act also requires the LTCCP to include a Group of Activities Statement (in detail for each of the first three years of the plan and in outline for each subsequent year of the plan) of:

- the intended levels of service provision for the group of activities, including the performance targets and other measures by which actual levels of service provision may meaningfully be assessed;
- the estimated expenses of achieving and maintaining the identified levels of service provision, including the estimated expenses associated with maintaining the service capacity and integrity of assets; and
- how the expenses are to be met, the estimated revenue levels, the other sources of funds, and the rationale for their selection.

¹ Section 93(6) of the Act.
² Group of activities, as defined in the Act, means one or more related activities provided by, or on behalf of, a local authority or council-controlled organisation.
Overall, our observations of the quality and reliability of the information in the three individual content areas suggest that there is a need for better understanding of the levels of service currently delivered and those intended to be delivered during the 10 years of the LTCCP.

**Two common problems in preparing the LTCCP**

We observed two common problems in the LTCCP preparation process where improvements could be made:
- poor project management and poor management of the sequence for preparing and developing information; and
- poor identification of the issues that must be communicated in the LTCCP Statement of Proposal (including in the LTCCP Summary) and in the final LTCCP.

**Project management and the sequence for developing information**

Preparing an LTCCP involves reconciling past service information with future expectations and intentions:
- **Past service information** relates to matters such as existing strategies and policies, actual services provided, actual condition and performance of assets, and actual financial revenue and expenditure.
- **Future expectations and intentions** are formed by the process of identifying public issues and needs, and assessing the likely demand and opportunities for a local authority to respond to these issues. These expectations and intentions are informed by public feedback over time, as well as through specific consultation. This could occur through processes such as the community outcomes development process and through modelling the effect of likely demographic, environmental, and economic change on services and local authority operations.

At times there will be gaps between expectations and a local authority’s current ability to deliver to those expectations. These gaps should also be understood as a result of reconciling past service information with future expectations and intentions.

Our LTCCP audit methodology was built on the assumption that local authorities would be preparing information to allow this reconciliation through a sequential project management process, as shown in Figure 15.
Figure 15
Example of sequential project management process to prepare LTCCPs

### Likely date of completion

- **Up to June 2005**
  - Development of key policies:
    - Revenue and financing policy – funding of operational and capital expenditure; and
    - Treasury management policy – debt limits, investment policies, strategic assets.
  - Service levels established/reviewed through review of strategies, policies, and plans.
  - Start SM significant assumptions
  - Start SM section 102 policies
  - Start SM accounting policies
  - Continue understanding the LTCCP development process
  - Start SM balanced budget
  - Understand and document the internal control environment
  - Perform preliminary analytical review procedures
  - Perform risk assessment
  - Start SM groups of activities
  - Summarise and communicate the audit plan

- **Up to Sept 2005**
  - Development of asset management plans, and review of work programmes and activity level assumptions

- **Up to Dec 2005**
  - Development of operating divisions’ business plans
  - Overall control strategies, work programmes, budgets, funding impact statement, performance measures
  - Proposed LTCCP Statement of Proposal
  - Summary of the Statement of Proposal

- **Up to April 2006**
  - Final LTCCP

- **June 2006**
  - Final plan procedures
  - Issue report on final
  - Assess engagement quality

### LTCCP development process

- Community outcomes & consultation process
- Establish terms of engagement
  - Preliminary planning:
    - Start to understand the LTCCP development process and environment
    - Obtain SM community outcomes, decision-making, and consultation
    - Prepare environmental review
    - SM = Standard Module

### Audit procedures

- Establish terms of engagement:
  - Preliminary planning:
    - Start to understand the LTCCP development process and environment
    - Obtain SM community outcomes, decision-making, and consultation
    - Prepare environmental review
    - SM = Standard Module

- Development of operating divisions’ business plans
  - Overall control strategies, work programmes, budgets, funding impact statement, performance measures
  - Proposed LTCCP Statement of Proposal
  - Summary of the Statement of Proposal

- Final LTCCP
  - Final plan procedures
  - Issue report on final
  - Assess engagement quality
4.11 In mid-2005, our auditors began asking local authorities about their project management intentions for preparing the LTCCP, expecting that local authorities would:

- understand their current achieved levels of service and their asset performance and financial position; and
- have sought to understand the effects of issues and needs and, as a result, the likely demand and opportunities for their response to these issues and needs.

4.12 We expected that, in mid-2005, local authorities would be in a position to consider and confirm their strategies and policies, and their intended levels of service. What we found was that many local authorities were updating asset management information while simultaneously seeking to understand the current achieved levels of service and asset performance. However, this work had often started before community outcomes development and/or confirmation of relevant strategies, policies, and levels of service had been completed. Therefore, many local authorities were preparing asset management and financial forecasts without having formed deliberate objectives in terms of the nature and condition of assets required to deliver the intended services.

4.13 This meant that it was not easy to address our audit enquiries about how the LTCCP was contributing to an integrated long-term focus for decision-making, selection of activities, and co-ordination of the use of resources. In many instances, this could be assessed only when the LTCCP Statement of Proposal was close to being adopted for consultation, putting significant pressure on local authorities and auditors from March to May 2006.

4.14 To successfully reconcile past service information and future expectations and intentions, local authorities must improve their understanding of the sequence for information development and the relationship between sets of information. They must also be able to effectively integrate this information by applying project management disciplines.

4.15 LTCCPs contain a large amount of information. Changes in strategies, levels of service, and assumptions can appear minor but can have a significant effect within a group of activities and, on occasions, for a local authority as a whole. If information is not managed sequentially, it is difficult for local authorities and auditors to be sure that all such matters have been resolved and addressed during preparation of the LTCCP.
Identification of the issues that must be communicated in the LTCCP and the LTCCP Summary

4.16 The other significant aspect of the LTCCP preparation process where we observed common themes was the way that local authorities used the information being gathered for the LTCCP to form an overview to identify the main issues. This involves two types of consideration:

• a “What is this LTCCP saying overall and does it make sense?” test; and
• a “What do we need to emphasise and explain to the community or consult the community about?” test.

What is this LTCCP saying overall, and does it make sense?

4.17 As financial estimates were aggregated from Group of Activities Statements to the financial statements as a whole, we observed that local authorities often failed to stand back and consider what the financial statements were depicting. For example, many local authorities projected significant surpluses by the tenth year of their LTCCP but, when asked to elaborate, responded that they did not really expect these surpluses to eventuate.

4.18 We recognise that projecting expenditure 10 years ahead is complex and that it will not be possible to anticipate every expenditure need that is likely to arise. However, the LTCCP should set out the reasonably probable situation anticipated by the local authority.

4.19 Similarly, some local authorities forecast increasing cash levels and increasing debt. When asked to elaborate, they responded that this would also be unlikely to occur, as debt would be managed through internal borrowing.

What do we need to emphasise and explain to the community or consult the community about?

4.20 Local authorities need to carefully identify what should be communicated in the LTCCP Statement of Proposal and in the LTCCP Summary. Again, this would require a local authority to stand back and take an overview of the issues emerging, and consider what should be said about them in both the LTCCP Statement of Proposal and in the LTCCP Summary.

4.21 In many instances, we suggested that (in both the LTCCP Statement of Proposal and in the LTCCP Summary) a local authority refer to any matters that should be raised for public feedback and to significant trends that could be expected during the 10 years covered by the LTCCP. For example, for the overall financial position represented in an LTCCP, we asked local authorities to include an explanation and comments in their LTCCP in some instances where surpluses or other financial changes were very significant.
4.22 We also often noted that significant changes (such as changes in policies that in other circumstances would have required the use of a special consultative procedure) were not mentioned, and the effects on the community or others directly affected were not discussed.

4.23 As a result of a failure to take this overview of the LTCCP, many LTCCP Statements of Proposal did not appear to encapsulate the “right debate” on the main issues facing a local authority or to set out the strategic choices that were being made. More importantly, this also meant that the LTCCP Summary did not set out these issues and, therefore, was less useful than it might have been as a basis for general consultation.3 This failure was exacerbated by the time pressures faced by local authorities because of poor project management and poor management of the sequence for developing information.

4.24 Our audit experience was that LTCCPs tended to be more usable where local authorities embedded a process for preparing the plan. In our view, good sequential development and project management, including internal quality review processes, are necessary for preparing integrated LTCCPs. This approach can enhance a local authority’s own decision-making processes and the quality of the planning process for their communities and other stakeholders.
Part 5

The performance framework

5.1 In this Part, we discuss our observations of the first of the three main individual content areas of the LTCCP – the performance framework. We discuss asset management planning in Part 6 and the financial management framework in Part 7.

The Local Government Act 2002 and our expectations about the performance framework and performance information

5.2 The Act gives local authorities a framework and powers to decide the activities they carry out and how they will carry them out. In providing this framework, the Act also provides that local authorities are accountable to their communities. The LTCCP is a specific basis for this accountability.

5.3 A core element of achieving accountability, which in turn drives asset management and the financial forecast, is the required statement in the LTCCP of:

... the intended levels of service provision for the group of activities, including the performance targets and other measures by which actual levels of service provision may meaningfully be assessed.¹

5.4 The performance framework should reflect the local authority’s intended direction overall and for groups of activities. It should also provide clarity about what the local authority plans to achieve in the short term and an indication of its plans and performance in the longer term. It is the main mechanism for the local authority to inform its community about:

• the range, quality, quantity, and effect of the services it intends to provide; and
• the choices made by the local authority for its services.

5.5 How these levels of service have been developed, expressed, and related to other parts of the LTCCP has been of central interest to us when auditing the LTCCP, as the performance framework is one of the three matters on which the auditor is specifically required to report under sections 84(4)(c) and 94(1)(c) of the Act. These sections require the LTCCP to contain a report from the local authority’s auditor on:

... the extent to which the forecast information and performance measures provide an appropriate framework for the meaningful assessment of the actual levels of service provision.

¹ Schedule 10, clause 2(a).
5.6 Reporting on the forecast information and measures has required us to consider whether a local authority’s LTCCP provides a meaningful performance framework for its groups of activities that:

- sets out the rationale for the local authority’s involvement in each activity, the local authority’s objectives, and any significant risks or negative effects that need to be managed in the course of delivering the activity;
- sets levels of service measures that provide a useful way of understanding how the service delivers on the local authority’s rationale for performance involvement;
- provides information about the planned levels of service for the next three years and outlines planned levels of service for the subsequent seven years; and
- sets reasonable targets and other measures to allow the actual levels of service provision (as reported at the end of each financial year in the annual report) to be meaningfully assessed.

5.7 We identified 11 attributes of useful performance reporting and associated processes for the LTCCP. We expected performance reporting to:

- be approached in a systematic, transparent way throughout the local authority;
- present important information consistently across services;
- have a logical flow, including a sustainability context;
- relate to management decision-making;
- align with business and asset information;
- be based on sound information on resources and the infrastructure asset base;
- result in reasonable targets and reliable assumptions;
- identify risks and potential significant negative effects;
- be complete and balanced, with levels of service clearly identified;
- be relevant and meaningful to users and the community; and
- use performance measures that are accurate, neutral, and comparable.

5.8 Several elements are required for a local authority’s performance planning, reporting, and management framework to perform its intended functions in the areas of decision-making and accountability. Figure 16 outlines these elements and shows the flow of the Act’s requirements. Together, these elements form a feedback loop that allows local authorities to manage current service delivery and to plan for future delivery. Therefore, it is important that all the elements are in place, of good quality, and well-linked to provide a strong framework.
Observations from our LTCCP work

5.9 Our observations of the performance framework are drawn from issues raised with us by auditors.

5.10 There are no specific standards or guidance that we can rely on when considering whether a local authority has complied with the Act’s requirements for performance frameworks and information. Therefore, to reach conclusions about the extent to which a meaningful performance framework had been set out in the LTCCP, we used our own work and knowledge of local authorities to apply a "size and scale" approach.2

5.11 As a result, our conclusions about the meaningfulness of performance frameworks and information were based on the practice generally adhered to by relevant peer local authorities. The limitation of this approach is that the practice as a whole may not be as is intended by the Act – a limitation that we consider is relevant to performance frameworks and information in the LTCCP.

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2 We identified peer local authorities by grouping them according to size and scale, and common factors such as population, rates to median income, population to area, full-time equivalent staff, debt to equity, and other local authority income.
5.12 Two local authorities received non-standard audit opinions\textsuperscript{3} as a result of issues directly related to performance information:

- Gisborne District Council’s LTCCP Statement of Proposal and final LTCCP received a qualified audit opinion because the documents did not clearly set out the council’s desired levels of service. Consequently, the LTCCP documents did not adequately link forecast expenditure to what the council was trying to achieve through that expenditure. This affected our view on the reasonableness of the underlying information and the meaningfulness of the performance measures.

- Stratford District Council’s LTCCP Statement of Proposal received a non-standard audit opinion because it inconsistently outlined the desired levels of service and the associated performance measures. It did not, therefore, present a complete forecast and performance framework to the community. The council chose to review the information before releasing the final LTCCP. As a result of the improvements made after that review, we were able to issue an unqualified audit opinion on the final LTCCP.

5.13 While these two councils were the only ones to receive non-standard audit opinions for issues relating to performance frameworks and information, in our view, this was the area of greatest deficiency associated with the 2006-16 LTCCP Statements of Proposal.

5.14 Although we accept that best practice is developing as the local government sector learns more about preparing LTCCPs, a determined effort is needed to improve the ability of many local authorities to undertake planning that allows them to address the long-term needs of their communities.

5.15 Overall, the analysis from our LTCCP audits suggests that the performance framework is a major area requiring development for many local authorities. The attributes of effective performance reporting that we anticipated were often not reflected in the LTCCP or in the underlying information and assumptions.

**Common weaknesses in performance frameworks**

5.16 During our LTCCP audits, we noted weaknesses and issues throughout the elements and processes used by local authorities for their performance planning, reporting, and management frameworks. In our view, along with performance frameworks, noted above, the performance information processes used by most local authorities require significant development to achieve the intentions of the Act.

\textsuperscript{3} For a full explanation of non-standard audit reports, see article 1.5 in Local government: Results of the 2005/06 audits, ISBN 0-478-18186-8.
Part 5  
The performance framework

5.17 Common weaknesses that arose during our LTCCP audits related to:

- a lack of a logical flow in performance reporting;
- levels of service, and performance measures and targets; and
- outcomes monitoring.

Logical flow in performance reporting

5.18 The relevance and appropriateness of selected levels of service performance measures and targets can only be assessed if the local authority sets out the rationale for its activities clearly and logically, describing how its assessment of well-being and the community’s outcomes provide the basis for the selection and direction of its activities. The selection of levels of service and performance measures and targets should reflect this rationale, the local authority’s main strategies and objectives, and any associated risks and negative effects. Figure 17 shows the logical flow of the Act’s performance requirements.

**Figure 17**
Logical flow in the Local Government Act’s performance requirements

5.19 We found that many LTCCPs struggled to demonstrate the overall alignment of the performance framework. In about 25% of LTCCPs, there was a weak link between the rationale for measures and levels of service information. This was because the reasons that certain services were being provided were not clearly stated. In more than 30% of LTCCPs, activities were only weakly linked
to performance measures and outcomes, leading to confusion about how the activities would be measured and how they would contribute to furthering outcomes and/or well-being.

Levels of service and performance measures and targets

5.20 Information about levels of service and performance measures and targets is less meaningful when the logical flow of information is not complete or clear. Therefore, the logical flow weaknesses noted in paragraph 5.19 compounded issues about levels of service and performance measures and targets.

5.21 Almost 25% of LTCCPs lacked clarity about definitions of levels of service within the information on each group of activities. We were particularly surprised to find that about 20% of local authorities did not have clearly defined levels of service in their underlying asset management planning information (see Part 6).

5.22 Without sound asset information to give effect to intended levels of service, it is difficult to assess and plan for the asset capacity needed and the associated financial costs. It is also difficult to measure achievement of those levels of service.

5.23 This lack of information about levels of service affected the extent to which local authorities were able to identify accurate, neutral, comparable, and reasonably based best-estimate performance targets.

5.24 More than 65% of local authorities had performance measure shortcomings to varying extents, meaning that the intentions of the groups of activities were unclear and there was often no identifiable measure to assess achievement. These shortcomings most commonly related to:
   - the relevance of measures to the rationale for the activity;
   - the context of the environment and risks within which the activity operated; and
   - the reasonableness of the 10-year performance targets (that is, whether these were reasonably based best estimates).

5.25 We expected that the intended achievements resulting from a service or activity and the associated risks and potential negative effects would influence the selection of relevant performance measures.

5.26 Clause 2(1)(c) of Schedule 10 of the Act requires the LTCCP to, for each group of activities of the local authority, outline any significant negative effects that any activity within the group of activities may have on the social, economic, environmental, or cultural well-being of the local community. This requires the local authority to consider potential significant negative effects on community
well-being and to disclose crucial assumptions. We observed that about 30% of LTCCPs either did not include information on negative effects or had poor coverage of negative effects.

5.27 The risks and negative effects that were identified in contextual information for groups of activities did not appear to have resulted in performance measures and targets for managing such risks. For example, contextual information identified that resource consent requirements for taking water were being frequently breached or that there was not enough water available to meet demand at peak periods, but there was no discussion about how water supply issues were being managed.

5.28 A common approach used to measure the performance of levels of service information was to state that the levels of service, and, therefore, the performance measures and targets, were assumed to be constant for the duration of the LTCCP. More than 30% of local authorities had constant, or near constant, levels of service for the 10 years of their LTCCP. However, when considered in conjunction with the information on other groups of activities, it often appeared that local authorities had failed to integrate the effect of asset or financial decisions with their associated effects on levels of service. This meant that, while asset and/or financial information would be indicating significant change, levels of service information would inappropriately remain constant.

5.29 In 2006, this issue arose particularly around activity areas such as water services and building consents. Local authorities had not included the intended improvements in drinking water quality or supply within their levels of service and had not provided for changes affecting building consent services.

5.30 Many local authorities are struggling to meet the new requirements of the Building Act 2004 amendments, which raises a concern that local authorities are in a “double jeopardy” situation. The Building Act 2004 (among others) requires local authorities to process applications within certain time constraints. However, in many instances, the annual reports of local authorities show that these deadlines are not being met. The dilemma arises, therefore, whether a local authority’s LTCCP should show a reasonable estimate based on past performance and effectively plan to breach the Building Act or whether it should show an unreasonable target that reflects its legislative obligations.

5.31 In our view, a sustained historic failure to meet statutory requirements indicates the need to invest greater effort into a service. A local authority should advise within the activity information in the LTCCP that it has not previously met its statutory obligations and outline the steps it is taking to remedy this. In suggesting that local authorities outline such steps, we appreciate that reasons
for failure to meet statutory requirements may have long-term resourcing effects (for example, to increase funding to deal with new statutory requirements) or may not be resolvable in the short term (for example, where there are skills and expertise shortages).

Outcomes monitoring

5.32 In addition to inadequate performance measures and targets, supporting information on the achievement of outcomes was also frequently incomplete. Our analysis of the LTCCP audits found that nearly 30% of local authorities did not have complete outcomes monitoring. Again this shows the lack of a direct link to measuring specific community outcomes. These outcomes often did not have specific targets and measures. The monitoring arrangements for community outcomes that were included were often expressed very generally.

5.33 We were aware that the framework and measures for monitoring outcomes were in the very early stages of development because of the different arrangements for local authorities for identifying outcomes in their first LTCCP in 2003 or 2004. Local authorities were required to include the information for the first time in the 2006-16 LTCCP. As a result, we expect outcomes monitoring information to show improvement when local authorities publish their annual and community outcomes reports.

5.34 Monitoring outcomes is a critical component of the performance framework, as it allows local authorities to demonstrate the extent to which their activities are furthering community outcomes and/or well-being. Information disclosed in the LTCCP needs to communicate how the identified outcome is being achieved, with reference to the current state of the outcome and the measures used to assess change in the state of the outcome over time.

5.35 In more than 10% of LTCCPs, community outcomes were not clearly linked to the local authority’s strategy. This created confusion about how the local authority’s strategic vision integrated with the community vision, which is articulated through the community outcomes.

5.36 We noted a peculiarity in outcomes monitoring by two local authorities. They had disclosed activities and tasks under each identified outcome as the means intended to demonstrate how the outcome is being furthered, rather than using indicators that might allow the state of the outcome to be assessed. It does not seem likely to us that an activity-based or task-based approach to outcomes monitoring would fulfil the expectations of the Act. This is because the specified activities do not measure the outcome, so there is a weakness in the link. It raises the question as to whether the local authority is adequately monitoring the community outcomes.

4 See section 279(2) of the Act.
5.37 We consider that the better practice is to include evaluative indicators, rather than use activity reporting to measure outcomes. However, we could not see that an activity reporting approach was precluded by the Act. Therefore, we could only advise the two local authorities taking this approach of our view on the matter.

5.38 Every three years, local authorities are required to report on their monitoring of the achievement of community outcomes to show the attainment of community well-being and the community outcomes planned. To show how the local authority is contributing to community outcomes, it is required to report annually on how activities it carries out result in the furthering of community outcomes.

5.39 The community outcomes and well-being identified by the local authority should flow into the intended levels of service and the performance measures and targets to allow for meaningful assessment. Annual reporting should explain any variance between intended and actual levels of service, and how the levels of service link to activities that help to advance community outcomes and well-being.

**Our conclusions**

5.40 We are particularly concerned that levels of service identified by local authorities appear to be poorly defined. Levels of service are vital in their own right, and they also underpin asset management and financial planning.

5.41 The performance framework and information should form a feedback loop to fulfil its intended function. However, in our view, the performance framework and the information that comprise this feedback loop were the areas of greatest deficiency in the 2006-16 LTCCPs.

5.42 SOLGM has set up a working party to improve this area. We hope to provide input to this timely and vital initiative.
Part 6
Asset management planning

6.1 In this Part, we consider asset management planning as the second of three main individual content areas of the LTCCP. We discuss the performance framework in Part 5 and the financial management framework in Part 7.

The importance of good quality asset management planning

6.2 For more than a decade, the Auditor-General’s reports to Parliament have raised issues about asset management by local authorities. These reports have, in particular, highlighted:

- the importance of quality underlying information to allow reliable estimates to be prepared; and
- the need for asset management plans to be based on levels of service established in consultation with ratepayers or users of services.

6.3 As part of our LTCCP work, we undertook a range of assessments and enquiries to assess the asset information on which LTCCPs were based. Section 94(1)(b) of the Act states that the auditor must report on “the quality of the information and assumptions underlying the forecast information provided in the plan”.

6.4 Local authorities manage significant infrastructural and community assets that are the means by which they deliver most of their critical quality-of-life services to their communities. It is essential that local authorities clearly demonstrate the intended use of assets to enable communities to see what services will be provided if those plans are implemented.

6.5 For most local authorities, these assets also represent the largest value asset class in the Statement of Financial Position. Because they need to be maintained and renewed, and require continual capital development to deal with growth and changing standards, assets often also generate the greatest value expense in the Statement of Financial Performance. Therefore, the asset information base and the projections associated with this information were of particular interest in our audit work.

6.6 Various information requirements of the LTCCP have reinforced the need for reliable information so that communities can have confidence in the proposals and underlying information in these plans. In particular, clause 2(1)(d) of Schedule 10 of the Act requires local authorities to:

... identify the assets or groups of assets required by the group of activities and identify, in relation to those assets or groups of assets, —
(i) how the local authority will assess and manage the asset management implications of changes to —
   (a) demand for, or consumption of, relevant services; and
   (b) service provision levels and standards:
(ii) what additional asset capacity is estimated to be required in respect of changes to each of the matters described in subparagraph (i):
(iii) how the provision of additional asset capacity will be undertaken:
(iv) the estimated costs of the provision of additional asset capacity identified under subparagraph (ii), and the division of those costs between each of the matters in respect of which additional capacity is required:
(v) how the costs of the provision of additional asset capacity will be met:
(vi) how the maintenance, renewal, and replacement of assets will be undertaken:
(vii) how the costs of the maintenance, renewal, and replacement of assets will be met.

Our previous assessments of asset management plans

6.7 In our report on the results of the 2002/03 local government audits,1 we advised the results of our assessments of local authority asset management plans (or information that functions as such a plan), selecting the best and least developed plans of each local authority for review. Because many regional councils are not extensively involved in asset-intensive activities, they were included in the review only where they held significant assets.

6.8 The two selected plans for each local authority were ranked from 1 (low) to 5 (high) against 12 criteria. These criteria were based on the dimensions set out in the International Infrastructure Management Manual Creating Customer Value,2 which, in our view, represented current best practice for the sector in asset management planning.

6.9 The 12 assessment criteria were:
   • optimised decision-making;
   • updating;
   • implementation;

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1 Local Government: Results of the 2002-03 audits, Part 2.4 Asset management plans, parliamentary paper B.29(04b), page 52.
2 The Creating Customer Value manual is one in a set of manuals developed by the National Asset Management Steering Group. The manual is being revised in 2007.
• risk management;
• planning preparation;
• financial forecasts;
• integration;
• outline improvement programmes;
• planning assumptions and confidence levels;
• timetable;
• service levels; and
• description of assets.

6.10 In choosing to use these criteria, we were nonetheless aware that not all local authority asset information would need to be prepared to the extent suggested by the manual, and that the criteria were relevant primarily to key service and high-value assets.

6.11 At that time, we concluded that some local authorities needed to improve their asset information to meet the new disclosure requirements of the Act. We also considered that many needed to improve information on future-oriented uses, such as risk management and optimised decision-making.

Our assessment of asset management plans in 2005

6.12 In 2005, before we started our LTCCP audit work, we assessed 92 asset management plans covering 52 local authorities.3 This work suggested that common areas of weakness in asset management plans were likely to be:

• levels of service – the ability of local authorities to define levels of service that are meaningful to the public and that measure the achievement of community outcomes;

• improvement planning – the ability of local authorities to demonstrate a track record of improvement from earlier versions of plans and that they have in place an improvement plan that is specific and credible, and outlines the resources and time needed, with a clear way to assess its achievement; and

• financial forecasting – the ability of local authorities to set clear financial forecasts in their plans, based on the described levels of service and consistent with asset life cycle management needs.

Underlying asset information in the LTCCPs

6.13 As part of issuing audit opinions on LTCCPs, we assessed underlying asset information and reviewed LTCCP context disclosures.

Non-standard audit opinions issued

6.14 We issued five non-standard audit opinions (two “adverse” audit opinions and three “except-for” audit opinions) on LTCCP Statements of Proposal and final adopted LTCCPs for reasons related to the quality of underlying asset information.

Adverse audit opinions

6.15 We issued adverse audit opinions for:
- Carterton District Council; and
- Invercargill City Council.

6.16 For these two councils, we concluded that, overall, their LTCCPs were not fit for purpose because underlying information, mainly for infrastructure assets, was inadequate to support the prospective information. Because of the cumulative effect of these fundamental issues, we were unable to affirm that the LTCCPs were financially prudent.

6.17 For Carterton District Council, these information weaknesses related to both the prospective information on the levels of service that the council will provide the ratepayer and the associated operational and capital expenditure required to be incurred. The inadequacy of the information meant that the council’s costs could be materially misstated and that it was uncertain whether the council could deliver the levels of service agreed with the community.

6.18 For Invercargill City Council, our view was based on the cumulative effects of either inadequate or inconsistently applied underlying information. This underlying information was mainly infrastructure asset information associated with the council’s major service activities of water and roading. It was not possible to affirm that the level of proposed expenditure over the life of the LTCCP would deliver the levels of service or that the expenditure was not materially misstated. Further, the performance information could not be adequately linked to the disclosed performance measures.

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4 For more information on audit opinions, refer to Part 8.
5 See section 93(6) of the Act.
6 See section 101 of the Act.
Except-for audit opinions

6.19 In three other instances – Kaikoura District Council, Chatham Islands Council, and Dunedin City Council – we issued except-for audit opinions because these councils had not completed a water and sanitary services assessment, as required by section 125 of the Act.

6.20 For these councils, the asset management information held adequately supported the prospective information set out in the LTCCP. However, the failure to complete the water and sanitary services assessment (including the specific statements and proposals set out in sections 126 and 127 of the Act and consultation under section 128) meant that information may have been omitted that could have affected these councils’ asset management intentions. The statements and proposals relate to:

• current and estimated future demands for services;
• the options available to meet the current and future demands;
• the council’s intended role in meeting the current and future demands; and
• the council’s proposals for meeting the current and future demands.

General observations on underlying asset information

6.21 Our general observations have been drawn from issues raised by auditors when issuing LTCCP audit opinions. The observations are, therefore, primarily focused on assessing underlying asset information for the purpose of issuing an audit opinion, rather than assessing the state of asset management planning.

6.22 Many of the issues raised were remedied before the LTCCP Statements of Proposal were released. In instances where issues remained, they were assessed as being not material for the purpose of giving assurance on LTCCPs. Nonetheless, this does not mean that the local authorities do not need to improve these areas for the long-term needs of their communities. To give an accurate picture of a local authority’s long-term strategy, the LTCCP requires reliable underlying information and sound integration of those information sources and plans within the local authority. Consequently, internal systems for asset management and asset management planning are pivotal to supporting policies planned by local authorities.

6.23 The three areas of concern about asset management most common among local authorities were:

• the completeness and reliability of asset management plans;
• the disclosure of levels of service; and
• the effect of anticipated growth on asset management.
Completeness and reliability of asset management plans

6.24 In general, the completeness of asset management plans was poor. More than 20% of local authorities had asset management plans that were incomplete and, therefore, potentially unreliable. However, further testing found that, in most instances, the local authorities held information that allowed reasonable projections to be made in LTCCPs and that it was the plans that were inadequate or out of date.

6.25 Up to 15% more local authorities had asset management plans that were unreliable because the plans were out of date or in the process of being updated. Also, about 15% of local authorities had incomplete financial forecasts for asset management, indicating that the application of the underlying asset information was weak.

Disclosure of levels of service

6.26 Determining and understanding levels of service and their link to community outcomes provides the basis for a local authority to plan its asset management intentions.

6.27 About 20% of local authorities did not clearly define levels of service in their asset management plans. This has implications for the links from asset management plans to strategic corporate planning and community outcomes.

6.28 It also has implications for the links from asset management plans to the local authority's performance framework. Clause 2(2)(a) of Schedule 10 of the Act specifies that this information must include “a statement of intended levels of service provision for the group of activities, including the performance targets and other measures by which actual levels of service provision may meaningfully be assessed”.

6.29 This highlights the need to provide clear intentions about levels of service, along with the need for clear targets and other measures to assess achievement of those services and, more importantly, achievement of related community outcomes. Without clearly defined levels of service in asset management plans, local authorities will find it very difficult to measure the levels of service that are being achieved.

Effect of anticipated growth on asset management

6.30 Application of the growth assumption is the third area of concern. Because local authorities rely heavily on their assets, in particular, infrastructural assets, it is important that they consider the capacity of current assets to sustain the pressures of future growth and that they acknowledge the capital expenditure required to maintain that capacity.
6.31 Clause 2 of Schedule 10 of the Act requires local authorities to identify how they will assess and manage the asset management implications of changes to demand for, or consumption of, relevant services and what additional capacity is required for these changes. This creates a requirement to allocate capital expenditure to changes in demand for, or consumption of, relevant services; changes in levels of service and standards; and the maintenance, renewal, and replacement of assets.

6.32 About 30% of local authorities did not clearly allocate capital expenditure to growth, levels of service, renewals, or “other”, and did not separately and clearly identify the capacity and levels of service components of their asset management projections. Furthermore, two local authorities did not provide a clear explanation of asset management in relation to their allocation of capital expenditure. They also had no growth assumption.

6.33 About 15% of local authorities did not fully discuss the capacity of current infrastructure to meet future growth and the flow-on effect of how the maintenance, renewal, and replacement of assets will be carried out. Consequently, there was a weak link from growth strategies to financial forecasts.

6.34 These results demonstrate that a significant number of local authorities did not clearly meet the disclosure requirements of clause 2(1)(d) of Schedule 10 of the Act and, therefore, did not clearly explain the way they were dealing with anticipated growth in relation to asset management.

Review of asset management plans subsequent to the 2006-16 LTCCPs

What we did

6.35 For our review of the 2006-16 LTCCPs, we reassessed local authorities’ asset management plans (or information that functions as such a plan) using the same approach that we took in 2003. This approach involved selecting and reviewing the best and least developed plans of each local authority (see paragraphs 6.7-6.9).

What we found

6.36 Figures 18 and 19 show the average rankings for each of the 12 criteria for best and least developed asset management plans for both 2003 and 2006. A comparison of the figures allows us to see that, for 2003, most criteria were ranked between 2 and 3, whereas, for 2006, most criteria were ranked between 2 and 3.5. This demonstrates that, overall, there was some improvement in asset management plans.
Figure 18
Average rankings in 2003 for the 12 criteria for asset management planning
Of the best asset management plans we reviewed in 2006:

- three cities, 13 districts, and three regions scored 3 or above on every criteria ranked;
- nine cities, 12 districts, and three regions scored 3 or above for all but one or two of the criteria ranked; and
- no local authority scored 2 or less on every criteria ranked.

Of the least developed asset management plans we reviewed in 2006:

- three cities, 12 districts, and two regions scored 3 or above for all but one or two of the criteria ranked;
- four cities, 10 districts, and two regions scored 2 or below for all but one or two of the criteria ranked; and
- one region ranked no higher than 1 on all criteria.

For both the best and least developed asset management plans, the two criteria that were ranked lowest were risk management and optimised decision-making. This result is perhaps unsurprising – many local authorities initially drew up asset...
management plans in 1996 to help establish whether their projected operating revenue was enough to cover operating expenses, as required by amendments to the 1974 Act. Future uses of information, such as for risk management and optimised decision-making, would not have been a primary focus.

6.40 Nonetheless, we had hoped that, when local authorities recognised the benefits of asset management planning for managing and predicting the need for services, they would have enhanced their basic asset information. Although there has been some improvement, we consider that there is room for further improvement to better meet the intentions of the Act.

6.41 The results of our review suggest that there is not much variation in the quality of asset management plans between the best and least developed plans within each local authority. While this result is heartening, we are aware that some local authorities may not have prepared asset management plans for non-infrastructure-intensive assets – for example, parks and reserves. As our review looked at prepared information about assets, this could reflect a more positive state of asset management than actually exists for some types of assets.

Comparison of asset management plans in 2003 and 2006

6.42 A comparison of the results from the 2003 and 2006 reviews of asset management plans shows that, as a whole, the quality of asset management plans has improved. Despite this improvement, the main results in 2006 resembled those of 2003.

6.43 Improvement is evident because the ratings for the best and least developed asset management plans have either remained the same or improved for all criteria. As shown in Figure 20, both the best and least developed asset management plans experienced improvement for 75% of the criteria.
Figure 20
Comparison of best and least developed asset management plans

<table>
<thead>
<tr>
<th>Least developed asset management plans</th>
<th>2003</th>
<th>2006</th>
</tr>
</thead>
<tbody>
<tr>
<td>Local authorities scoring 3 or above for all but one or two of the criteria ranked</td>
<td>6</td>
<td>17</td>
</tr>
<tr>
<td>Local authorities scoring 2 or below for all but one or two of the criteria ranked</td>
<td>31</td>
<td>15</td>
</tr>
<tr>
<td>Local authorities ranked no higher than 1 on all criteria</td>
<td>2</td>
<td>1</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Best developed asset management plans</th>
<th>2003</th>
<th>2006</th>
</tr>
</thead>
<tbody>
<tr>
<td>Local authorities scoring 3 or above on every criteria ranked</td>
<td>6</td>
<td>19</td>
</tr>
<tr>
<td>Local authorities scoring 3 or above for all but one or two of the criteria ranked</td>
<td>17</td>
<td>24</td>
</tr>
<tr>
<td>Local authorities scoring 2 or less on every criteria ranked</td>
<td>4</td>
<td>0</td>
</tr>
</tbody>
</table>

6.44 Figure 20 shows that there has been a significant increase in the number of local authorities scoring 3 or higher in all, or all but one or two, of the criteria. In addition, there was a significant reduction in the number of local authorities scoring 2 or less for all, or all but one or two, of the criteria. Interestingly, there were no local authorities with best developed asset management plans that scored 2 or less on every criteria in 2006, whereas four local authorities did in 2003.

6.45 The range in quality between the best and least developed asset management plans for all criteria continues to be relatively small. This shows that local authorities have improved, in a similar proportion, the best and least developed asset management plans.

6.46 The main trends identified in 2006 have not changed significantly from those identified in 2003. Risk management and optimised decision-making were the two criteria that ranked lowest in 2003, and they maintained this grading in 2006. Although these areas were still weak, both experienced some improvement.
Our conclusions

6.47 Our review found some improvement in the asset management plans of local authorities. Notwithstanding this, a number of local authorities still need to further improve their asset information to give effect to the new disclosure requirements of the Act.

6.48 There is no statutory requirement for local authorities to follow a framework such as the criteria in the *Creating Customer Value* manual (see paragraphs 6.8-6.9) that we used to assess asset management plans. In our view, using such a framework would assist local authorities to prepare asset information that addresses most of the requirements of the Act. The National Asset Management Steering Group is actively involved in and supports the improvement of asset management planning.

6.49 All local authorities would benefit from investing effort in improving asset information to meet the requirements of the Act by gaining an enhanced understanding of:

- how assets deliver service and the effect of asset decisions on levels of service; and
- the cost of operating existing assets and the funding required for extra capacity.

6.50 Our review also suggests that, although most local authorities have a reasonable standard of base information, many need to apply the information to future-oriented uses, such as risk management and optimised decision-making. By using reliable asset information for these purposes, local authorities will be able to identify and meet future needs effectively and efficiently, and protect their ability to deliver critical services to communities.

6.51 We recognise the improvement achieved in this area to date, and encourage the sector and the National Asset Management Steering Group to continue their work towards further improvement. We will maintain our interest in the state of asset management information because of its importance for future LTCCPs.
Part 7
The financial management framework

7.1 In this Part, we discuss the third and final main individual content area of the LTCCP – the financial management framework. We discuss the two other main content areas in Part 5 (the performance framework) and Part 6 (asset management planning).

The importance of the financial management framework

7.2 For the LTCCP reader to understand a local authority’s proposed direction, the local authority needs to include its funding and financial policies and financial strategy in the LTCCP. Without such policies, it is often not apparent what the local authority is seeking to achieve and why certain financial results are forecast in the financial information. Further, the policies and strategy are integral to a local authority demonstrating that it is “prudent” in managing its financial resources.

7.3 The funding and financial policies are also important for determining from where and whom the local authority is seeking to fund its operations. There should be clear links between the policies and the LTCCP’s Group of Activities Statement, the rating level projected in the financial statements, the Funding Impact Statement, and the predicted financial position of the local authority.

7.4 The outworking of these policies, in conjunction with the intended directions for service provision, effectively set a local authority’s financial strategy for the duration of the LTCCP. Unfortunately, few LTCCPs contained any useful summary of the financial strategy used and how it might affect the local authority’s service provision. In many instances, we had to urge local authorities to include additional information – either by clarifying their financial strategy or the effect of that strategy or by stating their strategy in the first place.

7.5 The absence of a clear articulation of a local authority’s financial strategies affected the local authority’s ability to communicate “the right debate”. In our view, the LTCCP must clearly state the authority’s financial strategies. This is important for adding value to, and facilitating, appropriate and adequate public debate and agreement.

Three main aspects of the financial management framework

7.6 There are three main aspects of the financial management framework:

- The concept of the balanced budget. This is one of the most important
considerations within the Act\(^3\) and the LTCCP. It is closely associated with achieving intergenerational equity and the sustainability of a local authority’s service delivery.

- The **revenue and financing policy**. Arguably, this is the pre-eminent funding and financial policy – in particular, when combined with the Funding Impact Statement and Group of Activities Statement financial information.
- The **Cost of Service Statements** within the individual Group of Activities Statements. Group of Activities Statements and their related Cost of Service Statements are integral to understanding the local authority’s service intentions and financial strategy.

7.7 Clarity in all three areas within the LTCCP is important.

**The balanced budget and prudent financial management**

7.8 In our view, one of the most important yet misunderstood aspects of the Act is the balanced budget and prudent financial management provisions contained in sections 100 and 101.

7.9 During our review of the 2006-16 LTCCP audits, we identified concerns about how local authorities articulated their financial strategies – especially the explanation of surpluses.

7.10 In paragraphs 7.11-7.83, we provide our interpretation and application of the balanced budget and prudent financial management provisions of the Act, including how those provisions apply to surpluses. Also included are examples where we issued non-standard audit opinions to highlight concerns about the financial prudence of three local authorities’ LTCCP Statements of Proposal.

**Background**

7.11 The financial management principles and requirements for LTCCPs are set out in Subpart 3 of Part 6 of the Act.

7.12 While the Act appears to be written from the premise that a balanced budget – where forecast operating revenues are at least equal to forecast operating expenses – is, on the face of it, financially prudent, the most important provision is section 101, which sets out the principles of prudent financial management.

7.13 Section 100 contains the balanced budget requirement, and section 102 covers funding and financial policies. Figure 21 shows the hierarchy of these sections when assessing the financial prudence of any LTCCP.
Figure 21
Hierarchy of the Local Government Act 2002 assessment of financial prudence

section 101
Establishes a general requirement to manage financial matters prudently and in a manner that promotes the current and future interests of the community.

section 102
Requires local authorities to adopt certain funding and financial policies to provide predictability and certainty about sources and levels of funding.

section 100
Requires a local authority to balance the budget (break-even or surplus) or forecast a deficit where it is financially prudent having regard to:
- maintaining levels of service;
- intergenerational equity;
- section 102 policies, and
- revenue flows required to maintain asset service capacity and integrity.

Financial management provisions

7.14 The core financial management requirements set out in section 101 of the Act are:

(1) A local authority must manage its revenues, expenses, assets, liabilities, investments, and general financial dealings prudently and in a manner that promotes the current and future interests of the community.

(2) A local authority must make adequate and effective provision in its long-term council community plan and in its annual plan (where applicable) to meet the expenditure needs of the local authority identified in that long-term council community plan and annual plan.
(3) The funding needs of the local authority must be met from those sources that the local authority determines to be appropriate, following consideration of,—

(a) in relation to each activity to be funded,—

(i) the community outcomes to which the activity primarily contributes; and

(ii) the distribution of benefits between the community as a whole, any identifiable part of the community, and individuals; and

(iii) the period in or over which those benefits are expected to occur; and

(iv) the extent to which the actions or inaction of particular individuals or a group contribute to the need to undertake the activity; and

(v) the costs and benefits, including consequences for transparency and accountability, of funding the activity distinctly from other activities; and

(b) the overall impact of any allocation of liability for revenue needs on the current and future social, economic, environmental, and cultural well-being of the community.

7.15 A local authority gives effect to section 101 through the funding and financial policies mentioned in sections 102 to 108 of the Act.

7.16 The key sections (102 to 106) require local authorities to adopt four policies with prescribed content requirements:

- a revenue and financing policy — which specifies how operating and capital expenditure will be funded from sources such as rates, fees and charges, interest and dividends, development contributions, and borrowing;
- a liability management policy — which specifies how debt will be managed, including borrowing limits;
- an investment policy — which specifies how investments will be managed; and
- a policy on development contributions or financial contributions — which specifies the approach to obtaining funding for the asset costs arising from growth.

7.17 Operating and capital costs are a function of the levels of service that a local authority intends to provide. These policies provide the guidelines outlining who costs are recovered from and over what period.
Balanced budget requirement

7.18 The purpose of the balanced budget requirement is to ensure that there is access to enough funding to enable the services and assets of the local authority to be sustainably funded over the long term in a manner consistent with prudent financial management.

7.19 Section 100(1) of the Act sets out the balanced budget requirement:

A local authority must ensure that each year’s projected operating revenues are set at a level sufficient to meet that year’s projected operating expenses.

7.20 In this context, “sufficient to meet” means that operating revenues must at least equal operating expenses.

7.21 Under section 100(2), a local authority can set the projected operating revenues at a level different from that required to meet projected operating expenses if the local authority resolves that it is financially prudent to do so. In considering financial prudence, the local authority must have regard to:

- maintaining levels of service;
- maintaining service capacity and integrity of assets;
- intergenerational equity; and
- compliance with local authority funding and financing policies (established under section 102).

7.22 The Act improves the provisions in the Local Government Act 1974 in that it:

- provides that local authorities may choose not to balance the budget where they determine it prudent not to do so; and
- makes it clear that asset replacement and ongoing sustainability are relevant considerations in deciding not to balance the budget.

7.23 These provisions create an opportunity for local authorities to consider their funding requirements from an economic sustainability perspective, rather than the accounting perspective that is presented in the forecast financial statements.

7.24 The 2006-16 LTCCPs were for the minimum period of 10 years. However, the consideration around the balanced budget principles is not limited to the period covered by the LTCCP. This is shown by some of the statutory references:

- Section 100(2)(c) requires local authorities to consider funding for the provision and maintenance of assets over their useful life. The useful lives of most assets held by local authorities extend well beyond the period covered by the LTCCP.
- Section 101(3) sets out funding principles that incorporate the principle of
intergenerational equity. Again, such a funding principle generally extends beyond the period covered by the LTCCP.

7.25 The Act has provided much needed flexibility to the balanced budget requirements. However, the provisions noted in paragraph 7.21 also increase the complexity of the assessment and the judgements required of the local authority and its community.

Examining the balanced budget requirement and its links to financial prudence

7.26 The forecast financial statements – based on generally accepted accounting practice (GAAP) – are the starting point of any local authority’s consideration of the balanced budget requirement of section 100 and of the general financial prudence requirements of section 100(2).

7.27 The definition of operating revenue and operating expenses used for the purposes of considering the section 100 balanced budget requirements should be the same as that used for preparing the annual financial statements in accordance with GAAP. Therefore, projected operating revenue includes such items as assets vested or donated in the period, valuation adjustments for investment properties or forestry investments, interest and dividends, Land Transport New Zealand subsidies, development contributions, and rates. Projected operating expenses will similarly include depreciation, interest on borrowings, employment costs, asset maintenance costs, and other operating costs.

7.28 Section 100 creates a rebuttable presumption that an operating surplus is a pre-requisite to being financially prudent. There may be valid reasons to make adjustments to the GAAP statements of a local authority to determine its funding requirements. In situations where the timing of recognition of an item of revenue or expense for financial reporting purposes differs from any associated cash flows, a local authority may set the level of rates funding at a level different from that which would achieve a balanced budget. For example:

- **Use of reserves** – a local authority may decide to use reserves built up in previous years to fund an operating deficit in any year or years within an LTCCP.

- **Vested assets** – the fair value of vested assets is accounted for as revenue in the period they are vested in the local authority. However, the expense recognised in connection with these assets – that is, depreciation – is recognised progressively over the useful life of the asset. From a funding perspective, if the local authority elects not to rate to recover all the expenditure associated with vested assets, then current ratepayers will not be meeting the full cost associated with the vested asset.
- **Land Transport New Zealand revenue for capital projects** – where roading activity is capital in nature, the cost will be capitalised and depreciated over the useful life of the road. From a funding perspective, a local authority could consider it appropriate to only collect rates revenue on the portion of roading costs funded from local authority reserves, and not seek to rate to recover the depreciation on the Land Transport New Zealand-funded portion of the road asset. This approach assumes that the Land Transport New Zealand regime (or an equivalent regime) will be in place, so that future asset replacement will be funded in a similar manner and will not create a funding burden on future generations.

- **Major capital developments** – in many instances, major developments are funded by user charges, development contributions, or targeted rates. Often, there is a major timing difference between the depreciation expense and the point where revenue is recognised.

7.29 Our review considered whether any year within the LTCCP had an operating deficit, and assessed whether the local authority had passed a resolution after considering matters in section 100(2), as listed in paragraph 7.21.

7.30 There were several instances where local authorities were forecasting deficits in a particular year, and at least two instances where local authorities were forecasting deficits in most years of the LTCCP. All these local authorities had passed a formal resolution explaining why they proposed to operate deficits, and had explained in the LTCCP how their approach was financially prudent.

7.31 One-off deficits or minor deficits were typically easily justified, especially where they were the result of using reserves and cash balances established during previous years. However, where surpluses or losses were recurring, the local authority’s level of scrutiny needed to be considerably higher.

7.32 A local authority presenting an unbalanced budget in the LTCCP needed to be able to demonstrate that the plan complied with section 100(2) by having regard to three factors:

- achieving and maintaining the predicted levels of service;
- equitable allocation; and
- financial prudence and operating surpluses.

**Achieving and maintaining the predicted levels of service**

7.33 Local authorities are required to set out details of the intended levels of service
they will provide to their communities for each group of activities carried out and the costs of the identified levels of service, including the estimated expense associated with maintaining the service capacity and integrity of the assets.

7.34 The LTCCP has a minimum 10-year planning horizon. However, section 100(2)(a) requires that the local authority have regard to expenses associated with maintaining service capacity and asset integrity throughout the useful life of its assets. Therefore, local authorities need reliable asset information and must consider the levels of service and costs associated with the assets beyond the 10 years covered in the LTCCP.

**Equitable allocation**

7.35 In the context of the Act, equity is viewed as addressing the balance of interests between groups currently within the community and between current and future community members.

7.36 Through the equity provision, the Act imposes an obligation on the local authority to consider the pattern of costs to be incurred now and in the future. This is required to maintain a specified level of service and to ensure that these costs are forecast to be met by those members in the community who will receive the service (either directly or indirectly).

7.37 The core question is whether current ratepayers are paying an appropriate level of rates bearing in mind the services they are receiving.

7.38 The concept of equitable allocation was one of the main reasons for introducing the balanced budget test, initially through the 1996 amendments to the Local Government Act 1974. Although the focus of the balanced budget provisions of that Act ultimately became linked to funding depreciation, the thrust of the provisions was on intergenerational equity and moving away from a simple cash funding approach. The intention was to foster consideration of how the costs of services should be equitably funded over time, based on a sustainable level of service and asset replacement.

7.39 Depreciation is considered to be the proxy for the costs associated with the use of assets during the year. If operating costs, including depreciation, are not covered by operating revenues, it is arguable that the current users of the service are not paying the full cost for the benefits they receive.
7.40 One aspect of this approach of operating revenues not covering operating costs (including depreciation) was that, in periods where cash expenditure was lower than the average over time and local authorities considered it was appropriate to collect only enough revenue to cover cash operating and capital expenditures, ratepayers in the future could be faced with significantly higher relative costs with no corresponding increase in quality or level of service.

7.41 In paragraphs 7.55-7.62, we provide an example of a local authority that received a non-standard audit opinion around financial prudence so we could draw attention to the deficits forecast and the implications that this may have in future years.

**Financial prudence and operating surpluses**

7.42 Within the Act, the balanced budget aspect focuses on deficits. While an operating deficit may indicate that the local authority’s levels of service and/or financial operations are unsustainable and result in current costs being shifted to future generations, a surplus does not necessarily mean that the LTCCP is financially prudent.

7.43 It is conceivable that a local authority could be financially imprudent by running high surpluses. Excessive surpluses could also be an indicator of intergenerational inequities where costs are being disproportionately funded by current generations. Therefore, in addition to reviewing for operating deficits, we also considered the level of, and rationale for, operating surpluses and the prudence of the local authority’s overall financial forecasts.

7.44 Our focus was not simply on surpluses but also on the resulting Statement of Financial Position and Statement of Cash Flows. In several instances, we identified local authorities running substantial surpluses that were apparently contributing to increases in cash and investments but that did not appear to be required during the LTCCP. Other elements noted included decreases in debt levels in later years of the LTCCP.

7.45 In combination, factors such as high surpluses, increasing investment levels, and/or decreasing debt levels caused us to query the local authority’s funding approach and whether the approach was prudent, considering intergenerational equity.

7.46 Local authorities with financial forecasts reflecting these elements were asked to explain their financial strategy in the LTCCP, just like those local authorities that were forecasting deficits. The explanations typically cited various factors – for example, that the accumulation of depreciation funding was to be spent on renewals beyond the end of the LTCCP planning period. In some instances, the
explanation of the financial information included in the LTCCP indicated that local authorities needed to more fully consider whether the financial forecasts in the later years of the LTCCP were consistent with their overall financial management approach.

7.47 Of the non-standard audit opinions issued for financial imprudence, none related to the forecast level of surpluses or the strengthening of a local authority’s overall position. However, the LTCCPs were enhanced by providing information that explained the rationale behind surpluses, and cash and investment increases.

7.48 The main point with either scenario of operating deficits or surpluses is that they should not be viewed in isolation when assessing financial prudence. A reader of the financial statements should not unduly focus on the operating surplus produced by a local authority in assessing that local authority’s financial management strategy. The reasons for this include:

- A significant amount of a local authority’s operations are focused on delivering a capital programme. The asset addition is included in the Statement of Financial Position, while, in many instances, some or all of the revenue is included in the Statement of Financial Performance, creating a large surplus. Important contributing factors may be development contributions, vested assets, and grants and subsidies. The extent to which these sources are used and are reflected in the operating surplus of the local authority depends on the local authority’s funding approach.

- The Statement of Financial Performance includes unrealised changes in value, such as in investment properties, forestry, and financial instruments. Items such as these need to be considered when assessing any surplus or deficit.

- The Statement of Financial Performance is only one of three crucial financial statements. Information on the state of the local authority’s finances is reflected in the Statement of Financial Position (the focus should especially be on cash, investment, and loan balances) and the Statement of Cash Flows.

Audit opinions focusing on financial prudence

7.49 To demonstrate financial prudence, a local authority must have established a mechanism to show the effect of financial management decisions on current and future community interests. This mechanism must consider not just the 10-year period covered by the LTCCP but also future periods where the effects of current financial decisions will arise.

7.50 Any assessment of financial prudence requires an understanding of a local authority’s financial management strategy, which is documented in the funding and financial policies (as detailed in section 102 of the Act) and the results
displayed in all the forecast financial statements. An important element of
assessing a local authority’s financial prudence and financial strategy for current
and future community interests is to see whether the forecast finances of the
local authority are realistic and achievable.

7.51 The most challenging aspect of the 2006-16 LTCCP audits for our auditors was
trying to determine from the LTCCP whether a local authority was managing its
finances prudently.

7.52 A qualified audit opinion on an inability to demonstrate financial prudence was
one of the most significant qualifications that we issued on an LTCCP Statement
of Proposal. It meant that, in our view, the local authority and the public could not
use the document for meaningful long-term planning and decision-making.

7.53 Three audit opinions on the final adopted LTCCPs included specific reference to,
or qualification on the grounds of, inability to demonstrate that the plans were
financially prudent.

7.54 In the following three examples, there were different reasons each local authority
was issued a non-standard audit opinion on financial prudence. In each example,
we highlight the rationale for the audit opinion and the implications for the LTCCP
and the local authority.

Example 1: Porirua City Council – intergenerational equity (“emphasis of matter”
audit opinion)

7.55 Porirua City Council elected not to set operating revenues at a level to cover all
operating expenses. The council budgeted for enough cash operating revenues
to cover cash operating expenses and a portion of the non-cash depreciation
expense. As a consequence of this approach, the council forecast deficits in each
year of its LTCCP Statement of Proposal. The deficits ranged from $1.7 million to
$4.5 million, totalling $29.1 million.

7.56 The council articulated the rationale for its approach in the LTCCP Statement of
Proposal. First, it drew a distinction between the accruals approach taken in the
balanced budget and cash funding, showing that – during the 10 years covered by
the LTCCP – the council’s financial position remained sound, with small increases
in overall debt levels and small decreases in cash and investment levels. During
the 10 years, cash and investments decreased by $2.6 million to $21.9 million,
while debt increased by $3 million to $20.8 million. Debt levels remained within
the council’s liability management policy limits.

7.57 In terms of the replacement of assets, Porirua City Council’s infrastructure was
relatively new, with most assets constructed between 1950 and 1975. The council
expects that its wastewater, water, and stormwater assets will not require major renewal work until 2025 at the earliest. The council noted that its LTCCP included enough funding to maintain the levels of service of the assets, with no major funding increases immediately outside the life of the LTCCP.

7.58 The council estimated that a likely result of its approach would be an increase in rates of 9% from 2025, followed by a further 6% in later years. However, if a balanced budget was set, the council would have been debt-free by the end of the LTCCP period, with about $25 million surplus cash in the bank. The council considered that it could not justify that to its community.

7.59 The main risk we identified in Porirua City Council’s approach was the issue of intergenerational equity. We were satisfied that the levels of service for the assets would be maintained during the plan. However, the council’s forecasts showed that there would be reasonably substantial lumpy rates increases in the future that would be less likely to occur had a balanced budget been set in the period covered by the 2006-16 LTCCP.

7.60 Porirua City Council’s reasonably sound financial position and clear disclosure of its approach and potential implications were all factors that we considered in forming our view about whether the approach was financially prudent. We evaluated the arguments proposed by the council about its funding approach and concluded that the approach was financially prudent but with potentially significant risks that current and future ratepayers should be aware of.

7.61 We decided to draw particular attention to Porirua City Council’s approach in our audit opinion. We issued an “emphasis of matter” opinion on the LTCCP Statement of Proposal, which, while unqualified, included an explanatory paragraph that clearly highlighted the issue for ratepayers’ consideration.

7.62 The council received a number of submissions on its draft LTCCP within the LTCCP Statement of Proposal on the prudence or otherwise of the funding approach. While no change was made, the council resolved that, in preparation for the 2009-19 LTCCP, the chief executive would report on a strategy for funding the replacement of stormwater and wastewater reticulation.

**Example 2: Waitomo District Council – financial viability**

7.63 Unlike Porirua City Council, Waitomo District Council presented an LTCCP where each year forecast an operating surplus. However, the resulting audit opinion issued was a qualification that the plan was not financially prudent.

7.64 Waitomo District Council has aging and failing infrastructure, in part attributable to a focus on low rates levels in the short term in previous years. The council is
now faced with a significant amount of capital works to continue to provide existing services. This is in addition to day-to-day operating costs and any new requirements such as drinking water standards.

7.65 In the LTCCP Statement of Proposal, the ratepayer was left in no doubt as to the position of Waitomo District Council. The LTCCP clearly signalled the need for ratepayers to bear a substantial and increasing burden of costs to pay for catch-up work and increased levels of service.

7.66 The LTCCP Statement of Proposal included six alternatives that Waitomo District Council had considered to remedy this situation. The preferred option resulted in the level of debt increasing from $29.1 million to $69.1 million, being 19% of equity by the end of the LTCCP. Rates increased from $9.2 million a year to $15.3 million during the term of the plan — an increase of 66%. By the end of the 10 years of the LTCCP, interest costs were forecast to be $5 million a year. A third of rate income would directly service debt. The financial viability of the council also depended on the investment in its subsidiary, Inframax, which was expected to substantially increase in value and continue to provide dividends.

7.67 Our concerns centred on the sustainability of the funding strategy. The council’s LTCCP Statement of Proposal did not provide assurance that adequate revenue was available to cover all expenses — both operational and capital — notwithstanding the increase in rates that were forecast in the plan. The funding strategy also required a substantial increase in debt, and there was no certainty that the annual increase in borrowing would decrease after the life of the LTCCP. We also questioned whether Waitomo District Council would be able to raise the level of debt outlined in the plan.

7.68 We concluded that the LTCCP Statement of Proposal was not sustainable and therefore not financially prudent, and that Waitomo District Council had not made adequate and effective provision to meet the expenditure needs identified in the LTCCP Statement of Proposal.

7.69 After the LTCCP was adopted, the Department of Internal Affairs appointed an advisory panel to develop specific proposals to assist Waitomo District Council and its community to address identified issues for ongoing financial sustainability in advance of the 2007/08 annual plan round.

Example 3: Timaru District Council – non-inflation of financial forecasts

7.70 Timaru District Council’s scenario differs from both previous examples. The council did not provide cost-adjusted information in its LTCCP Statement of Proposal. Instead, it showed the information in constant dollar values. This non-cost-adjusted information showed surpluses in each year and an increasing level
of debt but overall a relatively sound financial position at the end of the 10-year planning period, with debt levels within liability policy thresholds.

7.71 Cost-adjusting of financial forecasts was a point of significant contention between us and local authorities in the earlier stages of the LTCCP process. In our view, the failure to inflate or cost-adjust the primary financial information included in the LTCCP is a departure from FRS-42, which requires prospective financial information to be based on best-estimate assumptions for events that are reasonably expected to occur. Price change is a best-estimate assumption.

7.72 Our evidence shows that the value of money changes over time and that this will probably occur in the future. Moreover, the price change rate can be forecast and – even if the forecast rate differs from the actual rate – the inclusion of some element of price change will be closer to reality than not including it.

7.73 From a financial management perspective, we were concerned that, by not including price change, the operational and capital costs would be materially different. For example, even assuming that price change was 3% a year on average, in the fourth year of the LTCCP (2009/10) costs would be understated by 9%. In the tenth year of the plan (2015/16), costs would be understated by about 30%.

7.74 Significantly different information may result in the local authority choosing different financing mechanisms. Just because costs are expected to increase does not necessarily mean that revenue streams, such as interest and grants and subsidies, increase in the same manner. The main variable income streams that local authorities manage are rates and user charges, with the main other financing mechanisms being debt and/or cash and investments. If Timaru District Council had had better information on estimated costs, the council could have been better placed to consider the amount of funding changes necessary and whether those increases would be acceptable to the community.

7.75 Consequently, our audit opinion was qualified on the basis that Timaru District Council’s LTCCP could not be financially prudent because the best estimate of costs was not included and because, if it had been included, different funding mechanisms may have been chosen.

7.76 The council included an Income Statement adjusted for future price change as supplementary financial information to the LTCCP Statement of Proposal. However, the assumption of future price change had not been consistently applied to the supplementary information, and the flow-on effect of future price change on balance sheet items had not been considered in the preparation of the supplementary information. Consequently, the supplementary information was incomplete and, in our view, could be misleading.
In the final LTCCP, Timaru District Council corrected the supplementary information so that it reflected price change appropriately. The clear disclosure of the additional price change information showed that the council’s financial strategy was sustainable, so the qualified audit opinion in relation to financial procedure was removed.

**Other examples**

We know of at least two other local authorities that originally prepared their financial information on a non-cost-adjusted basis. When they included price change, it significantly altered the level of rating and debt relative to other funding sources. In one situation, the forecast rates increases were considered unsustainable, so other options were considered.

**Future focus**

Financial prudence was an important focus of our review of the LTCCPs. It is a particularly complex area resulting from the many decisions that a local authority makes around the services it provides and how these services will be funded. There is a level of subjectivity inherent in assessing the financial prudence of any plan. Nevertheless, one of our main focuses in any future reviews of LTCCPs will be on financial prudence – in particular, to try and further differentiate between LTCCPs.

Our audit opinions on the 2006-16 LTCCPs identified those situations where local authorities were not clearly demonstrating financial prudence – effectively creating two categories of plans. However, we consider that there is likely to be a spectrum of plans from the financially imprudent to prudent. Our focus for the 2009-19 LTCCPs will be to distinguish more perceptively between plans and to report on local authorities that have heightened risk around their financial management strategies.

**Our conclusions**

The balanced budget test is only the starting point for assessing whether a local authority’s financial management strategy is financially prudent. Financial prudence needs to be considered after viewing the financial information included in all the financial statements and after understanding the local authority’s financial management strategy, which includes the funding and financial policies prescribed in section 102 of the Act.

For future LTCCPs, we consider that local authorities need to explain their financial strategy and summarise how they have given effect to their policies in the resulting financial information to stakeholders – irrespective of whether surpluses or deficits are forecast.
As noted in paragraphs 7.54-7.76, the final LTCCPs of three local authorities received a non-standard audit opinion because we wanted to highlight matters of financial prudence for the public to consider as part of consultation. In future, we will focus on providing more insightful comment on an LTCCP’s financial prudence to give more meaningful information to the community, stakeholders, and to the sector.

The revenue and financing policy

The revenue and financing policy is the main policy for understanding a local authority’s decisions about funding its operating and capital expenditure. The policy underpins the construction of the financial information within the LTCCP, including explaining which, how, and why individuals and groups within the community will pay for providing the local authority’s services.

In reviewing the LTCCPs, we noted a diversity of approaches to presenting the revenue and financing policy. Some policies were extremely detailed, and others provided information at a very high level with limited specificity. In our view, some of the approaches that were adopted substantially limited the usefulness of the policies to the reader of the LTCCP, although the policies complied with the provisions of the Act.

In the following paragraphs, we examine the requirements of the revenue and financing policy and provide examples of the policies adopted.

Background

The relevant provisions of the Act are section 101(3), section 103, and clause 2(2)(d) of Schedule 10.

Section 103 requires the revenue and financing policy to state the local authority’s policies for funding operating and capital expenses from a list of sources, which explicitly includes general rates (including choice of valuation system, differential rating, and uniform annual general charges), targeted rates, fees and charges, interest and dividends, borrowing, grants and subsidies, and any other funding source.

Section 103(3) requires the policy to show how the local authority has, for the sources identified in the policy, complied with section 101(3).

Section 101(3) states that the funding needs of the local authority must be met from those sources that the local authority determines to be appropriate after considering the:

- community outcomes to which the activity primarily contributes;
7.91 The only other relevant provision is clause 2(2)(d) of Schedule 10, which requires a statement for each group of activities of the estimated revenue levels and other sources of funds, and the rationale for their selection in terms of section 101(3).

Content and focus of revenue and financing policies

7.92 When we started the LTCCP audit process, we had a clear set of expectations about the content and focus of a revenue and financing policy. The policy should enable ratepayers and other users of the LTCCP to determine who pays for what services and the local authority’s rationale for selecting those funding sources, including its considerations. The policy should include funding thresholds or percentages so the reader can ascertain whether these have been applied in preparing the activity-level financial information.

7.93 Our expectations substantially differed from the practices used by many local authorities. In general, local authorities adopted one of two approaches to presenting information in their revenue and financing policies:

• A modification of the previous funding policies, showing the initial assessment of costs and benefits, modifications, and final position, typically in percentage terms, for each group of activities. This approach typically involved considerable narrative that explained the local authority’s considerations in terms of section 101(3).

• A brief rationale for the use of the funding sources listed in section 103, followed by a table or narrative listing the sources applicable to each activity. This was not always accompanied by funding proportions or percentages and did not always explain consideration of the issues in section 101(3).

7.94 As a generalisation, the small to medium local authorities typically included proportion or percentage information. Some larger local authorities did not include this level of detail.

7.95 One local authority used descriptors to show the application of funding sources.
The descriptors, such as marginal cost and full cost recovery, were defined and linked to the local authority’s objectives for the activity.

7.96 The variability in layout and the extent of disclosure within revenue and financing policies was driven by different but acceptable interpretations of the Act. However, we questioned whether some of the approaches adopted achieved the intent of the Act, because they were at such a general level that the funding principles and considerations were unclear. Our concerns about the form and content of the policies for meeting the requirements of the Act include:

- discussion of considerations;
- specifying a level of the funding source to be applied;
- rationale;
- linking of policies with financial information;
- completeness of disclosure around funding sources; and
- disclosure of the funding of capital expenditure.

**Discussion of considerations**

7.97 Section 103(3) requires a local authority to show how it has complied with section 101(3), which, among other things, details considerations about community outcomes and the distribution of benefits. We expected a local authority to outline its considerations within the policy. This would provide a link between the rationale required by clause 2(2)(d) of Schedule 10 and the funding sources listed in section 103 to show why the local authority selected the particular funding source for the activity.

7.98 An alternative permissible position adopted by many local authorities was to acknowledge the content of section 101(3) and to advise in the revenue and financing policy that they had considered those requirements in developing the policy. We consider that this omits information important to understanding the policy and makes the policy less transparent. This was worse where funding levels were not defined or the rationale for selection of funding sources was not explained well.

**Specifying a level of the funding source to be applied**

7.99 The Act does not require a local authority to specify a threshold or percentage for a funding source. Therefore, a local authority can state that an activity is funded from general rates, targeted rates, and/or user fees without providing an indication of the level or nature of costs that the local authority intends to fund from that source.
7.100 One possible reason for a local authority to omit detail in its revenue and financing policy is to reduce the chances that it will need to change the policy, triggering an amendment under section 102 of the Act. However, we are concerned that some approaches make the revenue and financing policy essentially meaningless to the reader of the LTCCP. While the source of funding selected will be reflected in the Cost of Service Statement, the reader cannot understand the local authority’s intent or whether the policy has been complied with in the absence of any description of the level or nature of the costs to be funded from that source.

7.101 In our view, some percentage range or descriptor is desirable, but it must be linked to the local authority’s rationale and not be an end in itself. A local authority’s approach to using the same types of funding may differ depending on the section 101(3) considerations. As a simplified example, a local authority may set user charges for libraries to recover a marginal or nominal cost, reflecting wider objectives around education. In contrast, resource consents may be set for full cost recovery, reflecting the direct benefit to the consent holder. It is critical that any percentage included in the policy is always linked to the underlying objectives for the local authority’s provision of the service.

7.102 A few local authorities provided excessive detail, such as percentages for funding sources for sub-activities within activities in a group. This level of information is not required, and significantly increases the risk of amendments for minor changes in funding approaches.

7.103 Many local authorities used a specific percentage. We suggest that a range of percentages would be appropriate, to provide useful information yet retain an appropriate level of flexibility in the policy.

Rationale

7.104 Clause 2(2)(d) of Schedule 10 of the Act requires a local authority to disclose its rationale for selecting funding sources for an activity. This content is typically included in the revenue and financing policy, rather than at activity level.

7.105 Most local authorities satisfied this requirement by listing their funding sources, explaining the circumstances where each funding source would be used, and listing the sources used for each activity. In general, the explanation of the circumstances where a funding source would be used could be enhanced.

Linking of policies with financial information

7.106 Ideally, there should be a clear link between the revenue and financing policy and the financial information included at activity level. We recognise that this is not always practical, because of the aggregation of multiple activities within a group.
However, local authorities should try to link the policy and the group of activities financial information as transparently as possible.

7.107 In reviewing LTCCP Statements of Proposal, we noted instances where the proposed revenue and financing policy was not applied in the preparation of financial information. Where this was noted, the difference was corrected or explained. However, the discrepancies are a concern, given the importance of the revenue and financing policy to a local authority’s overall financial management strategy. It suggests that financial information may be prepared in isolation from the policy in some instances.

Completeness of disclosure around funding sources

7.108 Many policies were silent or unclear on how non-activity-specific revenues (such as interest and dividends) were applied as funding sources, and the priority for their application in terms of activities and compared to other funding sources. For example, where council-wide revenues are allocated to activities, the policy should be clear how this is performed (for example, directly in proportion to the general rate) and why it is allocated in this manner. Where some activities have council-wide revenues allocated and others do not, this too should be explained.

Disclosure of the funding of capital expenditure

7.109 Funding sources for capital expenditure were generally poorly disclosed. Many local authorities advised that they used a pooled approach to funding capital expenditure or provided a general hierarchy of funding sources that would be used for capital expenditure. Few local authorities clearly articulated their rationale for using certain funding sources and what priority or hierarchy they would give to the selection of the relevant funding source in a particular situation. This was exacerbated where different funding approaches were used for different local authority activities. It was also unclear why some capital expenditure would be rated for, in contrast to when existing funds or borrowing would be used.

7.110 Typically, no distinction was drawn between funding for new assets and renewals. Both are capital expenditure, but local authorities use differing funding sources for each. Renewals, which replace existing assets, are more likely to be funded from rates and reserves/cash funds built up over time as the asset depreciates. New assets may be rated for, but it is also more likely that they will be funded, at least in part, from borrowing. This reflects that the benefit from the assets will continue into the future and that it would be inequitable to make the current ratepayers pay for the full asset cost now.
Our conclusions

7.111 The revenue and financing policy is the most critical policy for understanding a local authority’s financial strategy.

7.112 We had a clear set of expectations about the content and focus of a revenue and financing policy. The policy should enable ratepayers and other users of the LTCCP to determine who pays for what services and the local authority’s rationale for selecting those funding sources, including its considerations. The policy should include thresholds or percentages so the reader can ascertain whether these have been applied in preparing the activity-level financial information.

7.113 These expectations differed substantially from many of the revenue and financing policies included in LTCCPs. Some had such a limited amount of information that the reader could not determine the rationale for selecting the mechanism or what proportion of the activity the local authority intended to fund from that mechanism. The paucity of information made the policies of some local authorities essentially meaningless to an external user.

7.114 If the intent of the Act was to transparently show the rationale for selecting the funding sources, including a local authority’s considerations and the amount or relativities of funding sought, the legislation as it is currently drafted is not achieving this. The local government sector needs to consider whether our views about the intention of the policy are correct and whether the Act requires revision or additional interpretation and guidance around the revenue and financing policy.

Cost of Services Statement

7.115 Since the Local Government Act 1974 was amended in 1989, local authorities have been required to show financial information about the costs and funding of each of their activities in their annual plans and annual reports.

7.116 The clear presentation of activity-level financial information or the Cost of Services Statement has not developed substantially since that time. The information presented is often complicated and difficult to understand. There remain examples where the presentation of information appears to reflect a lack of understanding of local authority funding.

7.117 The 2006-16 LTCCP provided an opportunity to improve the presentation and understandability of the Cost of Services Statement. In an effort to provide guidance in this area, in conjunction with SOLGM we produced principles-based guidance, which included a template, to show how the Cost of Services Statement could be presented. Although some improvement was made by the sector, it was not as significant as we had hoped.
7.118 We again noted concerns around the underlying understanding and presentation of funding decisions, the clarity and internal consistency of information included in the statements, and the links from the revenue and financing policy to the Cost of Services Statement information and the forecast financial statements.

Background

7.119 The statutory provisions for preparing the Cost of Services Statement are found in Schedule 10 of the Act. Under Schedule 10, local authorities are required to include information about each group of activities. That information includes:

• the estimated expenses of achieving and maintaining the identified levels of service provision, including the estimated expenses associated with maintaining the service capacity and integrity of assets (clause 2(2)(b) of Schedule 10);

• a statement of how the expenses are to be met (clause 2(2)(c) of Schedule 10); and

• a statement of the estimated revenue levels, the other sources of funds, and the rationale for their selection in terms of section 101(3).

7.120 This information needs to be provided in detail for each of the first three years covered by the LTCCP and in outline for each of the subsequent financial years of the LTCCP. The financial information complements the levels of service information and performance measures included within each group of activities.

7.121 All local authorities sought to fulfil the provisions of clause 2(2)(b) and (c) by including a Cost of Services Statement (or equivalent financial statement).

7.122 The Cost of Services Statement reflects the operating and capital expenses of an activity and how those expenses will be funded. Disclosure of this information at activity level is important, as activities are typically funded differently. The Cost of Services Statement therefore provides the reader with activity-specific information. It usually most clearly reflects the relationship between the revenue and financing policy, which is set at activity level, and the local authority’s financial information.

Cost of Services Statement issues

7.123 The difficulties with the presentation and understandability of the Cost of Services Statement arise from two sources:

• the application of GAAP; and

• the need to clearly distinguish and understand the dual focus of the statement, as it covers the funding of both capital and operating expenditure.
7.124 Within this second point, the transparent disclosure of funding decisions — in particular, the use of “funded depreciation”, operating surpluses, and reserves — were recurring weaknesses in the presentation of information in the Cost of Services Statement.

**Application of generally accepted accounting practice**

7.125 Section 111 of the Act requires all information required by any provision of Part 6 or Schedule 10 of the Act to be prepared in accordance with GAAP if that information is of a form or nature for which there is a standard in GAAP.

7.126 GAAP prescribes accounting treatments for particular transactions and balances and the presentation of financial information. For the forecast information within an LTCCP, the relevant financial reporting standard is FRS-42 (see paragraphs 3.6-3.7).

7.127 FRS-42 provides that the prospective financial information must include a balance sheet, income statement, statement of changes in equity, and cash flow statement and notes, including accounting policies, significant assumptions, and other relevant underlying information. The standard also provides that “an entity shall apply the principles in this Standard to any prospective financial information published in conjunction with prospective financial statements.”

7.128 GAAP includes formats for the core financial statements specified in FRS-42, but does not include any suggested presentation for the Cost of Services Statements that local authorities are required to present. Consequently, while GAAP principles apply to the preparation of the information, such as differentiating between operating and capital expenditure, the format of the statements (including the level of detail to be included within the statement) is at the discretion of the local authority.

7.129 The lack of authoritative guidance contributes to the diversity of approaches that local authorities have adopted to presenting this information.

**Dual focus – income and expenditure, and funding**

7.130 The Cost of Services Statement must reflect both capital and operating expenditure. To show how these expenses are met, the Cost of Services Statement must include operating revenues and other funding sources that do not affect the overall statement of financial performance, such as borrowing or the use of reserves — mixing accrual and cash accounting concepts.

7.131 The two distinct concepts can cause confusion with the reader of the financial statements, especially to those who focus on an activity’s surplus without considering that the surplus may be used to fund expenditure of a capital nature.
This could include capital expenditure such as asset purchases or debt repayment. In some instances, it also appears that those preparing the financial information are confused about how to transparently present the funding decisions made by local authorities.

7.132 The main concerns identified in this respect were in:
- cash funding – funded depreciation;
- transfers into and out of reserves;
- split disclosure of revenue items;
- inclusion of internal revenue and expenses within an activity;
- presentation of operating expenditure; and
- aggregation of funding sources.

**Cash funding – funded depreciation**

7.133 The Cost of Services Statement includes accrual accounting estimates for operating revenue and expenditure, and cash funding requirements for capital expenditure. Accrual accounting includes non-cash items such as depreciation. Where total operating costs (including depreciation) are at least met by cash operating revenues such as rates, user charges, cash development contributions, interest, and dividends, the depreciation is considered to be “funded”. That is, on a cash basis, the operating results of the activity produce a cash surplus that can be spent to purchase assets, repay debt, or increase investments, or to lend to other activities as internal borrowing.

7.134 We noted several examples where the activity depreciation expense had not been covered by cash revenues, but the full depreciation figure was shown as a funding source for capital expenditure even though there was not enough cash to do this.

7.135 Conversely, there were instances where a local authority’s presentation of information in the Cost of Services Statement suggested that activities were being over-funded, and that funded depreciation had not been used or had not been clearly disclosed.

7.136 It is unclear whether this reflects a lack of understanding about how the funding works or is the result of attempts to simplify the presentation of information for the reader.

**Transfers into and out of reserves**

7.137 Local authorities maintain reserve balances for particular aspects of their operations that they keep track of differently, distinct from their general reserves.
For example:

- **rating reserves** – where any excess of funds resulting from a targeted rate are retained separately, to be spent in that area or on that type of asset in the future (conversely, any overspending is recorded for future recovery separate from other revenue sources); and

- **depreciation reserves** – some local authorities use funded depreciation only for asset purchases, and will therefore maintain records showing the balance of depreciation reserves available for future asset expenditure.

7.138 The disclosure of the transfer of funds into and out of reserves in the Cost of Services Statement was generally poor. In some instances, it appeared that reserves were simply a balancing figure in the Cost of Services Statement, or that the information seemed to reflect substantial draw-downs from reserves where not enough reserves were available at the start of or during the year. The movements were also inconsistent with information reflected in the Forecast Statement of Financial Position and/or Forecast Statement of Cash Flows.

**Split disclosure of revenue items**

7.139 We noted instances where GAAP revenue items, such as rates and development contributions, were shown either as a funding source only for overall net operating and capital requirements or split between operating and capital requirements. Those who support this split approach argue that local authorities can show where the revenue is to be spent, which potentially links more clearly to the revenue and financing policy and also shows more clearly those revenues that will be spent on capital expenditure, such as development contributions and components of Land Transport New Zealand subsidy revenues.

7.140 A result of this style of presentation is that any operating surplus shown for the activity is lower than the surplus prepared on a GAAP basis, while the overall financial result is the same. This moves the focus from any activity surplus to the funding decisions taken by the local authority.

7.141 However, this approach is inconsistent with the presentation of the statements of financial performance and financial position included elsewhere in the LTCCP. The approach does not follow GAAP, and sometimes similar revenue items are treated differently depending on their funding use.

7.142 In our view, the presentation of the Cost of Services Statement should include an “income statement” section, which includes all revenues that would be included in the Statement of Financial Performance. We also consider that the problems inherent in understanding an operating surplus in a local authority context are better resolved through an explanation at the overall financial statement level than through presenting operating revenue sources in this manner.
Aggregation of funding sources

7.143 In many instances, general rates were aggregated with separate rates as an overall rates figure, or they were aggregated with other general income sources such as interest and dividends as a general funds figure. Neither approach is ideal as they are a combination of unlike items. This practice can also obscure links to any funding levels included in the revenue and financing policy, making it more difficult for the reader to ascertain how funding decisions have been applied in practice.

Other presentation issues

Linking of policies with financial information

7.144 Ideally, there should be a clear and transparent link between the revenue and financing policy and the financial information included at activity level.

7.145 We recognise that this is not always practical because of the aggregation of multiple activities within a group. However, local authorities should try to make the link between the revenue and financing policy and the group of activities financial information as clear and transparent as possible.

Mixing operating and capital expenses

7.146 We noted at least one instance where a local authority included capital expenses for asset purchases with operating expenses in the draft LTCCP Statement of Proposal presented for audit. This was amended before the document was released for consultation.

7.147 Under GAAP, operating and capital expenses are treated differently – operating expenditure is included in the Statement of Financial Performance, while capital expenditure creates assets, which are included in the Statement of Financial Position. In addition to the practice noted in paragraph 7.146 not complying with GAAP, operating and capital expenditure often use different funding approaches. Aggregating the different types of expenditure can mask this difference and make the links to the revenue and financing policy less clear and transparent.

Inclusion of internal revenues and expenses within an activity

7.148 Many local authorities included internal revenues and expenses in their Cost of Services Statement. The statements typically included internal interest costs but also included items such as internal rental charges from property units.

7.149 The overall financial statements, such as the Statement of Financial Performance, should include only revenues and expenses that are external to the organisation. However, from a funding perspective, these are legitimate costs that should be shown at an activity level because they represent the actual cost of the activity.
They can be appropriately included in the Estimated Revenues and Expenses Statement, but should not be included in the Statement of Financial Performance. A reconciliation between the Cost of Services Statement and the overall financial statements assists in understanding how this information relates. We suggest that local authorities include this reconciliation in future LTCCPs to improve on current practice.

**Presentation of operating expenditure**

7.150 Local authorities adopted several approaches for disclosing operating expenses in the Cost of Services Statement within a group of activities. These were by:

- **township or ward** – in particular, where the funding approach for the activity differs depending on where the asset is located or the service is provided;

- **type of expense** (for example, operating expense, depreciation, and interest) – particularly useful for homogeneous populations where a single funding approach applies to the whole group of activities operating expenditure;

- **activity** – for example, sewerage reticulation and wastewater reticulation (functional expenses include all the relevant costs for that function, including depreciation and interest); and

- **a mixed approach** – where costs by activity or by ward were provided excluding depreciation, which was reflected as a separate line item.

7.151 While there is choice in which approach to adopt, some practices are better than others. For example, the mixed approach is not ideal.

7.152 The separate disclosure of depreciation is important, as it can then be linked to the funding used for capital expenditure. However, excluding it from the operating cost of the activity understates the expenditure, which is a particular issue when a group of activities includes multiple activities with differing funding sources. Where an activity or ward approach is adopted, depreciation could be disclosed in a note. Alternatively, an operating expenditure could be disclosed both by type and by activity or location.

**Showing three-year and 10-year information in separate parts of the LTCCP**

7.153 We saw examples where information on a group of activities showed three-year information only, with the balance or whole 10 years shown in a separate section of the LTCCP. Ideally, information on a group of activities should be provided in the same place, enabling the reader to see all of the information.

7.154 In some instances, the duplication of this information in two separate parts of the LTCCP added to the length of what was already a large document.
Suggested Cost of Services Statement layout

7.155 As previously noted (see paragraph 7.117), in conjunction with SOLGM, we produced a template and supporting guidance material to assist local authorities with disclosing financial information in the Estimated Revenues and Expenses Statement.

7.156 The template incorporates two distinct statements— an operating statement and a capital and reserves funding statement. The operating statement provides expenditure and revenue information consistent with GAAP-based recognition principles, while the separate capital statement is prepared on a cash basis.

7.157 One benefit from this layout is that the operating section is now consistent with the information presented in the Statement of Financial Performance. Physically splitting the two statements distinguishes between the accrual and cash funding approaches used in each section of the Cost of Services Statement, potentially reducing the difficulties that arise from combining the two different approaches in the same statement.

7.158 The layout of the statement and the principles behind it are also intended to make the disclosure of funding sources clear and transparent—in particular, for capital expenditure.

7.159 Some will argue that the prescriptive presentation and the additional funding disclosures proposed will be more onerous. However, the layout does more clearly present the activity’s funding source.

7.160 We recommend that local authorities adopt our proposed Cost of Services Statement layout shown in Figure 22. If local authorities consider that our proposed presentation does not appropriately reflect their requirements, we would appreciate the sector developing alternative presentation options.
### Figure 22
Our suggested layout for a Cost of Services Statement

#### Group/Activity – Operating Statement

**Operating Revenue**
- Activity Revenue $
- Targeted Rates $
- Development or Financial Contributions $
- General Rates $
- Other General Sources (e.g. Investment Income) $

**Total Operating Revenue** $

**Operating Expenditure**
- Expenditure (by Sub-activity/Type) $ 
  $ 
  $ 

**Total Operating Expenditure** $

**Operating Surplus (Deficit)** $
- Operating Surplus transferred to (specify) Reserve(s); or $
- Operating Deficit funded from (specify) Reserve(s) $

#### Group/Activity – Capital and Reserves Funding Statement

**Capital and Reserves Funding Requirements:**

**Capital Expenditure**
- Expenditure by Sub-activity $ 
  $ 
  $ 

**Total Capital Expenditure** $

- Loans Repaid $ 
- Operating Deficit $ 
- Transfers to General and Special Reserves $

**Total Funding Required** $

**Funded by:**
- Operating Surplus (via reserve) $
- Funding from Non-cash Expenses $
- Loans Raised $
- Transfers from General and Special Reserves $

**Total Funding Applied** $

Note: The suggested format has been prepared consistent with GAAP-based presentation for a Statement of Financial Performance. We acknowledge that there is a view that the Cost of Services Statement should begin with expenditure. In our view, either approach is acceptable.
Examples of Cost of Services Statements

Example 1

7.161 Figure 23 is reproduced from an adopted LTCCP to highlight some of the concerns that we identified. In Figure 24, we show this statement transferred to our suggested layout.

Figure 23
Example 1: Cost of Services Statement from an adopted LTCCP

<table>
<thead>
<tr>
<th></th>
<th>Forecast 2005/06 $000</th>
<th>Yr 1 2006/07 $000</th>
<th>Yr 2 2007/08 $000</th>
<th>Yr 3 2008/09 $000</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Operating Expenditure</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Expenditure</td>
<td>5,000</td>
<td>5,894</td>
<td>5,938</td>
<td>6,509</td>
</tr>
<tr>
<td>Interest</td>
<td>1,308</td>
<td>1,468</td>
<td>1,916</td>
<td>2,259</td>
</tr>
<tr>
<td>Depreciation of infrastructure</td>
<td>4,436</td>
<td>4,539</td>
<td>4,666</td>
<td>5,238</td>
</tr>
<tr>
<td>Depreciation of fixed assets</td>
<td>1</td>
<td>1</td>
<td>1</td>
<td>1</td>
</tr>
<tr>
<td><strong>Total Operating Expenditure (Note 1)</strong></td>
<td><strong>10,744</strong></td>
<td><strong>11,902</strong></td>
<td><strong>12,520</strong></td>
<td><strong>14,026</strong></td>
</tr>
<tr>
<td><strong>Funded by</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>General rates and other revenue</td>
<td>9,497</td>
<td>11,649</td>
<td>12,250</td>
<td>13,759</td>
</tr>
<tr>
<td>Grants and subsidies</td>
<td>1,200</td>
<td>243</td>
<td>249</td>
<td>230</td>
</tr>
<tr>
<td>Charges for services</td>
<td>47</td>
<td>10</td>
<td>21</td>
<td>37</td>
</tr>
<tr>
<td><strong>Total Funding of Operations (Note 3)</strong></td>
<td><strong>10,744</strong></td>
<td><strong>11,902</strong></td>
<td><strong>12,520</strong></td>
<td><strong>14,026</strong></td>
</tr>
<tr>
<td><strong>Capital Expenditure</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>New assets (Note 1)</td>
<td>5,979</td>
<td>8,211</td>
<td>7,514</td>
<td>8,000</td>
</tr>
<tr>
<td>Renewal assets</td>
<td>1,763</td>
<td>1,473</td>
<td>1,776</td>
<td>1,918</td>
</tr>
<tr>
<td>Vested assets</td>
<td>2,955</td>
<td>2,052</td>
<td>2,131</td>
<td>2,210</td>
</tr>
<tr>
<td><strong>Total Capital Expenditure (Note 2)</strong></td>
<td><strong>10,697</strong></td>
<td><strong>11,736</strong></td>
<td><strong>11,421</strong></td>
<td><strong>12,128</strong></td>
</tr>
<tr>
<td><strong>Funded by</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Development contributions</td>
<td>2,146</td>
<td>722</td>
<td>1,237</td>
<td>1,779</td>
</tr>
<tr>
<td>Vested assets</td>
<td>2,955</td>
<td>2,052</td>
<td>2,131</td>
<td>2,210</td>
</tr>
<tr>
<td>Loans</td>
<td>3,490</td>
<td>7,283</td>
<td>6,083</td>
<td>5,770</td>
</tr>
<tr>
<td>General rates and other revenue</td>
<td>1,806</td>
<td>1,661</td>
<td>1,970</td>
<td>2,119</td>
</tr>
<tr>
<td>Grants and subsidies</td>
<td>300</td>
<td>-</td>
<td>-</td>
<td>250</td>
</tr>
<tr>
<td>Capital funding account</td>
<td>-</td>
<td>18</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td><strong>Total Funding of Capital (Note 3)</strong></td>
<td><strong>10,697</strong></td>
<td><strong>11,736</strong></td>
<td><strong>11,421</strong></td>
<td><strong>12,128</strong></td>
</tr>
</tbody>
</table>

**Capital Expenditure**

|                       |                       |                   |                   |                   |
| Growth projects       | 1,780                 | 1,951             | 3,141             |                   |
| Other projects        | 9,956                 | 9,470             | 8,987             |                   |
| **Total capital expenditure** | **11,736**             | **11,421**        | **12,128**        |                   |
7.162 In Figure 23, rather than showing all operating revenues, the local authority splits operating revenues to show that the funding of both operating expenditure and capital expenditure are exactly the amount required to balance each area.

7.163 The operating section shows that all expenses are funded by cash revenues. Therefore, from a funding perspective for the 2006/07 year, there is $4,540,000 funded depreciation available to purchase assets, repay debt, lend to other activities, or invest.

7.164 The use of this cash should be reflected in the capital expenditure section of the Cost of Services Statement. However, in the example in Figure 23, there is no indication in the capital expenditure section of how the cash arising from the funded depreciation has been applied, including simply whether it had been included in a reserve. Although it is possible that the cash surplus is reflected in some manner through the internal loan in the loan line, this is not clear from the presentation. Additional disclosure to explain this would have been useful.

7.165 In Figure 24, the Cost of Services Statement has been set up in our suggested layout. The reformatted statement shows the surplus of $4,435,000 and how it has been applied to fund capital and reserves. In addition, the reader can also see the application of the cash-funded depreciation within the capital and reserves section.
## Figure 24

Cost of Services Statement using our suggested layout

### Operating Statement

<table>
<thead>
<tr>
<th>Description</th>
<th>$000</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Operating Revenue</strong></td>
<td></td>
</tr>
<tr>
<td>Activity Revenue</td>
<td>253</td>
</tr>
<tr>
<td>Targeted Rates</td>
<td>-</td>
</tr>
<tr>
<td>Development or Financial Contributions</td>
<td>722</td>
</tr>
<tr>
<td>General Rates and other revenue</td>
<td>13,310</td>
</tr>
<tr>
<td>Vested assets</td>
<td>2,052</td>
</tr>
<tr>
<td><strong>Total Operating Revenue</strong></td>
<td>16,337</td>
</tr>
<tr>
<td><strong>Operating Expenditure</strong></td>
<td></td>
</tr>
<tr>
<td>Expenditure</td>
<td>5,894</td>
</tr>
<tr>
<td>Interest</td>
<td>1,468</td>
</tr>
<tr>
<td>Depreciation</td>
<td>4,540</td>
</tr>
<tr>
<td><strong>Total Operating Expenditure</strong></td>
<td>11,902</td>
</tr>
<tr>
<td><strong>Operating Surplus (Deficit)</strong></td>
<td></td>
</tr>
<tr>
<td>Operating Surplus transferred to (specify) Reserve(s); or Operating Deficit funded from (specify) Reserve(s)</td>
<td>4,435</td>
</tr>
</tbody>
</table>

### Group/Activity XYZ – Capital and Reserves Funding Statement

Capital and Reserves Funding Requirements:

<table>
<thead>
<tr>
<th>Description</th>
<th>$000</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Capital Expenditure</strong></td>
<td></td>
</tr>
<tr>
<td>New assets</td>
<td>8,211</td>
</tr>
<tr>
<td>Renewal assets</td>
<td>1,473</td>
</tr>
<tr>
<td>Vested assets</td>
<td>2,052</td>
</tr>
<tr>
<td><strong>Total Capital Expenditure</strong></td>
<td>11,736</td>
</tr>
<tr>
<td>Loans Repaid</td>
<td>-</td>
</tr>
<tr>
<td>Operating Deficit</td>
<td>-</td>
</tr>
<tr>
<td>Transfers to General and Special Reserves</td>
<td>-</td>
</tr>
<tr>
<td><strong>Total Funding Required</strong></td>
<td>11,736</td>
</tr>
</tbody>
</table>

Funded by:

<table>
<thead>
<tr>
<th>Description</th>
<th>$000</th>
</tr>
</thead>
<tbody>
<tr>
<td>Operating Surplus</td>
<td>4,435</td>
</tr>
<tr>
<td>Funding from Non-cash Expenses</td>
<td>4,540*</td>
</tr>
<tr>
<td>Loans Raised</td>
<td>2,743</td>
</tr>
<tr>
<td>Transfers from General and Special Reserves</td>
<td>18</td>
</tr>
<tr>
<td><strong>Total Funding Applied</strong></td>
<td>11,736</td>
</tr>
</tbody>
</table>

*This layout shows the use of funded depreciation separately. It is possible that this remains in a reserve but is loaned back to that activity. However, the rationale for the use of funds in that way is unclear.
Example 2

7.166 Figure 25 is reproduced from an adopted LTCCP. The format is fundamentally the same as our standardised layout, except that rates are shown in the funding section rather than as a revenue item for the activity. This means that the operating section does not reflect GAAP operating revenues.

7.167 However, in this instance, the logic behind the funding mechanisms applied is unclear. The local authority shows that it is borrowing $2 million to fund aspects of the activity. This amount exceeds total capital expenditure for the year, and also, after considering other cash funding sources such as funded depreciation and the activity’s operating surplus, results in a transfer into reserves of $832,852 – essentially borrowing to put the money into the bank. This same observation also applies to 2008.

7.168 As well as adopting an appropriate way of presenting the Cost of Services Statement, a local authority must transparently disclose its funding decisions and, more fundamentally, ensure that the funding decisions are understandable to the reader.
Figure 25
Example 2: Cost of Services Statement from an audited LTCCP

**Sewerage**

<table>
<thead>
<tr>
<th></th>
<th>30 June 2007</th>
<th>30 June 2008</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Operating Income</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Fees and charges</td>
<td>4,998</td>
<td>5,153</td>
</tr>
<tr>
<td>Grants, subsidies &amp; donations</td>
<td>388,450</td>
<td>16,399</td>
</tr>
<tr>
<td>Sinking fund interest</td>
<td>4,822</td>
<td></td>
</tr>
<tr>
<td>Contributions</td>
<td>152,850</td>
<td>157,588</td>
</tr>
<tr>
<td><strong>Total Operating Income</strong></td>
<td>551,120</td>
<td>179,130</td>
</tr>
<tr>
<td><strong>Operating Costs</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Reticulation</td>
<td>502,645</td>
<td>876,507</td>
</tr>
<tr>
<td>Treatment and disposal</td>
<td>159,025</td>
<td>235,365</td>
</tr>
<tr>
<td><strong>Total Operating Costs</strong></td>
<td>661,669</td>
<td>1,111,873</td>
</tr>
<tr>
<td><strong>Net Cost of Service</strong></td>
<td>(110,549)</td>
<td>(932,742)</td>
</tr>
<tr>
<td><strong>Capital Expenditure</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Reticulation renewals</td>
<td>89,800</td>
<td>172,074</td>
</tr>
<tr>
<td>Land designayion / investigation</td>
<td>10,000</td>
<td>-</td>
</tr>
<tr>
<td>Pump station</td>
<td>1,000,000</td>
<td></td>
</tr>
<tr>
<td>Lake ferry sewerage system</td>
<td>625,000</td>
<td>1,340,300</td>
</tr>
<tr>
<td>Alternative disposal systems</td>
<td>60,000</td>
<td>82,480</td>
</tr>
<tr>
<td>Oxidation ponds</td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Total Capital Expenditure</strong></td>
<td>1,789,800</td>
<td>1,594,854</td>
</tr>
<tr>
<td><strong>Public Debt</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Loan repayments</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Sinking fund contributions</td>
<td>65,500</td>
<td>205,500</td>
</tr>
<tr>
<td><strong>Total Debt Requirements</strong></td>
<td>65,500</td>
<td>205,500</td>
</tr>
<tr>
<td><strong>Total Capital &amp; Debt</strong></td>
<td>1,855,300</td>
<td>1,800,354</td>
</tr>
<tr>
<td><strong>Funding Required</strong></td>
<td>1,965,849</td>
<td>2,733,096</td>
</tr>
</tbody>
</table>

**Funded By:**

<table>
<thead>
<tr>
<th></th>
<th>30 June 2007</th>
<th>30 June 2008</th>
</tr>
</thead>
<tbody>
<tr>
<td>Rates Income</td>
<td></td>
<td></td>
</tr>
<tr>
<td>General rates</td>
<td>545,654</td>
<td>1,059,323</td>
</tr>
<tr>
<td>Target rates</td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Total Rates Income</strong></td>
<td>545,654</td>
<td>1,059,323</td>
</tr>
<tr>
<td>Loans</td>
<td>2,000,000</td>
<td>4,500,000</td>
</tr>
<tr>
<td>Depreciation</td>
<td>234,202</td>
<td>317,194</td>
</tr>
<tr>
<td>Reserve transfers</td>
<td>(832,852)</td>
<td>(3,222,340)</td>
</tr>
<tr>
<td>Other</td>
<td>18,845</td>
<td>78,919</td>
</tr>
<tr>
<td><strong>Total Other Funding</strong></td>
<td>1,420,195</td>
<td>1,673,773</td>
</tr>
<tr>
<td><strong>Total Funding</strong></td>
<td>1,965,849</td>
<td>2,733,096</td>
</tr>
</tbody>
</table>
Example 3 – Alternative presentation options

7.169  At least one local authority (Far North District Council) included financial information in a Cost of Services Statement for years 1-3 of the LTCCP and provided operating revenue and expenditure, and capital expenditure and funding, as bar graphs for all 10 years for each activity. The graphs reflected all of the information within the Cost of Services Statement in a different form.

7.170  The approach met the requirement to provide information for years 4-10 as an outline and was also easy to understand, with trends and relative changes between years easily observed. This is another option that could be considered in presenting group of activities financial information.

7.171  Figure 26 shows an example of a Cost of Services Statement from the Far North District Council’s 2006-16 LTCCP.
Figure 26
Example 3: Cost of Services Statement from Far North District Council’s adopted LTCCP

<table>
<thead>
<tr>
<th>OPERATING REVENUE/EXPENDITURE</th>
<th>2006</th>
<th>2007</th>
<th>2008</th>
<th>2009</th>
</tr>
</thead>
<tbody>
<tr>
<td>Revenue</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Targeted Rates</td>
<td>4,457</td>
<td>5,419</td>
<td>5,691</td>
<td>6,663</td>
</tr>
<tr>
<td>Rates Other</td>
<td>56</td>
<td>58</td>
<td>60</td>
<td>63</td>
</tr>
<tr>
<td>Other Income</td>
<td>38</td>
<td>32</td>
<td>40</td>
<td>41</td>
</tr>
<tr>
<td>Salaries Projects</td>
<td>1,526</td>
<td>243</td>
<td>291</td>
<td>333</td>
</tr>
<tr>
<td>fees &amp; Charges</td>
<td>63</td>
<td>120</td>
<td>123</td>
<td>126</td>
</tr>
<tr>
<td>Development Contributions</td>
<td>0.022</td>
<td>1,022</td>
<td>1,022</td>
<td>1,022</td>
</tr>
<tr>
<td>Total Revenue</td>
<td>5,395</td>
<td>7,003</td>
<td>7,427</td>
<td>8,352</td>
</tr>
<tr>
<td>Expenditure</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Activity Expenses</td>
<td>3,273</td>
<td>3,873</td>
<td>4,020</td>
<td>4,288</td>
</tr>
<tr>
<td>Depreciation</td>
<td>0.90</td>
<td>1,155</td>
<td>1,267</td>
<td>1,390</td>
</tr>
<tr>
<td>Interest</td>
<td>0.022</td>
<td>568</td>
<td>807</td>
<td>997</td>
</tr>
<tr>
<td>Total Expenditure</td>
<td>4,673</td>
<td>5,675</td>
<td>5,014</td>
<td>4,675</td>
</tr>
<tr>
<td>Operating Profit (loss)</td>
<td>792</td>
<td>1,387</td>
<td>1,333</td>
<td>1,577</td>
</tr>
<tr>
<td>Applied to/from</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>development Contributions</td>
<td>533</td>
<td>1,022</td>
<td>1,022</td>
<td>1,022</td>
</tr>
<tr>
<td>Other Capital Reserve</td>
<td>150</td>
<td>345</td>
<td>291</td>
<td>333</td>
</tr>
<tr>
<td>Operating Profit/deficit/surplus/deduction</td>
<td>-1</td>
<td>20</td>
<td>20</td>
<td>20</td>
</tr>
<tr>
<td>Applications of Profit (loss)</td>
<td>792</td>
<td>1,367</td>
<td>1,333</td>
<td>1,577</td>
</tr>
</tbody>
</table>

Legend for the Years Ending 30 June

- Development Contributions
- Other Income
- Rates
- Salaries Projects
- Total Revenue

Diagram showing revenue and expenditure trends over 10 years.
Our conclusions

7.172 There remain considerable opportunities to improve the presentation and ease of understanding of Cost of Services Statement information in LTCCPs. Many statements do not clearly and transparently show the operating and capital expenditure, and revenue and funding sources chosen and, therefore, do not aid a reader’s understanding of how funding works within the local authority.

7.173 We suggest that the local government sector consider developing one or more standardised layouts and associated guidance for Cost of Services Statements, such as the one included in Figure 22.

7.174 The benefits from a more standardised approach include greater clarity around funding sources and links to the revenue and financing policy, increasing the likelihood that the reader of the LTCCP will find the funding choices to be logical, clear and transparent, and easy to understand.

Common issues with LTCCP Statements of Proposal

7.175 The majority of our audit work was undertaken in delivering our audit opinions on the LTCCP Statements of Proposal. Some other common issues arose at that stage involving:

- asset revaluations;
- price change; and
- adoption of NZ IFRS.

7.176 The majority of these issues were “fixed” by the local authority before finalising...
the LTCCP Statement of Proposal and associated draft LTCCP, so they did not carry over to the final adopted LTCCP.

7.177 We suggest that local authorities consider these common issues in the lead-up to the 2009-19 LTCCP. The issues arose in part because of pressures for timeliness, the breakdown of project control, and, in particular, the lack of internal quality review processes (see paragraphs 8.27-8.45).

Asset revaluations

7.178 For prospective information to be reasonable, local authorities had to consider the effect of the probable need to revalue assets – in particular, infrastructure assets – that are generally valued on a depreciated replacement cost basis.

7.179 Revaluations have a real effect on the main estimates, such as depreciation, and the assessment of sustainable funding of asset-based services.

7.180 Sixteen local authorities did not revalue correctly – either by not applying the revaluation process or by not estimating the effect of any revaluation requirement. A further 18 local authorities did carry out revaluations but did not disclose either the basis of the revaluation or that there were errors in the assumptions they made.

7.181 Revaluations are an integral part of compiling forecast financial information. While the current climate of a tight contractors’ market and increasing asset replacement costs remains, local authorities will be required to actively align their revaluation policy and assumptions about future price change to ensure that they maintain the integrity of the forecasts. In the current environment, the need to revalue is almost certain.

Price change

7.182 The sector established the need to estimate the effect of price change when it considered matters that would affect forecasting. We recognise, in particular, the lead taken in this matter by the SOLGM Financial Management Working Party.

7.183 For estimates to meet the reasonableness test outlined in FRS-42, preparers of LTCCPs had to account for the effects of price change.

7.184 In an issue similar to that of revaluations, 28 local authorities had not adequately applied the assumptions of price change. The issues related mainly to the consistent application of price change factors to all financial information.

7.185 This was the first time that local authorities had prepared financial forecasts on this basis. While there was substantial debate within the sector as to how to
actually apply the recommended rates when preparing the financial information, most local authorities capably dealt with the application of price change in the published information.

Adoption of New Zealand equivalents to International Financial Reporting Standards

7.186 Through our reports to Parliament on the effect of NZ IFRS, we have questioned the value of the changes in accounting standards ushered in by the adoption of these reporting standards. However, the LTCCP process has required the sector to adopt the NZ IFRS-based standards a year earlier than mandatory.

7.187 Our auditors considered that there would be a minimal real effect on forecast financial information for many local authorities. However, it was important that all local authorities considered the effects and adopted accounting policies consistent with NZ IFRS.

7.188 Thirteen local authorities had difficulty with this aspect of preparing the forecasts. This included not having a clear statement of the effects of conversion to NZ IFRS and not clearly identifying the changes in their Statement of Accounting Policies.

7.189 This matter should be less of an issue for the preparation of the 2009-19 LTCCPs, as the sector will have had three years’ experience dealing with NZ IFRS. However, it does highlight that adherence to GAAP during preparation of the LTCCP is important for the successful compilation and audit of financial forecasts.

Disclosures

7.190 A number of minor disclosure matters arose. While they were minor in nature, this reflects the pressure of preparation on individual local authorities and often the inability to include adequate and timely internal quality review of the draft LTCCP.

7.191 Twelve local authorities did not disclose the forecast effect of their rates remission policy – including not disclosing the reasons for, and the forecast financial effects (ideally at an activity level) of, the application of the policy.

7.192 Seventeen local authorities overlooked the requirement in FRS-42 to separately disclose the estimate for depreciation and interest expense. While a matter of detail, both of these disclosures are important for understanding the nature of a local authority’s cost structure (and therefore funding needs) and for understanding the changes in a local authority’s balance sheet.

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6 For example, Local government: Results of the 2004-05 audits, parliamentary paper B.29[06b].
7 In auditor terminology, the appropriate term is “not material”.
Summary

7.193 While these matters are related to GAAP, they do represent reasonably straightforward issues that were fixed by the respective local authority when our auditor raised them. However, such co-operation also reflects a transaction cost to the local authority that is higher than if its own processes had adequately dealt with the matters in the beginning.

7.194 As our auditors were also giving these messages, it often cast them in the light of being solely focused on compliance with the Act. The risk of seeing them in this light could have been avoided if local authorities had implemented and maintained sound project management practices for effective and timely internal quality review of the draft documents.
Part 8

LTCCP audit opinions and timeliness of adoption

8.1 Our core reporting responsibility is to effectively report on whether the draft LTCCP (in the LTCCP Statement of Proposal) and the final LTCCP are fit for purpose – that is, whether they meet the intended purposes of the Act and are of ongoing usefulness to the local authority and its community. We express “being fit for purpose” in our overall audit opinion:

In our opinion the LTCCP ... provides a reasonable basis for long term integrated decision-making by the [council] and for participation in decision-making by the public and for subsequent accountability to the community about the activities of the [council].

8.2 The audit opinion emphasises that the LTCCP is future-focused and is relevant in assessing the local authority’s actions in terms of:

• its expressed intentions outlined in the LTCCP;
• enabling the local community to participate in future decision-making, with reference to the LTCCP; and
• a benchmark against which to measure actual services provided to the community by the local authority.

8.3 Our audit opinion then concludes on whether the necessary elements are in place to support this assessment. We conclude separately, but in support of the overall opinion, on the:

• information’s compliance with the legislative requirements of the Act – in other words, that the requisite information has been provided;
• adequacy (in terms of quality) of the underlying and supporting information used;
• reasonableness of the assumptions used;
• adherence to appropriate accounting practice when preparing prospective information; and
• suitability of the forecast information and performance measures as a means of assessing the performance of the local authority.

8.4 The majority of our fieldwork was carried out in preparing to deliver an audit opinion on the LTCCP Statements of Proposal. The review of the final LTCCPs centred on observing and assessing the results of a local authority’s process of consultation with its community and the subsequent decisions made by that local authority to finalise its LTCCP.

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1 This is a direct quotation from our audit opinion on the final LTCCP. The same wording is used in the LTCCP Statement of Proposal audit opinion.

2 Section 96(1) of the Act notes that an LTCCP is “a formal and public statement of the local authority’s intentions”.

3 This is described in the Act as generally accepted accounting practice, which is outlined in FRS-42.
8.5 The Act does permit a “shortened” form of audit opinion to be provided on the final LTCCP. Section 94(2) of the Act enables the form of the opinion to be limited to a confirmation of, or amendment to, the LTCCP Statement of Proposal opinion. However, in all cases, we issued a full audit opinion on the final LTCCP, rather than issue any abbreviated form. We adopted this approach because the finalised LTCCP (including its audit report) stands in its own right.

8.6 Both the LTCCP Statement of Proposal and the audit opinion on the statement become obsolete once the final LTCCP is adopted. Most local authorities removed their LTCCP Statement of Proposal from their websites when they published their final LTCCP.

8.7 In our view, this approach by local authorities was logical and required us to include a full audit opinion on the final LTCCP. The adopted LTCCP remains in force for three years.4

Unqualified and non-standard audit opinions

8.8 There are 85 local authorities in New Zealand. This meant that we issued 85 separate audit opinions on the 2006-16 LTCCP Statements of Proposal and then, after the local authorities consulted with their communities and finalised their LTCCP, we issued a further separate 85 audit opinions.

8.9 The bulk of our audit work was carried out in delivering the audit opinion on the draft LTCCP, which is contained in the LTCCP Statement of Proposal. The audit opinion on the final LTCCP also required substantive work. While, in general, the amount of work on the final LTCCP was less, substantial audit effort was required in some instances.

8.10 We were able to issue our standard unqualified audit opinion for 72 of the 85 LTCCP Statements of Proposal and for 68 of the final LTCCPs. Overall, we see this as a positive outcome. Clearly, the audit opinion is determined on the evidence available in each situation. However, it does indicate that the majority of local authorities were able to issue final LTCCPs that are useful for ongoing planning, decision-making, and accountability by the local authority concerned — in other words, information that is fit for purpose.

8.11 A non-standard audit opinion is one that contains:

- a qualified opinion; and/or
- an explanatory paragraph.5

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4 Section 93(3) of the Act.
5 For further discussion on non-standard audit opinions, see our report Local government: Results of the 2004-05 audits, “Part 1.7 Non-standard audit reports issued”, parliamentary paper B.29[06b].
The Appendix summarises the non-standard audit opinions that we issued for both the LTCCP Statements of Proposal and the final LTCCPs.

The analysis of non-standard audit opinions shows that, generally, the opinion received on the LTCCP Statement of Proposal remained after the LTCCP was finalised. However, an analysis of overall non-standard opinions shows that two of the 13 local authorities that received non-standard opinions on their LTCCP Statement of Proposal were able to have that qualification removed at the time they issued their final LTCCP.

A further eight local authorities’ final LTCCPs were qualified because of inadequacies in their LTCCP Statement of Proposal Summary, which is required for effective consultation. Two of these had already received a non-standard audit opinion on their Statement of Proposal. This meant that the overall number of non-standard audit opinions increased from 13, by a net increase of six, to 17 on the final LTCCPs.

For most of the local authorities that were issued a non-standard audit opinion, the matter giving rise to the qualification was of such a nature that it could not be remedied in time. For instance, those local authorities that did not have adequate asset information would generally be unable to correct the absence of relevant information within the limited time available between the LTCCP Statement of Proposal and adoption of the final LTCCP.

Our conclusions

We are responsible for reporting our audit opinion on the LTCCP. We have no mandate to require any action of the local authority – particularly where we report a qualified opinion. Where local authorities received a non-standard audit opinion, they were still able to continue to adopt the LTCCP and, as it is closely allied to the planning process, set their rates for the next financial year.6 The LTCCPs with their defects are still “in force”.

This means that some local authorities have set their strategic direction based on inadequate underlying information and with levels of service that probably cannot be delivered by the proposed level of expenditure. This position is accentuated for those local authorities we issued with a “full adverse” audit opinion. In our view, these LTCCPs were not fit for purpose.

In some situations, local authorities have indicated they will try to rectify the issues raised by our audit opinion before the next LTCCP for 2009-19. This will probably require them to pursue an amendment to the existing LTCCP.

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6 Through section 95(4) of the Act, the LTCCP also constitutes the annual plan in its first year of the LTCCP’s application. The annual plan is closely associated with setting rates.
8.19 The non-standard audit opinions generally reflect the cumulative effect of a number of matters. An LTCCP is required to be integrated. Consequently, an opinion matter may affect a range of aspects within the LTCCP. The lack of adequate underlying information means that not only is the prospective financial information unsupported but also the costs of delivering desired levels of service cannot be demonstrated. Further, it probably also means that funding approaches and levels are less certain and, as shown in a number of our opinions, often overall financial prudence cannot be demonstrated.

8.20 We consider these matters to be of serious concern for the ratepayer, as well as undesirable.

8.21 We note that the local government sector is beginning to revise its understanding and definition of good practice. It is focusing on those areas where the majority of issues arose during the 2006-16 LTCCP round. These were:
- underlying information (with specific emphasis on asset management planning);
- performance frameworks;
- assessing levels of service; and
- a local authority’s contribution to community outcomes through its activities.

8.22 The sector groupings dealing with these matters intend to work with the sector before the next round of LTCCPs for 2009-19 to achieve improved planning and information for their ratepayers and their communities. We endorse this process, and, where it is relevant, we are working with these groupings to develop improvements.

8.23 The clear implication of this work is that the sector will define and expect a higher level of acceptable practice in these areas. To the extent those changes are consistent with our statutory role as auditor, our future audit opinions will report against the improved standard that the sector expects of its members when the next LTCCPs, due to start on 1 July 2009, are prepared and consulted on.

8.24 We note the eight audit opinions on final LTCCPs that received a “minor qualification” for producing inadequate summaries of the LTCCP Statement of Proposal. We were surprised at the difficulty local authorities had in meeting the requirement.

8.25 Summaries are pivotal to consultation. LTCCPs are substantial documents, and the ability to summarise the major matters is important for local authorities to effectively communicate and to enable debate within the community. Local

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7 Section 89 of the Act. The summary is required to summarise the “major matters” in a form determined by the local authority. This resonates with our comments in the Auditor-General’s Overview about the “right debate”.

8 Section 89(c) of the Act.
authorities are not unused to such requirements. Consequently, we were disappointed with this result.

8.26 None of the qualifications affected our overall audit opinion, but the possibility remains in the future that a significant deficiency could affect our view of the overall reasonableness of the final LTCCP in meeting its purpose.

**Timeliness of adoption**

8.27 The development of an LTCCP is a substantial undertaking – arguably one of the largest from a corporate perspective. It requires co-ordination of effort and resource from throughout the local authority and the linking of substantial information sources.

8.28 Obvious examples include:

- Growth in population affects most activities of a local authority. The assumption adopted on growth in population should be consistently used throughout the local authority.
- Underlying asset information (such as maintenance cycles and renewal profiles) affects not only asset management but also financial projections.

8.29 We have noted that the sequencing of information is important. Because it is central to the development of an organisation-wide document, the sequencing of information is ideally developed on a council-wide basis. It is at its most effective when combined with a sound project management process.

8.30 We asked local authorities to outline the basis they used to prepare the draft LTCCP in the self-assessment process we began in mid-2005. The results indicated that the sector was generally adopting a project management approach to preparing the draft LTCCPs and, indeed, for the final adoption of the LTCCP after its consultation stages.

8.31 The sector struggled to meet the deadlines it initially projected. In general, we formed the view that few local authorities actually adhered to project management principles.

8.32 The evidence to support this view was that:

- the majority of local authorities were unable to complete draft LTCCPs by the date they projected;
- the minimal time available to our auditors between preparation and adoption of the draft LTCCPs (and associated LTCCP Statements of Proposal);
- the lack of time for local authorities to carry out their own quality control processes before releasing information to our auditors; and
8.33 By October 2005, there were signs that the sector would find it difficult to meet LTCCP completion deadlines. Matters still outstanding at that date were:

- often incomplete asset management plans or information;
- some local authorities yet to decide on an appropriate approach to developing the LTCCP – in particular, deciding on appropriate software to build the LTCCP financial model; and
- a general concern that performance frameworks – including levels of service – were incomplete.

8.34 Despite these incomplete matters, local authorities still projected that their LTCCP Statements of Proposal, containing the draft LTCCPs, would be generally complete and cleared by the auditor by 12 April 2006. This was the date we had calculated as optimal to enable a local authority to consider the auditor’s report, make changes if necessary, and publish the LTCCP Statement of Proposal for consultation. Further, this enabled adequate time for actual consultation and enough time for a local authority to consider those submissions before adopting the final LTCCP by 30 June 2006.

8.35 At 18 January 2006, all but seven of the 85 councils were predicting that their LTCCP Statement of Proposal would be completed in time for an audit opinion to be given and to meet the recommended time of 12 April 2006. In reality, at 12 April 2006, we were still waiting to receive 12 LTCCP Statements of Proposal for initial review, and a further 10 were still in the process of clearance.

8.36 The last two LTCCP Statements of Proposal were not cleared until 30 June 2006 and 19 July 2006 respectively.

8.37 There was a similar scenario for the adoption of the final LTCCP. Because of the number of local authorities going to consultation later, many were forced to truncate consideration of submissions (once the statutory minimum period for consultation and receiving submission was concluded) and adopt the final LTCCP close to or on 30 June 2006.

8.38 Seven final LTCCPs were adopted after the statutory required date of 30 June 2006. Four were adopted in July 2006, two in August 2006, and the last outstanding LTCCP on 14 September 2006.

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9 We discussed optimal times to enable adequate consideration of issues by local authorities in our LTCCP newsletter No. 8, issued in December 2005.

10 Section 83(2) requires that this phase take at least one month.
While these late adoptions breached the statutory requirement, we generally supported these local authorities taking their time to get their documents “right” rather than rushing them through to meet the statutory deadline. This view was based on the importance of the LTCCP in setting direction rather than a disregard for a statutory provision. In all instances, the local authorities acknowledged they had breached the statutory timeline.

From our analysis of the seven final LTCCPs adopted after 30 June 2006:

- two had significant strategic issues that needed adequate analysis — in particular, after the calling for, and hearing of, submissions;
- one was the result of a senior staff change in the lead-up to the preparation and adoption of the LTCCP Statement of Proposal (containing the draft LTCCP);
- and
- four were late, in our view, because of either poor processes or inadequate information.

Our conclusions

The development of an LTCCP is a significant local authority-wide undertaking, requiring the sequential development of various sources of information from different parts of the organisation.

It is an important statutory responsibility that sets the immediate direction of the local authority for the medium term.

Some local authorities managed the process well, planning and adhering to timetables. Their project planning process generally gave the ratepayer and broader community appropriate time to be involved in consultation and deliberation.

Regrettably, the majority of local authorities did not appear to maintain adequate project management disciplines, and most of them had to delay their intended adoption dates for either their LTCCP Statement of Proposal or their final LTCCP. This risked rushing the process and truncating the time needed for optimal consideration of all aspects of this important planning process.

Clearly, there is a need for local authorities to address the issue of timeliness of LTCCP preparation to ensure adequate participation by the community in their decision-making process.

Audit fees

Consistent with professional audit practice, we sought to advise local authorities of our estimate of fees in advance of auditing the LTCCP. Usually, the fee estimate
would stand, subject to “client performance” or potentially (and less likely) that the fee estimate compared to actual cost was different to the effective time taken to do the job.

8.47 In all circumstances, we sought to align the setting of the LTCCP fee with our usual letter of undertaking process and provided support systems for local authorities wanting further information on fees.

8.48 However, all of those involved faced a unique situation. Based on our research, there was no precedent either locally or internationally for estimates of an audit of 10 years of prospective information, as required in the LTCCP.

8.49 Our approach was to build onto our methodology development processes with an analysis and estimate of the likely fees associated with the audit. Both the methodology development and fees assessment drew on the collective experience of all three audit service providers11 that carry out audits in the local government sector on the Auditor-General’s behalf.

8.50 A task group, comprising representatives from the audit service providers, considered the likely fee, based on the assumptions that each local authority would:

- implement adequate project management and quality control over their LTCCP development processes;12
- develop underlying information, assumptions, and performance frameworks in a timely manner; and
- make draft documents available with adequate time for elected member input and subsequent auditor review and provision of an audit opinion.

8.51 On this basis, the task group estimated that the LTCCP audit fee would range between 50% and 65% of the annual 2004/05 audit fee. (Figure 27 shows the range of audit fees). There is an element of economy of scale to the assessed fee: the larger local authorities have an estimate tending to 50% of the audit fee, while the smaller local authorities converged towards the 65% level.

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11 Audit New Zealand, Deloitte, and Ernst & Young.
12 As previously noted, this assumption was reasonable because the sector was generally indicating through the self-assessment process that it was implementing relevant controls.
Figure 27
Range of estimated fees for LTCCP audit in 2006

<table>
<thead>
<tr>
<th>Band</th>
<th>Number of councils</th>
</tr>
</thead>
<tbody>
<tr>
<td>$20,000-29,999</td>
<td>9</td>
</tr>
<tr>
<td>$30,000-39,999</td>
<td>34</td>
</tr>
<tr>
<td>$40,000-49,999</td>
<td>20</td>
</tr>
<tr>
<td>$50,000-59,999</td>
<td>12</td>
</tr>
<tr>
<td>$60,000-69,999</td>
<td>3</td>
</tr>
<tr>
<td>$70,000-79,999</td>
<td>2</td>
</tr>
<tr>
<td>$80,000-89,999</td>
<td>2</td>
</tr>
<tr>
<td>$90,000-99,999</td>
<td>1</td>
</tr>
<tr>
<td>$100,000-109,999</td>
<td>-</td>
</tr>
<tr>
<td>$110,000-120,000</td>
<td>2</td>
</tr>
</tbody>
</table>

(Median $39,964)

8.52 We published the general basis for our fee estimates through our LTCCP newsletter for the sector and informed each local authority directly. While our auditors had some minor discretion to seek to vary the fee estimate for known issues, few did so because of the inherent uncertainty in predicting the fee and the uniqueness of the situation.

8.53 The collective fee estimate totalled nearly $3,700,000.

8.54 In association with the estimated fees, the task group also estimated the resource requirement on the three audit service providers based on auditor hours. Overall, it was estimated that about 23,000 hours would be required to undertake all 85 engagements.

8.55 The assumptions on which we based the resource and fee estimates were generally over-optimistic, with the sector generally being unprepared and late in delivering required draft documents. This had the inevitable effect of increasing the hours of audit teams and the fee costs of the audits.

8.56 The audits actually required more than 34,000 auditor hours (a 48% increase over the estimate). In addition, more input was required by senior members of the
audit team than anticipated – in particular, the input at partner/audit director level was proportionately greater than estimated. Individual auditors began steps to recover costs for the extra hours.

8.57 The Auditor-General reviewed the costs incurred, revenue generated, and reasons for the variations on estimates. It was generally felt that substantial time had been spent discussing with local authorities their statutory obligations under the Act and, in effect, assisting them to implement the new planning provisions. Auditors devoted substantial time to these discussions with individual local authorities in the period leading up to Christmas 2005. However, most of the time taken related to the various states of preparedness of individual local authorities.

8.58 In conjunction with the audit service providers, we agreed that, other than in a few exceptional cases, the auditors would not pursue any additional fee over and above the original estimate.

8.59 The decision not to seek additional fees was welcomed by the sector. It was recognised that the auditors had contributed significantly to the development of local authorities’ strategic planning approaches and, generally, the fee write-off enabled individual local authorities to learn from the first round of audited LTCCPs without the “penalty” of extra fees.13

8.60 While recognising this benefit to the sector, we have indicated that the sector should not expect that our approach to auditing the 2009-19 LTCCPs will be similar. In short, local authorities need to act on what they have learned from their experiences in producing the 2006-16 LTCCP and review their processes to ensure that the changes we have indicated as necessary are actually implemented for the 2009-19 LTCCP round.

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13 There was a substantial range of fee write-off related to each local authority. A few local authorities largely delivered “on time” and with sufficient quality that the LTCCP audit could be brought within the initial fee estimate. There was also a high correlation between these local authorities’ 2006-16 LTCCPs and the audit confidence that could be taken into the audit of their 2005-06 annual report. In these few instances, the auditors were able to discount their audit fees for the 2005/06 annual report.
Appendix

Description of non-standard audit opinions issued

Full adverse audit opinions

Carterton District Council

Overall, Carterton District Council’s LTCCP did not fulfil its statutory purposes (see section 93(6) of the Act) – it was not, in our view, fit for purpose. This was our conclusion at the time of preparation of the LTCCP Statement of Proposal and the final LTCCP. The underlying records were insufficient to support the prospective information – both the prospective information relating to the levels of service that the council will provide the ratepayer, and the associated operational and capital expenditure required to be incurred.

The inadequate underlying information predominantly related to infrastructure asset information. The inadequacy of the information means that the council’s costs could be materially misstated. Further, it remains uncertain whether the council can deliver the levels of service agreed with the community. The council also could not adequately identify that all the funding came from appropriate sources for the individual groups of activities. Because of the cumulative effect of these fundamental issues, we were unable to affirm that the plan is financially prudent (see section 101 of the Act).

(In the 2006/07 financial year, Carterton District Council agreed to amend its 2006-16 LTCCP to rectify the deficiencies identified in our audit opinion. Because of the extent and quality of this work to upgrade the underlying information supporting the LTCCP, our auditor was able to amend this adverse opinion on the 2006-16 LTCCP and issue an unqualified opinion on the LTCCP Statement of Proposal. Consultation on the amendment was held concurrently with the council’s 2007/08 Annual Plan consultation process.)

Invercargill City Council

Overall, Invercargill City Council’s LTCCP did not fulfil it statutory purposes – it was not, in our view, fit for purpose. This was our conclusion at both the time of preparation of the LTCCP Statement of Proposal and the final LTCCP. We formed this view based on the cumulative effects of either inadequate or inconsistently applied underlying information. This underlying information predominantly was infrastructure asset information associated with the council’s major service activities of water and roading. It is not possible to affirm that the level of proposed expenditure over the life of the plan will deliver the levels of service or that the expenditure was not materially misstated. Further, the performance information could not be adequately linked to the disclosed performance...
measures. The council also could not identify that all funding of individual groups of activities came from appropriate sources of funding. These issues are fundamental, and we were unable to confirm that the LTCCP was financially prudent.

While this matter did not affect our overall audit opinion, we did note that the summary of the LTCCP Statement of Proposal did not alert the reader to our views about the inadequacy of the underlying information. As this is important for the readers to know, we consequently formed the view that the summary only partially complied with the statutory responsibility to disclose all major matters from the LTCCP Statement of Proposal (see section 89(a) of the Act).

Timaru District Council

At the time of preparation of Timaru District Council’s LTCCP Statement of Proposal, we qualified our overall audit opinion because the prospective financial information assumed that the effect of price changes during the 10 years of the plan was nil. In our view, this meant the financial information provided in the prospective financial information (including the groups of activities) was not based on the best information currently available to the council, nor could it demonstrate prudent financial management in terms of section 101 of the Act. The council did provide supplementary information with the LTCCP Statement of Proposal, in which the prospective Income Statement was adjusted for future price changes. However, in our view, the price change assumptions were applied inconsistently and rendered the supplementary information inadequate. Consequently, we concluded that this additional information was incomplete and could be misleading.

However, between the LTCCP Statement of Proposal and finalisation of the LTCCP, the council did provide revised supplementary information which indicated that the future rates requirement was cumulatively understated by $33.7 million. As a result of the revised supplementary information provided by the council, we were able to affirm that the plan – if adjusted for the effects of price changes – is financially prudent. This meant that, while our overall audit opinion retained its qualification on the adequacy of the prospective financial information provided, we could – with the aid of the revised supplementary information – conclude positively on the prudence of the overall final LTCCP.

Waitomo District Council

We qualified our audit opinion on Waitomo District Council’s LTCCP because we formed the view that the adopted plan was not sustainable and, therefore, not
Appendix

Description of non-standard audit opinions issued

financially prudent. As a result of this conclusion, we consider that the LTCCP is not fit for purpose. This was our conclusion at both the time of preparation of the LTCCP Statement of Proposal and the final LTCCP. While the council’s LTCCP acknowledges substantial issues in delivering the desired levels of service, it contained a funding mix – involving rates increases and, importantly, debt – that was unsustainable. We saw no evidence to indicate that the proposed strategy of increasing debt would correct either within or after the end of the LTCCP’s 10-year horizon.

Although it did not affect our overall audit opinion, we did note that the summary of the LTCCP Statement of Proposal did not alert the reader to our views about the inadequacy of the underlying information. As this is important for the readers to know, we consequently formed the view that the summary only partially complied with the statutory responsibility to disclose all major matters from the LTCCP Statement of Proposal.

**Except-for audit opinions**

**Central Otago District Council**

We qualified our audit opinion on Central Otago District Council’s LTCCP because the council did not follow its own accounting policies in preparing the prospective financial statements. The accounting policies of the council state that fixed assets will be periodically revalued. Estimated future revaluations were not incorporated into the prospective financial information. This affects forecast asset values and the estimate of depreciation. The implication of this omission is that both asset values and depreciation are likely to be misstated.

The audit opinion on the LTCCP Statement of Proposal was further qualified as the statement did not apply the council’s current development contribution policy. In preparing the draft LTCCP, the council elected to use an older policy, which meant that the forecast financial statements were not consistent with the policies on which they were prepared. The council chose to follow its adopted policy when finalising the LTCCP. This enabled this aspect of the LTCCP Statement of Proposal qualification to be removed.

**Gisborne District Council**

Gisborne District Council’s LTCCP Statement of Proposal and final LTCCP were qualified as neither document clearly set out the council’s desired levels of service. Consequently, the LTCCPs did not establish an adequate link between forecast expenditure and what the council was trying to achieve through that expenditure. This affected our view on the reasonableness of the underlying information and the meaningfulness of the performance measures.
Kaikoura District Council

Kaikoura District Council did not include asset revaluations in its prospective financial statements of the LTCCP, which implies that asset values and depreciation are likely to be misstated. In addition, the council had not completed a water and sanitary services assessment, as required by section 125 of the Act. Both these matters affected the council’s LTCCP Statement of Proposal and final LTCCP.

Another matter that affected the council’s LTCCP Statement of Proposal was that the prospective financial statements did not adequately account for an estimate of vested assets. This matter was rectified by the final LTCCP, so it was omitted from the final non-standard audit opinion.

Napier City Council

Napier City Council chose not to adjust its forecast capital expenditure for the effect of estimated future price changes. Consequently, the probable effect is that projected funding requirements in respect of that expenditure are understated. This means that the LTCCP does not reflect the best information available to the council, in relation to this capital expenditure and its funding requirements.

This matter also affected the LTCCP Statement of Proposal, which the council used to consult with its community.

Matter of emphasis audit opinion

Porirua City Council

The prospective statement of financial performance for Porirua City Council projected successive losses. This matter applied to both its LTCCP Statement of Proposal and the final LTCCP. Operating revenue had not been set at levels sufficient to match operating expenditure. These deficits were attributed to the council resolving not to fund depreciation on infrastructure assets. However, the council considered that such forecasts still represented a financially prudent position.

The position adopted by the council is important in the consideration of what is an equitable allocation of responsibility for funding between generations, and we considered it important to disclose it.

We note that the matter of emphasis is a non-standard audit opinion, but does not represent an actual qualification of the forecast information. Rather, it draws the reader’s attention to a matter of significance in reading and assessing the
information provided by the council and the strategies on which those forecasts are based.

**Minor qualifications that did not affect our overall audit opinion on the LTCCP**

**Chatham Islands Council and Dunedin City Council**
Both Chatham Islands Council and Dunedin City Council failed to complete a water and sanitary services assessment, as required by section 125 of the Act. This affected both of their LTCCP Statements of Proposal and final LTCCPs.

**Horizons Regional Council, Northland Regional Council, Selwyn District Council, Tasman District Council, Waimate District Council, Waitaki District Council**
In our view, the summaries prepared by these councils and used to consult with the public over the draft LTCCP were inadequate. While this matter did not affect our overall audit opinion on the final LTCCP, the summary is intended to provide important information for the readers. We concluded that the summary only partially complied with each council’s statutory responsibility to disclose all major matters from the LTCCP Statement of Proposal (see section 89(a) of the Act).

This matter only affected the final LTCCP and not these councils’ LTCCP Statements of Proposal.

**Non-standard audit opinions on the LTCCP Statement of Proposal that did not carry forward to the opinion on the final LTCCP**

**Horowhenua District Council**
Horowhenua District Council’s LTCCP Statement of Proposal was non-standard because, in our view, it failed to reasonably estimate development contribution revenue arising from a fair application of the council’s adopted policy. Rather than include a cumulative estimate of development contributions amounting to $987,000, no amount was included.

The matter was corrected for the final LTCCP so our audit opinion was unqualified.

**Stratford District Council**
Stratford District Council’s LTCCP Statement of Proposal received a non-standard audit opinion on the basis that it inconsistently outlined the desired levels of
service and the associated performance measures. It did not present a complete forecast and performance framework to its community.

The council chose to review the information provided in the final LTCCP. Because of the improvements that were made, we were able to issue an unqualified audit opinion on the final LTCCP.
Publications by the Auditor-General

Other publications issued by the Auditor-General recently have been:

- Local government: Results of the 2005/06 audits – B.29[07b]
- Effectiveness of the New Zealand Debt Management Office
- Statements of corporate intent: Legislative compliance and performance reporting
- Department of Labour: Management of immigration identity fraud
- Assessing arrangements for jointly maintaining state highways and local roads
- Sustainable development: Implementing the Programme of Action
- New Zealand Customs Service: Collecting customs revenue
- Ministry of Health and district health boards: Effectiveness of the “Get Checked” diabetes programme
- Guidance for members of local authorities about the law on conflicts of interest
- Managing conflicts of interest: Guidance for public entities
- Te Puni Kōkiri: Administration of grant programmes
- New Zealand Qualifications Authority: Monitoring the quality of polytechnic education
- Annual Plan 2007/08 – B.28AP(07)
- Waste management planning by territorial authorities
- Central government: Results of the 2005/06 audits – B.29[07a]
- Department of Internal Affairs: Effectiveness of controls on non-casino gaming machines
- Controlling sensitive expenditure: Guidelines for public entities
- Performance of the contact centre for Work and Income

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