

MAY 2002

LOCAL GOVERNMENT NEWSLETTER

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Local Government Seminars

We're repeating our highly successful series of financial reporting and accounting seminars. Topics will include financial reporting changes and performance reporting trends as well as sector specific issues. Diary these dates:

Christchurch	June 24
Auckland	July 3
Palmerston North	July 4

and watch our website
www.auditnz.govt.nz for more details



The Local Government Bill – it may not rule yet, but it is certainly dominating Councillors, Chief Executives and Senior Managers' thinking. When will it be reported back to the House? Will it be passed before the election? These are the usual questions posed during our many discussions with the sector. While many of the issues in the Bill are still being robustly debated – Part 5, for example – many councils appear anxious to start work now on the expected regime. We

are fielding a number of calls on preparing strategies and LTCCPs.

The Bill also promotes the concept of Triple Bottom Line Reporting or, as it is increasingly known, Sustainable Development Reporting. In this edition, our specialist Leanne Holdsworth looks at the Bill through an SDR lens.

As well as the Local Government Bill, councils also now have the Rating Act to wrestle with. In the midst of these challenges, comes the annual "audit round". This year sees the introduction of the new Financial Reporting Standard 3: Accounting for Property, Plant & Equipment. FRS-3 has been much debated and was the core subject of our well-attended accounting seminars last year. The focus now is implementation. This issue has two articles on assets not generally recognised under SSAP 28 but which must be recognised for 2002 under FRS-3 – heritage assets and land under roads. The question is what value to put on these? Brian Smith outlines the broad view on heritage assets, augmented by a think piece on our website www.auditnz.govt.nz, while John Dunckley of DTZ New Zealand comments on valuing land under roads.

All in all, 2002 looks like being a challenging year for councils and auditors alike!

Bruce Robertson
Leader, Local Government Sector Group

SUSTAINABLE DEVELOPMENT AND THE LOCAL GOVERNMENT BILL

The Local Government Bill redefines local authorities' purpose in a way that turns the spotlight on the emerging area of sustainable development. Defined by the World Commission on Environment and Development as "development that meets the needs of the present without compromising the ability of future generations to meet their own needs", the practice of sustainable development involves acting in a way that maximises the integrated social, environmental, cultural and economic impacts of an entity's operations both now and in the future.

The Bill, currently at select committee stage and due to be reported back in July, draws heavily on the principles behind sustainable development.

Examples of this include the definition of the purpose of local government in Clause 8:

To enable local decision-making, by, and on behalf of, individuals in their communities, to democratically promote and action their social, economic, environmental, and cultural well-being in the present and for the future

and Clause 62, which states the key principle of decision-making is:

(d) a local authority must, in making significant decisions, assess whether the benefits in terms of the social, economic, environmental, and cultural well-being of the community are sustainable

Clause 62(b) requires local authorities to think in terms of "community outcomes" and Clause 62(e) requires them to "seek" to make decisions which:

ensure that community outcomes are promoted in the most integrated and efficient manner possible, in terms of both the financial costs and benefits and the non-financial costs and benefits of different options

The Bill doesn't lay down a requirement that local authorities start preparing sustainable development reports. But it does promote sustainable development reporting (also known as triple bottom line reporting) through its references to a broader ambit of social, environmental, cultural and economic performance – likely to encourage proactive councils to consider how that performance is best measured and reported.

The Ministry for the Environment is currently funding a project facilitated by Audit New Zealand on triple bottom line reporting within local authorities. Results of this project will be publicly available some time after 30 June 2002.

However, should you like more information about the project or sustainable development, please contact Leanne Holdsworth, Audit New Zealand's Senior Manager, Sustainable Development.

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ACCOUNTING FOR HERITAGE ASSETS

The Office of the Auditor-General has signalled that more attention must be paid to recognition of heritage assets in financial statements.

This raises valuation and depreciation issues. FRS-3 – Accounting for Property, Plant and Equipment – states that heritage assets that meet the definition of property, plant and equipment are required to be accounted for in accordance with the standard. But FRS-3 doesn't clarify what assets are heritage, and which heritage assets might or might not meet the FRS-3 definition.

SOLGM has previously provided heritage asset accounting guidance, as has the Auditor-General in an article in the 1997 report to Parliament. Unfortunately these predate FRS-3.

Audit New Zealand has been thinking about the heritage asset accounting issues, and a formative paper has been prepared for discussion with local government stakeholders. This paper will shortly be on our website – www.auditnz.govt.nz – to enhance understanding and encourage wider debate on the issue.

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COUNCIL BRIEFINGS

Since the elections a number of councils have asked us to brief new councillors on their responsibilities for accountability and explain the role of the Auditor-General and Audit New Zealand. Our directors would be happy to provide such a briefing for any other Councillors, Councils or Executive Officers. Please contact your Audit Director to arrange a time.

VALUATION - LAND UNDER ROADS

John Duncley is a senior member of the valuation and consultancy division of DTZ New Zealand. He chairs the New Zealand Valuation and Property Institutes Standards Board and is the current chair of the International Valuation Standards Board. John comments:

"Land under roads is an issue currently before the New Zealand Property Institute Standards Board.

The valuation of land under roads has become a real issue for valuers since the introduction of local authority accounting requirements. To date three general methods of valuation have been applied:

- ▲ Land valued at the same rate as the surrounding land values
- ▲ Land valued at a discounted rate based on surrounding land values
- ▲ Land valued at zero

The Office of the Auditor-General has indicated that it is no longer acceptable to include land under roads at a nil value under normal circumstances.

It is proposed that a guidance note will be prepared for members by NZPI. It is expected the assessment of the land will be in accordance with the following principles:

- ▲ For extensively used land (normally rural or recreation type activities) the land value under roads is likely to be close to the average value rate for surrounding land
- ▲ For semi-intensively developed or used land such as residential, the land value is likely to be equivalent to the block value rate, that is, approximately 30% of the surrounding average land value

- ▲ For very intensive land such as in commercial zones the value is likely to be the block value of the land less an allowance to reflect the restricted use of the land. That is, a value less than 30% of the surrounding average land values
- ▲ Roads forming part of a motorway system will have an increased land value reflecting their increased service potential

The Australian Property Institute circulated a discussion paper in late 1999 that followed the general principles outlined above."

ASSET MANAGEMENT PLANNING

Creating Customer Value

This is the National Asset Management Steering Group (NAMs') latest project initiative. Probably the most important aspect of asset management is to agree levels of service with customers. This hasn't really been adequately tackled in the past.

Almost all Asset Management Plans have taken existing service levels as their starting point. Along with the industry generally, both Audit New Zealand and the Office of the Auditor-General have been concerned at the lack of progress in this area.

What makes it even more important is that the Local Government Bill, through Clause 85, will make it a legislative requirement for councils to have a policy on changes to service levels.

The NAMs project will deliver, firstly, a generic guide on how to agree levels of service with customers and, secondly, service specific guidelines for transport, water/wastewater, storm water/land drainage, solid waste, property and parks/recreation. Sub-committees for each of these service areas have been appointed as well as an overview group and a communication group. A website is being created.

Already 42 councils have agreed to participate in this project. We hope the remaining councils will give this serious thought and respond positively to the request to participate. NAMs' previous successes have been built on wide participation of councils.

Audit New Zealand is committed to the success of this project and is represented on NAMs by Local Government Team member Brian Smith.

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OFF COUNCIL CASH COLLECTION SITES

The Auditor-General has asked his appointed auditors to review an important area of all local authorities' operations – cash collection at "off council sites".

The cash collection review might appear to be "old-style" auditing – for those of you who can remember that far back. However, the need for effective cash receipting controls is essential due to the attractive nature of cash. Cash handling is a key risk area for employee misappropriation. While such events are not usually of high monetary value to the council, a misappropriation is time-consuming and embarrassing. Often there is a breach of trust that affects the culture within the council.

In the case of one recently reviewed authority, we found a lack of formal and consistent cash collection policies and practices across all 13 sites visited. The risk of misappropriation was heightened by a lack of segregation of duties, irregular bankings, erratic pre and post banking checks, little review of cancelled receipts, an excessive number of petty cash floats and lack of a consistent write-off policy.

A lack of systems exposed the council to undue risk and exposed individual staff to potential criticism, even for inadvertent administrative errors.

We reported extensively on our findings to the council. It has helped tighten procedures and minimise risks. The work for the Auditor-General is not expected to be as extensive as this independently commissioned report, but it will provide councils with satellite cash collection sites with a snapshot of the strength of internal control procedures and practices.

CAPITAL PROJECTS

Major capital projects such as new roads, bridges, buildings, water supply and IT systems present some of the most significant challenges and risks that public sector organisations have to face.

Increased media interest in capital projects within the public sector has meant projects such as Britomart and the Department of Corrections regional prison-building programme have received extensive media coverage.

Our capital project assurance service is designed to give confidence that councils have taken all reasonable steps to mitigate the major risks associated with managing a capital project. This could include failure to meet original objectives, budget and/or time over-runs.

Assurance given over "real time" will help alleviate the major risks associated with managing a capital project. Client benefits are:

- ▲ obtaining an independent, real-time view on the robustness of processes to manage capital projects
- ▲ receiving confidence that the processes adopted compare favourably with recognised good practice
- ▲ learning of the risks associated with managing capital projects and ways to mitigate them
- ▲ receiving feedback on opportunities to improve project management processes for future capital projects

For further information contact your Audit Director or:

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GOVERNANCE AND RISK HOW TO SLEEP AT NIGHT

People, culture and business processes all need to be managed to ensure an organisation is adequately prepared for risk. A risk aware environment is one where an open and honest culture exists, where risk and opportunity are openly discussed, where risk taking and mitigation is promoted and where people are supported and trained on risk management techniques.

Management of risk can pose a real challenge for local authorities, who face increased demands from stakeholders in an ever-changing environment. For example, a number of councils have expressed concerns about risks they may be exposed to over compliance with legislative requirements.

The Local Government risk management standard (SNZ HB 4360:2000) provides advice on governance, legal compliance, business risk, and capital projects, citing specific examples of projects where risks have, or have not, been managed effectively. The standard's quote under accountability and organisational structure for risk management: "The day to day responsibility for risk management should remain with the operational managers" highlights the importance of ensuring that an organisation's people are fully engaged in managing risk.

We were recently invited by the Northern branch of SOLGM to provide speakers for a panel discussion on governance and risk management in local government. The presentation followed SOLGM's Northern Branch Annual Meeting.

A panel of five Audit New Zealand speakers included: Bruce Robertson, Director and Chair of our Local Government Sector Group; Allan Frost, General Manager Northern Region; Brian Smith, Specialist Services Director; Ben Halford, Director and Alida Robey, Manager Specialist Assurance Services.

Topics covered included: 'How Others Are Coping Nationally'; 'The Role of Risk Management In Providing Comfort'; 'How Does a Governing Body Gain Comfort and Assurance?'; 'Big Projects Mean Big Risks And Need Comfort'; and 'How To Manage The Dynamics And Uncertainty During Organisational Change'.

The panel promoted the view that the supposedly "soft" people and cultural dimensions of risk management are as important as business processes.

If you have any queries on any of these areas or would like to have a panel discussion along similar lines, please contact:

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WELL DONE!

Congratulations to Watercare Services Ltd and Wellington City Council on their success at the 2002 ICANZ Annual Report Awards. Watercare Services won the Public Sector Entities: Local Government section, and Wellington City Council received a commendation.

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DISCLAIMER

Every effort has been made to ensure accuracy in this newsletter, but the items are necessarily generalised and readers are urged not to rely solely on this text, but to seek specific advice on particular matters.