

MAY 2003

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## AUDIT NEW ZEALAND SERVICES

As well as offering **AUDIT SERVICES**, we support the local government sector through our:

**TAX SERVICES**, including compliance reviews and tax position assurance

**ASSURANCE** over:

- ▲ Asset Management
- ▲ Capital Projects
- ▲ Consultation Processes
- ▲ Contract Management
- ▲ Governance
- ▲ Information Systems
- ▲ Organisational Change
- ▲ Performance Reporting
- ▲ Product & Service Costing
- ▲ Project Management
- ▲ Sensitive Expenditure
- ▲ Tenders
- ▲ Treasury Management

## LOCAL GOVERNMENT NEWSLETTER



Five months into the life of the new Local Government Act 2002 (the Act), how would we say we are faring? At its most immediate and commonplace, the Act reformulates and restates many of the principles and processes that we were all familiar with in the Local Government Act 1974. Yet the LGA Listserv and our conversations with you simply buzz with questions, confusion, tips and hints. The Act is clearly challenging our thinking.

One of the ways in which it challenges us in the Audit Office is the delicate balancing on the one hand of allowing community governance to work and grow for itself, and on the other of our responsibility to protect the interests of the public.

Some people have asked the Audit Office to provide more guidance on the requirements of the Act. We have consciously avoided setting 'the rules' for implementing the full scope of the Act. We've done this because we think the challenge is to councils. As both the practitioners and as community leaders, only you can work through and discern the best practice that will achieve the objectives of the Act and the well being of your communities. However we have a specific reporting role in relation to two documents: the LTCCP – key issues are what we expect in an LTCCP and what sort of opinion we should give to achieve the statutory intentions; and the annual report – where we expect the LTCCP will have an important "flow on" effect on reporting in the future.

We're keen to work with the sector as we develop our expectations in these two areas. We also know how important it is that you are aware of our expectations well in advance of the need to prepare plans and reports. We are working toward having our expectations out in early 2005. During this time and over the run-up to audited LTCCPs in 2006, our appointed auditors will be working closely with you so we are all prepared.

**Kevin Simpkins, Deputy Auditor-General**

## LOCAL GOVERNMENT ACT – SEMINAR FEEDBACK

The external presenters at our April Roadshows were an undoubted success. When we invited them to speak, we asked them to consider the same questions we asked participants during the seminar:

- ▲ What are the good points of the new Local Government Act 2002?
- ▲ What are the worrying aspects?
- ▲ What lessons will you take into 2004/05 and beyond?

All speakers had a "free rein" and gave valuable and valued advice.

Without fail, our six speakers delivered important insights – too many to list here. Our presenters were:

- ▲ Dunedin City Council – Athol Stephens and Graham Spargo
- ▲ Christchurch City Council – Bob Lineham
- ▲ Greater Wellington Regional Council – John Allard
- ▲ Palmerston North City Council – Brian Trott
- ▲ Auckland City Council – Robert Nelson

As the seminar organisers, we had the benefit of their collective wisdom. Snippets of particular note included:

- ▲ Keep the value to the ratepayers in mind when preparing your 2004/05 LTCCP; for example, put as much effort as you can devote into the summary of information (refer S82 and 89) to make your planning documents accessible to the ratepayer
- ▲ Councils need to be innovative in reaching the community, beyond just the “old, regular” interested ratepayer groups. This becomes important as you engage or develop the community’s outcomes (S91)
- ▲ The response to the Act requires a joint approach by Council and management. Some independent/external input can be valuable in “getting the message across” and avoiding a particular perception and concern of “staff capture/agendas” in the outcomes and LTCCP processes
- ▲ It will probably take five years to get non-council agencies up to speed and buying into a consultative and collaborative process on defining and delivering of outcomes
- ▲ Councils are being asked to think strategically and consider all options. This is good but does require Council to observe carefully the requirements for appropriate consultation and planning ahead to reach a timely decision
- ▲ The Act’s changes are good – it is encouraging good practice
- ▲ There are undoubted challenges but it is important Councils take risks to be responsive to community aspirations and desired outcomes
- ▲ Treat the lack of prescription in the Act as an opportunity. Use it to be flexible in developing your response to the community

These reflected just some of the positive comments. Obviously there are concerns, particularly over the LTCCP including timing, eventual integration of the auditor into its clearance and controlling planning costs. However despite these concerns we were impressed all these presenters and their Councils indicated they were positively responding to the challenges in the Act. The seminars reflected how crucial it is that the experiences of Councils are shared to develop understanding, good practice and generate new ideas. As we develop and respond to the Act’s obligation as auditors, we will be equally seeking to share our observations prior to 2006.

Currently we are focussing on the 2003/04 annual plans and also the “earlier compliers” (by our latest count there are nine!). As we continue to review these we will be keen to bring our own observations to assist those of you working towards a 2004/05 LTCCP.

**Bruce robertson, (03) 474 7122**

**Email: [bruce.robertson@auditnz.govt.nz](mailto:bruce.robertson@auditnz.govt.nz)**

## ASSET MANAGEMENT – RAISING THE BAR

Complying with the spirit and intent of the Local Government Act 2002 is ‘raising the bar’ for local government in a number of different areas – policy formulation, performance measurement consultation, partnership and collaboration, to name a few. And so it is with asset management. A read of Schedule 10 of the Act, and in particular Clauses 2(1) and 2(3), provides a very clear steer that a Council must know a lot about its assets. Some of the word-bites in these clauses include.

- ▲ demand for services
- ▲ consumption of services
- ▲ intended levels of service
- ▲ actual levels of service
- ▲ service standards
- ▲ additional asset capacity required and associated costs
- ▲ how maintenance, renewals and replacement of assets will be met

...and this is not the complete list! All this information is required (no doubt in summarised form) to be included in the LTCCP.

The National Asset Management Steering Group (NAMS, [www.nams.org.nz](http://www.nams.org.nz)) has been doing its bit to provide guidance on the asset management tasks essential for full compliance with the Act.

Last year NAMS supplemented its International Infrastructure Management Manual (the ‘Black’ Manual), which included criteria for advanced asset management. The criteria neatly dovetails with the asset management requirements in the Act.

A much larger NAMS project has been to provide guidance on levels of service. This guidance (called Creating Customer Value: Guidelines for agreeing and delivering service levels) is a must-read for Councils given the Act’s emphasis on levels of service. Generic guidelines were published late 2002, and are presently being augmented by specific guidance in six service areas. This will be published in June 2003. While most Councils have subscribed to the project, there is time for remaining Councils to join up. To do this Councils should contact Lisa Roberts at Meritec ([lisa.roberts@meritic.org](mailto:lisa.roberts@meritic.org)). NAMS publications can be obtained through the Ingenium website ([www.ingenium.org.nz](http://www.ingenium.org.nz)). Remember that this guidance has been prepared by local government people to better prepare local government for the demands of the new Act.

Brian Smith, (03) 961 3460

Email: [brian.smith@auditnz.govt.nz](mailto:brian.smith@auditnz.govt.nz)

## LTCCPS – The Early Nine

Nine brave local authorities have elected to “go early” in adopting Long Term Council Community Plans (LTCCPs) for the 2003/04 year. Coincidentally this is the same number as went early under the financial management reforms in the 1996 Amendment Act. Audit New Zealand has put in place a hot review team to review each of these early adopters with the objectives of providing comprehensive feedback to each of the Councils and of identifying areas of good practice and potential risk.

We intend to take lessons learned from the early nine forward as part of our support for other local authorities, which will be adopting their first LTCCP in 2004/05. Already a number of themes have been identified and in particular examples of good or innovative practice noted.

### Attributes of an effective LTCCP include:

- ▲ A guide to the document helps the reader understand its structure and find their way through it
- ▲ Diagrams depicting community outcomes, Council's strategic objectives and goals, and its activities can clarify the relationships and linkages between these
- ▲ An outline demonstrating Council's contribution to community outcomes in relation to the contribution of other agencies and community groups
- ▲ A comprehensive statement of forecasting assumptions
- ▲ A description of how community outcomes were determined, e.g. how they were identified using the full consultative process, or where they were determined by Council under the transitional provisions, the source of those outcomes
- ▲ Some Statements of Service Performance (SSPs) have a greater focus on outcomes, with the introduction of new (higher level) measures (although specific targets are generally limited)

### Trends noted in relation to new requirements under the LGA 2002:

- ▲ In the Policy on Significance, there is a trend towards repeating the wording in the Act and not having specific criteria and/or thresholds
- ▲ Councils are rolling on with RMA contributions and no Development and Financial Contributions policies under LGA 2002 have been seen yet
- ▲ A variety of approaches to identifying significant negative effects
- ▲ Some councils are including an "out" clause in relation to the Special Consultative Procedure. This is usually so they can avoid repeating public consultation
- ▲ Specifying service levels is generally not done well
- ▲ Schedule 10, Clause 2(d) – little information on assets and how these are to be managed and funded

### Other matters noted:

- ▲ Wide variations in the level of detail in various areas and in the documents as a whole. Some LTCCPs are around 300 pages
- ▲ There is a project emphasis in some documents, particularly in SSPs and in terms of the financial detail and focus on capital expenditure
- ▲ SSPs largely still have a one-year focus. Some are essentially unchanged from prior years' annual plans

We commend a thorough read of all the "Early Nine" LTCCPs as local authorities develop their 2004/05 planning response. Good features have been noted in all LTCCPs reviewed. It will be interesting at the end of the 2003/04 planning cycle to hear from the "Early Nine" whether their communities have picked up on the LTCCP and whether there are any lessons to take forward in engaging the community in effective planning into the future.

At our recent Roadshow series, we shared many of these insights and we will continue to expand and share our developing

understanding as we work with the sector. Any member of our in-house "hot review" team that assisted local directors in their feedback to the early LTCCPs can expand on our developing views.

Team members are **Bede Kearney (Convenor) (03 961 3464)**, **Rudie Tomlinson (04 496 3141)**, **Miriam Taris (07 577 8218)**, **Alastair Boulton (04 496 3114)** and **Bruce Robertson (03 474 7122)**.

## AUDITOR'S FOCUS ON 2003/04 RATING

The 2003/04 period will be the first in which Councils will rate under the Local Government (Rating) Act 2002. We know that extensive preparation has been done by Councils to position themselves for 1 July 2003.

Councils' implementation of the Act will be a key focus of the audit this year. Particular areas under scrutiny will be:

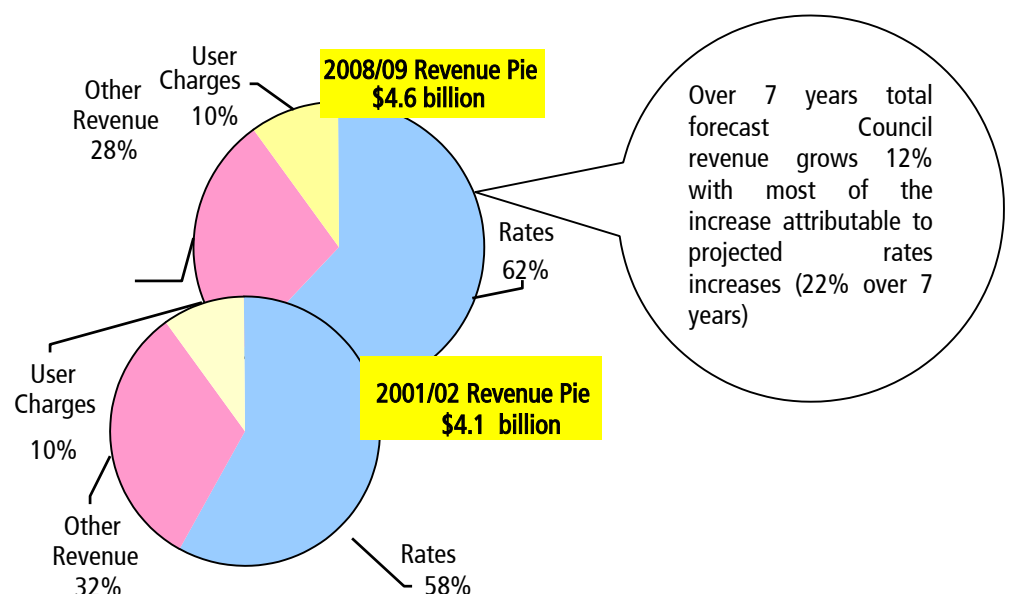
- ▲ Reviewing the processes Council has used to validate the transition from occupier to owner and potential implications for rate collection
- ▲ Reviewing Council's assessment of non-rateable and 50% rateable properties
- ▲ Reviewing Council's calculation of the cap on fixed targeted rates and uniform annual general charges. The cap is complicated to calculate and therefore creates potential for inadvertent beaches
- ▲ Ensuring that the mandatory rating policies, such as Rates Relief for Maori Freehold Land, have been developed and reviewing any policies developed for Remissions and Postponements
- ▲ Reviewing the information in Council's Funding Impact Statement in the draft annual plan and raising any potential legislative compliance concerns with Council
- ▲ Ensuring that Council's rates assessment and rates invoices comply with the provisions of the Act

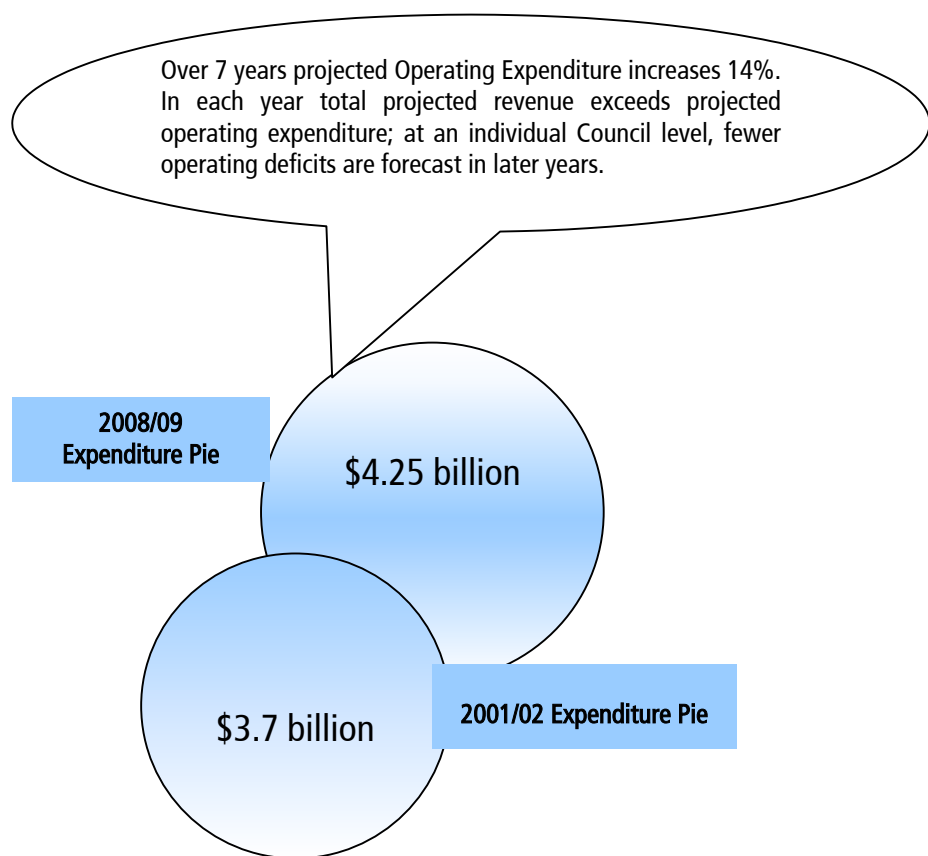
Your audit teams look forward to working closely with each Council's rating and financial services staff to ensure the provisions of the Act are complied with and to provide advice and guidance to the application of the new Act.

If you wish to understand more about our approach, please contact your local audit director or our "internal rating hotline" managers, **Scott Tobin, (03) 961 3463, [scott.tobin@auditnz.govt.nz](mailto:scott.tobin@auditnz.govt.nz)**, or **Ken Morris (07) 839 3349, [ken.morris@auditnz.govt.nz](mailto:ken.morris@auditnz.govt.nz)**

## AUDIT NEW ZEALAND RESEARCH

In this issue we outline several findings from our 2002 analysis of all Councils' LTFs for the eight-year period 2001-2009. We'll publish more findings in later issues.





## TAX UPDATE

### GST ON RATES PENALTIES

Section 14(3) of the Goods and Services Act 1985 was recently amended to state that a charge in the nature of penalty or default interest imposed under an enactment (other than under section 132 of the Rating Powers Act 1988) is treated as an exempt supply.

A number of IRD publications have indicated that the amendment would make rates penalties exempt from GST with effect from 1 July 2003. However, we have recently been advised by the Corporates Unit of the IRD that the Commissioner considers that rates penalties imposed under Local Government [Rating] Act 2002 will **not** be exempt from GST because the penalties are not "a charge in the nature of penalty or default interest".

We understand that the IRD intends to send a letter to all local authorities to clarify their view on this matter.

#### *GST on rates remissions*

Section 86 of the Local Government [Rating] Act 2002 ("LGRA") states that, for accounting purposes, remitted rates must be recorded as being paid by the local authority of behalf of the ratepayer.

Due to concerns regarding the GST impact of this section, the IRD was recently asked to confirm that rates remitted under the LGRA are not paid on behalf of the ratepayer for GST purposes, and that local authorities will still be permitted to claim an input tax deduction in relation to the credit notes issued for remitted rates. We understand the IRD is of the view that:

- ▲ Rates remitted under the LGRA should be treated as being paid on behalf of the ratepayer for GST purposes.
- ▲ The issue of a credit note for remitted rates is not appropriate as there is no cancellation of a supply or alteration of the consideration.

Based on this interpretation, local authorities will not be able to claim GST on rates remitted under the LGRA.

### CCO DEFINITION

At present, the Income Tax Act 1994 ("ITA") states that local authorities are subject to tax on income (other than rates) derived from any LATE. It also states that LATEs do not qualify for the charitable income tax exemption. However, as a result of replacing the term LATE with CCO and CCTO, it has been necessary to make a number of consequential amendments to the ITA. With effect from 1 July 2003, the ITA will state that:

- ▲ Local authorities are subject to tax on income (other than rates) derived from any CCO.
- ▲ CCOs do not qualify for the charitable income tax exemption.

However, it is important to note that the CCO definition in the ITA is different from the definition in the Local Government Act 2002. Basically, the tax definition includes a CCO company, a CCTO organisation and a CCO organisation that controls a CCO (i.e. a holding organisation).

In general, the consequential amendments are intended to maintain the status quo. However, it should be noted that the CCTO definition refers to the purpose of making a profit whereas the LATE definition refers to the intention or purpose of making a profit. The removal of the word "intention" could mean that some organisations that are currently LATEs for tax purposes may not be CCOs for tax purposes. These organisations may therefore be able to qualify for the charitable tax exemption from 1 July 2003.

J Jason Biggins, (09) 914 8636

Email: [jason.biggins@auditnz.govt.nz](mailto:jason.biggins@auditnz.govt.nz)

AUDIT NEW ZEALAND LOCAL GOVERNMENT DIRECTORS	
Bruce Robertson	Direct Dial (03) 474 7122 <a href="mailto:bruce.robertson@auditnz.govt.nz">bruce.robertson@auditnz.govt.nz</a>
Allan Frost	Direct Dial (09) 914 8603 <a href="mailto:allan.frost@auditnz.govt.nz">allan.frost@auditnz.govt.nz</a>
Bede Kearney	Direct Dial (03) 961 3464 <a href="mailto:bede.kearney@auditnz.govt.nz">bede.kearney@auditnz.govt.nz</a>
Ben Halford	Direct Dial (07) 577 8215 <a href="mailto:ben.halford@auditnz.govt.nz">ben.halford@auditnz.govt.nz</a>
Brian Smith	Direct Dial (03) 961 3460 <a href="mailto:brian.smith@auditnz.govt.nz">brian.smith@auditnz.govt.nz</a>
Devan Menon	Direct Dial (03) 961 3443 <a href="mailto:devan.menon@auditnz.govt.nz">devan.menon@auditnz.govt.nz</a>
Jo Smaill	Direct Dial (09) 914 8623 <a href="mailto:jo.smaill@auditnz.govt.nz">jo.smaill@auditnz.govt.nz</a>
John O'Connell	Direct Dial (04) 496 3156 <a href="mailto:john.oconnell@auditnz.govt.nz">john.oconnell@auditnz.govt.nz</a>
Karen MacKenzie	Direct Dial (09) 914 8605 <a href="mailto:karen.mackenzie@auditnz.govt.nz">karen.mackenzie@auditnz.govt.nz</a>
Ken Boddy	Direct Dial (03) 961 3442 <a href="mailto:ken.boddy@auditnz.govt.nz">ken.boddy@auditnz.govt.nz</a>
Laurie Desborough	Direct Dial (06) 350 1316 <a href="mailto:laurie.desborough@auditnz.govt.nz">laurie.desborough@auditnz.govt.nz</a>
Miriam Taris	Direct Dial (07) 577 8218 <a href="mailto:miriam.taris@auditnz.govt.nz">miriam.taris@auditnz.govt.nz</a>
Rudie Tomlinson	Direct Dial (04) 496 3141 <a href="mailto:rudie.tomlinson@auditnz.govt.nz">rudie.tomlinson@auditnz.govt.nz</a>

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