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**REPORT 3**  
*(1215/52/01/1M)*

## **IMPLICATIONS FOR COUNCIL OF NEW AND PROPOSED FINANCIAL REPORTING STANDARDS**

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### **1. Purpose of Report**

The purpose of this regular report is to inform the Subcommittee of new and proposed Financial Reporting Standards and their likely impact for the Council.

### **2. Recommendations**

Officers recommend that the Audit and Risk Management Subcommittee:

- 1. Receive the information*
- 2. Note the developments in New Zealand generally accepted accounting practice (GAAP) since the last regular Subcommittee meeting in March 2010.*

### **3. Background**

The Local Government Act 2002 requires the Council to comply with GAAP in preparing the Annual Report. GAAP is defined by the Accounting Standards Review Board (ASRB) to encompass all applicable Financial Reporting Standards (FRSs) and other sources of appropriate authoritative support (for example; exposure drafts of Financial Reporting Standards, International Accounting Standards etc).

Council Officers have undertaken to report to the Subcommittee on a regular basis in relation to any new FRSs and any exposure drafts currently on issue by the New Zealand Institute of Chartered Accountants (the Institute). This report outlines developments in GAAP and the implications for the Council since the last regular Subcommittee meeting on 19 March 2010. Although not currently applicable for the Council, developments in International Public Sector

Accounting Standards (IPSAS) will also be presented to this Subcommittee for completeness.

#### **4. Local Government Amendment Bill**

Over the last two months the Council has reviewed the Local Government Act 2010 Amendment Bill and approved the Council's submission at SPC on 17 June 2010. The Bill shifted a great deal from the Minister of Local Government's original proposals for the review of the Local Government Act 2002. The Council supports a number of aspects of the Bill, although we consider that the Bill does not make the most of the opportunity to amend and modernise the Act, nor does it achieve all that the government has stated that it has set out to do. We do not believe that the Bill will result in significant additional value for the local government sector and the communities that it serves.

In the financial reporting area, the Council's submission focuses on recommending the removal of the proposed Pre-election Report and seeking clarification on the purpose of the proposed performance management rules to ensure they add value and are well designed. We have offered to be involved in the development of the rules as Chair of the Metro Sector Chief Executive's Group, particularly as Auckland Council is unlikely to have spare capacity to be actively involved.

A full copy of the final submission is included in Appendix 1.

#### **5. Developments in Financial Reporting Standards**

##### **5.1 Submissions made**

The Council makes submissions on discussion papers or exposure drafts where there is potential for it to have a significant impact on either the Council as a reporting entity or the level of funding provided by ratepayers. We also consider whether the proposals are appropriate, in our opinion, from a standard setting perspective.

Since the last subcommittee meeting on 19 March 2010 the Council has made one submission on exposure draft 2010/1, detailing the proposed amendments to the measurement of liabilities in IAS 37: Provisions, contingent Liabilities and Contingent Assets.

This exposure draft proposes a number of changes to the measurement of liabilities and seeks to clarify the meaning of "best estimate" when calculating the value of a provision and also to specify the costs that entities should include when measuring a liability.

The previous standard did not specify what costs would need to be included in provisions. It required entities to make their "best estimate" of the provision. This meant that if liabilities were not considered "probable" they were not recognised as a provision. Under the new proposals these liabilities may now

have to be recognised based on a probability-weighted average calculation which considers a range of outcomes and probabilities. The proposed amendment also states that if an obligation is to pay cash to another party, the future outflows used to measure the obligation would be the expected cash payment plus any associated costs, such as legal fees.

This would have an impact for the calculation of the Council's provisions, especially on the weathertight homes provision and the provision for landfill post-closure costs.

A copy of the full submission is included in Appendix 2.

## **5.2 Summary of Exposure Drafts reviewed since last Subcommittee meeting**

There were a number of exposure drafts reviewed which have been divided between exposure drafts with a potential impact for the Council and those with limited or no expected impact.

### **5.2.1 Exposure drafts reviewed with potential impact for Council reporting**

| <b>Exposure Draft/<br/>Discussion Paper</b>  | <b>Impact/Summary</b>  |
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| IASB ED/2009/12 Financial Instruments: Amortised Cost and Impairment                             | <p>This exposure draft modifies the way that financial instruments held at amortised cost are measured. Currently the incurred loss model is used to determine the amount of the impairment of such assets. This exposure draft proposes moving to the expected loss model and includes requirements for how to include credit loss expectations in the measurement of financial assets.</p> <p>Although this may change the methodology we use to calculate the impairment of financial assets, this is not expected to significantly affect the value of the provision that the Council makes for the impairment of receivables.</p> |
| IASB Exposure Draft ED/2010/2 Conceptual Framework for Financial Reporting: The Reporting Entity | <p>This exposure draft is a request for comment and is part of a phased review of the overall conceptual framework project by the IASB. This exposure draft focuses on finalising conceptual matters relating specifically to the reporting entity by introducing an approach for defining what constitutes a reporting entity. It also</p>  |

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|  | <p>discusses the concept of control and whether entities which have control over other entities should be required to prepare consolidated financial statements.</p> <p>In general we do not believe that the framework adequately addresses the needs of public benefit entities. We are currently preparing a submission outlining that the needs of public benefit entities should be incorporated into the conceptual framework. This will be presented at the next subcommittee meeting.</p> |
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### ***5.2.2 Exposure drafts reviewed with limited or no expected impact on Council reporting***

| <b>Exposure Draft/<br/>Discussion Paper</b>  | <b>Impact/Summary</b>   |
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| FRSB ED 120 on Proposed Amendments to NZ IAS 26 - Accounting and Reporting by Retirement Benefit Plans | The main change proposed is to align the scope of the New Zealand equivalent of the standard with IAS 26. This is intended to clarify the scope of NZ IAS 26 and remove the potential for inconsistency between the scope of NZ IAS 26 and IAS 26. This change is not expected to have any impact on the Council. |

### ***5.2.3 Exposure drafts relating to International Public Sector Accounting Standards (IPSAS)***

While the Council is not currently required to apply International Public Sector Accounting Standards (IPSAS), we continue to review them and assess the impact on the Council if we were required to move to reporting under IPSAS.

| <b>Exposure Draft/<br/>Discussion Paper</b>   | <b>Impact/Summary</b>  |
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| IPSASB Exposure Draft 43, Proposed International Public Sector Accounting Standard (IPSAS) Service Concession Arrangements: Grantor | The Council's contract with United Water to operate the Clearwater Sewerage Plant (Moa Point) is currently the only contract that meets the definition of a service concession arrangement. This service arrangement obliges the operator (United Water) to provide the services to the public on behalf of the Council. |

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|   | <p>The current NZ IFRS guidance is restricted to how the operators of the contract should account for the contract (United Water) rather than the grantor (the Council). If the Council was required to apply IPSAS in the future, we would be required to recognise a liability equal to the present value of contractual payments that are still outstanding to United Water until the end of the contract, rather than the current treatment of recognising the payments as they are due.</p>   |
| <p>IPSASB Consultation Paper, Reporting on the Long-Term Fiscal Sustainability of Public Finances</p> | <p>The consultation paper highlights that the global financial crisis has increased the financial pressures on national governments and has led to increased interest by taxpayers in understanding the long-term financial consequences of government interventions. This consultation paper proposes that a good way to achieve this would be to include projections on future government spending and receipts in general purposed financial reports. The paper focuses on reporting for central governments and government departments. Even if it was proposed that the reporting requirements were extended to local government, a large portion of the information that we would be required to report the long-term sustainability of public finances would already be contained in the LTCCP (as required by the LGA 2002).</p> |

### **5.3 Exposure Drafts on Issue**

The following exposure drafts are currently open for comment and will be reviewed by the Council before the next subcommittee meeting:

- ED/Code of Ethics: Independence in Assurance Engagements
- IASB Discussion Paper DP/2010/1 Extractive Activities

- IASB Exposure Draft ED/2010/4 Fair Value Option for Financial Liabilities
- IASB ED/2010/3 Defined Benefit Plans Proposed amendments to IAS 19
- IASB ED/2010/5 Presentation of Items of Other Comprehensive Income (Proposed Amendments to IAS 1)
- IPSASB Exposure Draft 44 Improvements to IPSASs (April 2010)

We are currently reviewing these exposure drafts to determine any potential impacts on the Council. We will provide analysis of impacts for the Council and copies of any submissions made at the next Subcommittee meeting.

## **6. Conclusion**

We will circulate any key documents to Subcommittee members as they become available. We will also continue to report developments in Financial Reporting Standards to the Subcommittee on a quarterly basis.

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## Supporting Information

### **1) Strategic Fit / Strategic Outcome**

The report supports Council's overall vision by ensuring that legislative compliance with GAAP (NZ IFRS) is appropriately managed.

### **2) LTCCP/Annual Plan reference and long term financial impact**

The report has no specific Annual Plan reference. There is no long term financial impact arising from the report.

### **3) Treaty of Waitangi considerations**

There are no specific Treaty of Waitangi considerations.

### **4) Decision-Making**

There are no significant decisions required by the paper.

### **5) Consultation**

#### **a) General Consultation**

There are no parties significantly affected by this paper.

#### **b) Consultation with Maori**

Maori are not significantly affected by this paper.

### **6) Legal Implications**

This report has no specific legal implications.

### **7) Consistency with existing policy**

This report is consistent with existing policy.