Other Financial Forecasting Information

In addition to the significant forecasting assumptions outlined above, the Council makes a number of other judgements and estimates in preparing the LTCCP. This section details other relevant forecasting information.

1. Funding Principles:

Revenue and Financing Policy

Assumptions and principles in relation to funding of the Council's activities and capital expenditure programme are included within the Council's Revenue and Financing Policy (refer page xx). It is assumed that the current Revenue and Financing Policy will remain in effect for the entire 10 year period covered by the LTCCP.

2. Balanced Budget Requirement:

Section 100 of the Local Government Act 2002 (LGA) requires local authorities to set each year's operating revenue at a level sufficient to meet its operating expenditure for that year. This is known as the balanced budget requirement.

However, the LGA provides local authorities with discretion to vary its operating revenues where it resolves that it is financially prudent to do so. In reaching this decision a local authority must have regard to:

> *"(a) the estimated expenses of achieving and maintaining the predicted levels of service provision set out in the long-term council community plan, including the estimated expenses associated with maintaining the service capacity and integrity of assets throughout their useful life; and*
>
> *(b) the projected revenue available to fund the estimated expenses associated with maintaining the service capacity and integrity of assets throughout their useful life; and*
>
> *(c) the equitable allocation of responsibility for funding the provision and maintenance of assets and facilities throughout their useful life; and*
>
> *(d) the funding and financial policies adopted under section 102."*

The overarching principles for application of the balanced budget requirement are contained in the Council's Revenue and Financing Policy. The financial impact of these principles is detailed in both the Funding Impact Statement and within the Significant Forecasting Assumptions.

In accordance with section 100 of the LGA the Council has resolved that it is financially prudent to depart from the balanced budget requirement in the following circumstances:

Accounting for fair value changes

Principle

Under New Zealand equivalents of International Financial Reporting Standards (NZ IFRS), changes in the fair value of certain assets must be accounted for within the Income Statement. In accordance with Section 100 of the Local Government Act 2002, it is not considered financially prudent to fund changes in the fair value of assets or liabilities as these are essentially “unrealised” accounting adjustments.

Rationale

Changes in the fair value of assets and liabilities are non cash in nature but are required to be recorded in the income statement for accounting purposes. The associated gains and losses will remain unrealised until disposal of the underlying assets. The proposed exemption will ensure that non cash income and expenditure movements are excluded from the assessment of the level of rates funding required to pay for the projected operating expenditure. Further, in the event that the gains / losses are realised during the disposal of the underlying assets / liabilities then the proceeds from disposal will be used for the purposed of repayment of borrowings in accordance with the Council’s Investment Policy.

No inter-generational equity issues have been identified in applying this exemption. Therefore, having had regard to the principles in section 100 (2), it is recommended that it is financially prudent not to fund, or account for, unrealised gains and losses arising from the change in fair value of underlying assets and liabilities.

Non-funding of depreciation on Council assets

Principle

In accordance with section 100 of the Local Government Act 2002 the Council has previously satisfied itself that it is not financially prudent to fund all/part of the depreciation expenditure on the following assets:

- Clearwater Sewerage Treatment Plant.
- Living Earth Joint Venture
- Transport assets funded by NZTA.

In principle the Council will fund depreciation on existing assets as a way of either replacing the asset at the end of its useful life or to repay the borrowings on the original construction or purchase of the asset. Accordingly, as a matter of principle the Council considers that it is not financially prudent to ask ratepayers to fund all / part of the depreciation expenditure on an asset.

- Where the original asset purchase was not funded by borrowings, or the original borrowings have been repaid, and
  - Where, on an ongoing basis, the replacement of the asset at the end of its useful life will be funded by a third party, or

- Where the Council has elected not to replace the asset at the end of its useful life.

- Where a third party has a contractual obligation to either maintain the service potential of the asset throughout all or part of its useful life (or to replace the asset at the end of its useful life) and the Council already effectively funds this through operating grants/tariffs payable to the third party.

Rationale
With respect to the specific assets identified above the Council considers that it is not financially prudent to fund all / part of the depreciation on these assets because:

Clearwater Sewerage Treatment Plant

United Water has a 21-year contract to operate and maintain the Clearwater plant, so the Council has no need to put aside extra maintenance money. United Water is required to fund any repairs over this period. United Water is also required to return the plant to the Council after the end of its 21-year contract with a future life expectancy of at least 25 years. Despite this contractual arrangement, the Council still owns the Clearwater plant assets and is required to cover all operating expenses associated with the plant, including depreciation and financing costs.

Living Earth joint venture

Living Earth is expected to have only a short life (21 years) and during this time the Council will have no maintenance costs, as these are being covered by the contractors. In addition to maintenance costs there are also costs associated with the depreciation of the asset. The Council has elected not to fund depreciation on these assets for the following reasons:

- the Council has considered that the Living Earth asset is not critical to the Council’s long term treatment and disposal of sewage
- the Council has not planned to replace it at the end of its useful life, and
- not funding depreciation will not alter the planned life of the Council’s landfills, nor will it affect the environmental objectives the Council is achieving with Living Earth.

Transport assets funded by NZTA

Each year the Council receives funding from NZTA as part of the overall replacement and renewal programme for the City’s roading infrastructure. The Council recognises the subsidies as income in accordance with GAAP. As the subsidies are received for capital purposes, they cannot be used to offset the rates requirement. Therefore the Council shall recognise a surplus equivalent to the amount of NZTA subsidies for capital purposes, and account for this as a special reserve to be applied against funding the depreciation expense that results on completion of the associated asset.

A non-funding exemption is available in respect of the associated depreciation to the extent that replacement is funded by NZTA. It is financially prudent for the Council not to fund this depreciation through rates, as it would be inequitable to place the funding burden on ratepayers when NZTA is already contributing the overall cost of replacement.

The exemptions from the balanced budget requirement in respect of the non-funding of depreciation on the assets identified above will not impact on the predicted levels of service provision set out in the LTCCP. No inter-generational equity issues have been identified in applying this exemption. Therefore, having had regard to the principles in section 100 (2), it is recommended that it is financially prudent not to fund all / part of the depreciation expenditure on the assets identified above.

Receipt of Capital Revenues

Principle
The financial forecasts in the LTCCP include a level of projected revenue that will be received for the purpose of funding capital projects. For example, the Council receives subsidies from NZTA in respect of its transport capital projects and from development contributions for growth related capital expenditure. The receipt of this revenue is recognised as income in the Income Statement in accordance with generally accepted accounting practice even though the subsidies represent an inflow of cash specifically for capital, rather than operating, purposes. As a result, it is inappropriate for these capital subsidies to be treated as income for rates funding purposes. The Council shall therefore recognise an operating surplus equivalent to the amount of NZTA subsidies and development contributions received for capital purposes in each year.

Rationale
The proposed exemption from the balanced budget requirement will not impact on the predicted levels of service provision set out in the LTCCP. The proposed approach of applying capital subsidies for the purpose for which they were received (ie, to fund capital expenditure projects) supports the concept of inter-generational equity as it ensures that funding received for capital projects is not utilised to offset the rates requirement in a particular year but instead the benefit is spread over the life of the asset by way of reduced borrowings.

Therefore, having had regard to the principles in section 100 (2), it is recommended that it is financially prudent not to apply the receipt of capital subsidies, recognised as income in the Income Statement, to offset the rates funding requirement in each year.

3. Capital Expenditure Programme

All significant capital expenditure is included within the LTCCP. The Council's capital expenditure programme includes:

- Renewal of existing assets (principally in accordance with the underlying Asset Management Plans).

- Planned upgrades of existing assets.
- New investment in the City’s asset infrastructure base where these have been identified, planned and approved by the Council.

4. Asset Sales

No asset sales are planned except as disclosed in the LTCCP.

5. Financial Reporting Standard 42: *Prospective Financial Statements*

In accordance with the New Zealand Institute of Chartered Accountants Financial Reporting Standard 42: *Prospective Financial Statements*, the following information is provided in respect of the LTCCP:

(i) Description of the nature of the entity’s current operations and its principal activities

The Council is a territorial local authority, as defined in the Local Government Act 2002. The Council’s principal activities are outlined on pages XX to XX.

(ii) Purpose for which the prospective financial statements are prepared

It is a requirement of the Local Government Act 2002 to present prospective financial statements that span 10 years, and that these are presented in the Council’s LTCCP. This provides an opportunity for ratepayers and residents to review the projected financial results and position of the Council.

(iii) Bases for assumptions, risks and uncertainties

The financial information has been prepared on the basis of best estimate assumptions as to future events which the Council expects to take place. The Council has considered factors that may lead to a material difference between information in the prospective financial statements and actual results. These factors, and the assumptions made in relation to the sources of uncertainty and potential effect, are included within the principal assumptions underlying the forecasts are noted on page xx.

(iv) Cautionary Note

The financial information is prospective. Actual results are likely to vary from the information presented, and the variations may be material.

(v) Other Disclosures

The prospective financial statements were authorised for issue on 26 March 2009 by Wellington City Council. The Council is responsible for the prospective financial statements presented, including the assumptions underlying the prospective financial statements and all other disclosures.

The LTCCP is prospective and as such contains no actual operating results.

It is intended to update these prospective financial statements during the preparation of the final LTCCP by 30 June 2009.