

Local Leadership
**Working with
the New Acts**
(An LGA Support Programme)

**LOCAL GOVERNMENT
(FINANCIAL MANAGEMENT)
REGULATIONS 1999**

LGA Discussion Paper

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16 Hutt St Adelaide South Australia 5000
GPO Box 2693 Adelaide SA 5001
Ph (08) 8 224 2000 Fax (08) 8 232 6336

1. Introduction

The *Local Government Act 1999* promotes a shift towards greater transparency and accountability and this is reflected in changes to the financial management requirements. The *Local Government (Financial Management) Regulations 1999*, (the Regulations), provide additional information pertaining to, and detailing, the requirements of the Act. The Regulations were effective 1 January 2000.

Accounting and auditing requirements within the Regulations have been designed to support the aims of open and accountable government. New provisions have been included to direct the preparation of annual statements and strengthen the audit and internal control environment both to Councils and Council controlled subsidiaries. There is an increased emphasis on maintaining appropriate records and the use of financial and non-financial information, including performance measures, to facilitate efficient and effective government. The Regulations also take up several requirements previously outlined in other, now obsolete, regulations dealing with insurance and long service leave.

The Local Government Act 1999 now includes some provisions, which were included in the previous version of the Regulations (the *Local Government Accounting Regulations 1993*).

This discussion paper outlines the key changes from the previous regulations and time frames to implement these changes.

2. Changes to the Local Government Act 1999

The Local Government Act 1999 contains some specific requirements relating to financial management. The regulations attach to some of these requirements.

Issues in the Local Government Act 1999 that have relevance to financial management are listed below and referenced to the primary section numbers:

- Subsidiaries - 42, 43, schedule 2
- Delegations - 44
- Commercial Activities - 46, 47
- Prudential Requirements for Projects - 48
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- Allowances and Benefits - 76 - 80, Regulations
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- Investment - 139, 140
- Fees and Charges - 188

3. Requirements of the Previous Regulations now covered by the Act.

The following requirements of the previous Local Government Accounting Regulations 1993 have been dealt with in the new Local Government Act 1999:

- contract and tendering policies - refer LGA Discussion Paper titled "*Commercial Activities, Contracts and Tenders, Sale and Disposal of Land and Other Assets*" and LGA Model Policy titled "*Model Competitive Tendering, Contracting, Purchasing, Sale and Disposal of Land and Other Assets Policy*".
- internal control - refer LGA Discussion Paper titled "*Internal Control Policies*".
- Requirement for accounting records to be maintained – refer to Section 124 of the Act and LGA Discussion Paper titled "*Internal Control Policies*".

4 Changes to the Regulations

4.1 Subsidiaries

The Regulations specifically extend to cover single Council and regional Subsidiaries (in many cases these bodies would have formerly been Section 199 and Section 200 Controlling Authorities)

Subsidiaries are required to prepare budgets as specified by the Local Government Act 1999 and Regulations and adopt these budgets after 31 May for the ensuing financial year and before a date fixed by the Council. The Regulations specify that this budget must be provided to the Chief Executive Officer of each constituent Council within five days of its adoption. Further information on Subsidiary Budgets has been included in item 4.2 below.

Provisions relating to the appointment of auditors by subsidiaries are also included in the Regulations.

The Regulations require that audited financial statements of each Subsidiary must be presented to the Council(s) on an annual basis and in sufficient time to permit the reporting requirements of the relevant Council(s) to be met. Schedule 2 of the Act specifies that this deadline is to be on or before the day determined by the Council. Obviously, this time frame needs to be sufficient to allow consideration of a Subsidiaries financial information in preparing the financial statements of Council.

Subsidiaries with *material* (Australian Accounting Standard 5) assets or activities will require consolidation into a Council's annual financial statements. This includes all single Council Subsidiaries and any regional Subsidiaries in which one Council has a greater controlling interest. In other cases the *equity method of accounting* (Australian Accounting Standard 14) may apply. A Council must, in respect of each Subsidiary it has an interest in, include by way of note to its financial statements information that:

- identifies the Subsidiary
- describes its nature and purpose,
- details financial contributions made by the Council to the Subsidiary during the year and vice versa,

as well as including any other relevant information such as that relating to guarantees or contingent liabilities.

The provisions governing the establishment of a Subsidiary are contained in the sections 42 and 43 and Schedule 2 of the Act.

4.2 Budgets

The Regulations enable a Council or Subsidiary to prepare their budget in a format that suits their own needs, provided that:

- the budget deals with each principal activity on a separate basis, and;
- in the case of a Council, the following forms prescribed by the Regulations are included in the budget package:
 - a) the budgeted operating statement,
 - b) the budgeted statement of financial position,
 - c) the budgeted changes in equity,
 - d) the budgeted statement of cash flows, and
 - e) the statement reconciling cash and non-cash revenues and expenses in order to provide a basis for determining rates (form is not prescribed – see “Rate Determination Statement” below)
- section 123(3) of the Local Government Act 1999 requires a Council to prepare an Annual Statement (see “Annual Statement” below).
- A Subsidiary must ensure its budget is consistent with its business plan and Council’s strategic management plans.

4.2.1. Adoption and Review

The Local Government Act 1999 requires the budget documents to be adopted between 31 May and 31 August in each financial year. In the case of a Subsidiary, the CEO of the relevant Council(s) must be provided with a copy of the budget within five business days after its adoption. The CEO should ensure Council is provided with a copy of the budget.

Under the Regulations a Council or Subsidiary must reconsider its budget at least 3 times during the course of the financial year at intervals of not more than three months, between 30 September and 31 May in the relevant financial year. The first reconsideration must make reference to the prior years audited financial position, accordingly Council or a Subsidiary cannot complete the first formal reviews of its budget until the final audit has been completed. A Council or Subsidiary may reconsider and revise its budget more frequently during the course of the financial year.

The revision process should result in the inclusion of additional information in the budget papers clearly and concisely explaining; major changes in assets and liabilities, significant revisions to the budget, and significant budget variations.

4.2.2. Annual Statement

The Local Government Act 1999 now requires a Council to prepare, as part of its budget or in association with the preparation of its budget, a statement known as the "Annual Statement". The statement must address the activities the Council intends to undertake in the ensuing year to achieve its objectives and the measures (financial and non-financial) that the Council will use to assess its performance against its objectives.

The annual statement provides a link to the strategic management plans of Council. Section 122(1)(c) of the Act requires the strategic management plans to include estimates of revenues and expenses of the Council over the period of the plans and 122(1)(d) requires measures (financial and non-financial) that are to be used to monitor and assess the performance of the Council.

The annual statement is to be in a form determined by Council. It could be a separate document or incorporated within the budget adopted by Council.

Irrespective of the format chosen by Council, the annual statement should show how the budget reflects the strategic direction of Council and the measures (financial and non-financial) that Council will use to assess its performance against its objectives.

If the Annual Statement is a separate document it should provide an executive overview of the information contained in the detailed budget documents including the various sources of revenue (eg grants, rates, commercial activities, contributed assets) and a picture of how the funds are being applied (eg recurrent expenses, capital works, economic development).

If Council chooses to incorporate the Annual Statement within the budget then this can be achieved by inserting the additional information (ie. activities Council intends to undertake to achieve its objectives and the measures to be used to assess performance against objectives) within the primary budget document. The effect is to create a single budget document containing the "words" of the Annual Statement.

4.2.3. Rate Determination Statement

The statement referred to at 4.2(e) above was described by the previous regulations as a rate determination statement. The format of the statement is not prescribed by the new Regulations and hence Councils are to determine what is most suitable for their needs.

The purpose of the Rate Determination Statement is to reconcile the difference between cash outflows and cash inflows for the year with the difference being the amount required to be raised by rates. The statement is very similar to a statement of cash flows without a rates revenue line item.

4.3 Audit

The Local Government Act 1999 specifies that a Council must appoint an auditor. The Regulations specify that a Subsidiary must appoint an auditor. New criteria applies to the qualifications, eligibility and term of appointment of the auditor (refer to the LGA Discussion Paper "*Selection of Auditors*" for more detailed information)

For the first time, Councils and Subsidiaries are required to appoint a registered company auditor for a term of 5 years by written agreement. Provisions applying to the duties and functions of auditors have not changed substantially. See "Transitional Arrangements" below in relation to audit agreements in existence prior to the 1 January 2000.

The Act and regulations require that audits of a Council and its Subsidiaries must be conducted in accordance with Auditing Standards and Auditing Guidance Statements published by the Australian Society of Certified Practising Accountants and the Institute of Chartered Accountants. The audit of the financial statements is required to take place "within a reasonable time of the statements being referred to the auditor", ie for a Council within 2 months of the referral and for a Subsidiary within a reasonable time to meet the requirements of the Council(s).

Under the Regulations the auditor must give due consideration to the adequacy of a Council or a Subsidiary's policies, practices and procedures of internal control in forming their audit opinion. This requirement, consistent with the new provisions of the Act, requires a Councils and its Subsidiaries to ensure an appropriate internal control environment is implemented and maintained to ensure adherence to management policies, safeguard assets, strengthen the reliability of accounting records, and assist in achieving efficiency and effectiveness aims. Council is empowered to form an Audit Committee to enhance this process and, if it so chooses, it may be extend to include a Subsidiary.

As with the previous Act, the auditor's obligations to report to the Minister any serious financial irregularity in the accounting practices of the Council or Subsidiary, or in the management of their financial affairs, or any breach of the Local Government Act 1999, or failure to rectify any previously identified irregularity, remains.

4.4 Financial Statements

The format of the Annual Financial Statements is set out in the Schedule to the Regulations. This format also applies to Subsidiaries. The term Community Wealth has been replaced with the more common expression "equity".

The previous regulations also gave Councils an option to format the annual financial statements under "functional" headings. This no longer applies, although a Council may choose to include a note to the statements that includes a "functional" style report.

The Regulations require that audited financial statements of a Subsidiary must be presented to the Council in sufficient time to permit consolidation into Councils financial statements (see 4.1 above).

The Regulations require that Councils submit a copy of their audited financial statements by 30 November to:

- the Minister,
- the South Australian Local Government Grants Commission, and
- the South Australian Regional Director of the Australian Bureau of Statistics.

These statements must be accompanied by information that accords with the "Supplementary Data to the Financial Statements" issued by the Australian Bureau of Statistics for use by Councils. In addition the C.E.O. must certify that this information is consistent with the audited financial statements.

4.5 Reporting – Full Cost Attribution

From July 2002, a Council or Subsidiary must ensure that reporting on a function, activity, good or service contained in its financial statements, or in any other external financial report, is made according to a *full cost attribution* basis.

Full cost attribution is a system under which all costs, including indirect and overhead costs, are allocated to a function, activity, good or service on a reliable or consistent basis.

The implication of this requirement is that Councils (and their Subsidiaries) must have appropriate accounting systems in place by July 2002 to enable such reporting.

4.6 Transitional Arrangements

Transitional arrangements are dealt with in the Local Government (Implementation) Act and the Local Government (Implementation) Regulations 1999. Certain transitional arrangements have been prescribed for financial matters, including:

- Auditors – A person holding office as the auditor of a Council immediately before the relevant day (1 January 2000) but who is not qualified to be appointed as an auditor under the Local Government Act 1999 may nevertheless continue as the auditor of the Council until the completion of the audit for the financial year ending on the 30 June next following the relevant day.
- Investments – Any investment made by a Council before the relevant day is not affected by the operation of the Local Government Act 1999.
- Term of appointment of auditors –
 - (1) An appointment of an auditor for a fixed term in existence immediately before 1 January 2000 is not affected by section 128 (6) of the Local Government Act 1999.
 - (2) An appointment of an auditor for an indeterminate term in existence immediately before 1 January 2000 will cease to have effect on the completion of the audit for the 1999/2000 financial year.

4.7. Rating Policy

The Local Government Act 1999 requires Council to prepare and adopt a rating policy (in conjunction with its declaration of rates). Amongst other things, the rating policy must indicate the relationship between the Council's strategic management plans, its budget and its rating structure.

The objective of this policy is to link the Council's planning documents with its most reliable and important source of income - its rates. The focus is therefore aimed at driving planning, monitoring and reporting through a consistent method and approach (refer to the LGA Model Rating Policy for further information).

4.8. Long Service Leave

The *Local Government (Financial Management) Regulations, 1999*, include provisions previously included in the *Local Government (Long Service Leave) Regulations, 1987*. These provisions are largely unchanged and include the requirements governing inter-Council contributions relating to the long service leave entitlements of employees who transfer between Councils and a method for calculating these amounts.

4.9 Risk Management and Insurance

Whilst the types of funding and investment arrangements a Council is able to enter into has not changed under the Local Government Act 1999, an increased level of monitoring and risk management is emphasised. Consistent with this aim, the Regulations now contain provisions previously contained in the *Local Government (Section 166a - Insurance) Regulations, 1995*. These conditions require the Council to take out and maintain insurance to cover its civil liabilities to a minimum level of \$50 million.

4.10 Asset Revaluation

The Regulations specify that a Council or Subsidiary must undertake a revaluation of all *material* land and infrastructure assets in accordance with the requirements of Australian Accounting Standards, and, unless otherwise determined by these standards, a revaluation must be undertaken at least once in every five years. Under the previous regulations, this requirement extended to plant and equipment assets, however this is no longer applicable. Plant and equipment assets are only required to be revalued as directed by the Australian Accounting standards, ie when these assets are being carried at an inappropriate value.

5 Summary

The provisions of the *Local Government Act 1999*, and the *Local Government (Financial Management) Regulations 1999*, are for the most part, enhancements of the existing framework of control.

The revisions are aimed largely at providing a greater degree of assurance that Council and its Subsidiaries functions and activities are being carried out efficiently and effectively.

The Local Government Act 1999 also encourages a greater degree of autonomy; in regard to the range of services a Council may provide and the choices it uses for service provision, and the linking of strategic management planning activities to the monitoring and review of operations. The Regulations support this framework.

