



LOCAL GOVERNMENT  
ASSOCIATION OF  
QUEENSLAND INC.

Report on  
**Best Practice Simplified Internal  
and External Reporting**  
for  
**Local Governments in Queensland**

Prepared for the

**Local Government Association of Queensland**

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**BDO** *Kendalls*



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## **EXECUTIVE SUMMARY**

### ***Period of Significant Change for Local Government***

This report is timely in that it follows a period of significant change for Local Governments in Queensland in terms of external reporting to ratepayers, management reporting to Councillors and financial management generally. Since the early 1990s, there have been a number of financial management and related reforms which have required an increased level of management and councillor attention.

There is however widespread dissatisfaction with the useability of information provided to many elected members in local government and in terms of what is seen as overly complex financial reporting requirements.

While it is appreciated that accountants in local governments have taken enormous efforts to introduce accrual accounting and business management changes, the increasing importance of good financial management to the success and viability of Local Governments means that reforms need to continue.

### ***Complexity in Financial Reporting***

It is noted that complexity in financial reporting is seen to be occurring at a number of levels:

1. The three additional primary financial statements which are required under Queensland Local Government legislation. We understand that the Minister has agreed to bring Queensland into line with the reporting requirements under Australian Accounting Standard AAS27 (which more closely reflects generally accepted accounting practices in the private sector, in other levels of government and in large not-for-profit organisations). This will provide some simplification by reducing the number of primary financial statements - noting that some of the information from the superseded statements will still be required as part of the notes to the financial statements.
2. Action to make the external financial statements more easily understandable which includes consideration of the inclusion within annual reports of a Management Discussion and Analysis section which provides easy to read information including in tabular and graphic format.
3. Consideration of improvements in the quality of internal management reporting provided to Councillors and to senior management with the view of making this information more relevant in terms of performance management. This includes the use of graphical presentations to assist in the interpretation of the information provided.

The brief for this report focuses on items 2 and 3 above.

### ***Responsibilities of Elected Members***

Elected members are entrusted with responsibility for significant community funded assets. As is the case with directors of corporations in the private sector, Councillors have important fiduciary duties for the effective and efficient use management of community resources including of all assets held. The statutory and common law duties which fall upon a company director include:

- to act in good faith in the best interests of the organisation;
- to act with care and diligence;
- to avoid a conflict of interest; and
- to not misuse corporate information.

For Councillors, there are additional challenges as compared with a company director in that Local Governments often are comprised of a number of different types of operations and businesses with

often differing objectives to be met. These require a different focus in terms of reporting as outlined in the following table.

**Reporting focus of an Entity**

<b>Internal Business Units</b>	<b>Tax/Revenue Office</b>	<b>Monopoly GOE's/ Commercialised Business Units</b>	<b>Private or Private Sector Firm in competitive market</b>
<i>Financial performance, Financial risk</i>	<i>Financial performance</i>	<i>Financial Performance, Financial Risks</i>	<i>Financial Performance, Financial risks</i>
<b>Government Departments</b>	<b>Taxing raising Authority</b>	<b>Statutory Authorities/Boards</b>	<b>Not-for-Profit Organisation</b>
<i>Community objectives performance, contribution to operating capacity</i>	<i>Community objectives performance, Operating Capacity, Financial risk</i>	<i>Financial risk, Community objectives performance, Operating capacity</i>	<i>Financial risk, Community objectives performance, Operating capacity</i>

**COMMUNITY RETURNS**

*Low Risk* *High Risk*

Local governments are often comprised of a mix of non-commercial and commercial activities. There may be a mix of fully commercialised or corporatised business activities (sometimes required to provide community service obligations) as well as a range of activities which are meeting social or community objectives. Performance measures for business activities will focus on business objectives including rate of return on equity employed, whereas social objectives can cover a range of quantitative and qualitative data.

Councils and government departments are largely characterised by having low financial risk and a focus on social returns. In this respect, performance indicators need to focus primarily on the achievement of community objectives. Financial risk issues will largely be secondary and mainly relate to ensuring that current and projected costs are sustainable in terms of the size and growth of the revenue base. Financial performance issues are usually not paramount except for the obvious need to remain within budgetary allocations and to demonstrate fiscal responsibility.

**PART A. Exposure Draft on Internal Management Reporting**

**Internal Management Reporting**

In terms of management reporting, it is clear that simply relying on budget variance reporting during the financial year is insufficient to ensure that the Council is efficiently managed and has adequate liquidity to pay its debts as they fall due. Local Governments need to monitor liquidity throughout the year and the Council also needs to review the sustainability of its debt levels and financial structure at least annually. Ideally, the annual review of the financial structure and debt levels should be conducted during the budget process. It may be necessary to review this both at the beginning and the end of the budget process, since the cumulative effect of budget decisions could cause deterioration in the original targets.

During the financial year, regular reviews of liquidity and related issues such as rates arrears and outstanding debtors needs to occur. Ideally, this should occur within the governance structure established by the Council for the management of its finances. Therefore the committee charged with responsibility for financial matters (for example the finance committee or audit committee) should regularly review and monitor Council liquidity indicators.

This review has made the following findings in relation to management reporting:

- Financial reporting is seen as a key part of the organisation's knowledge management framework.
- Financial reporting is one of the organisation's main feedback, learning and improvement processes.
- Financial reporting is closely linked to the achievement of the organisation's objectives.
- There is widespread dissatisfaction with traditional internal financial reporting.
- Management can only assimilate a limited amount of information, so reports must be focussed. More is not necessarily better. Higher level reporting (reporting of key performance measures on one page) with the ability to drill down for further information is best practice.
- For financial information to be useful, it must be:
  - accurate, timely and reliable;
  - coupled with analysis (based on analytical tools), and insights on the implications for the achievement of objectives;
  - forward looking (forecasts etc);
  - in a language or format preferred by the reader (usually non-numeric – eg graphs, charts, ratios);
  - short reports focussed on exceptions and pertinent issues (requiring management attention or corrective action); and
  - contain peer comparisons (benchmarking).

It is worth noting that the development of sophisticated financial management software and information technology generally provide opportunities for Local Governments to gain business benefits including in linking financial management reporting and other processes.

### ***Best Practice Management Accounting Framework***

The following are the issues which need to be addressed for Council seeking to achieve best practice management accounting:

#### ***Governance***

- Mechanisms for elected members to monitor key financial information throughout the year, for example the finance committee or audit committee, at least on a quarterly basis.
- Such committee should be charged with responsibility for monitoring the council's financial risks (liquidity and long-term debt levels), operating capacity, and achievement of community objectives.
- Such committee need not focus on detailed variance reports and cheque listings.
- Instead, this committee should monitor the issues outlined in the suggested balanced scorecard outlined above.

#### ***Reporting***

- Financial reporting should be linked to the achievement of the organisation's objectives
- Financial information needs to be:
  - Accurate, timely, and reliable;
  - Coupled with graphical interpretations with analysis of implications for the achievement of objectives (using trends and ratios);

- Include forward-looking information such as projected end of year results; Short (10 pages or less) focused on exceptions and pertinent issues which require management attention or corrective action; and
- Include comparisons with targets or benchmarks with similar councils.

***Systems and reporting processes***

- Councils need to review their financial operating practices to make best use of available software features, so as to expedite timely reporting and release resources for analysis and exception reporting.
- If current software does not allow such reporting, the need for an upgrade should be reviewed.
- One-day reporting concepts should be applied

***Financial Management Competencies***

- There made may a need to reduce the manual resources used to prepare external reports and operate internal financial processes.
- These resources need to be applied to improve internal reporting based on the above principles.
- Accountants in Local Government need to have skills in:
  - Determining the information requirements of managers and councillors;
  - Understanding the corporate objectives and financial management implications
  - Presenting and interpreting accounting data and other key information in ways that are readily understandable;
  - Developing efficient internal processes to meet the above reporting requirements;
  - Distilling the key information which needs to be brought to councillor and management attention for corrective action; and
  - Assessing and monitoring financial risks - short-term and long-term.

***Applying Balanced Scorecard and Triple Bottom Line Reporting concepts.***

There is a move within public sector entities, including a number of Local Governments in Australia and in Queensland, towards a more holistic approach to reporting which links financial and non-financial performance management. These incorporate the use of Key Performance Indicators sometimes linked with the Balanced Scorecard approach to planning and management. These approaches should be integrated with the strategic planning processes of organisations and allow for the use of a mix of financial and non-financial measures of performance and also allow for broader assessments of outcomes in terms of community impact. (See also Chapter 5)

An example of such a framework adopted by a Local Government in Queensland is as follows:



Most traditional financial reporting focuses on financial results, which underpin the public sector requirement to monitor the operating capacity of the organisation. This has traditionally been the main role of management accountants.

The Government Accounting Office in the United States of America published its research into 'Creating Value through world-class financial management' in April 2000. It found that management accountants in all sectors are increasingly being required to supplement their traditional role with more management-oriented analysis and advice.

World-class finance units can be defined in terms of their goals:

- \_ Improved business analysis;
- \_ Innovative solutions to business problems;
- \_ Reduced operating costs;
- \_ Increased capability to perform ad-hoc analysis; and
- \_ Improved overall business performance.

Best practice organisations make financial management improvement an entity-wide priority by building a foundation for value-added feedback and accountability that supports external reporting and performance management.

More advanced organisations have operational feedback systems which provides managers and employees with timely, accurate information, both financial and non-financial, on the efficiency, quality, and cycle times of business processes.

In New South Wales, the Auditor-General reviewed the financial reporting practices of a number of agencies in 2001, and found serious deficiencies and has developed a better practices guide for use by agencies.

Based on the above research, we recommend the following:

- Recommendation 1**      **It is recommended that councils review their routine financial operations and make best use of facilities available in the computer software so as to release additional resources to value-added analysis and reporting activities.**
- Recommendation 2**      **It is recommended that councils consider the establishment of simplified reporting to elected members based on Key Performance Indicators which align with the Strategic Plan.**
- Recommendation 3**      **It is recommended that the Local Government Association of Queensland develop and present training programs across the State on financial management for:**
- **Councillors primarily - on what information to ask for; and**
  - **Financial Management Staff – on the preparation and presentation of best practice management reports.**

### ***Local Government Balanced Scorecard***

Although smaller and medium sized Councils may feel that they are too small to warrant a Balanced Scorecard framework, the Councillors at the LGAQ focus group in June 2001 clearly expressed a need for information which fits neatly within such a framework. Based on these findings, the following is a suggested framework of measures that may be applicable to many local governments or used as a basis for tailoring a balanced scorecard for the organisation. Councils may find it useful to select 15-20 indicators which seem most relevant to their needs.

### ***Community objectives***

- Delivery of promised activities (by exception).
- Service level measures (eg. library borrowing levels, roadwork activity).
- Customer or community satisfaction survey (if conducted).
- Numbers of complaints.
- Other key performance measures based on the corporate plan.
- Value for money indicators (eg. Average rates).

### ***Financial Risk***

- Liquidity (working capital or current ratio).
- Solvency (debt ratios).
- Revenue ratio (reliance on specific sources of non-rates revenue).
- Overall budget variances (for operational revenue, operational expenditure, capital revenue, capital expenditure).
- Revenue sustainability (revenue forecasts compared to expenditure trends).
- Unrestricted reserve levels.

### ***Operating Capacity/Internal Processes***

- Corporate overheads as % of total expenditure.
- Rate arrears ratio.
- Percentage of bills paid on time.
- Percentage of funded depreciation .
- Internal and external audit report issues.
- Operating expenditure per capita (excluding depreciation) compared to similar councils.

### ***Competencies, Learning and Innovation***

- Employee indicators:
  - average sick days/absenteeism per employee;
  - employee turnover; and
  - leave liability balances.
- Average training days per employee.
- Innovative changes in the organisation.
- Percent of revenue from innovative functions (special-purpose grants, private works, etc).
- Councillor and CEO satisfaction with management reports.

## ***Key Financial Measures***

From an assessment of indicators utilised around Australia for Local Government, it is considered that the following measures represent best practice financial performance indicators for Local Governments as a whole. There are benefits including for benchmarking purposes for a level of consistency between local governments across Australia.

### ***Financial Risk Indicators***

The financial risk indicators include a number of long term solvency indicators and one short-term liquidity indicator which have widespread usage across Australia as follows:

- Debt Servicing Ratio
- Debt/Rates ratio (Total debt to total rates)
- Working Capital

The addition of the debt/rates ratio is to overcome weaknesses in the debt servicing ratio – since the latter ratio can give the erroneous impression of debt problems if a Council accelerates its debt repayments. However it is retained because of its widespread usage and understandability in the community.

### ***Operating Capacity***

The following representative range of indicators cover revenue, expenditure and capital:

- Revenue source ratios;
- Rate arrears; and
- Capital expenditure ratio (to depreciation).

### ***Community Objectives***

These indicators cover value for money objectives:

- Average rates per assessment; and
- Average operating expenditure per assessment.

## **PART B. Simplified Financial Reporting and Management Discussion and Analysis**

### ***External Reporting to the Community and Other Stakeholders***

During the last decade or so there has been a range of developments which has made the management of local governments more complex. There have also been a number of initiatives – particularly accrual accounting - which has sought to introduce improved reporting on the use of all resources. These initiatives have an impact on the manner of reporting to the community.

The need for simplification of the financial performance information provided to elected members is a key issue in this report. There should not be a requirement that elected members be experts in financial reporting in order to analyse and manage council finances. Elected members, however, should be presented with financial and other performance information which allows them to make a range of decisions about the finances of the Local Government.

To do so, elected members should be able to rely upon the expertise of the senior management of the Local Government. The Chief Executive Officer and other senior managers need to have a stronger knowledge and understanding of the finances of the Local Government although they, in turn, should be able to rely upon the specific expertise and technical knowledge of the Chief Financial Officer.

### ***Linking of Planning, Budgeting and Performance Management***

Local Governments are required to have a performance management framework which links the corporate planning, budgeting and performance management reports including financial information. This information needs to be presented in a style, format and standard that can be easily understood. The lack of specialist financial knowledge should not be an impediment to being provided with useable information on financial and related performance. This understanding needs to be achieved both at manager and Councillor levels within Local Government and also for ratepayers and the general community.

### ***Effective Communication***

This would suggest the need for effective communication of key information to internal management and to the community.

Research indicates that, whilst there are many examples of good practice in terms of internal reporting and in developing effective means of communication with the community, generally there is room for improvement. Generally, due to low print runs and distribution, current financial reporting is not proving to be an effective communication tool.

The need for effective processes to communicate information to the community is a high priority. A number of local governments have taken action to develop a brochure or newsletter to ratepayers which

incorporate some financial details - most notably at the time of the rates notice and incorporating some graphical and tabular information in easy to read format.

**Recommendation 4**      **It is recommended that all Local Governments be encouraged to provide abridged budget/financial information (unaudited) in a brochure to ratepayers early in the financial year in question or in a regular newsletter.**

### ***Annual Report***

The ability to use the Annual Report as a means of communicating information to ratepayers is limited. It is primarily a report on past financial operations and generally is not available until five or six months after the financial year.

Research has noted very limited use by ratepayers of Annual Reports as a means of communication with the community or as an effective process of accountability.

An increase in the use of the Web as a means of communication has been noted, as have a number of examples of local governments placing their annual reports on the Web. Others are using technology such as CD-ROM as a means of disseminating annual reports and financial statements.

**Recommendation 5**      **It is recommended that all Local Governments be encouraged to publish Annual Reports on the Web as one element of accountability and as a means of communication of information generally to the staff of the Council, to other Councils and to the community generally.**

It is noted however that Annual Reports are used to communicate information other than to ratepayers. They are a valuable resource for other levels of government, for other local governments (including for benchmarking), for internal staff communication and for briefing applicants for positions within the local government.

### ***Simplified Financial Reporting***

The review explored the possibility of local governments being able to issue a concise annual report similar to the option afforded to corporations. This option relates to a Management Discussion and Analysis requirement under Corporations Law and the accounting standard for Concise Financial Reports (AASB1039). However, there is little merit in providing this option to Councils given the limited use (and demand) for existing annual reports and the need in any event for full general purpose financial reports to be provided in line with accounting standards.

The question of simplification of financial reporting has two elements to it – one being the decision taken to reduce the number of primary financial statements such that Queensland Local Governments comply with the Australian Accounting Standard for Financial Reporting by Local Governments (AAS27). The second element is to ensure that the information provided is simplified or is easier to use.

**Recommendation 6**      **It is recommended that support be given to the process under way to simplify general purpose financial reporting by moving to reporting in Queensland in line with the Australian Accounting Standard for Financial Reporting by Local Governments (AAS27).**

### ***Management Discussion and Analysis***

As part of the process to simplify reporting, to ensure that non-expert users are able to have better information on the financial position of the Local Government, it is recommended that Local Governments from financial year 2002/2003 be required to include a Management Discussion and

Analysis section in the Annual Report. Note that similar information to this should form part of the simplified reporting by brochure or newsletter mentioned earlier.

This Management Discussion and Analysis section is supplementary to and enhances the financial statements by providing a discussion and analysis of the key performance of the Local Government and in particular of the financial performance, financial position and financing/investing activities of the Local Government. Management Discussion and Analysis is a narrative interpretation of the Council through the eyes of managements and therefore requires more than a restatement of information already presented in the financial statements. Management Discussion and Analysis is intended to expand on and explain the financial statements.

**Recommendation 7** It is recommended that the Local Government Finance Standards be amended to require Local Governments from financial year 2002/2003 to include a Management Discussion and Analysis section in Annual Reports. (Note: This is to be supplementary to and not form part of the Financial Statements of the Local Government)

However, it is not considered possible to prescribe the form and content of management and discussion sections. This is because the circumstances of each Local Government will vary one from another and also from year to year depending upon the strategic issues being addressed. This report, however, outlines the attributes for management discussion and analysis and provides examples of best practice already adopted for management discussion and analysis.

**Recommendation 8** It is recommended that Local Governments utilise the guidance provided in this report on the content of management and discussion analysis sections of annual reports.

### *Principles of Management Discussion and Analysis*

In preparing the Management Discussion and Analysis report we support the use of the following seven disclosure principles to be taken from the current Canadian Institute of Chartered Accountant's exposure draft.

- Principle 1: Information Disclosed through the Eyes of Management
- Principle 2: Complement and Supplement the Financial Statements
- Principle 3: Be Forward Looking
- Principle 4: Focus on Long-Term Value Creation
- Principle 5: Short and Longer Term Time perspectives
- Principle 6: Materiality to Decision-Making Needs of Users
- Principle 7: Usefulness

MDA is about communication of results and how to move forward. To achieve this MDA requires the following attributes.

### *Guidelines on Management Discussion and Analysis*

MDA is a narrative interpretation of the Council through the eyes of management. Requires more than a restatement of what is already presented in the financial statements, MDA is intended to expand and explain the statements. MDA requires an analytic discussion rather than a numerical analysis.

- Look at the **Operating Statement** and review of the main activities that lead to the result for the period.
- Look at the **Statement of financial position** and Statement of Cashflows. Review the capital structure, cash from operations and other sources, liquidity and funding.

- A discussion of trends and factors underlying the result. Look at the adverse change in the reliance on rates or the times-interest-earned ratio. Is this deterioration or improvement in conditions expected to continue into future reporting periods?
- Explain what the financial KPIs mean and how they relate to the financial information. Also put them into context, for example, what would a good result be, what was in the corporate plan, what are comparable councils achieving.
  - **Comprehensive and unbiased.** Balanced and objective, dealing even-handedly with both positive and negative aspects of the Council. Presenting information that is **material** to the users of report.
  - **Easy to understand.** MDA requires clear and succinct reporting without the use of technical language.
  - **Forward looking orientation.** What does the result mean for the future? Forward-looking MDA explains past events, decisions, circumstances and performances in the context of whether they are reasonably likely to have a material impact on future prospects. How is a negative result going to be remedied?
  - **Consistent.** Reporting should roll forward and be capable of being read as a set. Refer to comments made in previous statements.
  - **Useful for users.** Reporting should aim to be of use for the potential audience.
  - **Trends.** Trend information would be expected to be beneficial for users especially in those circumstances where a Local Government is seeking to achieve a change in financial position over a number of years.

### **Structure**

- **Outline Objectives and how measured.** What were the Council's goals for the reporting period? How were those goals to be measured (KPIs)? Linking to a previously published corporate plan makes reporting more meaningful.
- **Results.** Should be divided into the three main areas: Community Objectives, Operational Capacity and Financial Risk and compared to the goals in the corporate plan. Variances (both positive and negative) should be explained particularly in context of what the result means for the organisation in the next reporting period.
- **Corporate Governance.** What governance arrangements are in place to monitor the above matters.

### **Use of Comparative Reporting**

We have noted a range of developments in the use of comparative reporting around Australia and overseas. Queensland produces the Queensland Local Government Comparative Information which is a sound basis for the further development of comparative information. It is noted that this report is not seen as being published in a timely manner. It does however rely upon the provision of information from a large population of Local Governments. We also note that there were some gaps in the information provided with some Local Governments not participating. This publication is potentially a valuable document to enable benchmarking of Local Governments.

**Recommendation 9**     **It is recommended that steps be taken to enable earlier publication of the Queensland Local Government Comparative Analysis reports including publication of information progressively on the Internet. Along with reports of this nature it is also recommended that the measures reported on be reviewed in the light of the recommendations in this report.**

### ***Timeliness of Reporting***

We understand that one of the major impediments to the publication at an earlier date of the Queensland Local Government Comparative Analysis report is the provision of information from Local Governments. The primary time restriction is in terms of the process of completion of audits and production of Annual Reports. The legislation currently provides five month period to completion of audited financial statements for Local Governments in Queensland.

We note action taken within the Queensland public sector to reduce the time period for completion of audits and the lodgement of Annual Reports to Parliament. This has generally introduced a three month (reduction of one month) reporting period for departments, government owned corporations and public sector authorities generally.

A December 2001 report on Annual Reporting in the Queensland public sector by the Public Accounts Committee whilst not considering local government entities has recommend that ministers encourage agencies to report as early as practicable.

We have however suggested that the shorter timeframe for reporting be brought in from the 2003/2004 financial year to allow a period of time for Local Governments to implement a number of the changes currently in progress.

**Recommendation 10**     **It is recommended that the Department of Local Government and Planning in consultation with the Queensland Audit Office give consideration to a reduction in the time provided for the completion of Annual Reports included audited financial statements.**

# 1. BACKGROUND

## 1.1. Key Points

- Increasing complexity in financial management and the discharge of a Local Government's accountability to the community require that corporate plans and reports need to be presented in a style, format and standard that can be easily understood without specialist financial knowledge. Understood by managers, Councillors and the general community.

## 1.2. Developments in Financial Management in the 1990s

Since the early 1990s, there have been a number of financial management and related developments which have had an impact on Local Governments and which have required an increased level of management and councillor attention.

These include:

- Pressure on local governments to deliver a wider range of services to the community and to do so without significant increases in the level of available resources.
- Focus on more efficient and effective use of resources including commercialisation of business activities and demand management through user charging.
- The development of accounting standards for Local Government and the introduction of accrual accounting. This includes the development of financial statements including a Statement of financial position which reports on local government assets and liabilities.
- The introduction of asset management practices by local governments. These are often linked with Total Management Planning requirements for infrastructure assets subsidised by State government.
- The impact of national competition policy, regulated pricing and competitive neutrality arrangements (including tax equivalents) for certain activities.
- Wider use of internal Service Level Agreements.
- Out-sourcing of a wider range of services.
- Changes in purchasing arising from electronic cataloguing and procurement.
- Improvements in communication arising from e-mail and the use of the internet and corporate intranets.
- Changes to auditing processes including a mandate for performance management systems audits for the Queensland Auditor General.
- The availability of more sophisticated computerised financial management systems which provide the capability to provide flexible reporting of financial performance information.
- Greater community interest in matters of corporate governance.
- Developments in Balanced Scorecard and Triple Bottom Line reporting.

## 1.3. Corporate Governance

### *Accountability*

According to Dr Ted Campbell, Director-General Department of Local Government and Planning many Councillor duties can be discharged through an effective financial management process. Financial Management provides the means for a local government to:

- measure the achievement of the Council's objectives (management); and
- provide a means for the council to be gauged against its stated objectives (accountability).

Queensland Councils have a great deal of freedom in determining their own destiny. This responsibility and freedom brings with it the need for some form of accountability. Major accountability of the elected council is the community's reaction to its performance in elections held every four years. A council must spell out each term what its objectives are and provide reports which give the public a clear picture of performance against objectives. In addition it should set out clearly the level of standards it expects to achieve, and what the cost of achieving these standards will be.

The shift in social, political, financial and economic agendas by Councils needs to be sifted by processes of consultation and debate, and synthesised in a flexible form delivered as a corporate plan. The corporate plan needs to be reviewed each year and further distilled into a budget. The value of the plan depends on how well it is sold to the community.

This consultative approach to the production of reporting requires that the community have a very clear understanding of Council's performance against its corporate plan. This implies that corporate plans and annual reports need to be written in a style, format and standard that can be easily understood by the general community. There is the need for a balanced output which recognises both the professional and statutory requirements and the need for the community to know where the council is.

### ***Councillor Focus Group***

The Councillor focus group in June 2001 noted that being an elected member in Local Government brings with it a range of responsibilities not unlike that of a company director. In many respects, the responsibilities are wider in that, in addition to having management responsibilities for the community resources under their control, Councillors also have responsibilities to the community in terms of broader social, economic and environmental issues.

Elected members are entrusted with responsibility for significant community funded assets. As is the case with company directors (especially of a public company), Councillors have an important fiduciary duty for the effective and efficient use of all assets held. The statutory and common law duties which fall upon a company director include:

- to act in good faith in the best interests of the organisation;
- to act with care and diligence;
- to avoid a conflict of interest; and
- prohibiting the misuse of information obtained by directors.

Councillors have similar responsibilities, a number of which are outlined in Queensland's Local Government Act. Effective financial management encompasses many of the responsibilities of elected members.

### ***Information Needs of Elected Members***

The Councillor focus group identified the following information types as being needed by Councillors to meet their responsibilities. These are as follows:

<b>INFORMATION REQUIREMENTS</b>	
<b>STRATEGIC – FUTURE DIRECTION (ANNUAL)</b>	<p>In order to effectively carry out the responsibilities for the setting of the strategic direction the elected members need a range of information including:</p> <ul style="list-style-type: none"> <li>(a) Information on the growth within the community / details of units of rateable property / population trends / other economic information.</li> <li>(b) Information on the community needs and the priorities.</li> <li>(c) Details of external funding opportunities and grants.</li> <li>(d) A capital works plan which is drawn preferably from an asset management plan covering issues such as the replacement, refurbishment and renewals of assets and considering issues of funding options and the policy on funding of depreciation</li> <li>(e) Details of debt levels / trends over time and likely borrowing</li> </ul>

BEST PRACTICE SIMPLIFIED INTERNAL AND EXTERNAL REPORTING

<b>INFORMATION REQUIREMENTS</b>	
	<p>requirements</p> <ul style="list-style-type: none"> <li>(f) Information papers on the changing role of local government – service provision.</li> <li>(g) Details of the future impact of funded facilities / services</li> <li>(h) Future financial projections including information on trends with overall assets and liabilities and the operating capability of the Council.</li> </ul>
<p><b>BUDGETING &amp; OPERATIONAL PLANNING (ANNUAL – FEBRUARY TO JUNE)</b></p>	<p>In order to undertake the Budgeting and Operational Planning the Councillors will require:</p> <ul style="list-style-type: none"> <li>(a) A set of budget parameters within which the Council will manage the budget.</li> <li>(b) Details of the likely position in terms of asset/liabilities</li> <li>(c) Information on the likely impact of one off decisions for special funding.</li> <li>(d) Information on trends.</li> <li>(e) Details to allow an assessment of the liquidity of the Council including cash flow information</li> <li>(f) Prior year information and the expected end of year financial position for the year.</li> <li>(g) Information for effective management of infrastructure including roads.</li> <li>(h) Details of expected capital works including whole of life information on major infrastructure to allow an assessment of future impacts of current decisions.</li> <li>(i) Information on different scenarios and the funding options available.</li> <li>(j) Details of plant replacement</li> <li>(k) Details of reserves to be utilised and the management of reserves generally.</li> <li>(l) Specific attention to the construction of budgets to allow an assessment of the programs being delivered and an assessment of whether the services and activities are in line with the desired outcomes of the Council.</li> </ul>
<p><b>MONTHLY MONITORING OF BUDGET/ FINANCES</b></p>	<p>Monthly information required to enable a monthly monitoring of the budget to include:</p> <ul style="list-style-type: none"> <li>(a) Reporting on actuals as against the budget highlighting variances (noting that the budget should be activity driven)</li> <li>(b) cash flow information including forecasts of the expected outturn for the year (high level)</li> <li>(c) Additional reporting on any adverse positions (exception reporting)</li> <li>(d) Other analytical information associated with the performance year to date.</li> </ul>
<p><b>QUARTERLY OR RATE CYCLE MONITORING OF PERFORMANCE</b></p>	<p>Quarterly or Rate Cycle information on financial management will include:</p> <ul style="list-style-type: none"> <li>(a) Details of capital expenditure against the capital works budget including information on the physical delivery of projects.</li> <li>(b) Information on the performance of the budget to operational plans</li> <li>(c) Reports on major budget variances including information which may require the Budget to be varied.</li> <li>(d) Reporting of key performance information – service performance which links financial information with non-financial measures.</li> <li>(e) Information on position with key ratios including likely position at the end of the financial year.</li> <li>(f) Reports from commercialised or corporatised entities.</li> <li>(g) A report on the compliance with the financial requirements and on the audit controls.</li> <li>(h) Report to Council on the systems including progress with the implementation of any new systems or processes.</li> <li>(i) Specific reports on areas of efficiency improvement or savings sought through the budget process.</li> </ul>

## 2. METHODOLOGY AND FRAMEWORK

### 2.1. Key Points

- An organisation's level of risk will determine the focus of its performance indicators.
- Councils as a tax raising authority have lower financial risk than many other entities. There, performance indicators will have a bias towards social returns.
- The risk profile of segments within a council, for example a commercialised service unit, may force a different reporting focus to the council as a whole.

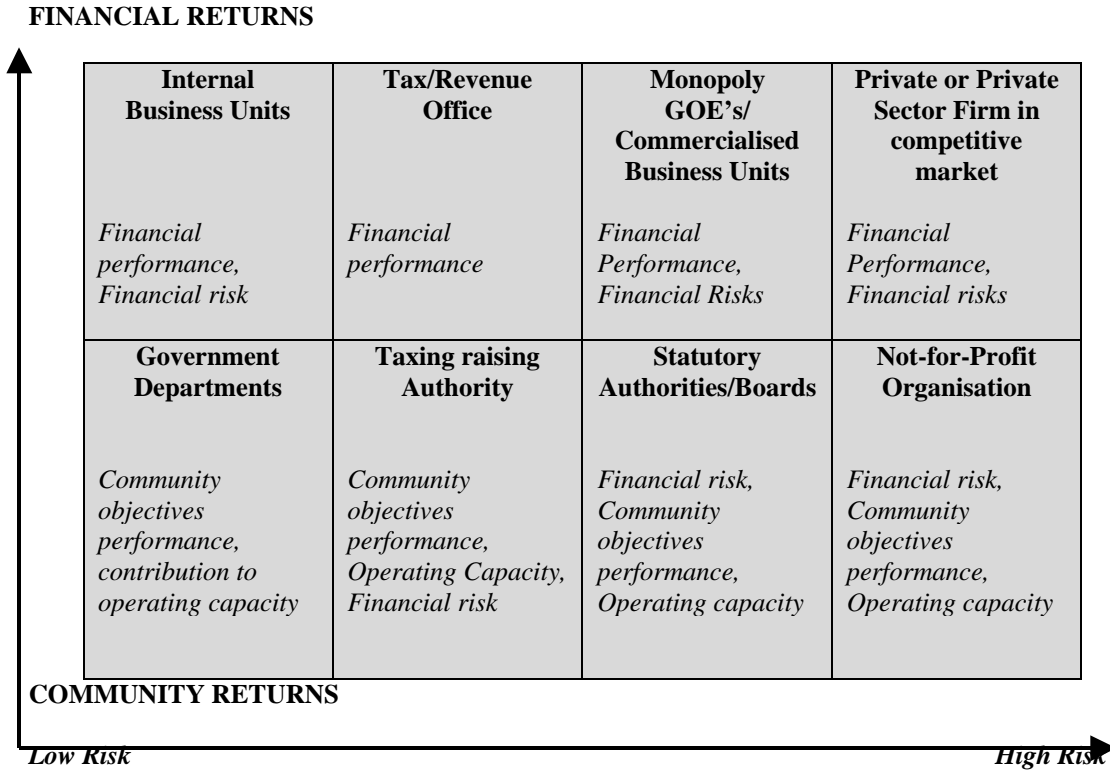
### 2.2. Framework

In the landmark publication "The Leading Company: Growth, Learning and Longevity in Business" Arie de Geus outlines the criteria for organisations to be successful in the long-term. He notes that "we can see that money must play an important role in a company's survival and evolution. With money, a company can buy resources (and time) which allow it to evolve more rapidly. In addition, people who see companies as machines for earning money measure the success of a company's evolution by the extent to which it can make more money than its competitors." He then outlines the possibility that leaving too little money in the organisation could reduce the survival chances of the company, and looks at the research on the criteria for survival organisations. His conclusion is that 'long-lived organisations have a conservative approach to financing. They were rigidly careful about their borrowing and investment capital.' Any organisation's survival therefore is not only related to performance of its objectives, but also the risks it takes in creating its operating capacity.

The following KPI framework model was developed by David Spearritt and further researched by Assoc. Prof. Chew Ng for the Public Sector Accounting Centre of Excellence, CPA Australia.

The starting point of this model is to regard an organisation as an investment by its stakeholders and to assess that investment in terms of the risk and return profile of the organisation. In relation to risk, independent entities which have to raise their own funds have a higher risk than those which are funded through a Government or Council budget. Along this continuum, entities that are funded from a government budget (such as a government department) have low financial risk, followed by independent entities such as a government or local Council which have taxing powers. Organisations which generate revenue in a monopoly market have more risk than a taxing authority but less risk than a firm operating in a competitive market. Entities which have tax raising powers have a different risk profile from those which have to generate their revenue in a competitive market. In relation to return, the main variable is whether the entity has been established to provide a social return to the community, or a financial return to its shareholder. These factors create different issues for monitoring and assessing the performance of the organisation, as shown in the following diagram.

FIGURE 1: REPORTING FOCUS OF AN ENTITY



Local governments are often comprised of a number of these types of entities. For example Ipswich City Council is a tax raising authority which has a number of departments with community objectives, several internal business units with financial objectives, the Finance Department which levies rates, a monopoly business units in the form of Ipswich Water. The Council also owns a private company Global Info-links operating in a competitive environment and controls the Ipswich Arts Foundation which is a not-for-profit organisation. Each of these entities has internal and external financial reporting requirements.

Council and government departments are characterised by having low financial risk and a focus on social returns. Therefore, performance indicators amongst this group need to focus primarily on the achievement of community objectives. Financial risk issues will largely be secondary and mainly be used to ensure that liabilities are not unnecessarily incurred impacting on their owner government or Council. Financial performance issues are usually not paramount except for the obvious need to remain within budgetary allocations. However, Councils need to develop their operating capacity to deliver services which satisfy community objectives.

Tax raising authorities similarly need to monitor achievement of community objectives. However monitoring financial risk, for example, levels of debt is necessary to ensure continuing viability of an independent entity, and to ensure that debt levels do not cause future increases in taxes and rates. Financial performance is usually related to the extent to which the operating results affect the operating capacity of the organisation. In the widely referenced Brisbane City Council publication ‘Accounting Concepts for Accountability in Local Government’ the Council applied the physical concept of capital whereby:

‘Capital is understood to be operating capability provided by the resources (assets) of the entity. Profit, therefore, is considered to be the total gain arising during a period, which could be distributed in full whilst still maintaining capital, in the sense of the operating capability, at the level which existed at the beginning of the period.’

Under this concept of capital, the entity viewpoint of financial reporting is applicable. This holds that the objectives of the entity are to continue to carry out particular functions. ‘These may include profit-making through specific business activities for my hands of, ... the supply of services including the

custodianship of public assets'. But from those viewpoint, 'the primary requirement is to maintain the ability of the entity to carry out the functions which are its *raison d'être* and it is there for all concerned with maintaining the physical operating capacity which will enable it to do so.' From this perspective, financial performance is related to improvements in the physical operating capacity of the Council.

Statutory authorities, for example in government control markets, usually have a number of community objectives which need to be achieved. However since revenue is predominantly from trading activities, the level of risk is higher and there is a need for appropriate monitoring of activities. Such entities usually also have some financial objectives.

Not-for-profit organisations are financially independent and usually operate in a non-monopoly trading environment. Therefore financial risks need to be closely monitored. However, their prime reason for existence is to achieve community objectives and therefore these need to be monitored. Financial performance monitoring is also required since these organisations need to generate sufficient operating surplus to be able to achieve community objectives.

Internal business units are similar in nature to government departments with the key difference that they have financial performance requirements rather than community objectives. They have a lower level of financial risk than corporatised business units or government owned enterprises and therefore monitoring financial risk is a lower priority.

Government and Council revenue offices are primarily concerned was generating income through taxation measures. Therefore, these offices are focused on financial results rather than social performance of financial risks. However the organisation faces implicit community objectives to ensure that the cost of collecting tax revenue is minimised including inconvenience to the taxpayer.

Government business enterprises usually are primarily focused on achieving financial results. The owning government or Council may require community objectives in the form of Community Service Obligations, however a government or Council normally funds. Since these organisations have a high level of financial independence financial risk issues need to be closely monitored.

Public and private firms operating in fully competitive environments will be primarily focused on achieving financial performance and minimising financial risks. The emphasis of this report is on the whole of council as an independent taxing authority. However, the KPI framework of an entity model allows the issues to be transported to other sectors for indicators that are common.

## 2.3. Types of Indicators

From the above analysis it can be seen that key indicators comprise three main categories: financial performance, social objective performance, and financial risk. In the private sector financial performance indicators have been developed over a long period of time. These centre on profitability indicators such as earnings before interest and tax (EBIT), and are supplemented by number of analytical measures to assess the source and sustainability of profitability. In the public sector, as we have noted, financial performance is related to changes in the physical operating capacity of the organisation.

**Community performance indicators** will necessarily be different for each organisation which these are applicable to. In each case these need to be directly derived from the defined objectives of the organisation. However, some generic indicators have been included in this study, such as 'value for money' measures.

**Financial risk indicators** are normally grouped into two main categories based on the time perspective. Short-term indicators monitor liquidity or the ability of the organisation to pay its bills, whereas the long-term indicators relate to long-term solvency issues such as the overall level of gearing or debt.

**Operating capacity indicators** cover a range of issues such as the level of capital investment and replacement, as well as revenue and expenditure issues.

## 2.4. Accountability and Management Cycle

### *Financial Management Cycle*

Most organisations have a management cycle where resources are allocated through internal processes to produce product or service outputs, aimed at achieving desired outcomes. Ideally there is a regular review process to adjust these factors and improve outcomes. This process is managed by the organisation's leadership through applying and developing strategies, structure, and culture by means of organisational policies and procedures.

FIGURE 2: ORGANISATIONAL MANAGEMENT CYCLE<sup>1</sup>

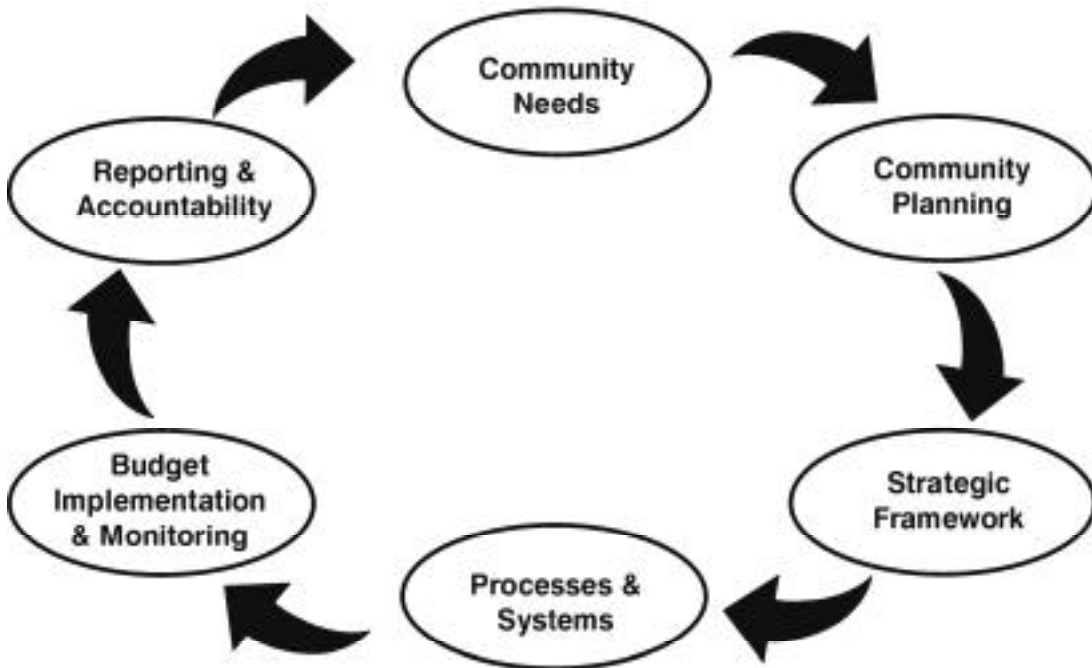


A similar process operates for the financial management cycle. At the beginning of this cycle strategies are formulated, budgets developed and monitored, with accountability reports on the outcomes. This model is outlined in the following diagram. Ideally the organisational and financial management cycles are synchronised.

Each point in this cycle management requires different information. At the strategy development stage, management needs strategic information such as long-term forecasts and models, comparative benchmarks, economic parameters, and information on new and emerging issues which need to be addressed to meet community needs. As the budget is being developed information is required on the resourcing impacts on service levels and on the progressive budget balance. During the financial year, strategic indicators become less important and focus on monitoring adherence to the budget planning an achievement of the desired outcomes. During the implementation of the budget ongoing work is required to ensure productivity improvements occur and the community is receiving value for money. At the end of this cycle management is required to report on its performance in accountability reports such as the annual report and the audited financial statements.

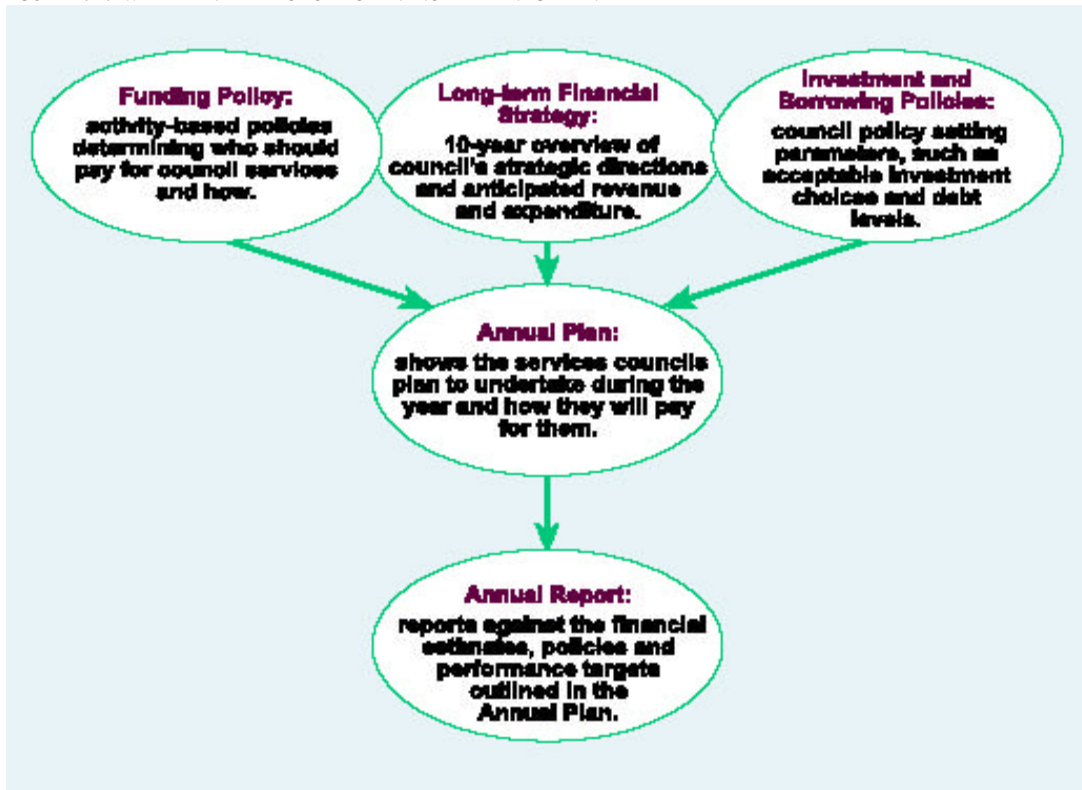
<sup>1</sup> Developed by David Spearritt and Alex Taylor

FIGURE 3: FINANCIAL MANAGEMENT CYCLE<sup>2</sup>



The following diagram outlines the New Zealand approach to financial management, which is similar to that outlined above but not shown as an annual cycle.

FIGURE 4: NEW ZEALAND APPROACH TO FINANCIAL MANAGEMENT



<sup>2</sup> Developed by David Spearritt and Alex Taylor

## **2.5. Methodology**

The Methodology applied in this project will be to review the documentation literature throughout Australia and the world, both in terms of conceptual theory and practical case studies, with the emphasis on the last 10 years. Research will be conducted in three areas namely the external reporting, internal reporting, and performance management reporting. In order to determine this practice, the examples uncovered will be assessed against the risk return framework outlined above (with particular reference to community objectives, financial risk, and operating capacity issues) and the accountability and management cycle. In each area, the research will penalise developments in both the issues reported on as well as reporting techniques. From this conclusions will be developed and recommendations presented.

## 3. REPORTING GENERALLY

### 3.1. Key Points

- Primarily reporting needs to be seen as a means of communication.
- For the facilitation of decision making, either internally by management and councillors or externally by the community, reporting needs to:
  - contain relevant and reliable information; and
  - be presented in a comparable and understandable way.
- For communication with external reporting users non-traditional means of reporting need to be explored. For example the use of the internet and leaflets.

### 3.2. Attributes of a Report<sup>3</sup>

The purpose of financial reporting is the disclosure of information useful to the recipient<sup>4</sup>. In this way the preparers of financial reports discharge their accountability to the users. To discharge this function financial reports are required to have the following characteristics.

#### *Choosing which Financial Information to Present*

Relevance and reliability are the primary qualitative characteristics which financial information should possess in order to be the subject of general purpose financial reporting.

**Relevant** information is information ‘that has predictive power or feedback value and is timely’<sup>5</sup>. It influences the user’s decision-making by:

- (a) helping them form predictions about the outcomes of past, present or future events; and/or
- (b) confirming or correcting past evaluations; and

which enables users to assess the rendering of accountability by preparers.

**Reliable** information is ‘information that is complete and offers a fair presentation. It represents faithfully what it purports to represent and avoids the use of excessive language. It is neutral (that is, free from deliberate or systematic bias), balanced (includes bad news) and free from material error’<sup>6</sup>. Information that is subject to material uncertainties can be presented in the notes or supplementary schedules provided that there is a faithful presentation of the information including the uncertainties surrounding it. The information should be free from bias (that is, the information should be neutral). It should not be designed to lead users to conclusions that serve particular needs, desires or preconceptions of the preparers. Independent audit is important in relation to reliability

Once it has been decided that financial information is relevant and reliable, it is necessary to consider the information in the context of the individual circumstances of the reporting entity in question. The Materiality Test should be applied. The **materiality test** measures the extent to which relevant and reliable information may be omitted, misstated or not disclosed separately without having the potential to adversely affect the decisions made by the users of a report.

#### *Choosing how to Present Financial Information*

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<sup>3</sup> Statement of Accounting Concepts SAC 3 “Qualitative Characteristics of Financial Information”

<sup>4</sup> Statement of Accounting Concepts SAC 2 “Objective of General Purpose Financial Reporting”

<sup>5</sup> CICA MDA

<sup>6</sup> CICA MDA

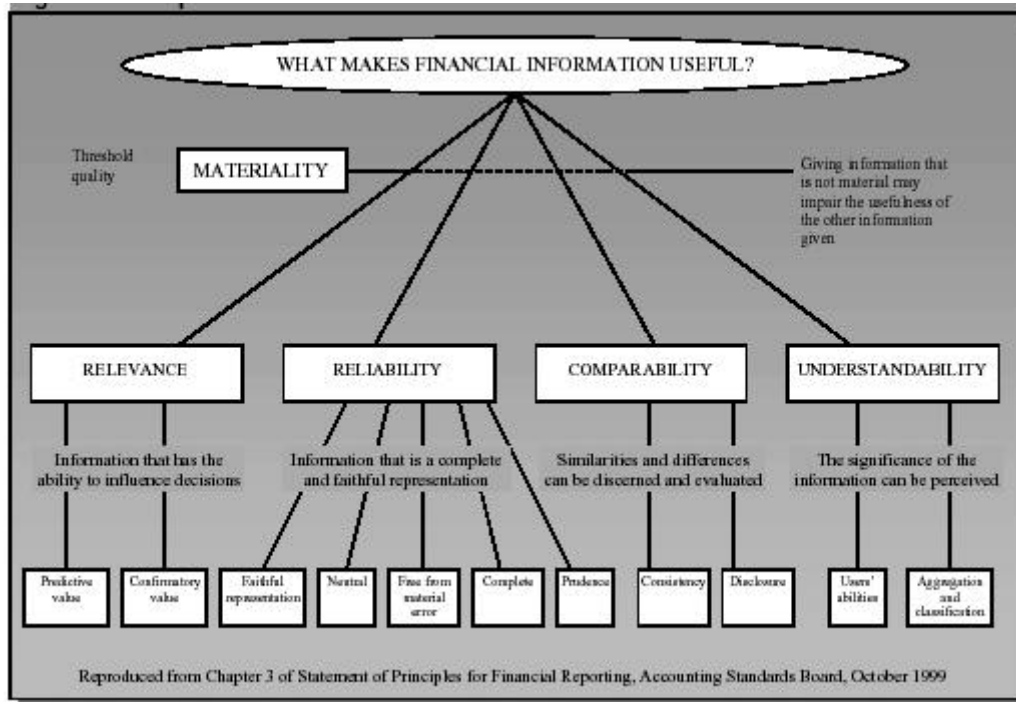
It is not enough that financial information is relevant and reliable. It also needs to be comparable, understandable, timely and cost efficient (the benefit exceeds the cost of preparation).

**Comparable** information enables a user to discern and evaluate similarities in, and differences between, the nature and effects of transactions and events, at one time and over time, either when assessing aspects of a single reporting entity or of a number of reporting entities. **Comparability** enables ‘meaningful trend identification and analysis over successive time periods and facilitates benchmarking among companies and business segments’<sup>7</sup>.

Comparability implies **consistent**, ‘once information is disclosed it should be updated and explained unless it becomes irrelevant. If no longer irrelevant, this should also be explained. In particular, performance measures, once selected and disclosed, should be reported consistently from period to period unless explicit explanation is given. The reporting entity should not avoid discussion of a previously raised issue by simply omitting it from a subsequent report.’<sup>8</sup>

**Understandable** information exists when users of that information are able to comprehend its meaning. This will depend in part on the capabilities of the users but reports are to be prepared for users who are prepared to exercise diligence in reviewing those reports and who possess the proficiency necessary to comprehend the significance of contemporary accounting practices.

FIGURE 5: WHAT MAKES FINANCIAL INFORMATION USEFUL?<sup>9</sup>



### 3.3. Reporting Techniques

Knowledge Management: The Basics, by Dr Dennis Sinclair and Dr Neil Hardie (CSIRO publication): Data is the sea of facts which surrounds us, much of it low quality, irrelevant or redundant. From this sea of data we have to select and combine relevant bits to create *information* - that which ‘informs’ people. Statisticians are very good at turning data into information. Information comes in many forms: graphs and tables, financial statements, the Balanced Scorecard, procedures manuals and work instructions, notice boards, newsletters, memos, e-mail, etc. People transform this information into knowledge through a process of learning and understanding. Clearly knowledge is a personal thing, and thus human capital or intellectual assets become a high priority for any organisation.

<sup>7</sup> CICA MDA

<sup>8</sup> CICA MDA

<sup>9</sup> Prospective Financial Information: Challenging the Assumptions (A discussion paper)

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In the Canadian model 'one of the key processes at the Information Level is to provide consistent and comparable financial and operational (non-financial) information and reports that meet the needs of managers. This information provides a basis for developing performance indicators, cost and quality measures and monitoring performance, to ensure that intended results are being achieved and to demonstrate accountability.

This capability flows from a history of having measured and managed organisational performance, which includes, for example:

- managing the organisation's information and knowledge resources as assets, so that information needed to make informed decisions is available (for example, by using simulations, historical trends and manipulating variables to see how they affect results);
- defining the relationships among variables that affect cost, quality and level of service and understanding how they impact on the organisation's desired results;
- using information to make informed choices among competing objectives like cost, quality and schedule;
- understanding the financial implications of decisions before making them, and monitoring their outcomes;
- using quantitative information to control variances (for example, fluctuations or changes) in the organisation's production or service delivery processes; and
- using quantitative information to balance among competing business line objectives (examples include, to reduce cost, increase productivity, improve quality, reduce risk, increase opportunities).'

## 4. PERFORMANCE REPORTING AND MEASUREMENT

### 4.1. Key Points

- Performance Measurement allows for the quantitative reporting of progress against the Local Governments Corporate Plan.
- Performance Reporting is often easier for report users to understand than traditional financial reporting.
- Generally, performance measures required for reporting are unique for each corporate plan.
- A range of prescribed performance indicators allows for the benchmarking of councils on key issues (financial viability). External benchmarking assists with internal management (what is reasonable performance) and the discharge of accountability.
- Relying on budget variance reporting is insufficient to ensure that the council remains solvent and is effectively managed.

### 4.2. Performance Management Framework

#### *General*

There is little difference between an organisation that fails to set objectives and one that sets objectives and fails to measure the output of them<sup>10</sup>.

The use of pre-determined objectives and performance reporting measures can help to overcome many previously experienced shortcomings in reporting. Reports from UK and US indicate that councillors and senior managers are often better able to understand their progress toward the achievement of desired results from reports based on performance measurement than from reports based simply on revenue and expenditure amounts.

There is an increasing expectation that national, state and local government bodies should operate in an open and accountable manner that includes the measurement and disclosure of performance.

The Commonwealth Government and each state and territory has adopted the principle of performance measurement and performance based management. It applies to Commonwealth and State Government agencies and to local governments. Australia wide, all levels of government are working toward improving their knowledge of community requirements, improving their practices in delivering services to meet those requirements and improving the evidential disclosure of performance efficiency and effectiveness<sup>11</sup>.

Reporting on performance in terms of outputs delivered allows an organisation to monitor the full accrual cost and the performance against the targets set. The attention to performance enables the active management of the overall financial position and the use of resources.

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<sup>10</sup> Department of Local Government Western Australia January 2001. "Performance Measurement Guidelines for Western Australian Local Governments". Part 1 Introduction

<sup>11</sup> Department of Local Government Western Australia January 2001. "Performance Measurement Guidelines for Western Australian Local Governments". Part 1 Introduction

The leading business thinker, Peter Drucker in "The Information Executives Truly Need" Harvard Business Review January-February 1995, claims that there are four sets of diagnostic tools to enable executives to make informed judgment. These are foundation information (key cash flow and liquidity measures), productivity information (especially the emerging use of economic value added measures), competence information (eg. innovation and research), and resource allocation information. In Chapter '7. Internal Reporting' it will be demonstrated that this is a very similar methodology to the balanced scorecard.

Osborne and Gaebler, in their influential book 'Reinventing Government' (1992) claimed that 'Because they don't measure results, bureaucratic governments rarely achieve them. With so little information about results, bureaucratic governments reward employees based on other things...' (p139). They also noted 'a growing frustration among taxpayers that they don't know what they're getting for their money.' They praised the performance management approach of Sunnyvale City Council in Silicon Valley, California: 'by measuring results, Sunnyvale gives its decision-makers the information they need to make intelligent decisions. They can tell success from failure.' Sunnyvale developed a four-part Municipal Performance Index, to monitor productivity improvements. This index has now been turned into a quality of life index.

Six principles of effective performance measures are:

- external focus, meaningful to customer or consumer;
- relevant, realistic, simple and consistent;
- provides a full and accurate picture;
- manageable (no of measures usually around 5 for each output group or sub- output)
- clear and understandable; and
- stated positively, providing guidance on what to do instead of what not to do.

The performance measures should incorporate the following criteria:

- **Quantity:** sometimes difficult to state precisely in first performance specification. If an estimate is provided there should also be range from which the estimate is taken, information on what the estimate is based upon, the level of confidence and a sensitivity analysis.
- **Quality:** includes dimensions such as: accuracy; completeness; accessibility; availability or continuity; risk coverage; compliance with legal standards and satisfaction of customer needs.
- **Timeliness:** perhaps overlaps with the perspective of quality, but the importance of timeliness warrant a separate measure.
- **Location:** specifies location of delivery.
- **Cost:** measured in total, average and/or unit basis. This performance measure is crucial to benchmarking or market testing.

## *Australian Jurisdictions*

### *Australia*

A report by the Productivity Commission an Australia, states:

'Traditionally, much of the focus on improving the effectiveness of government services has related to increasing the level of resources. This focus overlooks another important means of enhancing services — that is, finding better ways of using existing resources, and encouraging productivity growth. Productivity growth has had an important influence on living standards in Australia, accounting for about two thirds of the increase in average real income per person over the past three decades (IC 1997). Innovation (the introduction of new products or processes) can be important to productivity growth in all sectors, including government services. Providing performance information across jurisdictions can help spread innovation (and thus facilitate performance improvement) by identifying potential jurisdictions from whom other jurisdictions may learn. Reporting comparative performance can foster yardstick competition by promoting greater debate about comparative performance. Performance reporting is an important step in benchmarking. Reporting on comparative performance can also help government

assess whether the community is receiving the best set of services, and whether these services are being provided to those most in need, so as to achieve the best outcomes in the community.’

‘The Commonwealth Government has decided to introduce Service Charters for all departments and agencies that deal with the public. Both direct and indirect service delivery functions, as well as regulatory functions are covered in the initiative. Those agencies with policy development functions are also encouraged to develop Charters. A Service Charter is a simple public document; developed in consultation with staff and customers that continually grows with an organisation. It sets out the standards of service customers can expect. A Charter is a strong performance measurement and accountability tool as it focuses on customer service outcomes.’

‘The Government’s agreed framework for developing Service Charters is set out in the document *Putting Service First: Principles for Developing a Service Charter* which was developed by a task force of consumer, business and government representatives. In August 1997 a *Commonwealth Implementation Timetable* was published outlining each Minister’s commitment to develop Service Charters within his or her portfolio. In November 1997, the Government published *Developing Service Charters — A Guide for Commonwealth Departments, Agencies and Enterprises*,’

In the Productivity Commission report on Performance Indicator’s the Commission considers the following matters are relevant to local government:

- performance measurement should be linked to service outcome objectives directly;
- comparative performance measurement is most effective where there is responsibility and accountability but no competitive market pressure (In this case, resulting ‘yardstick’ competition can provide pressure for improved performance);
- the performance measurement process is likely to work more effectively when it:
  - tackles data issues iteratively;
  - makes any assumptions and qualifications transparent; and
  - is managed independently of service providers but takes advice from them;
- it is helpful to develop a framework which outlines the relationship between efficiency and effectiveness objectives and each outcome indicator;
- the context in which services are delivered needs to be taken into account in interpreting reported performance, with descriptive indicators identified and separately presented from the performance indicators; and
- performance measurement does not obviate the need for sound judgement in assessing the level of performance, that takes account of the local conditions and preferences.

According to the Commission, ‘the goal for performance measurement should be to develop and publish dispassionate and objective data to facilitate well informed judgements which result in sound public policy action.’

The commission noted,

“that many local governments have outlined their objectives in terms of the outcomes to be achieved, often as part of their corporate planning. However, an important part of developing comparative performance indicators is reaching agreement on a common set of objectives for activities across the participating organisations, recognising that differences in local communities will be reflected in the weighting placed on each objective in the set. As yet, a process to reach agreement across each state on a common set of objectives against which performance should be measured for local government and/or each of its activities does not seem to have been undertaken.

Performance measurement is not costless, requiring considerable effort to identify appropriate indicators and collect and analyse data. Thus, wherever practicable, the Commission has:

- drawn on the work and information collected as part of other performance measurement exercises; and
- used existing data collections such as those for agency annual reports and those undertaken by the Australian Bureau of Statistics.

However, as a result of differing objectives and priorities, all of the data required for performance measurement may not be available from parallel exercises and existing data collections. In this case, additional data collection effort may be required for the timely reporting of a complete range of performance information.”

### *State Government Agencies*

As part of our research we have reviewed actions being taken in terms of performance management including performance reporting by two Queensland Government Departments and a Government Owned Corporation. We have noted that both of the government departments reviewed have or are in the process of upgrading internal and external reporting through the use of a Balanced Scorecard approach.

One of the departments has invested heavily at the time of developing its 2000-2005 Corporate Plan in terms of grouping the strategies adopted into the following four groupings and identifying performance measures and the methods of measuring performance, which is adapted from the Balanced Scorecard.

The four groups are:

- Client and community relationship;
- People, learning and growth;
- Internal business processes; and
- Resource management.

This has been achieved again working within the Managing for Outcomes requirements including the overall priorities of government.

As stated in the Corporate Plan

‘Performance management includes evaluation of the Department’s outputs against statewide trends measuring economic, social and environmental changes in Queensland. This broad approach to our external performance is balanced by a focus on measuring our internal performance. In this way, we establish linkages between our actual performance, the expectations of our stakeholders and clients and how well we integrate our people, business process and resource management capabilities to provide high quality services. Investment management processes are critical linking processes in the performance framework.’

The Annual Report for 2000/2001 of this department incorporates a six-page report on internal measures of performance utilising the Balanced Scorecard perspectives.

The Government Owned Corporation reviewed has been going through a process to upgrade internal reporting to the Board concentrating on greater use of graphical information (Bar Charts etc) with the aim of providing easier to read information for Board Members and to provide an executive summary outlining any key issues related to the information provided.

The Annual Report of the Government Owned Corporation provides a report on performance primarily in financial terms although reporting is also provided on activities and management of same during the year, corporate governance, details of the Statement of Corporate Intent and information of initiatives to develop people within the organisation. Whilst having not adopted a triple bottom line or balanced scorecard approach the Corporation provides as part of the Annual Report folder an Environment and Social Report.

### *Tasmania*

Recently, Tasmanian councils have recognised the importance of greater accountability to their communities and the need to develop a measurement system to enable performance to be managed and monitored. They have identified two areas of performance measurement for Local Government

- Community Measures that describe the state of a Community in areas such as the economy, social well being and environmental health.

- Organisational Measures that describe the performance of a council as an organisation.

As this stage the Tasmanian Councils have chosen to focus on organisational measures.

The key areas for performance measurement outlined are:

- Governance;
- Management and finance;
- Regulatory;
- Infrastructure and utilities; and
- Community services and development.

### ***Western Australia***

In Western Australia it has been a statutory requirement since 1996 for WA local governments to disclose in their principal activity plans and annual reports the details of their objectives and performance measures. The Local Government Act 1995 established a statutory requirement for performance measurement but makes no attempt to prescribe the indicators to be used.

The performance measurement expectation has a basis in the principles of:

- Quality customer service delivery;
- Continuous improvement;
- Practical accountability; and
- Value for money.

Performance measurement compares a single organisation's achievements in relation to its own predetermined goals – not the goals of others. Local Governments must themselves develop performance indicators that best measure the achievements of the unique objectives.

FIGURE 7: COMMON TERMS IN WESTERN AUSTRALIA

Some Common Terms		
Services	= What we are about to do.	= Principal activities
Targets	= What we aim to achieve by doing it.	= Objectives
Worldload	= The extent to which we will do it.	= Comparative indicators
Outcomes	= The ratio between input (resources invested) and output (services or benefits delivered).	= Efficiency indicators
Achievements	= How well we achieved what we set out to achieve.	= Effectiveness indicators

### ***Other Jurisdictions***

#### ***United Kingdom***

The UK Audit Commission has stated that Performance Measurement is the essential foundation on which Performance Management can be built. Performance Measurement allows:

- improved public services;
- improved accountability;
- help identify good practice and learn from others;
- ensure that the organisation is focused on its key priorities; and
- affect the behaviour of the organisation through choice of performance indicators.

According to the UK Audit Commission effective Performance Measurement comprises the following attributed.

- **Clarity of purpose.** Understand who will use the information, and how and why the information will be used.
- **Focus.** Focus on the priorities of the organisation – its core objectives.

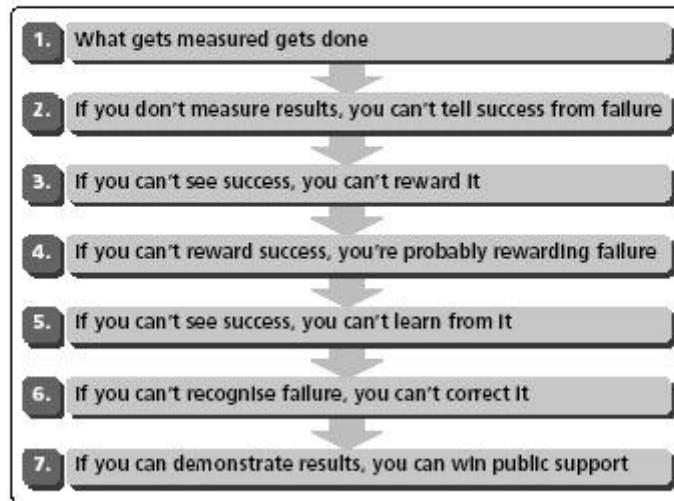
- **Alignment.** Performance measurement system should be aligned with the objective-setting and performance review processes of the organisation.
- **Balance.** A balanced picture of the organisation's performance.
- **Regular Refinement.** The performance measures should be kept up to date to meet changing circumstances.
- **Robust performance indicators.** See the discussion on performance indicators below.

FIGURE 7: UNITED KINGDOM REASONS TO MEASURE PERFORMANCE

EXHIBIT 1

Why measure performance?

Performance measurement can contribute to effective services.



Source: Extract from Osborne & Gaebler, *Reinventing Government*, 1992

### *New Zealand*

New Zealand undertook a significant program of reform in public sector management including financial management during the 1980s and 1990s.

A number of the reforms were:

- Separation of ownership and control in government businesses from departments;
- Separation of the government's interests as the owner of an organisation from its interests as the purchaser of the services of that organisation;
- Separation of funding, purchasing, and provision of public services;
- Clear specification of the performance objectives of government organisations, using commercial financial criteria for business organisations and outputs for core government administration;
- A distinction between outputs and outcomes; and
- Introduction of competition between service providers.

One element of the framework is the question of reporting on performance. As indicated by Scott Ball and Dale "(t)o give effect to the "purchase" dimension of performance in the annual report, departments are required to include a statement of service performance. This statement reports the outputs (services) produced by the department during the preceding period, so that these results can be compared against the prior specification of what was to be produced."<sup>12</sup>

<sup>12</sup> Scott, Ball and Dale (1999) – *New Zealand's Public Sector Management Reform* in *Reforming the Public Sector - Problems and Solutions* edited by Clark C and Corbett D.

The authors went on to note that as compared with the private sector where the customer is in the best position to monitor the delivery of services in the public sector the recipient of the service is frequently not the purchaser. The recipient of the service is less able to signal dissatisfaction through actual or threatened withdrawal of custom or legal action in relation to an existing contract. New Zealand in introducing the statement of service performance is attempting to substitute for the incentives associated with customer performance monitoring.

### *United States*

The US General Accounting Office noted (1999) “High-performing organisations consistently strive to ensure that their organisational missions and goals drive day-to-day activities. ...Performance improvements [do not] occur merely because an agency has issued an annual performance plan. Rather, performance improvements occur when agencies transform their organisational cultures so that achieving results becomes the driving concern of daily operations and when agency managers and external decision-makers use results-oriented plans and the planning and management processes that underpin them to inform decisions.”

### *Canada*

The Canadian Government is implementing a Financial Management Capability Model. Under this model, the following are the three essential elements of financial management:

- **Risk management and control.** It is essential that an organisation identify the risks it faces (anything that could interfere with its ability to achieve its established objectives); and that it establish a framework designed to manage and control those risks. An essential part of risk management and control is an environment that communicates the purpose, values and ethics of the organisation.
- **Information.** It is essential that the organisation establish procedures to manage and protect the integrity of its data and to produce the type of information needed by managers to conduct their business and account for their responsibilities. The organisation must also present this information when it is needed. This element includes management of information systems and financial and non-financial (operational and program) performance information.
- **Management of resources.** This component of financial management focuses on managing and directing the organisation’s resources economically and efficiently to achieve corporate objectives. It includes strategic planning, analysis and support for decisions.

The model outlines five levels of development in financial management. At the Information level, key process areas focus on integrating the organisation’s financial and non-financial systems, practices and procedures to provide information that can be used to manage resources with prudence and probity and in an efficient and economical manner.

At this level of development, an organisation will be capable of both measuring and managing its risks, and can tailor management practices within its various operating units to manage and reduce risk cost-effectively. At Level 3, the organisation will have information on the cost of producing a product of a given quality or delivering a service at a given level.

A key aspect of the information level is the changing role of the Finance function. The role begins to move away from performing only the traditional accounting functions to performing as a team player providing valuable support to operational managers. Finance works with operational managers to develop a financial structure that provides them with cost-effective controls and information. This information meets their day-to-day needs, for example, information on product costs. Operational managers have a broader understanding of their financial management responsibilities. They also recognise their responsibility to contribute to the organisation’s financial management capabilities.

Critical to achieving this level of capability is a climate that institutionalises financial management practice throughout the organisation’s culture. This would require that senior management explicitly demand and promote effective financial management and demonstrate its value. Such a culture is developed by formalising financial management policies and practices across the organisation and

supplementing them with appropriate training - and a system of rewards, recognition and sanctions that reinforces the culture.

At the Information Level, organisational standards for all processes and activities have been established to allow for measurement and comparison between similar business units across the organisation. These standard financial management practices can be tailored to each unit's nature and unique risks.

At the Optimising Level (Level 5) the focus is on continuous improvement. The organisation uses what it has learned from past experience to identify areas for future improvement. This involves:

- developing prospective information to anticipate both internal and external changes that may affect the organisation's performance (instead of reacting to changes) and making the necessary strategic or tactical decisions to manage their effects;
- measuring the organisation's performance against that of others in the same industry and setting strategic targets for improvement;
- finding best practices and learning from other organisations (benchmarking); and
- finding ways to minimise costs and maximise revenues, and to improve the quantity and quality of outputs, by introducing new technology or improving existing processes.

Gaston in "Successful Management Strategies for Creating the Knowledge-Oriented Organisation", *Mining Data for Knowledge*, 1997, Canadian Institute of Chartered Accountants (CICA), outlines the following steps to become a knowledge-oriented organisation:

- determine the knowledge that management needs and linking this to measurable goals and key corporate objectives;
- define the role and responsibilities of a knowledge officer;
- create a corporate knowledge policy that defines the needs and the means of obtaining and effectively mining knowledge;
- utilise knowledge management tools;
- determine the technical expertise required; and
- create strategic information systems plans and overall systems architectures and structures to feed and nourish knowledge workers.

### **4.3. Performance Indicators in Local Governments**

#### ***Definition***

Performance measurement is a simple process of identifying what will be done, what it will achieve and then reporting the quantitative and qualitative data gathered to measure and substantiate the achievements. Data that can be applied to formulae is commonly known as a performance indicator.

The development and use of performance indicators by councils for internal management purposes has increased markedly in recent years. This is being driven in part by the changes in local government legislation (for example, in New South Wales and Victoria) to require councils to adopt more strategic planning processes, including the development of corporate plans. In addition, the increasing sophistication of local government management is encouraging improved planning and performance measurement. The development of council and service specific objectives is a core element of corporate planning and the development of performance indicators to measure achievement of these objectives is now common. The Maribyrnong City Council noted that 'in Victoria, implementation of corporate planning principles has stimulated the development of performance indicators'.

#### ***United Kingdom<sup>13</sup>***

The UK Audit Commission, which oversees local governments, states that performance indicators should be used within a wider framework of performance measurement systems, performance

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<sup>13</sup> Audit Commission UK "On Target: The Practice of Performance Indicators". <http://www.audit-commission.gov.uk/publications/brtarget.shtml> Visited 18 January 2002.

management and overall strategic management of services and that robust performance indicators have the following attributes.

- Relevant to the aims of the and objectives of the organisation;
- Clearly defined, to ensure consistent collection;
- Easy to understand and use;
- Comparable and sufficiently accurate to allow comparisons between organisations and over time;
- Verifiable;
- Statistically valid;
- Cost Effective to collect, the benefits of using the information outweigh the cost of collection;
- Unambiguous, and clear as to what constitutes good performance;
- Attributable, so that the responsibility for achieving good performance is clear;
- Responsive, to reflect changes in performance clearly;
- Avoid perverse incentives and encourage behaviours leading to service improvement;
- Allow innovation in service delivery; and
- Timely.

### ***Tasmania***

Performance Indicators are measures that focus on the achievement of outcomes most critical to the current and future success of the organisation and have the following characteristics:

- Directly related to performance outcomes;
- Clearly defined in respect of purpose and use;
- Understandable; and
- Cost effective to collect.

Councils usually develop measures to monitor their own performance over time. This is good management practice. However, councils cannot use Council level indicators to compare their performance with that of others. To maximise their performance, they need to be able to identify what is attainable. They cannot know this unless they can compare their performance with that of other councils or other similar organisations. The lack of uniformity in the indicators developed at the council level and the extent to which this restricts inter-council comparison by councils, governments and taxpayers, is creating greater interest in development of statewide sets of indicators.

## ***Use of Performance Indicators***

### ***New South Wales***

In New South Wales, the *Local Government Act 1993* requires councils to prepare management plans which include objectives and performance targets/indicators against which actual performance is measured and reported. However, the New South Wales Department of Local Government noted that 'the essential autonomy of each council would suggest that the combination of indicators selected by each council in New South Wales would be unique'

The use of performance indicators in New South Wales councils was encouraged through the release of a *Reference Manual for the Development of Performance Indicators* (Econsult 1990). The New South Wales Department of Local Government also began publishing comparative information on Council costs, revenues and other financial information in 1991. The department requires all councils to report and publish annually against 26 performance indicators. To encourage meaningful comparisons, councils are grouped according to the Australian Classification of Local Government (ACLG Steering Committee 1994). Indicators are published for financial and corporate operations and a range of core service areas. However, the objectives of each activity against which performance is measured are not noted.

In New South Wales the local government regulations require that councils' financial reports comply with the Local Government Code of Accounting Practice and Financial Reporting (NSW Department of Local Government 1996). The following ratios are mandated:

- Current Ratio;
- Unrestricted Current Ratio;

- Debt Service Ratio;
- Rates and Annual Charges Coverage Ratio; and
- Rates and Annual Charges Outstanding percentage.

A number of councils in New South Wales are involved in benchmarking with other New South Wales councils, for example:

- Wyong, Liverpool, Sutherland, Gosford and Newcastle councils have benchmarked activities in a range of areas including mobile plant workshops, civil engineering design, civil infrastructure maintenance and building maintenance;
- Parramatta Council has developed key indicators for customer satisfaction, quality and efficiency, and is benchmarking against other childcare providers;
- North Sydney Council has developed performance indicators for public library services; and
- SHOROC (Warringah, Pittwater, Manly and Mosman) and four councils from the WSROC (Baulkham Hills, Blacktown, Fairfield and Liverpool) have benchmarked local building and development approval processes. New South Wales councils are also benchmarking with councils in other states and territories.

### ***Victoria***

In 1991, the Municipal Association of Victoria published comparative financial data on councils (Pensabene 1991) and subsequently developed core performance indicators for local government (Municipal Association of Victoria 1993). The indicators were intended as a source document from which councils could select indicators relevant to their internal management purposes. They included corporate indicators — to measure overall council performance — and functional (workload, efficiency, effectiveness and service delivery) indicators to measure the performance of individual council services or functions. From 1989 to 1996, the Association conducted an annual Local Government Finance and Efficiency Survey of Victorian Councils to give councils access to a finance database. The survey collected information on revenue, expenditure, debt, staffing, rates, facilities and functions. The data collected in the survey can be manipulated by councils using the software package, Statistical Performance Indicators for Council Evaluation, which contains 82 comparative performance indicators covering the main council activities.

More recently, performance measurement has become a key part of the government's Best Value program. The objectives of this program are:

- Local Accountability;
- Whole-of-organisation response;
- Consultation on performance;
- Best value outcomes;
- Benefits, not costs; and
- Encouraging innovation.

One of the main elements of this program is best value reporting on a set of Victorian Local Government indicators, which is linked to a constituent satisfaction survey which has been conducted over the last three years. Draft sector-wide indicators developed under this program are grouped into the following issues:

- Affordability/Cost of Governance;
- Sustainability;
- Services;
- Infrastructure; and
- Governance.

The program aims to develop a performance measurement culture through community well-being indicators, Council strategic directions, Council service performance and service-wide indicators. The financial indicators from the sector wide indicators are shown in the matrix below.

### ***Western Australia***

The Western Australian Department of Local Government publishes comparative data on councils in ACLG groupings. Most data are contextual, relating to statistics on demographics, area, dwellings, schools, hospital and nursing home beds, production and building activity, and local government operations. The latter includes financial indicators and some performance measures for library and recreation services. In January 2001, the government released 'Performance Measurement Guidelines for Western Australian Local Government'.

For many years the annual reports of Western Australian councils were required to include five financial indicators:

- the current ratio;
- the debt ratio;
- the debt service ratio;
- the rate coverage ratio; and
- the outstanding rates ratio.

The new guidelines outline a number of additional indicators. The performance indicators are based on information drawn from existing local government statistical returns to the grants commission, plus other statistical returns to government bodies. The performance measures are grouped into the following areas:

- Finance, Corporate and Governance;
- Library Services;
- Parks and Recreation;
- Road Management;
- Waste Management;
- Building Control;
- Health Services;
- Education and Welfare Services; and
- Planning Services.

The financial indicators are shown in the matrix below.

### ***Tasmania***

The Tasmanian budget papers present ten comparative financial performance indicators (table E.6) for each council derived from Australian Bureau of Statistics data on local government in Tasmania. The Tasmanian *Local Government Act 1993* does not require councils to include performance indicators in their strategic or operational plan. However a KPI project involving a number of Councils has developed a performance measurement system.

In September 2001, the Tasmanian Government released 'Measuring Council Performance in Tasmania'<sup>14</sup>. Performance measures were outlined in relation to:

- Governance;
- Management and Finance;
- Regulatory;
- Infrastructure and Utilities; and
- Community Services and Development.

The financial measures are shown in the matrix below.

### ***South Australia***

In November 2001, The South Australian Local Government Association released its "Comparative Performance Measurement in Local Government" which outlines its proposals for performance monitoring in Local Government, in the following areas:

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<sup>14</sup> Tasmanian Department of Premier and Cabinet "Measuring Council Performance in Tasmania". <http://www.dpac.tas.gov.au/divisions/lgo/information/KPI%20Report%2099-00.pdf> Visited December 2001.

- Governance;
- Financial/Asset Management;
- Community Satisfaction; and
- Quality of Life.

This project developed corporate level measures, as distinct from service measures, as we are interested in the performance of the corporate "body", ie the governance and decision making entity. It is intended that Councils will be able to cascade service measures down from these over time.

The Association has no mandate to report on performance, so this will be voluntary and carefully managed to ensure they do not end up with a "league table". The 18 measures have been developed by Councils and pilot tested to ensure they are relevant and useful. The financial measures in this set are shown in the matrix below.

### ***Northern Territory***

The Northern Territory initiated a collection of financial data from councils in 1996 to assist councils to better understand their financial position, identify emerging and existing financial problems, and develop strategies to deal with these problems. The data collected confirmed the large variation in financial reporting practices between councils.

In 1998 the Government released guidelines on 'Benchmarking for Local Government in the Northern Territory', followed by 'Good, Better, Best' guidelines on best practice in 1999. The indicators reported on in the Northern Territory are shown in the matrix below.

### ***ACT***

Since the 1996-97 budget, all agencies in the Australian Capital Territory have been required to report on performance against performance indicators addressing quantity, quality/effectiveness, timeliness and cost. Performance information is published in the Australian Capital Territory budget papers. Output statements are required as part of the financial statements and are subject to audit. The performance indicators used are subject to refinement, and ACT City Services has concentrated on benchmarking as a means of identifying the best indicators. The Australian Capital Territory is a member of the Austroads Benchmarking Group and ACT City Services is a member of the Strategic Partners' Agreement, participating in an ongoing benchmarking project on urban and nature parks. The partners include city and municipal councils, mainly in south-east Australia and in New Zealand.

### ***United Kingdom***

In the United Kingdom, performance measurement has been used widely since the 1980s to improve the quality and responsiveness of the public service. Individual local councils, consumer bodies (such as the National Consumer Council) and the Audit Commission have developed indicators on the performance of local councils. The work of the Audit Commission is significant in that it has raised the level of public awareness of the importance of performance indicators for public accountability. The Audit Commission program was an initiative introduced under the Major Government's National Citizen's Charter.

For local authorities in England and Wales, the Audit Commission sets performance indicators. The Audit Commission widely consulted on the choice of indicators. It conducted a public survey of councils, consumer groups, government departments and other interested parties to identify the indicators which are relevant and of interest to the public. The independence of the Audit Commission from central government is cited as a particularly useful factor in its dealings with local governments. The Accounts Commission sets the indicators for local authorities in Scotland. Local councils are required to publish council performance indicators in local papers. The Audit Commission collates and publishes all council information to enable the comparisons of one local government authority with another.

A wide range of services are covered by 200 indicators. The Audit Commission uses more than one measure of the performance of a service. This is to discourage councils diverting money or other resources into one part of the service where its performance is measured under the Citizen's Charter. Some indicators on service quality have also been included to help in the assessment of unit cost comparisons. Contextual information (for example, population density; social deprivation; geographic

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differences; language and cultural differences; age of population; housing and historical differences; regional pay and cost differences; and daily or seasonal changes in population) is also published to help the community understand the differences between council performance. However, no measures of customer satisfaction, equity or access are included at this stage.

The Audit Commission considers that the publication of comparative data influences public opinion, creating pressure to improve management. The publishing of performance indicators appears to have encouraged councils to set performance targets in areas previously unmeasured. After its third year of publishing information, the Audit Commission suggested that:

- it has the greatest impact on the worst performers;
- its impact on the bulk of councils — that is, those clustered around the average — is slower and less marked;
- there are big variations between the performance of similar councils for some services; and
- in a few services for some groups of councils, there has been no significant improvement in performance while other similar councils have advanced (Audit Commission 1997).'

### ***Australian Government***

The 2001 APS performance management framework notes that 'Some agencies have adopted a broader performance management approach using 'balanced scorecard' concepts. Typically, this includes the measurement of additional indicators (eg. people, clients, innovation) beyond the outcomes/outputs and financial indicators traditionally used. DEWRSB uses balanced scorecard performance reporting arrangements through an Executive Information System (DOORS) that reports on performance against:

- Business plan key performance indicators (KPIs);
- Financial resources (departmental and administered);
- People management KPIs (using HRM Inform); and
- Client satisfaction indicators.

In February 1993 the then Management Advisory Board and Management Improvement Advisory Committee, issued a paper 'Performance Information and the Management Cycle' which boldly asserted that "performance information is being used in both program management and in central decision-making, including in the budget and context; and the quality of performance reporting is improving". It did however identify a number of areas for "further improvement" including the need for "outcome oriented objectives" and "refocusing targets to cover outcomes and outputs as well as throughput and activity". The subsequent MAB/MIAC report "Building a Better Public Service" claimed that "there are still improvements to be made in the quality of performance information...[it] has to be clearly relevant to program objectives... and should include both quantitative and qualitative". There are systemic barriers to delivering these improvements, including:

- No real link between appropriations and objectives. The Commonwealth had a system of so-called program budgeting, but in reality had program reporting only. Budgeting was on a different basis. In the legislative process for appropriations, the mix of items was largely determined by history; in the decision making process by Ministers, an eclectic mixture of activities, programs or agencies was used at various times.
- No clear read between the budgeted performance promises and the actual performance reported in Annual Reports.
- Responsibility for program definition and reporting devolved almost entirely to departments and agencies, with little legislative or executive oversight.

The new budgeting framework is in part designed to overcome some of these past barriers to the production of useful performance information measures of effectiveness".

### ***Queensland***

The Queensland Department of Local Government and Planning (DLGP) conducts an annual collection of local government financial information used to prepare a statistical publication, the *Local Government Finance Review*. In 1996, the department initiated a project to collect, collate and publish financial and non-financial performance information on councils. The department views this project as

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being consistent with the Local Government Ministers' Conference commitment by the states and territories to publish comparative data on the performance of local government.

The Local Government Association of Queensland is concerned with providing outcome focused indicators which measure outcomes from a client perspective as a means of integrating perceptions of service quality and price (sub. 7). Accordingly, the Association has been involved in work on customer satisfaction with local government services. In 1995, the Association commissioned research of overall community attitudes to local government. This work was extended in 1997 to develop concepts and tools to allow local government, at both a collective and individual level, to monitor and track performance in terms of their customers' priorities. The study developed and carried out a survey of community attitudes towards the importance of and performance of local government services and functions. The results provide an initial collective benchmark against which other councils, using the survey, can assess their own performance (Market Facts and Morton Consulting Services 1997).

The Queensland Department of Local Government and Planning recommend the following indicators for monitoring Local Governments in the Tropical Accounts:

Ratio	Definition	Formula
Revenue Ratio	Council's dependence on rates income.	Net Rates and Utility Charges Revenue / Total Revenue
Working Capital Ratio	Ability to meet current commitments.	Current Assets / Current Liabilities
Debt Servicing Ratio	Percentage of revenue to service Debt	Debt Servicing and Redemption Cost / Total Revenue
Net Debt Payback	Anticipated Number of Years to pay debt in full	
Rate Arrears Ratio	The effectiveness of rates and charges collection	Rates Outstanding at Year-End / Rates and Charges Levied during financial year.
Capital Expenditure Ratio	Ratio of Capital Expenditure to Depreciation	Capital Expenditure / Depreciation Expense
Unfunded depreciation ratio	Percentage of unfunded depreciation to total depreciation	Unfunded Depreciation / Total Depreciation
Change in community equity ratio	Percentage change in net assets of the Council	Change in Equity / Equity at beginning of year

In addition to the recommended indicators, our review of current reporting practices identified the following ratios currently being used by Queensland Local Council's.

Change in Accumulated Surplus	Change in Accumulated Surplus / Net Rates and Utility Charges Revenue
Debt Exposure	Total Liabilities / Total Assets
Interest Cover	Operating Capability & Debt Servicing Cost / Interest
Gross Debt per Capita	Total Debt / Population or Number of Assessments
Debt Commitment Ratio	Debt Servicing and Redemption Cost / Net Rates and Utility Charges Revenue

### *Matrix of Local Government Indicators used around Australia*

#### *Financial Risk*

Performance Indicator	Qld	NSW	Vic	Tas	SA	WA	NT
Debt Servicing	X	X		X	X	X	X
Working Capital	X			X		X	
Current Ratio		X				X	X
Gearing			X				
Debt to Rates revenue	Being considered by DLGP						

**BEST PRACTICE SIMPLIFIED INTERNAL AND EXTERNAL REPORTING**

<b>Performance Indicator</b>	<b>Qld</b>	<b>NSW</b>	<b>Vic</b>	<b>Tas</b>	<b>SA</b>	<b>WA</b>	<b>NT</b>
Interest Cover	Some Councils						
Borrowing ratio	X						
Payback period	Tropical Accounts						

***Operational Indicators***

<b>Performance Indicators</b>	<b>Qld</b>	<b>NSW</b>	<b>Vic</b>	<b>Tas</b>	<b>SA</b>	<b>WA</b>	<b>NT</b>
Revenue source ratios	X	X	X	X			
Revenue growth				X			
Revenue Autonomy	X					X	X
Rate Coverage				X		X	
Rate Arrears	X	X		X		X	
Investment yield						X	
Operating expense growth				X			
Budget achievement –exp/rev/cap				X			
Outsourcing %				X			X
Operating surplus ratio			X		X		
Commercial business surplus							X
Renewals capital to depreciation			X				
Capital Expenditure ratio	X		X* (per assessment)	X	X		X
Capital expenditure to depreciation					X		
Unfunded depreciation	X						
Change in Community equity	X					X	

\* Per Assessment

***Community Indicators***

<b>Performance Indicators</b>	<b>Qld</b>	<b>NSW</b>	<b>Vic</b>	<b>Tas</b>	<b>SA</b>	<b>WA</b>	<b>NT</b>
Av rates per sector						X	
AV Rates per assessment			X	X			X
Operating Revenue per capita		X					
Operating Expenses per capita/assessment		X	X			X	
Members expense ratios						X	

***Suggested Indicators***

Ideally there should be consistency between Tropical model accounts and DLGP published requirements, as well as consistency between Local Government's in other States.

### ***Financial Risk Indicators***

From the above matrix of financial risk indicators we have selected long term solvency indicators and one short term liquidity indicator which have widespread usage across Australia as follows:

- Debt Servicing Ratio
- Debt/Rates ratio (Total debt to total rates)
- Working Capital

The addition of the debt/rates ratio is to overcome weaknesses in the debt servicing ratio – since the latter ratio can give the erroneous impression of debt problems if a Council accelerates its debt repayments. However it is retained because of its widespread usage and understandability in the community.

### ***Operational Indicators***

It should be noted that many of the above indicators are very similar or overlap, so the differences may not be as significant as it appears. We have selected the following representative range of indicators which cover revenue, expenditure and capital:

- Revenue source ratios
- Rate Arrears
- Capital expenditure ratio (to Depreciation)

### ***Community Indicators***

The following indicators are suggested as simple overall value for money measures. These also need to be supplemented with service level measures in relation to specific council services.

- Av Rates per assessment
- Av operating expenditure per assessment

## **4.4. Case Studies**

### ***Berlin***

Following the re-unification of Germany and the re-establishment of Berlin as the National Capital, the city embarked on a massive capital works program. During this period the Federal Government cut back on Grants and subsidies to alleviate its own financial constraints associated with re-unification, however the City continued spending heavily on capital works, using debt to replace the reduced grants. This was followed by a financial scandal due to the collapse of a banking business owned by the Council, plunging the city into massive debt to bail out the bank. The City's debt is now double that of its annual budget for operating and capital works. The crisis led to the downfall of the Council which was terminated and new elections called. The new Council is implementing a severe austerity program on services, while attempting to continue a large capital works program.

### ***New York***

The problems of New York City, when it became bankrupt in the 1970's, have been well documented. The bankruptcy was largely caused by borrowing for operating costs and running down assets, which ultimately resulted in a bailout, by the State Government. The Government required the introduction of accrual accounting, which then spread to other public sector organisations throughout the world. However, a review by the New York State government around 20 years later showed that the Council was still using unsustainable statement of financial position items such as assets sales for funding of operational programs.

### ***Burke***

Burke Shire Council faced severe liquidity problems during the 1980s. Local Government Department assessed the Council's financial situation and recommended to the Council that either rates be increased by 25% or expenditure reduced by a similar amount. Council refused to take corrective action and was dismissed and an administrator appointed. The administrator increased rates by approximately 25% and after a period of time fresh elections were called.

### ***Cloncurry***

More recently Cloncurry Shire faced similar problems to those which confronted Burke Shire, however the Council agreed to take corrective action over a period of time following representations by the Department and Auditor-General. Although the Queensland Government guarantees loans raised by local governments, the government requires councils to trade their way out of any problems so that it is not called upon financially. Therefore the government has shown it is prepared to use its reserve powers and appoint an administrator if the Council does not take corrective action to address any insolvency problems.

### ***Laidley***

In mid to late 1990s, Laidley Shire Council faced severe liquidity problems. The Council had become financially dependent on high levels developer contributions associated with rural residential development. Suddenly the real estate market for this type of development collapsed, but the Council continued with a high level of capital works spending in order to keep its construction staff employed. As a short-term solution, additional loan borrowings were raised, as well as running down cash reserves, to replace lost developer contributions funding. The problem was exacerbated when rates arrears on rural residential properties dramatically increased, resulting in a severe liquidity problem. Since then the Council has undertaken an austerity program and staffing levels have been almost halved. According to the CEO it takes two to three times as long to trade out of a problem than it took to create the problem.

During the time Council has been addressing the problem of the percentage of total revenue from rates has increased from 43 percent to over 70 percent. The CEO and council monitors rates arrears, debt indicators, other liabilities such as leave balances, and working capital. The Council has a target in relation to debt levels that the interest and redemption should not be greater than 30 percent of rate receipts (as opposed to accrued rate revenue due to the high level of rates arrears).

The CEO claims that the experience highlights the important of long term modelling and financial planning, and the danger of relying on variable income sources for a fixed cost structure.

### ***Conclusions***

It is clear that simply relying on budget variance reporting during the financial year is insufficient to ensure that the Council is efficiently managed and has adequate liquidity to remain solvent. Therefore there is a need to monitor liquidity throughout year and the Council also needs to review the sustainability its debt levels and financial structure at least annually. Ideally the annual review of the financial structure and debt levels should be conducted during the budget process. It may be necessary to review this both at the beginning and the end of the budget process, since the cumulative effect on budget balancing decisions could have caused deterioration in the original framework and parameters.

During the financial year regular reviews of liquidity and related issues such as rates arrears and outstanding debtors need to occur. Ideally this should occur within the governance structure established by the Council for the management of its finances. Therefore the committee charged with responsibility for financial matters (for example the finance committee or audit committee) should regularly review and monitor Council liquidity indicators. This is dealt with further in Part 6.5 Best Practice Management Accounting Framework.

## 5. EXTERNAL REPORTING

Considering the vast array of users of GPFRs it is not surprising that these reports have been criticised for taking “insufficient consideration of the objectives that financial reports should aspire to achieve, the users for whom those reports should be prepared and their information needs”<sup>15</sup>. It is the purpose of this chapter to examine the needs of users and how best to meet them.

### 5.1. Key Points

- The purpose of External Reporting by councils is to communicate with the community the councils progress against plan for Community Objectives, Operating Capacity and Financial Risk.
- To be communicative General Purpose Financial Reports need to be simpler and more explanatory through the use of Management Discussion and Analysis and Key Performance Indicators. Key Performance Indicators are discussed in Chapter 5.
- Best practice reporting is reporting that focuses on the message to be delivered and reduces information overload (examples are attached).
- Management Discussion and Analysis could include:
- As stated the GPFR is a critical document for communicating with the community but our review of current reporting practices revealed that current distribution and consequently readership levels are low. It is proposed that Councils should be encouraged to use other communication methods to leverage the GPFR. This could include the use of the worldwide web and leaflets delivered with rates notices to report on performance.

### 5.2. External Reporting Content

#### *General Purpose Reporting*

‘Local councils are accountable, not only to those providing funds, but also to other members of the community (in respect of whom those funds are provided) for the management of resources under their control’<sup>16</sup>.

#### *General Purpose Financial Reports*

The general purpose financial reports (GPFR) including notes, supplementary schedules and explanatory material are the principal means of communicating financial information about a reporting entity to those users who are generally unable to command the preparation of reports tailored to their particular needs. The accounting concepts<sup>17</sup> identify these users in four broad groups: resource providers; recipients of goods and services; parties performing a review or oversight function; and, managements and governing bodies.

According to Financial Reporting by Local Governments the users of Local Council GPFRs include<sup>18</sup>:

- *Management* for planning and control purposes;
- *Statistical Agencies* as input for national or industry statistics;
- *Regulatory Agencies* as evidence that relevant legislation or regulation has been complied with or as input for determining that sound financial policies and practices have been employed by management;

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<sup>15</sup> Financial Reporting by Local Governments, page 1

<sup>16</sup> Financial Reporting by Local Governments, page 1

<sup>17</sup> Statement of Accounting Concepts 2

<sup>18</sup> Financial Reporting by Local Governments, page 11

- *Votes and other ratepayers* (and their representative groups) as input for voting or other decisions;
- *Funding agencies* and other resource providers as input for decisions on the magnitude of resources to be allocated to the council in the future; and
- *Councillors* as input for decision-making about the financial resources for which they are responsible. Councillors will also require financial reports to be prepared to discharge their accountability obligations to constituents.

### ***Other General Reports***

As stated the GPFR is a critical document for communicating with the community but our review of current reporting practices revealed that current distribution and consequently readership levels are low. It is proposed that Councils should be encouraged to use other communication methods to leverage the GPFR. This could include the use of the worldwide web and leaflets delivered with rates notices to report on performance.

## ***Specific Purpose Reporting (Regulators Requirements)***

### ***Queensland Competition Authority***

The Queensland Competition Authority has a strong interest in the quality of reporting both for internal management purposes as well as for external reports.

There are some specific needs for information related to the responsibilities of the Queensland Competition Authority in terms of assessments related to the incentive funding. The Queensland Competition Authority however see a need for quality information to be available in terms of competition reforms generally including competitive neutrality requirements, Third Party Access issues and monopoly prices oversight.

At the present moment the Queensland Competition Authority (QCA) require all statutory reports including annual reports incorporating the audited financial statements, corporate/strategic plans, operating plans and annual performance plans for commercial activities and the Budget including program budgets.

The QCA has a need to identify a range of information related to community service obligations including full cost pricing, asset valuation including optimisation and contributed asset information. The QCA would also like to have clearer information on the linkages between Full Cost Pricing Budgets and the General Budget of the local government.

The QCA would like to see improved management discussion and analysis including the status of infrastructure assets and commercial business viability. Furthermore, it is keen to see information related to asset management and the question of funding of depreciation.

### ***Australian Bureau of Statistics***

The Australian Bureau of Statistics (ABS) has advised that following a review of Local Government data collections in 2000/2001 the data needs of the ABS are being considered. At the moment there are 39 different ABS collections affecting Local Government with some of these being quarterly. There is a desire to reduce the load on Councils in terms of the provision of information.

The Queensland process for the collection of Local Government Finance Statistics is not typical of the processes in other States/Territories. Currently, the ABS gather the financial information from the Annual Reports of 125 Councils in Queensland to be broken down into Government Finance Statistics codes for National Accounts purposes. ABS have developed a dissection schedule which is forwarded to Councils to input further information.

ABS and the Local Government Grants Commission in Queensland are seeking to obtain a common data set to meet Government Finance Statistics purposes.

### ***Other Agencies and Departments***

The Grants Commission would like to see the use of common systems to assist in the process of collection of information for their purposes.

The Queensland Audit Office has a direct interest in the quality of financial reporting given the audit role to be undertaken. The QAO has as its principal client the Queensland Parliament and their role is driven from the role prescribed in legislation. The QAO is however happy to undertake audits of commercial activities by arrangement. In terms of the proposed changes in reporting the QAO will be interested to see the audit requirements for management discussion and analysis information.

The Queensland Department of Local Government and Planning has initiated a process to make changes to the Local Government Finance Standard to simplify the financial reporting requirements.

## **5.3. Reporting Techniques**

### ***Management Discussion and Analysis***

“Management discussion and analysis (MDA) is narrative disclosure provided by the management or governing body of an entity which expands and explains the information provided in a[n entity’s] financial statements.

MDA reports are designed to supplement and enhance general-purpose financial reports. The narrative provided should help users better understand the current position of the entity and its likely future performance”<sup>19</sup>

Currently, there is no requirement for a council to include MDA in their annual reporting. This report recommends the inclusion of MDA in all forms of annual reporting, GPFRs and Council leaflets. In determining what is best practice for councils in producing MDA the following discussion draws from the Corporations Law, the Australian Stock Exchange Listing Rules and from the Canadian Institute of Chartered Accountants. Our research did not identify any states or territories which have legislated to require management discussion and analysis.

### ***Australian Corporations***

#### **Concise Financial Reports**

The Corporations Law (Section 314) allows a company the discretion of sending members either a full financial report or a concise report. The concise financial report must be drawn up in accordance with the accounting standard on “Concise Financial Reports” (AASB 1039). The standards definition of a Concise Financial Report includes MDA and outlines what should be included in the discussion (Section 5.3).

The information reported in the financial statements will be enhanced by a discussion and analysis of the principal factors affecting the financial performance, financial position and financing and investing activities of the entity. The extent of the discussion and analysis provided will vary from entity to entity, and from year to year, as is necessary in the circumstances to help compensate for the brevity of the concise financial report compared with the financial report.

In most situations, the content of the discussion and analysis would cover at least the following areas:

- (a) in relation to the profit and loss statement:
  - (i) trends in revenues arising from operating activities

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<sup>19</sup> Ernst & Young Corporate Governance Series. May 2000. “Management Discussion and Analysis Reports”. [http://www.ey.com/global/vault.nsf/Australia/Management\\_Discussion\\_Analysis/\\$file/MD&AMay00.pdf](http://www.ey.com/global/vault.nsf/Australia/Management_Discussion_Analysis/$file/MD&AMay00.pdf) Visited, December 2001

## BEST PRACTICE SIMPLIFIED INTERNAL AND EXTERNAL REPORTING

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- (ii) the effects of significant economic or other events on the operations of the entity
  - (iii) the main influences on costs of operations
  - (iv) measures of financial performance such as return on sales, return on assets and return on equity
- (b) in relation to the balance sheet:
- (i) changes in the composition of assets
  - (ii) the relationship between debt and equity
  - (iii) significant movements in balance sheet items
- (c) in relation to the statement of cash flows:
- (i) changes in cash flows from operations
  - (ii) financing of capital expenditure programs
  - (iii) servicing and repayment of borrowings

### Statement of Operations and Activities

The Corporations Law (Section 299) further requires general information about operations and activities. This is to:

- (a) contain a review of operations during the year of the entity reported on and the results of those operations; and
- (b) give details of any significant changes in the entity's state of affairs during the year; and
- (c) state the entity's principal activities during the year and any significant changes in the nature of those activities during the year; and
- (d) give details of any matter or circumstance that has arisen since the end of the year that has significantly affected, or may significantly affect:
  - (i) the entity's operations in future financial years; or
  - (ii) the results of those operations in future financial years; or
  - (iii) the entity's state of affairs in future financial years; and
- (e) refer to likely developments in the entity's operations in future financial years and the expected results of those operations; and
- (f) if the entity's operations are subject to any particular and significant environmental regulation under a law of the Commonwealth or of a State or Territory—details of the entity's performance in relation to environmental regulation.

### ***Australian Listed Corporations***

The Australian Stock Exchange (ASX) has a requirement<sup>20</sup>, based on the Corporations Law's Statement of Operations and Activities (Section 299), for listed Companies to include a review of operations and activities for the reporting period in the annual report. The ASX does not prescribe a format for the review of operations and activities but supports the Group of 100 Inc.<sup>21</sup> publication "Guide to review of operations and financial condition". The publication is attached to the listing rule.

The Guidance to review of operations and financial condition" requires that

'a company should explain its past performance and provide information which will increase understanding of its future directions. This can be achieved through a Review which provides a critical and objective analysis and explanation of a company's past and likely future performance and financial condition. This analysis should concentrate on the opportunities and risks associated with the past operations of the company and the opportunities and risks likely to impact on the future activities of the company.'

This review focuses on matters of significance to the company as a whole. Therefore, the review should:

- include matters that are likely to be significant to investors;
- follow up material comments or disclosures made in previous reports where actual outcomes warrant such updating;

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<sup>20</sup> Listing Rule 4.10.17 Review of Operations and Activities.

<sup>21</sup> The Group of 100 is an association of senior finance executives from Australia's business enterprises.

## BEST PRACTICE SIMPLIFIED INTERNAL AND EXTERNAL REPORTING

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- make clear how any ratios or other numerical information relate to the financial statements; and
- include a discussion of the initiatives, events and transactions which can, at the time of the Review, be expected to affect future reporting periods rather than limiting the discussion to the next reporting period.

Essential features of the Review:

- The Review should be comprehensive and easy for readers of the financial reports to understand.
- The focus of the review is on explanations and analyses. Replication of numerical information already included in the financial statements may enhance the understandability of the Review but it is not a substitute for an objective and balanced discussion and analysis of that information.

To meet the above requirements, the Review should:

- be written in a clear style and as succinctly as possible;
- be in narrative form, supported by figures and graphics where these assist understanding of the matters discussed;
- avoid the use of technical language as far as possible;
- be balanced and objective, dealing even-handedly with both positive and negative aspects of operations and financial condition;
- contain analytical description, rather than replicating information in the financial statements; and
- discuss individual aspects and segments of the organisation in the context of a discussion of the organisation as a whole.

Furthermore the “Guide to review of operations and financial condition” outlines the following areas as potential areas for discussion.

- **Objectives**, the objectives of the company and how they are achieved;
- **Performance indicators**, a discussion and analysis of key performance indicators used by management in their assessment of the company and its performance;
- **Dynamics of the business**, the main factors and influences that may have a major effect on results whether or not there were significant in the period under review;
- **Operating Results for the period**, the Review should discuss the main activities of the company, including significant features of operating performance for the period covered by the financial report;
- **Review of financial condition**, including the capital structure and treasury policy, cash from operations and other sources, liquidity and funding; and
- **Corporate governance**, a discussion of the company’s corporate governance policies and practices.

### **Canada<sup>22</sup>**

According to the Canadian Institute of Chartered Accountants MDA should enable readers to view past results and future prospects “through the eyes of management”. MDA reports should also:

- Complement as well as supplement financial statements;
- Have a forward-looking orientation;
- Focus on long-term value creation;
- Integrate long- and short-term perspectives;
- Present information that is material to decision-making needs of users; and
- Embody the qualities, comparability, consistency, relevance and understandability.

In preparing the MDA report there are seven disclosure principles that should be taken into account.

#### **PRINCIPLE 1: THROUGH THE EYES OF MANAGEMENT**

A company should disclose information in its MDA report that enables readers to view it through the eyes of management.

#### **PRINCIPLE 2: RELATIONSHIP TO FINANCIAL STATEMENTS**

MDA reports should complement and as well as supplement financial statements.

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<sup>22</sup> Canadian Performance Reporting Initiative Board. 2001. Review Draft “Management’s Discussion and Analysis: Guidance on Preparation and Disclosure”. [http://www.cica.ca/cica/cicawebsite.nsf/public/E\\_MD&A/\\$file/MD&A1English.pdf](http://www.cica.ca/cica/cicawebsite.nsf/public/E_MD&A/$file/MD&A1English.pdf) Visited, December 2001

**PRINCIPLE 3: FORWARD LOOKING**

A forward-looking MDA report explains past events, decisions, circumstances and performance in the context of whether they are reasonably likely to have a material impact on future prospects. It also describes not only anticipated future events, decisions, circumstances, opportunities and risks that management considers reasonably likely to materially impact future prospects, but also matters such as management's vision, strategy and targets.

**PRINCIPLE 4: FOCUS ON LONG-TERM VALUE CREATION**

In determining what to disclose in MDA reports, the focus should be on aspects of performance relevant to long-term value creation.

**PRINCIPLE 5: TIME PERSPECTIVE**

MDA reporting requires an integration of long- and short-term perspectives. In order to focus on the achievement of long-term value creation, management discussion of performance against one-year targets should be within the context of achieving longer-term strategic results.

**PRINCIPLE 6: MATERIALITY**

Information presented in the MDA report should be material to the decision making needs of the users. It is management's responsibility to identify, address, and communicate quantitative information necessary for users to understand and evaluate the company's nature, dynamics and prospects. MDA reports should be materially accurate at the time of their release.

**PRINCIPLE 7: USEFULNESS**

To be useful, information in MDA reports should embody the qualities of reliability, comparability, consistency over reporting periods, relevance and understandability. See the discussion on reporting above.

***United Kingdom***

The following was copied from the Ernst and Young Report "Management Discussion and Analysis"<sup>23</sup>. In considering the responsibility of boards with respect to financial reports the Cadbury Committee recommended that boards should pay particular attention to their duty to present "a balanced and understandable assessment of their company's position. Balance requires that setbacks should be dealt with as well as successes, while the need for the report to be readily understood emphasises that words are as important as figures."

A forward-looking Operating and Financial Review would serve this purpose. OFR is voluntary best practice. The essential features of an OFR are as follows:

- it should be written in a clear style and as succinctly as possible, to be readily understandable by the general reader of annual reports, and should include only matters that are likely to be significant to investors;
- it should be balanced and objective, dealing even-handedly with both good and bad aspects;
- it should refer to comments made in previous statements where these have not been borne out by events;
- it should contain analytical discussion rather than merely numerical analysis;
- it should follow a "top-down" structure, discussing individual aspects of the business in the context of a discussion of the business as a whole;
- it should explain the reason for, and effect of, any changes in accounting policies;
- it should make it clear how many ratios or other numerical information given relate to the financial statements; and
- it should include discussion of:
  - trends and factors underlying business that have affected the results but are not expected to continue in the future; and
  - are expected to impact on the business in the future.

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<sup>23</sup> Ernst & Young Corporate Governance Series. May 2000. "Management Discussion and Analysis Reports". [http://www.ey.com/global/vault.nsf/Australia/Management\\_Discussion\\_Analysis/\\$file/MD&AMay00.pdf](http://www.ey.com/global/vault.nsf/Australia/Management_Discussion_Analysis/$file/MD&AMay00.pdf) Visited, December 2001

Prospective Financial Information<sup>24</sup>

From the above MDA should be forward looking. The Institute of Chartered Accountants in England and Wales released a draft paper in October 2000 on prospective financial information (PFI). It was intended that the paper would be of use to preparers of the UK's Operating and Financial Review.

The overriding drivers of quality in forward-looking information include: clarity of strategy; analysis of the tasks that affect the strategy's effectiveness; quality of modelling and information processes; and board attitude to communication.

Required with PFI:

- inclusion of a dated statement acknowledging their responsibility for the PFI;
- explain the nature of the information presented and the inherent limitations that arise from the fact that it relates to the future;
- avoid selecting captions or time periods for presentation that are misleading; and
- accept that subsequent historical information will need to be prepared to allow a comparison and reconciliation of actual performance to PFI.

Preparers will need to have regard to:

- the nature of activities involved;
- the discretion they have for taking operations decisions that make achievement more likely;
- the time horizon;
- the quality of information systems;
- consistency with management plans;
- consistency with external information; and
- the expertise and experience of the people involved in its preparation.

The three main questions to determine whether any PFI represents a reliable forecast:

1. Does the PFI represent an outcome that the directors consider highly likely to be achieved?
2. Do the directors have a reasonably objective basis for believing that the PFI is highly likely to be achieved?
3. Do any disclosures of assumptions and related uncertainties cast doubt on whether the numbers in the PFI are highly likely to be achieved?

### ***MDA Conclusion***

General

MDA is about communication of results and how to move forward. To achieve this MDA requires the following attributes.

- ***Discussion and Analysis***. MDA is a narrative interpretation of the Council through the eyes of management. Requires more than a restatement of what is already presented in the financial statements, MDA is intended to expand and explain the statements. MDA requires an analytic discussion rather than a numerical analysis.
  - Look at the **Operating Statement** and review of the main activities that lead to the result for the period.
  - Look at the **Statement of financial position** and Statement of Cashflows. Review the capital structure, cash from operations and other sources, liquidity and funding.
  - A discussion of trends and factors underlying the result. Look at the adverse change in the reliance on rates or the times-interest-earned ratio. Is this deterioration or improvement in conditions expected to continue into future reporting periods?
  - Explain what the Financial KPIs mean and how they relate to the financial information. Also put them into context for example, what would a good be, what was in the corporate plan, what are comparable councils achieving.
- ***Comprehensive and unbiased***. Balanced and objective, dealing even-handedly with both positive and negative aspects of the Council. Presenting information that is **material** to the users of report.

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<sup>24</sup> The Institute of Chartered Accountants in England and Wales. October 2000. "Prospective financial information: Challenging the assumptions (A discussion paper)". [http://www.tb3.icaew.co.uk/viewer/index.cfm?AUB=TB21\\_4762](http://www.tb3.icaew.co.uk/viewer/index.cfm?AUB=TB21_4762) Visited, December 2001.

- **Easy to understand.** MDA requires clear and succinct reporting without the use of technical language.
- **Forward looking orientation.** What does the result mean for the future? Forward-looking MDA explains past events, decisions, circumstances and performances in the context of whether they are reasonably likely to have a material impact on future prospects. How is a negative result going to be remedied?
- **Consistent.** Reporting should roll forward and be capable of being read as a set. Refer to comments made in previous statements.
- **Useful.** See Chapter 4.
- **Trends.**

#### Structure

- **Outline Objectives and how measured.** What were the Council's goals for the reporting period? How were those goals to be measured (KPIs)? Linking to a previously published corporate plan makes reporting more meaningful.
- **Results.** Should be divided into the three main areas: Community Objectives, Operational Capacity and Financial Risk and compared to the goals in the corporate plan. Variances (both positive and negative) should be explained particularly in context of what the result means for the organisation in the next reporting period.
- **Corporate Governance.**

### ***Audit of MDA***

Under the Corporations Law the auditor is required to test that the information in the concise financial report is consistent with the full financial report. The auditor is also required to examine, on a test basis, evidence supporting the management, discussion and analysis and other disclosures which were not directly derived from the full financial report. This is in addition to the audit report provided on the general-purpose financial report.

This report is not recommending that the option of concise financial reporting be provided for local government in Queensland. This report however is recommending the introduction of a management discussion and analysis section in Annual Reports whilst also providing audited general-purpose financial statements in accordance with the accounting standard for Financial Reporting by Local Governments (AAS27). Accordingly we do not believe that an audit report is required on the management discussion and analysis section of the annual report.

### ***Current Reporting Practices***

Reporting is about communication. In choosing the following best practice examples we focused on reporting methods which made the information presentable and understandable to the community. In many cases, Program and Financial Data, was presented for two financial years. This format is useful but requires that the reader evaluate the data for themselves. Our modern, time-deprived community requires aids to assist the reader to determine variances and evaluate the change.

It should be noted that this summary of current reporting was written without examples from every council and not every identified best practice example is listed. If a Best Practice example has been omitted it is possible that we did not have a copy of the report or we had previously selected another Best Practice Example.

#### ***Program Reporting***

Many Councils begin their program reporting by outlining the vision and then report on performance during the financial year. Without the use of performance indicators, it is difficult to ascertain how the program is actually progressing. Best Practice organisations take the extra step of measuring the required outcomes and reporting against targets. Examples include:

- BHP Billiton Ltd (A) which reports cumulatively against the program plan;
- Caboolture Shire Council (F) had developed KPIs for each program and reported actual performance against targeted performance;

- Brisbane City Council (C&D) who developed a suite of KPIs for each program and reported each against targeted performance;
- Gold Coast City Council (G) who tied results back to the performance plan and clearly explained how variances were being addressed; and
- Pine Rivers Shire Council (M) succinctly outlined each performance plan, the objectives, the strategy for achieving the objectives, how performance is to be measured and progress to date.

### ***Ratios***

Many Councils presented the recommended ratios, in the style of Ratio Name, Mathematical Formula, 2 years of results, as a page towards the back of the annual report. While the information is useful this style of reporting did not enable the reader to determine whether or not it was a good result for the reporting entity. Best Practice organisations present their ratios along with:

- an explanation of the ratio, its purpose and what would be a good result for the council;
- comparative information including: budget; benchmarks (comparable councils); and
- other related ratios. The groupings showed a more complete picture than if the ratio was presented by itself.

Best Practice examples include:

- Tweed Shire Council (B) for forecast financial ratios;
- Caboolture Shire Council (G) who based their whole financial commentary on ratios and included five year trends; and
- Mount Isa City Council (L) who presented a three year trend and an explanation of each ratio and the reasons why they were changing.
- Warwick Shire Council (N) who presented KPIs grouped by theme, for example financial flexibility and vulnerability.

### ***Graphing***

Many Councils chose to present two to three pie charts: revenue (where the funds came from), and operational expenditure (how the funds were used). The optional third graph covers capital expenditure. It can be quite difficult to determine useful information from Pie graphs by themselves; additional aids including labels and quantification of each slice are required. There were several best practice examples the example chosen is for Caboolture Shire Council (E). Furthermore, when selecting a pie graph the presenter should be aware that they have a limited capacity to present comparative data.

### ***Presenting Financial Statements***

Most councils presented their annual report in two main sections; Part A was the report Council activities and Part B was the General Purpose Financial Statements. Most Councils presented Part B as a statutory minimum and made very little effort to make the statements more accessible to the community. Best Practice councils explained the financial statements to the community and/or preceded the statements with a Management Discussion and Analysis. Best Practice examples include:

Mareeba Shire Council (K) for their explanation of the financial statements purpose.

Logan City Council who explained the purpose of the financial statements combined with a commentary of the actual result (I) and graphically presented the relationship between the financial statements (J).

It should be noted that even in the case of best practice Councils the Management Discussion and Analysis rarely contained prospective comments. Prospective comments were confined to Part A of the annual report in the Mayor's or Chief Executive's report.

### ***Attachments***

- A. BHP Billiton Ltd Concise Annual Report 2001. The table goes beyond presenting actual KPIs; cumulative KPIs (across financial years) are matched against an equivalent period in the performance plan.
- B. Tweed Shire Council Management Plan 2001. The table presents trended KPIs, actual with forecast for the two outer years.

- C. Brisbane City Council Annual Report 2001. The table presents trended KPIs grouped by reported performance areas.
- D. Brisbane City Council Annual Report 2001. 'How do we know we're on track'. Actual KPIs for each program area are presented against targeted performance.
- E. Caboolture Shire Council Annual Report 2000. 'The use of Pie Graphs'. Each slice is labelled and quantified.
- F. Caboolture Shire Council Annual Report 2000. 'How we performed'. For each program the KPI is presented against target.
- G. Caboolture Shire Council Annual Report 2000. 'Financial Commentary'. KPIs are presented with explanations and trended graphs.
- H. Gold Coast City Council Annual Report 2000. 'S.581 (1) of the Local Government Act (1993)'. KPIs for performance areas are presented against Target and Forecast.
- I. Logan City Council Annual Report 2000. 'Interpretation of Statements'. An explanation of each statement is presented along with a brief statement of actual performance.
- J. Logan City Council Annual Report 2000. 'Interlinking of Financial Statements'. This page walks the reader through a summary of the financial statements; explaining to the reader how they interact.
- K. Mareeba Shire Council Annual Report 2001. 'How to Read the Financial Statements'. This page explains to the reader the purpose of each statement.
- L. Mount Isa City Council Annual Report 2000. 'Statutory Information'. KPIs are shown in trend and explained.
- M. Pine Rivers Shire Council Annual Report 2001. '6 years: The Key Statistics at-a-glance'. Financial and Community KPIs are shown in trend.
- N. Pine Rivers Shire Council Annual Report 2001. 'Operational Summary'. Council's goals are presented in context of strategy, performance measures and how performing.
- O. Warwick Shire Council Annual Report 2000. 'End of Year Results'. Individual KPIs are grouped enabling KPIs to be read in greater context than if they were presented individually.

### ***Triple Bottom Line Reporting***

In recent times, there has been growing concern for global environmental and social issues such as pollution, resource depletion, corruption and child labour. This has been reflected by a general trend toward increased expectations of accountability including<sup>25</sup> transparency, responsiveness and compliance. The concept of transparency requires organisations to make information publicly available which will assist in the judgement of accountability, that is the extent to which responsibility is taken for the consequences of their action or inaction. Associated with these expectations, is a change in the information needs of these "... new and influential stakeholder[s]..."<sup>26</sup> – both consumers of company products and shareholders looking to invest in 'socially responsible' entities. Although information on performance is desired in financial terms, information in environmental and social terms is now being sought as well. Increasingly, therefore, entities feel obliged to demonstrate 'corporate social responsibility' by looking beyond mere economic measures to incorporate interaction with its physical and social environment. It is important that they not only *act* responsibly, but also be *perceived* as acting responsibly.<sup>27</sup>

As a result of the community and political interest in environmental and social issues, the notion of, and need for 'sustainable development' (SD) has been evolved and acknowledged. The 1987 report, *Our Common Future*, by the World Commission of Environment and Development defined SD as:

...development that meets the needs of the present world without compromising the ability of future generations to meet their own needs.<sup>28</sup>

Subsequently, the 1992 United Nations Conference of Environment and Development expressed the need for annual reporting on an organisation's environmental performance in order to attain transparency. In addition, the community's "right to know" was regarded an important factor in SD

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<sup>25</sup> The Body Shop Australia. 2000. "Social Audit Overview". <http://www.thebodyshop.com.au/tbnl/s1.0r.htm> Visited, January 2002.

<sup>26</sup> Brayshaw, Geoff. 1999. "Triple Bottom Line Reporting: The profession's challenge". *Charter 70* [7]:36-38

<sup>27</sup> Deegan, Craig. 1999b. "Implementing Triple Bottom Line Performance and Reporting Mechanisms". *Charter 70* [4]:40-42

<sup>28</sup> Deegan, Craig. 1999a. "Triple Bottom Line Reporting: A New Approach For The Sustainable Organisation". *Charter 70* [3]:38-40

policy development.<sup>29</sup> John Elkington first introduced the Triple Bottom Line (TBL) concept in 1997, later defining it as follows:

“Sustainable development involves the simultaneous pursuit of economic prosperity, environmental quality and social equity. Companies aiming for sustainability need to perform not against a single, financial bottom line but against the triple bottom line.”

Use of TBL Reporting is of fundamental importance to the *achievement* of SD. Evidently; the three interlinking TBL components are closely aligned with the key principles underlying SD. These are, namely – the financial bottom line, the environmental bottom line and the social bottom line.

The Global Reporting Initiative (GRI) was formed in 1997 by the Coalition for Environmentally Responsible Economies (CERES) and the United Nations Environment Program (UNEP). Its purpose was to “...develop a globally applicable guideline...”<sup>30</sup> for sustainability report preparation, the first such guideline combining financial, environmental and social performance being released in 2000. Consistent with SAC 3, reporting should take environmental and social aspects into account where present, if the provision of information is to qualify as “relevant” to the decision-making process. However, ‘best practice’ implementation of TBL Reporting must involve integrating financial environmental and social responsibility into **internal** decision-making and culture so as to make communication to **external** stakeholders more meaningful.

Requiring long-term vision, TBL Reporting is an attempt at producing a more exhaustive indication of performance. According to Lagan<sup>31</sup>, Australia is presently at the stage where *awareness* of TBL issues is being developed. Few organisations are admitting to interest where social and ethical auditing is concerned “...for fear of peer disdain.” She does maintain that independent audits of the three TBL components will become the norm in future years, thus enabling intra- and inter-company benchmarking. Brisbane City Council has shown some initiative, generating their first ever TBL Report in 1999/2000. Commentary explains that each bottom line is reported according to Council’s expenditure, the practical application of which is demonstrated using a case study and some non-financial performance data.

### ***Social Bottom Line***

To be sustainable, an organisation must *measure* its performance against stakeholder and societal expectations and then *report* on that performance. Irrespective of how efficiently financial resources and the environment are being employed, failing to meet community expectations could have “...major implications for the [entity’s] ongoing survival...” This assessment can be made by undertaking external social audits. Outcomes are then made publicly available for transparency purposes<sup>32</sup>. Relevant information and opinions may be gathered from questionnaires, focus groups or individual interviews and may address such issues as:

- Corporate (ethical standards, human rights);
- Employees (child labour, workforce diversity);
- Local and Global Community (community consultation, complaints); and
- Customers (advertising standards).<sup>33</sup>

Social reporting frameworks in Australia have not progressed as far as those in other countries or those on public *environmental* reporting in Australia. A major difficulty lies in the “...lack of metrics and consistent frameworks.” with social indicators being less developed than environmental ones.

### ***Environmental Bottom Line***

Environmental Reporting in Australia – Background, Current Status, Initiatives to Improve

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<sup>29</sup> Environs Australia. “Triple Bottom Line reporting”. [http://www.environs.org.au/business/tbl\\_reporting.html](http://www.environs.org.au/business/tbl_reporting.html) Visited, January 2002.

<sup>30</sup> Environs Australia. “Triple Bottom Line reporting”. [http://www.environs.org.au/business/tbl\\_reporting.html](http://www.environs.org.au/business/tbl_reporting.html) Visited, January 2002.

<sup>31</sup> Moodie, David. 1999. “The greening of the boards”. *Charter* 70 [10]:32-34

<sup>32</sup> Deegan, Craig. 1999a. “Triple Bottom Line Reporting: A New Approach For The Sustainable Organisation”. *Charter* 70 [3]:38-40

<sup>33</sup> Environs Australia. “Triple Bottom Line reporting”. [http://www.environs.org.au/business/tbl\\_reporting.html](http://www.environs.org.au/business/tbl_reporting.html) Visited, January 2002.

- Reporting within annual reports is predominantly *voluntary*, the only statutory requirement to date being s299(1)(f) of the Corporations Law. Public and large proprietary companies must report within the Director's Report:
  - ...if the entity's operations are subject to any particular and significant environmental legislation under a law of the Commonwealth or of a State or Territory – details of the entity's performance in relation to environmental regulation.
- AASB 1034 requires material contingencies to be disclosed in a note to the accounts – this applies to environmental liabilities.
- Voluntary public reporting need not be in annual report form – pamphlets and newsletters are considered appropriate communication vehicles.
- There have been recent improvements in quality of environmental performance disclosure.
- Numerous voluntary agreements and codes include a mandatory environmental reporting requirement, for example:
  - Mineral Council – Code for Environmental Management; and
  - Commonwealth government's Greenhouse Challenge and Cities for Climate Protection Programs.
- The Environmental Protection Agency (NSW) and the Department of State and Regional Development (NSW) produced a guidance document on environmental performance evaluation and reporting.
- Commonwealth government released *A Framework for Public Environmental Reporting: An Australian Approach* to aid increased quality and quantity of reporting and alignment with the GRI<sup>34</sup>.
- The Institute of Chartered Accountants in Australia established an Environmental Task Force in 1995, although it has now become the Triple Bottom Line Issues Group to reflect the trend toward incorporation of social issues.
- The Australian Environmental Report Scorecard (AERS) was adapted from UNEP's sustainability criteria after 1999, enabling benchmarking against an organisation's own unique environmental and stakeholder issues<sup>35</sup>

#### Environmental Reporting specifically in relation to Local Governments<sup>36</sup>

The majority of expenditure on the environment in Australia occurs at local government level. The Australian Bureau of Statistics (ABS) conducts an annual Environment and Natural Resources Survey requiring local governments to generate a Statement of Green Cash Flows using environmental classifications taken from the United Nations System of Integrated Economic and Environmental Accounts (SEEA). Use of these classifications in local governments' **own** accounting systems reduces the burden of preparing information for the ABS (since it is being kept in the "desired format") and also facilitates better environmental management decisions (given the ability to link financial and environmental data). Benchmarking will become possible as more local governments adopt the SEEA classifications. The next stage would appear to be a move to green operating statement and statement of financial position. The move from *green* cash accounting to *green* accrual accounting it is expected to mirror the general decision-making improvements experienced following the recent move from cash to accrual accounting.

Local governments are asked to identify their receipts and expenditure which involve the environment and classify them according to the SEEA. In so doing, performance as against community expectations about their environmental responsibility can be expressed. Many local governments produce a State of the Environment Reports (SoER) – "...an inventory of environmental features in a region and their current condition." which can then be matched to information in their Statements of Green Cash Flows. Again, this assists in environmental management. In NSW, local governments are obliged to prepare comprehensive SoER or establish environmental management systems aimed at "...improv[ing] eco efficiency and reduc[ing] environmental costs in key operational processes."<sup>37</sup>

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<sup>34</sup> Environs Australia. "Triple Bottom Line reporting". [http://www.environs.org.au/business/tbl\\_reporting.html](http://www.environs.org.au/business/tbl_reporting.html) Visited, January 2002.

<sup>35</sup> Sydney Water. 2000. "Annual Environment & Public Health Report 2000: Towards 'triple bottom line' reporting". [http://www.sydneywater.com.au/html/AER2000/case\\_reporting.htm](http://www.sydneywater.com.au/html/AER2000/case_reporting.htm) Visited, January 2002.

<sup>36</sup> Miley, Frances and Read, Andrew. 2000. "Environmental reporting: Thinking local". *Australian CPA* 70 [3]:40-42

<sup>37</sup> Miley, Frances and Read, Andrew. 2000. "Environmental reporting: Thinking local". *Australian CPA* 70 [3]:40-42

Case Study – Eurobodalla Shire Council (ESC)<sup>38</sup>

Currently, a draft Code of Accounting Practice is being prepared through the ABS and CPA proposing a Special Schedule be attached to AAS27 listing the:

- operating expenses and revenues against the SEEA classifications;
- costs to maintain those environmental assets;
- the capitalised expenses to improve the environmental assets; and
- ultimately the loss of serviceability (defined as depreciation) of those environmental assets.

The environment will thus be managed in a way similar to the local government’s infrastructure assets. ESC has embraced this draft method of accounting by:

- recoding their Chart of Accounts for the SEEA classifications;
- introducing the philosophy of environmental accounting as a form of “asset management”;
- reporting environmental risks to council, quantifying them as financial costs or opportunities lost; and
- assessing projects by comparing traditional engineering approaches with environmental approaches.

***Conceptual Issues with Triple Bottom Line Reporting***

It is arguable as to whether financial, environmental and social performance should be reported **separately** within an annual report or merged into a “single metric”. It is expected that future debate will also centre on the viability of converting environmental and human impacts into monetary terms<sup>39</sup>. TBL Reporting has a number of benefits, including:<sup>40</sup>

- an increased capacity to respond quickly to initiatives (eg emissions trading);
- creation of market opportunities through new thinking and technology; protection of brand;
- indirect improvements in internal environment performance through the identification of inefficiencies and waste (revealed cost-savings and reduced liabilities);
- increased investor confidence;
- improved relationships with stakeholders (sharing corporate values creates trust and loyalty and stimulates positive stakeholder satisfaction<sup>41</sup>);
- maintenance of a “social license to operate” and access to resources;
- greater control of disclosures; and
- increased staff commitment.

***Implementation of Triple Bottom Line Reporting***

Landcare Research<sup>42</sup> states that effectively, an organisation:

- Establishes its own values in relation to social, environmental, and economic issues.
- Determines the performance issues of importance to its stakeholders (staff, customers, shareholders, communities, suppliers, insurers, etc).
- Integrates the above to establish a set of key performance areas, indicators and targets.
- Measures and openly reports performance, with external verification to increase trust.

***Current Reporting Requirements***

The *Local Government Finance Standard* 1994 requires each local to produce financial statements in compliance with AAS 27 Financial Reporting by Local Governments. AAS 27 requires Consolidated Financial Statements to be issued under AAS 24 Consolidated Financial Reports. This reporting is to include an Operating Statement, a statement of financial position, a statement of changes in equity and a statement of cash flows.

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<sup>38</sup> Miley, Frances and Read, Andrew. 2000. “Environmental reporting: Thinking local”. *Australian CPA* 70 [3]:40-42

<sup>39</sup> Deegan, Craig. 1999b. “Implementing Triple Bottom Line Performance and Reporting Mechanisms”. *Charter* 70 [4]:40-42

<sup>40</sup> Art 1 and 3 Environs Australia. “Triple Bottom Line reporting”. [http://www.environs.org.au/business/tbl\\_reporting.html](http://www.environs.org.au/business/tbl_reporting.html) Visited, January 2002.

Redesigning Resources. 2000. “Triple Bottom Line Reporting: Benchmarking Our Performance”. <http://www.redesigningresources.org/q2all.htm> October, 2000. Visited, January 2002.

<sup>41</sup> Grant, Andrew. 2001. “Take Stock”. *Australian CPA* 71 [2]:32

<sup>42</sup> Landcare Research. “Enviro-MarkNZ”. <http://www.landcare.cri.nz/science/sustainability/enviromark/> Visited, January 2002.

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The *Local Government Finance Standard* 1994 also requires a capital funding statement<sup>43</sup>, the net change in operating capability for each significant function or activity<sup>44</sup>, and statement of original budget compared with actual results<sup>45</sup>.

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<sup>43</sup> Section 50

<sup>44</sup> Section 51

<sup>45</sup> Section 52

## 6. INTERNAL REPORTING

This chapter examines the research around the world in relation to the content of financial reports required to cover the three areas of importance – achieving community objectives, enhancing operating capacity, and managing financial risk. The chapter then examines developments in improving internal reporting techniques.

### 6.1. Key Points

- Financial reporting needs to be part of the organisations knowledge management framework.
- It should be one of the organisation’s main feedback, learning and improvements processes.
- Financial reporting needs to be linked to the achievement of the organisation’s objectives.
- There is widespread dissatisfaction with traditional internal financial reporting.
- Management can only assimilate a limited amount of information, so reports must be focussed. More is not better.
- For financial information to be useful, the literature suggests it must be:
  - accurate, timely and reliable;
  - coupled with analysis (based on analytical tools), and insights on the implications for the achievement of objectives;
  - forward looking (forecasts etc);
  - in a language or format preferred by the reader (usually non-numeric – eg graphs, charts, ratios);
  - short reports focussed on exceptions and pertinent issues (requiring management attention or corrective action); and
  - contain peer comparisons (benchmarking).
- There is a move towards more holistic reporting, such as the Balanced Scorecard and Key Performance Indicators. (See also Chapter 5). A simplified Balanced Scorecard is included for use by small to medium councils.

### 6.2. Internal Reporting Content

As outlined in Framework and Methodology Chapter (Chapter 3), local government financial management needs to manage and monitor three inter-related areas: achieving community objectives, managing financial risk, and enhancing operating capacity. This implies that local government accountants have a wider role than their traditional role of management reporting and the production of statutory external reports. In ‘New Roles for Management Accountants’, Kaplan makes the following observations:

- Technological advances have allowed management accountants to become part of the organisations value added team.
- Management accountants must participate in the formulation and implementation of strategy, then help translate strategic intent into operational and managerial measures.
- Accountants need to move away from being scorekeepers and to become the designers of the organisations critical management information systems.
- Existing measurement systems focus on improving existing processes. The Balanced Scorecard, by contrast, focuses on what new processes are needed to achieve breakthrough performance objectives for customers and shareholders.
- This new environment requires greater cost and performance information on the organisation’s activities, processes, products, services and customers.

## *Achieving Community Objectives*

One of the major developments in internal management reporting over the last decade has been the increasingly widespread use of the Balanced Scorecard (BSC), initially published by Kaplan and Norton in 1992 (Harvard Business Review). Under the balanced scorecard, key performance measures are developed in four perspectives in a way intended to underpin the organisation's strategy. In other words the measures are aimed at measuring the progress towards achieving the strategy. The four perspectives are normally financial, customer, internal processes, and people/innovation and learning. It is intended that the balanced scorecard measures become the main focus of management attention rather than traditional management accounting reports. Interestingly, this is very similar to Drucker's suggestion previously outlined since competence is related to innovation and learning, productivity is related to internal processes, and the foundation information is related to the financial perspective. It is also a highly correlated to our three areas outlined in the framework and methodology-community objectives, financial risk and operating capacity. The comparison is shown in the following table:

<b>Balanced Scorecard</b>	<b>This Review</b>	<b>Peter Drucker</b>
Customer	Community objectives	-
Financial	Financial risks	Foundation information
Internal Business Processes	Operating Capacity	Productivity
People/Learning and Innovation	-	Competencies

Therefore, we will be applying a scorecard approach to monitoring the finances of the organisation in the following four perspectives:

- \_ Achievement of Community Objectives;
- \_ Managing Financial Risks;
- \_ Enhancing Operating Capacity; and
- \_ Financial Competencies and Learning.

The City of Charlotte is portrayed by Kaplan and Norton as a best practice example of using the balanced scorecard in the public sector, and was the first U.S. City to adopt the balanced scorecard approach. Charlotte's interest in the balanced scorecard approach resulted from their interest in using a more strategic, forward-looking framework to organise and implement performance measures. Prior to using the balanced scorecard, they had been measuring performance for decades in a more traditional management-by-objectives context.

In 1990, Charlotte City Council chose five areas (community safety, transportation, economic development, neighbourhoods, and restructuring government) on which to focus its strategic plan. These priorities formed the basic categories in their "corporate" level scorecard. In the mid-1990s, several Council members advocated for more outcome or results-oriented measures. During the first year of implementation in 1996, the City Council established the city's "corporate" scorecard, and city staff from four pilot business units began developing their balanced scorecards. By the end of 1997, all 13 of the city's business units had at some level developed their measures and balanced scorecards based on the corporate scorecard.

Charlotte is pursuing a balanced scorecard approach to performance measurement in the more formal sense. That is, they categorise measures according to the four "perspectives" typically associated with a balanced scorecard: financial, customer, internal business processes, and learning/growth. All thirteen of the city's business units participate in the measurement system, tracking a total of 266 measures. The customer perspective is the most emphasised of the four perspectives, accounting for 38% of the total measures. The other three perspectives account for the following: internal processes, 27%; growth and learning, 21%; and financial, 13%.

The next steps that Charlotte plans to take to improve its balanced scorecard system include the following:

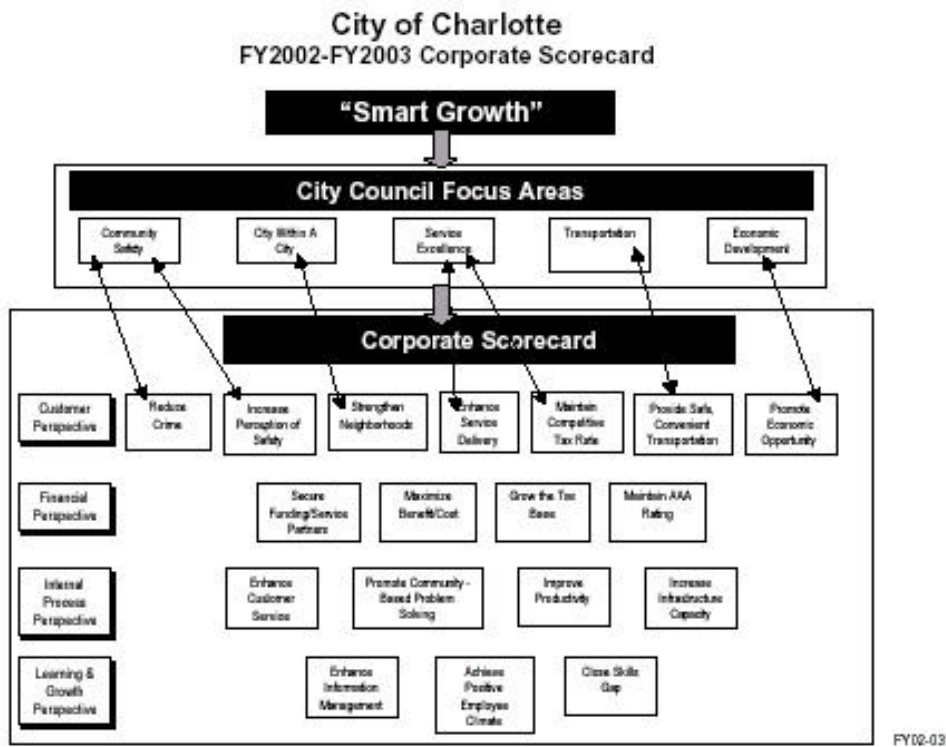
- \_ condense the current list of performance measures to the "critical few";
- \_ continue refining their business unit plans and scorecards;
- \_ move to a quarterly reporting system (from the current semi-annual schedule), and eventually
- \_ link performance results and resource allocations.

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Charlotte uses their balanced measures for several purposes: to communicate performance information to elected officials and the public, as input in their strategic planning process, in annual business unit and employee performance plans, and to identify areas for further evaluation and improvement. It is claimed that the City of Charlotte’s performance measurement effort has provided value to the city in the following ways:

- measuring performance has clarified vague concepts like strategic goals;
- the balanced scorecard helped to integrate common goals across departments;
- it has allowed them to set their performance measures into a more comprehensive, strategic context;
- it has encouraged them to narrow their list of performance measures to those that are more meaningful and useful; and
- building the scorecards has developed consensus and teamwork throughout the organisation.

**FIGURE 8: CORPORATE SCORECARD FOR CHARLOTTE, US**



The balanced scorecard minimises information overload by limiting the number of measures used. Companies rarely suffer from having too few measures. Disparate elements of the organisation are brought together in a single management report. Kaplan and Norton strongly recommend using the balanced scorecard to monitor progress in achieving the organisations strategies. This requires the measures used to be linked into a strategic framework.

Although Charlotte City applies the standard four perspectives developed by Kaplan and Norton (Customers, financial, internal processes, and people and learning) alternative ways of using a Balanced Scorecard in the public sector have been advocated and used by others. Olve, Roy and Wetter (in ‘Performance Drivers: a practical drive to using the balanced scorecard’) advocate applying the different perspectives in the public sector: Performance, Relationships, Activities/programs, and Future.

Similarly, in the US, the General Accounting Office (GAO) notes:

‘Some of these agencies, ... used a balanced scorecard approach, which is intended to provide a balanced perspective regarding agency results, customer satisfaction, and employee feedback. At one [agency’s] regional offices, for example, computerised

information is continuously displayed on video screens providing employees with current performance information.'

The GAO itself applies the balanced scorecard to evaluating programs and IT projects. However, it substitutes 'Strategic measures' for the financial perspective.

In CPA Australia's 'Applying the Balanced Scorecard', the experience of organisations in using the balanced scorecard in Australia was examined. The researchers found: In practice the balanced scorecard refers to any set of financial and non-financial measures. Balanced Scorecard is a shorthand way of putting all critical variables for running the organisation on one page. This includes balance among performance measures: balance between the leading and lagging; financial and non-financial; internal and external; and balance between the single minded financial view of the world with additional focus on non-financial ones.

The Balanced Scorecard can be used to articulate strategy, communicate its details, motivate people to execute plans, and enable executives to monitor results. The main advantage cited is improved decision-making. Financial measures, used alone, give an incomplete picture of an organisation's performance, which is equated to driving along a windy road through the rear-view window. The balanced scorecard was also claimed to:

- improve performance continuously;
- Implement more complex strategies;
- run lean, decentralised organisations;
- feed systems for organisational learning; and
- drive organisational change.

Much of an organisation's success depends on managing external relationships: partners, suppliers, customers, shareholders and other stakeholders. Therefore organisations should use measures that translate vision and strategy into concrete directions for action, for example:

- **Financial** – how can we show our strategy is succeeding financially.
- **Customer** – how can we show we're delivering to customers the value they expect.
- **Internal Business Process** – what processes must we excel at to deliver value to our customers.
- **Learning and Growth** – what action must the company take to prepare the people and organisation for the future.

The CPA Australia publication suggests cascading the scorecard down the organisation structure to the personal scorecard, and advises organisations to ensure that the corporate scorecard:

- must support the manager's scorecard;
- include a mix of lead and lag indicators; and
- must not exceed 15 measures.

In Australia, the Brisbane City Council is regarded as a leader in the introduction of the balanced scorecard in the public sector in Australia. In the Council's Annual Report, also published on their website, the Council outlines its achievement against the scorecard as follows:

**Customer and Community Outcomes**

- 74% community satisfaction with Council's rubbish and recycling services
- 69% community satisfaction with Council's water and sewerage services
- 71% community satisfaction with Council providing festivals and cultural events
- 74% community satisfaction with Council parks, gardens and open space areas

**Financial Outcomes**

- Maintenance of Standard and Poor's AA+ credit rating

**Process and Innovation Outcomes**

- 71% of staff understand how their job directly contributes to the objectives of the Corporate Plan

**People and Learning Outcomes**

- 76% of employees see Council as a good place to work
- Productivity lost to workers’ compensation reduced (target 0.45%, result 0.38%)

**FIGURE 9: BALANCED SCORECARD FOR BRISBANE CITY COUNCIL**



As part of our research we have reviewed actions being taken in terms of performance management including performance reporting by two Queensland Government Departments and a Government Owned Corporation. We have noted that both of the government departments reviewed have or are in the process of upgrading internal and external reporting through the use of a Balanced Scorecard approach.

The Quarterly Performance Review of one of the departments which is provided to the Senior Management Group is structured to report on a range of performance measures under the following broad headings:

- Stakeholder Relations;
- Financial and Delivery Performance;
- Internal Processes and Practices; and
- People and Learning.

The department has adopted a planning and performance management model which integrates the balanced scorecard into the overall framework. The overall model is structured within the context of the Government Priorities and the Managing for Outcomes framework.

The department further developed its performance management reporting practices including incorporating the Balanced Scorecard around 2 years ago and has recently reviewed its progress in implementation. This has led to a process of ongoing refinement of the performance management framework including further development of the performance measures in use.

For external reporting purposes the Annual Report of the Department incorporates a three-page report in Balanced Scorecard format.

***Enhancing Operating Capacity - The Accountant’s Role***

Most traditional financial reporting focuses on financial results, which we have seen underpin the public sector requirement to monitor and enhance the operating capacity of the organisation. This has traditionally been the main role of management accountants.

The GAO published its research into ‘Creating Value through world-class financial management’ in April 2000. It found that Management Accountants in all sectors are increasingly being asked to supplement their traditional role with more financial analysis and management consulting.

World-class finance organisation can be defined in terms of business outcomes:

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- Improved business analysis;
- Innovative solutions to business problems;
- Reduced operating costs;
- Increased capability to perform ad-hoc analysis; and
- Improved overall business performance.

The best organisations made financial management improvement an entity-wide priority by building a foundation of control and accountability that supports external reporting and performance management.

In another publication, the GAO has stated that ‘to reap the full benefits of financial reform, federal finance organisations must go beyond the audit opinion toward:

- establishing seamless systems and processes;
- routinely generating reliable cost and performance information and analysis;
- undertaking other value-added activities that support strategic decision-making and mission performance; and
- building a finance team that supports the agency’s mission and goals.’

In a book by leading management theorists Kaplan and Cooper “Cost & Effect: Using Integrated Cost Systems To Drive Profitability And Performance” 1998, the authors note that internal systems are required to provide feedback for learning and improvement within the organisation. They claim that most companies have financial systems which meet external financial reporting requirements and collect costs by responsibility centres, however this approach provides feedback to managers and employees which is too late, aggregated, and financial instead of providing useful feedback to improve business processes. More advanced organisations have operational feedback systems which provides managers and employees with timely, accurate information, both financial and non-financial, on the efficiency, quality, and cycle times of business processes.

According to Maskell in his provocative book “Making The Numbers Count: The Accountants As Change Agent On The World Class Team”, world class companies are those with fully evolved organisation-wide process improvements and performance measures and can be characterised as follows:

- the business is run primarily on non-financial measures;
- cost accounting has been eliminated;
- budgets are high level and only used for planning purposes;
- many aspects traditional accounting systems have been eliminated; and
- the focus of accounting staff’s effort is on process improvements and re-engineering.

Maskell also claims that the management accounting profession has been under fire over the last few years due to criticism of the traditional techniques and management accounting. Much of information traditionally provided by management accountants in the private sector is seen as wasteful, misleading and causing more problems than it solves. More relevant management accounting activities are emerging in best practice organisations including:

- activity based costing;
- activity based management;
- customer profitability;
- performance measurement;
- value added analysis;
- process mapping;
- target costing;
- value engineering;
- variety effectiveness process;
- life cycle costing;
- quality function deployment; and
- competitive benchmarking.

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Professors Kaplan and Johnson in "Relevance Lost: The Rise And Fall Of Management Accounting" 1987 were even more scathing about traditional management accounting by claiming that "cost accounting is the number one enemy of productivity." The key criticisms of traditional management accounting are that it is not directly related to the organisation's strategy, distorts costs, was inflexible, incompatible with world-class approaches and inappropriately linked to financial accounts.

In Australia, Ashton in the Management Accounting Centre Of Excellence (CPA Australia) publication 'Contemporary Perspectives on Management Accounting' 1999, observed

'In essence, the management accountant provides support of the decision-making process, providing management with information so needed it can select one course of action from a set alternative courses of action in the context of some predetermined objectives. In supporting the decision-making process, management accountants are also able to change managerial behaviour.

Management accountants will need to produce information about the operations of the organisation and those factors which may be affecting these operations. Management accountants will not be able to provide assistance nor will management, no matter how able, be able to function properly without an adequate flow of information. The degree to which a good decision can be made is governed by the quality of the analysis and information furnished. Therefore, it is apparent how important reporting and analysis are to the successful operation of business. There is often a general lack of perspective on modern management's real information needs at each level. As a result, the information and reporting systems fall short of what is needed and what is possible. The systems that do evolve are frequently disconnected, do not tie in with accounting records, and contain almost as many different reporting formats as there are managers demanding information. Such a situation hardly assures the best utilisation of company resources.'

According to Ashton, the criteria of a good reporting system are:

- it should mirror the company's organisation structure so that accountability for results is clearly shown;
- that for each organisational unit, it covers all the material control elements of performance that affect the unit's contribution to the overall organisational goals;
- it is represented, in total, an integrated plan of control, so that information is furnished to all levels of management; and
- it is, itself, under continuous control, so that it can be adjusted promptly to meet changing needs.

In New South Wales, the Auditor-General reviewed the financial reporting practices of a number of agencies in 2001, and found serious deficiencies. Therefore, he developed a better practices guide for the use by agencies. This guide is available on the Internet at [http://www.audit.nsw.gov.au/guides-bp/IFR\\_contents.htm](http://www.audit.nsw.gov.au/guides-bp/IFR_contents.htm)

The key theme of the report is the need to link financial results with indicators of performance of objectives, and simpler reporting. Since Auditor-General's report is very recent and higher relevant to the Australian public sector key aspects of the report had been reproduced below. The following are pertinent extracts from this guide:

- Sound internal financial reporting is essential for the proper management of resources and delivery of services. Ideally, the financial information included in these reports should be supplemented by non-financial information. Unlike external financial reporting, there are no standards or prescribed minimum requirements for internal financial reporting by NSW public sector agencies.
- There is a need for agencies to manage their information needs. A sound internal reporting system is essential for proper management. Within such a framework, internal financial reporting is pivotal to ensure proper control of resources, the efficient application of those resources to processes and the direction of those processes to the production of defined outputs.
- Internal financial reporting typically comprises financial information on revenue, expenditure, assets and liabilities against budgets or pre-determined limits. For internal financial reporting to be

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truly useful as a management tool, there is a need for it to contain non-financial information that supplements and where necessary elaborates on the financial information.

- Accordingly, for internal financial information to be effective there is a need to ensure that:
  - the vision of the organisation is translated into clear objectives and strategies;
  - the risks to the achievement of these objectives are clearly identified and managed;
  - the responsibilities of managers being consistent with the objectives of the organisation; responsibilities need to be clearly defined, communicated and understood by all key stakeholders and managers accountable for responsibilities allocated;
  - performance measures integrate financial and non financial performance information; and
  - performance measures are linked directly to the objectives of the organisation.
  
- Organisations should establish a structured approach to collecting, analysing, producing and using financial information that helps managers at all levels to manage. Improved performance often relies on the access to, and the integration of, financial and non-financial information. Information to improve performance often requires access to a range of databases within an organisation from which information can be extracted, manipulated and analysed. To enable this interface information systems need to integrate or interface. This can be achieved by using a central integrated system which is based around one system.

### ***NSW Auditor-General's Summary***

Better practice organisations:

- translate the vision of the organisation into clear objectives and strategies and identify clearly the risks to the achievement of the objectives;
- have management accounting and information systems that support the organisation's strategic objectives;
- integrate financial and non financial information for measuring and monitoring performance;
- assign responsibilities to managers being consistent with the objectives of the organisation and their authority;
- measure performance against assigned responsibilities;
- adopt accrual based accounting and reporting on a continuous basis has been implemented;
- apply business simulation techniques and conduct 'what if' scenario modelling to explore options and help make decisions that will improve performance;
- undertake internal and external benchmarking of performance against the relevant industry, other levels and jurisdictions of government, and the private sector;
- have an integrated database or established access to interrogate a range of systems, supporting easy access to information required; and
- use their information for the evaluation of capital investment decisions.

Better practice organisations:

- identify the type of information needed at various levels of management;
- provide financial and non-financial information in a balanced way;
- establish clear line of accountability;
- link budget to strategic plan;
- identify components of budget (costs, income, assets etc);
- provide timely and accurate information as to variations;
- compare trends over time, allowing comparisons to the previous year or years' figures and/or for the same period last year, and undertake internal comparisons and benchmarking;
- have regard to information needs that may vary from year to year and the particular emphasis or focus that can vary according to the time of year, seasonal factors, changes in agency responsibilities or unusual events;
- require a simple and uniform structure for the chart of accounts and based on need, limit the number of cost centres and accounts in the general ledger;
- present internal reports as close as possible to the format of external reports including the financial statements contained in the Annual Report;
- require commonality of the year end projections used in internal reports and Treasury Financial Information System (FIS) monthly reports;

- establish a business case for new information required but is not readily available [that is the cost to collect and report the information versus the benefits of obtaining the information];
- institute legal and regulatory "sign offs" as part of the preparation of statutory financial statements
- periodically review what information is currently available;
- provide commentary on the remedial action that is being taken or proposed to be taken to remedy any performance problems highlighted in the report.

Inclusion of full accrual costs, including depreciation, a possible capital usage charge, and so on, are essential for managers to be able to make fully informed decisions about the optimal use of resources. Better practice management includes the requirement that a business case, or equivalent, be prepared to support all significant investment proposals. Source: Beyond Bean Counting (page 69).

### ***Managing Financial Risk***

In a leading text on corporate governance "The fish rots from the head" Garratt, 1997, makes the following observations: "behind the key performance indicators and the overseeing of management performance systems is the basic notion that the board needs to be able to know where the company is in where it should be so that deviations can be assessed and resources wisely allocated to correct the situation. Otherwise it is taking unnecessary risk. Risk is essential to an enterprise. If we had full knowledge of the future there would be no risk. We live in a gloriously imperfect world that allows for great rewards, harsh punishments and major disasters. Corporate risk management is the ultimate responsibility of the board. In the end boards still tend to return to assessing financial risk as the highest priority for the enterprise's and board's survival. One increasingly used technique by financial analysts is the Z-score. Ratios appropriate to the enterprise are selected, weighted and then added together to produce a single index. Whilst there is no single model the typical z-score would comprise performance indicators for at least: profitability, working capital, financial risk, and liquidity."

The Cadbury report 'The Financial Aspects of Corporate Governance' 1992, recommends that the directors make statements in the annual report on the effectiveness of the internal systems of control is a way of assessing risk for shareholders'.

In New Zealand the Fiscal Responsibility Act 1994 specifies five principles of responsible fiscal management and strengthens government reporting requirements. The five principles of fiscally responsible management are:

- reduction of government debt to prudent levels;
- maintaining prudent debt levels over a reasonable period of time;
- achieving and maintaining levels of Crown net worth;
- managing fiscal risks in a prudent manner; and
- pursuing policies consistent with predictability about the level and stability of tax rates for future years.

It can be seen that all of these measures relate to financial risk issues.

Similarly the Blair government in Britain introduced the Code for Fiscal Stability to improve standards of transparency and accountability. Again five principles of fiscal management are outlined:

- transparency;
- stability;
- responsibilities;
- fairness; and
- efficiency.

Specific commitments under this policy included fiscal and debt management policies, explicit fiscal policy objectives, debt management policies, and better practice accounting methods used in the production of public accounts.

In Australia, the Howard government introduced the Charter Of Budget Honesty Act 1998 which requires the government to conduct its fiscal policy responsibly. The Charter includes the requirement

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to 'manage risks faced by the Commonwealth prudently, having regard to economic circumstances, including by maintaining Commonwealth and general government debt at prudent levels'

Over the past decade, all Australian State and Territory governments have adopted some form of medium-term fiscal management. A major objective of these fiscal management policies has been the achievement of debt reduction through expenditure restraint. In Queensland the government's fiscal management policy requires full funding of accruing liabilities and restricting borrowing to projects which can generate sufficient income to service the debt.

The Joint Committee of Public Accounts (1995) in its report on fiscal responsibility legislation claims that some key indicators need to be specified which the government must report against. The range of indicators included:

- net financial position/worth;
- net debt as a percentage of GDP/GSP;
- operating deficit/surplus; and
- other indicators including net worth indicators and debt to revenue indicators.

The steering committee on national performance monitoring of GTE's specified and defined in number of financial performance indicators in relation to financial risk, these are debt to equity, total liabilities to equity, current ratio, and interest cover.

The Office of Local Government Commissioner in Queensland developed a number of financial indicators for assessing financial strength of local governments for the boundary review and amalgamation assessments. Vulnerability indicators included reliance on grants and government projects, and reliance on revenue from particular industries or businesses. Flexibility indicators included operating surplus, interest cover, reserve and rate levels, and rate arrears.

It is interesting to note that one of the key indicators used by Charlotte City in its balanced scorecard is the maintenance of its AAA credit rating. Similarly, Brisbane City Council has a goal of maintaining its AA+ credit rating in its balanced scorecard. These credit ratings are issued by ratings agencies such as Standard & Poor. This organisation prepares credit ratings for a number of Local Governments, and includes the following criteria:

FIGURE 10: CREDIT RATINGS FOR LOCAL GOVERNMENTS



In assessing the financial position of local and regional governments, Standard & Poor's examines the following financial risk factors:

- liquidity;
- debt burden; and

- Off Balance Sheet Liabilities.

They also monitor financial flexibility and performance including reliance on particular revenue sources and financial flexibility.

### **6.3. Financial Management Issues**

A number of financial management responsibilities were identified in the Councillor Focus Group (Discussed in Chapter 2. Background). These provide a useful framework to analyse the financial management role and responsibilities of Councillors. These have been sorted into the balanced scorecard framework discussed above.

#### ***Community Objectives***

##### ***Delivery of Promised Outcomes – Strategic & Operational Planning***

Each council is accountable to the community for its performance. To ensure that there is a clear and common understanding amongst councillors and staff about the Council's desired goals, strategies and key performance measures, a strategic and operational planning process is needed.

The Council's strategic plan should set the framework for individual business plans to be developed by divisions, programs or business units which have ownership of the more specific strategies and measures used to steer their contribution towards achieving the Council's outcomes and goals.

The planning process should also link to the budget process so that the resources required for new initiatives are identified and allocated.

##### ***Value for Money***

The need for efficiency and effectiveness in the delivery of services is a key responsibility. This includes:

- a fair and competitive procurement policy and process is in place;
- the use of benchmarks to compare performance across comparable organisations and to prompt questions about disparities;
- comparisons of actual results against targets and previous results to encourage continuing improvements; and
- periodic reviews of work practices having regard for technological change and ideas on best practice.

#### ***Financial Risk***

##### ***Budget Setting and Monitoring***

The Budget is a key direction setting and management control document for any organisation including for local governments. The *Local Government Act 1993* (section 518) requires that all local governments adopt a budget each year for their operating fund sometime between 1 June and 1 September (or a later date fixed by the Minister). The Act requires the budget to be developed consistently with the Council's corporate plan and operational plan, while the Local Government Finance Standards require, amongst other things, the use of accrual accounting.

Apart from the purpose of genuine emergency or hardship, a local government may not incur spending that is not authorised by its Budget (section 519). Councillors may be liable for disbursements made other than in accordance with the budget or for emergency or hardship reasons (section 523).

##### ***Integrity of Finances (Sustainable Revenue Policy)***

Councillors have a responsibility to represent the overall public interest of their community. This public interest role includes the setting of rates that will provide a sustainable level of funding for the

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cost of services being provided for the current generation of ratepayers. This cost includes an allowance for the replacement of infrastructure and other depreciating assets. It also raises such issues as:

- equitable contributions toward the initial cost of facilities through developer contributions; and
- the need to subsidise or fund the expansion of commercial enterprises operated by Council.

Sustainable revenue policy means ensuring that a future generation of ratepayers will not need to pay for services which have been consumed by the current generation of ratepayers. Generally, the most significant issue of financial sustainability is the deferral of infrastructure replacement and the creation of maintenance backlogs. This question requires that these needs be identified and an assessment made of the extent to which annual depreciation costs are, or should be funded from rates or other revenue sources.

The Local Government Finance Standard requires that a council must adopt a number of financial management policies including:

- a policy on borrowings; and
- a policy about revenue (section 8).

In particular, the policy about revenue is to include:

- how rates and charges are decided, including the extent the rates and charges relate to relevant costs;
- any rebates and concessions on rates and charges;
- any limitation on increases in rates and charges;
- the extent that physical and social infrastructure costs for new developments are to be funded by charges for the development;
- whether it is intended to maintain, decrease or increase the operating capability of the local government and the extent to which it may be decreased or increased; and
- whether depreciation, or other non-cash expenses, are to be fully funded.

### ***Borrowings***

The Local Government Finance Standard indicates that a local government's policy on borrowings must include:

- new borrowings planned for the current financial year and the next 2 financial years;
- the purpose of the new borrowings; and
- the time over which it is planned to repay existing and proposed borrowings.

The Council also needs to have an understanding of the overall level of borrowings and to relate that in some meaningful way to the level of assets it is financing and the level of revenue required to support the annual financing costs (interest). The statement of financial position gives a useful snapshot view of a Council's level of assets and liabilities (including borrowings) – provided the values are current.

A useful indicator of debt servicing ability is the debt-servicing ratio, which covers both interest and debt repayments against operating revenue as follows:

$$(Annual\ interest\ expense + debt\ repayments) / annual\ operating\ revenue$$

Changes in this ratio over time indicate whether a Council's capacity to service its debt is improving or declining. There is no right level for all councils and the level will vary as interest rates change. Nevertheless, a council should consider adopting a target range and report against it regularly. Further, if it is considered that the debt level is currently too high, the council may adopt strategies aimed at meeting a target over time.

### ***Capacity to Manage "Shocks" (Reserves)***

Any organisation needs to maintain a level of reserves to cover unexpected events that cannot be reliably budgeted for. The level and nature of reserves is a decision to be taken by each Council and can include specific or general reserves.

Specific reserves can be set up for infrastructure – where funding is required over and above the replacement funding available from recovering depreciation expense through rates.

Grants, subsidies, developer contributions and other funding received in advance should be separately identified in the statement of financial position as “prepayments” or “unearned revenue”.

Special funding or levies such as street mall improvements or bushland preservation would need to be separately identified as not being available to meet Council’s normal operating costs.

### ***Forward Financial Planning (more than the next term)***

There are benefits for any Council to have some forward estimates for financial planning purposes. This is especially so when a Council is seeking to correct over time some element of the finances such as to reduce the level of debt servicing as a percentage of operating revenue.

It is noted that State governments adopt a three-year forward estimates process, while many utilities have financial plans extending out from 20 to 50 years.

## ***Operating Capacity/Internal Processes***

### ***Paying Bills on Time (Cash Management)***

Local Governments have a responsibility to ensure on an ongoing basis that they are meeting their financial obligations in a timely manner.

Effective cash management requires that an organisation should meet contractual and commercial terms of payment. As well, it requires that the organisation maximise the return on funds held (that is, paying neither early nor late). Council’s financial management systems should have the capacity to record the due date for payment of bills and to manage payments accordingly (by electronic transfer where possible).

### ***Managing Infrastructure***

While Council engineers have always had a concern for whether, when and how infrastructure needs to be built and replaced, the introduction of accrual accounting has highlighted these issues from a financial perspective and made them an on-going financial management responsibility of Councillors.

Accrual accounting requires the annual cost of “consuming” an asset to be recognised as an expense. This recognition of depreciation expense is necessary to fairly represent the cost of the Council’s operations each year - including to report on the extent to which those cost have been covered by revenues (that is, whether the Council has made an operating surplus or loss).

In addition, the effective management of infrastructure requires long-term asset management planning.

### ***Adequate Provision for Depreciation***

The Revenue policy mentioned above includes a requirement to assess whether depreciation is to be fully funded.

Assets are acquired with a combination of borrowings, grants and subsidies, internal reserves, use of depreciation funding, developer contributions, sale of other assets or a special levy or charge. The decision on whether to fully fund depreciation needs to be considered in the light of future asset replacement planning requirements.

Asset managers can provide information, as part of the asset planning process, on expected asset degradation and the expected expenditure required for refurbishment, replacement and renewal of assets. In terms of expansion of the infrastructure base, there will need to be consideration of the level of funding required from internal sources to complement the contributions of developers, grants and subsidies and level of borrowings.

### ***Systems, Processes, Controls, Auditability***

The elected member has a responsibility to ensure that there are appropriate systems, processes and controls which help manage the financial risks a council is subject to and to facilitate the audit process.

There are a range of requirements which should be in place including:

- financial management policies clearly defined in a manual;
- where appropriate, an internal audit function (either in-house or out-sourced);
- an audit committee of the council or a process whereby the full council may meet as an audit committee;
- an independent appraisal of all business related systems and related controls in place at least once every three years; and
- a process to ensure that appropriate action is taken on issues raised by the Auditor-General as the external auditor whether there is an Audit Committee or not.

### ***Competencies, Learning and Innovation***

#### ***Innovation – Other Income Streams (Enterprise) – but take care***

The focus group noted that innovation and enterprise are important aspects of the role of an elected member. Understanding of the risks and returns is a critical element of the up front assessment of the project or activity proposed.

All proposals requiring a significant level of funding should be supported by a proper business case which assesses the benefits, costs and risks.

#### ***External Funding Contributions***

The role and responsibilities of councillors includes considering opportunities from funding initiatives of other levels of government, community groups, etc..

Even if these do not require Council to contribute funding up-front, the longer-term consequences need to be assessed. Council needs to consider:

- the ongoing operational and maintenance costs;
- any community expectations that the initiative will be continued after the external funding is exhausted; and
- the need to replace assets.

#### ***Employing Good Finance Staff***

Like any organisation local governments need to ensure that competent staff are employed and that opportunities are provided for training and development. Even staff with accounting qualifications will need ongoing professional development.

For many isolated local governments, there are challenges in engaging and retaining quality financial staff. The need to access good quality financial management advice should not be overlooked.

#### ***Towards a Better Understanding of Financial Management***

There is a need for Councillors to understand the financial and performance information which is, or should be, regularly presented to them.

The ability to read and understand financial information contained in a statement of financial position and operating statement is an essential, while the need to have clear and user-friendly reports is equally important.

#### ***Challenges of Smaller Councils***

The focus group process noted the challenges for Councillors of smaller Councils and the need for assistance in terms of seeking best practice finance strategies. These Councils do not have the depth of

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qualified staff resources as compared with the larger Councils. Councillors from smaller Councils would welcome further guidance in terms of best practice finance strategies.

In assessing the scope of the issues identified by the focus group, BDO Kendall's reviewed the issues against the following criteria:

Issue	Capability of Elected Members and Council staffing	Strategic Direction Setting	Management Control	Performance Management and Monitoring	Audit/Accountability
Delivery of Promised Outcomes		X		X	X
Budget setting & monitoring		X	X	X	X
Integrity of Finances (sustainable revenue policy)		X			X
Borrowings		X	X		
Capacity to Manage "Shocks" (Reserves)		X			
Forward Financial Planning		X			
Paying Bills on Time			X		
Managing Infrastructure		X	X		
Adequate Provision for Depreciation		X	X		
Systems, Processes, Controls, Auditability			X		X
Value for Money			X	X	X
Innovation – Other Income Streams (Enterprise)		X			
External Funding Contributions		X			
Employing Good Finance Staff	X				
Understanding of Financial Management	X				

### ***Simple Local Government Balanced Scorecard***

Although many smaller and medium sized Councils may feel that their Council is too small to warrant a Balanced scorecard, the Councillors at the LGAQ focus group clearly expressed a need for information which fits neatly within a balanced scorecard framework. Based on these findings, the following is a suggested framework of balanced scorecard measures that may be applicable to many local governments or used as a basis for establishing a balanced scorecard within the organisation. It is suggested that 15-20 of the most relevant indicators could be used for this purpose. It should be noted that a pure balanced scorecard as outlined by Kaplan and Norton contains indicators that are limited to the overall strategy rather than a collection of indicators in each area. However, most organisations usually start with a collection of indicators and gradually shift to a more strategic scorecard.

#### ***Community objectives***

- Delivery of promised activities (by exception).
- Service level measures (e.g. library borrowing levels, roadwork activity).

- Customer or community satisfaction survey (if conducted).
- Numbers of complaints.
- Other key performance measures based on the corporate plan.

#### ***Financial Risk***

- Liquidity (working capital or current ratio).
- Solvency (debt ratios).
- Revenue ratio.
- Overall budget variances (for operational revenue, operational expenditure, capital revenue, capital expenditure).
- Revenue sustainability (revenue forecasts compared to expenditure trends).
- Unrestricted reserve levels.

#### ***Operating Capacity/Internal Processes***

- Corporate overheads as % of total expenditure.
- Rate arrears ratio.
- Percentage of bills paid on time.
- Percentage of funded depreciation.
- Internal and external auditor report issues.
- Operating expenditure per capita (excluding depreciation) compared to similar councils.

#### ***Competencies, learning and innovation***

- Employee indicators:
  - average sick days per employee;
  - absenteeism; and
  - leave liability balances.
- Average training days per employee.
- Innovative changes in the organisation.
- Percent of revenue from innovative functions (special-purpose grants, private works, etc).
- Councillor and CEO satisfaction with financial reports.

## **6.4. Improving Reporting Techniques**

### ***Overseas Experience***

The United States General Accounting Office “Executive Guide On Creating Value Through World-Class Financial Management”(April 2000) noted that ‘to effectively evaluate and improve the value derived from government programs and spending, ... decision makers must have accurate and reliable financial information on program cost and performance. Further, they must be able to rely on ... finance organisations to provide analysis and insight about financial implications of program decisions and the impact of those decisions on agency performance goals and objectives. Currently, financial data is not always useful, relevant, timely, and reliable enough to be used for ... decision-making, and many ... finance organisations are not yet well equipped enough to routinely provide analysis or advice related to this information.’

This report also noted a significant change occurring in the private sector. It noted a major study which had shown that in the 1980s, most CFO’S were spending 75 to 80 percent of their time on fiduciary issues, particularly external reporting, but today leading finance organisations owing to spend only 20 percent of their time on fiduciary duties in the remaining time providing strategic support activities including cost analysis of business performance analysis. Similarly, a 1996 report by the Institute of Management Accountants found that management accountants are being increasingly asked to supplement their traditional accounting role with more financial analysis and management advice.

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The GAO report claims that leading finance organisations have eliminated, reduced or redesigned much of their old management reporting formats to meet the needs of the user. New reporting formats have been designed around key business drivers rather than organisational structures to provide management with relevant forward-looking information on business unit performance. It also claims that leading finance organisations present relevant financial information in an understandable, simple formats with suitable details and explanations. According to the research standardised reports are designed to present information which is analysed so as to highlight pertinent and fundamental issues. In United States changes are underway in many government agencies to develop meaningful, user-friendly accountability reports on individual departments and agencies. In addition to meeting statutory compliance requirements, reports in these agencies show the degree to which the organisation has met its goals and at what cost, and assist the reader in determining whether the organisation was well run.

Best practice examples provided by the GAO include exception reporting and presentation of information in the form of charts and graphs so as to enhance the readability of the report increasing, the impact on the message and being sensitive to the demands on the reader's time. In these reports actual financial performance is supplemented with forecasts so as provide a perspective on what has happened together with a view of what is expected to happen in the future. Such reports also provide benchmarks or "peer comparisons" that compares the organisation's key measures to those of other organisations in the industry. Management reporting in these best practice organisations is driven by the overall objectives of the organisation rather than traditional management accounting approaches.

New technology has made financial data more available, but without the ability to translate that data into relevant, understandable information decision-makers are left powerless. Best Practice organisations have changed management reports to be focussed around key business drivers (not necessarily around organisational structures). Use of web technologies allow use of drill down, short summaries and supplemented with more detail below.

Good reporting shows the degree to which an agency met its goals and at what cost and assists the reader in determining whether the agency is run well.

The GAO report advocates redesigning management reports around key business drivers provides decision-makers with relevant, forward-looking information. Traditional reports use a monthly report which is very detailed, comprised of static reports and schedules entirely based on what has happened and contains no external or competitive perspectives. By contrast, best practice executive summaries feature "exceptions" or those items specifically worthy of focus. In addition, information is presented in charts and graphs. This approach enhances the documents readability, increases the impact of the message, and is sensitive to the demands on the audience's time. Good reporting need to be supplemented with forecasts so as to provide a perspective of what has happened with a view of what is expected to happen. Such reports also contains peer comparisons and benchmarking, since an external perspective is vital to assessing performance in a relevant context.

Maskell claims that many managers find accounting reports confusing and complicated. He notes that best practice organisations provide simpler standardised reports which are presented in a clear way focusing on key issues. For example, some provide for graphs on a single page for each area showing standard quality, cost, timeliness, and customer satisfaction measures used throughout the organisation.

In 'Towards better management reporting', the authors claim that excellent Financial Reports:

- Include Operational Data; and
- Include Updated Forecasts of Year End Results.

This requires management accounting reports to provide early warning of crises, so as to facilitate early corrective action. Reports also should provide advance indication of surpluses, to allow for better management of resources.

In 'Is Your Board Reporting Process Out Of Control': the author notes that current-reporting processes can be overly time consuming. To improve on this situation accountants need to:

- look to "variance to budget" reporting (look at YTD, not month variance);
- focus on key measures; and
- use icons and graphics in the reports.

## *Australian Experience*

The experience in Australia mirrors that in public and private sectors overseas. In the Management Accounting Centre of Excellence, Report "contemporary perspectives on management accounting 1999", Ashton claim: 'in the past it was generally assumed that the more information management received, the better informed it was. We now know that in reality management can only assimilate a limited amount of information. Many reports included in indigestible amount of information in a form that contains too many lines and columns with irrelevant and excessive detail. One of the most common causes of this condition is the attempt to make a report serve too many purposes. Others do not draw the distinction between information should appear on regularly issued reports and output should otherwise be held in reserve for the benefit of special analysis and study.

One of the most disappointing aspects of many present-day reports is that even when all the right information is included, it is not presented in a simple, clear, meaningful form that will permit a manager to make the property valuations and decisions. Sometimes the very form in which information is presented will cause managers to take the wrong approach in analysing their operations. In other instances, it may be either impossible to interpret a report correctly, or the effort to do so is prohibitive.... The responsibility for this situation lies both general in financial management.

The characteristics of a good report include:

- it covers an element of performance that materially reflects the end result;
- it facilitates measurement of performance by comparing results of goals;
- it reports only essential information, so that the reader gets a complete picture without being confused;
- its segregated controllable and uncontrollable items so that responsibility of the means of action is not obscured;
- it focuses attention on matters that require action by highlighting significant trends from expected performance;
- it appears in a form that is easy to understand and use;
- it is expressed in the language of the reader;
- it is distributed only to persons who are concerned with the subject in the degree of detail in which it is presented;
- it is issued promptly, regularly, and at appropriate intervals; and
- it is prepared economically in comparison to the value it produces.

Reports that are cumbersome, difficult to read, fraught with error, untidy, too detailed, and not on time do not establish the most suitable environment for an effective relationship between management and management accountants."

A report by the NSW Auditor General in June 2001 was critical of internal financial reporting mechanisms in NSW government Departments. He revealed that some agencies miscalculated projected costs and others exceeded their full year projections by mid-year. 'The report showed a lack of appreciation by most agencies of the need for sound financial reporting. It shows a lack of understanding by senior management of basic financial measures. Most agencies had not yet identified and or were not reporting against key performance indicators. In some agencies, the internal financial reports contained little, or no, operational performance information. The report also found:

- Managers lacked skills and training;
- Financial reports tend not to contain information on performance of activities;
- Agencies are producing large amounts of irrelevant information;
- Distribution and use of reports has not kept pace with technology.

It claimed that many organisations produce large volumes of financial information, yet managers do not always find what is available is complete, accurate, reliable, timely, concise, user-friendly and relevant.

As a result the NSW Auditor General prepared a Better Practice Guide to assist agencies. This Guide raises the following issues:-

“The sheer volume of some agencies’ monthly internal financial reports raises questions about the relevance of the material included. The length of reports produced by agencies ranged from 18 pages to over 150 pages. Better practice suggests that about 10 pages for executive level reports should be sufficient.

According to the Auditor General, better practice organisations streamline reports, use exception based reporting and cull data that are either duplicated or not used regularly. In distributing and presenting the reports, there is a need to consider the format of management reports, including the use of visual aids.

The printing and distribution of voluminous pages of financial information is time consuming and costly and increases the risk that reports will not be used. In many instances better use could be made of technology eg *Intranet*, to distribute financial reports more efficiently. To assist and inform this process there is a need for:

- a basis to measure the efficiency and effectiveness of the delivery of programs, outputs and outcomes (key performance indicators);
- integrated financial and other performance information for decision-making by management;
- agencies to benchmark operations with other organisations and evaluate the options to ‘contract out’; and
- agencies to track the costs of various functions over time notwithstanding a tendency to restructure.

Better practice organisations tailor their internal financial reports to meet the needs of identifiable groups of users. They have a system for identifying: what information is needed:

- who needs which types of information;
- when the information is needed by particular users;
- what format the information is required to be in; and
- how best to distribute the information.

Better practice organisations:

- provide prompt advice and allocation of budget funding as close as is practicable to the commencement of the financial year;
- provide reports available to senior management within two to five days after month end;
- actively monitor delays in provision of the reporting information;
- have quality assurance processes so that the content of reports is reliable;
- update budgeted, actual and forecast information on a monthly basis; and
- provide reports to the Board/Executive Group about one week prior to the executive meeting.

Better practice organisations:

- limit reports to ten pages or less;
- report on key performance indicators to supplement traditional financial reporting;
- ensure the financial information is future focused and balanced with non-financial information;
- limit numerical information (no more than 20%) in favour of graphs and charts in reports;
- recognise the need for flexibility and compromise in determining the content and format of reports as needs vary within user groups;
- customise reports to the extent possible but do need to find the right balance between too much and too little information;
- consider what needs can be adequately met on an ad-hoc and/or specialist basis rather than building too much into the mainstream reporting; and
- maintain an inventory or catalogue of the financial management reports available to managers in an agency. The inventory is regularly reviewed to ensure the reports are timely, relevant and accurate.

It is important that departments have information systems that enable efficient and effective production of reports to meet their reporting responsibilities, which at times require production of reports at

monthly, quarterly, half-yearly and annual intervals, and which may cover both financial and performance information.”

The report also noted that attention is being given to streamlining their information management and reporting processes to minimise the need to excessively extract and collate material for their various reporting requirements. It is important that departments and the central agencies distinguish between indicators that are relevant for internal management, central agency monitoring and external accountability.

### ***Queensland Local Government Experience***

ORION consulting recently conducted research for the LGAQ on the financial reporting needs of CEO's and senior managers. The survey findings were consistent with above research and found that:

- Accrual accounting has been widely accepted, but is seen as overly complex and too dominated by statutory requirements and complex jargon.
- There is confusion as to who is responsible for the Council finances. Ideally this needs to be clarified in the legislation, as it is for companies.
- Most Council executives feel that they are accountable for the financial performance of areas under their control, indicating that this is an important issue for them.
- Managers are feeling the pressure of cost increases, revenue pressures, increasing community expectations and the need to manage their existing assets. Interestingly, improved business unit performance is not seen as a major means to address these pressures.
- There appears to be a high level of usage of corporate and operational plans, with a large number developed prior to, or in conjunction with, the budget.
- Executives spend a relatively small proportion of their time reviewing financial reports, and this creates a need for short, simple to understand reports on a timely basis. Current reports do not always appear to satisfy this requirement.
- With improved reporting managers believe they will be able to:
  - Be more accountable;
  - Better manage the assets under their control within the same budget;
  - Improve financial performance in the Council and its businesses;
  - Improve community services and outcomes for the same budget; and
  - Be more able to stay within their budget.
- Preferences were expressed for the following reporting improvements –
  - Shorter reports (5-10 pages);
  - Simpler variance reports, by exception, which take account of major timing issues;
  - More use of trend and other graphs;
  - Improved linkages between expenditure and services/works performed;
  - Matching revenue and expenditure items;
  - Simpler terminology and additional training;
  - Online enquiries with drill-down capability;
  - Reduced statutory requirements coupled with improved internal reporting; and
  - Customised reports to individual readers, rather than each manager receiving the same whole-of-Council report.

### ***Use of Graphs***

All of the literature review stresses the importance of presenting financial information using graphs and charts. However some authors suggest that there are effective and ineffective ways of applying this technique. In the book 'How Well Do You Graph': the authors outline a list of do's and don't for use of graphing:

Do:

- consider length of time your audience will spend viewing the graph and the level of familiarity they have with the topic;

- use clearly defined data points;
- keep it simple;
- clean and uncluttered;
- bold contracts that differentiate groups; and
- no more than around 6 lines (we mentally de-construct graphs and commit information to short term memory, our short term memory can only cope with 8-10 items).

Use Caution with:

- perspective, since it can add numerous confusing visual cues and reading axes can be next to impossible; and
- pie charts, because it can be very difficult to rank slices in order of size.

### ***Responsive Reporting and Systems***

With the trend towards more responsive reporting many organisations are streamlining their accounting operations. This is often labelled as "Just In Time Accounting" or "One Day Reporting". John Petty and Stephen Ng outlined examples of this process in the Australian CPA (Aug 1999). Steps involved in process included process mapping, review of reports and information, identification of key drivers, system upgrades, and training and support.

Ipswich City Council applied many of these principles in its Financial Systems Streamlining Project, although it has not yet achieved a one day reporting cycle. Brisbane City Council is currently implementing its FILLIP project (Financial Leadership Improvement Project). A key component of this project is a 'System Benefits Realisation' project to make best use of the facilities which are available in its new financial software suite. This project was based on the GAO review outlined in 6.2.

The other aspects of this project are:

- **Accountabilities** (ensuring managers know their roles and expectations in relation to assets, tax, payroll, budgeting, revenue, purchasing, risk/internal controls, and financial performance reporting); and
- **Skills Development** (policy awareness training); and
- **Policies practices and procedures** (documentation of corporate practices on the intranet to create a 'no excuses' environment).

Both of the Ipswich and Brisbane projects involve monthly accruals so that the results are both timely and accurate. In contrast, most Councils in Queensland only perform accruals by annual or at best on a quarterly basis. It is common for One Day Reporting approaches to focus on the major accruals and to leave an exhaustive accruals process to a quarterly or annual review, however ignoring all accruals, monthly basis at best reduces the benefits of accrual accounting, and worst runs the risk that major expenses are missed and overspending could occur.

Another advantage of streamlining financial systems and processes is that it can release resources from returning functions to assist in analysis of financial results and advice on corrective action. In this way the overall resources in finance function need not be increased and can even reduce even though there is an increase in analytical and advisory resources. For example Ipswich City Council gradually reduced finance staffing levels by nearly 20% whilst nearly doubling the professional accounting resources.

It is therefore suggested that all councils should review their routine financial operations and make best use of facilities available in the computer software so as to release additional resources to analysis and reporting activities.

### ***Impact of NCP/Business Management***

The introduction of business management practices into local governments required by the National Competition Policy creates additional financial reporting requirements and sometimes may also change

the governance arrangements. It is important for than these new financial reporting needs are incorporated into the financial software available to local governments so that this does not creates additional resource requirements. It is understood that are to Local Government Association Queensland is already addressing this issue with software suppliers.

## **6.5. Best Practice Management Accounting Framework**

The following are the issues which need to be addressed within each council in order to achieve best practice management accounting:

### ***Governance***

- Mechanisms for elected members to monitor key financial information throughout the year, for example the finance committee or audit committee, at least on a quarterly basis.
- Such committee should be charged with responsibility for monitoring the council's financial risks (liquidity and long-term debt levels), operating capacity, and achievement of community objectives.
- Such committee should not focus on detailed variance reports or cheque listings.
- Instead, this committee should monitor the issues outlined in the suggested balanced scorecard (eg the simple balanced scorecard outlined above in 6.3).

### ***Reporting***

- Financial reporting should be linked to the achievement of the organisation's objectives
- Financial information needs to be:
  - Accurate, timely, and reliable;
  - Coupled with analysis (based on analytical tools) with insights on implications for the achievement of objectives;
  - Include forward-looking information such as projected end of year results;
  - In the format preferred by readers such as graphs, trends, charts and ratios;
  - Short (10 pages or less) focused on exceptions and pertinent issues which require management attention to corrective action; and
  - Include comparisons with targets or benchmarks with similar councils.

### ***Systems and reporting processes***

- Councils need to review their financial operating practices to make best use of the features and facilities available in their financial software, so as to expedite periodic reporting and release resources for analysis and exception reporting.
- Key elements of one-day reporting concepts should be applied including the accrual of major items for each reporting period.
- Reporting facilities of the financial software needs to incorporate the above reporting features.

### ***Financial Management Competencies***

- There needs to be a reduction in the resources used to prepare external reports and operate internal financial processes.
- These resources need to be applied to improve internal reporting based on the above principles.
- Accountants in Local Government need to ensure they have skills in:
  - Determining the information requirements of managers and councillors;
  - Understanding the corporate objectives and financial management implications
  - Interpreting accounting data and expressing this with non-financial methods;
  - Developing efficient internal processes to meet the above reporting requirements;
  - Distilling the key information which needs to be brought to councillor and management attention for corrective action;
  - Assessing and monitoring financial risks, both short-term and long-term; and
  - Communicating key issues to management and councillors using non-numeric techniques.

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## **ATTACHMENT – CURRENT REPORTING PRACTICES**

The following is a summary of responses to an e-mail sent to selected Councils. The questions asked were:

- \_ How many annual reports are produced?
- \_ How many annual reports are distributed to ratepayers? Is there a charge?
- \_ Is the annual report currently produced in CD-Rom format? Is there a charge?
- \_ Is the annual report available on the website?
- \_ Do any commercialised or corporatised units produce a separate annual report or annual review?
- \_ Is a brochure containing abridged financial information for ratepayers produced?

BEST PRACTICE SIMPLIFIED INTERNAL AND EXTERNAL REPORTING

Council	Aprox Rates Collection (\$'000s)**	No. of reports	Charge	Obtained by ratepayers	CD	Charge	Web Site	Annual Report on Web Site	Commercial Units*	Brochure Produced
Brisbane	808,735,000	2,000	N	most outlets run out during year	N	N	Y	Y	Y	Y
Cairns	91,143,687	1,000	\$20	100	N	N	Y	Y	N	Y
Emerald		45	N	10	N	N	Y	Y (excl financial statements)	N	Y
Gladstone	23,552,149	100	N	10 or 20	N	N	N	N	N	N
Gold Coast		1,200	N	?	Y	N	Y	Y	Y	Y
Herberton	2,570,252	20	\$26	~1	N	N	N	N	N	N
Ipswich	84,872,644	200	N	?	N	N	Y	N	Y	N
Laidley		14	?	only one sold since 1993	?	?	N	N	?	N
Logan	113,126,991	500	N	<125	Y	N	Y	Y	Y	Y
Noosa	33,075,913	500	N	most copies gen distributed	Y (some info)	N	Y	Y	N	N
Pine Rivers	63,309,000	600	N	<10	N	N	Y	Y	Y	Y
Redland		500	N	approx 20%	N	N	Y	Y	Y	Y (plus media releases)
*Separate Reports produced for Commercial Units.										
** Information was taken other sources; not from the email survey.										

## ATTACHMENT – CURRENT ANNUAL STATEMENT REPORTING PRACTICES

A survey of Annual Statements produced by Local Councils was undertaken to determine the current usage of Management Discussion and Analysis and Financial Ratios. This survey was not exhaustive, annual statements held in the LGAQ library and those donated directly by Local Councils were used.

### 2000/2001

Name of Council	Year of Report	Rates Collection	MDA present?	Details of MDA	Financial Ratios Used
Brisbane City Council	2000/2001	808,735,000	Y	comprehensive comm ind Triple Bottom Line Report	Y
Herberton Shire Council	2000/2001	2,570,252	N		N
Ipswich City Council	2000/2001	84,872,644	Y	comm - interpretation of fin statemts, sig events	Y
Mareeba Shire Council	2000/2001	10,795,452	Y	finance section w/ pie graphs + fin summ ind interpretation of statemts	Y
Noosa Shire Council	2000/2001	33,075,913	Y	numerous pie graphs - loans, rev, assets, cash reserves, cap expend	Y
Pine Rivers Shire Council	2000/2001	63,309,000	Y	fin overview ind tables & bar graphs	Y
Stanthorpe Shire Council	2000/2001	Not avail	Not avail		N
Warwick Shire Council	2000/2001	9,939,389	Y	fin services highlights ind tables & bar graphs	Y

BEST PRACTICE SIMPLIFIED INTERNAL AND EXTERNAL REPORTING

**1999/2000**

Name of Council	Year of Report	Rates Collection	MDA present?	Details of MDA	Financial Ratios Used
Boulia Shire Council	1999/2000	580,000	Y	commentary - rev, expend & general ind pie graphs	N
Brisbane City Council	1999/2000	721,593,000	Y	comprehensive comm ind Triple Bottom Line Report	Y
Bulloo Shire Council	1999/2000	2,180,038	Y	pie and trend graphs with brief commentary	Y
Bundaberg City Council	1999/2000	27,502,943	N		N
Burdekin Shire Council	1999/2000	17,058,582	N		N
Caboolture Shire Council	1999/2000	59,298,576	Y	fin comm w/ bar graphs, fin snapshot using pie graphs	Y
Cairns City Council	1999/2000	91,143,687	Y	fin summ - pie and bar graphs, comm	Y
Caloundra City Council	1999/2000	47,621,000	Y	fin summ - pie graphs	Y
Cambooya Shire Council	1999/2000	1,189,818	N		N
Douglas Shire Council	1999/2000	10,367,411	N		Y
Gold Coast City Council	1999/2000	284,216,478	N		N
Logan City Council	1999/2000	113,126,991	Y	fin snapshot - comm, graphs, explanatory diag	Y
Longreach Shire Council	1999/2000	2,612,252	N		Y
Maroochy Shire Council	1999/2000	82,938,000	N		Y
Milmeran Shire Council	1999/2000	2,263,903	N		Y
Mirani Shire Council	1999/2000	3,280,238	N		Y
Mount Isa City Council	1999/2000	13,616,000	Y	key fin statistics - op statemt, fin pos, non-current assets purchases	Y
Pine Rivers Shire Council	1999/2000	59,418,000	Y	perfoe highlights, bar & pie graphs, key stats, fin overview - comm	Y
Toowoomba City Council	1999/2000	53,484,589	Y	fin summ - Op statemt, statemt of fin positn, cap works, cash flows	Y
Waggamba Shire Council	1999/2000	2,836,000	Y	fin highlights	Y
Warwick Shire Council	1999/2000	5,604,362	Y	fin services highlights	Y
Whitsunday Shire Council	1999/2000	11,678,084	N		Y

BEST PRACTICE SIMPLIFIED INTERNAL AND EXTERNAL REPORTING

**1998/1999**

Name of Council	Year of Report	Rates Collection	MDA present?	Details of MDA	Financial Ratios Used
Boulia Shire Council	1998/1999	604,000	Y	commentary - rev, expend & general ind pie graphs	N
Brisbane City Council	1998/1999	703,675,000	Y	Fin comm w/ bar graphs, KPIs; highlights ind KP ratios & pie graphs	Y
Bulloo Shire Council	1998/1999	2,159,479	Y	pie and trend graphs with brief commentary	N
Bundaberg City Council	1998/1999	26,622,606	N		N
Burdekin Shire Council	1998/1999	16,485,894	Y	comm, summ table of major financials, bar graphs	Y
Caboolture Shire Council	1998/1999	55,534,901	Y	fin highlights - bar & pie graphs, tables, commentary	Y
Caloundra City Council	1998/1999	46,143,000	Y	fin summ - pie graphs	N
Gladstone City Council	1998/1999	23,552,149	N		N
Logan City Council	1998/1999	93,657,623	Y	fin snapshot - comm, graphs, explanatory diag	Y
Maroochy Shire Council	1998/1999	78,549,000	N		Y
Mirani Shire Council	1998/1999	2,968,294	N		Y
Pine Rivers Shire Council	1998/1999	56,448,000	Y	fin overview - comm	Y
Rockhampton City Council	1998/1999	38,682,559	N		N
Whitsunday Shire Council	1998/1999	10,957,884	N		Y
Winton Shire Council	1998/1999	1,804,000	Y	fin comm - rev, exp, cap works, shire debt, general	Y