

EXPLANATORY NOTES TO THE FINANCIAL STATEMENTS

1. SUMMARY OF ACCOUNTING POLICIES

Reporting Entity

Taranaki Regional Council is a regional local authority governed by the Local Government Act 2002.

The Taranaki Regional Council group (TRC) consists of Taranaki Regional Council and its subsidiary Port Taranaki Ltd (100% owned). Port Taranaki Ltd is a port company governed by the Port Companies Act 1988 and incorporated in New Zealand.

The primary objective of Taranaki Regional Council is to provide goods or services for the community or social benefit rather than making a financial return. Accordingly, Taranaki Regional Council has designated itself and the group as public benefit entities for the purposes of New Zealand equivalents to International Financial Reporting Standards (NZ IFRS).

Basis of preparation

The financial statements of the Taranaki Regional Council group have been prepared in accordance with the requirements of the Local Government Act 2002: Part 6, Section 98 and Part 3 of Schedule 10, which includes the requirement to comply with New Zealand generally accepted accounting practice (NZ GAAP).

These financial statements have been prepared in accordance with NZ GAAP. They comply with NZ IFRS, and other applicable Financial Reporting Standards, as appropriate for public benefit entities.

Accounting policies are selected and applied in a manner which ensures that the resulting financial information satisfies the concepts of relevance and reliability, thereby ensuring that the substance of the underlying transactions or other events is reported.

The financial statements have been prepared on a historical cost basis, modified by the revaluation of land and buildings, certain infrastructural assets, investment property, and financial instruments.

The financial statements are presented in New Zealand dollars. The functional currency of Taranaki Regional Council is New Zealand dollars.

The accounting policies set out below have been applied consistently to all periods presented in these financial statements.

Significant accounting policies

The following significant accounting policies have been adopted in the preparation and presentation of the financial report:

Subsidiaries

Consolidated prospective financial statements have not been prepared for the purposes of this *Plan*. The Council has not presented group prospective financial statements because the Council believes that the parent prospective financial statements are more relevant to users. The main purpose of prospective financial statements in this *Plan* is to provide users with information about the core services that the Council intends to provide ratepayers, the expected cost of those services and as a consequence how much the Council requires by way of rates to fund the intended levels of service. The level of rates funding required is not affected by subsidiaries except to the extent that the Council obtains distributions from, or further

invests in, those subsidiaries. Such effects are included in the prospective financial statements of the Council.

Associates

Associates are those entities in which the Council has significant influence, but not control, over the financial and operating policies. The financial statements include the Council's share of the total recognised gains and losses of associates on an equity accounted basis, from the date that significant influence commences until the date that significant influence ceases. When the Council's share of losses exceeds its interest in the associate, the Council's carrying amount is reduced to nil and recognition of further losses is discontinued except to the extent that the Council has incurred legal or constructive obligations or made payments on behalf of the associate.

Revenue

Revenue is measured at the fair value of consideration received.

Rates revenue. Rates are set annually by a resolution from Council and relate to a financial year. All ratepayers are invoiced within the financial year to which the rates have been set. Rates revenue is recognised when payable.

Other revenue. Government grants are assistance by the government in the form of transfers of resources to the Council in return for past or future compliance with certain conditions relating to operating activities. Government grants include government assistance where there are no conditions specifically relating to the operating activities of the Council other than the requirement to operate in certain regions or industry sectors. Government grants relating to income are recognised as income when the conditions to receive the grant have been met. Government grants that are receivable as compensation for expenses or losses already incurred or for the purpose of giving immediate financial support to the consolidated entity with no future related costs are recognised as income of the period in which it becomes receivable.

Revenue from the rendering of services is recognised by reference to the stage of completion of the transaction at balance date, based on the actual service provided as a percentage of the total services to be provided.

Direct charges. Sales of goods are recognised when the Council has transferred to the buyer the significant risks and rewards of ownership of the goods or services. The recorded revenue is the gross amount of the sale, including fees payable for the transaction. Such fees are included in other expenses.

Where a physical asset is acquired for nil or nominal consideration the fair value of the asset received is recognised as revenue. Assets vested in Taranaki Regional Council are recognised as revenue when control over the asset is obtained.

Interest income is recognised using the effective interest method.

Dividends are recognised when the right to receive payment has been established.

Income Tax

Income tax on the profit or loss for the year comprises current and deferred

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tax. Income tax is recognised in the surplus or deficit in the *Statement of Comprehensive Income* except to the extent that it relates to items of other comprehensive income, in which case it is recognised in other comprehensive income.

Current tax is the expected tax payable on the taxable income for the year, using tax rates enacted or substantially enacted at balance sheet date, and any adjustment to tax payable in respect of previous years.

Deferred tax is provided using the comprehensive balance sheet liability method, for temporary differences between the carrying amount of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. Deferred taxation assets attributable to tax losses or deductible temporary differences are recognised when realisation is probable. Deferred taxation liabilities attributable to taxable temporary differences are amounts of income taxes payable in future periods. However, deferred tax assets and liabilities are not recognised if the temporary differences giving rise to them arise from the initial recognition of assets and liabilities (other than as a result of a business combination) which affects neither taxable income nor accounting profit. Deferred tax assets and liabilities are calculated using the tax rates expected to apply when the assets are recovered or liabilities settled, based on those tax rates which are enacted or substantively enacted at balance sheet date.

The measurement of deferred tax liabilities and assets reflects the tax consequences that would follow from the manner in which the Company expects, at the reporting date, to recover or settle the carrying amount of its assets and liabilities. Deferred taxation assets and liabilities can be offset when they relate to income taxes levied by the same taxation authority and the Company intends to settle its current assets and liabilities on a net basis.

Foreign currency

Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of the transactions. Foreign exchange gains and losses resulting from the settlement of such transactions are recognised in the surplus or deficit in the *Statement of Comprehensive Income*. Foreign currency monetary items at reporting date are translated at the exchange rate existing at reporting date.

Cash and cash equivalents

Cash and cash equivalents includes cash in hand, deposits held at call with banks, other short-term highly liquid investments with original maturities of three months or less, and bank overdrafts. Bank overdrafts are shown within borrowings in current liabilities in the *Statement of Financial Position*.

Inventories

Stocks of riparian plants are valued at the lower of weighted average cost or net realisable value. Stocks of maintenance materials and supplies are valued at the lower of weighted average cost or net realisable value. Net realisable value represents the estimated selling price less all estimated costs of completion and costs to be incurred in marketing, selling and distribution. The write down from cost to net realisable value is recognised

in the surplus or deficit in the *Statement of Comprehensive Income*.

Financial assets and liabilities

Financial assets and liabilities are recognised in the Council's *Statement of Financial Position* when the Council becomes a party to the contractual provisions of the instrument. Financial assets are initially recognised at fair value plus transaction costs unless they are carried at fair value through profit or loss in which case the transaction costs are recognised in the surplus or deficit in the *Statement of Comprehensive Income*.

Purchases and sales of financial assets are recognised on trade-date, the date on which the Council and group commits to purchase or sell the asset. Financial assets are derecognised when the rights to receive cash flows from the financial assets have expired or have been transferred and the Council and group has transferred substantially all the risks and rewards of ownership.

The Council and group classifies its financial assets into the following categories: fair value through profit or loss, held-to maturity investments, loans and receivables and fair value through equity. The classification depends on the purpose for which the investments were acquired. Management determines the classification of its investments at initial recognition.

Fair value through profit or loss

Financial assets at fair value through profit or loss include financial assets held for trading. A financial asset is classified in this category if acquired principally for the purpose of selling in the short-term. Derivatives are also categorised as held for trading unless they are designated as hedges. Assets in this category are classified as current assets. The Council and group's financial assets at fair value through profit or loss include derivatives that are not designated as hedges. After initial recognition they are measured at their fair values with gains or losses on remeasurement recognized in the surplus or deficit in the *Statement of Comprehensive Income*.

Held-to maturity investments

Held-to-maturity investments, such as corporate bonds, are non-derivative financial assets with fixed or determinable payments and fixed maturities that management has the positive intention and ability to hold to maturity. They are measured at initial recognition at fair value plus transaction costs, and subsequently carried at amortised cost less impairment losses.

Loans and receivables

Loans and receivables, such as general loans and deposits, are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. They are measured at initial recognition, at fair value plus transaction costs, and subsequently carried at amortised cost less impairment losses.

Available for sale

Financial assets classified as available for sale are those that are designated as available for sale or are not classified in any of the other categories above. They are included in non-current assets unless

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management intends to dispose of the investment within 12 months of the balance date. The Council and group's financial assets available for sale comprise investments that it intends to hold long-term but which may be realised before maturity and shareholdings that it holds for strategic purposes.

The Council's investment in Port Taranaki Ltd is not included in this category as it is held at cost as allowed by NZ IAS 27 Consolidated and Separate Financial Statements.

After initial recognition available for sale equity investments are measured at their fair value, with gains and losses recognized directly in equity except for impairment losses, which are recognised in the surplus or deficit in the *Statement of Comprehensive Income*.

On derecognition the cumulative gain or loss previously recognised in equity is recognised in the surplus or deficit in the *Statement of Comprehensive Income*.

Financial liabilities and equity

Trade payables. Trade payables are initially measured at fair value, and are subsequently measured at amortised cost, using the effective interest method.

Derivatives

A derivative is a financial instrument or contract whose value changes in response to a specified interest rate, instrument price, commodity price, foreign exchange rate, credit index or other variable. It requires no or a nominal initial investment and is settled at a later date.

Derivative financial instruments are initially recognised at fair value on the date a derivative contract is entered into and are subsequently measured at their fair value at each balance sheet date. The Council and Group do not have any derivative instruments that qualify for hedge accounting and therefore any gain or loss on remeasurement to fair value is recognised immediately in the surplus or deficit in the *Statement of Comprehensive Income*.

The Council and Group may enter into foreign currency forward exchange contracts, to hedge foreign currency transactions when purchasing major fixed assets and when payment is denominated in foreign currency. Gains and losses on such contracts are recognised each year at balance date or date of completion by restating the asset or liability at the prevailing spot rate.

Impairment of assets

At each reporting date, the Council and Port Taranaki Ltd reviews the carrying amounts of its tangible and intangible assets to determine whether there is any indication that those assets have suffered an impairment loss. If any such indication exists, the recoverable amount of the asset is estimated in order to determine the extent of the impairment loss (if any). Where the asset does not generate cash flows that are independent from other assets, the Council and Port Taranaki Ltd estimates the recoverable amount of the cash-generating unit to which the asset belongs.

Recoverable amount is the higher of fair value less costs to sell and value

in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset for which the estimates of future cash flows have not been adjusted.

If the recoverable amount of an asset (or cash-generating unit) is estimated to be less than its carrying amount, the carrying amount of the asset (cash-generating unit) is reduced to its recoverable amount. An impairment loss is recognised in the surplus or deficit in the *Statement of Comprehensive Income* immediately, unless the relevant asset is carried at fair value, in which case the impairment loss is treated as a revaluation decrease.

Where an impairment loss subsequently reverses, the carrying amount of the asset (cash-generating unit) is increased to the revised estimate of its recoverable amount, but only to the extent that the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss been recognised for the asset (cash-generating unit) in prior years. A reversal of an impairment loss is recognised in the surplus or deficit in the *Statement of Comprehensive Income* immediately, unless the relevant asset is carried at fair value, in which case the reversal of the impairment loss is treated as a revaluation increase.

Property, plant and equipment

These assets consist of:

- Operational assets. These include land, buildings, motor vehicles, plant & equipment, office furniture, computer equipment and improvements.
- Infrastructure assets. These are fixed utility systems owned by the Regional Council such as the Waitara and Waiwhakaiho River Flood Protection Scheme assets. Each asset type includes all items that are required for the network to function.

Property, plant and equipment is shown at cost or valuation, less accumulated depreciation and impairment losses.

Additions

The cost of an item of property, plant and equipment is recognised as an asset if, and only if, it is probable that future economic benefits or service potential associated with the item will flow to the Council and the cost of the item can be measured reliably.

In most instances, an item of property, plant and equipment is recognised at its cost. Where an asset is acquired at no cost, or for a nominal cost, it is recognised at fair value as at the date of acquisition through the surplus or deficit in the *Statement of Comprehensive Income*. Cost includes expenditure that is directly attributable to the acquisition of the item. In the event that settlement of all or part of the purchase consideration is deferred, cost is determined by discounting the amounts payable in the future to their present value as at the date of acquisition.

Valuation

Unless stated valuations are carried out or reviewed by independent qualified valuers and are carried out at least on three yearly cycles. Valuations will be undertaken more regularly if necessary to ensure no

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individual item of property, plant and equipment within a class has a carrying value that is materially different from its fair value. The only classes of assets revalued are Council owned infrastructure assets (valued at depreciated replacement cost) and land owned by Port Taranaki Ltd (valued at fair value). All other classes of assets are held at cost.

Revaluation increases and decreases relating to individual assets within a class of assets are offset. Revaluation increases and decreases in respect of assets in different classes are not offset. Where the carrying amount of a class of assets is increased as a result of a revaluation, the net revaluation increase is credited to the revaluation reserve. The net revaluation increase shall be recognised in the surplus or deficit in the *Statement of Comprehensive Income* to the extent that it reverses a net revaluation decrease of the same class of assets previously recognised in the surplus or deficit in the *Statement of Comprehensive Income*. A net revaluation decrease for a class of assets is recognised in the surplus or deficit in the *Statement of Comprehensive Income*, except to the extent that it reverses a revaluation increase previously recognised in the revaluation reserve to the extent of any credit balance existing in the revaluation reserve in respect of the same class of asset.

Depreciation

Depreciation calculated on a straight-line basis, which writes off the value of the assets over their expected remaining lives after allowing for residual values where applicable. The depreciation rates are as follows:

Buildings	5 to 50 yrs	2 to 20%
Motor vehicles	5 yrs	20%
Plant and equipment	2.5 to 25 yrs	4 to 40%
Office furniture and fittings	5 to 10 yrs	10 to 20%
Computer equipment	3 to 5 yrs	20 to 33%

The residual value and the useful life of assets are reviewed at least annually.

Flood scheme assets – the nature of these assets is equivalent to land improvements and, as such, they do not incur a loss of service potential over time. Land and flood scheme assets are not depreciated. Maintenance costs are expensed as they are incurred in the surplus or deficit in the *Statement of Comprehensive Income*.

Intangible assets

Intangible assets acquired by the Council and Group comprise of computer software and are stated at cost less accumulated amortisation and impairment losses. Amortisation is charged to the surplus or deficit in the *Statement of Comprehensive Income* on a straight-line basis over the estimated useful life of the intangible assets. The estimated useful lives are as follows:

Computer software	2 to 5 yrs	20 to 50%
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Research and development

Expenditure on research activities, undertaken with the prospect of gaining

new scientific or technical knowledge and understanding, is recognised in the surplus or deficit in the *Statement of Comprehensive Income* when incurred. Expenditure on developing the application of any research findings will only be capitalised if able to demonstrate all of the following conditions: It is technically feasible to complete so it will be available for sale or use, intended to be completed, able to be used or sold, will generate probable future economic benefits, there are adequate technical, financial and other resources to complete the development to use or sell, and can be measured reliably during its development.

Investment property

Investment properties which are held to earn rental income and/or for capital appreciation are stated at fair value. An external, independent valuer revalues investment property portfolio on an annual basis. Any gain or loss arising from a change in the fair value of investment property is recognised in surplus or deficit for the period in which it arises. There is no depreciation on investment properties.

Employee benefits

Short-term benefits

Employee benefits that Taranaki Regional Council expects to be settled within 12 months of balance date are measured at nominal values based on accrued entitlements at current rates of pay. These include salaries and wages accrued up to balance date, annual leave earned to, but not yet taken at balance date, sick leave and retiring and long service leave entitlements expected to be settled within 12 months.

Long-term benefits

The provision for long service leave and retirement gratuities has been calculated on an actuarial basis bringing to account what is likely to be payable in the future in respect of service that employees have accumulated up until the reporting date.

Provisions

A provision is recognised in the balance sheet when the Council has a present legal or constructive obligation as a result of a past event, it is probable that an outflow of economic benefits will be required to settle the obligation and the amount of the provision can be measured reliably.

The amount recognised as a provision is the best estimate of the consideration required to settle the present obligation at reporting date, taking into account the risks and uncertainties surrounding the obligation. Where a provision is measured using the cashflows estimated to settle the present obligation, its carrying amount is the present value of those cashflows.

Borrowings

All loans and borrowings are initially recognised at fair value, net of transaction costs. Subsequent to the initial recognition, loans and borrowings are carried at amortised cost with any difference between the initial recognised amount and the redemption value being recognised in the surplus or deficit in the *Statement of Comprehensive Income* over the period of the borrowing using the effective interest rate method.

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Equity

Equity is the community's interest in the Council and is measured as the difference between total assets and total liabilities. Equity is disaggregated and classified into a number of reserves.

The components of equity are:

- Retained earnings—comprise accumulated surpluses over the years.
- Asset revaluation reserves—comprise accumulated revaluation increments/decrements.
- Reserves—formally imposed designations of public equity that indicate Council's intention to use a certain level of resources for a special purpose.

Goods and Services Tax (GST)

All items in the balance sheet are stated exclusive of GST with the exception of receivables and payables, which include GST. All items in the *Statement of Comprehensive Income* are stated exclusive of GST. Cash flows are included in the cash flow statement on a gross basis. The GST component of cash flows arising from investing and financing activities which is recoverable from, or payable to, the taxation authority is classified as operating cash flows.

Overhead allocations

Overheads have been allocated against activity centres on the basis of staff numbers. However, in the case of Councillors (Representation), they have been allocated on a 0.5:1 ratio.

Borrowing costs

The Group recognises as an expense within the *Statement of Comprehensive Income* all borrowing costs incurred, with the exception of interest costs incurred during construction/assembly of major capital projects, which are capitalised as part of the initial cost of the respective assets.

Operating lease payments

Payments made under operating leases are recognised in the surplus or deficit in the *Statement of Comprehensive Income* on a straight-line basis over the term of the lease, except where another systematic basis is more representative of the time pattern in which economic benefits from the leased asset are consumed.

Rental income from operating leases is recognised on a straight-line basis over the term of the relevant lease.

Borrowings are classified as current liabilities (either advances and deposits or current portion of term debt) unless the Group has an unconditional right to defer settlement of the liability for at least 12 months after the *Statement of Financial Position* date.

Statement of Cash Flows

Cash flows from operating activities are presented using the direct method.

Definitions of terms used in the Statement of Cash Flows:

- Cash means cash on deposit with banks, net of outstanding bank overdrafts.
- Investing activities comprise the purchase and sale of property, plant and equipment, investment properties and investments

- Financing activities comprise the change in equity and debt capital structure of the company
- Operating activities include all transactions and events that are not investing or financing activities.

Work-in-progress

Work-in-progress relates to unbilled time and costs (current asset) or time and costs billed-in-advance (current liability) for resource consent applications, resource consent compliance monitoring and unauthorised pollution incidents.

Critical accounting estimates and assumptions

In the application of NZ IFRS management is required to make judgements, estimates and assumptions about carrying values of assets and liabilities that are not readily apparent from other sources. The estimates and associated assumptions are based on historical experience and various other factors that are believed to be reasonable under the circumstance, the results of which form the basis of making the judgements. Actual results may differ from these estimates.

The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised if the revision affects both current and future periods.

2. CAPITAL EXPENDITURE

The proposed capital expenditure for 2011/2012 is:

2010/2011 Estimate \$		2011/2012 Estimate \$	2011/2012 LTCCP \$
\$10,000	General office	\$10,000	\$10,000
\$378,100	Plant and equipment	\$296,602	\$226,240
\$540,000	Information technology	\$956,000	\$840,000
\$143,000	Land and Buildings	\$110,000	\$90,000
\$500,000	Flood and river control assets	\$500,000	\$500,000
\$436,500	Vehicles (net of trade-in)	\$655,000	\$265,500
\$2,007,600	Total capital expenditure	\$2,527,602	\$1,931,740

The Council funds its capital expenditure consistent with the *Revenue and Financing Policy*. The Council fully finances all of its operating expenditure. This includes depreciation on all of the Council's assets. The Council's policy is to fund capital expenditure from accumulated cash surpluses arising from the full financing of depreciation. If for any capital project those accumulated operating cash surpluses are insufficient then the considerations outlined in the *Revenue and Financing Policy* will be applied to the project to determine the sources of financing appropriate for that project.

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3. RESERVES

Reserve funds are utilised to provide a fund for expenditure on specific purposes. In some circumstances the reserves are a legal requirement. The Council holds the following reserve funds:

MAKURI RIVER CONTROL SCHEME RESERVE

The Council sets a targeted rate, as and when required, based on land values in the Makuri Valley River catchment. Any surplus rates are transferred to this reserve. The reserve can only be spent on construction and maintenance of river control works on the Makuri Valley River.

2011/2012 Estimate \$	
Opening balance 1 July	940
Transfer from retained earnings	56
Transfer to retained earnings	0
Closing balance 30 June	996

NORTH TARANAKI/WAITARA RIVER CONTROL SCHEME RESERVE

The Council strikes a targeted rate, as and when required, based on capital values over the New Plymouth district. Any surplus rates are transferred to this reserve. The reserve can only be spent on the construction and maintenance of flood control or river control works required for flood protection in the New Plymouth district.

2011/2012 Estimate \$	
Opening balance 1 July	667,553
Transfer from retained earnings	40,053
Transfer to retained earnings	0
Closing balance 30 June	707,606

CONTINGENCY/DISASTER RESERVE

This reserve was created to meet the Council's share of the replacement cost of infrastructure assets affected by natural disasters. It also covers the Council's commitments under the National Civil Defence Plan in the event of emergencies. It is available for any other contingency or emergency response purposes, including oil spill response and flood response.

2011/2012 Estimate \$	
Opening balance 1 July	1,086,000
Transfer from retained earnings	0
Transfer to retained earnings	0
Closing balance 30 June	1,086,000

DIVIDEND EQUALISATION RESERVE

The Council transfers dividends received in excess of budget to this reserve. The reserve is to be used to equalise dividend returns over time. Dividends in excess of budget since 1996/97 have been transferred to the reserve. Prior to 1996/97 all dividends were used to repay debt incurred during the incorporation of Port Taranaki Ltd. From 1996/97 onwards dividends have been used to reduce the general rate requirement.

2011/2012 Estimate \$	
Opening balance 1 July	6,685,462
Transfer from retained earnings	0
Transfer to retained earnings	78,609
Closing balance 30 June	6,606,853

PASSENGER TRANSPORT TARGETED RATE RESERVE

The Council sets a targeted rate, as and when required, based on capital values over the New Plymouth district. Any surplus rates are transferred to this reserve. The reserve can only be spent on funding passenger transport services in the New Plymouth district.

2011/2012 Estimate \$	
Opening balance 1 July	244,089
Transfer from retained earnings	14,645
Transfer to retained earnings	100,000
Closing balance 30 June	158,734

RESERVE MANAGEMENT POLICIES

The Council, in the management of its reserve funds, will apply the following policies:

- the reserve funds will not be matched by specific investments
- transfers to and from reserve funds will be approved by the Council
- interest revenue will be credited to each reserve fund that represents funding from specific sources rather than from the general ratepayer base or from the disposal of assets or investments. The specific reserves that will receive interest revenue are the North Taranaki/Waitara River Control Scheme reserve and the Makuri River Control Scheme reserve
- movements in reserve funds will be reported to the Council as part of the *Monthly Financial Reports*.

4. STATEMENT OF COMPREHENSIVE INCOME

Included in the Statement of comprehensive income, but not separately disclosed, are the following balances:

Year	Depreciation	Employee Benefits
2011/2012	\$1,385,894	\$7,764,906