Submission
No 26

ASSETS, PREMISES AND FUNDING OF THE NSW RURAL FIRE SERVICE

Organisation: Murray River Council

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murray river council

Submission to the NSW Parliamentary Inquiry into Assets, Premises, and Funding of NSW Rural Fire Service

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Foreword

In order to assess the appropriateness of ownership, funding and operational structures, it is important to understand the purpose and core functions of the NSW Rural Fire Service (RFS).

While emergency management organisations (EMOs) undertaking services similar to RFS will usually have the word 'Fire" in the name, in current times, such organisations address a range of incidents well beyond firefighting. Such activities can be broadly categorised as follows:

- Localised Events: one-off incidents such as building fires or accidents.
- Widespread Natural Disasters: such as floods, bushfires and storm events.

Organisations such as the RFS will of course engage not just in responding to such events but also in educational, mitigative and preventative activities related to such events.

The focus of this submission is on an organisation that NSW Inquiry into RFS - Murra River Council Submission designed and geared more for the latter type of events, rather than the former.

Most large cities will have city-based entities that are designed to deal with localised events, generally referred to as fire and rescue services. While such organisations can be linked to municipalities, it is our view that in order to have an effective preparation, mitigation and response to more widespread natural disasters, a different calibre of organisation is required.

While the RFS may attend to localised events as required, the primary purpose and objective of the RFs is to address natural disasters.

Nature of Natural Disasters

If it is accepted that the primary purpose of the RFS is to address natural disasters, then it is also important to have some understanding of the nature of such disasters before attempting to establish the appropriate organisation models and funding and operational structures.

Some elements of natural disasters to be considered:

- Extent of Impact: Natural disasters are rarely limited to local government or municipal boundaries; they almost always cover much larger geographical areas. In a significant number of instances, they cross state boundaries, and in some instances even international boundaries.
- Frequency & Severity: Given changing weather patterns, it is an established fact that the frequency of natural disasters has been increasing in recent time, as has the ferocity and impact of such events.
- Cost Impact: The cost impact, both financial and otherwise of natural disasters are significant and increasing.

It is also pertinent to note that effective disaster management requires significant planning efforts, which in themselves are quite costly. In this context "Planning" is used to encompass:

- Preventive and mitigation activities
- Resourcing, including infrastructure, equipment, and personnel
- Communication & educational activities

Organisational Structure

In order to effectively address its core purpose, EMOs entrusted with the responsibility of addressing natural disasters such as the RFS, must at least have a statewide view. As indicated previously, given that quite often natural disasters cross state boundaries, if the EMOs are based on state boundaries, it is essential that they have an effective federal level (country wide) coordination mechanism while also establishing international relationships.

A state based organisational structure can conjure up images of a top-heavy bureaucracy that is capital city centric. However, this need not be the case. Given that Natural disasters can impact extensive geographical areas, and different areas can have differing impacts and therefore require different planning and response requirements, it is important for the structure of an organisation such as the RFS to have centrally coordinated but devolved decision-making processes.

We believe, the current organisational structure of the RFS which is state based, for the most part is fit for purpose for its mission and objectives. In summary the RFS currently is organisationally structured as follows:

- State-Level Management: led by a Commissioner who reports to the NSW Minister for Police and Emergency Services
- Divisional Structure: 17 divisions, each with a Chair and Delegate who form the State Council
- Branch Structure: branches aligned with Rural Fire Districts. With each brigade appointing delegates to their branch

This structure, at least in theory, allows for both local autonomy and centralized oversight, which is important for an organisation such as the RFS. What is important is that the operation of the organisation balances the top down instructions with the bottom up feedback.

It is also important to note that while the organisation has approximately a thousand (1,000) permanent paid staff, it is also served by over 72,000 volunteers. Emergency response measures require a much larger number of personnel resources than during times of Planning. Given that very dispersed locations that natural disasters can occur, and the limited number of days that concentrated disaster response is required, having a trained volunteer base that can be called up as and when required, enables the RFS to operate in a more cost-effective manner.

Despite the existence of a vast volunteer base, equipment and personnel resources of a state-based EMO can be stretched, especially when responding to natural disasters that can extend over longer periods. As such, as mentioned previously it is extremely important that a federal level coordination and cooperation mechanisms, which enables state level EMOs such as the RFS to call on their state counterparts for assistance. Such cooperation mechanisms as lo becomes a great avenue for information sharing and learning of best practices.

The need for relationships between EMOs internationally is based on the same rationale.

RFS and the SES

When discussing the organisation of disaster management within NSW, one has to also consider the role of the State Emergency Service (SES).

Some questions that need to be addressed include:

- Are the roles of the RFS and the SES that different that two separate organisations are required?
- Will the merger of these two organisations into a single unit, while retaining the local focus maintained by the brigades and branches of the RFS, result in better operational outcomes?
- Will a merger generate financial efficiencies?

Disaster Management Policy

While the major EMOs may be state based, we believe it is of utmost importance that discussion around disaster management policies, including funding models be had at the national/federal level, and where necessary at the National Cabinet, as the premier intergovernmental decision-making forum.

Example: One sector that natural disasters have a significant impact on is insurance. Insurance companies tend to be large organisations operating national and has a significant international component. Any policy decisions around the impact of natural disasters on the affordability of insurance must of necessity made at the national level.

The evolving nature, extend and severity of natural disasters dictate that another crucial element that needs to be addressed at the national level is how disaster management, ongoing preparatory and mitigation activities as well as responses to specific events, are to be funded.

Management & Operations

Despite the devolved nature of the organisational structure of the RFS, it is a specialised organisation of its own, with very specific needs in areas such as infrastructure, and equipment and training. As such it makes no sense for the management and operations of the RFS, and any component of the RFS (e.g. local brigades) to be handled by another party, who will most like not have as specialised knowledge and skill base in emergency management.

We don’t believe any other state organisation has a practice of canning out whole or part of its dispersed operations to other more locally based organisations. For example, would anyone be recommending that the NSW police require local governments to staff and operate the local police stations on behalf of the NSW Police? Why would that be any different for the RFS?

We believe it is imperative that the State use a legal entity (existing or to be created) that has the capability to own the assets required by the Divisions, Branches and Brigades.

Operation and maintenance of the assets (buildings, equipment etc.) used at the local level can be by the Branches and Brigades, while policies and procedures for acquisition, operation, maintenance, renewal, and disposal of the assets can be set ideally at the state level. Needless to say, assets that are shared statewide (e.g. water bombing airborne assets) will need to be operated at the state level.

Such an approach does not exclude the use of locally based organisations, whether they be local government entities or otherwise, for the delivery of selected services on a contracted basis, where it has been determined that the delivery of the specific service can be carried out more effectively or more efficiently (or both) using an outsourced contract.

Such models already exist within state entities and have been used very effectively for quite a while. One such example is the Road Maintenance Council Contract (RMCC) process that is used by Transport for NSW (TfNSW) to maintain its widely dispersed network of state roads. In order to maintain its own road networks, local government by necessity must maintain the required road maintenance and repair resources. It makes sense then for TfNSW to use those resources, on a contracted basis to maintain state roads, as opposed to TfNSW maintaining a series of maintenance crews and resources across the state. However, it would be unusual for TfNSW to use local government resources to build a new road or construct a significant bridge, as such activities are better delivered through more specialised organisations, usually from the private sector.

While having overall responsibility for its own operations and maintenance activities, RFS need to conduct an assessment on whether any elements of its services can be better delivered using outsourced contracts, with local councils or with other NFP or for-profit organisations. It would also make sense to have some level of uniformity on the types of services that are being outsourced and the contractual arrangements under which such outsourcing occurs.

During an emergency event, local government locations, equipment, and personnel, within the areas impacted by the event, can serve as a readily available additional pool of resources that RFS can call on. As such it is obvious that it is in the interest of all parties to maintain good working relationships and lines of communication between the RFS and local government entities. The Local Emergency Management Committees (LEMC) have proven themselves to be an effective vehicle for establishing the required connections.

Operations immediately prior to and during natural disaster events would be well served if there is an established and agreed upon understanding on which elements of the costs related to such activities are borne by the RFS and which by the local government entity.

Funding Arrangements

As indicated previously, we need to have a national level discussion on how we propose to fund ongoing natural disasters, including:

- Preparatory and mitigation efforts,
- Insurance arrangements,
- Specific event responses, and
- Reconstruction post-event

Expectations that local governments have the capacity to fund any sizeable portion of the costs associated with the above listed elements is wishful thinking and will only further deteriorate the precarious financial positions that most local governments find themselves in.

Subject to the proposals made in the section titled "Emergency Management Levy" below, it is our view that expecting local government to fund any significant portion of the funding required for managing natural disasters (including the requirements of RFS), will not serve the purposes of local government entities or that of the RFS. The significance of properly managing, mitigating, and responding to natural disasters cannot be understanded. Such measures require significant investment that is beyond local government entities.

As the Committee may be aware, the House o Representatives' Standing Committee on Regional Development, Infrastructure and Transport has set up an inquiry into the Sustainability of Local Governments. Murray River Council' submission to this committee's inquiry, appearing as Attachment 1, provides further insights into the sustainability pressures faced by local governments and identifies core causes creating those pressures.

Emergency Management Levy

Funding of direct expenses of local brigades is one element of the costs that potentially could be raised through local governments as a collection intermediary. For such a mechanism to be effective, it needs to be structured in a uniform manner as a state mandated "levy", that is outside of the routine general rates. Such a mechanism is in place in Queensland and can be used as a base model to build a process for NSW.

Some aspects that need to be addressed and established for such a levy would include:

- The process for each brigade to establish its budget for the next financial year, and have it endorsed by its Branch or Division.
- Extent (e.g. whole or part) of the budget to be funded by a levy.
- Levy basis (e.g. equal amount by each property, based on property values etc.)

Having the above matters applied uniformly across the state would assist with the understanding of the purpose of the levy by communities that will be contributing the funds. The levy will sit as a separate line item in the Rates Notice, which also helps with the communication process.

The funds collected through such a Levy can be onforwarded by Councils to whatever legal entity that has been established by the state to hold RFS assets, who in turn can disburse the funds to the individual brigades as they require the funding.

Accounting for "Red Fleet" Assets

Given the proposals that we are forwarding through this submission to the Parliamentary committee of inquiry, the matter about local governments accounting for the "red fleet" assets becomes a non-issue. As indicate previously, the state needs to assess and establish a legal entity tat can hold all assets, not just red fleet assets, on behalf of the individual brigades.

The funding mechanisms that are put in place needs to take into consideration the operational, maintenance, renewal, and replacement requirements of all such assets.

However, given the interest that this topic has garnered in recent times, we decided that it was appropriate to address the matter briefly.

During the early stages of the debate on who should be accounting for red fleet assets, the Office of Local Government of NSW (OLG) commissioned Mr. Colin Parker of GAAP Consulting, an accounting and advisory firm based out of Melbourne to conduct a review into the matter and provide a definitive recommendation. The draft report delivered by GAAP Consulting is appended hereto as Attachment 1.

It is interesting to note that GAAP consulting was specifically requested by the OLG not to consult with local government entities in conducting their investigation and compiling their recommendations. The OLG required that the "*draft report first be considered by Treasury, the RFS and the auditor-general before any consultation with the sector*." (page 4), a clear indication that neither the OLG nor those other organisations are committed to a transparent process in dealing with this matter.

The draft report among a host of other observations arrives at the following conclusions (page 24):

> *96. Users of not-for-profit financial statements are concerned with the ability of an entity to achieve its objectives, both financial and non-financial. Financial statements should show the results of the stewardship of management for the resources entrusted to it.*
>
> *97. The current accounting for fire-fighting equipment fails the information needs of the RFS's and councils' financial-statement users as the equipment has failed to be recognised by the entity that controls its potential to meet its objectives.*
>
> *98. In my opinion, fire-fighting equipment is controlled by the RFS as determined by application of accounting standards and the framework according to the facts and circumstances described.*
>
> *99. Recognition of fire-fighting equipment by the RFS in its financial statements, and derecognition by the councils from theirs, also satisfies the definition of an asset and qualitative characteristics of financial statements, including faithful representation and substance over form.*

The draft report was never required to be finalised and was not voluntarily released. It required a request for information under the Government Information (Public Access) Act 2009 (GIPA) by Local Government NSW to obtain the report.

Given the credentials of Mr. Colin Parker (see page 2 for a summary of credentials) and the contents of the draft report, we don’t believe any further statements need to be made on the manner in which the red fleet needs to be accounted for under current arrangements.

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Attachment 1 - Murray River Council's submission to the House of Representatives Standing Committee on Regional Development, Infrastructure and Transport inquiry into Local Government Sustainability

- *The financial sustainability and funding of local government*

(1) Cost shifting.

Successive State and Federal governments over an extended period have reduced or removed services (economic rationalism), despite the fact that services were still required. This encouraged disaffected and desperate councils to delve into non-core businesses to make up shortfalls. Often with mixed success.

Subsidises related to services for aged accommodation, medical, early childcare/education, youth, and community transport – which assist to maintain the social fabric of communities – have become commonplace on council's balance sheets.

Those with a more astute knowledge of local government may suggest that as these are peripheral type services why don't councils simply charge at cost-plus? I put it to the Standing Committee that the State or Federal Government wouldn't have walked away and passed the responsibilities onto councils, by default, if the fees were able to be recovered in the first instance.

Secondly, if there was a dividend to be made private enterprise would already be supplying the service and neither the federal, state, or local government would have originally needed to step in. Add the tyranny of distance found in country areas, and even more community pressure is placed on local government to fill the gaps after abandonment by the other two tiers of government.

The NSW Local Government Association recently published a report on cost shifting which tabled the amount at $460 per rate assessment. Providing the aforementioned (non-traditional) services wouldn't be so challenging, if at the onset, local government was given the financial powers to raise revenue to offset the expenses. Almost always the cost is shifted without the provision of ways of increasing the income.

(2) Federal Assistance Grants (FAGs).

In addition to the reduction of services, which in effect, is cost shifting (now named 'risk shedding' by some executives in federal government bureaucracies), the percentage of the Federal Assistance Grants (FAGs) is now a little over half a percent. (FAGs have declined from one per cent of federal taxation revenue in 1996 to just 0.5 per cent in 2024.) Whilst it doesn't seem significant, it is. Murray River Council's FAG is circa $10.8 million. If the FAG were raised to 1% the extra income would be a further $10.8 M.

(3) Legislative obligations.

The NSW Local Government Act in 1919 was 344 pages long. The Act, as it stands now, is 749 pages long, excluding Schedules. There is a true and genuine cost to comply with twice as many legal requirements. This is a point not often acknowledged by those introducing the never-ending stream of amendments. What was once the domain of the old 'Shire Clerk' (pre-1993 Act) is now far too onerous for a General Manager/CEO alone to keep abreast of and manage. Some larger councils now employ qualified legal counsels by necessity. As does Murray River Council.

There are many other legislative examples of increases in responsibilities harboured by councils, a few of which are as follows: Crown Lands, Internal Audit & Risk Committee (changes in costs), membership of Joint Organisations (previously Regional Organsations of Councils: free), pensioner rebates etc.

(4) Rate Capping

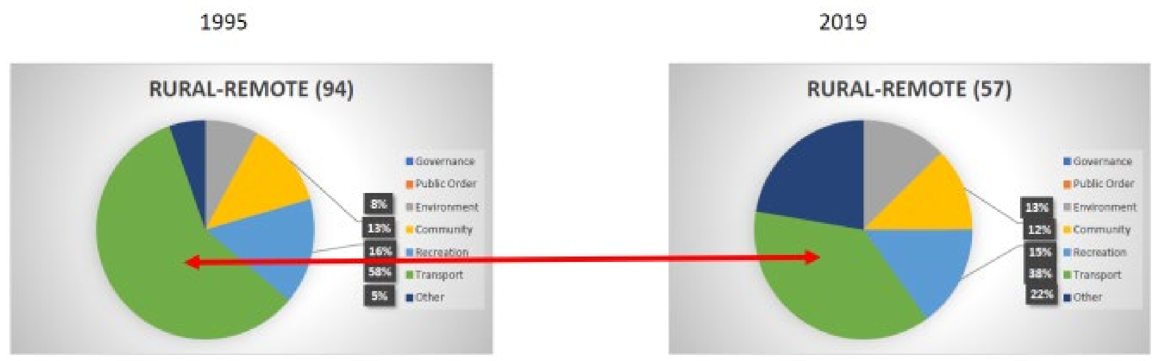
While NSW had employed a form of rate-pegging between 1901and 1952, which was discontinued due to its ' impracticality', the genesis of the modern method of rate-pegging may be found in the 1976 state election campaign. Under the Local Government (Rating) Further Amendment Bill, an interim type of rate-pegging was re-introduced by the victorious Wran Labor Government in 1977 and further refined into its contemporary form in 1978.

Whilst rate pegging achieved some of what it was initially designed to do, historically except for few occasions, the cap was set below inflation. There is a limit to how often, and by what quantum, government-imposed *efficiency dividends* can fund the difference between the rates cap and increases in councils' expenditure (caused by inflation).

Often this limit is measured by a rise in the infrastructure backlogs!

Subsequently, given the removal of services by other governments (a), the halving of FAGs (b), the more onerous compliance requirements (c), and the gap between rates caps and inflation (d), there is little wonder that rural or remote councils, over the last thirty years, have balanced budgets by reducing their largest expense: transportation (roads).

The following pie chart indicates this exactly. In 1995 rural or remote councils spent 58% of their budgets on transportation. Yet in 2019 that had reduced to 38%. Murray River Council spends 34% of our budget on transportation.



Yet the amount expended on 'other,' and 'environment,' has risen from 13 to 35% - with 'other' having the biggest increase (5 to 22%).

Council contacted the ex-President of the NSW Institute of Public Works Australasia (IPWEA) who provided council with a startling figure confirming the ubiquitous use of transport budgets to maintain solvency. The NSW Roads and Transport Directorate recently published a report tabling that the annual shortfall on transportation expenditure in the ninety-four (94) regional and outer metro council areas in NSW was $681 million. It can (and has) been argued that councils should use the Special Rates Variation (SRV) provisions to negate continually reducing their 'biggest bucket' (transportation budget) to balance their ledger.

This may be technically true. But if the system of financial governance weren't so broken, firstly, there wouldn't be a requirement to spend even more money to go through the SRV process, and secondly, the applications (as a percentage increase in rates) applied for by councils to IPART for wouldn't be so huge.

There have been at least three 'investigations' into local government sustainability in the last thirty years. **But there have been countless scholarly papers written about financial and infrastructure issues within local government (see appendix)**. Council found twenty in a quick Google search, there were many more webcasts, YouTube videos and other media on the subject.

This begs some questions…

Question one. If there have been dozens (if not hundreds) of scholarly investigations and well-regarded papers, webcasts, or video clips produced already, with little action by any government, why do another?

Why not just review and combine the points of the top 20 or 30 articles? Technology certainly has changed in the last 31 years, but the sustainability problem hasn't, nor has the lack of political will and the ability to remain in denial.

Question two. Or is the answer the government is seeking at odds with what a great many (quite esteemed) academics and practitioners recommended?

It has become the norm for councils to intricately assess Terms of Reference, and subsequently recommended actions, of (especially State) government, as frankly, the level of trust is almost zero.

Many in local government become despondent and stop listening at speeches by Ministers at events when the words, "collaborative, collegial, cooperative, or partnership," are used, knowing full well that they are superficial.

Question three. Is the new study designed to ensure <u>proper</u> consultation with councils?

A non-cynical observer may say that the government wants to consult properly with the industry. That would be fabulous. Recent history (early April 2024) shows that suggestion to be almost laughable, as councils discovered about the new tax on internment (cemeteries).

Councils didn't hear it from the government, we heard about it by reading a press release from the NSW Local Government Association. Less than a month ago, again without any consultation, changes were made regarding waste management, not only without consulting councils, but not speaking to waste industry providers either.

LG Grants Commission Report (1977)

- the property tax is an inadequate source of revenue to meet all the demands to provide services that extend far beyond those relating to property
- increasing trend for communities to look to their councils to provide a range of social, cultural and recreational services that are far in excess of what a rate on land can support
- Government foreshadowed intention to pay rates on certain crown lands
- introduced per capita component to ensure all councils received FAG (min 30%)

Inquiry into the Financial Sustainability of NSW Local Government (2006)

- relationship with higher tiers of government
- huge backlog in infrastructure renewals
- devolved government social and environment agenda
  - no or low $ recompense (cost shifting)
- expectations of higher standards of service, and public assets, that people increasingly demand of their councils
  - retirees moving to coastal and inland regional centres
  - sea- and tree-changers used to city standards
- maintaining existing service commitments, yet manage huge infrastructure bill
- rural councils will only survive with increased grant funding
- constraints on rate income
- restoring public faith in the development control process
- overcoming skills shortages
- greater resource sharing
- tools such as performance benchmarking

In reviewing the table above, it seems obvious that the government of the day cherry-picked the recommendations. The only two that have been implemented involved local government doing all the heavy lifting. Greater resource sharing evolved into the forcing of councils to join (and pay for) Joint Organisations, and now we benchmark.

In addition to the two-enquiries summarised in the above table, there was the Local Government Boundaries Commission investigation (circa 2016). Amalgamations were going to solve everything. The savings never eventuated, as the tyranny of distance wasn't taken into consideration at worst, or at best, the savings were less than the travel-time-distance-costs incurred over larger footprints.

The QLD experience with amalgamations resulted in the same. (Many in local government, and at least one esteemed academic, would say it achieved quite a few objectives of the State governments though.)

In addressing the first dot point provided by *The House of Representatives Standing Committee*, it gets down to basics and <u>remarkably simple</u> mathematics.

A council's income must be adequate to maintain services and fund asset consumption (in the form of depreciation). Most councils cash position indicates that services aren't their main issue, it's their ability to maintain infrastructure assets that they fail with.

Putting cynical observations, a predicable lack of genuine consultation, previous inaction after investigations, the disregard of scholarly papers aside, optimists within local government hope the new NSW Government with a new Minister (who is very experienced in councils) will listen – and not cherry pick findings to suit pollical agendas.

Unless government introduces a <u>genuine</u> financial mechanism for <u>incremental</u> and <u>ongoing</u> maintenance leading to financial sustainability, the time authors took in responding to the House of Representatives Standing Committee, will be valueless.

- *The changing infrastructure and service delivery obligations of local government*

(5) The dilemma of the 'Modern Standard Equivalent (MSE).'

Every time there is an accident that precipitates a change in a code or national standard, or there is a technological breakthrough, or anything that causes obsolescence, whatever the improvement is will inevitably cost more.

Whether it be the BASIX requirement for new buildings (now up to iteration number 5), or the width of new bridges, or specifications for pedestrian and cycle paths etc, not only does the initial cost rise, but the new assets also get added to the register at the higher capital value.

(6) Flawed depreciation model.

The methodology used to calculate depreciation is fundamentally flawed.

General purpose financial statements for both commercial entities and local government councils determine depreciation expenses in accordance and compliance with AASB 116.

AASB 116

Depreciation is the systematic allocation of the depreciable amount of an asset over its useful life.

Depreciable amount is the cost of an asset, or other amount substituted for cost, less its residual value.

Depreciation can be described/explained as follows:

"Depreciation is a planned, gradual reduction in the recorded value of an asset over its useful life by charging it to expense. Depreciation is applied to fixed assets, which generally experience a loss in their utility over multiple years. The use of depreciation is intended to spread expense recognition over the period of time when a business expects to earn revenue from the use of the asset."

It is also accepted that in commercial environment depreciation expenses are integral in determining the profit distribution through dividends.

In view of the above and from a practical perspective there are stark and fundamental differences between the relevance of depreciation expenses in a commercial environment as compared with a local government council.

In a council environment:

- There is no distribution of profits.
- Most Council assets are not intended to generate and/or maximise revenue.
- Numerous assets are externally funded (partially or fully) through grants and contributions.
- Some councils have brought to account and depreciated assets which they neither own nor control, nor have any financial obligations for asset maintenance or replacement (e.g. Rural Fire Service 'Red Fleet' assets).
- Arguments persist that certain asset categories e.g., roads, do not lose value should maintenance be adequate.
- Assets of council are subject to rapidly changing demographics, global trends, changes in Community Strategic Plans, legislation, and technology.
- In some cases, council determines that assets will not be replaced at the end of their useful life e.g., community halls due to changing demographics, community expectations etc.

Consequently, it is apparent that depreciation expenses as defined by Australian Accounting Standards and adhered to by commercial entities are not necessarily compatible nor applicable for local government assets.

<u>This situation was recognised as far back as 1922</u> when a Committee of Enquiry into Local Government Accounts stated:

"In Local Government Accounts a charge for depreciation means a provision for replacements. What local government bodies are concerned with are the cash and funds available for expenditure, so that unless depreciation written off is actually set aside in a special bank account no advantage is gained by writing it off."

This statement has some relevance today – "*depreciation means a provision for replacement."*

For the reasons enunciated earlier most councils' assets have been externally funded (partially or fully) through grants and contributions (roads/sewerage/water) and council will never be in a position, nor expected, to fully fund these assets when they are fully depreciated.

Additionally, some assets will never be replaced and 'assets' such as Rural Fire Service ('Red Fleet') are required to be depreciated even though Council has neither control nor obligation to fund nor replace. These factors are unique to local government and need to be accounted for as such.

This situation was recognised and addressed by the NSW Local Government Electricity County Councils in the late 1980's when their financial statements (audited by the NSW Audit Office) **effectively only depreciated the equity** that County Councils had contributed to the asset. This was achieved by amortising capital grants and contributions against the annual depreciation expenses.

Based on the NSW Local Government figures for year ended 2019/20 the State average for depreciation expenses as a percentage of Opex was 20.8% with significant variances between regions, particularly between rural and urban councils.

Sydney Central had the lowest Depreciation % to Opex (14.4%) whilst the Murray region % was the highest (29.9%).

Councils with highest depreciation as a % of Opex

- Liverpool Plains Shire Council 41.2%
- Carrathool Shire Council 36.6%
- Bland Shire Council 36.1%
- Balranald Shire Council 34.3%
- Lockhart Shire Council 34.0%

Councils with lowest depreciation as a % of Opex

- Council of the City of Ryde 8.9%
- Waverley Council 10.82%
- The Municipality of Kiama 11.96%
- Penrith City Council 12.04%
- Inner West Council 12.12%

It is no coincidence that the councils with the highest depreciation percentage to Opex are generally rural councils with extensive road networks.

Councils' depreciation expenses are of course made up from a series of different asset classes however in most cases road depreciation is often the largest single component and largely responsible for the considerable variances as illustrated.

Obviously then, one size doesn't fit all, yet no allowance is made for these depreciation variances when important ratios such as the Operating Performance Ratio are prepared.

No figure in local government financial statements is subject to greater uncertainty and variability than roads depreciation which is constantly subject to climate events (excessive rainfall/flooding etc), road transport regulations, grant funding, condition assessments etc. thereby making it potentially a most unreliable and misleading figure.

Added to this depreciation scenario is the fact that many other assets of council are subject to vastly different factors than those of a commercial entity.

This then begs the question. Why are all Council assets depreciated 100% based on cost or revalued amount when council has not financed (nor expected to have financed) the full cost of the asset?

Is there a better way?

As councils' financial statements are prepared in accordance with Australian Accounting Standards there is no scope for amendments to the depreciation expense as disclosed in the Operating Statement. Amendments can be made to the Statement of Performance Measures (Notes G5 & H) and in particular the Operating Performance Ratio.

Councils Operating Performance Ratios have been steadily decreasing over the past few years; with many councils reporting a negative %.

In the fiscal year ended 2020/21 the majority of NSW Councils (67) reported a negative operating performance ratio. This situation must be addressed as it is not truly reflective of performance.

It should be noted that with some exceptions councils' Special Schedules (7) report that most councils assets are rated satisfactory or better and only require continued maintenance work. Based on a limited sample many councils report less than 10% of their assets as requiring renewal.

Given these scenarios consideration be given to the following options:

1 Eliminate all depreciation expenses from the calculation of the operating performance ratio: OR,

2 Eliminate roads depreciation expenses and depreciation expenses applicable to asset equity funded from grants and contributions from the calculation of the operating performance ratio.

(7) The Stockholm Syndrome.

The average reliance on grant income in the category of councils that Murray River Council is defined in is circa 44%. Due to the inability to match expenses with income, almost all rural councils become dependent on grant income.

This dependency, year in, year out, of which a sizeable percentage isn't predicable (with the exception of some Federal grants), means that to survive councils are coerced to succumb to the will of whatever the 'captor' wishes – be it good, bad or indifferent.

Mostly it's good, at least for those assets that are on the 10-year Financial Plan or sorely needed by communities. This is especially the case with large and expensive upgrades to water filtration or sewerage treatment plants, or the provision of any infrastructure related to rapid population growth.

But preceding elections past governments have circumvented councils and offered *trinkets* and *bags of silver* directly to community groups, sporting clubs, and associations. All of which are housed on either crown land, or council owned operational land, on which council is the asset custodian (read: responsible for ongoing maintenance and depreciation).

As the government directly approaches these groups, councils have no say in the additional maintenance and depreciation expenses. Moreover, councils then get the task of delivering of the project – under the stringent procurement protocols not usually taken into consideration by the community (applicant) – which often means either a reduction in scope is required, or a cost overrun occurs. As an election is usually imminent, time constraints inevitably become an issue.

Any council which refuses to supply a letter of support to the community groups' grant application will quickly bring anger upon themselves.

(8) Small grants.

To administer a $50,000 project (SCCF - the Stronger Country Communities Fund minimum amount) often costs the same or more in staff time as administration of a $500,000 project. As multiple small value grants, strewn across a large geographical electorate, take up significantly more staff time than a larger value project in one location.

The impost and risk can quickly multiply, as the vast majority of low-cost projects are overseen by staff usually employed in community services, and mostly at a 'junior officer' level. This is because the charge-out rate for highly remunerated project mangers in a council, which may even be external contractors (even more expensive), would quickly consume the 10% project management allowance linked to the small grant.

Secondly, a Project Management Office (PMO) usually has the responsibility of delivering multimillion-dollar projects, which often span more than a year, which are also grant funded, and therefore on their own grant induced timeline.

If the real administration and acquittal costs weren't carried by a council, many smaller projects wouldn't be delivered.

The SCCF grant allowance for project administration was only 10%. Most PMOs in councils have an internal client charge out rate of 15%. But losing 5% wasn't the biggest issue, risk, and expense. Nor is the lack of highly remunerated, and otherwise engaged, professional project managers.

The onerous and costly requirement to effectively duplicate community consultation (already done as part of the Community Strategic Plan in all councils) and further the community development was not recognised as part of SCCF. This was the Black Hole councils were forced into.

These pre-election State Government inducements fly in the face of The Act, as councils spend an enormous amount of time and money to complete their Community Strategic Plan after each local government election to comply with the Integrated Planning and Reporting (IP&R) requirements of The Act.

Capital expenditure, ongoing maintenance, and depreciation expenses form part of the IP&R framework (The Act), in the form of having a 10-Year Financial Plan, 4 Year Delivery Plan and 1 Year Operational Plan.

The arbitrary additions (inducements) once per election cycle – begs the question why The LG Act forces councils to spend so much time and money on astute financial planning, community consultation (during the development of the Community Strategic Plan), reducing planned maintenance, and depreciation management.

(9) Grant application complexity.

The time taken to apply for the grants has become <u>much</u> more onerous. As the complexity and amount of information sought must be in concert with the latest guidelines on how to stop *Pork Barrelling* occurring (again).

Most medium sized rural councils now employ, by absolute (financial) necessity, a professional Grants Officer. This was unheard of ten years ago, and only has become commonplace in the last five or so years. The need to employ a Grants Officer, or contract it out, has created a new profession, as each year passes the skills become more finely honed and specific to local government.

Judging by recent experience, the *Pork Barrelling* continues. This is both predictable and unfortunate, as it's how our whole electoral system is designed. Each Opposition castigates the previous Government for Pork Barrelling, then changes to grant criteria and assessment inevitably occurs, which drives the increase in sophistication and need for specialist staff.

This in-turn then equates to increases in the cost to apply for grants, and a greater disappointment when reading the rationale as to why the grant application was unsuccessful.

(There is some irony though with the increase of sophistication of grant criteria. The challenge to the bureaucrats tasked with writing the *Dear John* letter is also far greater, as it's much harder for them to produce believable excuses on why a council missed out when the criteria was so eruditely met.)

(10) Timing of grant notifications.

Every year councils have their budgets on display for 28 days prior to adoption, which usually occurs in late May or June. The budgeting process takes months. Often, a state government knows they'll be a fiscal impact on councils well in advance (in recent memory prior to a state government election) but remain silent on their plans that will financially impact councils until just prior, or sometimes even after, councils have adopted their budget. This sleight of hand is never well received and causes stalwarts to lose trust very quickly.

(11) The cookie cutter approach.

States are as geographically diverse as they are large. The more removed from metro areas, the more bespoke infrastructure development and delivery needs to become based on these simple facts.

Due to many capacity and assessment constraints by the grant providers, often it is difficult for bureaucrats and Ministers alike to comprehend local factors. Or even if they do, have the capacity to adjust accordingly.

Worse still, recently council has observed that the grant criteria have been so focused on 'metro' that for a regional applicant the level of scrutiny is unrealistic, as are some assumptions that has led the government to think everything is fair and just. (Those Pork Barrells being specified in advance.)

To create economies of scope and scale, a one-size fits all grant criteria is usually the standard fare. This makes it extremely difficult for administrators/acquitters of the grants when there are time constraints caused by local circumstances. Or worse, a natural disaster.

(12) Announcement delays.

It is very frustrating for councils to be given a strict grant application due date, or else risk missing funding opportunities, only for the announcement of success to be delayed ensuring alignment with a bad news day or linked to an election announcement (usually a visit).

A delay by the grant provider often doesn't align with the acquittal date being pushed back by a pro-rata amount. This is especially the case pre-elections. This increases cost, as the *time, cost and quality triangle* must be in equilibrium. (To decrease time increases cost or reduces quality – the rule of project delivery.)

- *Any structural impediments to security for local government workers and infrastructure and service delivery*

(13) The first two budget casualties.

Councils that struggle to align budgets, which is every rural council, look at what expenses can be cut in their immediate budget.

- The first casualty of fiscal constraint is succession planning.
- The second casualty is strategic planning.

(The two die from different afflictions though.)

Has anyone in government every wondered why the supply of specialists within local government is so low, the demand so high - with the consultant fees to match?

What we sow we reap. It takes years to train a Building Surveyor, a Town Planner, a Water Filtration Plant Operator or Water Engineer, a Chief Financial Officer, a Ranger, or an Environmental Health Officer (and many more).

Although some of the skills and experiences are transferable from *private* to *public*, many are not. The guilds have become more local government orientated as The Act became more prescriptive.

Up until about the time economic rationalists convinced the world the economy would provide solutions for every demand generated, all tiers of governments were the incubators for almost every trade and guild. There was an extended period, in councils and state government departments, where meeting a Trainee was rare. Even in those councils with a large number of staff, the ratio of trainees in a workforce, compared to circa the mid-eighties (1985) was exceptionally low. As an industry, we're now paying for our financial inability to succession plan.

While councils continue surviving *hand-to-mouth*, the capacity to *grow your own* talent will always be a struggle. It's easy to not employ someone versus make someone else redundant. Faced with financial Armageddon, councils inexorably cut 'future' versus the 'current.'

In 2004, Planning Institute Australia brought the issue of lack of Town Planners to a head in their report titled National Inquiry into Planning Education and Employment.

In 2007 there was a plea from our Association, who articulated there was a problem with the number of Town Planners the industry was attracting and retaining.

In 2022 Local Government Workforce Skills and Capability Survey New South Wales Report was prepared for the Australian Local Government Association.

There have been other investigations and reports.

The root cause of the problems is many. Of the reports council has reviewed little has been articulated regards one of the main issue – the financial capacity to fund succession. All councils know that because many occupations we employ are so specialised we must develop our own workforce.

It's a shame that the financial asphyxiation applied to local government has now caused our costs to rise and services to reduce. It's **somewhat ironic**, as the reason rates pegging was introduced was to curb council expenditure, not coerce costs to rise!

(14) The death of strategic planning.

The second casualty in council budget sacrifices is strategic planning. This is just as much of an issue as a lack of succession planning. The difference is the industry pays for a lack of succession planning in years to come (which is now).

When human capacity constraints take effect, with things like employment freezes, the Executive (Directors) and Managers inevitably spend more time fighting fires (operational arena) than planning for the future (strategy).

The number one risk facing Murray River Council was caused by the Executive not having the time to work on 'tomorrow's requirements.' In reflection, many councils suffer or suffered the same fate. The risk caused by not spending time and money on strategy is usually related to large and expensive assets with a slow consumption rate or a slow and incremental decrease in production, such as water filtration plants, sewerage treatment works, arterial roads, water supply reservoirs, dam walls, and the biggest Achilles heel of them all: bridges.

- ## *Trends in the attraction and retention of a skilled workforce in the local government sector, including impacts of labour hire practices.*

(15) If you fail to plan, you plan to fail.

There have been many changes in where and who is targeted in attracting staff to regional or rural councils, and how we retain staff, only some of which was caused by COVID.

COVID certainly didn't assist but by no means the only driver. It did cause people to reassess their life goals, with much being written about 'The Great Resignation' by others.

As well as people changing their views about work-life-balance, often choosing life over work, other forces have been at play. Bernard Salt has cleverly dubbed the exodus to regional areas as 'VESPA's,' being 'Virus Escapees Seeking Provincial Australia.'

To some extent VESPAs initially rang true and helped Murray River Council. We did employ staff looking to escape Melbourne and Sydney, but not as many as industries whose staff could easily work from home (WFH).

In summary:

- ➢ The drivers seem to have changed to those seeking to escape from the economic reality of a million-dollar mortgage in a city. But even so, those seeking a tree change are more at the higher end of the remuneration scale than lower or middle. This can be particularly attractive to individuals and families looking to own property or upgrade to a larger home without the excessive costs associated with city living.

- Regional areas often offer a lower cost of living compared to major cities like Melbourne. This isn't just lower housing costs, there are reduced transportation expenses, and more affordable amenities, which may attract individuals looking to stretch their budget further.
- Improved Work-Life Balance: Regional centres often offer a slower pace of life and less congestion compared to cities like Melbourne. This can result in a better work-life balance, with more time available for leisure activities, family, and personal pursuits.
- Employment Opportunities: Some regional centres may have specific job opportunities that are not as readily available in major cities. This could be due to industries that are prominent in certain regions, such as agriculture and tourism in the Murray region, which may offer unique employment prospects.

  Commute Times: Working in Murray River Council means shorter commute times compared to navigating the traffic and congestion typical of major cities like Melbourne. This can result in less stress and a better quality of life for individuals who value proximity to their workplace.
- Community and Lifestyle: Regional centres often offer a strong sense of community and a more relaxed lifestyle, which can be appealing to individuals seeking a closer connection to their neighbours and surroundings. This can include access to nature, recreational activities, and cultural events. When asked, many of Murray River Council's staff say that was one of the reasons they moved here.
- Career Progression: In some cases, individuals may find that career progression opportunities are more accessible in regional centres, particularly if there is less competition for positions or a greater demand for skilled workers in specific industries.
- In small to medium sized rural council, you're not a 'number.' You don't get lost in a huge organisational hierarchical chart. It's both necessary for the organisation's survival, and fortuitous for staff who wish to extend their CV, for staff to learn more than a narrow Position Description would describe in a large organisation. For those with motivation, they can learn skills many times faster and much more broadly than metro councils.

Overall, the decision to leave a city like Melbourne and relocate to a regional centre for work can be influenced by a combination of the above factors, as well as personal preferences and individual circumstances.

- What is a challenge though, is that the staff from metro areas, especially those in large councils or private enterprise, expect the same or more in remuneration when making a tree change.

- The same can be said when our younger staff, who traditionally arrive just after finishing their degree or get funded by council in their degree, who see city counterparts earing 25-40% more than regional councils can offer. As the pool of talent shrinks, there has been a couple of younger staff leave Murray River Council due to being offered much more than their skill set and experience traditionally suggested.

- Overall, the cost for staff in more home-grown and or specialist positions has dramatically increased over the last three years.

- ## *The role of the Australian Government in addressing issues raised in relation to the above*

(16) Stacked committees.

To seasoned bureaucrats and politicians alike this submission will appear quite blunt. This was deliberate.

It saddened me in reading many reports from inquiries and scholarly articles written over the last thirty years (30), watching videos or listening to pod casts, and then reflecting on the number of National and State Conventions (local government) I attended only to conclude councils aren't any better off than when I received my first executive role in 1996.

History has shown the industry, quite clearly over many different governments of all political persuasions at all levels, that local government is almost held in contempt.

I argue that this is the case because of the huge volume of information and evidence provided by highly respected and qualified people – also of all political ilk – that hasn't been acted upon.

Except for amalgamations (which suited the government of the day), little attention has been made to what everyone knows and has been saying for at least twenty years. Local government hasn't the levers to use to raise enough funds, in a timely manner, to be sustainable.

The number one thing both the Federal, but especially the State (NSW) Government, <u>MUST</u> do is restore trust between local and state governments.

Too many times has local government, partly due to not being recognised in the constitution and being powerless, been the recipient of sleights of hand. (It's happened three times to Murray River Council in less than a month.)

All the scholarly papers, the parliamentary reviews, the networking at conferences, will mean nothing if behaviour and attitude of politicians and senior bureaucrats towards local government remains as it is today.

One avenue that may assist to bring faith and trust back would be to set up a panel **completely independent of the government** (read: not IPART) populated by respected people beyond reproach, such as retired judges.

This panel would report on the action (or inaction) of the government, including the views of local government if (read: when) there is a lack of consensus between Federal and State with Local Government.

Too many times, based on who holds 'the numbers,' recommendations have been crafted to suit political colours or cheery picked to appeal to popular opinion (and votes).

- *Other relevant issues.*

(17) Sitting on reports.

There have been many investigations and reports that have been suppressed and sat in Ministers' offices because they weren't aligned with the government of the days' previous statements, objectives, or promises. Local government hasn't been immune to this charade.

Somehow, which will be an enormous challenge and possibly a first in our country, there must be a methodology that cannot be interfered with when the report is nearing completion or completed, that ensures it sees daylight.

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Submission to NSW Parliamentary
Inquiry into RFS

murray river council

Attachment 2 - Review of accounting for 'red truck' assets and other fire-fighting equipment in NSW: An independent expert's report by Colin Parker, Principal, GAAP Consulting

GAAP Consulting

Review of accounting for ‘red truck’ assets and other fire-fighting equipment in NSW

An independent expert’s report

by

Colin Parker, principal, *GAAP Consulting*

Team leader – advisory and litigation support services

Former member of the Australian Accounting Standards Board

April 2018

GAAP Consulting

About the author – Colin Parker, principal, *GAAP Consulting*

I have had over 40 years' experience in financial reporting, auditing and ethics policy and implementation, including as director – accounting and auditing with CPA Australia, member of the Australian Accounting Standards Board, chairman of the Audit Advisory Committee to the board of CA ANZ, and as an adviser to the IPA on all aspects of professional standards.

I lead *GAAP Consulting*'s advisory and litigation team and have been involved in more than 40 litigation briefs as either an independent or consulting expert.

I have a public profile on emerging accounting and auditing issues, having given more than 300 talks, speeches and seminars in Australia and overseas (Singapore, Hong Kong, United Kingdom, Kuala Lumpur, Fiji and Dubai).

I have written many technical articles for CPA Australia and other bodies, numbering well over 200. I made contributions on contemporary issues to *Acuity* and the *Public Accountant*.

I am co-author of *Understanding and Implementing the Reduced Disclosure Regime* (two editions), co-authored *Australian GAAP* (nine editions). I was technical editor of the accounting bodies' *The Accounting and Auditing Handbook 1992-2001 (Volumes 1 & 2)* (10 editions).

I am editor of the monthly newsletter *GAAP Alert* and tweet and post on contemporary issues. I am also editor of the *GAAP Consulting* publications *Special GAAP Report* and *NFP Risks and Compliance* newsletter and a major contributor to the *Report Fraud and NOCLAR* newsletter.

About *GAAP Consulting*

On 1 July 2003, I founded *GAAP Consulting* with a vision and a motto. The motto was easy: *Excellence in financial reporting*. The vision was to give the best, independent advice on all matters to do with financial reporting, auditing and ethics.

GAAP Consulting provides independent financial reporting, auditing, ethics, and risk management solutions to reduce clients' risks. A description of my services, clients and information products is available at www.gaap.com.au. The expanding arch in the logo represents the client's journey from uncertainty to a sure solution through the use of my consulting services and products.

My core values are independence and integrity, and with my motto are reflected in the mnemonic:

T Trust
R Respect
I Innovate
E Energise
D Deliver
and PROVEN approach.

As principal of *GAAP Consulting*, I provide expert advice on GAAP and GAAS, quality-assurance reviews, representation expertise, tailored training courses, and litigation support to meet client needs.

Where appropriate, *GAAP Consulting* uses the services of a network of independent colleagues (subcontractors) to assist with engagements. My colleagues are *all partner-equivalents*.

The *GAAP Consulting* network members and their areas of expertise are:

- Colin Parker (financial reporting, audit, ethics, and risk management)
- Carmen Ridley (financial reporting and a current member of the AASB))
- Stephen LaGreca (financial reporting, audit, and risk management)
- Sonya Sinclair (audit, risk management, and financial reporting)
- Jim Dixon (public and not-for-profit sectors)
- Andrew Parker (marketing and event management), and
- Stephen Downes (client communications).

I also use the services of Stephen Newman, corporate lawyer, Hope Earle, when matters have a legal aspect.

My business model is premised on using only known names and very experienced practitioners in financial reporting, ethics and auditing. Collectively, a unique blend of skills and experience is provided to meet clients' needs.

As a boutique consultancy, *GAAP Consulting* has an impressive list of clients in the private and public sectors to which a wide variety of GAAP, GAAS and training services are provided. My clients include legal firms, regulators, accounting firms, listed entities, and public sector and not-for-profit entities.

About this report

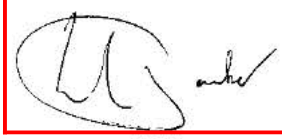
This report has been prepared on the basis of the information sources cited and a brief discussion with Stephen O'Malley, executive director, finance and executive services, chief financial officer, NSW Rural Fire Service. The New South Wales Office of Local Government (OLG) and Treasury provided preliminary input for an earlier draft.

Apart from the preceding, I have yet to hold interviews with key stakeholders, including relevant councils. The OLG has requested that my draft report first be considered by Treasury, the RFS and the auditor-general before any consultation with the sector.

The report has been subject to internal consultation with my quality-assurance reviewer Stephen La Greca and a blind review by Carmen Ridley.

The opinions expressed in this report are my own.

I trust that the report will be a helpful discussion document for all major stakeholders. I welcome feedback to progress its finalisation.



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11 April 2018

Executive summary

Introduction

1. Fire-fighting equipment provided by the Rural Fire Service (RFS) to local councils in New South Wales has been a vexed issue for many years. Who controls the assets – the RFS or the councils? This has not an easy question for stakeholders to answer due to factors such as:

- The legislative requirements and obligations of the RFS and councils, including the vesting of fire-fighting equipment with councils
- The choice of accounting under Office of Local Government (OLG) accounting code for local councils and their auditors to consider
- Long standing practices of the RSF and councils
- The effect of RFS service standards mandated for fire-fighting equipment (and its use) and rural fire district service agreements between the RFS and the councils
- The differing perceptions of control for red-fleet vehicles vis-a-vis associated land and buildings by the councils, and
- The lack of specific accounting standards addressing the control of an asset.

2. Under s119(1) of the *Rural Fires Act 1997*, fire-fighting equipment is defined as: *fire-fighting apparatus, buildings, water storage towers or lookout towers*. Fire-fighting apparatus is defined separately as: *all vehicles, equipment and other things used for or in connection with the prevention or suppression of fire or the protection of life or property in case of fire*.

3. There has been inconsistent treatment, as councils have been given the choice (in the OLG accounting code) to recognise or not to recognise fire-fighting equipment assets, but with the intention that this decision would be made in accordance with accounting standards, including the application of materiality. The RFS has not recognised fire-fighting equipment as an asset in its financial statements on the basis that these assets are vested with the councils as stated in the RFS's accounting policy note to the financial statements.

4. With the extension of the auditor-general's mandate to cover local government, she is seeking to ensure an appropriate treatment.

5. Stakeholders' positions vary. The NSW Audit Office, NSW Treasury, and RFS are of the view that councils should recognise fire-fighting equipment in their financial statements *primarily* based on the fire-fighting equipment *vesting* in the councils under the Act.

6. On the other hand, many councils believe that they do not *control* fire-fighting equipment and, therefore, should not recognise them in their financial statements. Furthermore, they believe that fire-fighting equipment should be recognised by the RFS.

7. Stakeholders have provided various arguments and opinions to support their positions, including references to accounting standards and other authoritative pronouncements that they considered relevant. These are summarised in the appendix *Facts and stakeholder views on fire-fighting assets* – where appropriate, I have commented on them. Readers of this report, may wish to familiarise themselves with the appendix before considering the body of my report.

8. A related issue is the control of land and buildings provided by the RFS. They are also fire-fighting equipment as defined. I understand that land and buildings are viewed generally as *controlled* by the relevant council and recorded in councils' financial statements. But are they controlled by the councils?

9. The principle of control should apply to all fire-fighting equipment. RFS-sourced land and buildings, these should be subject to the same control considerations as the red-fleet vehicles. There are likely to be further implications for councils where council land has been used as a contribution to infrastructure. These need to be determined by each council in accordance with their own facts and circumstances, applying the test of materiality. I understand that white vehicles are recognised by the RFS as not vested to councils and are held at RFS districts for RFS use only. Accordingly, this issue is not considered further.

Scope

10. The OLG requested a review of the present arrangements of *how these assets, including red-fleet vehicles*, should be recognised with particular reference to which entity controls them (and should therefore recognise them in financial statements) to improve consistency in financial reporting in accordance with AASB standards.

11. Specifically, the OLG requested consideration of issues about legal versus operational control, future economic benefits of the assets, control of assets' movements, expertise to maintain assets and insurance.

Relevant accounting pronouncements

12. Based on my review of *Facts and stakeholder views on fire-fighting assets* (appendix), and consideration of these in the context of accounting standards and the *Framework for the Preparation and Presentation and Financial Statements*, the issues in contention cannot be resolved by reference to a specific accounting standard. Accordingly, the GAAP hierarchy under AASB 108 *Accounting Policies, Changes in Accounting Estimates and Errors* is the starting point for deliberations as to the appropriate accounting for red-fleet vehicles and related issues.

13. In the framework, an asset is defined as '[a] resource: *controlled* [my emphasis added] by an entity as a result of past events; (a) and from which future economic benefits are (b) expected to flow to the entity'. The framework also addresses the concepts of 'faithful representation', 'substance over form', and 'service potential'. 'Control' is defined in SAC 1 *Definition of the Reporting Entity*. These definitions and concepts are helpful in determining who controls fire-fighting equipment (including the red-vehicle fleet).

14. I have also considered the requirements of following accounting standards, and applied them in my deliberations and in forming my opinion:

- AASB 101 *Presentation of Financial Statements*
- AASB 116 *Property, Plant and Equipment*
- AASB 138 *Intangible Assets*
- AASB 117 *Leases*
- AASB 16 *Leases*
- AASB 15 *Revenue from Contracts with Customers*, and

- AASB 10 *Consolidated Financial Statements*.

15. The assets in question meet the definition of 'property, plant and equipment' in AASB 116 *Property, Plant and Equipment*. AASB 116 does not set requirements or provide guidance to support the argument that legal ownership is necessary for asset recognition nor an indicator of it.

16. AASB 138 *Intangible Assets* provides guidance on control of an asset – power to obtain the future economic benefits flowing from the underlying resource and to restrict the access of others to those benefits. Also, an enforceable legal right, it is not a necessary condition for intangible asset recognition as there may be other means of exercising control.

17. AASB 117 *Leases* contains a notion of ownership for classification between operating and financing leases. If arguments were mounted based on the principles in AASB 117, it is likely that the conclusion reached would be risks and rewards incidental to ownership of an asset (red-fleet vehicles and related infrastructure) would be retained by RFS.

18. AASB 16 *Leases* applies from 1 January 2019 and employs the principle of 'a right to control the identified asset'. The notion of ownership of an asset is irrelevant under this model.

19. AASB 15 *Revenue from contracts with customers* applies from 1 January 2019 for not-for-profit entities. It uses control (not ownership) to describe when a good/service (an asset) is transferred to a customer – i.e., when the customer obtains control of it. In this context, control includes the ability to prevent others from directing the use of, and obtaining the benefits from, an asset.

20. AASB 10 *Consolidated Financial Statements* with its principle of 'control of investee' (an asset, for the purpose of this report) is a further authoritative source to be considered to the issue of who controls specifically the red-fleet vehicles and land and buildings.

21. In the absence of a specific accounting standard addressing the issues in contention, I have used the GAAP hierarchy and applied *collectively* the principles in AASB 116, AASB 138, AASB 117, AASB 10 and the recently issued standards AASB 16 and AASB 15 to help form my opinions.

22. These authoritative pronouncements strongly indicate that the fire-fighting equipment should be based on control rather than legal vesting (and related assessments of risks and rewards of ownership).

23. The issue also arises as to whether fire-fighting equipment is material in the context of the financial statements of councils concerned and the RFS. This assessment will need to be made by all parties. It may be that the fire-fighting equipment is immaterial to councils but material to the RFS.

In my opinion

24. The service potential of an asset is specific to an entity in meeting its objectives. An asset cannot be controlled by two entities. The fire-fighting equipment in question benefits both the councils and the RFS in helping them to comply with their legislative requirements.

25. The RFS has the substantive responsibilities for the prevention, mitigation and suppression of bush and other fires in local-government areas of New South Wales and controls fire-fighting equipment to meet its statutory objectives. It is the reason for the RFS's existence.

26. On the other hand, councils have their own unique responsibilities under the Local Government Act 1993 such as prescribed functions (s.21) and service functions, including the provision of goods, services and facilities and carrying out of activities (s.24), public land, environmental-upgrade agreements, and regulatory functions. The councils also have what I would consider as secondary or ancillary obligations under *Rural Fires Act 1997* to those of the RFS.

27. Through its service standards and rural fire district service agreements, the RFS has decision-making authority over fire-fighting equipment under the Act. The RFS exercises this authority through them, including the functions of zone managers and rural fire brigades. Many of the decisions are delegated by the RFS commissioner.

28. Furthermore, control of fire-fighting equipment by the RFS is evident by procurement (and replacement and retirement) decisions, service standards for care and maintenance, access, and deployment within the district and elsewhere. These are substantive rights of RFS. The RFS also has a protective right that prevents councils from selling or disposing of the assets without the written consent of the RFS commissioner. There are instances noted by some councils where the 'delegates' of the RFS restrict council access to fire-fighting equipment.

29. The councils have no substantive rights for the control of fire-fighting equipment – vesting by itself does not confer control.

30. As red-fleet vehicles are not controlled by the councils; also, any land and buildings provided by the RFS, as fire-fighting equipment, for its use are also likely not controlled by councils.

My recommendations

31. Fire-fighting equipment recognised by some councils should be derecognised. If the error is considered material, it should be disclosed as such under AASB 108 *Accounting Policies, Changes in Estimates and Errors*.

32. Fire-fighting equipment vested in councils whether recognised or unrecognised under options in the code should be recognised at cost in the RFS's financial statements. This should be accounted and disclosed as an error under AASB 108 *Accounting Policies, Changes in Estimates and Errors* if the error is determined to be material.

33. Given the diversity of opinion between two group of stakeholders over a long period, an argument could be made that rather than an error, it is a change in accounting policy resulting for consideration of recently issued accounting standards (i.e., AASB 10, AASB 15, AASB

16) that provide more definitive guidance on the control. Accordingly, it would be not treated as error.

34. Under AASB 108, 'an entity shall change an accounting policy only if the change: … (b) results in the financial statements providing reliable and more relevant information about the effects of transactions, other events or conditions on the entity's financial position, financial performance or cash flows' (AASB 108.14).

35. AASB 108 also identifies two circumstances that are not changes in accounting policies: (a) the application of an accounting policy for transactions, other events or conditions that differ in substance from those previously occurring and (b) the application of a new accounting policy for transactions, other events or conditions that did not occur previously or were immaterial' (AASB 108.16). For an argument of a change in accounting policy to be sustained the 'differ in substance test' would need to be argued.

36. As a change in accounting policy, the derecognition of fire-fighting equipment by those councils that had previously recognised such assets and their recognition by the RFS would present more reliable and relevant information to the users of their financial statements and be in line with the entities' objectives.

37. My preference is for an error correction as the appropriate treatment.

38. Turning specifically to RFS-sourced land and buildings, these should be subject to the same control considerations as the red-fleet vehicles. There are likely to be further implications for councils where council land has been used as a contribution to infrastructure. These need to be determined by each council in accordance with their own facts and circumstances, applying the test of materiality.

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My brief

Scope of engagement

1. The New South Wales Office of Local Government (OLG) has engaged Colin Parker, principal, *GAAP Consulting* to:

> '[U]ndertake a review of current arrangements to assess, identify and make recommendations on the appropriate recognition of Rural Fire Services (RFS) assets, including and how they should be treated for accounting purposes to create better clarity and consistency across the local-government sector'.
>
> 'In conducting the review and making a report and recommendations, the focus should be on:
> - a desktop review of legislation, policies, guidelines and reports
> - identification and consideration of all key issues
> - interviews with key stakeholders, including relevant councils
> - identifying all possible options for recognising RFS assets
> - forming an opinion about whether the best option would be for fire-fighting apparatus (assets) to be recorded in RFS's or councils' financial statements (note: land and buildings are generally controlled by the council and already recorded in councils' financial statements)
> - consequential impacts for local government of each option considered in the context of financial reporting, and
> - any other matter considered relevant for OLG to be aware of in the course of conducting the work'.

2. The deliverables identified were:
   - 'a report setting out the findings and recommendations of an evidenced-based review of current arrangements, including desktop research and interviews with key stakeholders, and proposed recommendation for the appropriate recognition of RFS assets, and
   - any consequential impacts for local government.'

The issue – who controls fire-fighting equipment?

3. Fire-fighting equipment provided by RFS to local councils is a vexed issue. Who controls the asset, the RFS or the councils?

4. Currently, the land and buildings provided by RFS are viewed *generally* as controlled by the council and recorded in councils' financial statements, the accounting treatment of other assets (particularly, the so called red-fleet vehicles) being the focal point of concern.

5. Some councils are concerned about who controls RFS assets, including red-fleet vehicles, and the consequential financial-reporting effects of 'ownership'.

6. Furthermore, there has been inconsistent treatment between the RFS, a state-government entity, and some councils. Councils are given the choice (in the OLG accounting code) to recognise or not to recognise the assets as determined by accounting standards.

7. As the auditor-general's mandate has been extended to cover local governments, the auditor-general is seeking to ensure an appropriate treatment. The auditor-general's office

recently formed a view that it believed that RFS assets, including red-fleet vehicles, are controlled by councils. This position was informed by a separate view provided by the NSW Treasury to the auditor-general.

8. The OLG requires a review of how *RFS assets, including the red-fleet vehicles*, should be recognised, with particular reference to which organisation controls them (and should therefore record them in their financial statements) for the purposes of informing greater consistency in financial reporting under the Australian Accounting Standards Board standards.

9. Relevant sources of legal and other relevant obligations include: *Rural Fires Act 1997* (the Act); *Local Government Act 1993*; OLG *Code of Accounting Practice and Financial Reporting*; and Australian Accounting Standards.

10. The *Local Government Code of Accounting Practice and Financial Reporting* (Update No. 25, June 2017) stated: 'Councils have the option to continue to recognise or not to recognise Rural Fire Services assets in their accounts until such time as the control issue is agreed upon with the Rural Fire Service'.

Key issues identified in the request for tender

11. The Request for Tender identified the following key issues:

'*Legal vs operational control* – As red-fleet vehicles are legally vested in the council, the RFS does not record them in its financial statements. Many councils also do not record them in their financial statements because they are effectively managed, used and maintained on a day-to-day basis by the RFS via *Rural Fire District Service Agreements* under s12A of the Act. These set out arrangements for maintenance, use, access and delegation of hazard reduction activities.

Future economic benefits of the assets – RFS assets benefit both councils and the RFS in helping them to comply with their legislative requirements. For the purposes of *The Framework for Preparation and Presentation of Financial Statements* for not-for-profit entities in the public sector, economic benefit of an asset equates to its service potential.

Control of movement of assets – Even though S119(2) of the Act vests the assets in the relevant council, S119(3) prevents the council from selling or disposing of the assets without written consent from the RFS commissioner.

Expertise to maintain assets – Under s119(5) of the Act, it is the relevant council's responsibility to take care and maintain the assets, based on standards set by the commissioner, but councils lack expertise to do so and transfer this obligation to the RFS through the agreement.

Insurance – While RFS assets are vested in councils, they may agree to an arrangement whereby the RFS acquires insurance coverage in its name. The RFS pays the premium from the Rural Fire Fighting Fund (RFFF) and is nominated as an insured party under the policy.'

My accounting opinion

Relevant accounting pronouncements

Application of GAAP hierarchy in the absence of a specific accounting standard

12. Based on my review of *Facts and stakeholder views on fire-fighting assets* (appendix), and consideration of these in the context of accounting standards and the *Framework for the Preparation and Presentation and Financial Statements*, I am of the opinion that the issues in contention cannot be resolved by reference to a specific accounting standard.

13. Accordingly, I have formed my views in accordance with AASB 108 *Accounting Policies, Changes in Accounting Estimates and Errors*. Relevant paragraphs are:

> '10 In the absence of an Australian Accounting Standard that specifically applies to a transaction, other event or condition, management shall use its judgement in developing and applying an accounting policy that results in information that is: (a) relevant to the economic decision-making needs of users; and (b) reliable, in that the financial statements: (i) represent faithfully the financial position, financial performance and cash flows of the entity; (ii) reflect the economic substance of transactions, other events and conditions, and not merely the legal form; (iii) are neutral, i.e. free from bias; (iv) are prudent; and (v) are complete in all material respects.
>
> 11 In making the judgement described in paragraph 10, management shall refer to, and consider the applicability of, the following sources in descending order: (a) the requirements in Australian Accounting Standards dealing with similar and related issues; and (b) the definitions, recognition criteria and measurement concepts for assets, liabilities, income and expenses in the Framework.
>
> 12 In making the judgement described in paragraph 10, management may also consider the most recent pronouncements of other standard-setting bodies that use a similar conceptual framework to develop accounting standards, other accounting literature and accepted industry practices, to the extent that these do not conflict with the sources in paragraph 11.'

14. I note that the various stakeholders did not use the GAAP hierarchy as a starting point for their deliberations. Instead, they selected specific accounting standards and/or the framework to support their contentions.

15. I have made my assessment based on the '11(a) requirements in Australian Accounting Standards dealing with similar and related issues'. Specifically, I considered the requirements of the following accounting standards and applied them *collectively* in my deliberations and in forming my opinion:

- AASB 101 *Presentation of Financial Statements*
- AASB 116 *Property, Plant and Equipment*
- AASB 138 *Intangible Assets*
- AASB 117 *Leases*
- AASB 16 *Leases*
- AASB 15 *Revenue from Contracts with Customers,* and
- AASB 10 *Consolidated Financial Statements*.

16. The standards cited above include those that date back to when Australia transitioned to international standards in 2005-2006 (AASB 116, AASB 117 and AASB 138), AASB 10 (operative from 1 January 2013) and recently issued standards (AASB 15 operative from 1 January this year and AASB 16 operative from 1 January next).

17. I have also considered the reference in my paragraph 13 above to 11(b) in relation to the definition of an asset.

18. In my view, these pronouncements collectively and substantively support the accounting principle that control of an asset takes precedent over ownership (vesting). Providing a weighting or ranking of asset and ownership is neither required nor necessary.

Framework for The Preparation and Presentation of Financial Statements

19. *The Framework for The Preparation and Presentation of Financial Statements* sets out the concepts that underlie the preparation and presentation of financial statements for external users which includes '1(d) assist preparers of financial statements in applying Australian Accounting Standards and in dealing with topics that have yet to form the subject of an Australian Accounting Standard'.

20. The framework, and accounting standards, use the term 'future economic benefits', which the Australian Accounting Standard Board explains in a not-for-profit context like this:

> 'Aus49.1 In respect of not-for-profit entities in the public or private sector, in pursuing their objectives, goods and services are provided that have the capacity to satisfy human wants and needs. Assets provide a means for entities to achieve their objectives. Future economic benefits or service potential is the essence of assets. Future economic benefits are synonymous with the notion of service potential and is used in this Framework as a reference also to service potential. Future economic benefits can be described as the scarce capacity to provide benefits to the entities that use them and is common to all assets irrespective of their physical or other form.'

21. The framework defines an asset as 'A resource: controlled by an entity as a result of past events; (a) and from which future economic benefits are (b) expected to flow to the entity' (F.49(a)). I note that the definition refers to control, not ownership of a resource. The resource is controlled by an *entity* and not *entities* (i.e. multiple entities cannot control the same asset with the exception of joint control under AASB 11 *Joint Arrangements*). So, the service potential of fire-fighting equipment would primarily flow to one entity.

22. The framework describes when an asset is recognised: '[W]hen it is probable that the future economic benefits will flow to the entity and the asset has a cost or value that can be measured reliably' (F.89).

23. 'Control' is defined in SAC 1 *Definition of the Reporting Entity* as:

> '[T]he capacity of an entity to dominate decision-making, directly or indirectly, in relation to the financial and operating policies of another entity so as to enable that other entity to operate with it in achieving the objectives of the controlling entity' (SAC 1.6)

24. The framework does not contain a definition of 'control of assets', although the withdrawn Statement of Accounting Concept SAC 4 *Definition and Recognition of the Elements of Financial Statements* contained such a definition. Some stakeholders cited it to support the contention that the councils did not control the red-fleet vehicles. The absence of such a definition is not a concern because other definitions and principles in individual standards can be applied to address the issue by analogy. This can often be achieved by substituting the term 'entity' with 'asset'.

25. The following statements regarding 'substance' and 'legal rights' in the framework are also particularly relevant:

- 'In assessing whether an item meets the definition of an asset, liability or equity, attention needs to be given to its underlying substance and economic reality and not merely its legal form (Framework .51)', and
- 'In determining the existence of an asset, the right of ownership is not essential' and 'Although the capacity of an entity to control benefits is usually the result of legal rights, an item may nonetheless satisfy the definition of an asset even when there is no legal control' (Framework .57).

AASB 101 *Presentation of Financial Statements*

26. AASB 101 is relevant as it requires consideration of 'material', 'purpose of financial reporting' and 'fair presentation':

- The definition of material: 'Material Omissions or misstatements of items are material if they could, individually or collectively, influence the economic decisions that users make on the basis of the financial statements. Materiality depends on the size and nature of the omission or misstatement judged in the surrounding circumstances. The size or nature of the item, or a combination of both, could be the determining factor' (AASB 101.7).

- Purpose of financial statements: 'The objective of financial statements is to provide information about the financial position, financial performance and cash flows of an entity that is useful to a wide range of users in making economic decisions. Financial statements also show the results of the management's stewardship of the resources entrusted to it' (AASB 101.9).

- Fair presentation: 'Financial statements shall present fairly the financial position, financial performance and cash flows of an entity. Fair presentation requires the faithful representation of the effects of transactions, other events and conditions in accordance with the definitions and recognition criteria for assets, liabilities, income and expenses set out in the Framework. The application of Australian Accounting Standards, with additional disclosure when necessary, is presumed to result in financial statements that achieve a fair presentation' (AASB 101.15).

AASB 116 *Property, Plant and Equipment* – no notion of legal ownership

27. The objective of AASB 116 *Property, Plant and Equipment* includes the following statement:

> '[To] prescribe the accounting treatment for property, plant and equipment so that users of the financial statements can discern information about an entity's investment in its property, plant and equipment and the changes in such investment. The principal issues in accounting for property, plant and equipment are the recognition of the assets, the determination of their carrying amounts and the depreciation charges and impairment losses to be recognised in relation to them'. (AASB 116.1)

28. AASB 116 defines 'property, plant and equipment' as tangible items that: '(a) are held for use in the production or supply of goods or services, for rental to others, or for administrative purposes', and '(b) are expected to be used during more than one period'. The red-fleet vehicles (also the 'white fleet'), and associated land and buildings fall within this definition; and must therefore be accounted for under this standard.

29. In relation to recognition, 'the cost of an item of property, plant and equipment shall be recognised as an asset if, and only if: (a) it is probable that future economic benefits associated with the item will flow to the entity; and (b) the cost of the item can be measured reliably' (AASB 116.8).

30. AASB 116 does not define or describe 'future economic benefits' but the framework extracts are helpful in this regard.

31. In reference to cost, AASB 116 requires that 'for not-for-profit entities, where an asset is acquired at no cost, or for a nominal cost, the cost is its fair value as at the date of acquisition' (AASB 116. Aus15.1).

32. *If* the fire-fighting equipment (and associated land and buildings) provided by RFS were an asset of the council, they would have to be fair-valued at acquisition date (and they would be carried at fair value going forward due to OLG's direction). It is likely that the RFS as the provider of such assets to council would have fair-value information, particularly of the red-fleet vehicles as the procurer of such assets.

33. AASB 116 does not contain any reference to a definition of control nor discussion of ownership for purpose of asset recognition.

34. In my opinion, there is nothing in AASB 116 which supports an argument that legal ownership is a 'strong indication of control' (Treasury view) and '[a]ssets are vested in the Council as per Rural Fire Services Act 1997, giving Council legal ownership' (NSW Audit Office). This finding is also borne out my consideration of other accounting standards – some dating back to the transition to IFRS in 2005-2006 others being more recent.

AASB 138 *Intangible Assets* –guidance on 'control'

35. AASB 138 *Intangible Assets* is helpful as it contains commentary about 'control of an asset'. It should be noted that AASB 138 contains higher asset-recognition tests than AASB 116 due to the nature of intangible assets and expenditures that give rise to assets, and the difficulty with recognition and measurement. Accordingly, this distinction needs to be borne in mind when applying AASB 138 to the present situation.

36. The objective of AASB 138 is:

> '[To] prescribe the accounting treatment for intangible assets that are not dealt with specifically in another Standard. This Standard requires an entity to recognise an intangible asset if, and only if, specified criteria are met. The Standard also specifies how to measure the carrying amount of intangible assets and requires specified disclosures about intangible assets.'

37. In relation to *control*, AASB 138 states:

> '13. An entity controls an asset if the entity has the power to obtain the future economic benefits flowing from the underlying resource and to restrict the access of others to those benefits. The capacity of an entity to control the future economic benefits from an intangible asset would

normally stem from legal rights that are enforceable in a court of law. In the absence of legal rights, it is more difficult to demonstrate control. However, legal enforceability of a right is not a necessary condition for control because an entity may be able to control the future economic benefits in some other way.
14 Market and technical knowledge may give rise to future economic benefits. An entity controls those benefits if, for example, the knowledge is protected by legal rights such as copyrights, a restraint of trade agreement (where permitted) or by a legal duty on employees to maintain confidentiality.
16 An entity may have a portfolio of customers or a market share and expect that, because of its efforts in building customer relationships and loyalty, the customers will continue to trade with the entity. However, in the absence of legal rights to protect, or other ways to control, the relationships with customers or the loyalty of the customers to the entity, the entity usually has insufficient control over the expected economic benefits from customer relationships and loyalty for such items (e.g. portfolio of customers, market shares, customer relationships and customer loyalty) to meet the definition of intangible assets. In the absence of legal rights to protect customer relationships, exchange transactions for the same or similar non-contractual customer relationships (other than as part of a business combination) provide evidence that the entity is nonetheless able to control the expected future economic benefits flowing from the customer relationships. Because such exchange transactions also provide evidence that the customer relationships are separable, those customer relationships meet the definition of an intangible asset.'

38. In summary, the principle espoused here is that an entity controls an asset if it has the *power* to obtain future economic benefits flowing from the underlying resource and to *restrict* the access of others to them. The enforceable legal rights ('normally stem from legal rights') are relevant, having regard to the nature of the asset. However, an enforceable legal right is not a necessary condition for intangible-asset recognition.

39. In my opinion, AASB 138 provides a lens through which the current issues should be viewed – 'control of asset' in terms of power, restricted access and that ownership alone does not equate to control. AASB 138, as a piece of authoritative literature, supports the argument for control rather than vesting (legal ownership) of assets leads to an asset's recognition in financial statements.

AASB 117 *Leases* – title not a deciding factor

40. AASB 117 *Leases* can be of assistance in deliberations as it has an ownership notion. The relevant paragraphs are:

4 A finance lease is defined as 'is a lease that transfers substantially all the risks and rewards incidental to ownership of an asset. Title may or may not eventually be transferred'.
7 The classification of leases adopted in this Standard is based on the extent to which risks and rewards incidental to ownership of a leased asset lie with the lessor or the lessee. Risks include the possibilities of losses from idle capacity or technological obsolescence and of variations in return because of changing economic conditions. Rewards may be represented by the expectation of profitable operation over the asset's economic life and of gain from appreciation in value or realisation of a residual value.

41. Identification of a finance lease results in the recognition of lease asset and liability in financial statements of the lessee. Whereas, an operating lease is disclosed as a commitment of the lessee.

42. I note that determination of risks and rewards is framed in a for-profit context to which I would overlay with the term 'service potential' in the current context.

43. I make the following comments about current circumstances:

1. Classification does not depend on the title passing, which, in my opinion, weakens the argument that vesting of the assets to the councils under the Act is a *significant factor* in determining asset recognition.

2. The risks and rewards incidental to ownership substantially rest with the RFS to achieve its objectives under the Act. Both the RFS and, to a far lesser degree, the councils benefit from fire-fighting equipment to meet their responsibilities under the Act. The councils have effectively outsourced their responsibilities to the RFS through rural district service agreements. Under these agreements, the red-fleet vehicles are effectively managed, used and maintained on a day-to-day basis by the RFS for the RFS.

3. The RFS has set extensive service standards on fire-fighting equipment and its use by volunteers which, in my opinion, gives the service decision-making powers over that equipment and its service potential.

4. The councils' only partially share any gain on disposal.

44. In my opinion, applying an ownership test based on risks and rewards to the red-fleet vehicles would see the risks and rewards (service potential) being substantially enjoyed by the RFS to meet its obligations under the Act.

45. I also note that the framework uses a finance lease as an example of substance over legal form:

'… in the case of finance leases, the substance and economic reality are that the lessee acquires the economic benefits of the use of the leased asset for the major part of its useful life in return for entering into an obligation to pay for that right an amount approximating to the fair value of the asset and the related finance charge. Hence, the finance lease gives rise to items that satisfy the definition of an asset and a liability and are recognised as such in the lessee's balance sheet.' (Framework .51)

46. In current circumstances, the legal form would focus on the vesting provisions of the Act. Whereas, in my opinion, the substance would take into account all facts and circumstances including:

- The responsibilities of the RFS and its commissioner and those of the councils under the Act and their respective relativities
- The service standards set by the RFS for use of the fire-fighting equipment
- The rural fire district service agreements, and
- Which entity substantially receives the benefit of service potential for the existence and use of the fire-fighting equipment to meet its objectives.

47. I note that *AASB 117 Leases* is to be replaced by AASB 16 *Leases* from 1 January 2019. AASB 16 employs the principle of 'a right to control the identified asset for a period of time in exchange for consideration'. The notion of ownership of an asset under AASB 1176 is superseded. AASB 16, the most recently issued standard, requires that asset assessments be based on control of the asset.

AASB 15 *Revenue from Contracts with Customer*s – further contemporary evident of control

48. I note that the recently issued AASB 15 *Revenue from Contracts with Customer* also uses the concept of control in its requirements regarding satisfaction of performance obligations:

> '31 An entity shall recognise revenue when (or as) the entity satisfies a performance obligation by transferring a promised good or service (i.e. an asset) to a customer. An asset is transferred when (or as) the customer obtains control of that asset.
>
> 33 Control of an asset refers to the ability to direct the use of, and obtain substantially all of the remaining benefits from, the asset. Control includes the ability to prevent other entities from directing the use of, and obtaining the benefits from, an asset.'

49. We can see that AASB 15 as another example of the principle of control and provides another consistent explanation of its meaning (for example, the ability to direct and obtain substantially all the asset's benefits and to prevent others from the assets' use).

AASB 10 *Consolidated Financial Statements* – analogous circumstances application

50. AASB 10 *Consolidated Financial Statements* is a relatively recent accounting standard compared with AASB 116, AASB 138, and AASB 117. It contains a level of detail of how control should be determined that is not found in the other standards I have cited. In this regard, it is helpful in further understanding the term 'control' and its use by analogy.

51. AASB 10 embodies the concept of control rather ownership of an investee (an asset). It defines the principle of control and establishes control as the basis for consolidation of an investee.

> 'An investor controls an investee when it has all of the following: *power* over the investee's exposure or rights to variable returns from its involvement with the investee, and the ability to use its power over the investee to affect the amount of the investor's returns' (AASB10.7).'

52. Again, I would use the notion of *service potential* as a substitute for *returns* to apply control in the current circumstances.

53. Power (rights) gives the entity the current ability to direct relevant activities (that significantly affect service potential) (AASB10.10).

54. AASB 10 identified considerations for the determination of control (I have substituted 'asset' for 'investee' to assist with its application by analogy):

> '(a) the purpose and design of the asset; (b) what the relevant activities are and how decisions about those activities are made; (c) whether the rights of the investor give it the current ability to direct the relevant activities; whether the investor is exposed, or has rights, to variable returns from its involvement with the asset; and (e) whether the investor has the ability to use its power over the asset to affect the amount of the investor's returns' (AASB 10.B3).

55. Understanding what constitutes 'relevant activities' is important in understanding 'power' over the 'asset':

> 'B9 To have power over an investee, an investor must have existing rights that give it the current ability to direct the relevant activities. For the purpose of assessing power, only substantive rights and rights that are not protective shall be considered.'

56. In the current circumstances, these powers are reflected in those assigned to the RFS commissioner under the Act. They include the setting of service standards and entering into rural fire district service agreements with councils. The powers of the RFS and its commissioner are summarised in the appendix as well as aspects of the service standards issued by the RFS.

57. Relevant activities and direction of relevant activities are linked to control:

> 'B11 For many investees, a range of operating and financing activities significantly affect their returns. Examples of activities that, depending on the circumstances, can be relevant activities include, but are not limited to: (a) selling and purchasing of goods or services; (b) managing financial assets during their life (including upon default); (c) selecting, acquiring or disposing of assets; (d) researching and developing new products or processes; and (e) determining a funding structure or obtaining funding.'
>
> 'B12 Examples of decisions about relevant activities include but are not limited to: (a) establishing operating and capital decisions of the investee, including budgets; and (b) appointing and remunerating an investee's key management personnel or service providers and terminating their services or employment.'

58. In my opinion, examples in B11 (b), (c), (d) and in B12 (a) and (b) are relevant activities of the RFS in relation to the red-fleet vehicles, and land and buildings. They are indicative of power under the three-step control-determination rules in AASB 10.

59. Specifically in relation to B11 and the current circumstances:
- Managing assets – maintenance criteria are specified in the RFS service standards
- Selecting, acquiring or disposing of assets – while councils are involved in the bid process for new fire-fighting equipment, the final decision is made by the RFS with, for example, the type of red-fleet vehicles to be acquired specified in RFS service standards
- Researching and developing new products or processes – this is a responsibility of the RFS as central procurer of fire-fighting equipment as are the processes and improvements determined by the RFS through its service standards, and
- Funding – through RRRF which is a restricted asset of RFS.

60. Specifically in relation to B12 and the current circumstances:
- Establishing operating and capital decisions for the fire-fighting equipment – these are set by the Act, and RFS service standards and not by councils, and
- Appointing service providers (volunteers) and terminating their services – these are set by an RFS service standard.

61. Also, AASB 10 addresses the circumstance where two or more investors each have existing rights that give them the unilateral ability to direct different relevant activities. In such a circumstance, the investor who has the current ability to direct activities that most significantly affect the returns of the investee has power over the investee (AASB 10.13).

62. In the current circumstances, councils have rights in terms of the vesting of fire-equipment with them and their use in meeting the council's responsibilities under the Act. In my opinion, though, they do not have a unilateral ability as they are constrained by the RFS commissioner's powers under the Act, including the setting of service standards, entering into rural fire district service agreements with councils, and restrictions on the disposal of fire-fighting equipment. In my opinion, the RFS has the substantive ability to affect the service potential of the fire-fighting equipment through the RFS commissioner's powers under the Act.

63. AASB 11 *Joint Arrangements* defines the term joint control – the contractually agreed sharing of control of an arrangement, which exists only when decisions about the relevant activities require the unanimous consent of the parties sharing control. In my opinion, joint control does not exist in the current circumstances for the reason stated in the preceding paragraph.

64. In my opinion, in considering the requirements in Australian accounting standards in dealing with similar and related issues under the GAAP hierarchy, AASB 10 is suitable to apply in making a judgement about an appropriate accounting policy along with the principles in AASB 116, AASB 138, AASB 117, AASB 16 and AASB 15.

Themes from authoritative literature

65. From my review of the above, the following principles are evident:

- Assets (and their inherent service potential) are the means for an entity to achieve its objectives by their use
- Focus should be on the underlying substance and economic reality and not merely its legal form
- Control of an asset is the power to obtain the future economic benefits flowing from the resource and to restrict the access of others to those benefits
- Only one entity can control an asset, but the service potential of the asset may be enjoyed by others. In such circumstances, control rests with the entity that substantially enjoys the asset's service potential
- An enforceable legal right is not a necessary condition for control of the asset; there may be other means of exercising control, and
- In the more recent standards, the control-based model for recognition is more evident than a legal ownership/risk and reward model.

Control of the fire-fighting equipment

Service potential

66. Fire-fighting equipment (that is, fire-fighting apparatus – all vehicles, equipment and other things used for or in connection with the prevention or suppression of fire or the protection of life and property in case of fire as well as buildings, water-storage and lookout towers) is an asset. The service potential is the ability to prevent, mitigate and suppress bush and other fires. Buildings and other infrastructure facilitate this ability.

67. Under accounting standards, fire-fighting equipment must be an asset of either the RFS or local councils as the definition of an asset is entity specific.

68. The RFS and individual local councils have 'fire-fighting' responsibilities under the Act in which fire-fighting equipment is used. The responsibilities of the RFS are extensive as described under the Act and include:

a) 'for the prevention, mitigation and suppression of bush and other fires in local government areas (or parts of areas) and other parts of the State constituted as rural fire districts, and
b) for the co-ordination of bush firefighting and bush fire prevention throughout the State.'

69. In comparison, councils' fire-firefighting responsibilities are somewhat limited – they have a duty to prevent the occurrence of bush fires on any land, highway, road and street that is vested in or is under their control. RFS enters rural fire district service agreements with councils to undertake these responsibilities on their behalf.

Rural fire district service agreements

70. It is understood that there may be some differences in the various agreements between the councils and the RFS.

71. Based on a review of a service agreement and some councils' comments on the broad nature of their agreements, the responsibilities of the RFS and a local council can be summarised as:

The RFS:

- Is responsible for the day-to-day management of RFS in the district, including deployment
- Can provide additional equipment to meet its responsibilities under the agreement
- Is responsible for maintenance of district equipment to the standards set by the RFS
- Maintains a register of district equipment, and
- Procurement decisions are made by the RFS with disputes settled by the Minister.

Councils:

- As legal owners have agreed that the RFS can use the district equipment
- Provide certain information to assist the RFS with its tasks in the district, and
- Engages in the procurement process.

72. The recitals and detail of these agreements tell us about the nature of the relationships between the RFS and councils. In essence, the councils' responsibilities under the Act have been contracted to the RFS. The RFS has control of district equipment and premises. It is the RFS that enjoys the assets' service potential.

Asset acquisition and control of their use

73. The NSW Rural Fire Fighting Fund (RFFF) holds all contributions required to meet the costs of co-ordinating bush firefighting and prevention throughout the state and to provision its rural fire services.

74. The fund is maintained by Treasury and used to acquire and build red-fleet vehicles, other assets and to fund RFS activities. RFS has control over the account based on an annual budget approved by the Minister. RFFF is funded by contributions from insurance companies (73.7 per cent), councils (11.7 per cent) and Treasury (14.6 per cent). The councils are entitled to share in the proceeds of disposal of assets (11.7 per cent).

75. The RFS zone manager makes decisions about capital improvements and new assets. While councils may be consulted as part of the decision-making process, they take no part in decisions. Fire-fighting equipment is procured or built, under the direction of the RFS and in accordance the relevant RFS service standards.

76. Under the Act (s119(2)) assets vest in the council for which they have been purchased or constructed. Section 119(3) prevents the council from selling or disposing of the assets without written consent from the RFS commissioner. This is a protective right of the RFS.

77. Under S119(5) of the Act, the councils have the responsibility to take care of and maintain these specialised assets. The Act authorises the RFS commissioner to set maintenance standards for the assets. The councils transfer their maintenance obligations to the RFS through the Rural Fire District Service Agreements.

78. A rural fire brigade (RFB) is generally constituted by the council, the commissioner having the power to constitute an RFB if the council fails to do so. The commissioner controls and directs the functions of the RFB. An RFB is mainly composed of volunteers, and its activities are supervised and co-ordinated by a fire control officer. The FCO is an RFS employee and reports direct to the commissioner.

79. The commissioner may, with the concurrence of the council, use any of the equipment to deal with incidents outside the district area.

80. From the information provided, councils do not have access to red-fleet vehicles and buildings. However, I am informed that this may vary from region-to-region with some councils have limited access to limited use of the red-fleet.

81. The RFS insures plant and equipment, and councils meet the outgoing of buildings and other infrastructure assets.

82. The Minister for Police and Emergency Services has powers regarding disputes between the RFS and councils on matters such as contribution.

Infrastructure provided by the RFS

83. While accounting treatment of red-fleet vehicles has been the focus for many, the appropriate accounting of land and buildings provided by the RFS also needs to be explicitly addressed as required by my brief. Given that the same accounting considerations arise for both red-fleet vehicles and the land and buildings provided by RFS, it puzzles me that stakeholders have failed to canvass appropriate accounting for the latter.

84. Land and buildings *provided by the RFS* have generally been regarded as owned and/or controlled by the councils and recorded in their financial statements. Arguments for the continued recognition of land and buildings have not been advanced.

85. From the information provided, it appears that the recognition of land and buildings is, in part, justified on the basis of councils' responsibility for their maintenance and insurance. In other aspects, they seem similar to red-fleet vehicles. Maintenance and insurance of buildings are obligations. They are not rights to control assets for their service potential to meet councils' objectives.

86. The underlying accounting for fire-fighting equipment, whether red-fleet vehicles or land and buildings, should be subject to the application of the same accounting principles as previously outlined.

87. In my opinion, as red-fleet vehicles are not controlled by the councils, land and buildings provided by the RFS in association with them are also *likely* not controlled by the councils. The latter need to be further investigated.

88. Where councils have provided land and buildings to the RFS, they will need to give consideration to requirements of AASB 117 *Leases* and AASB 1004 *Contributions* and also the new standard AASB 16 *Leases*.

Specific issues

89. The following issues were identified for consideration as part of this review and I provide my opinions on them.

90. *Legal vs operational control*: Accounting issues need to be considered in the context of control over the asset's service potential to contribute to the objectives of the entity. Legal ownership (vesting) is not the crucial determinant for control as explained in my review of the accounting standards and framework.

91. *Future economic benefits of the asset*: The service potential of an asset is specific to the entity and its objectives. An asset cannot be controlled by two entities. The fire-fighting equipment benefits both the councils and the RFS in helping them to comply with their legislative requirements. The RFS has the substantive responsibilities for the prevention, mitigation and suppression of bush and other fires in local government areas and other parts of the State, and controls fire-fighting equipment to meet its statutory objectives.

92. *Control (of movement) of assets*: The RFS has decision-making authority over fire-fighting equipment under the Act and rural fire district service agreements. The RFS exercises this authority through them, including the functions of zone managers and rural fire brigades.

93. Control of fire-fighting equipment is evident by procurement (and replacement and retirement) decisions, service standards for their care and maintenance, access restrictions, and deployment within the district and elsewhere in the state. These are substantive rights of the RFS. The RFS also has a protective right in that councils are prevented from selling or disposing of the assets without written consent from the RFS commissioner (s.119(3)).

Councils have no substantive rights for the control of fire-fighting equipment – vesting does not confer control.

94. *Maintenance of assets* (including expertise): As the decision-making authority, the RFS is exposed to the risks of poor fire-fighting equipment, with the exception of the exterior of some infrastructure assets within the district. While the relevant council has responsibility under the Act for care and maintenance of the vested assets, the standards of care and maintenance are set by the RFS commissioner under the Act (s119(5)). The councils have outsourced this obligation to the RFS through the rural fire district service agreements. Fire-fighting equipment, with exception of some infrastructure assets, is specialised, and expertise for its maintenance lies with the RFS and not councils. The RFS has set service standards for maintenance.

95. *Insurance:* As the decision-making authority, the RFS is exposed to the risks of loss of fire-fighting equipment with the exception of the exterior of some infrastructure assets that are insured by councils, and the RFS has insured against its risks.

Conclusion

96. Users of not-for-profit financial statements are concerned with the ability of an entity to achieve its objectives, both financial and non-financial. Financial statements should show the results of the stewardship of management for the resources entrusted to it.

97. The current accounting for fire-fighting equipment fails the information needs of the RFS's and councils' financial-statement users as the equipment has failed to be recognised by the entity that controls its potential to meet its objectives.

98. In my opinion, fire-fighting equipment is controlled by the RFS as determined by application of accounting standards and the framework according to the facts and circumstances described.

99. Recognition of fire-fighting equipment by the RFS in its financial statements, and derecognition by the councils from theirs, also satisfies the definition of an asset and qualitative characteristics of financial statements, including faithful representation and substance over form.

100. Fire-fighting equipment recognised by some councils should be derecognised and this should be accounted and disclosed as an error under AASB 108 *Accounting Policies, Changes in Estimates and Errors*.

101. Fire-fighting equipment vested in councils, whether recognised or unrecognised, under options in the code should be recognised in the RFS's financial statements. This should be accounted and disclosed as an error under AASB 108 *Accounting Policies, Changes in Estimates and Errors.*

102. Alternatively, an argument could be made that rather than an error, it is a change in accounting policy resulting for consideration of recently issued accounting standards (i.e., AASB 10, AASB 15, AASB 16) that provide more definitive guidance on the control. However, in my opinion the long-standing authoritative pronouncements (framework, SAC 1, AASB 116, AASB 138, and AASB 117) were sufficient to conclude that decisions should be made on the basis of control rather than ownership. Some may not share this view.

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Appendix: Facts and stakeholder views on fire-fighting assets

Introduction

1. Stakeholders have provided the Office of Local Government (OLG) with various arguments, opinions, and documents to support their positions on accounting for red-fleet assets in particular. The OLG has provided these for my consideration. Extracts from them have been included in this appendix along with salient matters from my discussions with certain stakeholders.

2. I have also included my views on several issues raised that link to the body of my report. However, I have not commented on individual arguments for and against recognition in the financial statements of councils or the RFS; these have been addressed in the body of my report.

3. The RFS is the lead combat agency for bush fires. It works closely with other agencies to respond to emergencies, including structure fires, motor-vehicle accidents and storms that occur within the rural fire districts.

4. The RFS website contains the following description of responsibilities:

> 'The NSW RFS has fire management responsibilities for over 95 percent of the landmass of the State and therefore the Service is spread across the length and breadth of NSW. A total of 47 districts are grouped into four regions.
>
> 'In each District NSW RFS staff members assist volunteers and brigades to prepare for and respond to operational incidents.
>
> 'A Fire Control Centre forms the administrative and operational base of the rural fire district or zone.
>
> 'The coordination and management of local brigade responses to fire and other incidents – including natural disasters, motor vehicle accidents and other civil emergencies – is undertaken through the Fire Control Centre.'

NSW Rural Fire Services (RFS)

Responsibilities of RFS and Councils

5. The Rural Fires Act 1997 (the Act) established the Rural Fire Service (RFS) to co-ordinate bush firefighting and prevention throughout the state and to provide rural fire services for New South Wales.

6. The objects of the *Rural Fires Act 1997* are to provide:

a) 'for the prevention, mitigation and suppression of bush and other fires in local government areas (or parts of areas) and other parts of the State constituted as rural fire districts, and
b) for the co-ordination of bush firefighting and bush fire prevention throughout the State, and

c) for the protection of persons from injury or death, and property from damage, arising from fires, and c1) for the protection of infrastructure and environmental, economic, cultural, agricultural and community assets from damage arising from fires, and
d) for the protection of the environment by requiring certain activities referred to in paragraphs (a)–(c1) to be carried out having regard to the principles of ecologically sustainable development described in section 6 (2) of the Protection of the Environment Administration Act 1999.' (s.3)

7. The following sections of the Act are noteworthy on control of fire-fighting equipment, and in particular the powers of the commissioner, the service standards, and the requirements of councils:

Functions

- The RFS consists of the commissioner and other staff of the service and volunteer rural fire fighters (s.8).
- The functions of the RFS include 'to provide rural fire services for New South Wales' with such services being defined to include 'services for the prevention, mitigation and suppression of fires in rural fire districts' (s9).
- The commissioner is, in the exercise of his or her functions, subject to the control and direction of the minister (s11).
- The functions of the commissioner include: 'The Commissioner is responsible for managing and controlling the activities of the Service and has such other functions as are conferred or imposed on the Commissioner by or under this or any other Act' (s12).

Service standards

- In relation to service standards '[the] Commissioner may from time to time issue written policy statements to members of the Service for or with respect to procedures to be followed in connection with the operation, management and control of the Service' (s13).

Brigades

- A local authority may form a rural fire brigade, and the commissioner may form one if the local authority refuses or fails to do so within the period prescribed by the regulations after being requested to do so by the commissioner (s.15).
- In relation to the area of operations and officers of groups of rural fire brigades: the fire control officer who forms a group of rural fire brigades is to determine the territory in which the group is to operate, and the officers of the rural fire brigades forming a group of rural fire brigades are those persons selected, in accordance with the service standards, to be officers for the group by the members of the rural fire brigades forming the group. A person selected to be an officer holds office for the period specified in the service standards (s.19).
- The functions of officers of rural fire brigades are conferred or imposed on the officer by or under this or any other Act. Functions may be conferred under the Act by the service standards (s.21).
- The general powers of rural fire brigade officers and others are described. Also, 'Any function that may be exercised, or action that may be taken, by an officer of a rural fire

brigade or group of rural fire brigades because of this section may be exercised or taken by the Commissioner' (s.22).

- Responsibilities of fire control officers and local authorities are: 'A fire control officer is, subject to any direction of the Commissioner, responsible for the control and co-ordination of the activities of the Service in the rural fire district for which he or she is appointed as fire control officer', and '[the] local authority for the rural fire district for which a fire control officer is appointed must provide facilities and accommodation to enable the fire control officer to exercise his or her functions' (s.37)'.

- The commissioner may authorise officers and members of rural fire brigades to exercise certain functions (s.39).

- The commissioner is to take charge of bush fire-fighting operations and bushfire prevention measures and to take such measures as the commissioner considers necessary to control or suppress any bushfire in any part of the state (with four circumstances identified). The commissioner may delegate the functions to individuals described (s.44).

- The commissioner may give such directions as he or she considers necessary to fire control officers, deputy fire control officers, officers of rural fire brigades, local authorities, officers or members of Fire and Rescue NSW, members of the NSW Police Force and other persons in connection with the prevention, control or suppression of any bushfire in the area or locality in which the commissioner has taken charge or is taking measures under this division (s.45).

8. Under s63, local councils have the duty to prevent the occurrence of bush fires on any land, highway, road and street that is vested in, or is under the control of, that council.

9. Under s119(1) of the Act, fire-fighting equipment is defined as: *fire-fighting apparatus, buildings, water storage towers or lookout towers*. Fire-fighting apparatus is defined as: *all vehicles, equipment and other things used for or in connection with the prevention or suppression of fire or the protection of life or property in case of fire*.

10. This section also requires:

- All fire fighting equipment purchased or constructed wholly or partly from money to the credit of the Fund is to be vested in the council (s119(2)).

- A council must not sell or otherwise dispose of3any fire fighting equipment without the written consent of the Commissioner (s119(2)).

- A council must take care of and maintain in the condition required by the Service Standards any fire fighting equipment vested in it under this section (s119(5)).

- The Commissioner may, with the concurrence of the council in which fire fighting equipment is vested under this section, use any of the equipment not reasonably required by the council to deal with incidents in the area of the council to deal with incidents outside the area (s119(6)).

Service standards

GAAP Consulting

11. The RFS sets service standards that are available on its website. They number more than 80 and include the following, which I have grouped under headings.

Delegations and the like

- SS 1.3.1 *Delegations and Authorisations (including supplementary delegations-unincorporated area of NSW)* – The statutory powers created by the Rural Fires Act 1997 (the Act) are vested in the Commissioner, Local Authorities, Fire Control Officers and Officers of Brigades. This Service Standard identifies the Delegations (s 14 of the Act) and Authorisations (s 39 of the Act) of the Commissioner with respect to the NSW RFS. It also includes Delegations (s 44 of the Act) of the Commissioner with respect to co-ordinated bush firefighting.

- SS 2.1.*1 Formation and Disbandment of Brigades and Groups of Brigades* – The NSW RFS is committed to providing a fire service which has relevance to local communities and recognises that local situations can change, and there is a need to periodically review the placement of Brigades.

- SS 2.1.4 *Appointment of Field and Group Officers* – The Rural Fires Act 1997 provides for the appointment of Brigade Officers in accordance with the Service Standards.

- SS 1.3.4 *Rural Fire District Service Agreements* – The majority of Local Authorities which have responsibilities for Rural Fire Districts have entered into Rural Fire District Service Agreements (RFDSAs) with the NSW RFS under section 12A of the Rural Fires Act 1997. In accordance with these RFDSAs, the Commissioner assumes responsibility for the exercise of functions imposed upon those Local Authorities by the Act.

Equipment

- SS 1.1.16 *Fundraising Activities (Provision of Goods and Services)* – Members of the Service engage in a range of fund raising activities in order to assist rural fire brigades and groups of rural fire brigades to acquire additional equipment and facilities, to assist in the payment of running costs and to otherwise enhance the service they provide to the community.

- SS 5.1.4 *Fire Fighting Appliance Construction Standards* – This Service Standard ensures that the NSW RFS provides safe, cost effective, standardised, fit for purpose fire fighting appliances across a range of categories.

- SS 5.1.6 *Secondhand Appliance Transfer Program* – The NSW RFS is continuing the program to modernise, standardise and maintain the fire appliance fleet and has a secondhand appliance transfer program that provides for appliances to be transferred between Districts at certain nominated stages.

- SS 5.1.9 *Breathing Apparatus* – This service standard defines the proper acquisition, use, training and maintenance associated with breathing apparatus in the NSW RFS.

- SS 5.3.*1 Equipment Maintenance* – To ensure the safety and effectiveness of rural firefighting and related activities, all equipment and related facilities need to be maintained in a serviceable condition.

- S 5.4.1 *Asset Disposal* – The NSW RFS is committed to the proper management of surplus or deficient physical assets that might otherwise reduce efficient, effective and safe service delivery. One of the key elements of asset management is the timely, appropriate and cost effective disposal of assets in a frame work that ensures probity, honesty and conformity to Government Policy.

Staffing

- SS 1.1.7 Code of Conduct and Ethics – It establishes standards of behaviour expected of all members of the NSW RFS.
- SS 1.1.2 Discipline –Sets out the procedure to be followed when disciplinary action is taken against a volunteer member of the NSW Rural Fire Service (NSW RFS).
- SS 6.1.3 Training in the NSW RFS – Members of the NSW RFS are required to have the relevant competency to carry out the functions for which they have volunteered or for which they have been employed.

12. The existence of these service standards and the nature of their subject matter need to be considered as to whether they indicate control of service-potential assets by the RFS.

RFS Annual Report 2016-2017

13. The RFS Annual report 2016-2017 provided some relevant contextual information which has reproduced below.

14. Commissioner's Report stated:

> 'The year has also seen the continued investment in building new, or refurbishing brigade stations and fire control centres across the state.'
> 'With a total of 6315 tankers, air and marine craft and other vehicles, we continue to assess and improve the effectiveness of the Service's fleet, making modifications, refurbishments and purchasing new as required.'

15. One noteworthy information was: There was 72,233 volunteers and 878 salaried staff; and 'In total across the reporting period, our members attended over 24,500 incidents, including bush and grass fires, motor vehicle accidents, hazard reduction activities and support for other agencies'.

16. The financial statements describe its accounting policy for rural fire-fighting equipment in note 1 as:

> 'The ownership of all fire fighting equipment purchased by the Rural Fire Fighting Fund is vested in the relevant local government council. The cost of such equipment is therefore expensed by the Service in the year of purchase.
> The exception to this is fire fighting equipment purchased for the State Mitigation Service which is recorded on the Service's asset register'.

17. Note 10 Restricted Assets described cash held as part of RFFF $139,532,000 (2016 $104,406,000 as: 'The Service holds funds that form the NSW Rural Fire Fighting Fund which is a special deposits account established under section 102 of the *Rural Fires Act 1997.*

Funds in the Rural Fire Fighting Fund can only be expended for the purposes defined in the Act.'

Rural fire district service agreements

18. I am informed that councils *generally* enter a rural fire district service agreement with the RFS to undertake these responsibilities on behalf of the council. For completeness, it should be ascertained how many councils have these agreements and those that do not. In relation to the latter, how the assets in question are accounted.

19. The Act (s12A) specifies arrangements for entry into *rural fire district service agreements*:

> (1) Without limiting section 12, the Commissioner may enter into a rural fire district service agreement (a service agreement) with any local authority or authorities responsible for a rural fire district or districts.
> (2) Without limitation, a service agreement:
> (a) may specify functions imposed on the local authority by or under this Act that are to be exercised by the Commissioner during a period (if any) specified in the agreement, and
> (b) may specify any obligations to be imposed on the local authority as a consequence of the Commissioner agreeing to exercise those functions, and
> (c) may set performance targets for the exercise of those functions, and
> (d) may provide for the evaluation and review of results in relation to those targets.
> (3) The Commissioner and the local authorities must, as far as practicable, exercise the functions and carry out the obligations in accordance with the service agreement.
> (4) The Commissioner is to report the results of the performance under a service agreement during a financial year to the local authority or authorities concerned within 3 months after the end of that year.

20. I note that this section gives the commissioner various powers over the services to be provided.

21. In my opinion, the existence and specifics of these agreements support the argument that the RFS has control of the assets in question.

22. I have considered one such agreement – made with Tweed Shire council. General comments made by some councils about their agreements, as described elsewhere in this appendix, are consistent with the extracts below.

Example of a rural fire district service agreement (Tweed Shire Council)

23. Under the Rural Fire Services Act 1997, the commissioner may enter a rural fire district service agreement with any local authority(ies) responsible for a rural fire district(s) (s.12A).

24. I have been provided with the agreement between Tweed Shire Council and the commissioner and have summarised key issues.

25. As noted later, other councils report a common approach to agreements.

26. The agreement began on 1 July 2010 and continues until terminated under clause 14 (cl.3).

27. The recitals include:
- Parties entered into agreement under section 12A of the Rural Fire Services Act 1997 (NSW)
- Commissioner agreed to exercise all the functions imposed on Council under the Act, other than those specified in clause 4.2
- Commissioner agreed to undertake all the day-to-day management of the rural fire services operating in the District on behalf of the Council
- Council has agreed to provide certain administrative accounting and maintenance services to the Commissioner and RFS
- The Council has agreed to allow Commissioner and RFS to use the District Equipment and Premises
- The Council and the Commissioner have agreed to establish a liaison committee, and
- The Council has agreed to delegate certain functions powers duties to members of the RFS.

28. District equipment is defined as 'Fire Fighting Apparatus and the other vehicles and equipment: owned by the State of NSW; owned by the Council; or vested in the Council and used by members of Rural Fire Service operating in the District'.

29. Premises are defined as 'Land and buildings or parts of land and buildings specified in schedule 1.' Nine brigade stations, one other station and one control station are identified.

30. The following details are also noteworthy.

Functions and management responsibilities are:
- The Commissioner exercises the Council's functions and manages the district (cl. 4) in consideration of $1 (cl.4.2). The functions include the day-to-day management of RFS in the District (cl.4.2). Certain functions are excluded (cl.4.2).
- The Council provides certain information to the RFS to help RFS to discharge its functions (cl.4.3).
- The Commissioner may, but is not obliged to, utilise or provide additional equipment or personnel in addition to the District Equipment and members of the RFS operating in the District (cl.4.4).

District equipment requirements are:
- Council to make available and allow the use of the District Equipment to Commissioner and RFS (cl.5.1).
- Commissioner agrees to maintain the District Equipment on behalf of the Council in accordance with applicable service standards (cl.5.1). The service standards are those issued by the Commissioner under s.13 of the Act (cl.5.2).
- The RFS will maintain a register of District Equipment with a copy provided to Council every six months (cl.5.3).

Land and buildings requirements are:
- Council agrees to allow the Commissioner and RFS to occupy and use the Premises, or other land and buildings as may be agreed (cl.6.1). Council grants a licence to enter and use (cl.6.2). Commissioner has a personal right of occupation on the terms specific in this licence; but no tenancy, estate, or interest in the land on which the Premises are situated (cl.6.3). Legal right of possession and control over the Premises and land on which they are situated remain vested in the Council (cl.6.4).
- The responsibilities of Council are: not to interfere with the Commissioner's use; pay rates, taxes etc; maintain premises in good repair (as described in cl.6.7); and insure buildings and have the designated public risk insurance coverage (cl.6.5).
- The Commissioner must not occupy or use the Premises other than the provision of fire-fighting services and for related incidental purposes; not assign the licence or grant a sub-

licence; carryout minor repairs (as described in cl.6.8); comply with all relevant laws regarding the Commissioner's use of property; and not alter the premises without the consent of Council (that shall not unreasonably be withheld) (cl.6.6). There are specific provisions regarding access Tweed Fire Control Centre (cl.6.7).

Finance requirements are:

- Annually the Council makes a bid of estimated probable expenditure on District for next financial year to the Commissioner. Following consultation with the Council, the Commissioner submits a probable allocation of expenditure and a probable contribution by the Council to the Rural Fire Fighting Fund. If the Council and Commissioner disagree on these, a determination on the contribution is made by the Minister (cl.8.1 to 8.3).
- The Commissioner, following consultation with Council, provides a four-year budget forecast expenditure, updated annually. Consultation with Council includes: Council's capacity to contribute to the fund; RFS and government policies for replacement of District Equipment, District's requirements by reference to Standard of Fire Cover and other policies; and standards of fire stations and other facilities. The Commissioner provides a draft 10-year capital work program undated annually (cl.8.4 to 8.6).
- The Council can provide funds for the delivery of rural fire services in the District in addition to statutory contribution. The Commissioner must manage those funds in accordance with the directions of the Council (cl.8.7).
- The Commissioner (and at his/her sole discretion) has unrestricted to and may expend monies received by the Council from the fund for delivery of rural fire services in the District. The Commissioner may also expend additional monies(cl.8.8).
- Funding for repairs and maintenance is a reimbursement basis (cl.8.9).

Insurance and related requirements are:

- Effect and keep current the following: property damage and public liability insurance for the property; compulsory third party and comprehensive insurance for motor vehicles that form part of District Equipment, except where agreed otherwise by the Council and the Commissioner; property damage and public liability insurance, third party and comprehensive insurance, for all Premises and District Equipment controlled, occupied, or managed by the Commissioner or RFS (cl.10.1).

In summary, the RFS:

- Is responsible for the day-to-day management of the RFS in the district, including deployment
- Can provide additional equipment to meet its responsibilities under the agreement
- Is responsible for maintenance of district equipment to the standards set by the RFS
- Maintains a register of district equipment, and
- Procurement decisions are made by the RFS with disputes settled by the Minister.

In summary, the council:

- As the legal owner has agreed that the RFS can use the district equipment
- Provides certain information to assist the RFS with its tasks in the district, and
- Engages in the procurement process.

31. The recitals and details reveal the nature of the relationship between the RFS and the council. In essence, the council's responsibilities under the Act have been contracted out to the RFS. The RFS has control of equipment and premises. It is the RFS that enjoys the service potential of these assets.

32. As the legal owner, the council has granted the RFS the right to occupy and use the premises (10 fire stations and one control centre). Outgoings and insurance are met by the council as are major repairs.

33. Where the land and building, constitute fire-fighting equipment provided by RFS, my comments on the accounting for red-fleet vehicles are likely to be equally relevant for their appropriate accounting.

34. Where the land and building were not provided by the RFS, further information is required about how these premises were acquired and whether on council land; and the implications assessed under AASB 117 and soon to be operative standards – AASB 16 and AASB 1058.

Rural Fire Fighting Fund

35. The NSW Rural Fire Fighting Fund (RFFF) holds all contributions required to meet the costs of co-ordinating bush firefighting and prevention throughout the state and to provide rural fire services for New South Wales (s.102)

36. A special RFFF deposit account is maintained by Treasury and used to acquire and build red-fleet vehicles, other assets and to fund RFS activities.

37. To assist the minister in preparing and adopting the rural fire brigade funding target for a financial year, the commissioner must prepare and give to the minister a written report and recommendations about rural fire brigade expenditure for the year and the estimated expenditure for each rural fire district and each relevant council (s.105).

38. The RFS has control over this account based on an annual budget approved by the minister.

39. As per the provisions of the Act, RFFF is funded by contributions from insurance companies (73.7 per cent), councils (11.7 per cent) and Treasury (14.6 per cent). These are recognised as income by the RFS.

40. The assets acquired or built using the RFFF are of two types:

- White-fleet vehicles, which are operational and commercial and are not designed to fight fires. These assets do not benefit councils and are used state-wide and recorded in RFS financial statements.

- Red-fleet vehicles, which are firefighting assets bought or constructed for the benefit of a particular council. As per s119 of the Act: *All firefighting equipment purchased or constructed wholly or partly from money to the credit of the Fund is to be vested in the council of the area for or on behalf of which the firefighting equipment has been purchased or constructed.*

41. Fire-fighting equipment is procured or built and overseen by the RFS.

Arguments advanced that councils control the fire-fighting equipment

NSW Treasury and Rural Fire Service

42. NSW Treasury and RFS formed the view that '[w]hile the arrangements are finely balanced, Treasury has concluded RFS's treatment of not recognising the fire-fighting assets was appropriate' (letter dated 29 September 2017 to the acting chief executive of the OLG).

43. Treasury cited AASB 116 *Property, Plant and Equipment* (para 7) and AASB *Conceptual Framework* (paras. 49 and 89); and Rural Fire Services Act 1997 in forming its view.

44. Treasury's observations were:

'1. Legal ownership sits with the Local Authorities (LA), a strong indication of control
2. RFS permission for disposal is only seen as a protective right
3. It is difficult to ascertain future economic benefits for a NFP. These FF assets allow RFS to comply with their governing legislation/ mandate in Rural Fires Act 1997 and to undertake various Statutory obligations imposed on Councils under the Act, for and on behalf of Councils. There are also potential benefits for Councils.
4. Use/control of assets – SLAs appear to give RFS unrestricted access to the assets. This however is predicated on the LA having the right to grant that access
5. Maintenance of the assets – Councils appear to take responsibility for maintenance
6. Insurance – for FF assets, this is paid and organised centrally by RFS to TMF (paid from the RFFF) for and on behalf of all Councils who have the insurable interest. RFS has no insurable Interest.'

45. The conclusion reached was:

'We acknowledge the ownership of assets is a matter of judgement. However, based on the above our view is that RFS should continue to not recognise the FF assets that have been vested to the Councils, as they receive little future economic benefit, are bound to the service level agreement as agreed with the Councils and do not have control to move the assets to other Councils without permission. This treatment would then be consistent with other assets that are used by RFS, namely land and buildings.

NSW Audit Office

Internal position paper

46. The audit office has produced an internal position paper titled *NSW Rural Fire Service Accounting treatment of Rural Fire Services Assets*.

47. The issue addressed was 'Since Red Fleet vehicles are vested in the council, RFS do not record these in their financial statements. Many councils also do not record the Assets'.

48. Control and other considerations were described:

- 'Even though S119(2) of the Act vests the Assets in the council for whom these have been purchased or constructed, S119(3) prevents the council from selling or disposing of the Assets without written consent from the RFS Commissioner.
- As per the *Framework for the Preparation and Presentation of Financial Statements*, for a not-for-profit entity in the public sector, future economic benefits from an asset is synonymous with the notion of its service potential. These Assets allow RFS to comply with their governing legislation and fulfil their mandate as per the Act. At the same time these Assets help fulfil council's duty under the Act, to prevent the occurrence of bush fires on land

controlled by the council. Economic benefits from the Assets are therefore enjoyed by both the council and RFS.

- Under S12A of the Act, the RFS Commissioner may enter into a Rural Fire District Service Agreement (Agreement) with any council responsible for a rural fire district. These Agreements are contractual licences that set out the understanding between the parties as to maintenance, use and access to firefighting equipment and premises.
- Under S63 of the Act, land owners have the responsibility of preventing the occurrence of bush fire. To comply with the requirements of the Act, councils are obliged to perform hazard reduction activities. Councils do not possess firefighting and hazard reduction expertise and therefore delegate the conduct of this activity to RFS through an Agreement under which the council provides RFS access to council Assets. Under the Agreement, the council agrees to make available to and allow the RFS Commissioner to use the Assets which are owned by, vested in or under the control of the council.
- A Rural Fire Brigade (RFB) is generally constituted by the council. The Commissioner has the power to constitute a RFB if the council fails to do so. A RFB can be disbanded by the person or body who constituted it. A RFB is mainly comprised of volunteers and its activities are supervised and co-ordinated by a Fire Control Officer (FCO), who is an RFS employee and reports directly to the RFS Commissioner. The Commissioner controls and directs the functions of the RFB. Under S38 of the Act, a council is obliged to provide facilities and accommodation to enable the FCO to perform his or her functions. Such facilities and accommodation should be of a standard approved by the Commissioner.
- As per S119(5) of the Act, it is council's responsibility to take care and maintain the Assets. The Act authorises the RFS Commissioner to set maintenance standards for the Assets. The Council lacks expertise to maintain such specialised nature Assets. Being the owner of the Assets, the councils transfers their maintenance obligation to RFS through the Agreement. RFFF is funded through an annual RFS budget, which includes planned maintenance expenditure for firefighting equipment held RFS districts. Councils contribute (11.7%) annually to these budgets which includes the maintenance component. Hence, any subsequent maintenance expenditure incurred by the council is reimbursed by RFS using these funds.
- Like planned maintenance expenditure, the expected insurance cost for the Assets is included in the RFS annual budget. Council, by way of its contribution (11.7%) to the RFFF, contributes to such insurance expenditure. While councils own the Assets, for administrative reasons, Treasury Managed Fund (TMF) and councils have agreed to an arrangement whereby RFS is permitted to acquire insurance coverage for the Assets in its own name. RFS pays the insurance premium from the RFFF and is nominated as an insured party under the insurance policy. RFS does not derive any insurable benefit under the insurance policy. In the event of a loss of an Asset (vested in the council), the insurance proceeds are used to reacquire or build a similar Asset, which then again vests in the same council. The arrangement between RFS and a council does not constitute a lease arrangement, since RFS is not paying any consideration to the council for the use of council's assets.
- The Agreement does not satisfy the conditions of a Joint Arrangement under the Australian Accounting Standards (AASB 11).'

49. There are appendices to the position paper *Appendix 1 – Illustration of the overall arrangement* and *Appendix 2 – Indicators of control*. The latter contains an assessment of control from the perspectives of the RFS and councils, applying:

- Legal ownership
- Future economic benefits and/or service potential
- Daily access and use
- Control of movement
- Maintenance, and

- Insurance.

50. The NSW Audit Office reached the following conclusion:
'Vesting provisions under the Act, substantiated by an Agreement whereby the council allows RFS to use these assets for and on behalf of the council, supports the conclusion that these assets are controlled by the council. In addition, council's responsibility of maintaining these assets and receiving the benefit of an insurance claim (in the event of a loss), further corroborates this conclusion.'

Audit Office final management letter for 30 June 2017

51. Tamworth Regional Council has provided the following extract from the Audit Office's management letter dated 30 June last year in its submission to the OLG on the 2017-2018 draft code:

'As at the 30 June 2017, the Council has exercised the option available under the Local Government Code of Accounting Practice and Financial Reporting not to recognise certain rural fire service assets. RFS assets, specifically the red vehicles, are vested in Council. Combined with other indicators there is a presumption that they are controlled by Council and should be recognised in the Council's financial statements. This is supported by an analysis of Rural Fire Services Act 1997 and service agreements between the councils and RFS.'

'The following are indicators of 'control' by the Council:

- Assets are vested in the Council as per Rural Fire Services Act 1997, giving Council legal ownership
- As the land owner, Council has the responsibility of fire mitigation and safety works under Rural Fire Services Act 1997
- The service agreement allows the RFS use of the assets for fire mitigation and safety works within the Council's area
- Council is responsible for maintaining the assets but has transferred this responsibility to RFS through the service agreement
- In the event of loss of an asset, the insurance proceeds are used to reacquire or build a similar asset, which is again vested in the Council.'

Arguments advanced that councils do not control the fire-fighting equipment

Albury City

Introduction

52. Albury City has prepared a *Position statement on the recognition of Rural Fire Service assets*. Excepts reproduced below reveal the council's view that equipment is not a council asset but land and buildings are.

Background

53. 'Rural Fire districts and Rural Fire Brigades are established generally in line with local council areas. Albury City shares a fire zone and Rural Fire District Service Agreement with Greater Hume Shire Council. Greater Hume Shire Council provides the majority of administrative support required under the service agreement. Albury City maintains buildings within its Local Government Area boundary and services RFS Vehicles through its maintenance depot upon request. Albury City charges the RFS for vehicle servicing costs.'

54. 'Rural Fire Services costs are shared between Albury City and Greater Hume Shire, with Greater Hume Shire paying 80% of the cost and Albury City 20%. The basis of this allocation is tied to the number of fire services identified in each Council area, Greater Hume Shire 19 and Albury City 5.'

55. 'Albury City accounts for land and buildings used by the RFS situated within the Albury City boundary, however does not account for Rural Fire Service plant or other equipment'.

Application of accounting literature

56. The following points are made with reference to the framework.

1. 'An asset is defined as a resource that is controlled by the entity as a result of past events and from which future economic benefits are expected to flow to the entity (49).
2. Attention needs to be given to its underlying substance and economic reality and not merely its legal form (51).
3. In respect of not-for-profit entities, economic benefit is synonymous with service provision or enabling them to meet their objectives to beneficiaries (54).
4. The right of ownership is not essential to the determination of control (57)'.

57. Reference was also made to AASB 116 *Property, Plant and Equipment:*
'[R]equires that an asset can only be recognised if it is probable that future economic benefits associated with the item will flow to the entity.'

58. Reference was also made to SAC 4 *Definition and Recognition of the Elements of Financial Statements* and definition of a 'control of an asset' ('the capacity of the entity to benefit from the asset in the pursuit of the entity's objectives and to deny or regulate the access of others to that benefit'). I note that SAC 4 has been withdrawn.

Facts and circumstances

59. Albury City's statement notes that the Act provides for:

- 'All firefighting equipment acquired from the fund is to be vested in the council of the area (S119)
- A council must not dispose of such equipment without the written consent of the Commissioner, and
- Albury City and Greater Hume Shire are entitled to a share of 11.7% of the disposal proceeds.'

60. The agreement between Albury City and the commissioner includes a basic section on district equipment (section 5):

- 'Council will allow the RFS to use the equipment which is owned by, vested in or under the control of the Council
- The Commissioner agrees to maintain the equipment on behalf of the council, and
- The RFS will maintain and supply to Council a register of the equipment.'

61. The statement further reads:
'This can be compared to a very detailed section on Land and Buildings (section 6) which specifically states that the legal right to possession and control over the premises and land

remains vested in Council and the RFS only has right of occupation. In addition: council must maintain the premises in good repair; council must pay all utility costs associated with the premises; and Council must pay all insurances associated with the building and public risk'.

62. In relation to land and buildings, it states:
'The Rural Fire Service Agreement clearly identifies that Council retains full legal right to possession and control over premises occupied by the RFS. Councils are required to maintain buildings, pay all utility costs associated with the building and pay all insurances on the buildings and public risk associated with the use of the building […] This is similar to a lease agreement, and as such Council retains control of the building and is required to hold the land and associated building as an asset'.

63. In relation to equipment:

- 'Section 119(3) of the Rural Fires Act 1997 (NSW) stipulates that Council must not sell or otherwise dispose of any firefighting equipment … without the consent of the Commissioner. Section 119 (4) requires any funds received from sale must be credited to the RFS fund'
- 'The RFS Zone manager makes all decisions about capital improvements and new assets, while Council may be consulted in these decisions it takes no part in the final decision'
- 'The RFS insures all plant and equipment', and
- 'In practice the RFS makes all decisions to switch fleet and equipment to other fire districts as it feels necessary. Council has no access to and is not permitted to use of any plant and equipment held by the RFS.'

Conclusion

64. The statement concluded:
'It is clear that the AASB Accounting Standards require a standard higher than ownership when accounting for assets. Entities may own an asset, but unless they have control of that asset and can clearly identify future economic benefits flowing to the entity from that asset, then it cannot be included in the entities assets schedule.'

'Council has taken the view that it has no control over the purchase, use or sale of any RFS equipment. As such the requirements SAC 4 have not been met and RFS equipment should not be included as assets in Councils accounts.'

'Albury City retains effective control of associated Land and Buildings, but that the RFS retains control of plant and equipment. Accordingly, Albury City's practice is to recognise associated Land and Buildings in its asset schedules, but not Plant and Equipment.'

'It is also considered that in regard to the objectives of financial reporting, councils obligation and commitment to the rural fire fighting function is fully and accurately reflected in the statutory contribution expense made and the net cost of other relevant facilities provided under the local agreement.'

Bellingen Shire Council

65. Bellingen Shire Council prepared a *Position Statement Rural Fire Service Assets Treatment* (November 2017). It is very similar to other councils' positions, and therefore the commonalities not repeated.

66. The following extracts are, however, noteworthy.

'For Bellingen, RFS assets total approximately $7.6M, with an annual depreciation expense of $0.5M per year. Bellingen Shire Council has taken the approach to *not* recognise any RFS assets on their books.'

'Under Bellingen Shire Council's Service Level Agreement with the RFS, the following conditions are in place:

- Council has agreed to allow the RFS and the Commissioner to use the district equipment
- Council has agreed to allow the RFS and the Commissioner to use the premises (per schedule 1 in agreement)
- The Commissioner agrees to maintain the equipment on behalf of the Council
- The RFS will maintain and supply to Council a register of the equipment
- With reference to the financing arrangements, the Commissioner will, by the 28 February each year, submit to Council: a probable allocation of expenditures for the district for the next financial year; and a probable contribution by the Council to the fund, and
- In the event the Commissioner and the Council cannot agree upon the contribution of the Council to the Fund within 28 days of the Commissioner delivering the probable allocation by Council, the Minister (Police and Emergency Services) will make a determination on behalf of the parties.'

'Further to the above, the following observations can be made about the RFS fleet and buildings:

- All RFS vehicles are managed through State Fleet NSW. Council has no control of the type of fleet purchased. Vehicles are insured and registered through State Fleet.
- Council has no control over the vehicles allocated to their RFS district: Council does not have keys or usage of these assets. Vehicles allocated to the district can be used throughout the State without Council consultation or permission.
- Council does not hold keys to the buildings, make decisions about the use of them, has no access to use of, nor earn any income from RFS buildings.'

67. The statement concluded:

1. 'The Accounting Standards require a standard higher than ownership when accounting for assets. Entities may own an asset, but unless they have control of that asset and can clearly identify future economic benefits flowing to the entity from that asset, then it cannot be included in the entities assets schedule.
2. Whilst the RFS Act refers to assets being 'vested' in Council, there is no mention of the Council having 'ownership' of these assets.
3. As per the RFS Act, Council does not receive the proceeds from the sale of the assets. You cannot have control of an asset without also having control of the proceeds.
4. Council do not insure or register the fleet assets, nor do Council hold keys or have access to any of these vehicles. Fleet are used throughout the state without the permission or knowledge of Council. This fails the very basic of asset control tests.
5. Council does not hold keys to the buildings, make decisions about the use of them, has no access to use of, nor earn any income from RFS buildings.
6. RFS (not Councils) receive future economic benefit from firefighting equipment assets in terms of both net cash flows and service provision.
7. Whilst Council has a detailed Rural Fire District Service Agreement, this appears to be an "on paper arrangement only" and does not represent what is happening in practice.
8. RFS make all the decisions about capital improvements and new assets. While Council is consulted, it has no final decision.
9. Should there be any disagreement as to Councils contribution to the fund, the Minister for Police and Emergency Services has the final say.'

68. And finally:

'It is clear that even the most basic of control tests have not been met, the evidence is also compelling that the RFS receives the flow of future economic benefits, not Council. Based on the evidence, Council, in complying with the Accounting Standards, has no choice but to not recognise the RFS Assets.'

Clarence Valley

Background

69. Clarence Valley Council wrote a *Position Statement on the Recognition of Rural Fire Service Assets* dated 3 October 2017. The council stated:

'Clarence Valley Council maintains buildings within its Local Government Area boundary whilst plant and other equipment is fully owned and maintained by RFS. Clarence Valley Council accounts for land and buildings used by the RFS situated within the Clarence Valley Council boundary.'

Application of accounting literature

70. Clarence Valley Council used the same accounting references as Albury City. They are not repeated.

Facts and circumstances

71. Cogent extracts from the statement include:

'The Rural Fire District Service Agreement (RFS 2) between Clarence Valley Council and the Commissioner includes a basic section on District equipment (section 5) and section on Land and Buildings (section 6)'. (The descriptions are the same as Albury City and not repeated.)

'The RFS is funded directly by the State; both operating and capital acquisitions are made directly by RFS Officers. Council has no input into the operations or capital acquisitions of the RFS. The Fire Services Act provides that The NSW Rural Fire Service has the function to provide rural fire services for New South Wales (9(1) (a)). It is considered therefore that it is the Rural Fire Service and not councils that receive future economic benefit from firefighting equipment assets in terms of both net cash flows and service provision.'

Conclusion

72. Clarence Valley Council has reached the same conclusion as Albury City. It is not repeated.

Tamworth Regional Council

73. Tamworth Regional Council prepared a *Position statement on the recognition of Rural Fire Service assets*. It is very similar to other councils' positions and is therefore not repeated.

OLG conversations with councils about the Rural Fire Service's assets

74. The OLG spoke to four councils (28 August 2017) on three issues. Did they recognise land and buildings? Did they write off the trucks in financial statements? Was this arrangement covered by an agreement with the RFS or a district or council?

75. The responses were:

Narrandera Shire Council (Hiscox):

> 'Recognise building and land only – not the red fleet. They don't believe they should recognise the fleet as it does not meet the 8 criteria of control as per the standards. They are covered by a zone agreement which would need to be updated as there are former councils on it. They will provide us with a copy.'

Leeton (Stewart):

> 'Recognise buildings only (they own the land). They do not believe they control the red fleet under the definition of the Standards, they have absolutely no control over the red fleet. They were even told by RFS that they did not have to insure them anymore and that RFS would. When the assets are sold the money goes to RFS and they replace the old with the new.'

Cowra (Scott):

> 'Recognise all assets including the red fleet – they wanted to change the policy but were told that they couldn't – once they have them in the books they had to stay. In their opinion they do not control the red fleet. They depreciate the fleet on the same basis as heavy vehicles. These vehicles turn over quite regularly and are quite expensive. RFS have the final say over these assets.'
>
> Email from Cowra (Stuart) to OLG (Love) dated 29 August 2017. 'Following up on our conversation yesterday regarding RFS assets here is a bit of additional information:
>
> - Bushfire sheds are located on land owned or controlled by Council
> - Bushfire sheds are included on council insurance schedule
> - Council is generally responsible for maintaining the shed although some reimbursement does come from RFS
> - RFS trucks are not under the control of council and can be required to attend fires or other emergencies at other NSW & interstate locations at the direction of RFS
> - RFS trucks are not registered by council
> - RFS are not insured by council
> - RFS trucks are not maintained by council
> - RFS truck maintenance & fuel costs are paid by council (due to the ridiculous funding arrangement) but reimbursed by RFS.'

Tweed (Chorlton):

> 'Recognise the buildings and land – not the red fleet. Does not believe that Council has control of the fleet. Believes the legislation needs to be changed to take out the [vesting] and should be the same as SES. [Agreed] that vested does not mean that councils have control.'

Narrandra Shire Council (Hiscox) email from to Crowe Horwarth (Lucas) headed *Assessment of the RFS Red Fleet as a council asset* and dated 22 September 2017. The email stated:
'Council has considered the following in determining that the RFS Red Fleet should not be booked as an asset on council's balance sheet.

- The items in the Red Fleet are specified and procured in a timeframe determined by the RFS in accordance with the RFS budget. Sale of items is determined by the RFS and proceeds of sale flow to the RFS
- Future economic benefits derived from the Red Fleet accrue to the RFS as the Red Fleet is used to address RFS objectives and service delivery exclusively
- Council has no access to the Red Fleet for any of its purposes
- The RFS determine where the Red Fleet is deployed within the shire and may task the fleet outside the shire

- Council maintain the Red Fleet under direction from the RFS and within a budget set by the RFS
- Council maintains brigade stations under councils building maintenance program and insures the buildings under council's policy
- The RFS has directed council not to insure the Red Fleet under council's motor vehicle cover.'

City of Parramatta (Matthew Walker) exchanged a series of emails with Audit NSW (Celia Withers) headed Rural Fire Assets and dated 23 and 24 September 2017. Relevant extracts from the City of Parramatta correspondence are:

- Extract from section 119(3) of the Rural Fire Services Act 1997 (NSW): 'A council must not sell or otherwise dispose of any firefighting equipment purchased or constructed wholly or partly from money to the credit of the Fund without the written consent of the Commissioner [...] This would indicate that Council does not have control of the assets as it does not possess the right to dispose of assets without consent of the RFS.'
- Extract from section 119(5) of the Rural Fire Services Act 1997 (NSW): 'A council must take care of and maintain in the condition required by the Service Standards any firefighting equipment vested in it under this section.
- 'In operation this is done in accordance within a service agreement with the Local Rural Fire Service Command. This maintenance is included in the annual budget prepared by the Local Rural Fire Command which is submitted to the central Rural Fire Service for approval and includes requests for Capital items to be funded by the Rural Fire Service. Access to Rural Fire Service buildings and equipment is restricted to the personnel (including volunteers) of the local rural fire area command and this indicates that Council cannot just access the assets for utilisation in the course of its daily operations.'
- 'Further highlighting issues with determination of control and the difference of crown land assets under council's care and control, where the access is not restricted nor is an annual budget prepared by another entity for services to be provided.'

Council comments on the draft *Code of Accounting Practice*

76. The OLG sought comments on the draft *Code of Accounting Practice* and some councils responded. The following comments and extracts are cited to help further understanding of the councils' views.

77. *Armidale Regional Council's* Mr Peter Dennis, CEO, stated in a submission to OLG dated 2 February 2018 that:

- AASB 116 *Property, Plant and Equipment* defines 'assets' and 'control of assets' and is the basis for Council's arguments on these terms. (I note that AASB 116 no longer defines these terms).
- 'With regards to Rural Fire Services assets (buildings, plant and equipment), Council is unable to determine there is a future economic benefit, an ability to gain control over the assets, or demonstrate there is a transaction that will give rise to control in future.'
- 'The Council's preferred position is that Rural Fire Services operates and is funded as NSW Fire Brigade and State Emergency Service. Where all that council is required [to do is] to make a financial contribution annually.'
- 'In applying AASB 116, Council should make no reference to Rural Fire Service assets, or recognition in the asset register. In addition, all reference to Rural Fire Service should be removed from the Code.'

78. *Cessnock Council's* Mr Robert Maginnity, director of corporate and community services, provided the following comments:

- 'I agree RFS assets should be recognised, but it should be with the RFS who have control of those assets. This is particularly so for the vehicle fleet. Council has no control of the purchase, disposal or usage of such asset, so to mandate recognition flies firmly in the face of not only common sense, but also the fundamental accounting concept of control.'
- 'RFS assets should only be accounted for by a council if in accordance with the accounting standards they determine that they have control of those assets and can clearly identify future economic benefits flowing to the council from those assets. Due to differing arrangements that are in place at the local level across the State, this may need to be assessed by each council on a case by case basis.'

79. *Finance Network Executive and Local Government Professionals Australia, NSW*, stated (undated):

'It is the view of the Finance Network Executive and Local Government Professionals Australia, NSW, that Rural Fire Service assets should only be accounted for by a council, if in accordance with the accounting standards, they determine that they have control of those assets and can clearly identify future economic benefits flowing to the Council from those assets.'

80. *Mid North Coast Regional Organisation of Councils* (MIDROC) made a submission to the OLG dated 30 January 2018. The submission contained background information and cited what MIDROC considers to be relevant accounting literature. They are not repeated here; these matters have been previously described.

81. MIDROC provided the following summary of a service-level agreement:

'Under councils Service Level Agreement with the RFS, the following conditions are in place:

- Council has agreed to allow the RFS and the Commissioner to use the district equipment;
- Council has agreed to allow the RFS and the Commissioner to use the premises (per schedule 1 in agreement);
- The Commissioner agrees to maintain the equipment on behalf of the Council; and
- The RFS will maintain and supply to Council a register of the equipment.
- With reference to the financing arrangements, the Commissioner will, by the 28 February each year, submit to Council: a probable allocation of expenditures for the district for the next financial year and a probable contribution by the Council to the fund. In the event the Commissioner and the Council cannot agree upon the contribution of the Council to the Fund within 28 days of the Commissioner delivering the probable allocation by Council, the Minister (Police and Emergency Services) will make a determination on behalf of the parties.'

The following observations were made about the RFS fleet and buildings:

- 'All RFS vehicles are managed through State Fleet NSW – Council has no control of the type of fleet purchased; and vehicles are insured and registered through State Fleet.
- Councils have no control over the vehicles allocated to their RFS district – Council does not have keys or usage of these assets; and vehicles allocated to the district can be used throughout the State without Council consultation or permission.
- Councils do not hold keys to the buildings, make decisions about the use of them, has no access to use of, nor earn any income from RFS buildings.'

82. MIDROC summarised its findings as follows:

- 'The Accounting Standards require a standard higher than ownership when accounting for assets. Entities may own an asset, but unless they have control of that asset and can clearly identify future economic benefits flowing to the entity from that asset, then it cannot be included in the entities assets schedule.

- Whilst the RFS Act refers to assets being "vested" in councils, there is no mention of the councils having "ownership" of these assets.
- As per the RFS Act, councils do not receive the proceeds from the sale of the assets. You cannot have control of an asset without also having control of the proceeds.
- Councils do not insure or register the fleet assets, nor do councils hold keys or have access to any of these vehicles. Fleet are used throughout the state without the permission or knowledge of councils. This fails the [most] basic of asset control tests.
- Councils do not hold keys to the buildings, make decisions about the use of them, has no access to use of, nor earn any income from RFS buildings.
- The RFS (not councils) receive future economic benefits from firefighting equipment assets in terms of both net cash flows and service provision.
- Whilst councils have detailed Rural Fire District Service Agreement, this appears to be an "on paper arrangement only" and does not represent what is happening in practice.
- RFS make all the decisions about capital improvements and new assets. While councils are consulted, it has no final decision.
- Should there be any disagreement as member council contributions to the fund, the Minister for Police and Emergency Services has the final say.'

83. MIDROC concluded:
'It is clear that even the most basic of control tests have not been met, the evidence is also compelling that the RFS receives the flow of future economic benefits, not councils.'

84. *Tamworth Shire Council*, Mr Rick Sanderson, stated in a submission dated 2 February 2018:
'Council considers that the only valid point (sic a reference Audit Office final management letter of June 2017) in this is legal ownership and ignores other significant elements of the accounting concept of control. Council's position on this issue is attached showing that we strongly believe that controls lies with RFS (Appendix A).'

85. *Temora Shire Council*, G C Lavelle, general manager, stated (2 February 2018):
'In the Council's view Rural Fire Service assets should only be accounted for by a Council, if in accordance with the accounting standards, they determine that they have control of those assets and can clearly identify future economic benefits flowing to the council from those assets. Temora Shire Council does not have control over the purchase sale, or usage of the Rural Fire Services Assets. We do believe we should recognise these assets in our financial statements.'

86. *Tweed Shire Council's*, Mr Brian Unwin, senior accountant, wrote:
'[The reasons] for local government not reporting RFS assets include, but are not limited to:

- Councils are unable to dispose of or restrict access to these assets – there is no control
- Councils are unable to effectively maintain an asset register for these assets – they have no access to the asset inventories and must rely on accurate and timely information being provided to them by RFS
- As Councils have no authority over the RFS they can't compel the RFS to provide this information
- It is unlikely that RFS will inform Councils when transfers of mobile assets occur between LGAs
- As RFS purchase these assets, acquisitions must be shown on Councils' income statements as non-cash contributions
- As RFS receives the cash for the disposal of these assets, Councils must disclose a loss on disposal when this occurs.

Whether or not legislation vests the legal ownership of these assets to local government, RFS clearly has control of these assets and should be fulfilling its reporting obligations.'

****