

## **New South Wales Local Government**

### **Benchmarking Depreciation**

*CHAIR: What is the way to deal with depreciation? Could you suggest to the inquiry how we could deal with that to get a benchmark that works for New South Wales, given all other issues that you have to deal with? There must be an answer for standardising that a little better.*

For depreciation benchmarking to occur across NSW Local Government there must be a uniform way in which each Council calculates its depreciation expense.

There are various factors that are involved in the annual calculation of a Council's depreciation expense. The main factors include:

- The method of depreciation used;
- The useful lives allocated to each asset; and
- The valuation methods for assets.

The three (3) main factors listed above involve a great level of subjective judgment to be made, with these judgements usually being made collaboratively by councils accounting and engineering departments.

The method of calculating depreciation is not mandated by the Local Government Code of Accounting Practice and Financial Reporting (the 'Code') and consequently is determined by each individual Council. The Code states:

*"a variety of depreciation methods can be used to allocate the depreciable amount of an asset on a systematic basis over its useful life. These methods include the straight-line method, the diminishing balance method, and the units of production method."*

**There should be a mandated depreciation method for Local Government to help achieve more comparable depreciation expenses across the industry.**

The useful life that is allocated to an asset is not mandated by the Code and is determined by each individual council. The Code stipulates that a Council must disclose the useful lives used, however it does not proscribe what those useful lives must be.

In regards to standardising depreciation, this is where the major dissensions occur. As a result of their geographical location, traffic volumes, geological compositions, etc. some Councils' assertion is that their assets' lives are longer or shorter than that of the average Council.

As a minimum and for ease of application, the straight line depreciation method should be adopted. The NSW Office of Local Government should then develop depreciation models for the different asset classes and make it mandatory for them to be used for depreciation.

**The useful lives that are to be applied to each of Council's assets should be mandated to help achieve more comparable depreciation expenses across the industry.**

There are other factors that influence the resulting depreciation costs of each particular council. Those factors include the unit values used in determining the fair value of a council's assets and the level of componentisation that is applied to each of the asset classes. However, similarly to the depreciation calculation, standardising the way in which these are applied across the industry will help increase comparability.

**The only solution to standardising depreciation is to mandate the way in which depreciation is calculated.**

Most importantly, this type of standardisation is achievable. Over the last three years South Sydney Region of Councils (SSROC) have been developing a standardised Strategic Asset Management Framework across all sixteen (16) member Councils, which includes the depreciation issue.

To date twelve (12) out of the sixteen (16) member Councils have agreed with a standardised 'SSROC' approach to asset life cycles, with discussions being held with the remaining four Councils to ensure a common approach.