Statement of Accounting Policies

FOR THE YEAR ENDED 30 JUNE 2008

Reporting Entity

Kaikoura District Council is a territorial local authority governed by the Local Government Act 2002.

The Kaikoura District Council group (KDC) consists of Kaikoura District Council and its subsidiary, the Kaikoura Enhancement Trust, a charitable Trust 100% owned by Council. That Trust in turn owns 100% of Innovative Waste Kaikoura Ltd.

The Council has an 11.5% interest in the Marlborough Regional Forestry joint venture.

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

The financial statements of KDC are for the year ended 30 June 2008. The financial statements were authorised for issue by Council on 31 October 2008.

Basis of Preparation

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

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

Accounting Policies

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

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

The financial statements are presented in New Zealand dollars and all values are rounded to the nearest dollar. The functional currency of KDC is New Zealand dollars.

Standards, amendments and interpretations issued that are not yet effective and have not been early adopted

Standards, amendments and interpretations issued but are not yet effective that have not been early adopted, and which are relevant to KDC include:

- NZ IAS 1 *Presentation of Financial Statements (revised 2007)* replaces NZ IAS 1 *Presentation of Financial Statements (issued 2004)* and is effective for reporting periods beginning on or after 1 January 2009. The revised standard requires information in financial statements to be aggregated on the basis of shared characteristics and introduces a statement of comprehensive income. The statement of comprehensive income will enable readers to analyse changes in equity arising from non-owner changes separately from transactions with owners. The revised standard gives KDC the option of presenting items of income and expense and components of other comprehensive income either in a single statement of comprehensive income with subtotals, or in two separate statements (a separate income statement followed by a statement of comprehensive income). KDC intends to adopt the standard for the year ended 30 June 2010, and is yet to decide whether it will prepare single statements or two separate statements.

- NZ IAS 23 *Borrowing Costs (revised 2007)* replaces NZ IAS 23 *Borrowing Costs (issued 2004)* and is effective for reporting periods beginning on or after 1 January 2009. The revised standard requires all borrowing costs to be capitalised if they are directly attributable to the acquisition, construction or production of a qualifying asset. The revised standard will also require borrowing costs to be considered when revaluing property, plant and equipment to fair value based on depreciated replacement cost. Any necessary adjustments to depreciated replacement cost will have flow on effects to depreciation expense. KDC intends to adopt this standard for the year ending 30 June 2010 and has not yet quantified the potential impact of the new standard.
- NZ IFRS 3 *Business Combinations (revised 2008)* and the amended NZ IAS 27 *Consolidated and Separate Financial Statements* are effective for reporting periods beginning on or after 1 July 2009 and must be applied prospectively from that date. The main changes the revised NZ IFRS 3 and the amended NZ IAS 27 will make to existing requirements or practice are:
    - Partial acquisitions – non-controlling interests are measured either as their proportionate interest in the net identifiable assets (which is the original NZ IFRS 3 requirement) or at fair value.
    - Step acquisitions – the requirement to measure at fair value every asset and liability at each step for the purposes of calculating a portion of goodwill has been removed. Instead, goodwill is measured as the difference at acquisition date between the fair value of any investment in the business before the acquisition, the consideration transferred and the net assets acquired.
    - Acquisition-related costs – these are generally recognised as expenses (rather than included in the cost of acquisition)
    - Contingent consideration – this must be recognised and measured at fair value at the acquisition date. Subsequent changes in fair value are recognised in accordance with other NZ IFRS's, usually in profit or loss.

  KDC will adopt the revised NZ IFRS 3 and amended NZ IAS 27 for the year ended 30 June 2010, which will impact on business combinations that occur on or after 1 July 2009.

Subsidiaries

KDC consolidates as subsidiaries in the Group financial statements all entities where KDC has the capacity to control their financing and operating policies so as to obtain benefits from the activities of the entity. This power exists where KDC controls the majority voting power on the governing body or where such policies have been irreversibly predetermined by KDC or where the determination of such policies is unable to materially impact the level of potential ownership benefits that arise from the activities of the subsidiary.

KDC measures the cost of a business combination as the aggregate of the fair values, at the date of exchange, of assets given, liabilities incurred or assumed, in exchange for control of the subsidiary plus any costs directly attributable to the business combination.

Basis of consolidation

The purchase method is used to prepare the consolidated financial statements, which involves adding together like items of assets, liabilities, equity, income and expenses on a line-by-line basis. All significant intragroup balances, transactions, income and expenses are eliminated on consolidation.

KDC's investments in its subsidiaries are carried at cost in KDC's own "parent entity" financial statements.

Joint ventures

A joint venture is a contractual arrangement whereby two or more parties undertake an economic activity that is subject to joint control. For jointly controlled operations KDC recognises in its financial statements its share of the assets that it controls, the liabilities and expenses it incurs, and the share of income that it earns from the joint venture.

Of KDC's interest in the Marlborough Regional Forestry joint venture, 13.37% is held in trust on behalf of Environment Canterbury. This is recognised as a non-current liability in the financial statements.

Revenue

Revenue is measured at the fair value of consideration received.

Rates revenue

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

Other revenue

Water billing revenue is recognised on an accrual basis. Unbilled usage, as a result of unread meters at year end, is accrued on an average usage basis.

KDC receives government grants from Land Transport New Zealand, which subsidises part of KDC's costs in maintaining the local roading infrastructure. The subsidies are recognised as revenue upon entitlement as conditions pertaining to eligible expenditure have been fulfilled.

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

Sales of goods are recognised when a product is sold to the customer. Sales are usually in cash or by credit card. The recorded revenue is the gross amount of the sale, including credit card fees payable for the transaction. Such fees are included in other expenses.

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

Where revenue is derived by acting as an agent for another party, the revenue that is recognised is the commission or fee on the transaction.

Interest income is recognised using the effective interest method.

Development contributions

The revenue recognition point for development and financial contributions is at the later of the point when KDC is ready to provide the service for which the contribution was levied, or the event that will give rise to a requirement for a development or financial contribution under the legislation.

Borrowing Costs

Borrowing costs are recognised as an expense in the period in which they are incurred.

Grant Expenditure

Non-discretionary grants are those grants that are awarded if the grant application meets the specified criteria and are recognised as expenditure when an application that meets the specified criteria for the grant has been received.

Discretionary grants are those grants where KDC has no obligation to award on receipt of the grant application and are recognised as expenditure when a successful applicant has been notified of the KDC's decision.

Income Tax

Income tax expense in relation to the surplus or deficit for the period comprises current tax and deferred tax.

Current tax is the amount of income tax payable based on the taxable profit for the current year, plus any adjustments to income tax payable in respect of prior years. Current tax is calculated using rates that have been enacted or substantially enacted by balance date.

Deferred tax is the amount of income tax payable or recoverable in future periods in respect of temporary differences and unused tax losses. Temporary differences are differences between the carrying amount of assets and liabilities in the financial statements and the corresponding tax bases used in the computation of taxable profit.

Deferred tax liabilities are generally recognised for all taxable temporary differences. Deferred tax assets are recognised to the extent that it is probable that taxable profits will be available against which the deductible temporary differences or tax losses can be utilised.

Deferred tax is not recognised if the temporary difference arises from the initial recognition of goodwill or from the initial recognition of an asset and liability in a transaction that is not a business combination, and at the time of the transaction, affects neither accounting profit nor taxable profit.

Deferred tax is recognised on taxable temporary differences arising on investments in subsidiaries and associates, and interests in joint ventures, except where the company can control the reversal of the temporary difference and it is probable that the temporary difference will not reverse in the foreseeable future.

Deferred tax is calculated at the tax rates that are expected to apply in the period when the liability is settled or the asset is realised, using tax rates that have been enacted or substantially enacted by balance date.

Current tax and deferred tax is charged or credited to the income statement, except when it relates to items charged or credited directly to equity, in which case the tax is dealt with in equity.

Leases

<u>Finance leases</u>

A finance lease is a lease that transfers to the lessee substantially all the risks and rewards incidental to ownership of an asset, whether or not title is eventually transferred.

At the commencement of the lease term, KDC recognises finance leases as assets and liabilities in the statement of financial position at the lower of the fair value of the leased item or the present value of the minimum lease payments.

The amount recognised as an asset is depreciated over its useful life. If there is no certainty as to whether KDC will obtain ownership at the end of the lease term, the asset is fully depreciated over the shorter of the lease term and its useful life.

<u>Operating leases</u>

An operating lease is a lease that does not transfer substantially all the risks and rewards incidental to ownership of an asset. Lease payments under an operating lease are recognised as an expense on a straight-line basis over the lease term.

Cash and Cash Equivalents

Cash and cash equivalents includes cash in hand, deposits held at call with banks, other short-term highly liquid investments with original maturities of three months or less, and bank overdrafts.

Bank overdrafts are shown within borrowings in current liabilities in the statement of financial position.

Trade and Other Receivables

Trade and other receivables are initially measured at fair value and subsequently measured at amortised cost using the effective interest method, less any provision for impairment.

Loans, including loans to community organisations made by KDC at nil, or below market interest rates are initially recognised at the present value of their expected future cash flows, discounted at the current market rate of return for a similar asset/investment. They are subsequently measured at amortised cost using the effective interest method. The difference between the face value and present value of the expected future cash flows of the loan is recognised in the statement of financial performance as a grant.

A provision for impairment of receivables is established when there is objective evidence that KDC will not be able to collect all amounts due according to the original terms of receivables. The amount of the provision is the difference between the asset's carrying amount and the present value of estimated future cash flows, discounted using the effective interest method.

Financial Assets

KDC classifies its financial assets into the following four categories: financial assets at fair value through profit or loss, held-to-maturity investments, loans and receivables and financial assets at fair value through equity. The classification depends on the purpose for which the investments were acquired. Management determines the classification of its investments at initial recognition and re-evaluates this designation at every reporting date.

Financial assets and liabilities are initially measured at fair value plus transaction costs unless they are carried at fair value through profit or loss in which case the transaction costs are recognised in the statement of financial performance.

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

The fair value of financial instruments that are not traded in an active market is determined using valuation techniques. KDC uses a variety of methods and makes assumptions that are based on market conditions existing at each balance date. Quoted market prices or dealer quotes for similar instruments are used for long-term debt instruments held. Other techniques, such as estimated discounted cash flows, are used to determine fair value for the remaining financial instruments.

The four categories of financial assets are:

- <u>Financial assets at fair value through profit or loss</u>

  This category has two sub-categories: financial assets held for trading, and those designated at fair value through profit or loss at inception. A financial asset is classified in this category if acquired principally for the purpose of selling in the short term or if so designated by management. Assets in this category are classified as current assets if they are either held for trading or are expected to be realised within 12 months of the balance sheet date.

  After initial recognition they are measured at their fair values. Gains or losses on remeasurement are recognised in the statement of financial performance.

  Currently, KDC does not hold any financial assets in this category.

- <u>Loans and receivables</u>

  These are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market.

  After initial recognition they are measured at amortised cost using the effective interest method. Gains and losses when the asset is impaired or derecognised are recognised in the statement of financial performance. Loans and receivables are classified as "prepayments and receivables" in the statement of financial position.

- <u>Held to maturity investments</u>

  Held to maturity investments are assets with fixed or determinable payments and fixed maturities that KDC has the positive intention and ability to hold to maturity.

  After initial recognition they are measured at amortised cost using the effective interest method. Gains and losses when the asset is impaired or derecognised are recognised in the statement of financial performance.

  Investments in this category include: local authority and government stock, sinking funds and bank term deposits.

- <u>Financial assets at fair value through equity</u>

  Financial assets at fair value through equity are those that are designated as fair value through equity or are not classified in any of the other categories above.

  This category encompasses:

  Investments that KDC intends to hold long-term but which may be realised before maturity; and shareholdings that KDC holds for strategic purposes. KDC's investment in its subsidiary is not included in this category as it is held at cost (as allowed by NZ IAS 27 Consolidated and Separate Financial Statements) whereas this category is to be measured at fair value.

After initial recognition these investments are measured at their fair value.

Gains and losses are recognised directly in equity except for impairment losses, which are recognised in the statement of financial performance. In the event of impairment, any cumulative losses previously recognised in equity will be removed from equity and recognised in the statement of financial performance even though the asset has not been derecognised.

On derecognisation the cumulative gain or loss previously recognised in equity is recognised in the statement of financial performance.

Currently Council does not have any assets in this category.

Impairment of Financial Assets

At each balance sheet date KDC assesses whether there is any objective evidence that a financial asset or group of financial assets is impaired. Any impairment losses are recognised in the statement of financial performance.

Non-Current Assets Held for Sale

Non-current assets held for sale are classified as held for sale if their carrying amount will be recovered principally through a sale transaction, not through continuing use. Non-current assets held for sale are measured at the lower of their carrying amount and fair value less costs to sell.

Any impairment losses for write-downs of non-current assets held for sale are recognised in the statement of financial performance.

Any increases in fair value (less costs to sell) are recognised up to the level of any impairment losses that have previously been recognised.

Non-current assets (including those that are part of a disposal group) are not depreciated or amortised while they are classified as held for sale. Interest and other expenses attributable to the liabilities of a disposal group classified as held for sale continue to be recognised.

Property, Plant and Equipment

Property, plant and equipment consists of:

- <u>Operational assets</u>
  These include land, buildings, harbour assets, library books, plant and equipment, and motor vehicles.

- <u>Restricted assets</u>
  Restricted assets are parks and reserves owned by KDC which provide a benefit or service to the community and cannot be disposed of because of legal or other restrictions.

- <u>Infrastructure assets</u>
  Infrastructure assets are the fixed utility systems owned by KDC. Each asset class includes all items that are required for the network to function, for example, sewer reticulation includes reticulation piping and sewer pump stations.

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

<u>Additions</u>

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

In most instances, an item of property, plant and equipment is recognised at cost. Where an asset is acquired at no cost, or for nominal cost, it is recognised at fair value as at the date of acquisition.

<u>Disposals</u>

Gains and losses on disposals are determined by comparing the proceeds with the carrying amount of the asset. Gains and losses on disposals are included in the statement of financial performance. When revalued assets are sold, the amounts included in asset revaluation reserves in respect of those assets are transferred to retained earnings.

<u>Subsequent costs</u>

Costs incurred subsequent to initial acquisition are capitalised only when it is probable that future economic benefits or service potential associated with the item will flow to KDC and the cost of the item can be measured reliably.

Depreciation

Depreciation is provided on a straight-line basis on all property, plant and equipment other than land, at rates which will write off the cost (or valuation) of the assets to their estimated residual values over their useful lives. The estimated useful economic lives of major classes of assets have been estimated as follows:

Infrastructural Assets	**Years**	**Rate (Rounded)**
Roading		
Land and Road Formation		Not Depreciated
Base Course	50	2%
Bridges	67	1.5%
Sealed Top Layer	12	8.3%
Kerb and Channels	100	1%
Drainage	75	1.3%
Traffic Facilities	8	12.5%
Seawalls	45	2.2%
Footpaths – Structure		Not Depreciated
Footpaths – Surface	12	8.3%
Street Lighting	12	8.3%
Sewerage		
Land		Not Depreciated
Buildings	50	2%
Equipment and Pump Stations	50	2%
Rising Mains/Gravity Reticulation	25 – 77	From 1.3% to 4.0%
Water		
Rural Water Supplies	50	2%
Land		Not Depreciated

Buildings and Equipment	50	2%
Intake Gallery	77	1.3%
Chlorine Treatment Facility	20	5%
Groundwater Bores and Pumps	20 – 60	From 1.7% to 5.0 %
Pressure Mains	50 – 77	From 1.3% TO 2.0%
Valves and Fittings	15 – 50	From 2.0% to 6.7%
Stormwater		
Manholes, Outlets, Pipes	44 – 72	From 1.4% to 2.3%
Drums	8	12.5%
Operational Assets		
Landfill Post Closure	40	2.5%
Buildings – Structure	50	2%
Buildings – Services	30	3.33%
Buildings – Internal Fit out	5	20%
Harbour Seawall	50	2%
Computer Equipment	5	20%
Plant, Vehicles and Machinery	5	20%
Land		Not Depreciated
Library books	12	8.33%
Library non-books	5	20%
Restricted Assets		
Parks and Reserves Buildings	50	2%
Parks and Reserves Land		Not Depreciated

In relation to infrastructural assets, depreciation has been calculated at a component level based on the estimated remaining useful lives as assessed by Council's engineers and independent registered valuers. A summary of these lives is detailed above. The residual value and useful life of an asset is reviewed, and adjusted if applicable, at each financial year-end.

Revaluation

Those asset classes that are revalued are valued on a three yearly cycle on the basis described below. All other asset classes are carried at depreciated historical cost. The carrying values of revalued items are reviewed at each balance date to ensure that those values are not materially different to fair value.

<u>Operational land and buildings</u>

At fair value as determined from market-based evidence by an independent valuer. The most recent valuation was performed by Sarah Rowse, (ANZIV, SPINZ) of Quotable Value New Zealand, and the valuation is effective as at 30 June 2007, and included all assets not valued as at 30 June 2006. Several key properties; the Council office, Memorial Hall, pensioner flats and the swimming pool, were valued to component level by Sarah Rowse, (ANZIV, SPINZ) of Quotable Values as at 30 June 2006. Carrying values for those specific assets are shown less accumulated depreciation and plus any subsequent additions at cost.

<u>Restricted land and buildings</u>

At fair value as determined from market-based evidence by an independent valuer. The most recent valuation was performed by Sarah Rowse, (ANZIV, SPINZ) of Quotable Value New Zealand, and the valuation is effective as at 30 June 2007. Additions are recorded at cost.

Infrastructure

This includes roads, bridges & footpaths, water systems, sewerage systems and stormwater systems

At fair value determined on a depreciated replacement cost basis by an independent valuer. At balance date KDC assesses the carrying values of its infrastructure assets to ensure that they do not differ materially from the assets' fair values. If there is a material difference, then the off-cycle asset classes are revalued. The most recent roading valuation was performed by Murray Fletcher, Chartered Engineer, of Connell Wagner Ltd, and the valuation is effective as at 30 June 2007. The most recent water, sewerage and stormwater valuations were performed by Martin Dasler, Chartered Engineer, of Connell Wagner Ltd, and the valuation is effective as at 30 June 2007. All infrastructure asset classes carried at valuation were valued. Additions are recorded at cost.

Deemed Cost

Land under roads

Land under roads, was valued based on fair value of adjacent land determined by Connell Wagner Ltd effective 30 June 2001. Under NZ IFRS, KDC has elected to use the fair value of land under roads as at 30 June 2001 as deemed cost. Land under roads is no longer revalued.

Library collections

Library Books were valued at 30 June 2007 using actual cost per book, by the Kaikoura District Librarian.

Accounting for revaluations

KDC accounts for revaluations of property, plant and equipment on a class of asset basis.

The results of revaluing are credited or debited to an asset revaluation reserve for that class of asset. Where this results in a debit balance in the asset revaluation reserve, this balance is expensed in the statement of financial performance. Any subsequent increase on revaluation that off-sets a previous decrease in value recognised in the statement of financial performance will be recognised first in the statement of financial performance up to the amount previously expensed, and then credited to the revaluation reserve for that class of asset.

Forestry Assets

Forestry assets owned via the Marlborough Regional Forestry joint venture, and also Council's own forestry assets, are independently revalued annually at fair value less estimated point of sale costs. These valuations are performed by Merrill & Ring Ltd. Fair value is determined based on the present value of expected net cash flows discounted at a current market determined pre-tax rate.

Gains or losses arising on initial recognition of forestry assets at fair value less estimated point of sale costs and from a change in fair value less estimated point of sale costs are recognised in the statement of financial performance.

The costs to maintain the forestry assets are included in the statement of financial performance.

Investment Property

Properties leased to third parties under operating leases are classified as investment property unless the property is held to meet service delivery objectives, rather than to earn rentals or for capital appreciation.

Investment property is measured initially at cost, including transaction costs.

After initial recognition, KDC measures all investment property at fair value as determined annually by an independent valuer, Quotable Values.

Gains and losses arising from a change in the fair value of investment property are recognised in the statement of financial performance.

Impairment of Non-Financial Assets

Non-financial assets that have an indefinite useful life are not subject to amortisation and are tested annually for impairment. Assets that have a finite useful life are reviewed for impairment whenever events and changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss is recognised for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs to sell and value in use.

Value in use is depreciated replacement cost for an asset where the future economic benefits or service potential of the asset are not primarily dependent on the assets ability to generate net cash flows and where the entity would, if deprived of the asset, replace it's remaining future economic benefits or service potential.

The value in use for cash-generating assets is the present value of expected future cash flows.

If an asset's carrying amount exceeds its recoverable amount the asset is impaired and the carrying amount is written down to the recoverable amount. For revalued assets the impairment loss is recognised against the revaluation reserve for that class of asset. Where that results in a debit balance in the revaluation reserve, the balance is recognised in the statement of financial performance.

For assets not carried at a revalued amount, the total impairment loss is recognised in the statement of financial performance.

The reversal of an impairment loss on a revalued asset is credited to the revaluation reserve. However, to the extent that an impairment loss for that class of asset was previously recognised in the statement of financial performance, a reversal of the impairment loss is also recognised in the statement of financial performance.

For assets not carried at a revalued amount, the reversal of an impairment loss is recognised in the statement of financial performance.

Employee Benefits

<u>Short-term benefits</u>

Employee benefits that KDC expects to be settled within twelve months of balance date are measured at nominal values based on accrued entitlements at current rates of pay.

These include salaries and wages accrued up to balance date, annual leave earned to, but not yet taken at balance date, and sick leave.

KDC recognises a liability for sick leave to the extent that absences in the coming year are expected to be greater than the sick leave entitlements earned in the coming year. The amount is calculated based on the unused sick leave entitlement that can be carried forward at balance date, to the extent that KDC anticipates it will be used by staff to cover those future absences.

KDC recognises a liability and an expense for bonuses where contractually obliged or where there is a past practice that has created a constructive obligation.

Long-term benefits

Superannuation schemes

Obligations for contributions to defined contribution superannuation schemes are recognised as an expense in the statement of financial performance as incurred.

KDC belongs to the Defined Benefit Plan Contributors Scheme (the scheme), which is managed by the Board of Trustees of the National Provident Fund. The scheme is a multi-employer defined benefit scheme.

Insufficient information is available to use defined benefit accounting, as it is not possible to determine from the terms of the scheme, the extent to which the surplus/(deficit) will affect future contributions by individual employers, as there is no prescribed basis for allocation. The scheme is therefore accounted for as a defined contribution scheme.

Provisions

KDC recognises a provision for future expenditure of uncertain amount or timing when there is a present obligation (either legal or constructive) as a result of a past event, it is probable that expenditures will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation. Provisions are not recognised for future operating losses.

Provisions are measured at the present value of the expenditures expected to be required to settle the obligation using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the obligation. The increase in the provision due to the passage of time is recognised as an interest expense.

Borrowings

Borrowings are initially recognised at their fair value. After initial recognition, all borrowings are measured at amortised cost using the effective interest method.

Equity

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

The components of equity are:

Public equity – accumulated funds
Special reserves
Special funds
Asset revaluation reserves

Special and Council Created Reserves

Special reserves are a component of equity generally representing a particular use to which various parts of equity have been assigned. Reserves may be legally restricted or created by KDC.

Restricted reserves are those subject to specific conditions accepted as binding by KDC and which may not be revised by KDC without reference to the Courts or a third party. Transfers from these reserves may be made only for certain specified purposes or when certain specified conditions are met.

Council created reserves are reserves restricted by Council decision. The Council may alter them without references to any third party or the Courts. Transfers to and from these reserves are at the discretion of the Council.

Goods and Services Tax (GST)

All items in the financial statements are stated exclusive of GST, except for receivables and payables, which are stated on a GST inclusive basis. Where GST is not recoverable as input tax then it is recognised as part of the related asset or expense.

The net amount of GST recoverable from, or payable to, the Inland Revenue Department (IRD) is included as part of receivables or payables in the statement of financial position.

The net GST paid to, or received from the IRD, including the GST relating to investing and financing activities, is classified as an operating cash flow in the statement of cash flows.

Commitments and contingencies are disclosed exclusive of GST.

Budget Figures

The budget figures are those approved by the Council at the beginning of the year in the annual plan, after a period of consultation with the public. The budget figures have been prepared in accordance with NZ GAAP, using accounting policies that are consistent with those adopted by KDC for the preparation of the financial statements.

Cost Allocation

KDC has derived the cost of service for each significant activity of the Council using the cost allocation system outlined below.

Direct costs are those costs directly attributable to a significant activity. Indirect costs are those costs, which cannot be identified in an economically feasible manner, with a significant activity.

Direct costs are charged directly to significant activities. Indirect costs are allocated to Council activities on a percentage of use basis.

Critical Accounting Estimates and Assumptions

In preparing these financial statements, KDC has made estimates and assumptions concerning the future. These estimates and assumptions may differ from the subsequent actual results. Estimates and judgements are continually evaluated and are based on historical experience and other factors, including expectations or future events that are believed to be reasonable under the circumstances. The estimates and assumptions that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year are discussed below:

Landfill aftercare provision

Note 10 discloses an analysis of the exposure of KDC in relation to the estimates and uncertainties surrounding the landfill aftercare provision.

Infrastructural assets

There are a number of assumptions and estimates used when performing DRC valuations over infrastructural assets. These include:

- The physical deterioration and condition of an asset, for example the Council could be carrying an asset at an amount that does not reflect its actual condition. This is particularly so for those assets, which are not visible, for example stormwater, wastewater and water supply pipes that are underground. This risk is minimised by Council performing a combination of physical inspections and condition modelling assessments of underground assets;
- Estimating any obsolescence or surplus capacity of an asset;
- Estimates are made when determining the remaining useful lives over which the asset will be depreciated. These estimates can be impacted by the local conditions, for example weather patterns and traffic growth. If useful lives do not reflect the actual consumption of the benefits of the asset, then KDC could be over or under-estimating the annual depreciation charge recognised as an expense in the statement of financial performance. To minimise this risk, KDC's infrastructural asset useful lives have been determined with reference to the NZ Infrastructural Asset Valuation and Depreciation Guidelines published by the National Asset Management Steering Group, and have been adjusted for local conditions based on past experience. Asset inspections, deterioration and condition modelling are also carried out regularly as part of KDC's asset management planning activities, which gives KDC further assurance over its useful life estimates.

Experienced independent valuers perform the Council's infrastructural asset revaluations.

Critical Judgements in Applying KDC's Accounting Policies

Management has exercised the following critical judgements in applying KDC's accounting policies for the period ended 30 June 2008:

Classification of property

KDC owns a number of properties, which are maintained primarily to provide housing to pensioners. The receipt of market-based rental from these properties is incidental to holding these properties. These properties are held for service delivery objectives as part of KDC's social housing policy. These properties are accounted for as property, plant and equipment.

Statement of Cash Flows

Cash means cash balances on hand, held in bank accounts, demand deposits and other highly liquid investments, with original maturities of three months or less, in which Council invests as part of its day-to-day cash management.

Operating activities include cash received from all income sources and cash payments made for the supply of goods and services. Agency transactions (the collection of Regional Council rates) are recognised as receipts and payments in the Statement of Cash Flows because they flow through the Council's main bank account.

Investing activities are those activities relating to the acquisition and disposal of non-current assets.

Financing activities comprise the change in equity and debt structure of the Council.

Cost of Service Statements

The cost of service statements, as provided in the Statement of Service Performance, report the net cost of services for significant activities of the Council, and are represented by the costs of providing the service less all revenue that can be allocated to these activities.

Changes in Accounting Policy

There have been no significant changes in accounting policies. The accounting policies have been applied on a basis consistent with those used last year.