

Report 99.303
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Report to the Policy and Finance Committee
from Greg Schollum, Chief Financial Officer

Accounting Policy – Silviculture Costs

1. Purpose

To seek approval to amend Council's current accounting policy in relation to the treatment of forestry silviculture costs.

2. Background

The current accounting policy in relation to silviculture costs requires all such costs to be expensed when they are incurred. This gives the appearance within the forestry activities (Plantation Forestry within Utility Services and Reserve Forests within Wairarapa) that the Council is borrowing to fund large operating deficits.

This is a very conservative treatment (and arguably misleading) in that the silviculture work is carried out because it adds value to the forestry investment (or it would not be carried out).

3. Proposed Accounting Treatment

I am proposing that Council's accounting policy be changed so that silviculture costs are capitalised (ie added to the value of the forestry investment) rather than expensed, with effect from 1 July 1999. I would prefer that the proposed treatment be reflected in the 1999/2000 Annual Plan so that actuals and budgets for the 1999/2000 year and beyond were "in sync".

The proposed change in treatment will not affect rates as the forestry areas are required to return an internal dividend, irrespective of the operating surplus position.

Both the Divisional Managers affected by this suggested change concur with my proposal.

4. Why Change the Accounting Policy?

I consider that changing the accounting policy will have the following benefits:

- It will mean the forestry areas (and the Council as a whole) will report a more accurate operating surplus/deficit position. (Removing silviculture costs will increase the operating surplus by approximately \$500,000 per annum).
- It will show the continued borrowing in the forestry areas as being more prudent, in that it will reduce the unfortunate impression of the Council “borrowing to pay for the groceries”.
- It will gradually close the gap between the current book value of the forestry investment of approximately \$13m and its real value of approximately \$30m (ie the accounting treatment will progressively become more meaningful).

5. Communications

The change in accounting policy, if approved, needs to be included within both the 1999/2000 Annual Plan and the 1999/2000 Annual Report. I do not consider that any additional communication is required.

6. Recommendations

- (1) *That the report be received and the contents noted.*
- (2) *That the Committee recommend to Council that the current accounting policy in relation to silviculture costs be changed so that such costs are capitalised with effect from 1 July 1999.*

GREG SCHOLLUM
Chief Financial Officer

