LOCAL COUNCIL FINANCIAL MANAGEMENT: ASSESSING THE IMPACT OF POLICY CHANGE AND PROPOSED ALMAGAMATIONS

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ABSTRACT New South Wales (NSW) councils are tasked with providing a wide range of resources and services to their communities. However, the conditions and rules under which councils are allowed to operate are not constant. Changes in state government policies and political affiliation have the capacity to alter the focus and rules under which councils function. Political and economic events result in new and sometimes radically different requirements with which councils are required to conform. As policies change, reforms are introduced and the political landscape alters, councils are expected to alter their actions to coincide with expectations of the state government, while still meeting the needs and expectations of their respective communities.

This paper evaluates the way that councils have reacted to changes in investment policy prior, and subsequent to, the Global Financial Crisis (GFC) and compares those actions to those currently being undertaken by councils in response to the state government review of local councils with a particular focus on measures of financial viability. The purpose is to demonstrate how council's actions are influenced by changes to policy and requirements of the state government and to consider the role that accounting plays in facilitating council's actions. One purpose of financial reports is to provide information to assist users to make valid and informed decisions, to aid planning and inform strategic decision making. Financial reports which are affected by changing

requirements due to the political environment, future financial and governance decisions will also be impacted.

KEYWORDS Local councils, policy, amalgamation, investment, accounting.

1. INTRODUCTION

Policy (and changes to policy) have the capacity to significantly influence the actions of councils. This paper considers the impact that changes in investment policies had on the behaviour of councils prior and subsequent to the GFC. The policies governing the types of products which councils were allowed to invest in have changed over time. From 2000 through to 2007 (the time of the GFC) the policies concerned with the products in which NSW councils were permitted to invest gradually became more relaxed. Accordingly councils were able to choose the level of risk that they were willing to embrace. Following the GFC the policies were tightened and councils were only allowed to invest in capital secured products, primarily within government backed term investments such as term deposits in the big four banks. Behaviour of investment managers within councils varied substantially over that time, primarily due to either their personal preferences, or the internal policies of their respective councils. The state government investment policies established the outer boundaries, yet within individual councils, acceptance of risk by finance managers, or those that determine individual council policies, either added further constraints to investment practices or meant that investments on the edge of state government constraints were pursued. This phenomenon is examined through the lens of Bourdieu's (1977) habitus. We suggest that the differing habitus within councils served to influence each body's level of risk acceptance. Further, it is likely that habitus in some councils also provided differing levels of governance of actions by the finance officers.

This paper also reviews how the current rhetoric by the state government, in respect to the financial management of local councils, has influenced behaviour and actions of those charged with financial management duties. NSW councils have been warned that those councils whose financial performance is assessed as unfit may be faced with forced amalgamation. This assessment has been conducted by the Independent Pricing and Regulatory Tribunal (IPART, 2015). Councils have therefore been incentivised to consider ways that they can improve their financial performance (or at least the perception) and avoid amalgamation. We speculate that accounting has been used to shape the

perceptions of the users of financial reports and has also been implicated in influencing the behaviour of officers within local councils.

A primary function of financial reports is to provide decision useful information for the users of the reports (AASB, 1990). This relies on the information in the financial reports being relevant and reliable. If the reports are inaccurate or information is omitted, then the decision usefulness is diminished. This means that those charged with governance who are seeking to make informed decisions will make them without the proper knowledge. Strategic decisions rely on accurate information to develop both short and long term plans. It is important that financial reports are free from error or confusion to properly inform the decision making process.

2. ROLE OF COUNCILS

Local councils in Australia hold a unique position in the Australian political arena. They have no statutory authority or power of their own, yet they are tasked with providing a wide range of services to their communities. Such communities are both metropolitan and regional in nature. While federal and state governments have their authority ensconced within the constitution, with their power to operate and raise funds clearly established, local councils in all Australian state and territory jurisdictions exist and operate solely under the authority of their respective state/territory governments. Local councils are able to operate with some degree of autonomy, yet at the same time their actions are also constrained by limits determined by the state/territory government. These limits are disseminated to the councils and enforced through the provision of legislative rulings, policies, circulars and procedures. Democratically elected councillors, who have the responsibility to provide direction for each local council, normally oversee them. However, those councillors may be removed and replaced with administrators appointed by the state government at any time if the state government perceives this is necessary.

Individual state and territory governments are responsible for specifying the powers and responsibilities of the local council entities within each state (Boon *et al.*, 2005). The Commonwealth Constitution does not mention local councils (Stilwell and Troy, 2000, p. 115) and as such they have no legal standing at the federal level. As a result, local council's authority to supply community services and generate revenue

through rates is vested in the power granted to them by the respective state governments (Brown, 2005). Local governments receive financial support from state and federal agencies and are accountable to those agencies for delivery of projects and services (Walker and Jones, 2006).

To varying extents local councils are reliant on federal and state government funding, yet prior research (Kloot, 1999) has shown that there are only low levels of accountability and that little effective performance measurement takes place. Consequently, local councils have been perceived by some commentators as inefficient, and unable to manage the commercial elements of their operations (Barrett, 2002). This has led to proposals that a more businesslike approach to the management of the local government sector should be adopted (Hood and Peters, 2004; Modell, 2004; 2005; Skalen, 2004; Worthington and Dollery, 2002).

These concerns have resulted in demands from the public for additional information on how local governments manage and spend public funds (Kent, 2003). By the late 1970's due to the absence of specific standards for the public sector, the Commonwealth and State Auditors-Generals began to apply private sector standards to the public sector (Chua and Sinclair, 1994). Recently, changes "have been imposed on the sector, enhancing local and central accountability, making it more business-like" (Kloot, 2006, p. 565). While the emphasis of these changes has been on the accountability for financial and budgetary measures, the performance of programs and people has also been addressed. In addition, the expanding regulation of local councils continues to increase the need for disclosure in a wide range of areas (Gray, 2001). These regulations and funding from state and federal governments impose duties on local councils to be accountable and to provide reports and information to meet both the regulatory requirements of state and federal governments, and to address the needs of a variety of stakeholders.

Legislative reforms (*Local Government Act 1993*) enacted during the 1990s have had the effect, according to Dollery *et al*. (2006, p. 555), of empowering local government with "greater flexibility to change both the way in which it operates and the range of services that it provides". At the same time "community expectations of local government seem to have increased and higher tiers of government have simultaneously devolved various new functions to local authorities" (Dollery *et al*., 2006, p. 555). These changes have led to an environment where local councils are expected to perform at high levels, maximising financial opportunities while demonstrating good financial management. At the same time they are being expected to provide an increasing range of high quality

services. The reporting of their financial operations is the primary method of demonstrating good financial management. However, the nature of financial reports means that information may be difficult for users to interpret. For example, previous research has shown that few councils chose to write off Collateralised Debt Obligations (CDOs) when the market failed (Jones and Bowrey, 2010, 2013). Instead these losses were carried forward to the term of the investment, dissipating over several years. Returns on investments were amalgamated so that the low or nil returns from the CDOs investments were less evident when combined with returns from other investments. This aggregation helped councils show that they were achieving reasonable returns despite having invested in CDOs.

3. INVESTMENT POLICIES

Managing cash reserves and achieving satisfactory returns from those investments is the responsibility of each individual local council. The minister's orders set the restrictions for the types of investments councils are allowed to participate in. The investment guidelines and policies with which local councils were required to conform during the period from 1997 through to 2011 has been compiled. Particular attention has been given to identifying the financial investments policies, which NSW local councils were following in the period preceding the GFC. The purpose of this is to show the investment environment in which local councils were functioning, and how the Minister's order provided a framework within which local councils were required to make their investment decisions.

NSW local councils have, over a 15 year period, been permitted to invest in a diverse variety of products. Approved products are stipulated by the NSW treasury and have been subject to a series of changes. After the introduction of the *Local Government Act 1993* there were significant modifications to the type of investments that councils could make. Prior to 1993 local councils were only permitted to invest in capital secured products, such as government bonds, so that their initial investment was secure. When the *Local Government Act 1993* was introduced, it referenced the *NSW 1925 Trustees Act* and required local councils to acknowledge that they were custodians and trustees of public assets. Within that role they were required to exercise due care and diligence in the investment of public monies (*Trustees Act 1925* (NSW) Section 14). Later amendments to the *Local Government Act 1993* removed reference

to the T*rustees Act 1925* (Dollery *et al*., 1998; Dollery *et al*., 2006) diminishing the requirement for capital protection. Further alterations to the Ministerial investment orders meant that NSW local councils, provided they continued to meet the requirements of the *Local Government Act 1993*, were able to invest in products without the same level of capital protection (meaning the initial capital investment was not protected from loss) thereby increasing the risk of losing their initial investment.

Significant changes were also made to the investment guidelines after the GFC began and in response to the release of the Cole Report (2008) which highlighted the losses suffered by NSW Local councils. Table 1 highlights the types of Ministry approved investment products available for use by NSW Local councils during the period from 1997 through to 2011. The investment policy documents issued by the Minister were supplemented by circulars provided to local councils from the Department of Local Government (DLG) which provided guidance on how to interpret the policies. While most of these documents are available from the DLG website, there were several, which were unavailable from that source. These were obtained from a financial investment advisor to local councils who was interviewed during this research project.

Table 1. Summary of Ministers Orders by Date.

Policy date/Type of investment	02/05/1997	01/05/1998	17/03/2000	16/11/2000	15/07/2005	31/07/2008	12/01/2011
Deposits	Deposit with the Local Government Investment Service Pty Ltd	Unchanged	Unchanged	Unchanged	Unchanged	Deposit with Local Government Financial Services	Deleted
Securities	Bill of exchange drawn or accepted by a bank	Unchanged	Debentures or securities issued by a bank, building society or credit union	Unchanged	Deleted		
Treasury Deposits	Deposit with the Treasurer	Unchanged	Deposit with New South Wales Treasury Corporation or investment in Hour-Glass facility of New South Wales Treasury Corporation	Unchanged	Unchanged	Unchanged	Unchanged
Body Issued Securities with Credit rating	Deposit with funds manager parent entity (immediate or ultimate) Maintaining minimum credit rating by Standard and Poor's of A, or Moody's of A2	Unchanged	Any securities which are issued by a company or body with a Moody's Investors Service, credit rating of ``Aaa", ``Aa1", ``Aa2", ``Aa3", "A1" or "A2" or a Standard & Poor's Investors Service, credit rating of ``AAA", ``AA+", ``AA", ``AA-"; "A+"; or "A"	Unchanged	Unchanged	Deleted	
Securities given a Credit Rating			Moody's Investors Service credit rating of ``Aaa",``Aa1", ``Aa2", ``Aa3", "A1"; "A2" or ``Prime-1" or a Standard and Poor's Investors Service, credit rating of ``AAA", ``AA+", ``AA", "AA-", "A+"; "A"; A1+" or ``A1"	Unchanged	Added Fitch Rating Credit rating AAA, AA+, AA, AA-, A+ or A	Unchanged	Unchanged
Government Securities			Any public funds or Government stock or Government securities of the Commonwealth or any State of the Commonwealth	Unchanged	Unchanged	Added or territory	Unchanged
NSW Guaranteed Debentures			Any debentures or securities guaranteed by the Government of New South Wales	Unchanged	Unchanged	Deleted	

Source: the Authors

Table 1 (Continued). Summary of Ministers Orders by Date.

Policy date/Type of investment	02/05/1997	01/05/1998	17/03/2000	16/11/2000	15/07/2005	31/07/2008	12/01/2011
LGA Debentures			Any debentures or securities issued by a LGA	Unchanged	Unchanged	Unchanged	Unchanged
Mortgage			Mortgage of land in any State or Territory of the Commonwealth	Unchanged	Unchanged	Restricted to 1st mortgages and 60% of value	Deleted
Land Purchase			Purchase of land in any State or Territory of the Commonwealth	Unchanged	Unchanged	Deleted	
Bank deposits			Interest bearing deposits in a bank authorised to carry on the business of banking under any law of the Commonwealth or of a State or Territory of the Commonwealth	Unchanged	Unchanged	Combined to any authorised deposit taking organisation Exclude subordinate debt obligations	Unchanged
Credit Union Deposits			Interest bearing deposits with a building society or credit union	Unchanged	Unchanged		
Bills of Exchange			Any bill of exchange which has a maturity date of not more than 200 days; and confers on the holder a right of recourse against a bank, building society or credit union an amount equal to the face value of the bill	Unchanged	Unchanged	Unchanged	
Shares				Inland Marketing Service	Deleted		

Source: the Authors

Table 1 indicates that prior to the collapse of the CDO market in 2007, and the subsequent write down of investments in those types of products, it was permitted for NSW local councils to invest in a wide range of products. Changes to the investment guidelines were gradually becoming less restrictive. This followed on from changes to the *Local Government Act 1993,* in the late 1990s, which saw the removal of reference to the *Trustees Act 1925* which required councils to take a zero risk approach to managing public funds. This requirement had required councils to first and foremost look for capital protection and avoid risk. In this new environment, some councils may have believed that if they were complying with the guidelines then that demonstrated that they were discharging their governance requirements.

In general, councils were allowed to invest in products that either had been issued by a company with a credit rating of A or better, or securities which had been given a credit rating of A or better. This assumed that it was suitable to rely on the validity of credit ratings assigned to each of the individual CDOs, and that they were an appropriate tool with which to govern the investment decisions of local councils. The production of investment policy guidelines with which local councils were required to comply reinforced the concept that the guidelines were a mechanism with which the Minister could govern the investment actions of local councils. Therefore, local councils were able to invest in CDOs where the primary issuer had a credit rating of A or better provided the tranche in which they invested was rated A or better. This meant that local councils were able to invest in products that they would not normally have been permitted to invest in, provided they were contained within a suitable CDO. In hindsight, NSW local councils were marketed CDO products that were overrated and sold to an audience who did not understand the complexity of the products (Dorizas, 2008).

As there was a policy reliance on the credit rating of investment products, and the ministerial guidelines stipulated the appropriate rating level, it is likely that some local councils may have assumed that meeting the guidelines and complying with directives from the DLG satisfied their corporate governance requirements with respect to investments. It is also likely that some local councils were unaware of the risks associated with these types of investments. As CDOs were typically offering 2-3 per cent greater return than similarly rated bonds it would also seem logical for local councils to try to maximise the returns from their investments if they were unaware of the allied risk.

Recognition of risk with CDOs was difficult even for sophisticated investors and this coupled with the prevailing economic conditions which were showing reasonably stable 2 per cent growth in GDP (RBA, 2012), steadily increasing interest rates and increasing bond returns from 2000-2011 (Eslake, 2011a; 2011b) provided local councils with the expectation that capital growth and investment returns would continue into the foreseeable future. However, what had occurred, primarily due to the nature of the assets backing CDOs was the creation of a bubble which overinflated the true value of CDOs (Adam *et al*., 2004; Levin and Coburn, 2011; Tett, 2007; 2009; 2010). While it may have seemed logical that councils from different regions (remote, rural and metropolitan) may have had different financial resources and therefore more or less capacity to invest in these products, prior research has shown that there was no difference in the proportion of councils from different regions who chose to invest, or not to invest, in CDOs (Jones and Bowrey, 2010).

The apparent result was that the relaxation of the ministerial policies opened the door for local councils who wished to pursue aggressive investment polices to indulge in higher risk investment activities. The subsequent closing of investments in derivatives and rated products during 2008 may be seen as a result of the losses sustained by local councils who had taken the opportunity to invest in higher risk products (Cole, 2008). This demonstrates that unanticipated outcomes may eventuate when policies allow flexibility in investment decisions. From a Bourdieuian perspective flexibility encourages higher risk behaviour by organisations with a habitus (Bourdieu, 1977; 1990) that supports, or at least does not discourage, undertaking risk.

For Bourdieu (1977), practice is based upon the inherent pre-existing dispositions of the actors. For this research the primary actors were finance managers within councils. Bourdieu proposed that the actors seek to improvise and pursue strategic goals and interests, while acting within their societal and situational environments which also have strong existing internal norms. Bourdieu (Cited in Wacquant, 2004) sought to show that social agents develop strategies which are adapted to the area which they inhabit and that these strategies are unconscious results of prior learning and social expectations. Bourdieu desired to analyse actors in the practical arena, while considering their performance, and their meaning as part of a social product which was linked to their cultural and symbolic actions (Breiger, 2000, p. 109).

Bourdieu also sought to connect empirical research with his theoretical ideas and offer insights into “how objective and subjective factors are interrelated” (Berard, 2005, p. 205). Bourdieu refers to three main

elements, capital (the level of power) of the individuals, fields (arena in which they function and habitus. This paper is primarily concerned with the Bourdieuan concept of habitus. In this research local councils are viewed as fields with their own rules, policies and structures designed to lead to certain activities. Within each council a particular habitus has been developed. Habitus captures the 'cultural unconscious' that shapes action through encapsulating the dialect between structure and agency. Habitus is the residue of past actions, knowledge, knowhow, behaviour and responses that now function in the present and influence behaviour (Bourdieu, 1984). Habitus is therefore the social norms or tendencies that guide behaviour, actions and thinking (Webb *et al*., 2002). We suggest that the relaxation of the NSW Ministerial guidelines affected the perception of what were considered appropriate types of investments. Those councils who relied on the policy as a mechanism of governance, may have taken up opportunity to engage in these products (which in the case of CDOs were high-risk investments) believing that following the investment policy discharged their governance requirements. However, not all councils chose to invest in CDOs. Individual local councils were also able to control the level of risk that they were willing to undertake through their own investment policies. Ultimately it was the habitus (Bourdieu, 1977; 1990) and acceptance of risk within each of the individual local councils, which was an important component in determining whether or not they engaged in these types of investments. Those councils who were conservative by nature avoided investing in these types of products as they were unable to sufficiently understand them. It may also have been that some local councils failed to recognise the risk associated with these investments. This may have been due to an over reliance on advice of the DLG and the ministerial investment orders, or by taking the view that having permission to invest in CDOs was a reflection of the safety of these products. Indeed, some mayors of local councils have justified their decisions to invest in CDOs as "having been made in accordance with the *Local Government Act 1933* and the Ministerial Order on Investment seems to imply there was a sufficient condition to make such an investment and results in a responsibility for the current problem" (Cole, Cited in Dorizas, 2010). However, Michael Cole elaborated by saying that "it ignores the fiduciary responsibility to protect the capital of the council's investment and accept full responsibility for all investment outcomes" adding "it wasn't enough to say 'they were consistent with the order, they have been ticked and I have no further responsibility" (Cole, Cited in Dorizas, 2010).

4. STATE GOVERNMENT CALLS FOR AMALGAMATION

The rules and policies with which councils need to comply continually change, particularly when there is a change in the political party controlling the state government. The game, for NSW councils, has once again changed with the new Baird (Liberal-National Coalition) government, signalling that they consider there are too many councils in NSW and that council mergers will allow more efficient operations. Premier Mike Baird stated that the "government considered there were significant benefits to be had from larger councils" declaring that "KPMG has looked at the proposals and they say there is $2 billion in benefits that come back to councils," and that "it's about delivering better services, more infrastructure and downward pressure on rates" (Davies and McKenny, 2015). The savings of $20 billion dollars are based on projected savings over the next 20 years. The state government has warned that councils whose financial performance is judged as unfit may be faced with the threat of merging with another council (Davies and McKenny, 2015). Metropolitan and rural councils were assessed under different measures on whether they were fit for the future. These measures, while different for metropolitan and rural councils, were based on the same range of criterion which included: scale and capacity, sustainability, infrastructure and service management (IPART, 2015). Most of these measures are financial and reflect the individual council's ability to generate revenue, meet their financial commitments, maintain and renew infrastructure and service debt. It should be noted however that the IPART (2015) report found that "only 7 of the 26 councils amalgamated in 2004 were 'fit for the future'". This suggests that amalgamations may not deliver the projected savings, with Professor Dollery declaring "that no difference exists between the performance of merged and unmerged council in terms of a range of performance indicators" (Robertson, 2015) and that the costs of amalgamation may exceed any benefits. Nevertheless, irrespective of the value (or cost) of amalgamations, we suggest that such statements from the NSW state government have created an environment in which councils wanting to avoid amalgamation need to be (or at least appear to be) financially viable.

Local councils are reliant on revenue from rate payers (rates account for approximately 40 per cent of local council revenue) (Gold, 2008; Stilwell and Troy, 2000) and grants from the state government. The ability of NSW councils to increase revenue from rates is limited by state government policies yet councils are required to supply an increasing

number of functions and services. One of the difficulties that NSW councils face is that revenue from rates is capped by a rate pegging system with NSW being the only Australian state which uses this method. Rate pegging prevents councils raising rates above the percentage stipulated by state government. Fundamentally, it means that the state government determines the upper limit on any property tax increases which local councils can apply (Dollery and Wijeweera, 2010). Councils in different regions face differing pressures on the use of financial resources and hence have different reliance on rates as a source of revenue. If councils want to raise their rates above the pegged percentage then they need to apply, stipulating the reasons why an exemption should be granted.

Reasons for the state government to grant variations may be many and varied, however, one reason relates to councils' need to maintain and repair fixed assets (Dollery, and Wijeweera, 2010). Since the introduction of Australian accounting standard ASS 27 in 1996 councils have been required to report on infrastructure assets which includes maintenance and depreciation of roads. Complying with this standard has meant that councils are required to report the maintenance costs and the decline in their assets (Pilcher, 2002). The Local Government Infrastructure Audit (NSW DLG, 2013) showed that many NSW councils have focused on creation of new assets and failed to recognise the long-term lifecycle costs of existing assets related to operation, maintenance and renewal. The Office of Local Government estimated in 2013 that there was a backlog of over $7 billion for maintenance and renewal of infrastructure within NSW local councils. There is also a disparity between what councils estimate as their estimated expenditure on infrastructure repairs and maintenance and what they actually spend. For example, from 2009-2013 NSW councils only spent 74 per cent of their total estimated needs for required annual maintenance (according to information provided to the Office of Local Government (NSW DLG, 2013)). For example over the last 5 years Liverpool Council has provided justification for a need to raise their rates by 10 per cent per year citing a large infrastructure repair bill and that increases in rates were needed to maintain infrastructure (Robertson and Buckingham-Jones, 2015). This justification was aimed at two primary groups; state government who have allowed councils to increase their rates above the pegged amount and; ratepayers who in paying higher rates have had an expectation of receiving infrastructure improvements.

As noted above, the NSW state government has highlighted that poorly performing councils will face amalgamation. A possible reaction to this by one council has been to conduct significant revaluations of the infrastructure liabilities. From information available in their financial report Liverpool council had $260 million of infrastructure liabilities in 2012. Following accounting standards, the council has revalued that liability to $60 million (Robertson and Buckingham-Jones, 2015). So how can $260 million in estimated liabilities become $60 million? Under the accounting standards there are various permitted methods for valuing liabilities and Liverpool City Council has adopted an alternative valuation method: the annual report stated "the trend for [the Infrastructure Backlog Ratio] shows a marked improvement over the last three years mainly due to a change in the measurement methodology to ascertain the backlog" (Liverpool City Council, 2014). This accounting policy change has been disclosed in the notes to the financial report (Davies and McKenny, 2015). They have also employed an independent valuer to conduct this revaluation. Other metropolitan and regional councils in NSW have also reduced their recorded liability for infrastructure repairs by more than a billion dollars without recording anywhere near this level of repairs and maintenance expense.

This legitimate accounting practice may have helped NSW councils protect themselves from amalgamation by promoting their financial management. Councils (like other reporting entities) have accounting policy choices and it is possible to adopt accounting measurement methods that provide the most favourable outcome. It is interesting to observe that councils are subject to differing views of interest groups. As a tool to justify rate increases it may suit councils to report infrastructure liabilities. However, in a climate of threatened amalgamations large infrastructure liabilities may be seen as a detrimental. A possible motivation by some councils may be to protect their regions and the interests of their respective ratepayers from the perceived negative impact of forced amalgamations. This suggests that accounting practices have a role to play in determining council behaviour and the way they signal their performance to different interest groups.

5. CONCLUSION

The first part of this paper reviewed the way NSW local councils have behaved when there have been changes to legislative requirements, policy and ministerial orders related to investment policies. There were changes

in behaviour when the rules were relaxed. A number of councils took the opportunity to accept more risk, choosing to take on investments in CDOs and achieve higher returns. Some councils did this aware of the increased risk profile, however, others perceived the ministerial orders as permission without fully understanding the risk involved. Legislation and policy changes were accepted as instructions as to what constituted acceptable behaviour. The removal of reference to the *Trustees' Act 1925,* and later, removal of the provision of protection of capital, provided the impetuous for councils willing to seeking high returns from their investment to engage in high risk investment practices. Bourdieu's (1977) Theory of Practice was used to describe the factors that influenced some councils to consider investing in CDOs. Councils with a risk averse habitus avoided investing in CDOs while those who were more accepting of risk considered investing in them. Additionally, some councils believed that complying with the Treasury investment guidelines was sufficient to discharge their accountability requirements and failed to consider if they understood the risk. Councils in full accordance with accepted accounting practice combined returns on investments in their financial reports.

The second part of this paper reflected on how NSW councils have reacted to a change in government. The new Baird government wanted councils to be financially viable and under the IPART (2015) 'fit for the future' program evaluated councils on how they managed their finances. Liverpool City Council was used to illustrate an accounting practice that is evident in council financial reports. Previously they had justified increases in rates, above the pegged amount, on the basis that they had a large liability for repair and maintenance of infrastructure. However, the change in policy by the state government may have resulted in a change to how they viewed the benefit of having a large infrastructure repair liability. As a result many councils chose to revalue their repair and maintenance liability for infrastructure (Robertson and Buckingham-Jones, 2015). Further work could be done to explore the links between the Baird government announcement and local council accounting revaluations. In the case of Liverpool City Council they were able to reduce a $260 million liability to only $60 million.

This paper has shown that legislative changes, alterations to policy, stipulation on the types of investments and even changes to the ruling political party can influence behaviour within local councils. Care needs to be taken when changing the rules. The old saying that you 'need to be careful what you measure because that is what you will get' holds true.

When the rules and environmental influences change, individuals and organisations may change their actions to influence the way they are perceived. Legitimate accounting practices such as amalgamating amounts in financial reports, combining returns from investments into one amount and the lack of requirements to disclose individual returns from investments make interpreting financial reports difficult for many users. A primary purpose of financial reports is to inform decision making. Further research could focus on the ways that the users of local council financial reports use this information to inform decision making. Strategic planning by local councils, particularly the area of asset management and maintenance, consumes a substantial proportion of resources and represents a valuable area for future research.

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