

ALLOCATION OF SURPLUS FUNDS POLICY

No. 0066.100.E.R

1 PURPOSE

This Policy outlines the process that should be followed to identify and allocate surplus general funds.

2 SCOPE

This Policy aims to ensure that surplus general funds are allocated in a manner consistent with Council's view of long term financial sustainability and in line with best practice financial management.

While this policy focusses on the General Fund(s), similar principles should be applied to any other specific funds.

The concepts of surplus and deficits of general funds being used in this policy bear a close relationship to requirements of Section 127 of the *Local Government Act 2008* (NT) and Section 13 of the *Local Government (Accounting) Regulations 2014* (NT). Both state that "a council must not budget for a deficit". Section 13 of the *Local Government (Accounting) Regulations* define a deficit as:

A deficit occurs if overall expenditure for a financial year (disregarding depreciation) exceeds income. Transfers into, and out of, specific reserves are to be taken into account.

The above definition is also followed when compiling the annual budget and the resulting financial statement called the 'Municipal Plan Summary' represents the reconciliation of Council's funding inflows, including transfers from reserves, matched with Council's funding outflows, including transfers to reserves. Provided the net funding result from the Municipal Plan Summary is zero or positive, Council has met the requirements of the *Local Government Act 2008* (NT) and the *Local Government (Accounting) Regulations 2014* (NT).

If the budget result on the above basis is zero or positive then the projected general funds available working capital at year end should also reflect that, and so too will the actual results if they closely follow the budget.

A working capital surplus occurs when funding inflows exceed funding outflows ie. there is an increase in net current assets (current assets less current liabilities). Such surplus funds can occur at any time including at the end of the financial year. Throughout the financial year, if surplus funds are identified then they are normally allocated through the quarterly budget review. At the end of the financial year it is necessary to wait until the annual financial statements have been verified through external audit to determine if surplus funds exist in the form of available working capital. If available working capital does exist at this time, and Council decides to utilise those funds as a surplus, then it should be dealt with under the process outlined in this Policy as should any significant surplus identified at any other time.

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Therefore for the purposes of the policy an end of financial year 'surplus' of free/available working capital is considered to have occurred when working capital is positive (as measured by a review of working capital and the liquidity ratio in conjunction with any particular adjustments set out in the policy statement section).

Working capital is calculated by deducting current liabilities from current assets (net current assets). If the result is positive then the entity has sufficient assets readily convertible to cash, including cash at bank and investments, to cover its current debts owed. In practical terms, working capital is having enough money to pay the current obligation/bills as they fall due.

3 POLICY STATEMENT

Surplus funds should not be used to fund discretionary expenditure throughout the year unless the expenditure falls within one of the priority groups outlined in this Policy.

The following priorities should be considered when allocating surplus funds in the order listed. However, Council's individual circumstances at the time the surplus funds are identified may impact on the order of priorities at that time.

3.1 CONSIDER PRIORITIES IN THE LONG TERM FINANCIAL PLAN

The first priority when allocating surplus funds should be to review Council's Long Term Financial Plan and the priorities contained therein. Specifically, Council should consider:

- Whether there are any projects that are funded from loan borrowings that could instead could be fully or partly funded by the surplus;
- Whether there are any priority projects deferred due to lack of available funding (such as maintenance and renewals) that could now be brought forward and funded by the surplus;
- Whether there are any areas in the Long Term Financial Plan where the surplus could be applied to alleviate pressure on rate increases or other fee and charge increases.

If a priority is identified in the Long Term Financial Plan then the surplus should be transferred to a reserve clearly marked for that specific purpose until it is required.

3.2 EXISTING BORROWINGS

A review of existing borrowings should be undertaken if surplus funds are available as paying off existing debt will release funding equivalent to the annual loan repayment within the budget to redirect to other priorities.

3.3 ASSESS ADEQUACY OF RESERVES

If surplus funds are available, a review should be undertaken to assess the adequacy of Council's reserves to determine if current levels are sufficient to meet future commitments.

3.4 UNFUNDED NEW INITIATIVES

Surplus funds could be considered to fund any priority new initiatives that were not funded in the current year's budget.

3.5 FUTURE YEAR BUDGET PRIORITIES

If the above priorities have been considered and surplus funds remain then any remaining funds should be transferred to a reserve to fund future year budget priorities.

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3.6 CALCULATION OF END OF FINANCIAL YEAR AVAILABLE WORKING CAPITAL

To determine if available working capital at the end of financial year exists the following calculation should be undertaken, which is based on the working capital calculation adjusted for non-cash items. The required figures are available from the audited Statement of Financial Position as at 30 June:

Item	Reason Why Calculation Adjusted
Total Current Assets	
Less: Total Current Liabilities	
= Working Capital	
Less: Cash-Backed Reserves	Working capital must be able to find cash backed reserves before declaring any surplus
= Working Capital	
Less: Non Current Assets Held for Sale if disclosed as a current asset	While cash may be received from the sale of assets, these funds will be placed in a reserve at the time they are received (for example, usually only fleet operations and is required in the budget to go towards replacements, therefore not free/available surplus funds).
Plus: Current Waste Fund Borrowings (principal only if fully funded in following financial year budget)	General Funds 30 June should not be required to support waste repayments that are covered by the following year budget. (However even though General Fund borrowings are also normally covered in following budget they are not adjusted, so as to create an element of prudence and conservatism in declaring the free/available working capital)
Less: Non Current Employee Leave Entitlement Provisions	While not a current liability, all ELE provisions should be backed by realisable assets. Currently they are backed by working capital and therefore this amount is not considered to be free/available funds.
Plus: Current portion of Waste remediation liability (if fully funded in following financial year budget)	This adjustment eliminates the current portion of waste remediation liability if able to be fully funded in the budget year immediately following 30 June. If not able to be fully funded in the following year budget then some working capital 30 June should be reserved to cover it as it may be inappropriate to eliminate it and declare the funds "surplus".
= Free/Available Working Capital	

If the result of the above calculation is positive then available working capital exists that can be allocated as per this Policy. Council may also elect to leave the available working capital balance as a buffer against budget shocks or unforeseen events.

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Testing the above calculation against cash liquidity

To remain prudent and conservative a second test should be undertaken to check the possibility that there is insufficient cash liquidity at preceding financial year end to cover cash-backed reserves 30 June plus any proposed transfer to reserve or other utilising of the apparently free/available working capital the above calculation as if that transfer was being actioned at 30 June.

This test can be achieved by following the table below:

Item
Cash & Cash Equivalents 30 June
Plus Other Financial Assets/Investments 30 June
= Total Financial Assets 30 June
Less Total Other Reserves 30 June (internally and externally restricted "cash-backed" reserves only)
= Unrestricted Financial Assets 30 June
Less proposed transfer of available working capital to cash-backed reserves (or other proposed utilisation)
= Remaining unrestricted financial assets (negative result means insufficient liquidity to action the transfer or other utilisation)

Should items within the Statement of Financial Position be reclassified or new items appear in the future then the above calculation would need to be reviewed in line with this.

3.7 RISK CONSIDERATIONS

Utilisation of available working capital as a surplus should be undertaken in the context of Council's overall approach to risk. Consideration should be given to the level of cash-backed internal reserves and the budgetary environment that Council is operating in at the time. In periods of uncertainty available working capital can provide a buffer against budget shocks or unforeseen events.

4 DEFINITIONS

Current assets: Generally assets expected to be realised within 12 months after the reporting period (AASB 101)

Current liabilities: Generally liabilities expected to be settled within 12 months after the reporting period (AASB 101)

Net current assets: Current assets less current liabilities

Working capital: Net current assets. In other words net assets that are continually circulating (AASB 101)

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5 LEGISLATIVE REFERENCES

Section 127 of the *Local Government Act 2008* (NT)
 Section 13 of the *Local Government (Accounting) Regulations 2014* (NT)

6 PROCEDURES AND RELATED DOCUMENTS

City of Darwin 0032.100.E.R Policy Framework Policy

7 RESPONSIBILITY AND APPLICATION

Implementation of this policy is by way of identification of surplus funds and consideration of allocation of surplus funds as defined within and by the policy.

This policy will be reviewed once in every term of Council or as required.

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