Land under roads and the power of politic
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Abstract
Purpose – The purpose of this paper is to answer the following questions: What are the theoretical and practical antecedents for recognising land under roads (LUR) as an asset in local government financial reports? Why was the process of regulating this aspect of accounting practice so protracted and so controversial?
Design/methodology/approach – The method used a critical analytical review and synthesis of relevant literature.
Findings – This study rejects the recognition of LUR, and suggests that the requirements to account for LUR should be withdrawn immediately. Regardless of the way that the debate has evolved as to the need or otherwise to value LUR or the methodology to be adopted, until the issue of a consistent, standards-based data set is addressed, there is unlikely to be a unified useful outcome.
Research limitations/implications – The study’s findings provided opportunity to reach an overall conclusion and make policy recommendations regarding the saga of accounting for LUR by Australian local governments. However, the ability to generalise beyond Australia to other countries would need to be tested by additional research.
Practical implications – The study’s findings provided assessment of the impact of valuing LUR on financial reporting by local governments and suggested policy recommendations.
Social implications – This study provided an understanding of Australian local governments’ accounting choices in regard to the valuation of LUR and documented the history of early adoption of valuation of LUR by local governments.
Originality/value – The literature on the public sector and accrual accounting is extensive and varied. However, there have been only isolated studies on the specific issue of LUR (Barton, 1999a, 1999b; Hogue, 2004; Rowles et al., 1998a, 1998b, 1998c, 1999). This study adds to the few isolated studies on the specific issue of accounting for LUR. Originality/value – This study provided policymakers with rich information about accounting for LUR and, it should have the capacity to impact on the future policy directions and recommendations.
Keywords AAS27, AASB1051, Australian local government, Land under roads
Paper type Literature review

Accounting for land under roads (LUR) by local governments has been one of the most controversial and protracted episodes in the setting of Australian accounting standards. The release of AASB 1051 in 2007 finally brought some regulatory closure to these issues (AASB, 2007). However, after more than two decades most LURs have not been recognised in local government balance sheets, and a survey of local government practitioners reveals that LURs were neither sought nor welcomed by the sector; a strong opposition to the practice persists.

1. Introduction
This study seeks to answer the questions: what are the theoretical and practical antecedents for recognising land under roads (LUR) as an asset in local government financial reports?
Why was the process of regulating this aspect of accounting practice so protracted and so controversial? The methodological approach used to answer these research questions included two distinct phases:

1. phase one presents the background and context, with the method used being a critical analytical review and synthesis of relevant literature; and

2. phase two is the evaluation and implications, being a detailed analysis and synthesis of all findings from phase one to reach an overall conclusion and make policy recommendations.

The critical analytical review and synthesis of the relevant literature also explores and identifies four main themes and matters:

1. the definition and recognition of assets;
2. the valuation and measurement of LUR;
3. the relevant regulation; and
4. the usefulness and/or reliability of the financial reporting of LUR and the implications for the comparability of financial statements.

Section 2 provides answer the first research question.

2. What are the theoretical and practical antecedents for recognising LUR as an asset in local government financial reports?

The background and context of the saga of accounting for LUR as an asset in the financial reports of Australian local governments indicates that in the early 1980s, Australian local governments had increasingly become responsible for delivery of a variety of services to their residents, including economic development and environmental management and social and community welfare. Therefore, and as noted previously, there was increasing public concern about perceived inefficiency and a lack of accountability in Australian local government (Halligan and Power, 1992, p. 120), and this included allegations of poor management, waste and inadequate reporting techniques during the 1980s (Siddiquee, 2006, p. 339; Russell, 1991, pp. 1-18).

In the late 1980s, laissez-faire, market-oriented governments saw the private sector accrual accounting model of financial reporting as the appropriate model to assist in delivering the reforms that would lead to leaner local governments with improved efficiency, effectiveness and accountability. This was part of a paradigm shift to new public management policies (Russell, 1991, pp. 1-18), amidst increasing public concern about local government’s inefficiency and lack of accountability (Halligan and Power, 1992, p. 120). However, these reforms, according to Carnegie and West (2005, p. 923):

have failed to achieve their stated purpose of promoting enhanced mechanisms of accountability within the public sector because their almost exclusive financial focus fails to embrace the need for a much broader discourse of accountability within public sector settings.

Since the 1980s, according to Jones (2009, p. 1), local governments:

have moved well beyond the traditional three Rs (roads, rates and rubbish). They are now responsible for projects and services in a diverse range of areas such as health, Indigenous youth, environmental management, climate change mitigation, and child care.
However, Jones (2009) argues that local governments are increasingly unable to attract sufficient revenue from state governments to fulfil these responsibilities and this reflected poorly on them, as a result of on-going tensions between them and the state governments.

During the 1990s, there was extensive and widespread organisational reform in Australian local governments, at the macro level, the subsequent reforms entailed legislative, workplace, structural and financial change and it is the latter of these that was of interest to this research. The agenda behind the reforms as noted previously was to improve the efficiency, effectiveness and accountability of local governments, and the accrual accounting model appeared to the standard-setters to be an appropriate model to assist in achieving these goals (Russell, 1991, pp. 1-18, Guthrie et al., 2003, p. 3).

Financial reporting reform of Australian local government, which is of interest to this research, was precipitated in 1991 through AAS 27 which set out the standards for the form and content of general purpose financial reporting of Australian local governments (AAS 27, 1991, para. 8; 1993, para. 8; 1994, para. 8; 1995, para. 8; 1996, para. 8). AAS 27 mandated the use of the private sector accrual accounting model for local government financial reporting, and AAS 27 (1996, para. 107) stated that:

where application of this Standard leads to initial adoption of accrual accounting, the assets, liabilities and equity of the local government as at the beginning of the reporting period of initial adoption are to be determined and recognised, so that the operating statement will faithfully represent the revenues and expenses for that reporting period.

Accounting standard-setters held that the comprehensive application of accrual accounting would increase local government’s accountability to the public by enabling comprehensive disclosures of their “performance, financial position, financing and investing, and compliance” (AAS 27, 1991, para. 9; 1993, para. 9; 1994, para. 9; 1995, para. 9; 1996, para. 9). In addition, accounting standard-setters held that “these disclosures should facilitate better-informed assessments of the local government’s financial position and performance” (AAS 27 1996, para. 114).

A particularly significant change imposed by AAS 27 was the requirement for local governments to account for infrastructure and related resources – such as drains, bridges, signage, footpaths and the like – as assets for financial reporting purposes (AAS 27, 1991, para. 90; 1993, para. 94; 1994, para. 103; 1995, para. 103; 1996, para. 111). Although not explicitly mentioned in the earlier versions of AAS 27 – but perhaps implied by reference to “roads” and “streets” – it was understood that LUR under the jurisdiction of local governments was one of the resources that should be considered for recognition as an asset.

The revised version of AAS 27 issued in 1996 made this explicit and offered the following definition of LUR: “land under roadways, and road reserves (including land under footpaths, nature strips and median strips)” (AAS 27 1996, para. 12). However, attempts by local governments to account for LUR precipitated an era of regulation, re-regulation, controversy and chaotic accounting, and LUR proved to be perhaps the most controversial of these “assets” to be valued and recognised in local government balance sheets.

In recognition of this and as noted previously, AAS 27 provided for an extensive transition period, running from the 1991 until the issue of AASB 1051 in 2007 (AAS 27 1991, para. 88-98; 1993, para. 91-93; 1994, para. 100-102; 1995, para. 100-102; 1996, para. 108-110). The purpose of the transitional provisions according to AAS 27 (1996, para. 119), is “to provide an adequate period within which interested parties can address whether and, if so, how concerns about reliable measurement of land under roads can be overcome”. AASB 1051 sought to bring closure to this issue and it required LUR acquired after 1 July 2008 to be valued and recognised for financial reporting purposes; and it also gave local
governments discretion regarding the recognition of LUR acquired before 1 July 2008. However, this comprised a “watered-down” requirement.

The opponents regarded the changes as highly inappropriate, arguing that the uniqueness of the public sector meant that many of the obligations of AAS 27 proved to be problematic, including accounting for LUR (Barton, 1999a, b; Rowles et al., 1998a, b, c; Hoque, 2004). In addition, the accounting changes needed to be matched with the distinctive characteristics of local governments and this required an alternative model of accrual accounting (West and Carnegie, 2010, p. 202; Christensen, 2009; Deegan, 2005; Carnegie and West, 2003, p. 83).

There is a wide diversity in the characteristics of Australian local governments, according to Kloot and Martin (2007, p. 486); for example, the populations of Victorian local governments vary from very wealthy inner suburbs to lower socio-economic populations, to those suffering extreme hardship in rural areas hit by drought and rural decline. Furthermore, Victorian local governments can be broken down into two main areas: purely rural local government areas and remote areas. Remote areas can be further broken down into: regional cities and towns; those located in newer outer suburban areas; those semi-rural areas and spanning outer suburbs; and finally, those located purely in older suburban areas. Therefore, the needs of the local communities in these areas are varying and fluctuating. In addition, in this diverse setting, local governments are relied upon to provide different kinds of services and different emphases in service delivery.

Likewise, the International Federation of Accountants (2011, p. 5) stated that government and other public sector entities are vastly different in their nature and also in the environment in which they operate in comparison with the private sector. This has significant implications for the concepts that underpin accounting requirements, the guidance for these entities, the development of a conceptual framework that reflects public sector circumstances and the process of setting accounting standards for the public sector. Moreover, accrual accounting has created accounting technical issues linked to the valuation and recognition of public sector assets due to the fact that many of the public sector’s resources are not primarily of a financial character. Furthermore, the major goals of the public sector are social not financial (Carnegie and West, 2003, pp. 83-84).

In addition, others considered the changes as highly inappropriate for local government, arguing that local governments “generally enjoy monopoly control over basic services and their businesses are rarely exposed to competitive pressures” (Dollery, 1997, p. 445), and local governments were not profit generating businesses. Rather, they are organisations controlling community resources including social and caring support, art galleries and parks. Also:

the history of structural reform in Australia has shown that objective rationale[s] are not the sole determinants of amalgamations, and any future structural changes must be examined in light of state/local relations, amongst other factors (Worthington and Dollery, 2002, p. 11).

Moreover, accounting in general is a social commodity, and can be an agent for social change, as it affects the welfare of different groups in society. Accounting numbers inform investments, affect the welfare of firms, employees and society and government policy (Hopwood and Miller, 1994, p. 1). Consequently, the LUR figures reported in local government financial reports are likely to have significant impacts and implications on these groups and other users. Therefore, and as noted previously, the third research question of this study will identify and describe the impacts of accounting for LUR on the financial reports of Australian local governments, and it will also identify and describe the
overall implications and effects of the AASB 1051 and recognition of LUR for each state individually.

3. Why was the process of regulating this aspect of accounting practice so protracted and so controversial?
A critical analytical review and synthesis of the relevant literature reveal that the process of regulating this aspect of accounting practice was protracted and controversial owing to the influence of many factors including regulation (which included guidance and communication from the accounting standard-setters), and diversity in the approaches state regulations and the standard-setters; definition and recognition of assets, including definitions of the terms “Road” and “Land Under Roads”; valuation and measurement of LUR, including whether LUR should or should not be valued, whether LUR is an asset or not, and the valuation methodologies and reliability of the measurements of LUR; and usefulness and/or reliability of LUR and the comparability of the financial statements, including the cost and benefits of accounting for LUR, the usefulness and/or reliability of the LUR information and the comparability of the financial statements from year to year and from local government to local government, the impacts of accounting for LUR on financial reporting by local governments and users and the compliance with AASB 1051. Section 3.1 provides a critical analytical review and synthesis of the relevant literature for each of these individual factors.

3.1 The guidance and communication from the accounting standard-setters
The Victorian Auditor-General (2009a, p. 30) stated that most of the blame should be apportioned to the Department of Planning and Community Development, as it has “a key role in enhancing the accountability and management of the local government sector”. However:

[...] the lack of guidance from the Department of Planning and Community Development regarding the recognition and measurements of land under roads has resulted in councils not adopting a consistent approach in the treatment of this asset (Victorian Auditor-General, 2009a, p. 30).

The Victorian Auditor-General (2009a, p. 30) said:

[...] my recommendation is [that] the Department of Planning and Community Development should provide guidance to entities within the local government sector to improve the utility and comparability of the financial information across the sector).

However, according to Ernst & Young (2007), the AASB needs to revisit the structure and location of the standards, and address the issue of the reliable measurement of LUR. As well, the AASB should be seeking to discuss with stakeholders the issues relating to LUR and endeavouring to reach a workable solution. Besides, detailed guidance needs to be provided to the local governments by the AASB in regard to how best to value LUR. Such guidance according to FinPro (2007) is critical for ensuring the consistency of the approach across the Australian local government sectors, in addition, on a national basis; such guidance is also critical and essential in terms of preparing relevant and reliable financial statements. Ernst & Young (2007) claimed that without such guidance, there is a high likelihood that different approaches will be adopted by different entities which will lead to inconsistent treatment of LUR across sectors as a result of the difficulties associated with valuing LUR, and the absence of the guidance from the standard-setters.
Whitehorse City Council (2007) stated that no sector or relevant professional associations had completed any detailed and publicly available analysis of the valuation techniques of LUR, including the standard-setters. Consequently, in the absence of that, there is a high likelihood of inconsistent treatment across the sector. Therefore, in line with the transitional provisions, there is an ongoing need for guidance to help ensure that the information presented in local governments’ financial statements about the value of LUR is relevant and reliable.

Haines Norton (2007) also felt that it is important that as much guidance as possible is given in this standard [AASB 1051]. In particular, LUR has been a topical issue since the beginning of the AAS 27 in 1991. In addition, it has remained on the board’s outstanding list for a considerable period and, at the same time; the board did not address the issue of control and development of objective valuation principles for it.

3.2 The diversity between the state regulations and the standard-setters
The theoretical and practical antecedents for recognising LUR as an asset in local government financial reports, and the critical analytical review and synthesis of the relevant literature has shown that LUR is subject to diverse regulations and general laws, such as the Land Act 1994 of Queensland and the Land Titles Act 1994 of Queensland which stated that LUR network within the local government area has been dedicated and opened for public use, and it is not controlled by local but by the state government (Bulloo Shire Council, 2009, p. 30).

In Western Australia, the Financial Management Regulation 16(a)(i) prohibits Western Australian local governments from recognising LUR as an asset. It is stated that while such treatment is inconsistent with the requirements of AASB 1051, Local Government Financial Management Regulation 4(2) provides in the event of such an inconsistency, the Local Government Financial Management Regulations prevail (Albany City Council, 2009, p. 40).

3.3 The definition of the term “road” and “land under roads”
Thomas Kuen, Manager Engineering Assets of the Glen Eira City Council in Victoria, said in his submission on ED156 that the term “road” needs defining and in the state of Victoria:

There are numerous Acts, Regulations and other statutory documents that define roads differently. There are also legal precedents (non-statute based) that apply. In addition, Thomas Kuen said that if this is the case in one state, I expect the national position is even more confusing (Glen Eira City Council, 2007).

Queensland Department of Environment and Resource Management (1994, p. 1) defined a road as, an area of land, whether surveyed or unsurveyed that is taken under the acquisition of Act such as the Land Act 1967 of Queensland and/or Transport Infrastructure Act 1994 of Queensland, and this acquisition is for the purpose of a road for public use. In addition, it is dedicated, notified or declared to be a road for public use. The term “road” according to Queensland Department of Environment and Resource Management (1994, p. 1), includes, first, a bridge, causeway, culvert or other works which is in, on, over or under a road; second, any part of a road; and third, a street, esplanade, reserve for esplanade, highway, pathway, thoroughfare, track or stock route.

In addition, the Queensland Department of Environment and Resource Management (1994, p. 1) claimed that “a constructed carriageway may not even exist”, and they said that:

A road is not only the area covered by the actual road formation (carriageway) but encompasses the entire area of land set apart for road purposes, from property boundary to property boundary.
Also a road may be according to Queensland Department of Environment and Resource Management (1994, p. 1), “dedicated as: freehold land (s 51 of the Land Title Act 1994) [or] State land (s 94 of the Land Act 1994)

(Barton 1999a, p. 10) claimed that “most property and Information Systems [IS], and most Geographic Information Systems [GIS], focus on the management of free-hold land”. A GIS, according to the Ballarat City Council (2008, p. 7), is the most reliable tool that most local governments have used it to assist them in the task of determining the actual amount of LUR in a municipality.

However, the regulation, control and management of the most roads, as stated by the Queensland Department of Environment and Resource Management (1994, p. 1), lies with the relevant local government, while the ownership of the road rests with the state as outlined in the Local Government Act 1993 of Queensland. However, the Queensland Department of Environment and Resource Management said that if a road is a declared road under the Transport Infrastructure Act 1994 of Queensland, then, its control and management rests with the Department of Transport and Main Roads. The space occupied by roads, according to (Barton 1999a, p. 10), “is often the gap between these specifically identified parcels of land”, and “much of this land is not owned by local government”, besides, “the road reserve may not also even contain a constructed road asset”.

3.4 Whether LUR should or should not be valued

The adoption of AASB 1051 has created a huge debate relating to whether LUR should or should not be valued as an asset by Australian local governments and government departments (Maxwell and Maxwell, 2008, p. 1). The Municipal Group of Valuers (2007) suggested that the requirements to account for LUR should not be introduced or imposed at this stage but be further held in abeyance until some of the issues and matters associated with accounting for LUR are resolved. On the other hand, AustRoads National Office (2000, p. 49) argued that “land in road reserves should be valued using an average of rateable values for a wide area such as a local government area or a postcode area”. However, they said that LUR typically provides access to nearby properties, which boosts their value and does not provide a reliable indicator of its own value.

3.5 LUR is an asset or not?

After the promulgation of AAS 27 in 1991, further concerns were raised by valuers, accountants and financial managers who viewed the recognition of LUR as not complying with the asset recognition criteria, and who were “questioning the correctness of that classification” (Rowles et al., 1998a, p. 260, 1999, p. 66).

Opponents of the requirements to account for LUR believe that LUR is not an asset, and they said that normally LUR can only be sold by local governments after a legal process has been completed, and until this happens, the local governments cannot assume that it has land that can be sold. Therefore, when the local governments are actually in a legal position to sell the land, at that time, LUR can be consider as an asset. This of course is a different issue as to whether a local government was the legal owner of the land at the commencement of the process (Glen Eira City Council, 2007).

Rowles (1991, p. 70) found that road assets have been identified as “wasting assets” by both Vicroads and the Traffic Authority of New South Wales, and it is anticipated that they be capitalised at current replacement cost. New South Wales Treasury (2007) stated in their submission on ED 156 that they broadly agreed with the comments of the “Head of Treasuries Accounting and Reporting Advisory Committee”. Head of Treasuries
Accounting and Reporting Advisory Committee – Tasmania (2007) stated in their submission on ED 156 that:

- LUR cannot be measured reliably, thus they have previously written to the chair of the AASB on that matter;
- the proposed standard does not adequately address the issue of the LUR and supports the transitional arrangements on the basis that they are enacted for further year only and should not be extended beyond that;
- the issue is broader than whether fair value at the date of the acquisition can be determined retrospectively, which as referred to in the Basis for Conclusions, para. BC 22;
- the LUR cannot be measured reliably either at the date of the acquisition or even at the date of the transactions;
- the inclusion of the deemed cost transitional provisions using the fair value at the date of the transactions or some earlier period it is seem to be irrelevant;
- the continual extension of the transitional requirements is clear evidence that reliable measurement of the LUR has not been possible; and
- the point has come to clearly acknowledge this to avoid inconsistencies across jurisdictions.

Others such as the New South Wales Treasury Office (1997, p. 26) has supported the recognition of LUR in their “Consolidated Financial Statements of the New South Wales Public Sector 1996-1997”, and they claimed that LUR “satisfy the recognition criteria for an asset as set out in Statement of Accounting Concepts, SAC 4 […] and should be recognised in the consolidated statement of financial position”. Likewise, the AustRoads National Office (2000, p. 49) suggested that LUR should be accounted for as an infrastructure asset.

An asset has been defined by SAC 4 (Australian Accounting Research Foundation, 1995, para. 14) as “future economic benefits controlled by the entity as a result of past transactions or other past events”. The control of an asset has been defined by SAC 4 (1995, para. 14) as “the capacity of the entity to benefit from the asset in the pursuit of the entity’s objectives and to deny or regulate the access of others to that benefit”.

However, this regulatory document (SAC 4) is no longer relevant as the International Accounting Standards Board framework now takes precedence. Deegan (2012, p. 67) stated that the “conceptual framework does not require an item to have a value in exchange before it can be recognised as an asset”.

The definition of asset provided by SAC 4 identifies three main fundamental characteristics of an asset: the first is that there must be future economic benefits; the second, the entity must have control over the future economic benefits such that it is able to enjoy the benefits and regulate or deny the access of others to the benefits; and finally, the transaction or other event giving rise to the entity’s control over the future economic benefits must have occurred (SAC 4, 1995, para. 15).

The definition of “asset” provided by SAC 4 suggested that for LUR to be recognised as an asset in an Australian local government’s balance sheet it must have future economic benefits. Future economic benefits, according to SAC 4 (1995, para. 18), is:

synonymous with the notion of service potential […] Future economic benefits can be described as the scarce capacity to provide benefits to the entities that use them, and […] Thus, assets provide a means for entities to achieve their objectives.
However, in not-for-profit entities, according to SAC 4 (1995, para. 20), “whether in the public or private sector, the future economic benefits are also used to provide goods and services in accordance with the entities’ objectives”. In addition, according to SAC 4 (1995, para. 18), both not-for-profit and profit-seeking entities provide services and goods that:

have the capacity to satisfy human wants and needs. Both types of entity create utility and value in essentially the same way – by using assets to provide goods and services that their customers or beneficiaries desire or need.

In spite of this, as the entities do not pursue profit objectives according to SAC 4 (1995, para. 20):

the provision of goods and services may not result in net cash inflows to the entities as the recipients of the goods and services may not transfer cash or other benefits to the entities in exchange.

AASB (2009, p. 13) contended that for any asset to qualify for recognition it must satisfy the basic test as set out by AASB 116 which states that:

the cost of an item of property, plant and equipment shall be recognised as an asset if, and only if: it is probable that future economic benefits associated with the item will flow to the entity; and the cost of the item can be measured reliably (AASB 2009, para 7).

Barton (1999a, p. 13) stated that in regard to LUR, historical cost is rarely available, and the current realisable value and current replacement cost are fundamentally the same in the case of land that is current market price, and he claimed that in those metropolises where LUR has been valued, it seems that “rateable values of adjoining properties” have been used with rateable values established on the current market value of these properties; however, he argued that this is a relatively easy process, but it is random and lacks validity.

As noted previously, SAC 4 (1995, para. 15) stated that for any asset to qualify for recognition “there must be future economic benefits”. AustRoads National Office (2000, p. 49) stated that all agencies that control surplus land, land held for future infrastructure and land within road reserves “are accountable for those assets as resources”. Control is the second fundamental characteristic for an asset according to SAC 4 (1995, para. 15), which stated that for any asset to qualify for recognition “the entity must have control over the future economic benefits such that it is able to enjoy the benefits and regulate or deny the access of others to the benefits”.

3.6 The valuation methodologies and reliability of measurements of LUR
AASB 1051 identified two main approaches to valuing LUR; first, all LUR relating to roads controlled by the entity should be calculated by the cost method (i.e. valued on acquisition only); second, all LUR relating to roads controlled by the entity should be valued by the fair value approach (i.e. periodically re-valued) (see Paragraph 13 and 14 of the AASB 1051 2007a, pp. 13-14).

AASB 1051 gave local governments discretion regarding the recognition of LUR acquired before 1 July 2008. However, if the local governments chose not to account for LUR acquired before 1 July 2008, then, according to Mornington Peninsula Shire Council (2009, pp. 2-3), this would be a simpler approach, and local governments would never need to account for LUR which was acquired before 1 July 2008, except they would need to record and track all the LUR acquired on or after 1 July 2008. If the local governments had elected to do so, then, the value of LUR recognised would be an incomplete and unfinished picture of the total assets managed by local government. Also, local governments could not decide to
AASB 1051 gave local governments discretion regarding the recognition of LUR acquired before 1 July 2008, and if the local governments chose to account for all LUR before 1 July 2008, according to the Mornington Peninsula Shire Council they would need to undertake additional work, initially to capture all data of all LUR, and the information available in the Road Management Act Register, and GIS may assist. However, it was recommended that local governments should recognise all LUR on their balance sheets at deemed cost, and by doing so, they would avoid the need to revalue them again in the future years. Nonetheless, if the fair value approach is adopted by local governments, then future revaluations will need to be undertaken, and the book values should be adjusted for any material changes. However, this choice may impact on the local government’s balance sheet by a significant amount (e.g. early modelling shows up to $300m for an inner metropolitan council) (Mornington Peninsula Shire Council, 2009, pp. 2-3).

These different approaches raise the concern that accounting for LUR would result in significant variability from year to year, from local government to local government and even from state to state, particularly where current market value was used. In addition, the value ascribed to LUR would often be so great that it would “swamp” the local government’s balance sheets (AASB, 2001, p. 56).

Opponents of the changes such as the Municipal Group of Valuers (2007, p. 1) argued that there is no empirically based historical verification that will let anyone reach a perfect value for all LUR, and “the concept is such a theoretical one that any approach [they] might use is totally arbitrary”. And they said that no one approach/method is necessarily essentially inherently better or superior than another, and the possible results in terms of value expose the “full length of the spectrum from zero to the most valuable land”.

3.7 The costs and benefits of accounting for LUR

After the promulgation of AAS 27 in 1991 further concerns were raised by valuers, accountants and financial managers who viewed the recognition of LUR as a “pointless exercise” and costly and who were “questioning the correctness of that classification” (Rowles et al., 1998a, p. 260, 1999, p. 66). Australian Government – Department of Finance and Deregulation (2009, p. 1) contended that local governments should only account for LUR acquired on or after 1 July 2008 if the cost or other value of the LUR could be measured reliably. However, there are two types of costs: the cost of LUR and the cost of undertaking valuation of LUR.

In the debate over the cost of LUR, Rowles et al. (1999, p. 66) suggested that LUR is a sunk cost, meaning that the cost cannot be recovered as it cannot be sold and therefore has no value. AASB (2001, pp. 55-56) identified some costs associated with accounting for LUR such as those that arise as a result of: the preparers of the financial reports; the development of the valuation methodology; measurement of LUR by consultant firms and regulatory authorities checking compliance with AASB 1051. These costs trigger the question, what are the benefits from undertaking such valuations? Particularly and according to FinPro (2007), the valuation of LUR would be an ineffective and inefficient use of limited valuable resources due to the absence of any demonstrable benefits to the local government’s community.
AASB (2001, pp. 55-56) determined that there were some benefits from accounting for LUR, including minimisation of “investment” in land and determining road width. Furthermore, LUR is fundamental to the:

- provision of road services and there are no legal impediments to road authorities gaining benefit from land under roads or denying or regulating access by others to the benefits embodied in the land.

In addition, accounting for LUR is “likely to benefit users of financial reports” (AASB, 2001, pp. 55-56). However, the benefits of valuing LUR, according to the AustRoads National Office (2000, p. 49), “will exceed the costs involved provided the valuation methodology reflects the purpose of the valuation”.

Regarding the costs of undertaking the valuation and revaluation of LUR, there are significant costs associated with that, according to Brown et al. (1992, p. 37). These include first, record-keeping costs; second, the costs charged by the auditors for the additional review; third, the fees charged by the valuer and finally, the out-of-pocket costs and the opportunity of the time directors spend in reviewing the figures to be reported, and discussing them with the auditors.

According to Brown et al. (1992, p. 37), these costs are alleged to be sufficiently large to influence management’s revaluation decision, for example:

The fee recommended by the Australian Institute of Valuers for a property with an appraised value of $30,000 was about 0.5 per cent of the appraised value, and for a property with an appraised value of $2 million, about 0.2 per cent.

The usefulness and/or reliability of LUR information and comparability of the financial statements was another important factor which the Section 3.8 provides more detail.

### 3.8 The usefulness and/or reliability of LUR information and the comparability of the financial statements from year to year and from local government to local government

One of the primary objectives of preparing financial statements in accordance with accounting standards as said by the Victorian Auditor-General (2009a, p. 30, b), is to enhance the comparability, usefulness and effectiveness of the financial information reported. However, after the promulgation of AAS 27 in 19991, further concerns were raised by valuers, accountants and financial managers who viewed the recognition of LUR as “having no useful purpose” and who were “questioning the correctness of that classification” (Rowles et al., 1998a, p. 260, 1999, p. 66).

Likewise, the AustRoads National Office (2000, p. 49) argued that LUR value “is unlikely to be useful in assessing the efficiency of an agency in providing road services”. Although financial information is important to users, its interpretation can be a difficult task. Therefore, the value of LUR and reserves, “is spelling out what the information actually means” (Neilson and Paul, 1993, p. 53; Pilcher, 2000, p. 54; Hoque, 2004, p. 2).

AASB (2004, p. 16) in its own “Framework for the Presentation and Preparation of the Financial Statements” sets out a number of “Qualitative Measures” which are important and required to be complied with, to determine the usefulness of information in the financial reports. Qualitative characteristics according to AASB (2004, para. 24), “are the attributes that make the information provided in financial reports useful to users”, and the four main principal qualitative characteristics according to AASB are “understandability, relevance, reliability and comparability” (AASB, 2004, para. 24).

Moreover, Australian Accounting Research Foundation (1990, pp. 14-15) stated in SAC 3 that the general purpose financial reporting “shall include all financial information which
satisfies the concepts of relevance and reliability, and which passes the materiality test” (Australian Accounting Research Foundation, 1990, para. 48). Furthermore, the general purpose financial reporting “shall be presented on a timely basis and in a manner which satisfies the concepts of comparability and understandability” (Australian Accounting Research Foundation, 1990, para. 49).

To enhance the comparability, usefulness and effectiveness of the financial information reported AASB suggested that it must be:

- readily understandable by users [. . .] information about complex matters that should be included in the financial report [. . .] should not be excluded merely on the grounds that it may be too difficult for certain users to understand (AASB, 2004, para. 25).

However, for the information to be useful it:

- must be relevant to the decision-making needs of users. Information has the quality of relevance when it influences the economic decisions of users by helping them evaluate past, present or future events or confirming, or correcting, their past evaluations (AASB, 2004, para. 26).

Nevertheless:

- the relevance of information is affected by its nature and materiality. In some cases, the nature of information alone is sufficient to determine its relevance [. . .] both the nature and materiality are important (AASB, 2004, para. 29).

Then again, for the information to be material, as stated by AASB, it must be the case that “its omission or misstatement could influence the economic decisions of users taken on the basis of the financial report” (AASB, 2004, para. 30). The materiality however depends on the:

- size of the item or error judged in the particular circumstances of its omission or misstatement [. . .] provides a threshold or cut-off point rather than being a primary qualitative characteristic which information must have if it is to be useful (AASB, 2004, para. 30).

However, for the information to be useful, according to AASB it:

- must also be reliable. Information has the quality of reliability when it is free from material error and bias and can be depended upon by users to represent faithfully that which it either purports to represent or could reasonably be expected to represent (AASB, 2004, p. 31).

In addition, the users of that information must be able to:

- compare the financial reports of an entity through time in order to identify trends in its financial position and performance [. . .] compare the financial reports of different entities in order to evaluate their relative financial position, financial performance and cash flows (AASB, 2004, p. 39).

In addition, the varying decisions made by Australian local governments on the measurement and recognition of LUR, though endorsed by the accounting standard, according to the Victorian Auditor-General (2009a, p. 30), “have led to a reduction in comparability across the sector. This has reduced the usefulness of the reported information for this asset”. Likewise, FinPro (2007) argued that the recognition of LUR as an asset will not improve the relevance or the reliability of the information for users of local government’s financial statements. A non-depreciable and non-saleable item, including the value of LUR, would not add to the decision-making ability of either local governments or other financial statement users. Furthermore, accounting for LUR may well reduce the relevance, and the reliability of the financial statements because of the distorting effect that potentially large
asset values, such as LUR, will have on the local governments balance sheets, and also on the financial ratios. FinPro (2007) also contended that any decisions about assets by local governments need to take into consideration: asset utilisation; asset rationalisation; long-term cost; depreciation; maintenance; the needs of the community; growth potential; construction and finally, upgrade. Therefore, including a value for LUR would add no value regarding practical decisions about the assets which need to be made by the local governments.

One of the primary objectives of preparing financial statements in accordance with accounting standards is to enhance the comparability, usefulness and effectiveness of the financial information reported (Victorian Auditor-General, 2009a, p. 30), and the information reported must be understandable, relevant, precise, reliable, timely, clear, comparable and consistent to be communicated effectively (Jones, 1992, p. 259).

This degree of problematisation over accounting for LUR gives rise to important question: What are the impacts of accounting for LUR on the financial reports of Australian local governments and users? The Section 3.9 provides more detail.

### 3.9 The impacts of accounting for LUR on financial reporting by local governments and users

According to the Glen Eira City Council (2007), the implementation of AASB 1051 is a real challenge to local governments, and there will be significant impacts as a result of the termination of the transitional provisions for LUR. Hoque (2004, p. 10) found from his interviews with the Alpha City Council’s managers that a major effect on users of reporting LUR is that the finance providers would charge and make their decisions on the inflated asset position, and all areas exposed to bias and undue error, and there are no means available to the local government to report this information in such a way as to eliminate these potential biases, and this by itself raises the question as to how reliable the value that they have reported for LUR and local government’s parklands actually is.

The impacts of accounting for LUR on financial reporting by local governments and users also included that the current value of LUR information disclosed could easily be misinterpreted by the users of that information, as they may interpret LUR values as a kind of asset which could be sold to finance other projects or pay debts (AASB, 2001, p. 56); accounting for LUR:

* May influence road pricing but would have no real impact on day to day asset management decisions [… ] will represent a significant item in balance sheets and profit and loss statements (AustRoads National Office, 2000, p. 49).

The value ascribed to LUR would often be so great (Rowles, 1991, p. 70); the inclusion of such large figures for LUR in the balance sheets would “swamp” local government balance sheets (AASB, 2001, p. 56).

The Section 3.10 addresses one of the factors which related to the compliance with AASB 1051.

### 3.10 Compliance with AASB 1051

The requirements of AAS 27 to account for LUR were established through widespread consultation between the Public Sector Accounting Standard Board and its constituents, including publication of Discussion Paper No. 12 in 1988 and ED 50 for public comment in November 1989, as well as Australia-wide seminars on ED 50. During this consultation, significant concerns were expressed about the total cost of reporting LUR (Neilson and Paul, 1993, p. 53). AASB (2001, pp. 55-56) identified some costs associated with accounting for
LUR, such as those that arise as a result of regulatory authorities checking compliance with AASB 1051.

Compliance with AASB 27 requirements to account for LUR has at best been ad-hoc with a history of continual transitional periods for more than 16 years being implemented as a result of measurement and recognition difficulties associated with accounting for such assets. Therefore, in an attempt to overcome the compliance challenge, a transitional period was specified in which it was hoped that a reliable measure of LUR would be determined (Paul, 1996, p. 54), and it was identified as a particularly controversial issue, with widespread uncertainty and concern over compliance issues (Barton, 1999a, p. 9).

Finally, to overcome these compliance challenges, the structure of the conceptual framework would, according to McGregor (1990, p. 48), "include less problems for responsible practitioners, opportunities for creative accountants, and difficulties for regulators in seeking to enforce compliance with financial reporting requirements".

4. Evaluation and implications
The detailed analysis and synthesis of the findings from phase one suggested that the long and difficult saga of accounting for LUR has constituted a case of regulatory failure, that is, regulatory activity was undertaken that has not yielded a demonstrable benefit relative to the costs of developing and enforcing the regulation and achieving compliance. The presumed rationale for the issuance of an accounting standard is that it will resolve some "problem" in financial reporting and improve the reliability, usefulness, comparability or some other aspect of financial reports. However, the benefits of the regulatory activity that culminated with AASB 1051 are not easily discerned.

Opponents of the changes claimed that the costs associated with ascertaining, auditing and reporting such values would likely exceed any associated benefits; that the recognition of LUR serves no useful purpose, and it is unlikely to be useful in assessing the financial position and/or performance of local governments. Further, such recognition means that the financial reports of local governments will not be comparable from year to year, from state to state and even from local government to local government.

The recognition of LUR has the capacity to transform an entity’s balance sheet and the financial ratios and other financial indicators derived from it. Different compliance and different valuation models have been used in different states, and this reduces the usefulness, effectiveness, comparability and consistency of financial reporting across the local government sector from year to year and from local government to local government. Therefore, the opponents of the changes suggested that a better approach would be to continue the existing exemption from applying AASB 116 to the LUR.

5. Overall conclusion and policy recommendations
The theoretical and practical antecedents for recognising LUR as an asset in local government financial reports, and the critical analytical review and synthesis of the relevant literature has shown that the process of regulating this aspect of accounting practice was influenced by many factors as noted previously. The critical analytical review and synthesis of the relevant literature related to these factors has shown that some felt that: LUR should not be valued; LUR is not an asset because it does not satisfy the recognition criteria for an asset as set out in SAC 4; the costs associated
with ascertaining, auditing and reporting such values are likely to exceed any associated benefits; the recognition of LUR having no useful purpose, and it is unlikely to be useful in assessing the efficiency of local governments; financial reporting by local governments will not be comparable from year to year, from state to state and even from local government to local government as a result of valuing of LUR; the implementation of AASB 1051 is a real challenge to the local governments, and there will be significant impacts as a result of accounting for LUR on financial reporting by local governments and users. In addition, it will completely transform an entity’s balance sheets and financial ratios and other financial indicators derived from it; it is highly likely that different approaches will be adopted by different entities which will lead to inconsistent treatment across the sectors as a result of the difficulties associated with valuing LUR, and the absence of guidance from the standard-setter. A better approach would be to continue the existing exemption from applying AASB 116 to the LUR; LUR is subject to diverse regulations and general laws which prohibit local governments in some states such as Western Australia and Queensland from recognising LUR as an asset, and it is stated that while such treatment is inconsistent with the requirements of AASB 1051, the regulations should prevail; and there is no single appropriate valuation method applicable to all Australian local governments.

Finally and as noted previously, what has often been absent is guidance as to how assets are measured and a valuation methodology, and it seems that the accounting standard-setters have failed to produce guidance and rules for the local governments as to how to best to value the LUR, and therefore, it was not surprising to find that there has been different compliance and different valuation models used in different states, and this has reduced the usefulness, effectiveness, comparability and consistency of financial reporting across the local government sectors from year to year and from local government to local government.

This study has provided policymakers with rich information about accounting for LUR and, therefore, it should have the capacity to impact on the future policy directions and recommendations. All the findings have indicated that two main positions have been taken. The first is that of the opponents of the changes who rejected the recognition of LUR as an asset and who comprised the majority. The second is that of the supporters of the changes comprised the minority. In order for this project to provide policy recommendations, a choice between these two main positions was required. Based on the data presented in this study, and on the findings from phases one and two, this study rejects the recognition of LUR, and makes the following policy recommendations:

- the requirements to account for LUR should be withdrawn immediately; and
- any existing LUR recognised in the accounts of local governments should be removed immediately and the recognition of LUR discontinued, to enhance rather than diminish the usefulness and reliability of the financial reports of Australian local governments.

The main justification for this stance includes that the saga of accounting for LUR by Australian local governments has been on-going for more than three decades without clear or effective resolution, and that this seems to have arisen from the regulators being in a “conceptual corner” in which the application of unmodified accrual accounting to diverse public-sector settings was seen as necessary and unproblematic.

Finally, based on the arguments and justifications presented above and all the findings, this study rejects the recognition of LUR, and suggests that the requirements to account for
LUR should be withdrawn immediately, as several methods can be used to come up with a number, as noted above. Regardless of the way that the debate has evolved as to the need or otherwise to value LUR or the methodology to be adopted, until the issue of a consistent, standards-based data set is addressed, there is unlikely to be a unified useful outcome. This degree of problematisation over accounting for LUR gives rise to the prospect that it may constitute an episode of regulatory and/or accounting failure which was supported by Elhawary and West (2015, p. 38).

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Further reading


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