Department of Human Services

Report on Findings

Accounting Treatment for Pre-paid Fees
“Provision for Loss on Prepaid Fees”

6 March 2009

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Executive Summary

This report has been prepared for the Department of Human Services and follows on from the previously issued ‘Discussion Paper – Validation of accounting treatment of pre-paid fees’. This report specifically addresses the methods of calculating and valuing a provision for loss on pre-paid fees, journal entries to record any provision, and the appropriate accounting policy and associated note disclosures in the financial statements. Data to illustrate and support our discussions was supplied by two Trusts – The Necropolis and The Geelong Cemeteries Trust.

The following information (as a minimum) is required in order to appropriately assess a provision:

- The amount of the fee received from the customer;
- The nature of the goods and services to which the fee relates; and
- The present value of the expenditure required in order to settle each obligation associated with the fee received.

Two valuation approaches are discussed in relation to the determination of the present value of the expenditure; being:

1. Valuation Approach 1 - The cost required today (or at reporting date) to deliver the particular good or service;
2. Valuation Approach 2 - The best estimate of the expenditure required to settle the obligation, taking into account the time value if money (i.e. the present value of the future cash flow).

Risks and difficulties in the application of these valuation approaches have been identified to include:

- Use of inconsistent definitions for the classification of costs. Inconsistent classifications may lead to mis-statement of Trusts’ liabilities, comparability of reported results across the industry as well as over time being hindered, and inappropriate decisions being made based on reported information. It was noted however that these risks are minimised by the implementation of the Cemeteries common Chart of Accounts (‘CCA’).
- Differences in the methodology applied to assign indirect and overhead costs to total cost for provision of the good and service. Similar risks as those noted in respect to inconsistent classification of costs apply to use of different methodologies.
- High level of subjectivity involved in assessment of data inputs – such as time period in which the contract is likely to be settled, forecast inflation rate and discount rate - with the application of valuation approach 2. Due to subjective nature of these inputs, agreement on common rates and methodology (to promote consistency) may be difficult to obtain.
High degree of manual assessment and calculation required (particularly if Valuation approach 2 is applied) leading to increased risk of transposition and other human errors.

From our review, observations and findings (including consideration of information provided by the two nominated Trusts), we recommend:

- Use of Valuation Approach 1 as the most practical, efficient and effective method for the Trusts to adopt in the valuation of any provision for loss on pre-paid fees. This may need to be reviewed in the future where a provision for loss on pre-paid fees is likely to be material to the Trust and its results.

- A separate note disclosure be included in the first year of recognition of the provision that details the nature of the error (ie loss not previously identified and recorded), the amount of the correction at the beginning of the earliest prior period presented and the extent to which other line items are affected by the error. An example note disclosure is provided.

- The inclusion of an accounting policy note in the financial statements in respect to provisions, and incorporating commentary on provision for loss on pre-paid fees specifically. An example accounting policy note is provided.

- The provision for loss on pre-paid fees be treated as a current liability (in the same manner as unearned income) in the balance sheet.

- A note be included in the Notes to the Financial Statements disclosing the composition of the value of total provisions in the balance sheet. An example Note to the Financial Statements is provided.

- The Cemetery Trusts follow a set of guidelines for the calculation and recording of a provision for loss on pre-paid fees to promote consistency, comparability and reliability in reported results. These guidelines are provided as Appendix 4 to this report.
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1. Introduction

The Department of Human Services (‘DHS’) contracted with us to assist the Cemeteries Financial Policy Committee (‘CFPC’) with a review of the accounting policy and practices in relation to pre-paid fees. “Pre-paid fees” is the generally accepted term within the industry to describe fees received for goods and services (such as interment services and cremation services) prior to the need to perform those services.

A discussion paper was prepared in May 2008 addressing the accounting approach in valuing the pre-paid fees and identified a secondary issue - the potential recognition of a “provision for loss on pre-paid fees”.

The “provision for loss on pre-paid fees” arises when the costs to deliver goods and services exceeds the amount received.

This report:

- Briefly recounts the outcomes from the May 2008 discussion paper;
- Discusses the valuation methodology for determining the “provision for loss on pre-paid fees”, including a discussion of the identification of direct and overhead costs, and risks associated with this information;
- Presents the observations and findings from collation of information from the Nominated Trusts (The Necropolis and The Geelong Cemeteries Trust), including pro forma accounting journal entries based on those findings; and,
- Provides recommendations with regards to accounting policies, disclosure and application to prior periods.

1 The phrase ‘goods and services’ is used in this report to refer to situations where goods only are to be provided, services only are to be provided and goods and services are to be provided in respect to the fees received.
2. Brief

Original brief

The original brief called for the completion of a number of activities in order to deliver:

- An issues paper, including clear recommendations, in relation to the valuation methodology arrived at following consideration of all relevant applicable accounting standards (Deliverable 1)
- A report identifying data requirements (and their source) in order to apply the appropriate valuation methodology. This report will also identify alternate data that may be reliably substituted in the event the required data is not readily available. Risks and issues associated with the collection and quality of the data will be noted (Deliverable 2)
- Draft and final project reports incorporating a summary of findings, options and recommendations as well as journal entries, financial report extracts, and accounting policy notes and disclosures. The draft report will first be circulated and presented to CFPC members. Feedback received will be integrated in the final report (Deliverable 3)
- Pro-forma financial model template (in Microsoft Excel format) together with guidelines and instructions on use and a schedule of data fields required for populating the model (Deliverable 4)

Deliverable 1 – discussion paper in relation to the validation of accounting treatment for pre-paid fees – was issued in May 2008. The discussion paper focused on two issues:

1. Recognition and measurement of pre-paid fees, including the utilisation of a fair value model (such as a Discount Cash Flow model) to appropriately measure the current liability of pre-paid fees received; and,
2. The recognition of a provision in respect of any potential losses made on the provision of the goods and services.

The discussion paper suggested the following outcomes in respect to each of these issues.

Issue 1

The discussion paper stated the appropriate method for accounting for pre-paid fees is to recognise the nominal value as revenue on provision of the goods and/or services.

Where the delivery of the goods and services are deferred to future years, it is appropriate to take up a liability as unearned income and subsequently recognise the revenue at such a time as the goods and services are provided. This is consistent with the current accounting approach.

It was suggested by the CFPC that a Discounted Cash Flow model (‘DCF’) calculation may be used to determine the fair value of the liability.
The discussion paper suggested this was inappropriate as pre-paid fees do not constitute a financial instrument within the definition contained in AASB 132 *Financial Instruments: Presentation*.

**Issue 2**

As the cemetery trusts receive fees in advance, it was noted that consideration had not been given to the recognition of any potential losses that may be incurred in providing those services at some future date.

Under AASB 137 Provisions, Contingent Liabilities and Contingent Assets and the definition of an ‘onerous contract’, this loss should be recognised at the point in time where the costs to provide the goods and services exceed the fees received. This in essence is recognising an expense for the future loss on a pre-paid fee transaction.

AASB 137 provides that where a contract becomes onerous, a provision shall be raised for the estimated future loss.

Accounting for losses by raising a provision must be a best estimate of the expenditure required to settle the obligation, which takes into consideration the time value of money and is recorded at the present value of the future cash flow – i.e. the present value of the amount required to settle the obligation in the future.

The identification of the second issue resulted in shifting the focus from assessing the valuation of the pre-paid fees towards assessing potential losses associated with the provision of pre-paid goods and services. Consequently, our brief was amended to address this change in focus.

**Resultant Brief**

The amended brief now called for:

- The appropriate valuation methodology for the provision for loss on pre-paid fees having regard to current accounting standards;
- The data required to be captured in order to apply the appropriate provision valuation methodology above;
- The extent to which sufficient and reliable data is available at the two nominated Trusts for examination (being The Necropolis and the Geelong Cemeteries Trust), however, verification procedures were not conducted;
- Alternate data (if any) that may be used for the purpose of valuation;
- Journal entries required to record the initial transaction, any subsequent valuation adjustments and the transaction at the time of extinguishment of the liability;
- Pro-forma accounting policy note disclosures for the treatment of unearned income;
- Associated note disclosures required in relation to the application of the appropriate provision valuation methodology (particularly in the first year of application); and,
• The impact of the appropriate provision valuation methodology on the financial reports (balance sheet and operating statement) in relation to the nominated Trusts.

Adjusted Deliverables

As a result of the amendments to the brief, deliverables 2 to 4 inclusive were revised and combined into one deliverable being a report covering:

• Identification of data requirements (and their source) in order to apply the appropriate provision valuation methodology. Identify alternate data that may be reliably substituted. Risks and issues associated with the collection and quality of the data will be noted (Section 4 of this report).

• Summary of findings, options and recommendations as well as journal entries, financial report extracts and accounting policy notes and disclosures (Sections 5 and 6 of this report).

• Pro-forma summary worksheet for capture of relevant information together with guidelines and instructions on use and a schedule of data fields required for populating the worksheet (Appendix 4 to this report).
3. Approach

The following process was adopted in preparing this report:

- Identification of data requirements (and relevant sources) to determine valuation via consultations with key staff of the nominated Trusts.
- Attendance at nominated Trust sites, and discussions of information requirements, risks and difficulties associated with obtaining the information.
- Review of information gathered and of relevant accounting records.
- Review of responses to survey (conducted by DHS) circulated to remaining Trusts.

During this process, the following key people were consulted from the nominated Trusts:

<table>
<thead>
<tr>
<th>Dale Mitchell</th>
<th>Trevor Colbert</th>
</tr>
</thead>
<tbody>
<tr>
<td>Finance Manager</td>
<td>Manager, Finance and Administration</td>
</tr>
<tr>
<td>The Necropolis</td>
<td>The Geelong Cemeteries Trust</td>
</tr>
</tbody>
</table>
4. Valuation Methodology

4.1 Minimum Requirements

In order to appropriately assess any provision, three items of information are required for each pre-paid fee received:

1. The amount received from the customer;
2. The nature of the goods and services to which the fee relates; and,
3. The present value of expenditure required in order to settle each obligation associated with the fee received.

The “provision for loss on pre-paid fees” will represent the difference between the pre-paid fee received (1) and the expected expenditure (3) where the expected expenditure exceeds the fee received.

4.1.1 Pre-paid Fees

As the information may generally be required for operational and audit purposes, it is understood that Trusts should be able to produce reports detailing:

- Customers
- Goods and services purchased
- Amount received (ie pre-paid fees amount)
- Date of receipt

4.1.2 Present Value of Expenditure

We require the present value of the expenditure necessary to settle the obligation (ie. to deliver the good and service) in order to determine any potential loss to be incurred on settlement.

Two (2) valuation approaches were considered in order to determine the present value of the expenditure.

Valuation Approach 1

The cost required today (or at reporting date) to deliver the particular good or service may provide an appropriate estimation of the present value of the expenditure required in order to settle the obligation.

The basis of calculation of an appropriate estimate at reporting date was determined in conjunction with senior finance staff at the selected Trusts (The Necropolis and Geelong Cemeteries Trust) as follows:

- Direct Costs
  
  All direct costs associated with the provision of goods and services should be recorded.
Direct costs should incorporate such items as the labour incurred, the cost of raw materials consumed, costs associated with plant and equipment utilised to provide the service, and so on.

- **Overhead Costs**

  An appropriate assignment of overheads and expenses should be incorporated in the calculation of total costs associated with the provision of the goods and services. Overheads and expenses include general grounds maintenance (common areas) costs and administration expenses.

In assessing these costs, it is important to note that only costs that are incurred as a result of delivering the goods and services should be included.

It is believed that this approach represents a practical and effective solution to the calculation of present value. An alternate solution is detailed under Valuation Approach 2.

**Valuation Approach 2**

As previously noted, the provision for an onerous contract should be a best estimate of the expenditure required to settle the obligation, taking into consideration the time value of money so as to be recorded at the present value of the future cash flow – i.e. the present value of the amount required to settle the obligation in the future.

With Valuation Approach 2, calculation of a provision for an onerous contract will require the following factors to be determined:

1. Estimation of the future period when settlement of the pre-paid fees is likely to occur;
2. Estimation of the cost required to settle the pre-paid contract at this future date; and,
3. A present value calculation of that future cost.

This calculation will be required for each pre-paid fee amount received.

The considerations in respect to direct costs and overhead costs noted under Valuation Approach 1 equally apply to this Approach. Thus, this Approach may be viewed as an extension of Valuation Approach 1 for determining the present value of the future cost required to settle the obligation.

**4.2 Risks and Difficulties in Determination of Cost**

**Direct Costs**

The classification ‘direct costs’ refers to those costs incurred that may be directly attributed to the provision of particular goods and services. The nominated Trusts were both able to calculate their direct costs per unit in much the same manner; namely, by dividing the total of their direct costs recorded in the general ledger by the number of goods and services provided. This method of calculation is discussed further in Section 5 of this report.

Based on the ability of the nominated Trusts to extract and summarise the necessary data from the general ledger and supporting records, it is reasonable to
expect the remaining Trusts will also be able to determine the direct costs associated with providing the goods and services in a similar manner.

Some risk exists as a result of the inconsistent definition of ‘direct costs’ and the nature of individual items that comprise this classification. For example, one Trust may record a loss on a particular transaction whereas another may not due to the application of different definitions to the direct costs classification. The risk of under (over) statement of Trusts’ liabilities may arise as a consequence of inconsistent definitions being applied. In addition, comparability of Trusts’ reported results across the industry is hindered. Inconsistent application of definitions from period to period will also hinder comparability of results over time. A risk also arises in respect to inappropriate decisions being made as a result of these inconsistencies.

These risks are minimised by the implementation of the Cemeteries Common Chart of Accounts (‘CCA’) with effect from the 2007/08 financial year.

**Overhead Costs**

A generally accepted method of assigning overhead expenses across the delivery of goods and services is required for consistency and comparability purposes.

It is noted that an ‘overhead charge’ may vary significantly in amount from Trust to Trust given different operating structures, size, variety of services provided and other matters.

Despite the differences in value, the method of assignment however should be consistently applied. In this regard, it is noted that the nominated Trusts calculated their administration overhead component in different ways as follows:

- The Necropolis - applied a similar methodology in determining their overhead costs as to their direct costs. This method involved extracting the total administration costs from the general ledger for the year and dividing this amount by the total number of goods and services provided for the year.
- The Geelong Cemeteries Trust - applied what they deemed a reasonable percentage to the direct costs amount to arrive at a representative value for administrative costs.

Both methods of calculation are discussed further in Section 5 of this report.

Similarly to the issues addressed in relation to direct cost calculations, the risk of under (over) statement of liabilities exists where inconsistent methods of calculation are applied across the industry.

The determination of a reasonable percentage to be applied to arrive at an estimated administration overhead charge (as per approach taken by The Geelong Cemeteries Trust) is subjective in nature. It is therefore difficult to apply on a universal basis.

In this regard, determination of an overhead allocation using the approach taken by The Necropolis appears appropriate and provides a value that may be readily verified from review of the general ledger and supporting records. This methodology is also consistent with that applied in relation to the calculation of direct costs, and with the CCA Costing Worksheet report (which appears in the CCA & Reporting User Manual).
Consideration should also be given to the type of administration costs included in total administration used for the estimate of future costs. In this respect, some costs included as administration expenses may be period specific (for example, a revaluation decrement in respect to the Trust’s assets) and therefore may not be appropriate for the estimate of costs to be incurred in the provision of the goods and services. As for direct costs, consistent definition of costs to be included in the administration classification is required for comparability and reporting purposes.

It is noted that a number of Trusts, in their response to the survey, commented that determination of costs will be easier following the full implementation of the CCA.

**Present Value Calculation (under Valuation Approach 2)**

Calculation of the net present value adds a layer of complexity to the overall calculation of the estimated provision for loss on satisfaction of the contract as additional matters must be addressed during the estimation process. These include:

1. Determination of which time period the contract is likely to be settled (i.e. when is the cost likely to be incurred).

   The following methods were suggested to assist in this determination:

   (a) **Turnover** - This is an assessment based on the average period the pre-paid fees are held prior to delivering the goods and services.

   (b) **Life expectancy** - An assessment is made on when the liability is likely to be satisfied based on the age of the person who has purchased the goods and services.

   Based on our understanding of the general information captured within current accounting systems, both of these methods may be problematic as the information may not be readily available (for instance, we believe the age of the person paying the fees may not presently be captured).

2. Determination of cost:

   (a) The future cost to be paid is a function of the cost today, extrapolated at a forecast inflation rate to the estimated future time period when settlement of the contract is likely to occur. Application of an inflation rate is subjective in nature and does not provide a definitive result on what the future cost will be.

   (b) The future cost, as derived in (a) above, is then discounted back to arrive at the present value of the future cost. Determination of an appropriate discount rate is also subjective and therefore carries the inherent risks associated with use of subjective inputs. The reasons for using a different rate for inflationary and discount purposes will require notation in order to determine the reasonableness of the final costs calculated. Due to the subjectivity of these rates, agreement on a common rate, to promote consistency across the industry, may be difficult to obtain.
3. Number of pre-paid goods and services contracts:

The determination of the present value of costs associated is required for each individual good and service pre-paid contract.

Applying the above elements to each individual pre-paid contract may be overly burdensome and impractical. For instance, The Necropolis Springvale site alone had recorded pre-paid fees for approximately 10,000 pre-paid customers at 30 June 2007. The time and effort required to perform the calculations on an individual basis may outweigh any benefit to be gained from the theoretically most accurate calculation. Consequently, assessment may require application of materiality principles in order to achieve a reasonable outcome on a practical basis.

4.3 Expected Outcome

As noted above, the provision for loss on pre-paid fees will be determined after a matching of the pre-paid fee received against the expected expenditure.

The present value approaches described above may result in different outcomes as illustrated by the examples below.

Valuation Approach 1

Table 1 below illustrates an example of the expected outcome as a result of the work conducted for an interment service, where the estimated costs to provide the service have been matched against the pre-paid fee received. This example assumes that the service to be provided is the same; hence, the same costs have been applied. The value of the provision has not been discounted.

<table>
<thead>
<tr>
<th>Detail of Service to be provided</th>
<th>A Pre-paid Fee Received</th>
<th>B Direct Cost for goods and services</th>
<th>C Overhead Cost for goods and services</th>
<th>D Total Cost at 30 June 2008 B + C</th>
<th>E Provision Required (cost exceeds pre-paid fee received) A - D</th>
</tr>
</thead>
<tbody>
<tr>
<td>Interment – Person 1</td>
<td>$1,000</td>
<td>$800</td>
<td>$400</td>
<td>$1,200</td>
<td>$200</td>
</tr>
<tr>
<td>Interment – Person 2</td>
<td>$1,100</td>
<td>$800</td>
<td>$400</td>
<td>$1,200</td>
<td>$100</td>
</tr>
<tr>
<td>Interment – Person 3</td>
<td>$1,200</td>
<td>$800</td>
<td>$400</td>
<td>$1,200</td>
<td>$0</td>
</tr>
<tr>
<td>Interment – Person 4</td>
<td>$1,300</td>
<td>$800</td>
<td>$400</td>
<td>$1,200</td>
<td>$0</td>
</tr>
</tbody>
</table>

| VALUE OF PROVISION                 | $300                   |
Valuation Approach 2

As previously noted, this approach involves discounting the provision to ensure it represents the present value of the expenditures expected to be required to settle the onerous contract. The calculation of the present value firstly requires an assessment of each individual contract to determine when the good and/or service will be provided. Once the expected time period in which payment is to occur has been determined, an estimation of the future cost is necessary. Taking a practical stance, this will generally involve an assessment of today’s costs extrapolated at an inflation rate to the point in time in which provision of the good and/or service is made. Finally, this future cost is then discounted back to arrive at its present value.

Based on initial assessments performed by The Necropolis, an inflation rate of 4% and a discount rate of 6% have been used. The appropriateness of these rates has not been investigated.

Table 2 provides an example of this approach. The base information has been carried forward from Table 1 – Valuation Approach 1.

<table>
<thead>
<tr>
<th>Detail of Service to be provided</th>
<th>D Total Cost to provide good/service at 30 June 2008 (Table 1)</th>
<th>F Estimated period in which provision of good/service is likely to occur</th>
<th>G Future Costs based in inflation rate of 4% extrapolated over period in which payment is likely to occur</th>
<th>H Present Value of future cost discounted back at 6%</th>
<th>A Pre-paid Fee Received (Table 1)</th>
<th>E Provision Required (cost exceeds pre-paid fee received) A - H</th>
</tr>
</thead>
<tbody>
<tr>
<td>Interment – Person A</td>
<td>$1,200</td>
<td>2 years</td>
<td>$1,298</td>
<td>$1,155</td>
<td>$1,000</td>
<td>$155</td>
</tr>
<tr>
<td>Interment – Person B</td>
<td>$1,200</td>
<td>3 years</td>
<td>$1,350</td>
<td>$1,133</td>
<td>$1,100</td>
<td>$33</td>
</tr>
<tr>
<td>Interment – Person C</td>
<td>$1,200</td>
<td>4 years</td>
<td>$1,404</td>
<td>$1,112</td>
<td>$1,200</td>
<td>$0</td>
</tr>
<tr>
<td>Interment – Person C</td>
<td>$1,200</td>
<td>5 years</td>
<td>$1,459</td>
<td>$1,091</td>
<td>$1,300</td>
<td>$0</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>VALUE OF PROVISION</td>
<td>$188</td>
</tr>
</tbody>
</table>

The example in Table 2 demonstrates that a determination of the provision using Valuation Approach 2 is likely to result in a lower provision than that calculated under Valuation Approach 1 where the discount rate applied is greater than the inflation rate.
4.4 Additional Risks

During discussions with the senior finance staff at the nominated Trusts, it was noted that determination of the provision for loss on pre-paid fees will largely require manual assessment. Due to the significant level of manual input required, the risk of transposition and other human errors is heightened.

There are also practical issues – such as volume of transactions – to consider in the decision of the most appropriate approach to produce desired outcomes.
5. Observations and Findings

5.1 The Necropolis

5.1.1 Summary of Financial Information

The Necropolis has provided an analysis for the year ended 30 June 2007 for the Springvale site only.

Due to the large variety and volume of transactions, an assessment of all pre-paid fees was deemed unreasonable for the purpose of this assignment.

Consequently, data has only been provided for 60% of the total value of pre-paid fees in the balance sheet as at 30 June 2007, as follows:

- Total Pre-paid fees as at 30 June 2007: $9,269,650
- Pre-paid fees used in analysis below: $5,571,234
- Representing: 60%

The provision has been calculated on this sample only. It will be necessary to revise the provision, if the change of accounting policy is implemented, so as to include all pre-paid fee items due to an inability to confirm that the sample is representative of the total population (or balance of pre-paid fees).

Information for the cost components was extracted from the general ledger as at 31 May 2008. This data is considered to represent a reasonable determination of the costs associated in delivering the goods and services as at 30 June 2007 given that there has been no material changes to operations during the intervening period.

5.1.2 Summary of Results

Table 3 summarises the results from the information provided by The Necropolis for the year ended 30 June 2007. Note that the following information has been calculated under Valuation Approach 1.

Table 3 – review of pre-paid fees for The Necropolis

<table>
<thead>
<tr>
<th>Type of Good/Service</th>
<th>Pre-paid Fees per Financial Statements</th>
<th>Calculated Provision Valuation Approach 1 [1]</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cremation</td>
<td>$3,006,555</td>
<td>$113,139</td>
</tr>
<tr>
<td>Interment</td>
<td>$2,441,520</td>
<td>$83,741</td>
</tr>
<tr>
<td>Plaque</td>
<td>$123,159</td>
<td>$25,451</td>
</tr>
<tr>
<td></td>
<td>$5,571,234</td>
<td>$222,331</td>
</tr>
</tbody>
</table>

[1] Provision represents the amount where the cost to provide the good and service at the relevant time period exceeds the fees received. This has been assessed on a contract by contract basis.
As demonstrated in Table 2, the likely outcome of applying Valuation Approach 2 to arrive at the present value would result in a provision less than that calculated under Valuation Approach 1 (as above in Table 3) where the discount rate is greater than the inflation rate.

Consequently, use of Valuation Approach 1 may be considered a conservative and appropriate method of calculation.

5.1.3 Determination of Costs

Direct costs

The direct costs were determined using the total direct costs$ expense in the general ledger for the year for that particular location (that is, the Springvale site) and dividing this by the number of times in the year the related good or service was provided.

Direct Costs included items such as:

- Salaries and wages of staff associated with the provision of the particular goods and services.
- Direct running costs of plant and equipment (e.g. electricity and gas)
- Consumables and raw materials.
- Depreciation of plant and equipment.

As noted previously, this data has not been verified or audited in any way by us.

Example 1A: The Necropolis – Direct cost per unit

| (A) Direct Cremation costs per general ledger | $1,332,117 |
| (B) No. of cremations during period | 5,825 |
| Direct unit cost per cremation (A) / (B) | $229 |

Indirect and overhead costs

The indirect and overhead costs3 assignment per unit was determined by summarising all administration costs from the general ledger for the period and dividing this total by the total number of goods and services provided at the Springvale site only during the same period.

It is understood that the total administration expenses used for this assessment may incorporate expenses that relate to other sites under the administration of The Necropolis. Eliminating these ‘group’ expenses has not been conducted for the purposes of this exercise.

---

2 Data used related to the 11 months ended 31 May 2008 (as previously noted) due to being readily available for this exercise, and a reasonable approximation of costs as at 30 June 2007.

3 As per footnote 2
Administration Costs included items such as:

- Administrative staff salaries and wages
- Administration costs (e.g. depreciation of administrative plant and equipment, audit fees, insurance, etc)
- Sales and marketing related expenditure

This unit cost was then added to the direct cost per unit to come to a total unit cost per good and service.

**Example 1B: The Necropolis – Administration cost per unit**

<p>| | |</p>
<table>
<thead>
<tr>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>(A) Total Administration costs per the General Ledger</td>
<td>$5,008,946</td>
</tr>
<tr>
<td>(B) Total goods/services provided for the year</td>
<td>23,049</td>
</tr>
<tr>
<td>Administration cost per unit (A) / (B)</td>
<td>$217</td>
</tr>
</tbody>
</table>

**Total Cost**

**Example 1C: The Necropolis – Total unit cost**

<table>
<thead>
<tr>
<th></th>
<th>$</th>
</tr>
</thead>
<tbody>
<tr>
<td>Direct unit cost per cremation (per Example 1A)</td>
<td>229</td>
</tr>
<tr>
<td>Add Administration cost applied to each cremation (per Example 1B)</td>
<td>217</td>
</tr>
<tr>
<td><strong>Total cost per cremation</strong></td>
<td><strong>446</strong></td>
</tr>
</tbody>
</table>

Calculations of these costs were provided by The Necropolis and have been reviewed by us and determined to be reasonable based on the information provided.

Appendix 1 provides additional details in relation to the calculation of per unit costs for The Necropolis.

**5.1.4 Valuing the Provision (Valuation Approach 1)**

As demonstrated in Table 1, the unit cost for each good and service type is matched on a line-by-line basis with each pre-paid fee received. Where the cost exceeded the revenue received, a loss was identified. The total of these losses equated to the **provision for loss on pre-paid fees** of **$222,331**.

As noted earlier, the valuation of the provision has been performed on a sample basis and does not consider the loss that may require recognition across all pre-paid fees received. Consequently, should this approach be undertaken at future reporting periods, it will be necessary to assess all pre-paid fee line items, subject to materiality considerations.
5.1.5 Recording the Provision – Journals required at reporting date

The accounting journal entry required to recognise the total provision calculated in the example for the year ended 30 June 2007 is as follows:

<table>
<thead>
<tr>
<th>Journal Entry</th>
<th>DR</th>
<th>CR</th>
</tr>
</thead>
<tbody>
<tr>
<td>30/06/07 Loss on pre-paid interment services</td>
<td>Expense</td>
<td>113,139</td>
</tr>
<tr>
<td>30/06/07 Loss on pre-paid cremation services</td>
<td>Expense</td>
<td>83,741</td>
</tr>
<tr>
<td>30/06/07 Loss on pre-paid plaques</td>
<td>Expense</td>
<td>25,451</td>
</tr>
<tr>
<td>30/06/07 Provision for loss on pre-paid fees</td>
<td>Liability</td>
<td>222,331</td>
</tr>
</tbody>
</table>

Recognise provision at year end

The above journal has been generated based on the following assumptions:

- The amount recognised is the total provision required at 30 June 2007, thereby assuming a $nil provision in relation to the unassessed pre-paid fees.
- Prior period adjustments have been made (discussed further in section 6.2 of this report).
5.2 The Geelong Cemeteries Trust

5.2.1 Summary of Financial Information

The Geelong Cemeteries Trust provided information and data for the years ended 30 June 2006 and 30 June 2007 inclusive, on a site by site basis. The costs of providing the goods and services were classified by service type for each site.

5.2.2 Summary of Results

Table 4 summarises the results of the review of information provided by the Geelong Cemeteries Trust:

<table>
<thead>
<tr>
<th>Balance Date</th>
<th>Pre-paid Fees per Financial Statements</th>
<th>Calculated Provision Valuation Approach 1</th>
</tr>
</thead>
<tbody>
<tr>
<td>30 June 2007</td>
<td>$1,430,599</td>
<td>$49,635</td>
</tr>
<tr>
<td>30 June 2006</td>
<td>$1,257,982</td>
<td>$40,722</td>
</tr>
</tbody>
</table>

[1] Provision represents the amount where the cost to provide the good and service at the relevant time period exceeds the fees received. This has been assessed on a contract by contract basis.

As previously noted, Valuation Approach 2 will generally result in a lower provision where the discount rate used is greater than the inflation rate assumed. Given that the provision of $49,635 calculated above may generally be considered as immaterial, and the additional time and effort required, the provision was not recalculated using Valuation Approach 2 for comparison.

Consistent with the approach taken with The Necropolis, use of Valuation Approach 1 may be considered a conservative and appropriate approach.

5.2.3 Determination of Costs

Direct Costs

Similar to The Necropolis, the direct costs were determined using the total direct costs expense in the general ledger (but for the year ended 30 June 2007) for that particular service and dividing that total by the number of times in the year the related goods and services were provided.

Direct Costs included items such as:

- Salaries and wages of staff associated with the provision of the particular goods and services;
- Direct running costs of plant and equipment (e.g. electricity and gas);
- Consumables and raw materials;
- Depreciation of plant and equipment.
As noted previously, verification and audit procedures have not been performed on this data.

**Example 2A: The Geelong Cemeteries Trust – Direct costs per unit**

<table>
<thead>
<tr>
<th></th>
<th>$</th>
</tr>
</thead>
<tbody>
<tr>
<td>(A) Direct costs per general ledger</td>
<td>$175,430</td>
</tr>
<tr>
<td>(E) No. of cremations during year</td>
<td>1,009</td>
</tr>
<tr>
<td><strong>Direct Cost per Cremation</strong></td>
<td><strong>$174</strong></td>
</tr>
</tbody>
</table>

**Indirect and overhead costs**

In determining the assignment of overheads on a per unit basis, the Geelong Cemeteries Trust has applied a percentage to direct costs to arrive at a representative value of administration costs attributable to the cost of providing goods and services.

The following percentages were applied:

- Administration: 20% (applied to all goods/services)
- Perpetual maintenance: 15% (applied to interment services only)
- Cremator fees: 35% (applied to cremation services only)

It is understood that the percentage application for administration costs has been based on the professional judgement, and the performance of some analytical procedures, of the senior finance staff at The Geelong Cemeteries Trust.

It is our understanding that the cremator fees percentage represents an allowance for future replacement costs of the cremators. Such provision would generally be incorporated within direct costs per unit under the application of an appropriate depreciation policy of plant and equipment utilised in the provision of cremation services. As we have not verified or audited the underlying data, we are unable to comment on the reasonableness of this additional cost. We note that care should be taken to ensure an effective “duplication” of costs is not performed via the (1) application of an appropriate depreciation policy and (2) application of percentage allowance for replacement costs.

The application of a percentage uplift for perpetual maintenance costs may be inappropriate as such costs are not directly attributable to the provision of interment services (that is, to the physical act of interment for which the fee relates).

**Example 2B: The Geelong Cemeteries Trust – Total cost per unit**

<table>
<thead>
<tr>
<th></th>
<th>$</th>
</tr>
</thead>
<tbody>
<tr>
<td>(A) Direct costs per cremation (as per above)</td>
<td>$174</td>
</tr>
<tr>
<td>(B) Administration overhead cost (20% of A)</td>
<td>$34</td>
</tr>
<tr>
<td>(C) Cremator fees (35% of A)</td>
<td>$61</td>
</tr>
<tr>
<td>(D) Total (A + B + C)</td>
<td><strong>$269</strong></td>
</tr>
</tbody>
</table>
5.2.4 Valuing the Provision (Valuation Approach 1)

The unit costs as determined above were matched on a line-by-line basis with the pre-paid fees received. Where the cost exceeded the revenue received, a loss was identified and the total of these losses equates to the provision for loss on pre-paid fees of $49,635 for the year ended 30 June 2007.

5.2.5 Recording the provision – Journals required at reporting date

The following provides an example of the accounting journal entries required at each reporting date to recognise the provision for the onerous contract.

<table>
<thead>
<tr>
<th>Journal entry</th>
<th>DR</th>
<th>CR</th>
</tr>
</thead>
<tbody>
<tr>
<td>30/06/06 Loss on pre-paid goods and services</td>
<td></td>
<td>40,722</td>
</tr>
<tr>
<td>Provision for loss on pre-paid fees</td>
<td></td>
<td>40,722</td>
</tr>
<tr>
<td>Recognise provision at year end</td>
<td></td>
<td></td>
</tr>
<tr>
<td>30/06/07 Loss on pre-paid goods and services</td>
<td></td>
<td>8,913</td>
</tr>
<tr>
<td>Provision for loss on pre-paid fees</td>
<td></td>
<td>8,913</td>
</tr>
<tr>
<td>Recognise increase in provision/loss for the year ($49,635 - $40,722)</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

The above journals have been generated based on the following assumptions:

- ‘Prior period adjustment’ (refer to Section 6.2) has been made for the year ended 30 June 2006
- The amount recognised at 30 June 2007 represents the movement in value of the provision from 30 June 2006; that is:
  - Value of Provision at 30 June 2006: $40,722
  - Value of Provision at 30 June 2007: $49,635
  - Increase in Provision for loss on pre-paid fees: $8,913
5.3 Review of survey responses

A copy of the Request for Information is provided as Appendix 3. In response to this request, 12 of the 14 Trusts were able to provide some information.

The information returned was in line with expectations, in that 11 Trusts were able to provide detailed listing of their pre-paid fees, but unable to easily determine the costs associated with providing those goods and services.

In general terms, the information provided with regards to their pre-paid fees enables the first element of the provision for loss on pre-paid fees to be calculated.

Four respondents noted they will be better positioned to determine the costs associated with delivering their goods and services following full implementation of the CCA (which provides a framework for data capture in a consistent manner).
6. Recommendations

6.1 Valuation Approach

We believe Valuation Approach 1 provides a practical, efficient and effective method for the Trusts to adopt in the valuation of any provision for loss on pre-paid fees.

In forming our belief, we have taken into consideration the work performed at The Necropolis and the resultant provision which did not appear to be materially different to that calculated under Valuation Approach 1. We have also taken into consideration the complex and subjective nature of the calculations required under Valuation Approach 2 which do not appear to be warranted given that the simpler, direct method yields a materially similar result.

This should however be reviewed in future reporting periods as a provision may become material, and the application of a detailed valuation methodology (such as that under Valuation Approach 2) may be warranted.

6.2 Prior Period Adjustments

Under AASB 108 Accounting Policies, Changes in Accounting Estimates and Errors, we believe the above transactions will be deemed an ‘accounting error’ and, where the impact of the error is considered material, will require adjustment to the financial statements retrospectively (that is, a prior period adjustment).

This is likely to be classified as an error rather than an accounting policy change as the nature of the loss should have potentially been identified and recorded in previous periods.

This will require a separate note disclosure detailing the nature of the error, the amount of the correction at the beginning of the earliest prior period presented (in this case, 2006) and the extent to which other line items are affected by the error and have changed.

An example of this note disclosure (using the provision amounts as calculated for the Geelong Cemeteries Trust) is provided below.

Example 3: Note disclosure of an error in prior periods (where deemed material)

Note X: Prior period error

a) The entity has disclosed for the first time in its financial statements, a provision for loss on pre-paid fees in relation to pre-need fees received for goods and services. This has resulted in an error in the previous years financial statements and the effect of which has been disclosed below.
The aggregate effect of the error on the annual financial statements for the years ended 30 June 2006 and 30 June 2007 was as follows:

<table>
<thead>
<tr>
<th></th>
<th>Previously stated $</th>
<th>2006 Adjustments Dr/(Cr) $</th>
<th>Restated $</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Balance Sheet</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Provision for loss on pre-paid fees</td>
<td>-</td>
<td>(40,722)</td>
<td>(40,722)</td>
</tr>
<tr>
<td>Net Assets</td>
<td>1,000,000 [1]</td>
<td>(40,722)</td>
<td>959,278 [2]</td>
</tr>
<tr>
<td><strong>Income Statement</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Loss on pre-paid goods/services (or other component of the Income Statement)</td>
<td>-</td>
<td>40,722</td>
<td>40,722</td>
</tr>
<tr>
<td>Profit/(loss) for the period</td>
<td>200,000 [1]</td>
<td>40,722</td>
<td>159,278 [2]</td>
</tr>
</tbody>
</table>

|                        |                     |                             |            |
| **2007**               |                     |                             |            |
| **Balance Sheet**      |                     |                             |            |
| Provision for loss on pre-paid goods and services | -                 | (49,635)                    | (49,635)   |
| Net Assets             | 2,000,000 [1]       | (49,635)                    | 1,950,365 [2]|
| **Income Statement**   |                     |                             |            |
| Loss on pre-paid goods/services (or other component of the Income Statement) | -                 | 8,913                       | 8,913      |
| Profit/(loss) for the period | 400,000 [1]       | 8,913                       | 391,087 [2]|

[1] Theoretical balance representing value prior to adjustments

6.3 Accounting Policy

We recommend the following accounting policy note be included in the financial statements:

**Provisions**

Provisions are recognised when either a legal or constructive obligation, as a result of a past event, exists at the balance sheet date and where the amount of the obligation can be reliably estimated. A provision will also be recognised for onerous contracts where the unavoidable costs of meeting the obligations under the contract exceed the economic benefits that expect to be received under it.

**Provision for loss on pre-paid fees**

A provision is recognised in relation to pre-paid fees where the cost of providing the purchased goods and services is expected to be greater than the amount received / revenue to be recognised.

The provision represents the present value of the expenditure required to provide the goods and services, less the amount of revenue to be recognised.
6.4 Classification – Current vs Non-Current

The provision for loss on pre-paid fees should be classified in a consistent manner with the current classification of the pre-paid fees (unearned income) liability. It is our understanding that unearned income is classified as a current liability.

An argument may arise where the future payment of the provision for loss on pre-paid fees is not expected within a period of 12 months, leading to possibility that a portion of the provision may in fact be non-current in nature.

This same argument may be made for the pre-paid fees, however we understand that as the Trust’s do not have an unconditional right to defer settlement, the liability for pre-paid fees is recorded as a current liability. As noted above, we believe the provision for loss on pre-paid fees should be treated in the same manner as the potential payment for the loss on pre-paid fees cannot be deferred.

6.5 Financial Statement Disclosures

In addition to the accounting policy noted above, the following Provisions note should be included in the Notes to the Financial Statements.

An example has been provided below, using the information provided by the Geelong Cemeteries Trust.

*Example 4: Notes to the financial statements - Provisions*

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Provision for loss on pre-paid goods and services</td>
<td>$49,635</td>
<td>$40,722</td>
</tr>
<tr>
<td>Other provisions (eg. Employee Entitlements etc)</td>
<td>$X</td>
<td>$X</td>
</tr>
<tr>
<td><strong>Total Provisions</strong></td>
<td><strong>49,635</strong></td>
<td><strong>40,722</strong></td>
</tr>
</tbody>
</table>

6.6 Calculation of provision for loss on pre-paid fees

A set of guidelines has been developed to assist Trusts with the calculation and recording of a provision for loss on pre-paid fees, and is included as Appendix 4. We recommend these guidelines, which are consistent with the costing methodology utilised in the CCA Costing Worksheet, be followed by Trusts in the calculation of the required provisions to promote consistency, comparability and reliability in reported results.
Appendix 1

Calculation of Costs – The Necropolis

DIRECT COSTS

### Cremation Services

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>(A) Direct costs per general ledger</td>
<td>1,332,117</td>
</tr>
<tr>
<td>(B) No. of cremations during year</td>
<td>5,825</td>
</tr>
<tr>
<td>Direct unit cost per cremation (A) / (B)</td>
<td>229</td>
</tr>
<tr>
<td>Administration cost applied to each cremation</td>
<td>217</td>
</tr>
<tr>
<td>Total cost per cremation</td>
<td>446</td>
</tr>
</tbody>
</table>

### Interment Services

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>(A) Direct costs per general ledger</td>
<td>1,005,654</td>
</tr>
<tr>
<td>(B) No. of interments during year</td>
<td>1,831</td>
</tr>
<tr>
<td>Direct unit cost per interment (A) / (B)</td>
<td>549</td>
</tr>
<tr>
<td>Administration cost applied to each interment</td>
<td>217</td>
</tr>
<tr>
<td>Total cost per interment</td>
<td>766</td>
</tr>
</tbody>
</table>

### Memorial plaques

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cost per most recent purchase invoice</td>
<td>163</td>
</tr>
<tr>
<td>Administration cost applied to each plaque</td>
<td>217</td>
</tr>
<tr>
<td>Total cost of each plaque</td>
<td>380</td>
</tr>
</tbody>
</table>
### OVERHEAD COSTS

#### Calculation of per unit cost

<table>
<thead>
<tr>
<th>Type of activity</th>
<th>Number of times activity performed during the period</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cremations</td>
<td>5,825</td>
</tr>
<tr>
<td>Interments (burial)</td>
<td>1,831</td>
</tr>
<tr>
<td>Interments (mausoleum)</td>
<td>110</td>
</tr>
<tr>
<td>Cremation memorial sales</td>
<td>2,486</td>
</tr>
<tr>
<td>Net Pre-paid Cremation/Interments etc sales</td>
<td>1,008</td>
</tr>
<tr>
<td>Function Room bookings</td>
<td>1,104</td>
</tr>
<tr>
<td>Chapel services</td>
<td>2,326</td>
</tr>
<tr>
<td>Granite sales</td>
<td>851</td>
</tr>
<tr>
<td>Plaque sales</td>
<td>4,261</td>
</tr>
<tr>
<td>Mausoleum sales</td>
<td>98</td>
</tr>
<tr>
<td>Urns/Jewellery</td>
<td>489</td>
</tr>
<tr>
<td>Grave sales</td>
<td>2,660</td>
</tr>
<tr>
<td><strong>TOTAL ACTIVITIES</strong></td>
<td><strong>23,049</strong></td>
</tr>
<tr>
<td>Total administration costs per the general ledger</td>
<td><strong>$5,008,946</strong></td>
</tr>
<tr>
<td>Administration cost applied to each good/service</td>
<td><strong>$217</strong></td>
</tr>
</tbody>
</table>
Appendix 2 - Calculation of Costs – The Geelong Cemeteries Trust

DIRECT & OVERHEAD COSTS

Cremation Services

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>(A) Direct costs per general ledger</td>
<td>$175,430</td>
</tr>
<tr>
<td>(B) Administration overhead cost (20% of A)</td>
<td>$35,086</td>
</tr>
<tr>
<td>(C) Cremator fees (35% of A)</td>
<td>$61,401</td>
</tr>
<tr>
<td>(D) Total (A + B + C)</td>
<td>$271,917</td>
</tr>
<tr>
<td>(E) No. of cremations during year</td>
<td>1,009</td>
</tr>
<tr>
<td>Average cost per cremation (D / E)</td>
<td>$269</td>
</tr>
</tbody>
</table>
Interment Services

The direct costs were taken from the general ledger for the year ending 30 June 2007. These costs have been classified according to each cemetery site as the costs differ between each site.

<table>
<thead>
<tr>
<th></th>
<th>Eastern</th>
<th>Western</th>
<th>Highton</th>
<th>Grovedale</th>
<th>Geelong MP</th>
<th>Flinders MP</th>
<th>Leopold</th>
<th>Drysdale</th>
<th>Portarlington</th>
<th>Mt Duneed</th>
</tr>
</thead>
<tbody>
<tr>
<td>(A) Direct costs per general ledger</td>
<td>$167,357</td>
<td>$58,866</td>
<td>$51,410</td>
<td>$148</td>
<td>$3,865</td>
<td>$8,255</td>
<td>$6,064</td>
<td>$12,123</td>
<td>$12,797</td>
<td>$2,916</td>
</tr>
<tr>
<td>(B) Administration overhead cost (20% of A)</td>
<td>$33,471</td>
<td>$11,773</td>
<td>$10,282</td>
<td>$30</td>
<td>$773</td>
<td>$1,651</td>
<td>$1,213</td>
<td>$2,425</td>
<td>$2,559</td>
<td>$583</td>
</tr>
<tr>
<td>(C) Perpetual maintenance costs (15% of A)</td>
<td>$25,104</td>
<td>$8,380</td>
<td>$7,712</td>
<td>$22</td>
<td>$580</td>
<td>$1,238</td>
<td>$910</td>
<td>$1,818</td>
<td>$1,920</td>
<td>$437</td>
</tr>
<tr>
<td>(D) Total (A + B + C)</td>
<td>$225,932</td>
<td>$79,469</td>
<td>$69,404</td>
<td>$200</td>
<td>$5,218</td>
<td>$11,144</td>
<td>$8,187</td>
<td>$16,366</td>
<td>$17,276</td>
<td>$3,936</td>
</tr>
<tr>
<td>(E) No. of interments during year</td>
<td>377</td>
<td>121</td>
<td>149</td>
<td>-</td>
<td>10</td>
<td>19</td>
<td>14</td>
<td>25</td>
<td>24</td>
<td>7</td>
</tr>
<tr>
<td><strong>Average cost per interment (D / E)</strong></td>
<td>$599</td>
<td>$657</td>
<td>$466</td>
<td>N/A</td>
<td>$522</td>
<td>$587</td>
<td>$585</td>
<td>$655</td>
<td>$720</td>
<td>$562</td>
</tr>
</tbody>
</table>

**ADDITIONAL COSTS**

These costs are for additional goods/services available, at an additional cost to the direct cost in the table above. These costs are uniform across each of the sites.

- Oversize Grave: Additional 33% of total cost
- 9' Interment: Additional 33% of total cost
- Inter Cremated Remains: $30 (for 0.5 hours)
- With Attendance: $45 (for 0.75 hours)
- Ledger Removal: $120 (for 2 staff for 1 hour)
- Sand: $69 (for 3 metres)

**Note:** Detailed cost calculations for the year ended 30 June 2006 were not provided by GCT.
Appendix 3

Request for Information

To: (Name of Trust)

Thank you for assisting in this information gathering process.

Purpose

We have commissioned Pitcher Partners Consulting (‘PPC’) to undertake an accounting project in regards to the accounting treatment of pre-paid (pre-need) fees.

PPC are seeking to gain a better understanding of the information available in relation to the recording of the fees received in respect to pre-need services as a liability and the direct costs associated with providing those services.

This request for information (‘RFI’) form is aimed at collating a base level of information in relation to these areas which may then be used by PPC to tailor their approach.

Please read each request fully. Any queries in relation to the information required may be directed to either Robert Thorp or Louise James for clarification. Contact details appear below.

Information Required

1. Listing of all pre-need services purchased that comprise the balance in the liability account as at 30 June 2007 and as at 30 June 2006. It is envisaged that this listing will show the following (as a minimum):
   - the type of service for which the fees were received (ie cremation services, interment services, and memorialisation - purchase of urn, plaque or similar memorialisation item - services)
   - the amount of fees received in relation to the service listed (ie this may not be the same as the total amount received which may have included an amount in relation to the right of interment and administration fees which were taken up as income at the time of receipt)

2. The direct costs associated with the provision of each of the pre-need services (ie. interment, cremation and moralisation services) in the listings above as at 30 June 2007 and as at 30 June 2006.

An example is attached for your reference.

Please also provide contact details for the person preparing the response (so as to direct any points for clarification to the appropriate person) in the box provided below.

The completed schedules should be returned to the attention of Ms Anna Achia, either by fax or email as provided below, by close of business on Friday, 30 May 2007.
Contact details for any queries on information requirements – Pitcher Partners

<table>
<thead>
<tr>
<th>Details</th>
<th>1st contact</th>
<th>2nd contact</th>
</tr>
</thead>
<tbody>
<tr>
<td>Name</td>
<td>Mr Robert Thorp</td>
<td>Ms Louise James</td>
</tr>
<tr>
<td>Phone</td>
<td>8610-5531</td>
<td>8610-5389</td>
</tr>
<tr>
<td>Fax</td>
<td>8610-5999</td>
<td>8610-5791</td>
</tr>
<tr>
<td>Mobile</td>
<td>0402 289 825</td>
<td>0408 318 084</td>
</tr>
<tr>
<td>Email</td>
<td><a href="mailto:robert.thorp@pitcher.com.au">robert.thorp@pitcher.com.au</a></td>
<td><a href="mailto:louise.james@pitcher.com.au">louise.james@pitcher.com.au</a></td>
</tr>
</tbody>
</table>

Contact details of person preparing the information – Cemetery Trust

<table>
<thead>
<tr>
<th>Details</th>
<th>Contact</th>
</tr>
</thead>
<tbody>
<tr>
<td>Name</td>
<td></td>
</tr>
<tr>
<td>Phone</td>
<td></td>
</tr>
<tr>
<td>Fax</td>
<td></td>
</tr>
<tr>
<td>Email</td>
<td></td>
</tr>
</tbody>
</table>

Contact details for return of information – Department of Human Services

<table>
<thead>
<tr>
<th>Details</th>
<th>Contact</th>
</tr>
</thead>
<tbody>
<tr>
<td>Name</td>
<td>Ms Anna Achia</td>
</tr>
<tr>
<td>Phone</td>
<td>9096-5044</td>
</tr>
<tr>
<td>Fax</td>
<td></td>
</tr>
<tr>
<td>Email</td>
<td><a href="mailto:Anna.achia@dhs.vic.gov.au">Anna.achia@dhs.vic.gov.au</a></td>
</tr>
</tbody>
</table>
Appendix 4

Guidelines for determining ‘provision for loss on pre-paid fees’

Unearned income liability (Pre-paid fees received)

Each Trust should maintain a list of pre-paid fees received and include the following essential information for each customer at a minimum:

- Customer name (and/or other applicable reference)
- The nature of the goods and services (for example, interment, cremation, plaque);
- Date fee was received; and,
- Nominal amount received;

To facilitate the matching of the nominal amount received with the cost of the service, Trusts may choose to maintain this information in a spreadsheet format. In such instances, the above information would be contained in the spreadsheet columns as illustrated in the following table:

<table>
<thead>
<tr>
<th>Customer ref</th>
<th>Service</th>
<th>Date</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Person 1</td>
<td>Interment</td>
<td>1/1/1998</td>
<td>$500</td>
</tr>
<tr>
<td>Person 2</td>
<td>Interment</td>
<td>1/1/2000</td>
<td>$750</td>
</tr>
<tr>
<td>Person 3</td>
<td>Cremation</td>
<td>1/3/2001</td>
<td>$600</td>
</tr>
</tbody>
</table>

The columns to the right of these within the spreadsheet may then be used to capture cost information.

The sorting of this information by service may assist with the completion of the cost information within the spreadsheet as the cost for each particular service will remain constant – for example, the cost per interment at the end of the reporting period will be the same for each pre-paid fee for interment, and so on. Therefore, the cost information may be input in the first cell relating to that particular service and copied down that column for each pre-paid fee received.

Cost determination

Note – the determination of cost per good and service as described in these guidelines is consistent with the methodology used in the CCA Costing Worksheet. Trusts may refer to the guidelines for that report in the CCA & Reporting User Manual for additional information. Trusts may use the CCA Costing Worksheet for the purpose of determining total cost per good and service for use in the calculation of the value of provision for loss on pre-paid fees.

Direct costs

Direct costs will be determined with reference to data extracted from the general ledger, and will include all costs that may be attributed to the particular goods and services.
Direct costs may include:

- Labour costs to perform the services (such as salary and wages, superannuation, work cover, and other related staff costs)
- Cost of materials consumed in the provision of the goods and services
- Costs associated with the plant and equipment used in the performance of the service (such as depreciation, repairs and maintenance, and plant hire fees)

The direct cost per unit may be calculated as:

\[
\frac{\text{Total direct costs for the goods and services (specific nature) for the year}}{\text{Total number of goods and services (specific nature) provided}}
\]

**Example – direct costs attributable to cremation services**:

Direct costs for 2008/09 are:

- Crematorium staff (eg salary and wages, oncosts and other staff related) $75,000
- Materials (eg remains containers) $5,000
- Cremators (eg depreciation, repairs, general maintenance) $20,000
- Other direct costs (eg gas, light and power, cleaning, computer services) $20,000
- **Total direct costs** $120,000

Total cremations provided during 2008/09 = 1,200

**Total direct cost per cremation** = $100

Calculated as follows:

\[
\frac{\text{Direct costs}}{\text{Number of cremations}} = \frac{120,000}{1,200}
\]

**Allocatable overheads**

Allocatable overheads is a classification of costs within the CCA. It is defined as relating to those costs that may be easily identified to each service business unit (such as interments, cremations, mausoleum, and so on); however, are not directly attributable to a particular service within that business unit and therefore are not included in direct costs. For example, interment within a lawn grave is a particular service within the interments business unit. Direct costs are those that may be attributed to providing interment services within a lawn grave and allocatable overheads may be attributed to interment services in general. Further clarification on the distinction of these classifications may be obtained from the CCA & Reporting User Manual.

The allocatable overhead (`AOH`) cost per unit may be calculated as:

\[
\frac{\text{Total direct costs}}{\text{Total number of goods and services (specific nature) provided}}
\]

\[
\frac{120,000}{1,200} = 100
\]

Footnote:

4 The distinction between direct costs and allocatable overheads was not made in relation to the nominated trusts (in the body of the report) as the information was not readily available for the relevant years.
Total AOH for the service business unit for the year
Total number of goods and services (for the unit) provided

Example – allocatable overheads attributable to cremation services:

Allocatable overheads for 2008/09 are:

- Customer services staff (e.g., salary and wages, oncosts and other staff related) \( \$20,000 \)
- Printing & stationery \( \$5,000 \)
- Other general expenses \( \$5,000 \)

**Total direct costs \( \$30,000 \)**

Total cremation services (including chapel) provided during 2008/09 = 1,500

**Total allocatable overhead per cremation = \$20**

Calculated as follows:

\[
\frac{\text{Allocatable overheads}}{\text{Number of services}} = \frac{30,000}{1,500} = \$20
\]

Indirect and overhead costs

Indirect and overhead costs, as discussed in the report, include:

- Grounds maintenance costs; and,
- Administration costs

In general, grounds maintenance includes costs associated with the maintenance of the common areas and which are not attributable to a particular service business unit.

Grounds maintenance costs are assigned in two parts:

1. To the service on the basis of land dimensions; and,
2. To the unit of service on the basis of number of services provided.

Details in relation to the calculation of land dimensions for assignment purposes are provided in the guidelines to the CCA Costing Worksheet.

Example – grounds maintenance attributable to cremation services:

Grounds maintenance for 2008/09 are:

- Labour costs (e.g., salary and wages, oncosts and other staff related) \( \$200,000 \)
- Materials (e.g., soils, pesticides) \( \$15,000 \)
- Plant & equipment (e.g., depreciation, repairs, general maintenance) \( \$50,000 \)
- Other costs (e.g., loose tools, motor vehicle) \( \$35,000 \)

**Total grounds maintenance costs \( \$300,000 \)**

Land dimensions:

---

5 The distinction between grounds maintenance and administration costs was not made in relation to the nominated trusts (in the body of the report) as the information was not readily available for the relevant years.
• Total cemetery = 25,000m²
• Cremation services = 1,000m²

Total cremation services (including chapel) provided during 2008/09 = 1,500

Grounds maintenance relating to cremation services:

\[
\begin{array}{ccc}
\text{Cremation services} & \times & \text{Grounds maintenance costs} \\
1,000 \text{ m}^2 & \times & 25,000 \text{ m}^2 \\
= & 12,000 \\
\end{array}
\]

Total grounds maintenance per cremation = $8

Calculated as follows:

\[
\frac{\text{Grounds maintenance}}{\text{Number of services}} = \frac{12,000}{1,500}
\]

In general, administration includes costs associated with the general administration of the cemetery trust and which are not attributable to a particular service business unit. Examples include:

• Administrative and finance staff salaries and wages, salary oncosts and other staff related (such as training)
• Depreciation on administrative plant & equipment
• Professional service fees such as accounting, audit, legal

Administration costs may be assigned based on the total number of goods and services provided by the Trust during the year.

Example – administration attributable to cremation services:

Administration costs for 2008/09 are:

\[
\begin{align*}
\text{Staff costs (eg salary and wages, oncosts and other staff related)} \quad & 440,000 \\
\text{Computer expenses} \quad & 25,000 \\
\text{Printing & stationery} \quad & 15,000 \\
\text{Professional fees} \quad & 60,000 \\
\text{Depreciation} \quad & 10,000 \\
\text{Other costs (eg motor vehicle)} \quad & 50,000 \\
\text{Total administration costs} \quad & 600,000
\end{align*}
\]

Total goods and services for the Trust provided during 2008/09 = 6,000

Total administration per cremation = $100

Calculated as follows:

\[
\frac{\text{Administration costs}}{\text{Total number of services}} = \frac{600,000}{6,000}
\]
Total cost per unit

This value represents the sum of each of the components as calculated above, namely:

Values taken from above examples:

<table>
<thead>
<tr>
<th>Description</th>
<th>Value ($)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Direct cost</td>
<td>100</td>
</tr>
<tr>
<td>Allocatable overhead</td>
<td>20</td>
</tr>
<tr>
<td>Grounds maintenance</td>
<td>8</td>
</tr>
<tr>
<td>Administration</td>
<td>100</td>
</tr>
<tr>
<td><strong>Total cost</strong></td>
<td><strong>$228</strong></td>
</tr>
</tbody>
</table>

Calculation of provision

Using the listing of pre-paid fees, the total cost per good and service as calculated may be matched against each pre-paid fee received (ie for each individual contract). A loss results where the cost exceeds the nominal fee received. The sum of these losses equates to the provision on loss of pre-paid fees required to be disclosed at reporting date. An example of this process is shown in the table below.

<table>
<thead>
<tr>
<th>Customer ref</th>
<th>Service</th>
<th>Date</th>
<th>Fee received</th>
<th>Total Cost at 30/6/09</th>
<th>Provision Required (cost exceeds pre-paid fee received)</th>
<th>C - D</th>
</tr>
</thead>
<tbody>
<tr>
<td>Person 1</td>
<td>Cremation</td>
<td>1/1/1999</td>
<td>$180</td>
<td>$228</td>
<td>$48</td>
<td></td>
</tr>
<tr>
<td>Person 2</td>
<td>Cremation</td>
<td>1/1/2002</td>
<td>$200</td>
<td>$228</td>
<td>$28</td>
<td></td>
</tr>
<tr>
<td>Person 3</td>
<td>Cremation</td>
<td>1/1/2004</td>
<td>$230</td>
<td>$228</td>
<td>$0</td>
<td></td>
</tr>
<tr>
<td>Person 4</td>
<td>Cremation</td>
<td>1/1/2006</td>
<td>$250</td>
<td>$228</td>
<td>$0</td>
<td></td>
</tr>
</tbody>
</table>
| **Total pre-paid fees per GL** | $860     | **VALUE OF PROVISION** | $76

Journal entries

Using the above example, the journal entries required would be as follows:

Value of provision year 30 June 2008 | $50
Value of provision year 30 June 2009 | $76
Journal entry | DR | CR
--- | --- | ---
30/06/08 | Loss on pre-paid goods and services | Expense | 50
| Provision for loss on pre-paid fees | Liability | 50
| Recognise provision at year end | | |
30/06/09 | Loss on pre-paid goods and services | Expense | 26
| Provision for loss on pre-paid fees | Liability | 26
| Recognise increase in provision/loss for the year ($76 - $50) | | |

Financial Statement disclosures

The following disclosures to be included in the Notes to the Financial Report at balance date:

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Provision for loss on pre-paid goods and services</td>
<td>76</td>
<td>50</td>
</tr>
<tr>
<td>Other provisions (eg. Employee Entitlements etc)</td>
<td>10</td>
<td>10</td>
</tr>
<tr>
<td>Total Provisions</td>
<td>86</td>
<td>60</td>
</tr>
</tbody>
</table>

Accounting Policy Note disclosure

We recommend the following accounting policy note be included in the financial statements.

**Provisions**

Provisions are recognised when either a legal or constructive obligation, as a result of a past event, exists at the balance sheet date and where the amount of the obligation can be reliably estimated. A provision will also be recognised for onerous contracts where the unavoidable costs of meeting the obligations under the contract exceed the economic benefits that expect to be received under it.

**Provision for loss on pre-paid goods/services**

A provision is recognised in relation to pre-paid fees where the cost of providing the purchased goods and/or services is expected to be greater than the amount received/revenue to be recognised.

The provision represents the present value of the expenditure required to provide the goods and/or service, less the amount of revenue to be recognised.