New South Wales Treasury Corporation

Tweed Shire Council

Financial Assessment and Benchmarking Report

4 October 2012

Prepared by NSW Treasury Corporation as part of the Local Infrastructure Renewal Scheme

Disclaimer

This report has been prepared by New South Wales Treasury Corporation (TCorp) in accordance with the appointment of TCorp by the Division of Local Government (DLG) as detailed in TCorp's letters of 22 December 2011 and 28 May 2012. The report has been prepared as part of the Local Infrastructure Renewal Scheme (LIRS) announced by the NSW Government.

The report has been prepared based on information provided to TCorp as set out in Section 2.2 of this report. TCorp has relied on this information and has not verified or audited the accuracy, reliability or currency of the information provided to it for the purpose of preparation of the report. TCorp and its directors, officers and employees make no representation as to the accuracy, reliability or completeness of the information contained in the report.

In addition, TCorp does not warrant or guarantee the outcomes or projections contained in this report. The projections and outcomes contained in the report do not necessarily take into consideration the commercial risks, various external factors or the possibility of poor performance by the Council all of which may negatively impact the financial capability and sustainability of the Council. The TCorp report focuses on whether the Council has reasonable capacity, based on the information provided to TCorp, to take on additional borrowings within prudent risk parameters and the limits of its financial projections.

The report has been prepared for Tweed Shire Council, the LIRS Assessment Panel and the DLG. TCorp shall not be liable to Tweed Shire Council or have any liability to any third party under the law of contract, tort and the principles of restitution or unjust enrichment or otherwise for any loss, expense or damage which may arise from or be incurred or suffered as a result of reliance on anything contained in this report.

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Section 1 Executive Summary

This report provides an independent assessment of Tweed Shire Council's (the Council) financial capacity and its ability to undertake additional borrowings. The analysis is based on a review of the historical performance, current financial position, and long term financial forecasts. It also benchmarks the Council against its peers using key ratios.

The report is primarily focused on the financial capacity of the Council to undertake additional borrowings as part of the Local Infrastructure Renewal Scheme (LIRS).

Council has made two applications for drainage schemes for $2.3m, and $1.1m respectively, to be repaid over 10 years.

TCorp's approach has been to:

- Review the most recent three years of Council's consolidated financial results
- Conduct a detailed review of the Council's 10 year financial forecasts. The review of the financial forecasts focused on the particular Council fund that was undertaking the proposed debt commitment. For the Council, the project is being funded from the General Fund so we focused our review on the General Fund

The Council has been well managed over the review period based on the following observations:

- While Council has incurred operating deficits (excluding grants and contributions for capital purposes), Council's underlying operating results (measured using EBITDA) have improved from $33.5m in 2009 to $37.6m in 2011
- Council's Unrestricted Current Ratio has been well above benchmark in the past three years indicating Council has sufficient liquidity
- Council has been spending at levels close to benchmark in respect of asset maintenance

Council's reported Infrastructure Backlog of $58.0m in 2011 represents 3.5% of its infrastructure asset value of $1,659.4m. Other observations include:

- While Council has been spending at levels close to benchmark in respect to asset maintenance, the required asset renewal benchmarks are not being met consistently to keep the assets in their current condition, therefore it is likely that the backlog will grow

The key observations from our review of Council's 10 year forecasts for its General Fund are:

- Council's operating results are forecast to improve over the lifetime of the forecast
- Council's level of fiscal flexibility is sound as Own Source Operating Revenue is maintained at levels above 70.0%
- Council anticipate a funding gap of $10.0m p.a. between budgeted expenditure amounts and amounts required to be expended to keep assets in their current condition
- Council needs to update their asset valuation technique, to generate more accurate depreciation estimates which will improve financial planning
- The key assumptions that underpin the financial forecasts are considered to be reasonable

In our view, the Council has the capacity to undertake the combined additional borrowings of $4.4m for the two LIRS projects. This is based on the following analysis:

- The DSCR remains above a benchmark of 2.00x each year of the 10 year forecast
- The Interest Cover Ratio remains above the benchmark of 4.00x for the majority of the 10 year forecast

In respect of the Benchmarking analysis TCorp has compared the Council's key ratios with other councils in DLG Group 5. The key observations are:

- Council's financial flexibility as indicated by the Operating Ratio and Own Source Operating Revenue Ratio has improved to be in line with the group's average
- Council's DSCR and Interest Cover Ratio are close to the benchmark and below the group average. In the medium term Council is forecasting ratios in line with benchmark
- Council was in a sound liquidity position which on average is slightly above the group's average liquidity level
- Council performs strongly in terms of its Building and Infrastructure Asset Renewal Ratio and comparatively low level of Infrastructure Backlog

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Section 2 Introduction

2.1: Purpose of Report

This report provides the Council with an independent assessment of their financial capacity and performance measured against a peer group of councils which will complement their internal due diligence, and the IP&R system of the Council and the DLG.

The report is to be provided to the LIRS Assessment Panel for its use in considering applications received under the LIRS.

The key areas focused on are:

- The financial capacity of the Council to undertake additional borrowings
- The financial performance of the Council in comparison to a range of similar councils and measured against prudent benchmarks

2.2: Scope and Methodology

TCorp's approach was to:

- Review the most recent three years of the Council's consolidated audited accounts using financial ratio analysis. In undertaking the ratio analysis TCorp has utilised ratio's substantially consistent with those used by Queensland Treasury Corporation (QTC) initially in its review of Queensland Local Government (2008), and subsequently updated in 2011
- Conduct a detailed review of the Council's 10 year financial forecasts including a review of the key assumptions that underpin the financial forecasts. The review of the financial forecasts focused on the particular Council fund that was undertaking the proposed debt commitment. For example where a project is being funded from the General fund we focussed our review on the General fund
- Identify significant changes to future financial forecasts from existing financial performance and highlight risks associated with such forecasts
- Conduct a benchmark review of a Council's performance against its peer group
- Prepare a report that provides an overview of the Council's existing and forecast financial position and its capacity to meet increased debt commitments
- Conduct a high level review of the Council's IP&R documents for factors which could impact the Council's financial capacity and performance

In undertaking its work, TCorp relied on:

- Council's audited financial statements (2008/09 to 2010/11)
- Council's financial forecast model
- Council's IP&R documents
- Discussions with Council officers
- Council's submissions to the DLG as part of their LIRS application
- Other publicly available information such as information published on the IPART website

Benchmark Ratios

In conducting our review of the Councils' financial performance and forecasts we have measured performance against a set of benchmarks. These benchmarks are listed below. Benchmarks do not necessarily represent a pass or fail in respect of any particular area. One-off projects or events can impact a council's performance against a benchmark for a short period. Other factors such as the trends in results against the benchmarks are critical as well as the overall performance against all the benchmarks. As councils can have significant differences in their size and population densities, it is important to note that one benchmark does not fit all.

For example, the Cash Expense Ratio should be greater for smaller councils than larger councils as a protection against variation in performance and financial shocks.

Therefore these benchmarks are intended as a guide to performance.

The Glossary attached to this report explains how each ratio is calculated.

Ratio	Benchmark
Operating Ratio	> (4.0%)
Cash Expense Ratio	> 3.0 months
Unrestricted Current Ratio	> 1.50x
Own Source Operating Revenue Ratio	> 60.0%
Debt Service Cover Ratio (DSCR)	> 2.00x
Interest Cover Ratio	> 4.00x
Infrastructure Backlog Ratio	< 0.02x
Asset Maintenance Ratio	> 1.00x
Building and Infrastructure Asset Renewal Ratio	> 1.00x
Capital Expenditure Ratio	> 1.10x

2.3: Overview of the Local Government Area

Tweed Shire Council LGA	
Locality & Size	
Locality	North Coast
Area	1,307 km²
DLG Group	5
Demographics	
Population	85,105
% under 20	23.9%
% between 20 and 60	49.6%
% over 60	26.5%
Expected population 2031	125,000
Operations	
Number of employees (FTE)	655
Annual revenue	$137.0m
Infrastructure	
Roads	1,447 km
Road Bridges	277
Infrastructure backlog value	$58.0m
Total infrastructure value	$1,659.4m

Tweed Shire Council Local Government Area (LGA) is located in the north east corner of New South Wales, in a diverse area featuring coastal villages, urban centres, rural villages and agricultural activities. The LGA adjoins the NSW shires of Byron, Lismore and Kyogle with the Gold Coast City Council area and Scenic Rim Regional Council to its north.

Council has a sizeable infrastructure to manage. There are 1,262 km of sealed roads, 185 km of unsealed roads, and 277 road bridges to manage. Putting further demands on council resources are 83 playgrounds, three libraries and three swimming pools.

The LGA has one of the fastest growing populations in NSW, with population growth estimated at 2.5% p.a. compared to the NSW average of 2.1%. This will result in increased demand for new services and place greater demands on existing infrastructure.

The Council employs 655 full time equivalent employees which increased from 648 at 30 June 2009.

2.4: LIRS Application

Council has made two LIRS applications.

Project 1: Blue Jay Circuit Drainage Scheme

Description: The Blue Jay Circuit Drainage Scheme drains from east to west and discharges to the Kingscliff Drain. The catchment area contains extensive existing urban development and is zoned to provide significant future urban growth, including residential and industrial subdivision. There is no alternative drainage outlet available to the catchment. This trunk drainage pipeline will prevent flooding of existing developed areas of Kingscliff and facilitate residential subdivision and development throughout the catchment.

Amount of loan facility: $2.3m

Term of loan facility: 10 years

Project 2: Drainage – General works

Description: Rehabilitation and upgrade of existing drainage assets.

Amount of loan facility: $1.1m

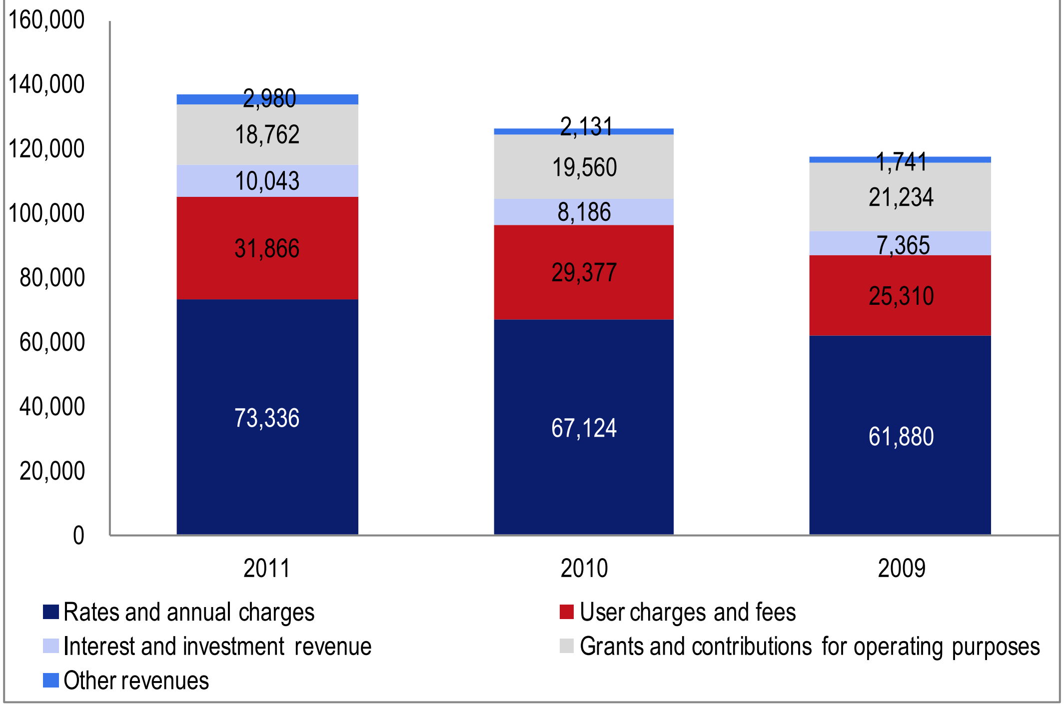
Term of loan facility: 10 years

Section 3 Review of Financial Performance and Position

In reviewing the financial performance of the Council, TCorp has based its review on the annual audited accounts of the Council unless otherwise stated.

3.1: Revenue

Figure 1 - Revenue Sources for 2008/09 to 2010/11 ($'000s)



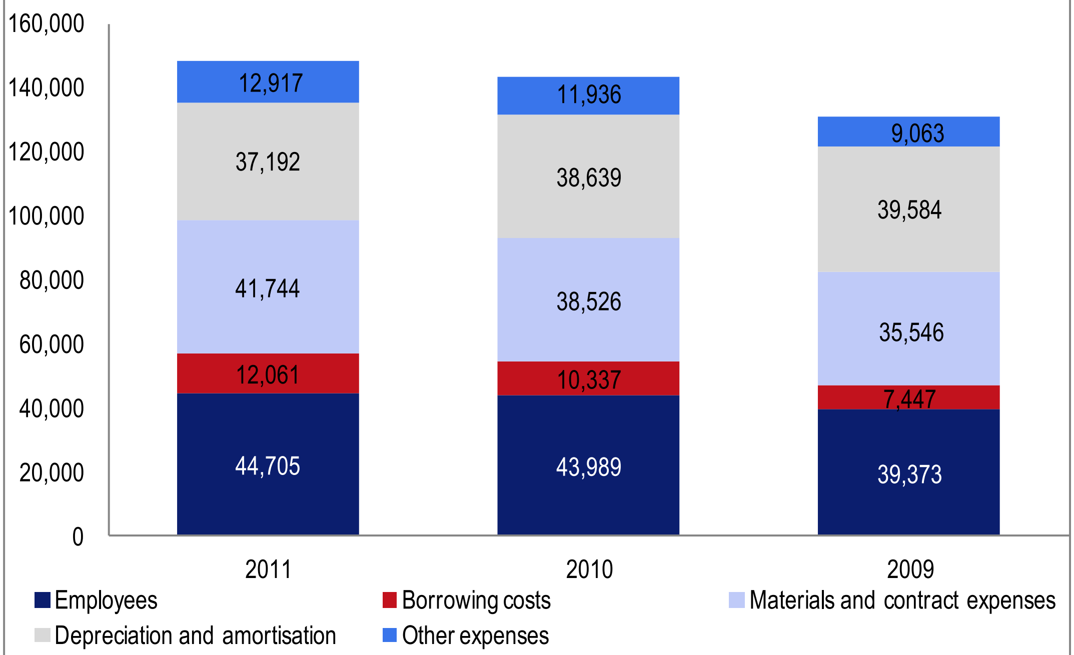
Key Observations

- Rates and annual charges have been increasing above the IPART approved rate peg levels for the review period. 2011 was the final year of a 4.0% special rate variation over seven years, to assist with costs associated with sealing of unsealed roads and asset maintenance in general.
  2011 was also year five of a seven-year ministerial approved variation to fund the projects and activities identified in a seven year infrastructure and services plan. In 2011 this variation was 8.5% above the rate peg.
- Water supply services, waste management and sewerage services are the major contributors to user fees and charges. This category of revenue increased by 16.1% in 2010 and 8.5% in 2011 to $31.9m. Also driving the increases over the last two years were non domestic waste management user charges which increased from $1.1m in 2009 to $3.16m in 2011 due to a new contract with Council's waste management contractor. Domestic waste management services user charges revenue increased from $0.6m in 2009 to $1.8m in 2011. Increases in waste management revenue were offset by the introduction of the NSW waste levy in 2009.

- Another major revenue source was holiday park revenue which increased from $6.0m in 2009 to $6.9min 2011. The holiday parks produced an operating surplus of $0.6m in 2011. Council has no control over returns from caravan parks, which are managed by the Tweed Coast Holiday Parks Reserves Trust which reports to the State Government.

3.2: Expenses

Figure 2 - Expenses for 2008/09 to 2010/11 ($'000s)



Key Observations

- After increasing by 11.7% in 2010, employee costs rose by a further 1.6% in 2011 to $44.7m. Salary regrades, award increases, increased workers compensation insurance and superannuation costs in 2010 were the reason for the substantive increase in costs.
- Borrowing costs increased by 38.8% in 2010, and a further 16.7% in 2011 to $12.1m. This reflects the additional $30.0m in borrowings undertaken by Council to fund the Banora Point Waste Water Treatment Plant Upgrade.
- Despite the value of infrastructure assets increasing due to the Asset Revaluations, depreciation decreased between 2009 and 2011 as Council reassessed the remaining useful life of roads, bridges, footpaths, and storm water drainage assets.
- Materials and contract expenses increased by 8.4% p.a. over the past two years to $41.7m in 2011. Council has incurred significant expenditure on asset maintenance as part of their seven year infrastructure and services plan for which they secured the SRV.

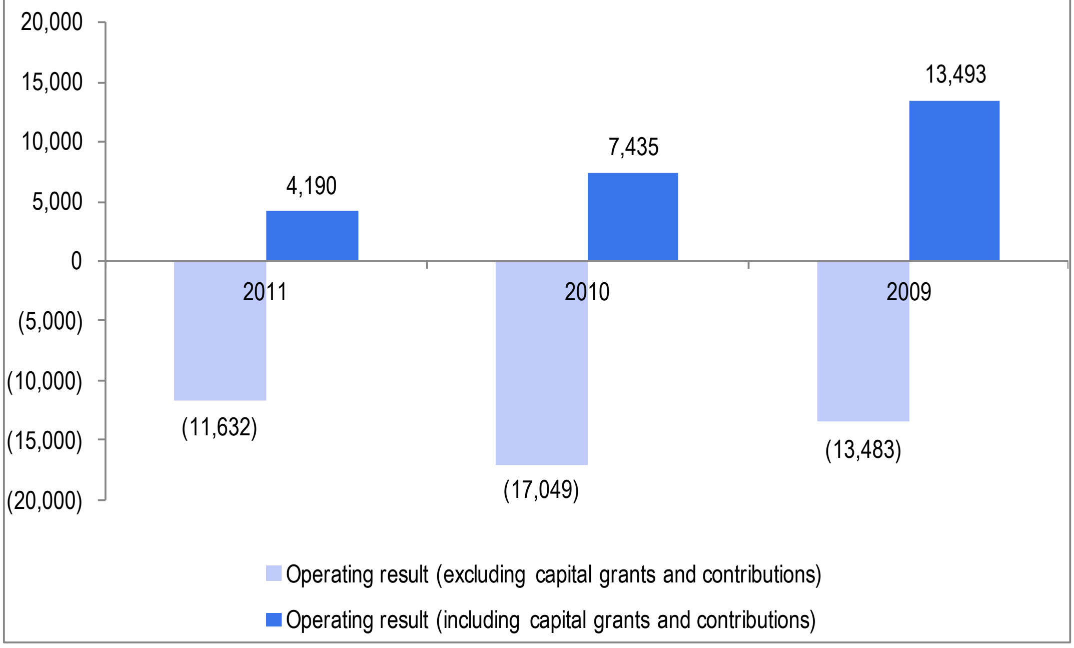
3.3: Operating Results

TCorp has made some standard adjustments to focus the analysis on core operating council results. Grants and contributions for capital purposes, realised and unrealised gains on investments and other assets are excluded, as well as one-off items which Council have no control over (e.g. impairments).

TCorp believes that the exclusion of these items will assist in normalising the measurement of key performance indicators, and the measurement of Council's performance against its peers.

All items excluded from the income statement and further historical financial information is detailed in Appendix A.

Figure 3 - Operating Results for 2008/09 to 2010/11 ($'000s)



Key Observations

- Council reported an improved operating deficit in 2011 compared to 2009 and 2010
- Council expenses include a non-cash depreciation expense, ($37.2m in 2011), which has decreased over the past three years following the Asset Revaluations process. Whilst the non cash nature of depreciation can favourably impact on ratios such as EBITDA that focus on cash, depreciation is an important expense as it represents the allocation of the value of an asset over its useful life.

3.4: Financial Management Indicators

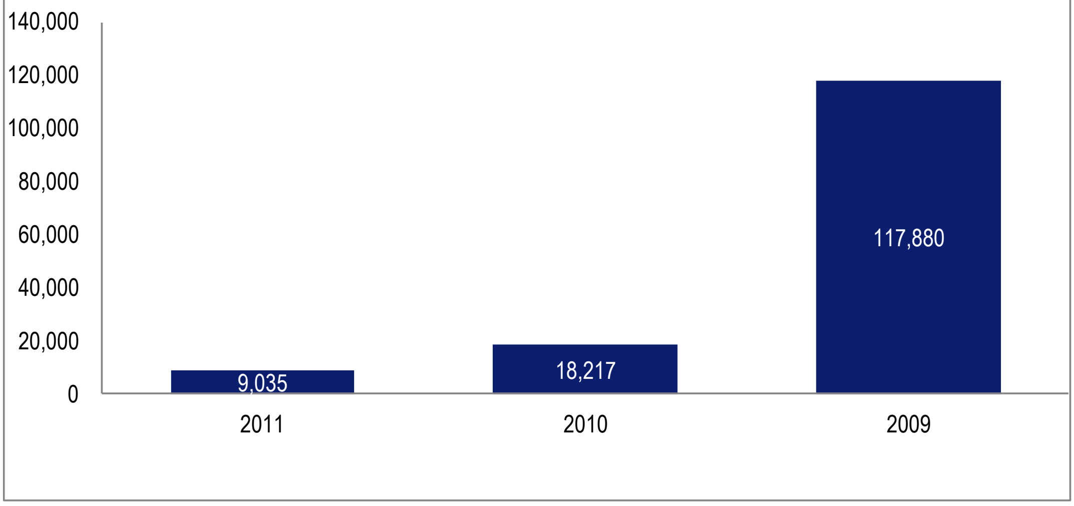
Performance Indicators	Year ended 30 June		
	2011	2010	2009
EBITDA ($'000s)	37,621	31,927	33,548
Operating Ratio	(8.5%)	(13.5%)	(11.5%)
Interest Cover Ratio	3.12x	3.09x	4.50x
Debt Service Cover Ratio	2.07x	2.24x	3.24x
Unrestricted Current Ratio	2.77x	2.65x	2.37x
Own Source Operating Revenue Ratio	68.8%	64.0%	60.3%
Cash Expense Ratio	1.1 months	2.3 months	16.8 months
Net Assets ($'000s)	2,503,002	2,332,699	1,956,786

Key Observations

- Council's underlying operating performance (measured using EBITDA) increased over the three year period.
- Council's DSCR was above the benchmark indicating that they have flexibility in regard to carrying additional debt. Council had $186.9m (7.5% of Net Assets) in borrowings outstanding in 2011 of which $112.1m was related to an extensive capital works program in the Water and Sewerage Funds undertaken over recent years.
- The Unrestricted Current Ratio has been above the benchmark of 1.50x over the past three years, indicating that Council had acceptable liquidity.
- Although the Cash Expense Ratio was below benchmark in 2010 and 2011, Council had substantial amounts in long term deposits which can be used to service liabilities.
- Net Assets have increased by over $546.2m between 2009 and 2011 due to the consecutive Asset Revaluations in 2010 and 2011, which increased the value of Council's infrastructure assets.
- The Asset Revaluations over the last three years have resulted in a high level of volatility in Net Assets over this period. Consequently, in the short term the value of Net Assets is not necessarily an informative indicator of performance. In the medium to long term however, this is a key indicator of a Council's capacity to add value to its operations. Over time, Net Assets should increase at least in line with inflation plus an allowance for increased population and/or improved or increased services. Declining Net Assets is a key indicator of the Council's assets not being able to sustain the ongoing operations of a Council.
- When the Asset Revaluations are excluded, the underlying trend in all three years has been an expanding infrastructure, property, plant, and equipment (IPP&E) asset base with asset purchases being larger than the combined value of disposed assets and annual depreciation. Over the three years this amounted to a $141.8m increase in IPP&E assets.

3.5: Statement of Cashflows

Figure 4 - Cash and Cash Equivalents for 2008/09 to 2010/11 ($'000s)



Key Observations

- While cash and cash equivalents have decreased considerably, total cash and investments have increased over the three years. Council had $172.6m in total cash and investments in 2011 of which $148.4m were held in long term deposits.
- Within the $172.6m in total cash and investments, $141.9m was externally restricted, $28.7m was internally restricted, and $2.0m was unrestricted.
- The cash and investment reserves along with the Unrestricted Current Ratio indicate Council has sufficient liquidity.
- Council held $2.8m in managed funds in 2011 which are no longer prescribed by the State government. Council will dispose of these grandfathered investments when financially advantageous to them.

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3.6: Capital Expenditure

The following section predominantly relies on information obtained from Special Schedules 7 and 8 that accompany the annual financial statements. These figures are unaudited and are therefore Council's estimated figures.

3.6(a): Infrastructure Backlog

Figure 5 - Infrastructure Backlog for 2008/09 to 2010/11 ($'000s)

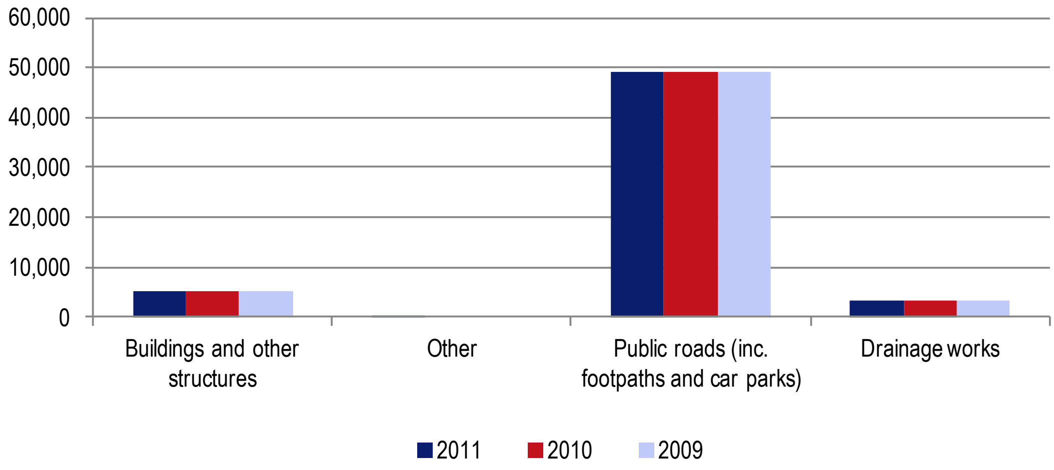
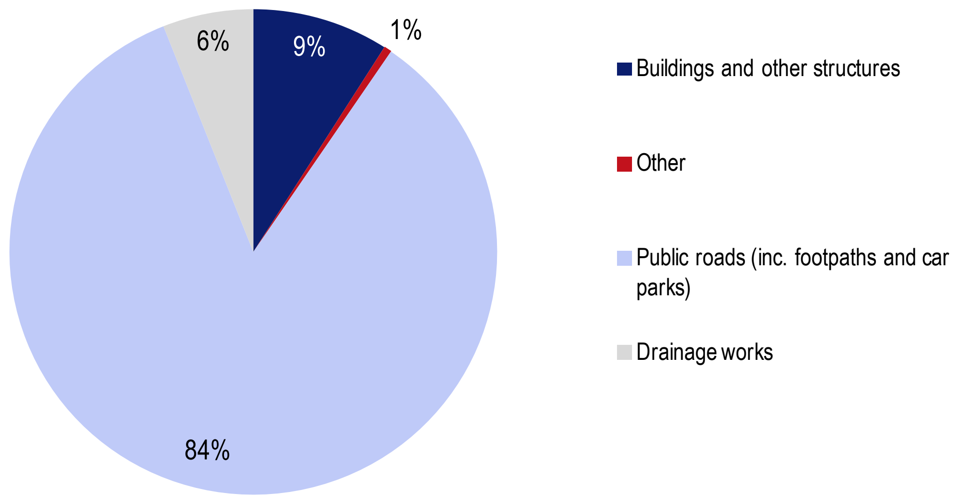


Figure 6 - Infrastructure Backlog Composition for 2010/11



The Council reported a $58.0m backlog in 2011, up slightly since 2009. The Infrastructure Backlog is 84.4% road related. As Tweed LGA has over 1,262 km of sealed roads, and over 192 km of unsealed roads this is a considerable level of road infrastructure to maintain. The seven year ministerial approved rate variation granted in 2004 was to assist with costs associated with sealing of unsealed roads and asset maintenance in general.

Council have consulted the community on their views on the backlog. The results of community consultation show that 22.3% of respondents would put more funds into roads and bridges, however most respondents say community services are their most pressing concern.

3.6(b): Infrastructure Status

Infrastructure Status	Year ended 30 June		
	2011	2010	2009
Bring to satisfactory standard ($'000s)	58,060	57,760	57,760
Required annual maintenance ($'000s)	28,854	27,272	20,704
Actual annual maintenance ($'000s)	26,928	25,390	14,540
Total value of infrastructure assets ($'000s)	1,659,360	1,628,726	1,137,865
Total assets ($'000s)	2,727,099	2,523,724	2,135,045
Building and Infrastructure Backlog Ratio	0.03x	0.04x	0.05x
Asset Maintenance Ratio	0.93x	0.93x	0.70x
Building and Infrastructure Renewals Ratio	0.53x	2.66x	0.67x
Capital Expenditure Ratio	1.60x	2.48x	2.61x

The Building and Infrastructure Asset Renewal Ratio did not meet the benchmark in 2011 and indicates that Council did not spend enough on asset renewal in two out of the last three years. The Capital Expenditure Ratio has been exceeding the benchmark mainly due to Council's major water and sewage capital projects.

3.6(c): Capital Program

The following figures are sourced from the Council's Annual Financial Statements at Special Schedule No. 8 and are not audited. New capital works are major non-recurrent projects.

Capital Program ($'000s)	Year ended 30 June		
	2011	**2010**	**2009**
New capital works	23,244	12,788	55,183
Replacement/refurbishment of existing assets	0	0	0
Total	**23,244**	**12,788**	**55,183**

Council did not provide complete information on the replacement/refurbishment of existing assets in Special Schedule No. 8.

Council's major capital works completed in the last three years include:

- Bray Park Waste Treatment Plant $73.9m
- Kingscliff Sewage Treatment Plant $32.0m
- Pool upgrade and multi story car park $17.0m
- Jack Evans Boatharbour $8.7m
- Kyogle Road upgrade $4.7m

3.7: Specific Risks to Council

- Asset management funding. There is a shortfall between the required funding as identified in the Asset Management Plans ($30.0m p.a.) and the current funding that is provided in the LTFP ($20.0m p.a.).
- Isolated events. Erosion at Kingscliff beach has cost Council $2.0m to date. When Council has to fund unforseen events such as this, other capital projects have to be deferred.
- Development applications. Council gave the example of how processing development applications is at a greater cost to Council under a more complex regulatory framework, whilst development fees are fixed by government and have not increased for over 10 years. Council have estimated the net costs per development application have increased from $775 in 2004 to $5,466 in 2011.
- Cost shifting from other levels of government to Council. Examples of schemes previously funded through grants that are now 100.0% funded by Council include, the Tweed River Management Plan, and the Aboriginal Worker Program which cost Council $0.3m and $0.1m p.a. respectively. Council are examining specific resourcing strategies to offset these effects such as establishing satellite offices, regional resource sharing, and outsourcing.

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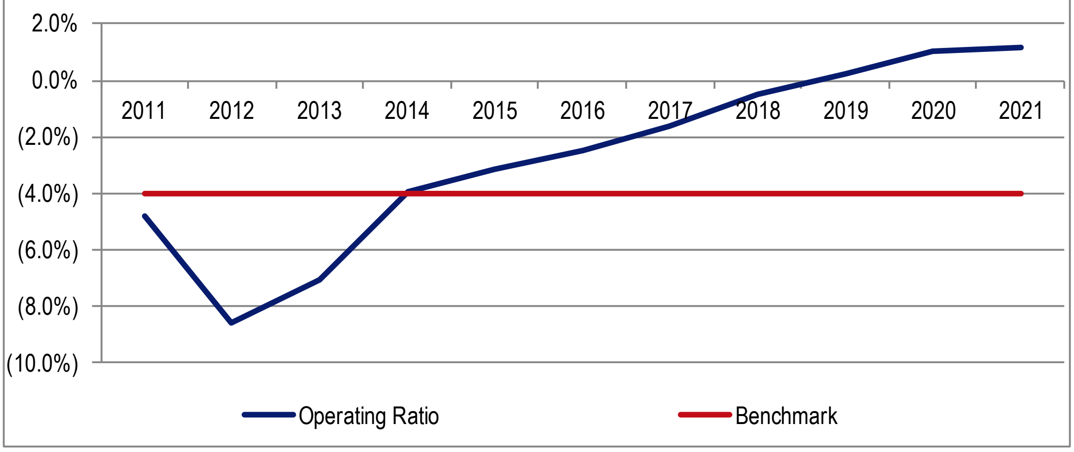
Section 4 Review of Financial Forecasts

The financial forecast model shows the projected financial statements and assumptions for the next 10 years. The model includes the two loans worth $4.4m in total without any LIRS subsidy.

The LIRS loans relate to the General Fund, therefore we have focused our financial analysis solely upon this Fund. Council's consolidated position includes both a Water and Sewer Fund however these are operated as independent entities, which unlike the General Fund are more able to adjust the appropriate fees and charges to meet all future operating and investing expenses.

4.1: Operating Results

Figure 7 - Operating Ratio for General Fund



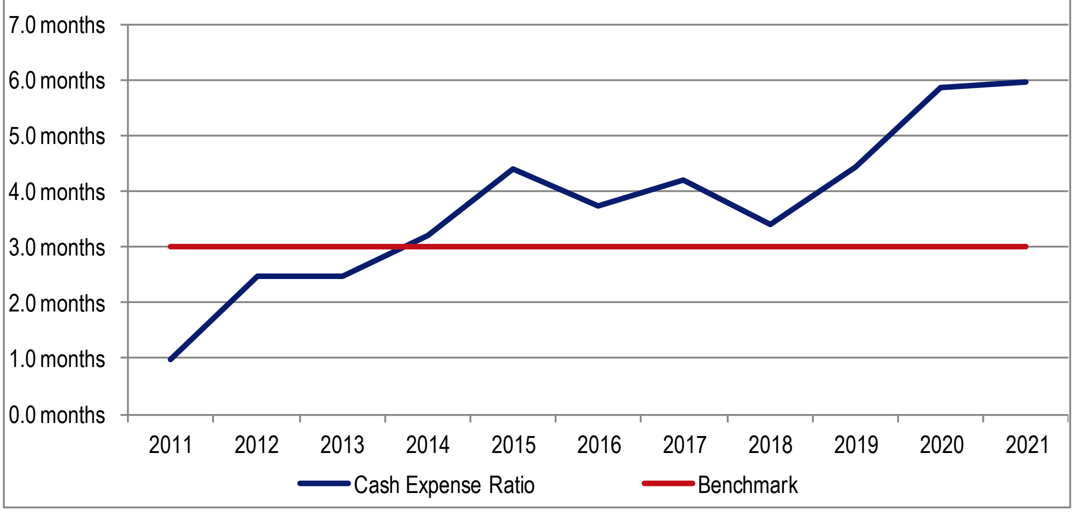
A reduction in user fees and charges and operating grants and contributions forecast in 2012 adversely affects the Operating Ratio, however results are forecast to gradually improve over time as increases in revenue exceed increases in expenditure, mainly driven by increased rate revenue caused by population increases.

4.2: Financial Management Indicators

The financial management indicators are linked to the utilisation of debt in early years and improve over time as the amortising debt reduces and operating deficits also improve.

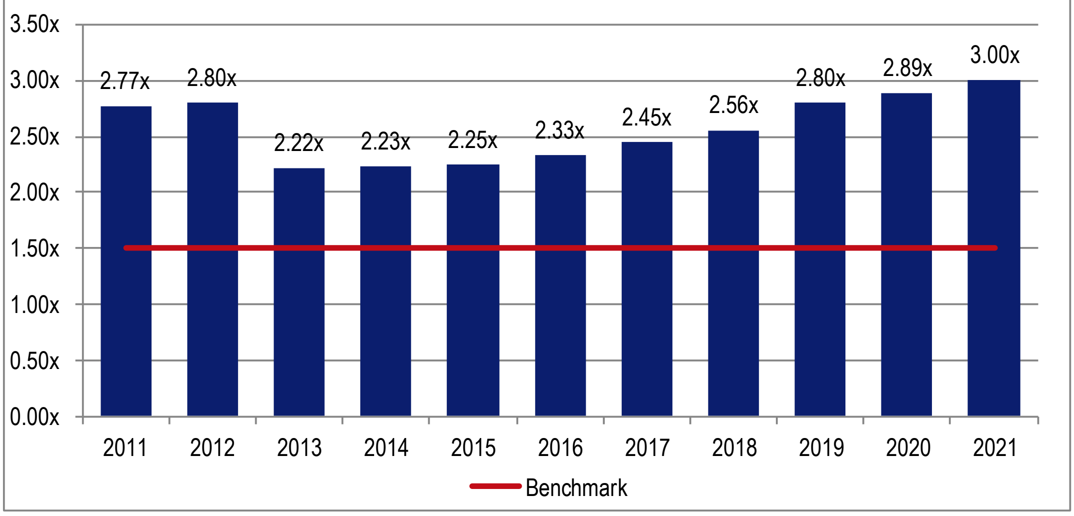
Liquidity Ratios

Figure 8 - Cash Expense Ratio for General Fund



As discussed in Section 3 Council's Cash Expense Ratio is below benchmark in 2011 due to Council's strategy of placing funds within investments such as long term deposits. Due to the improving operating performance, cash reserves increase, and the Cash Expense Ratio increases above benchmark.

Figure 9 - Unrestricted Current Ratio for General Fund



The Unrestricted Current Ratio indicates that Council will have sound liquidity. Council should be able to service all short and long term liabilities, and currently scheduled capital expenditure.

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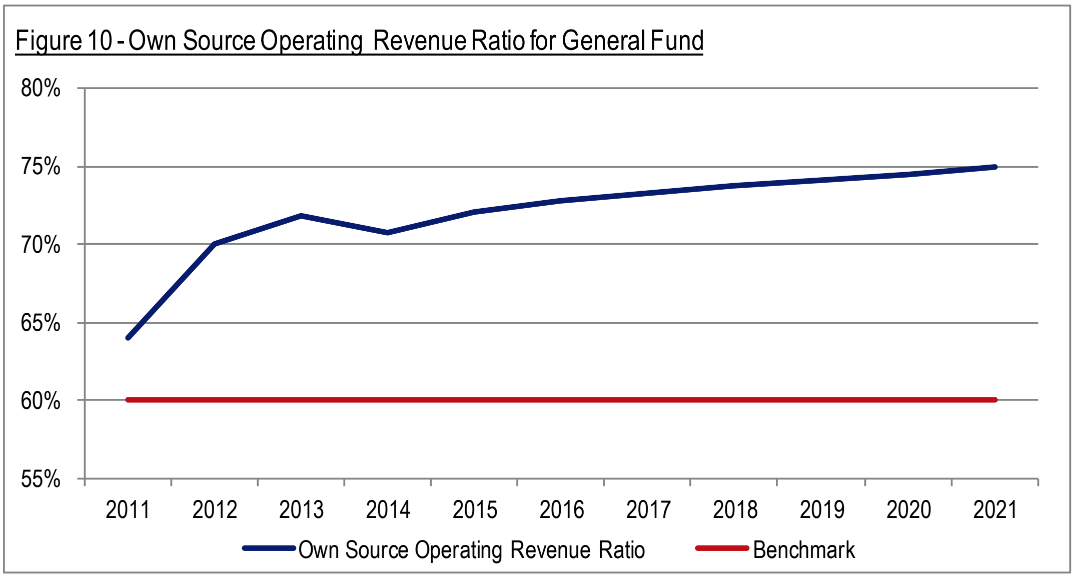
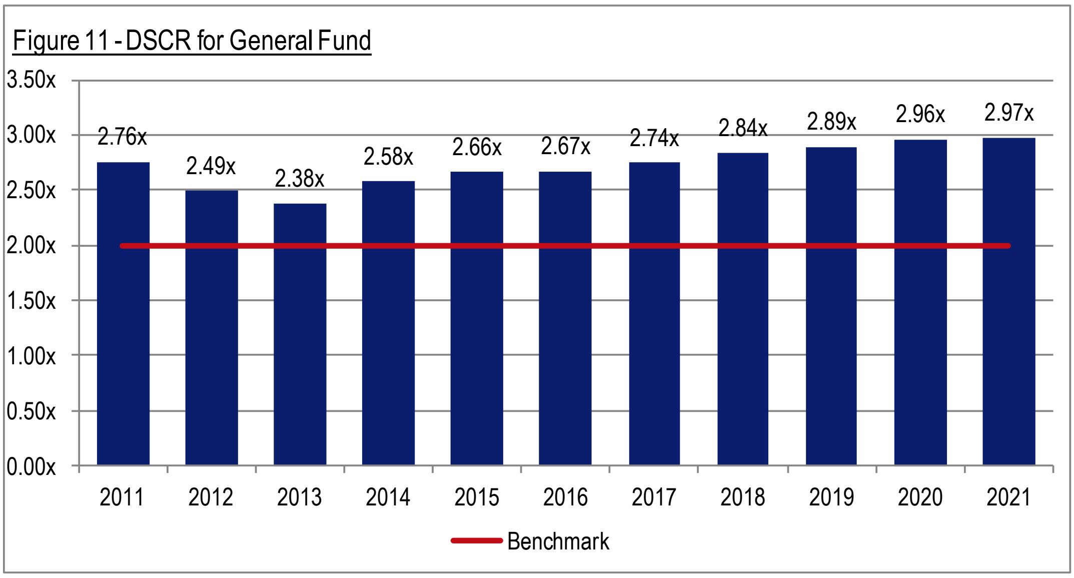
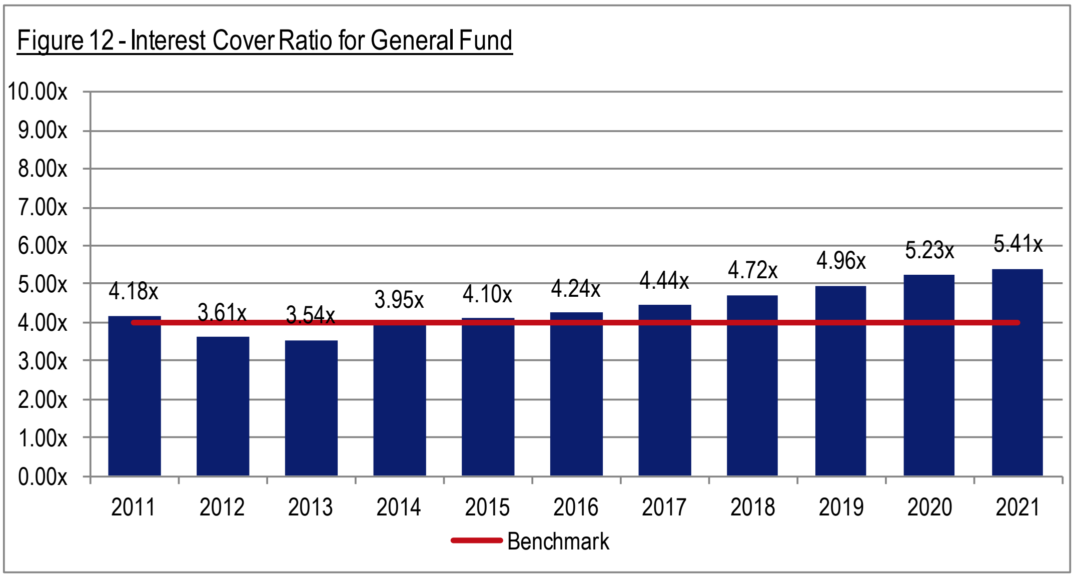
Fiscal Flexibility Ratios



The Own Source Operating Revenue Ratio remains above the benchmark for each year of the forecast. The ratio is rising over the lifetime of the forecast due to capital grants and contributions forecast being lower than historically received. This skews the proportion of Own Source Revenue Ratio upwards.

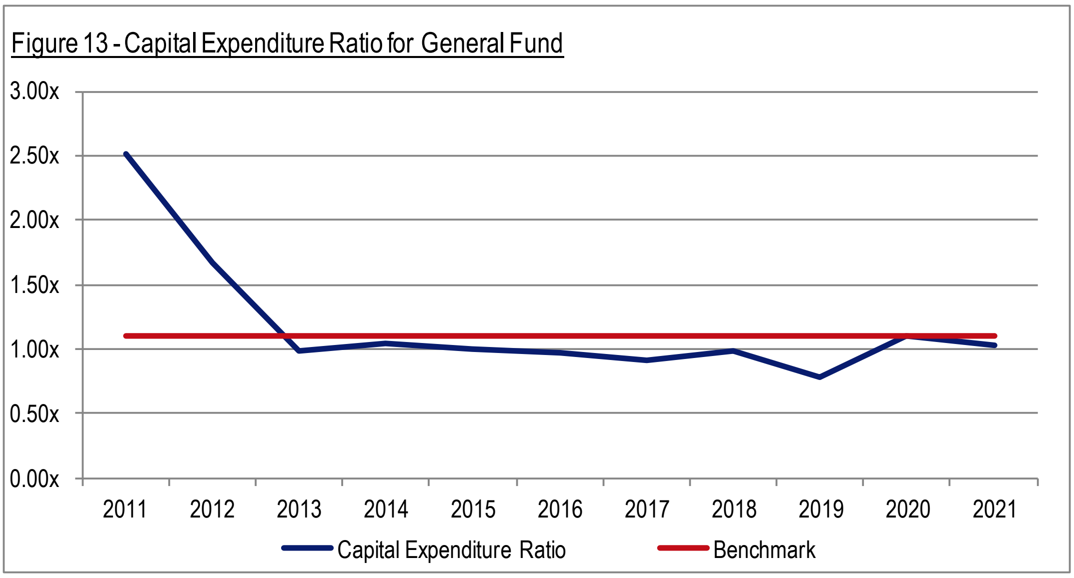


The DSCR shows that Council has the capacity to service the $4.4m loans relating to the drainage schemes, and the other planned drawdowns of $2.0m p.a. Outstanding borrowings in the General Fund will peak in 2013 at $83.2m reducing to a low of $68.8m in 2021.



The Interest Cover Ratio, similar to the DSCR, shows the Council has sufficient capacity to service scheduled debt commitments, including the LIRS loan. There is capacity to service further debt interest costs once the Council's ratio increases to the 4.00x benchmark from 2015 onwards

4.3: Capital Expenditure



Council's LTFP presents a funding shortfall in the General Fund which assumes a growth in assessable properties of 500 p.a. The required level of funding is based on maintaining Council assets at their current condition levels. Council estimate the shortfall at around $10.0m p.a. Therefore it is likely that the Infrastructure Backlog may grow. If there is an asset management funding shortfall as predicted, Council and the community will need to address this through further revenue generating opportunities or efficiency gains.

Council's liquidity indicators are increasing over the lifetime of the LTFP, which indicates Council could allocate more resources to asset renewal over time.

4.4: Financial Model Assumption Review

Councils have used their own assumptions in developing their forecasts.

In order to evaluate the validity of the Council's forecast model, TCorp has compared the model assumptions versus TCorp's benchmarks for annual increases in the various revenue and expenditure items. Any material differences from these benchmarks should be explained through the LTFP.

TCorp's benchmarks:

- Rates and annual charges: TCorp notes that the LGCI increased by 3.4% in the year to September 2011, and in December 2011, IPART announced that the rate peg to apply in the 2012/13 financial year will be 3.6%. Beyond 2013 TCorp has assessed a general benchmark for rates and annual charges to increase by mid-range LGCI annual increases of 3.0%
- Interest and investment revenue: annual return of 5%
- All other revenue items: the estimated annual CPI increase of 2.5%
- Employee costs: 3.5% (estimated CPI+1%)
- All other expenses: the estimated annual CPI increase of 2.5%

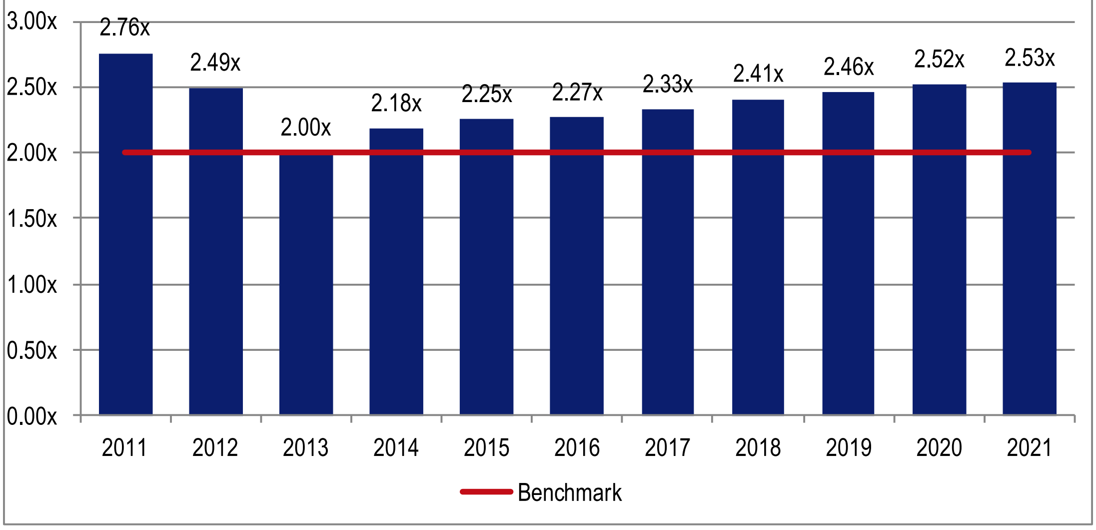
<u>Key Observations and Risks</u>

- The LTFP assumes that current service levels will remain unchanged.
- Rates and annual charges are forecast to grow by around 4.0% p.a. The LTFP assumes revenues to be boosted by 500 additional rate assessments p.a.
- User fees and charges are forecast to decrease by 16.0% in 2012 then gradually increase for the lifetime of the forecast.
- Depreciation has not been indexed from 2012 onwards. Council maintains they need more detailed asset information to make reasonable assumptions.
- Employee costs are forecast to increase at around 3.0% p.a. for the majority of the forecast.
- TCorp finds the majority of assumptions reasonable if slightly optimistic. Revenue consistently increasing at higher rates than expenses is not consistent with historical performance. Further, with a high level of forecast population growth, it could be expected that higher service levels may be required.

4.5: Borrowing Capacity

When analysing the financial capacity of the Council we believe Council will be able to incorporate additional loan funding in addition to the LIRS loan facilities. Some comments and observations are:

Figure 14 - DSCR for General Fund with an additional $12.0m in borrowings



- Based on a benchmark of DSCR>2.00x, $12.0m could be borrowed in addition to the $4.4m borrowings proposed under LIRS in 2013, and the additional forecast drawdowns of over $2.0m p.a. for the lifetime of the forecast
- This scenario has been calculated by basing borrowing capacity on a 10 year amortising loan at 8.0% p.a.

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Section 5 Benchmarking and Comparisons with Other Councils

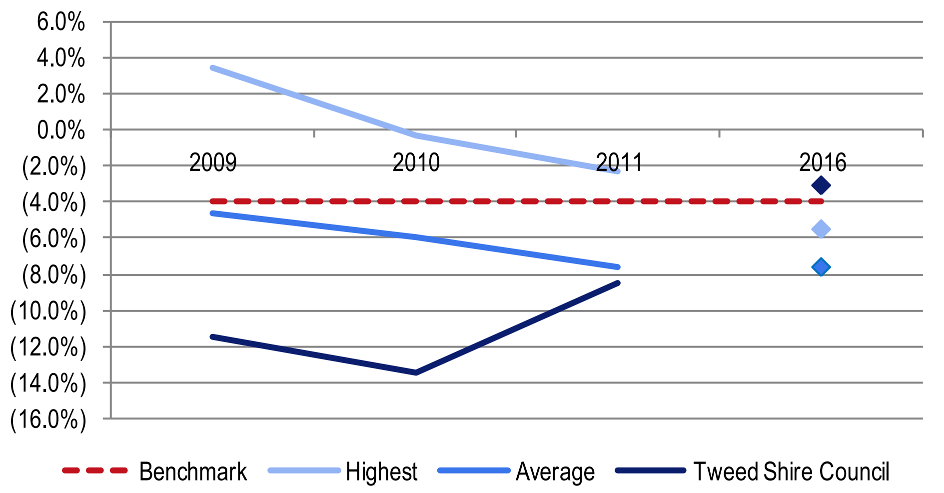
As discussed in section 2 of this report, each council's performance has been assessed against ten key benchmark ratios. This section of the report compares the Council's performance with its peers in the same DLG Group. The Council is in DLG Group 5 and there are six councils in this group.

In Figure 15 to Figure 21, the graphs compare the historical performance of Council with the benchmark for that ratio, with the average for the Group, with the highest performance (or lowest performance in the case of the Infrastructure Backlog Ratio where a low ratio is an indicator of strong performance), and with the forecast position of the Council as at 2016 (as per Council's LTFP). Figures 22 to 24 do not include the 2016 forecast position as those numbers are not available.

Where no highest line is shown on the graph, this means that Council is the best performer in its group for that Ratio.

Financial Flexibility

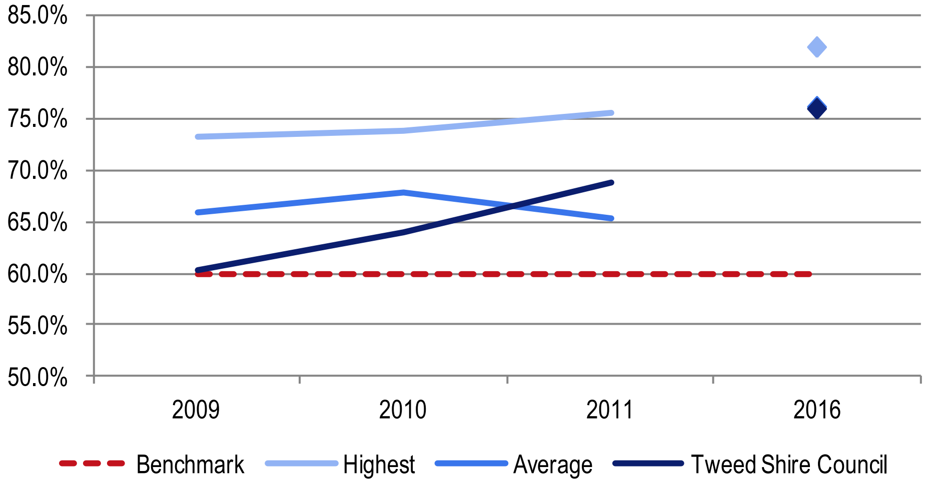
Figure 15 - Operating Ratio Comparison



Council's Operating Ratio was below the group average in the past three years, though it improved significantly in 2011. The results are forecast to improve further in the medium term to be above the group's average and benchmark.

New South Wales
Treasury Corporation

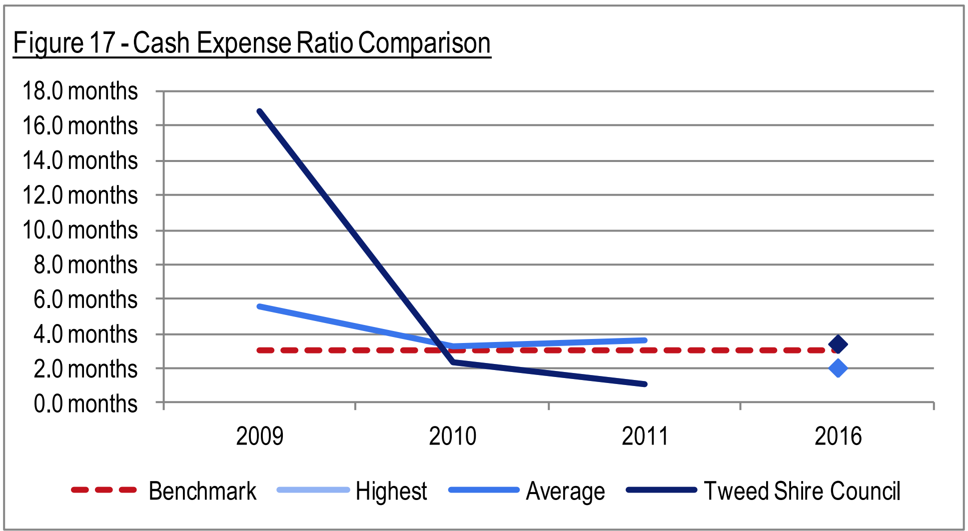
Figure 16 - Own Source Operating Revenue Ratio Comparison

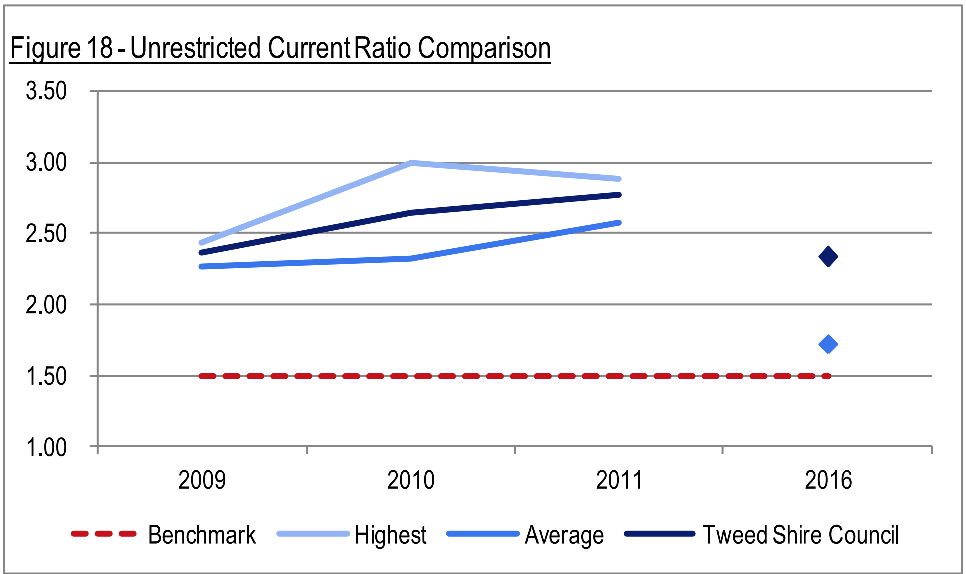


Council's Own Source Operating Revenue Ratio was below the group average in two of the last three years, though it improved to be above the group average in 2011. The ratio has improved over the period and is forecast to improve further in the medium term. By 2016 Council's results will be equal to the group average.

Overall, Council's financial flexibility is close to the group's average.

Liquidity





On average over the past three years, the Council's liquidity position has been sound and this is forecast to remain relatively stable in the medium term.

Debt Servicing

Figure 19 - Debt Service Cover Ratio Comparison

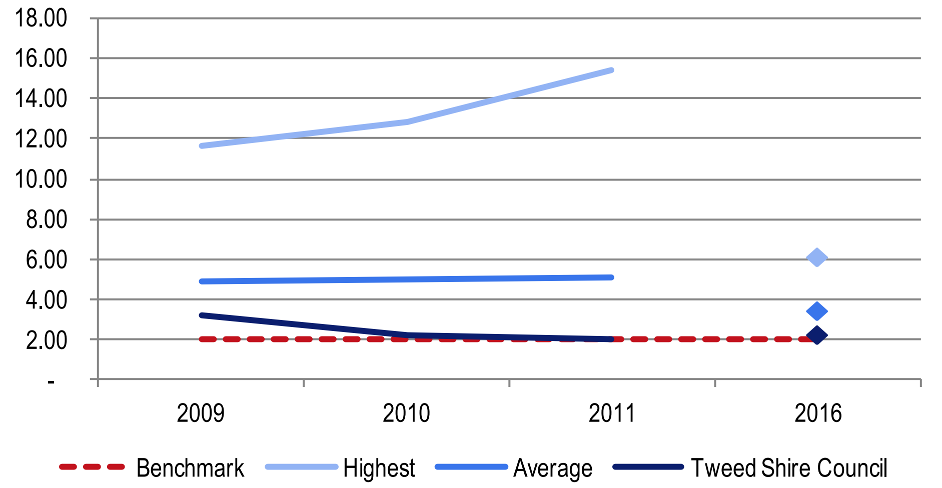
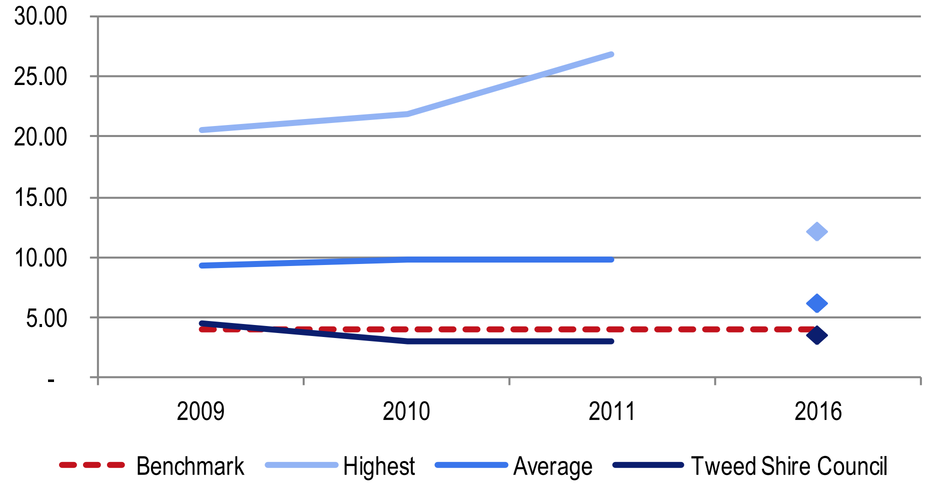


Figure 20 - Interest Cover Ratio Comparison



Council's DSCR and Interest Cover Ratio's have been at or near benchmark in recent years but are below the group average. Both ratios improve marginally in the medium term.

Asset Renewal and Capital Works

Figure 21 - Capital Expenditure Ratio Comparison

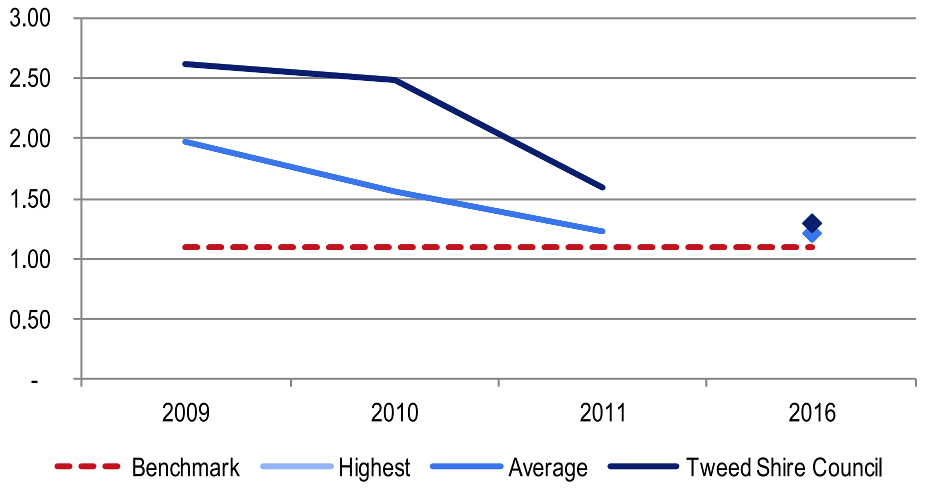
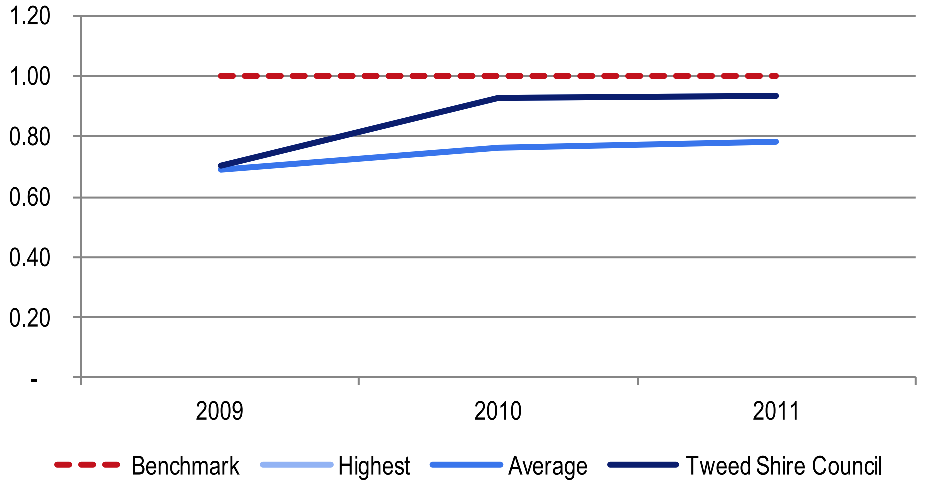
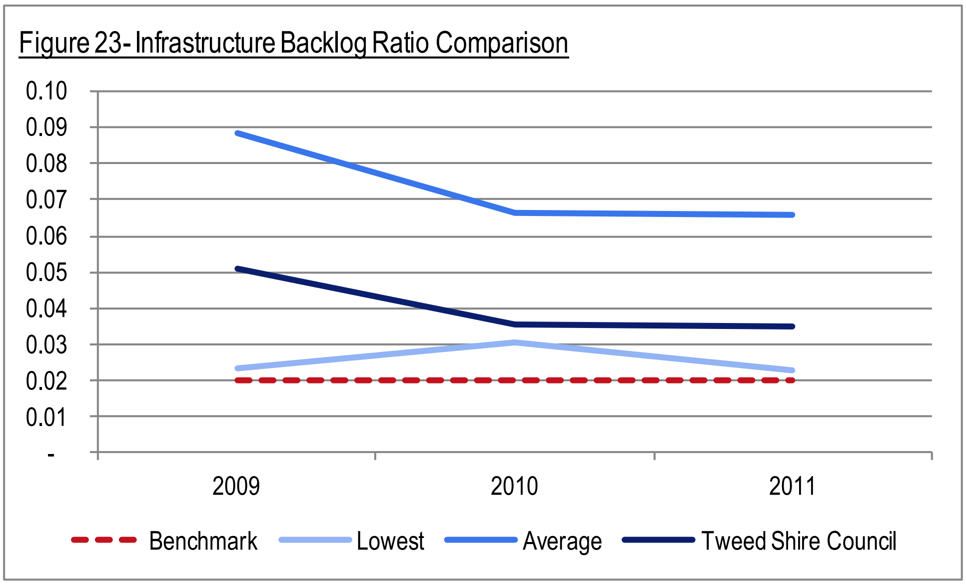
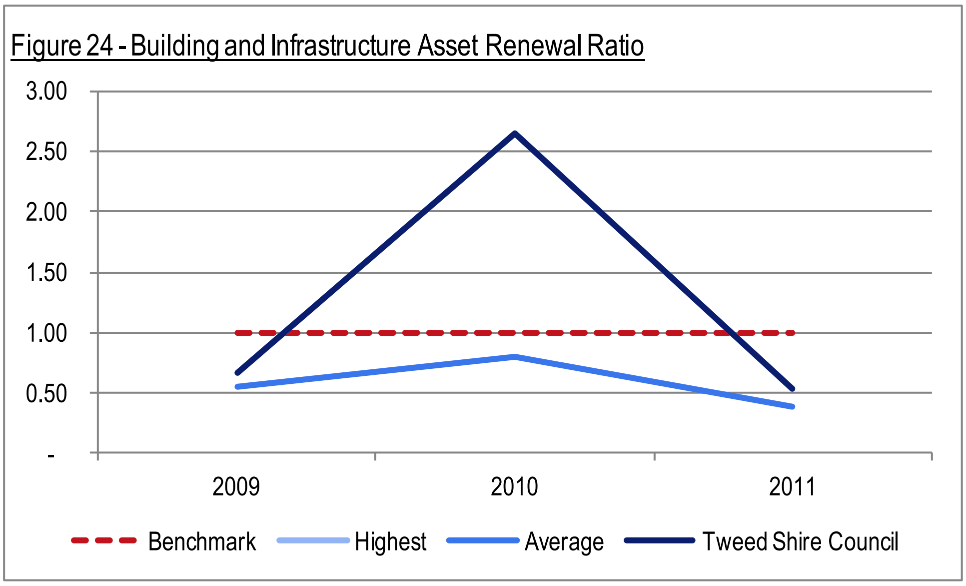


Figure 22 - Asset Maintenance Ratio Comparison







Overall, the Council has lower than the group average Infrastructure Backlog, but I needs further improvement to reach the benchmark. It is the strongest council in the group in terms of its spending on building and infrastructure asset renewal, asset maintenance spending and capital expenditure. Despite being the best Council in this group, Council is below the benchmark in the Asset Maintenance Ratio.

Overall the Council has kept its existing assets well maintained and its Infrastructure Backlog low.

Section 6 Conclusion and Recommendations

Based on our review of both the historic financial information and the 10 year financial forecast within Council's long term financial plan we consider Council to be in a satisfactory financial position.

We base our recommendation on the following key points:

- Council's underlying operating results (measured using EBITDA) have improved from $33.5m in 2009 to $37.6m in 2011
- Council's Unrestricted Current Ratio has been well above benchmark in the past three years indicating Council has sufficient liquidity
- Council has managed a significant capital works program in the last three years on vital infrastructure such as water and sewage treatment plants

However we would also recommend that the following points be considered:

- Council review asset management strategies to improve depreciation forecasts, which should provide improved asset management and financial planning
- The General Fund will not generate sufficient funds for capital expenditure to match depreciation of its assets. It is likely that Council will need to review current service levels, or raise additional revenues to keep infrastructure to their current standards

Appendix A Historical Financial Information Tables

Table 1- Income Statement

Income Statement ($'000s)	Year ended 30 June			% annual change	
	2011	2010	2009	2011	2010
Revenue					
Rates and annual charges	73,336	67,124	61,880	9.3%	8.5%
User charges and fees	31,866	29,377	25,310	8.5%	16.1%
Interest and investment revenue	10,043	8,186	7,365	22.7%	11.1%
Grants and contributions for operating purposes	18,762	19,560	21,234	(4.1%)	(7.9%)
Other revenues	2,980	2,131	1,741	39.8%	22.4%
Total revenue	**136,987**	**126,378**	**117,530**	**8.4%**	**7.5%**
Expenses					
Employees	44,705	43,989	39,373	1.6%	11.7%
Borrowing costs	12,061	10,337	7,447	16.7%	38.8%
Materials and contract expenses	41,744	38,526	35,546	8.4%	8.4%
Depreciation and amortisation	37,192	38,639	39,584	(3.7%)	(2.4%)
Other expenses	12,917	11,936	9,063	8.2%	31.7%
Total expenses	**148,619**	**143,427**	**131,013**	**3.6%**	**9.5%**
Operating result (excluding capital grants and contributions)	**(11,632)**	**(17,049)**	**(13,483)**	**31.8%**	**(26.4%)**
Operating result (including capital grants and contributions)	**4,190**	**7,435**	**13,493**	**(43.6%)**	**(44.9%)**

Table 2 - Items excluded from Income Statement

Excluded items ($'000s)			
	2011	2010	2009
Grants and contributions for capital purposes	15,822	24,484	26,976
Fair value adjustments financial instruments	159	899	(608)
Assets previously not recognised	4,598	0	0
Fair value of interest free loan	(879)	5,381	0
Fair value adjustments investment properties	(717)	69	0
Net gain/(loss) from the disposal of assets	(4,663)	(4,779)	(3,052)

Table 3 - Balance Sheet

Balance Sheet ($'000s)	Year Ended 30 June			% annual change	
	2011	2010	2009	2011	2010
Current assets					
Cash and cash equivalents	9,035	18,217	117,880	(50.4%)	(84.5%)
Investments	109,400	115,641	0	(5.4%)	N/A
Receivables	19,185	17,827	14,241	7.6%	25.2%
Inventories	1,660	1,212	1,019	37.0%	18.9%
Other	2,369	1,358	1,204	74.4%	12.8%
Total current assets	141,649	154,255	134,344	(8.2%)	14.8%
Non-current assets					
Investments	54,190	21,510	23,089	151.9%	(6.8%)
Receivables	2,913	2,861	2,644	1.8%	8.2%
Infrastructure, property, plant & equipment	2,526,044	2,342,044	1,971,731	7.9%	18.8%
Investments accounted for using the equity method	1,688	2,405	2,336	(29.8%)	3.0%
Investment property	615	649	901	(5.2%)	(28.0%)
Total non-current assets	2,585,450	2,369,469	2,000,701	9.1%	18.4%
Total assets	**2,727,099**	**2,523,724**	**2,135,045**	8.1%	18.2%
Current liabilities					
Payables	14,786	10,403	14,220	42.1%	(26.8%)
Borrowings	6,419	4,699	3,232	36.6%	45.4%
Provisions	16,916	17,756	19,685	(4.7%)	(9.8%)
Total current liabilities	38,121	32,858	37,137	16.0%	(11.5%)
Non-current liabilities					
Payables	523	353	240	48.2%	47.1%
Borrowings	180,510	153,630	135,651	17.5%	13.3%
Provisions	4,943	4,184	5,231	18.1%	(20.0%)
Total non-current liabilities	185,976	158,167	141,122	17.6%	12.1%
Total liabilities	**224,097**	**191,025**	**178,259**	17.3%	7.2%
Net assets	**2,503,002**	**2,332,699**	**1,956,786**	7.3%	19.2%

Table 4-Cashflow

Cash Flow Statement ($'000s)	**Year ended 30 June**		
	2011	**2010**	**2009**
Cash flows from operating activities	34,072	20,401	35,371
Cash flows from investing activities	(70,975)	(144,892)	(87,439)
Proceeds from borrowings and advances	33,847	28,715	62,245
Repayment of borrowings and advances	(6,126)	(3,887)	(2,899)
Cash flows from financing activities	27,721	24,828	59,346
Net increase/(decrease) in cash and equivalents	**(9,182)**	**(99,663)**	**7,278**
Cash and equivalents	9,035	18,217	117,880

Appendix B Glossary

Asset Revaluations

In assessing the financial sustainability of NSW councils, IPART found that not all councils reported assets at fair value.[1] In a circular to all councils in March 2009[2], DLG required all NSW councils to revalue their infrastructure assets to recognise the fair value of these assets by the end of the 2009/10 financial year.

Collateralised Debt Obligation (CDO)

CDOs are structured financial securities that banks use to repackage individual loans into a product that can be sold to investors on the secondary market.

In 2007 concerns were heightened in relation to the decline in the "sub-prime" mortgage market in the USA and possible exposure of some NSW councils, holding CDOs and other structured investment products, to losses.

In order to clarify the exposure of NSW councils to any losses, a review was conducted by the DLG with representatives from the Department of Premier and Cabinet and NSW Treasury.

A revised Ministerial investment Order was released by the DLG on 18 August 2008 in response to the review, suspending investments in CDOs, with transitional provisions to provide for existing investments.

Division of Local Government (DLG)

DLG is a division of the NSW Department of Premier and Cabinet and is responsible for local government across NSW. DLG's organisational purpose is "to strengthen the local government sector" and its organisational outcome is "successful councils engaging and supporting their communities". Operating within several strategic objectives DLG has a policy, legislative, investigative and program focus in matters ranging from local government finance, infrastructure, governance, performance, collaboration and community engagement. DLG strives to work collaboratively with the local government sector and is the key adviser to the NSW Government on local government matters.

Depreciation of Infrastructure Assets

Linked to the asset revaluations process stated above, IPART's analysis of case study councils found that this revaluation process resulted in sharp increases in the value of some council's assets. In some cases this has led to significantly higher depreciation charges, and will contribute to higher reported operating deficits.

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[1] IPART "Revenue Framework for Local Government" December 2009 p.83

[2] DLG "Recognition of certain assets at fair value" March 2009

EBITDA

EBITDA is an acronym for "earnings before interest, taxes, depreciation, and amortisation". It is often used to measure the cash earnings that can be used to pay interest and repay principal.

Grants and Contributions for Capital Purposes

Councils receive various capital grants and contributions that are nearly always 100% specific in nature. Due to the fact that they are specifically allocated in respect of capital expenditure they are excluded from the operational result for a council in TCorp's analysis of a council's financial position.

Grants and Contributions for Operating Purposes

General purpose grants are distributed through the NSW Local Government Grants Commission. When distributing the general component each council receives a minimum amount, which would be the amount if 30% of all funds were allocated on a per capita basis. When distributing the other 70%, the Grants Commission attempts to assess the extent of relative disadvantage between councils. The approach taken considers cost disadvantage in the provision of services on the one hand and an assessment of revenue raising capacity on the other.

Councils also receive specific operating grants for one-off specific projects that are distributed to be spent directly on the project that the funding was allocated to.

Independent Commission Against Corruption (ICAC)

ICAC was established by the NSW Government in 1989 in response to growing community concern about the integrity of public administration in NSW.

The jurisdiction of the ICAC extends to all NSW public sector agencies (except the NSW Police Force) and employees, including government departments, local councils, members of Parliament, ministers, the judiciary and the governor. The ICAC's jurisdiction also extends to those performing public official functions.

Independent Pricing and Regulatory Tribunal (IPART)

IPART has four main functions relating to the 152 local councils in NSW. Each year, IPART determines the rate peg, or the allowable annual increase in general income for councils. They also review and determine council applications for increases in general income above the rate peg, known as "Special Rate Variations". They approve increases in council minimum rates. They also review council development contributions plans that propose contribution levels that exceed caps set by the Government.

Infrastructure Backlog

Infrastructure backlog is defined as the estimated cost to bring infrastructure, building, other structures and depreciable land improvements to a satisfactory standard, measured at a particular point in time. It is unaudited and stated within Special Schedule 7 that accompanies the council's audited annual financial statements.

Integrated Planning and Reporting (IP&R) Framework

As part of the NSW Government's commitment to a strong and sustainable local government system, the *Local Government Amendment (Planning and Reporting) Act 2009* was assented on 1 October 2009. From this legislative reform the IP&R framework was devised to replace the former Management Plan and Social Plan with an integrated framework. It also includes a new requirement to prepare a long-term Community Strategic Plan and Resourcing Strategy. The other essential elements of the new framework are a Long-Term Financial Plan (LTFP), Operational Plan and Delivery Program and an Asset Management Plan.

Local Government Cost Index (LGCI)

The LGCI is a measure of movements in the unit costs incurred by NSW councils for ordinary council activities funded from general rate revenue. The LGCI is designed to measure how much the price of a fixed "basket" of inputs acquired by councils in a given period compares with the price of the same set of inputs in the base period. The LGCI is measured by IPART.

Net Assets

Net Assets is measured as total assets less total liabilities. The Asset Revaluations over the past years have resulted in a high level of volatility in many councils' Net Assets figure. Consequently, in the short term the value of Net Assets is not necessarily an informative indicator of performance. In the medium to long term however, this is a key indicator of a council's capacity to add value to its operations. Over time, Net Assets should increase at least in line with inflation plus an allowance for increased population and/or improved or increased services. Declining Net Assets is a key indicator of the council's assets not being able to sustain ongoing operations.

Roads and Maritime Services (RMS)

The NSW State Government agency with responsibility for roads and maritime services, formerly the Roads and Traffic Authority (RTA).

Section 64 Contribution

Development Servicing Plans (DSPs) are made under the provisions of Section 64 of the Local Government Act 1993 and Sections 305 to 307 of the Water Management Act 2000.

DSPs outline the developer charges applicable to developments for Water, Sewer and Stormwater within each Local Government Area.

Section 94 Contribution

Section 94 of the Environmental Planning and Assessment Act 1979 allows councils to collect contributions from the development of land in order to help meet the additional demand for community and open space facilities generated by that development.

It is a monetary contribution levied on developers at the development application stage to help pay for additional community facilities and/or infrastructure such as provision of libraries; community facilities; open space; roads; drainage; and the provision of car parking in commercial areas.

The contribution is determined based on a formula which should be contained in each council's Section 94 Contribution Plan, which also identifies the basis for levying the contributions and the works to be undertaken with the funds raised.

Special Rate Variation (SRV)

A SRV allows councils to increase general income above the rate peg, under the provisions of the Local Government Act 1993. There are two types of special rate variations that a council may apply for:

- a single year variation (section 508(2)) or
- a multi-year variation for between two to seven years (section 508A).

The applications are reviewed and approved by IPART.

Ratio Explanations

Asset Maintenance Ratio

Benchmark = Greater than 1.0x

Ratio = actual asset maintenance / required asset maintenance

This ratio compares actual versus required annual asset maintenance, as detailed in Special Schedule 7. A ratio of above 1.0x indicates that the council is investing enough funds within the year to stop the infrastructure backlog from growing.

Building and Infrastructure Renewals Ratio

Benchmark = Greater than 1.0x

Ratio = Asset renewals / depreciation of building and infrastructure assets

This ratio compares the proportion spent on infrastructure asset renewals and the asset's deterioration measured by its accounting depreciation. Asset renewal represents the replacement or refurbishment of existing assets to an equivalent capacity or performance as opposed to the acquisition of new assets or the refurbishment of old assets that increase capacity or performance.

Cash Expense Cover Ratio

Benchmark = Greater than 3.0 months

Ratio = current year's cash and cash equivalents / (total expenses – depreciation – interest costs)*12

This liquidity ratio indicates the number of months a council can continue paying for its immediate expenses without additional cash inflow.

Capital Expenditure Ratio

Benchmark = Greater than 1.1x

Ratio = annual capital expenditure / annual depreciation

This indicates the extent to which a council is forecasting to expand its asset base with capital expenditure spent on both new assets, and replacement and renewal of existing assets.

Debt Service Cover Ratio (DSCR)

Benchmark = Greater than 2.0x

Ratio = operating results before interest and depreciation (EBITDA) / principal repayments (from the statement of cash flows) + borrowing interest costs (from the income statement)

This ratio measures the availability of cash to service debt including interest, principal and lease payments

Infrastructure Backlog Ratio

Benchmark = Less than 0.02x

Ratio = estimated cost to bring assets to a satisfactory condition (from Special Schedule 7) / total infrastructure, building, other structures and depreciable land improvement assets (from note 9a)

This ratio shows what proportion the backlog is against total value of a council's infrastructure.

Interest Cover Ratio

Benchmark = Greater than 4.0x

Ratio = EBITDA / interest expense (from the income statement)

This ratio indicates the extent to which a council can service its interest bearing debt and take on additional borrowings. It measures the burden of the current interest expense upon a council's operating cash.

Operating Ratio

Benchmark = Better than negative 4%

Ratio = (operating revenue excluding capital grants and contributions – operating expenses) / operating revenue excluding capital grants and contributions

This ratio measures a council's ability to contain operating expenditure within operating revenue.

Own Source Operating Revenue Ratio

Benchmark = Greater than 60%

Ratio = rates, utilities and charges / total operating revenue (inclusive of capital grants and contributions)

This ratio measures the level of a council's fiscal flexibility. It is the degree of reliance on external funding sources such as operating grants and contributions. A council's financial flexibility improves the higher the level of its own source revenue.

Unrestricted Current Ratio

Benchmark = 1.5x (taken from the IPART December 2009 Revenue Framework for Local Government report)

Ratio = Current assets less all external restrictions / current liabilities less specific purpose liabilities

Restrictions placed on various funding sources (e.g. Section 94 developer contributions, RMS contributions) complicate the traditional current ratio because cash allocated to specific projects are restricted and cannot be used to meet a council's other operating and borrowing costs. The Unrestricted Current Ratio is specific to local government and is designed to represent a council's ability to meet debt payments as they fall due.