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Lachlan Shire Council

Financial Assessment, Sustainability and Benchmarking Report

19 March 2013

Prepared by NSW Treasury Corporation for Lachlan Shire Council, the Division of Local Government and the Independent Local Government Review Panel.

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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 to assist the DLG and the Independent Local Government Review Panel in its consideration of the Sustainability of each local government area in NSW.

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, and Council's future Sustainability, within prudent risk parameters and the limits of its financial projections.

The report has been prepared for Lachlan Shire Council, the DLG and the Independent Local Government Review Panel. TCorp shall not be liable to Lachlan 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 Lachlan Shire Council's (the Council) financial capacity, and its future Sustainability. 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.

TCorp's approach has been to:

- Review the most recent four years of Council's consolidated financial results
- Conduct a detailed review of the Council's 10 year financial forecasts, with a particular focus on a council's General Fund. Where a council operates a Water or other Fund the financial capacity of these other Funds may be reviewed where considered necessary.

We have analysed the management of Council's operating performance over the review period and make the following observations:

- Council achieved an operating surplus of $2.9m in 2012, when capital grants and contributions are excluded, following three years of operating deficits. The surplus was generated by the prepayment of half the 2013 Financial Assistance Grant (FAG) of $1.9m and a $2.1m increase in RMS contributions. Council has confirmed that the RMS contribution increase was incorrectly stated in 2012 as operating revenue instead of capital revenue
- Council's liquidity remained adequate throughout the four years
- Council has operated with minimal borrowings through the review period and is debt free in 2012

The Council reported $85.0m of Infrastructure Backlog in 2012 which represents 39.7% of its infrastructure asset value of $214.2m. Other observations include:

- Council's reported Backlog has remained above $81m in each of the four years
- Public roads is the highest Backlog asset category at $70.1m in 2012
- Council has spent adequately on upgrades and new assets in each year but not sufficiently to reduce the Backlog
- On a cumulative basis Council has spent adequately on renewals since 2010, however annual maintenance funding has not been adequate in each of the four years

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

- As Council is still in the process of completing their Asset Revaluation process and their AMP, the current depreciation figure within the LTFP may increase which would have an adverse impact on the forecast operating position
- Council is forecasting marginal operating surpluses in each year with the largest being $0.3m in 2022
- Council's liquidity is forecast to remain adequate but at a lower level than historical figures
- Council is forecast to adequately spend on capital expenditure when compared against the current forecast depreciation expenses, but as we note above, depreciation is expected to be understated until the Asset Revaluations are completed

Based on the current LTFP, the Council has the capacity to undertake additional borrowings of up to $22.4m. This is based on the following analysis:

- Based on a benchmark of DSCR>2.0x, up to $22.4m could be borrowed in addition to any existing borrowings

Based on our review of both the historic financial information and the 10 year financial forecast within Council's current version of their LTFP we consider Council to be moderately Sustainable in the short term. Council faces increasing pressures in the medium to long term in relation to their infrastructure asset funding.

In respect of the long term Sustainability of the Council our key observations are:

- Council's operating performance has been adequate over the review period and is projected to achieve consecutive marginal operating surpluses within the General Fund over the next 10 years.
- Council is heavily reliant on operating grants and contributions from State and Federal Government and other public sector agencies. Any reduction in the historical amounts received could adversely affect Council's operating performance
- The completion of Council's Asset Revaluations will assist in providing a clear position regarding the asset funding that is required so that these requirements can then be incorporated within the AMP and LTFP
- The shortfall in asset maintenance and renewals funding identified in the current AMP highlights that Council is unable to maintain the current service levels of their infrastructure assets, especially the large road network

In respect of our Benchmarking analysis we have compared the Council's key ratios with other councils in DLG group 10. Our key observations are:

- Council's financial flexibility as indicated by the Operating Ratio is above the group average however the Own Source Operating Revenue Ratio is below the group average indicating that Council's performance has been boosted more from operating grants and contributions
- Council is the only Council within the group that operates debt free but does have capacity to utilise borrowings if required
- Council was in a sufficient liquidity position which on average is similar to the group average liquidity level
- Council performs strongly in terms of its Capital Expenditure Ratio but poorly in the Asset Maintenance Ratio and has a comparatively high 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, Sustainability and performance measured against a peer group of councils. It will complement Council's internal due diligence, the IP&R system of the Council and the DLG, together with the work being undertaken by the Independent Local Government Review Panel.

The report is to be provided to the DLG and the Independent Local Government Review Panel.

The key areas focused on are:

- The financial capacity of the Council
- The long term Sustainability of the Council
- 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 four 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 Council's General Fund
- Identify significant changes to future financial forecasts from existing financial performance and highlight risks associated with such forecasts, including those that could impact Council's Sustainability
- 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 and achieve long term Sustainability
- Conduct a high level review of the Council's IP&R documents for factors which could impact the Council's financial capacity, performance and Sustainability

In undertaking its work, TCorp relied on:

- Council's audited financial statements (2008/09 to 2011/12)
- Council's financial forecast model
- Council's IP&R documents
- Discussions with Council officers
- Other publicly available information such as information published on the IPART website

In completing the report, TCorp worked closely with Council management to analyse and understand the information gathered. The Council was given a draft copy of the report for their review and comment. Based on our discussions with Council:

- Council agrees with the findings of the report and has acknowledged TCorp's comments

Definition of Sustainability

In conducting our reviews, TCorp has relied upon the following definition of sustainability to provide guidance:

"A local government will be financially sustainable over the long term when it is able to generate sufficient funds to provide the levels of service and infrastructure agreed with its community."

Benchmark Ratios

In conducting our review of the Councils' financial performance, forecasts and Sustainability 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
Building and 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

Lachlan Shire Council LGA	
Locality & Size	
Locality	Central West
Area	14,973 km²
DLG Group	10
Demographics	
Population as at 2011	6,476
% under 18	27%
% between 18 and 59	48%
% over 60	25%
Expected population 2025	6,100
Operations	
Number of employees (FTE)	119
Annual revenue	$28.5m
Infrastructure	
Roads	4,446 km
Bridges	47
Infrastructure backlog value	$85.0m
Total infrastructure value	$214.2m

Lachlan Shire Council Local Government Area (LGA) is located to the west of regional centres Orange and Parkes, approximately a six hour drive west of Sydney. The main towns and villages are Condobolin, Lake Cargelligo, Tottenham, Tullibigeal, Bircher, Albert and Fifield.

The population is declining and ageing with a median age of 40 against the NSW average of 37.2.

The LGA has a large aboriginal community that represents approximately 16.4% of the population compared to the Australian average of 2.3%.

The Shire is the home to many traditional farming cultures and is one of the largest grain producing areas of NSW. It is a rich agricultural area with many other activities including sheep, wool and beef production.

The LGA has experienced six natural disasters since December 2009 with five floods and one bushfire.

A small but very successful light-manufacturing sector has emerged in both Condobolin and Lake Cargelligo. Council has also established industrial estates in an attempt to promote further growth. Tourism is an emerging industry with the natural beauty of the Lachlan River, the picturesque Lake Cargelligo, Gum Bend Lake and the Shire being regarded as the true gateway to the outback.

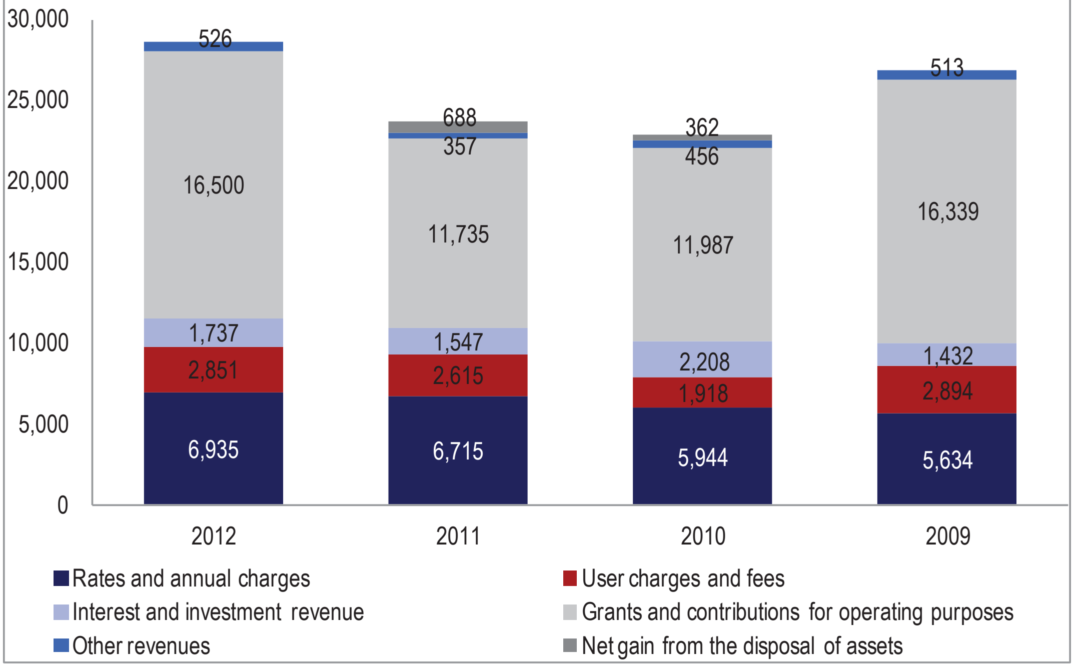
Lachlan Shire has the largest road network responsibility for any single LGA in NSW.

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 2011/12 ($'000s)



Key Observations

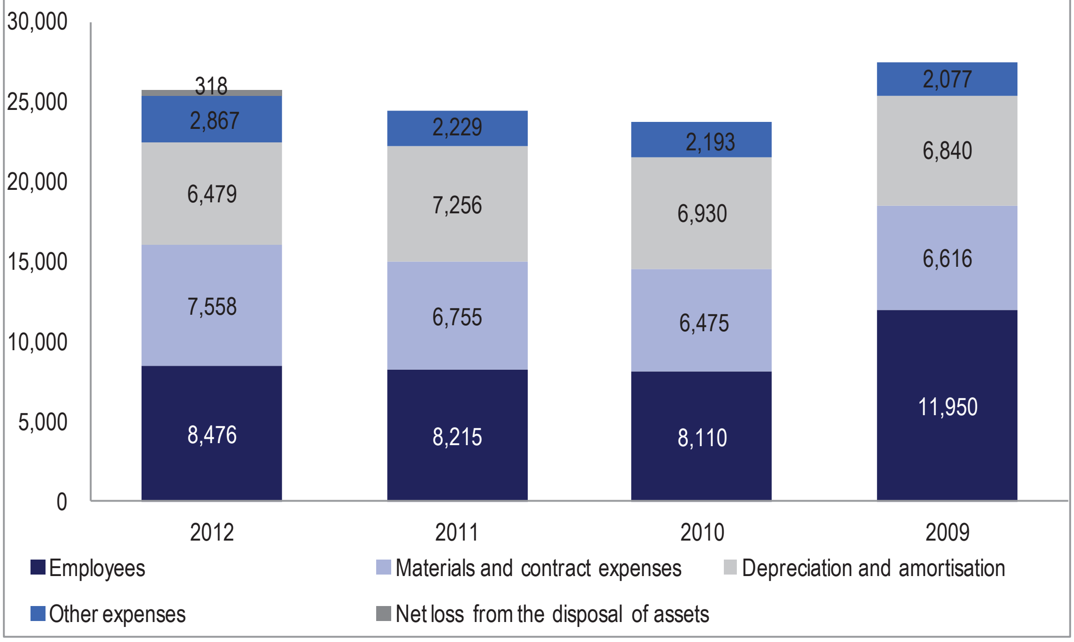
- Total operating revenues have increased by $1.7m (6.5%) over the review period to $28.5m in 2012.
- Rates and annual charges have increased year on year at rates of between 3.3% and 13.0% p.a. The 13.0% increase in 2011 occurred due to an increase in farmland ordinary rates, water supply and sewerage services and the addition of a non-domestic waste management charge that added $0.2m to the total.
- User fees and charges have fluctuated over the period and have reduced marginally when comparing 2012 to 2009. The 2009 figure included $0.9m revenues from the Condobolin District Retirement Village, the operation of which was contracted out in 2010 to The Whiddon Group with Council retaining ownership of the property. The increase in water supply services has driven the increase from 2010 increasing by $0.6m to $1.5m in 2012.
- Operating grants and contributions are Council's largest revenue sources and have fluctuated over the period. In 2012 the total increased due to the prepayment of half the 2013 Financial Assistance Grant (FAG) that increased the total by $1.9m while it was also boosted by a $0.7m increase in flood damage transport grants and a $2.1m increase in RMS contributions. Council has confirmed that the RMS contribution increase was incorrectly stated in 2012 as operating revenue instead of capital revenue. The 2009 total included $2.4m in community

care grants related to the retirement village while it also benefitted from advance payment of a portion of the 2010 FAG.

- Net gains from the disposal of assets have been included as Council have included these within their LTFP forecast. The gains made in 2010 and 2011 relate to the sale of plant and equipment.

3.2: Expenses

Figure 2 - Expenses for 2008/09 to 2011/12 ($'000s)



Key Observations

- Total operating expenses have decreased by $1.8m (6.5%) over the review period to $25.7m in 2012.
- Employee costs were the main factor for the decrease with the 2009 figure including the salary and wages of the employees of the retirement village that Council relinquished management of in 2010. The annual increases from 2010 to 2012 have been between 1.3% and 3.2% showing that Council have managed this expense well.
- Materials and contract expenses have been on an upward trend with the increase in raw materials and consumables cost in 2012 linked to the additional road maintenance and remediation work completed following flood damage.
- Depreciation expense was on a small upward trend until 2011 but decreased in 2012 by $0.8m following the disposal of plant and equipment with the depreciation amended accordingly.
- Other expenses have been on an upward trend with a 28.6% increase in 2012 driven by an increase in electricity and heating costs of $0.2m, a stock revaluation loss of $0.2m relating to an audit of Council's gravel/aggregate stockpiles and cleaning expenses of $0.1m.

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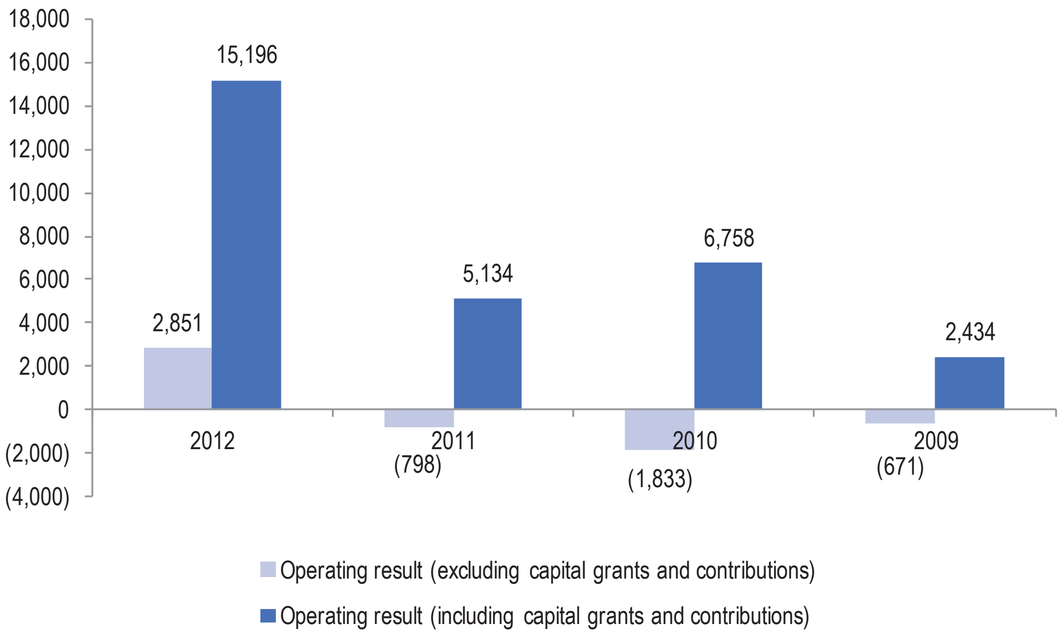
3.3: Operating Results

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 2011/12 ($'000s)



Key Observations

- Council has posted an operating surplus in 2012 following three annual deficits when capital grants and contributions are excluded.
- With operating grants and contributions being Council's largest revenue source the variations in this category impact the operating results and the improved 2012 result is because of the increase in this category.
- Depreciation expense has fluctuated over the review period and is at its lowest in 2012 however Council has not yet completed their Asset Revaluations in full and this may impact this figure in future years as has been experienced by other councils.

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3.4: Financial Management Indicators

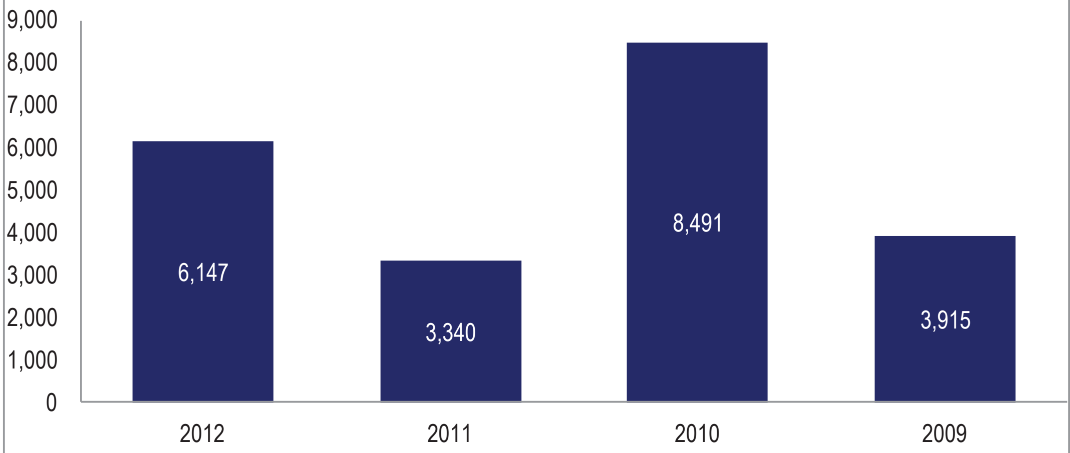
Performance Indicators	Year ended 30 June			
	2012	2011	2010	2009
EBITDA ($'000s)	9,330	6,458	5,097	6,169
Operating Ratio	10.0%	(3.4%)	(8.4%)	(2.5%)
Interest Cover Ratio	N/A	N/A	N/A	N/A
Debt Service Cover Ratio	N/A	N/A	N/A	N/A
Unrestricted Current Ratio	4.90x	4.26x	2.97x	3.70x
Own Source Operating Revenue Ratio	23.9%	31.5%	25.8%	28.5%
Cash Expense Ratio	3.8 months	2.3 months	6.1 months	2.3 months
Net assets ($'000s)	255,725	206,093	199,686	191,007

Key Observations

- Council's underlying operating performance, measured by EBITDA, has improved in 2012. The timing differences of the operating grants and contributions contributed to this improvement.
- The Operating Ratio has been above the negative 4% benchmark in three of the four years indicating a relatively Sustainable operating performance over the review period.
- Council has operated debt free throughout the review period therefore the DSCR and Interest Cover Ratio are not able to be calculated.
- The Unrestricted Current Ratio has been above the 1.5x benchmark throughout the review period and has been on an upward trend since 2010.
- The Own Source Operating Revenue Ratio has been significantly below the benchmark in each year, highlighting Council's strong reliance on grants and contributions to assist with managing their operations.
- The Cash Expense Ratio has seen a varied performance and has been above the 3.0 months benchmark in 2010 and 2012 but below in 2009 and 2011. This is because of a fluctuating level of cash and cash equivalents as highlighted in Section 3.5 due to additional funds being classified as investments in certain years. Council had an adequate level of liquidity overall
- Net Assets have been on an upward trend over the period due in part to the partially completed Asset Revaluations. In each year Council revalued their infrastructure assets and buildings which increased the value of these assets over the period by $35.6m.
- When the Asset Revaluations are excluded there has been a $23.5m increase in the IPP&E asset base over the three year period, compared to the written down value of disposed assets and depreciation.

3.5: Statement of Cashflows

Figure 4 - Cash and Cash Equivalents for 2008/09 to 2011/12 ($'000s)



Key Observations

- Cash and cash equivalents have varied over the review period as illustrated above however Council has also held funds in current investments.
- When including current investments, Council's funds have remained static with a total of $16.9m in 2012 compared to $17.5m in 2009.
- Cash and cash equivalents, current and non-current investments total $26.7m in 2012. Of this total, $11.7m was externally restricted, $15.0m was internally restricted.
- Of the $20.5m in investments, $17.3m was held in non current term deposit accounts and $3.2m was held in Negotiable Certificates of Deposit and FRNs.
- The level of cash and cash equivalents along with the Unrestricted Current Ratio above the benchmark indicates Council has had sufficient liquidity.

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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 2011/12($'000s)

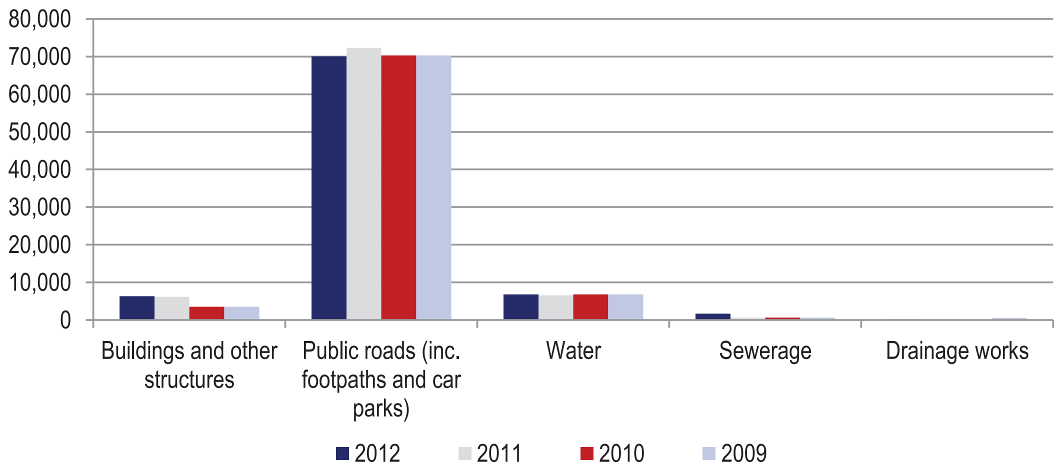
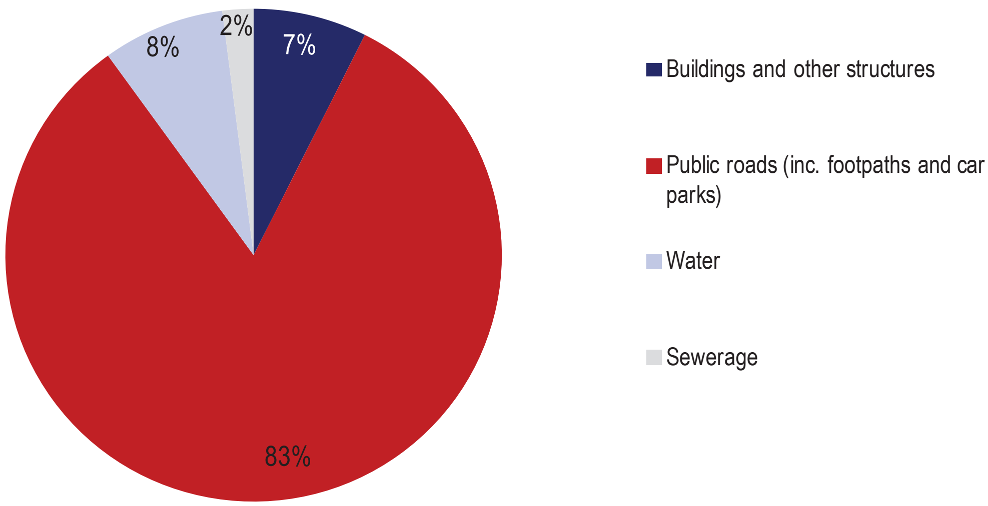


Figure 6 - Infrastructure Backlog Composition for 2011/12



Council's Infrastructure Backlog total is $85.0m as at 2012. This total has increased marginally from $81.8m in 2009.

Public roads are the largest backlog asset class with a total of $70.0m (82.4%) in 2012.

Council is still in the process of completing their Asset Revaluations therefore the Backlog total may grow further once this has been finalised.

3.6(b): Infrastructure Status

Infrastructure Status	Year ended 30 June			
	2012	2011	2010	2009
Bring to satisfactory standard ($'000s)	85,022	85,926	81,266	81,821
Required annual maintenance ($'000s)	10,440	9,175	8,795	8,795
Actual annual maintenance ($'000s)	5,225	0	4,088	4,110
Total value of infrastructure assets ($'000s)	214,189	168,231	163,925	158,705
Total assets ($'000s)	267,575	215,658	210,210	200,661
Building and Infrastructure Backlog Ratio	0.40x	0.51x	0.50x	0.52x
Asset Maintenance Ratio	0.50x	0.60x	0.46x	0.47x
Building and Infrastructure Renewals Ratio	0.72x	1.10x	1.54x	0.08x
Capital Expenditure Ratio	3.10x	1.47x	1.51x	1.43x

The Building and Infrastructure Backlog Ratio has reduced over the period, due to the Asset Revaluation process increasing the total value of infrastructure assets as opposed to any reduction of the Backlog figure.

The Asset Maintenance Ratio has not met the benchmark in any period highlighting Council has not been adequately providing for maintaining the operating standard of their assets.

The Building and Infrastructure Renewals Ratio has been on a downward trend since 2010 and decreased back below the benchmark in 2012 indicating Council invested enough to renew assets to their original standard in 2010 and 2011 but not in 2009 or 2012.

Council's Capital Expenditure Ratio, which takes into account assets which improve performance or capacity, has remained above the 1.10x benchmark each year. This indicates Council has expanded their Net Assets over the period as confirmed in Section 3.4 and the ratios suggest that Council has focussed on expanding the asset base as opposed to maintaining or renewing the existing assets. The spike in the ratio in 2012 is related to the $14.5m water supply augmentation project.

3.6(c): Capital Program

Council's capital works program and purchases for 2011 and 2012 included:

- Water supply augmentation - $14.5m
- Road construction/renewals - $9.3m
- Purchases of plant used for roadworks- $5.1m
- Building construction - $2.9m

3.7: Specific Risks to Council

- Large road network. Council has to manage the largest road network within all 152 LGAs at 4,446km. This provides a significant challenge for Council in terms of maintenance and renewals however due to the low population, it means that the road network is not subjected to heavy traffic volumes. Despite this, Council has identified within their AMP for roads that "present funding levels are insufficient to continue to provide existing services at current levels in the medium to long term". Unless additional funding is provided, Council will have to manage the assets "through a risk management process to minimise the impact on assets and users".
- Inability to reduce Infrastructure Backlog. The issue with the roads stated above highlights the fact that Council do not have the capacity to reduce the Infrastructure Backlog and the ongoing shortfall in maintenance and renewals funding will result in an increase in the Backlog as opposed to it decreasing. Due to Council's relatively low population, compared to the Backlog total, Council will not be able to raise enough funding from their own sourced operating revenue to make a significant impact on the Backlog, therefore it appears only an increase in grant funding will assist the situation. Council will also have to investigate other options including operating efficiencies and the possible rationalisation of assets.
- Environmental disasters / climate change. Council has experienced six natural disasters since December 2009 due mainly to flooding. This has a major impact on Council's ability to manage the infrastructure assets with the rehabilitation of flood damaged roads taking priority over scheduled maintenance and renewals.
- Ageing and declining population. Council's population has a median age of 40 and is above the NSW median of 37.2 and the population is forecast to decrease by approximately 6% by 2021. Recent demographic trends have seen people leave the LGA in search of a better standard of living, due to isolation of the LGA, flood and drought cycles affecting the agricultural economy, and increased education and job opportunities in other LGAs for the younger generations. Council is expected to provide increased service levels as the population grows older while their own sourced operating revenue base diminishes.
- Reliance on grants and contributions. While a significant number of councils rely on this source of funding to boost their revenues, at 75% of total revenues in both 2011 and 2012, Council is especially susceptible if any changes in grant and contribution funding occurs. Council is therefore likely to see a large deterioration in operating results when the prepayment of the FAG ceases and Council receive a significantly lower level than received in 2012.

Section 4 Review of Financial Forecasts

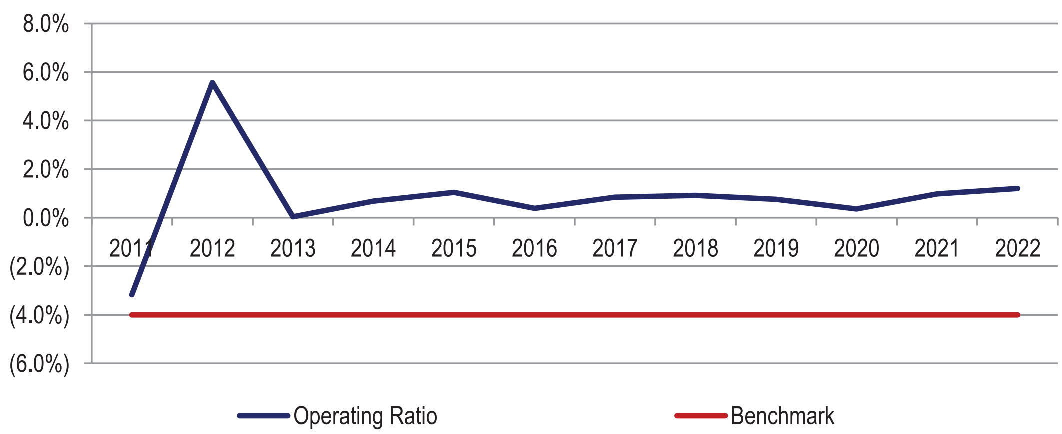
The financial forecast model shows the projected financial statements and assumptions for the next 10 years. We have focused our financial analysis upon the General Fund as Council's consolidated position includes both a Water and Sewer Fund that are operated as independent entities, which unlike the General Fund are more able to adjust the appropriate fees and charges to meet all future operating and investing expenses.

Council has completed three scenarios, a 'base case', along with a 'pessimistic' and 'optimistic' case.

The base case has been adopted by Council, with this representing a continuation of the current service levels. The modelling was completed prior to the 2012 historic results being finalised. We have used actual 2012 results in the graphs and analysis below.

4.1: Operating Results

Figure 7- Operating Ratio for General Fund



The Operating Ratio is forecast to reduce from the 5.6% surplus in 2012 to a break-even position in 2013 before remaining in small surpluses each year with a high of 1.2% ($0.3m) in 2022.

The decrease in 2013 is predominantly due to the projected decrease in the FAG and flood related grants that result in a $2.5m decrease in operating grants and contributions, alongside a $1.2m increase in depreciation expense. This is off-set by a decrease in materials and contract expenses of $1.3m as flood related works decrease.

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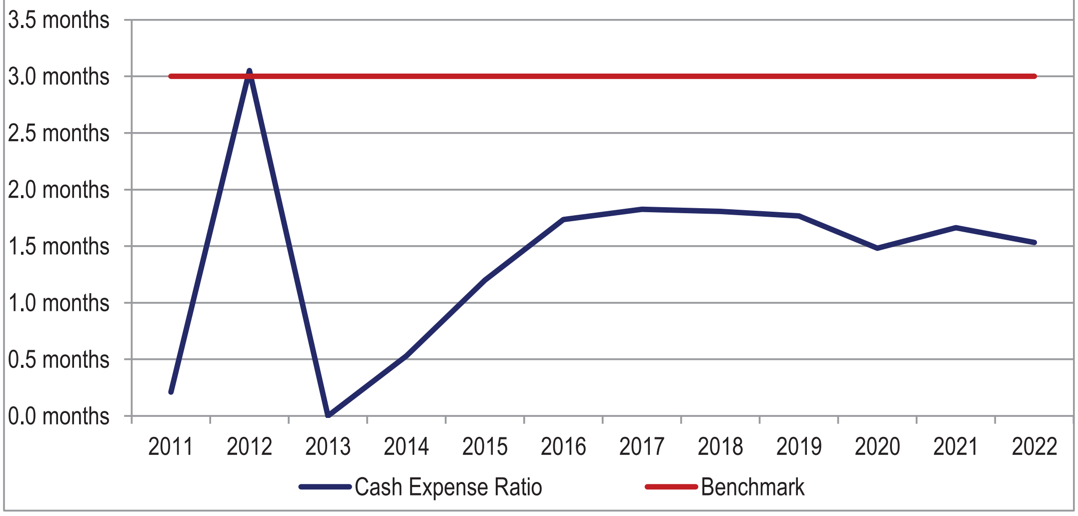
4.2: Financial Management Indicators

Liquidity Ratios

Figure 8 - Cash Expense Ratio for General Fund

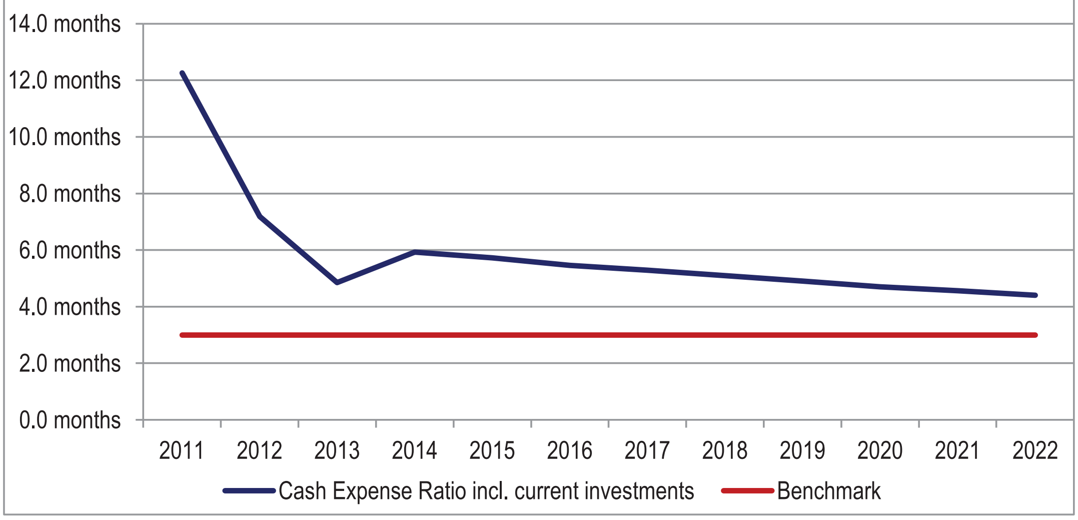


The 2013 Cash Expense Ratio is forecast at zero with Council's projected funds of $6.8m classified solely as investments. This is unrealistic and Council has stated that this is a modelling error and they would manage their cashflows so that a minimum $0.5m would remain in cash and cash equivalents at any one time.

In each year from 2014 to 2019 the cash and cash equivalents total is projected to increase up to $2.3m and remain above $2.0m for the remaining years of the forecast.

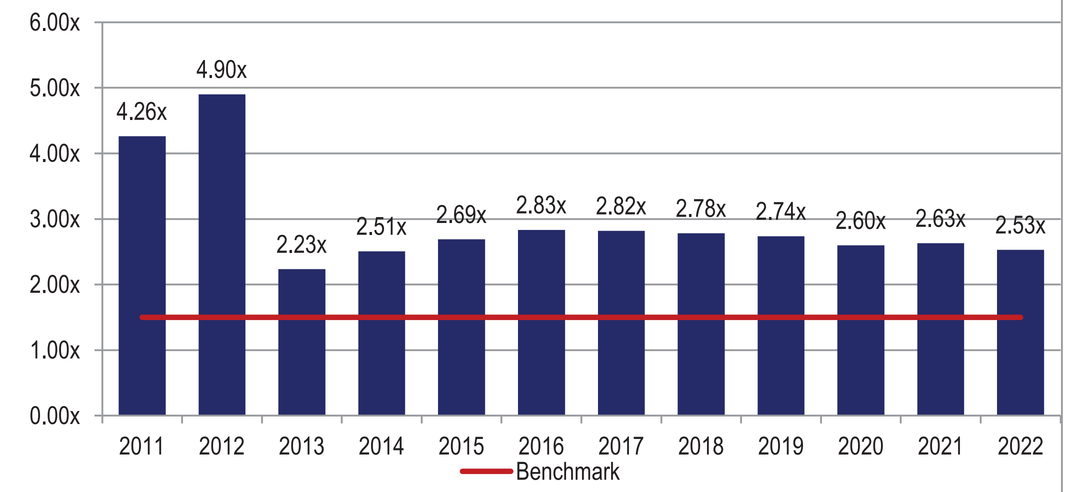
Throughout the forecast period the investments have been modelled to remain static at $6.8m.

Figure 9 - Cash Expense Ratio for General Fund including current investments



With the current investments included Council's funds remain above the benchmark in all 10 years.

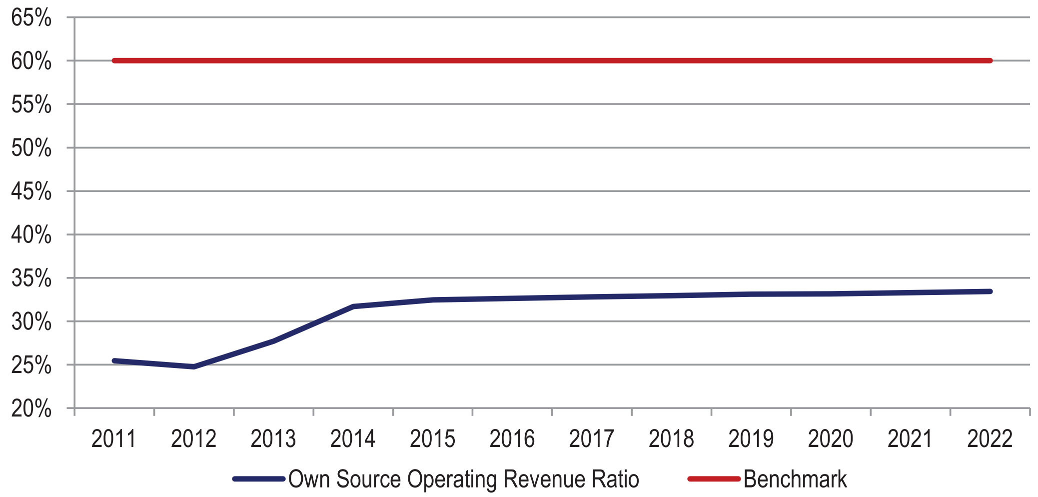
Figure 10 - Unrestricted Current Ratio for General Fund



Council is forecasting the Unrestricted Current Ratio to remain above the benchmark in each year indicating Council's liquidity will continue to be adequate over the period.

Fiscal Flexibility Ratios

Figure 11 - Own Source Operating Revenue Ratio for General Fund



Council has historically relied heavily on grants and contributions with 75% of their revenues being generated from these sources in both 2011 and 2012.

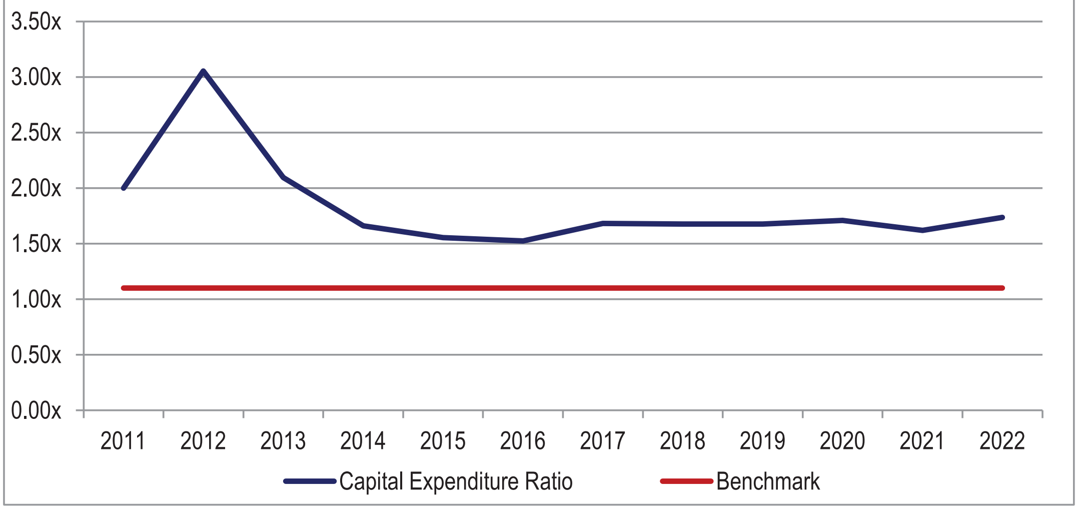
Council has forecast that their own source operating revenues will increase in 2013 and 2014 as the FAG and flood related grants reduce however Council is forecast to remain reliant on grants and contributions for over 65% of the revenues.

Council is planning to continue to operate without the need for any borrowings therefore the DSCR and Interest Cover Ratio are unable to be calculated.

Based on the current LTFP, Council do have the capacity to utilise borrowings as stated in Section 4.5.

4.3: Capital Expenditure

Figure 12 - Capital Expenditure Ratio for General Fund



Council's Capital Expenditure Ratio is forecast to decrease from the high levels achieved in 2011 and 2012 but remain comfortably above the 1.10x benchmark throughout the forecast period with a low of 1.52x in 2016.

This results in a projected increase in the value of IPP&E within the General Fund by $28.9m over the forecast period.

Council has stated that they are still in the process of completing their Asset Revaluations and that these will be completed in time for the 2014 financial year. The current depreciation figures stated within the LTFP are $6.5m p.a., above the 2012 figure of $5.4m. A further increase in the forecast depreciation will result in a reduction of the Capital Expenditure Ratio.

If depreciation does not increase above the LTFP figures and Council is able to invest at the forecast levels then it appears the Infrastructure Backlog should begin to reduce.

The strong performance of the Capital Expenditure Ratio is in contrast to the asset management information within the LTFP document and the AMP for roads that state that Council has an annual shortfall for asset maintenance and renewals of $9.6m, with $6.5m of the shortfall relating to roads and bridges. This indicates it is likely that the Asset Revaluations will result in Council having higher depreciation expenses.

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 5.0%
- All other revenue items: the estimated annual CPI increase of 2.5%
- Employee costs: 3.5% (estimated CPI+1.0%)
- All other expenses: the estimated annual CPI increase of 2.5%

<u>Key Observations and Risks</u>

- Council's Asset Revaluations are not due to be completed in full until 2013 therefore the AMP does not include complete data. The depreciation figures within the LTFP may subsequently be understated, resulting in inflated operating results.
- Council's adopted 'base case' has been modelled on current service levels continuing as best as possible given the projected shortfall in asset maintenance and renewals funding.
- Rates and annual charges are forecast to increase by 4.4% in 2013 and 3.0% p.a. thereafter.
- User charges and fees are forecast to decrease by 13.3% in 2013 and then increase 3.5% in 2014 and 2.9% p.a. thereafter. The 2013 decrease is due to a larger than forecast increase in caravan fees being received in 2012 that are not forecast at such a level within the LTFP.
- Operating grants and contributions are forecast to reduce by 15.1% in 2013 and 20.5% in 2014 as Council's grants reduce from the normalisation of the FAG payments and flood related grants, before increasing between 3.0% and 3.2% p.a.
- Council has forecast a gain from the disposal of assets of $0.25m p.a. relating to the sale of residential and industrial land subdivisions that has been created by Council. The profit from these sales is to be used to repay the internal loans utilised to construct the estates.
- Employee expenses are forecast to increase between 3.1% and 4.0% p.a.
- Materials and contracts costs are forecast to decrease by 21.9% in 2013 and by 68.0% in 2014 as Council complete the flood related works before steadying and varying between a 0.2% decrease in 2017 and a 13.7% increase in 2016. The large decreases in 2013 and 2014 reduce this expense from $6.0m in 2012 to $1.5m in 2014, a level significantly below all of the review years. Council has confirmed that there is a difference in the classification of some expenses within the LTFP and the audited financial statements. In future some expenses that are classified within other expenses in the LTFP will be transferred to materials and contract expenses in line with the audited financial statements.

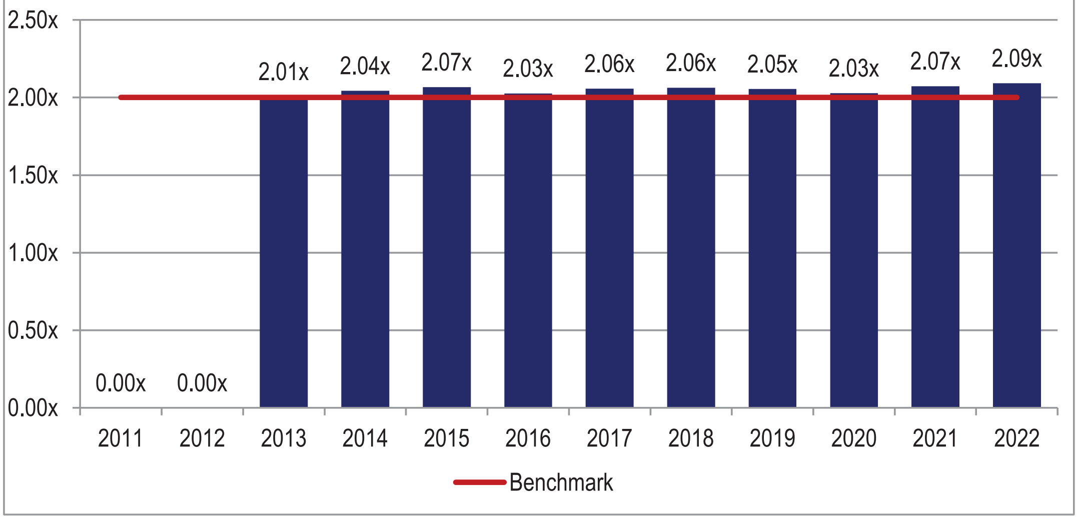
- Depreciation is forecast to increase by 21.5% in 2013 to $6.5m and remain static for the remaining nine years. It is not clear if this is an accurate assumption until the Asset Revaluations are complete.
- Other expenses are forecast to increase by 42.9% in 2013 to $3.9m and then increase between 2.3% and 3.6% p.a. thereafter. As explained above, this is due to the classification of some expenses that will be re-classified within materials and contracts expenses in future.
- Council's underlying assumptions appear reasonable with the exception of the projected decrease in materials and contracts costs that reduces this expense significantly below historical levels. The re-classification of a portion of other expenses should rectify this for future LTFPs. We note that this is partly due to a decrease in flood related works. There is also the uncertainty regarding the depreciation expenses noted above.

4.5: Borrowing Capacity

When analysing the financial capacity of the Council, based on the current LTFP, we believe Council will be able to incorporate new loan funding. Some comments and observations are:

- Based on a benchmark of DSCR>2.0x, up to $22.4m could be borrowed in addition to any existing borrowings
- This scenario has been calculated by basing borrowing capacity on a 10 year amortising loan at an interest rate of 7.5%

Figure 13 - DSCR for General Fund with new borrowings of $22.4m in 2013



4.6: Sustainability

Financial

TCorp believes Council is currently in a moderately Sustainable position. Council's operating position has been above the negative 4.0% benchmark in three of the four review years however it has only achieved an operating surplus in 2012.

Council is forecasting marginal operating surpluses within the General Fund in each year of the forecast. The finalisation of the Asset Revaluations due to be completed in 2013 will provide accurate asset information and depreciation figures to incorporate into the LTFP forecast. Council also has the issue of meeting their ongoing asset maintenance and renewals commitments.

Council needs to focus their capital program on renewals as opposed to new assets as has occurred in recent years. With Council projecting a maintenance and renewals shortfall of $9.6m p.a. the addition of new assets appears to be compounding the issue and the annual funding gap for maintenance and renewals will continue to increase.

The LTFP written document highlights that Council has historically not borrowed externally and that this has not always been the most efficient way to fund capital works. Council has stated that the LIRS scheme is an option to receive external borrowings at discounted rates however they have confirmed that this has not been explored as yet.

Council also has the option of applying for an SRV however a 5% increase over the rate peg that would be permanently included in the rate base is projected to raise an additional $2.5m over the 10 year period and will not make a significant impact on the Infrastructure Backlog. This has not been applied for or included within the current scenarios of the LTFP but has been stated within the LTFP as a future possibility.

Council is one of 16 councils alongside one water county council that are members of CENTROC with the aim of advocating and improving operating efficiencies for its members. It provides joint tenders and contracts for services such as electricity supply, fuels and lubricants. It also provides cost savings from economies of scale achieved through the buying power of one larger organisation.

Infrastructure

Council has the largest road network of all 152 LGAs in NSW, for a population of approximately 6,500.

The challenge Council faces is that they have a large Infrastructure Backlog without the financial capacity to reduce the total while the shortfall in maintenance and renewals funding of $9.6m p.a. highlights the Backlog total is only going to increase in the future.

As Council's AMP for road's details, their present funding levels are insufficient to continue existing service levels in the medium to long term therefore it appears without additional grants and contribution funding, Council will likely have to consult with the community to prioritise key assets while reducing the service levels for low priority assets, identify operating efficiencies or rationalise some non-core assets.

In considering the longer term Sustainability of the Council we make the following comments:

- Council's operating performance has been adequate over the review period and is projected to achieve consecutive marginal operating surpluses within the General Fund over the next 10 years.
- Council is heavily reliant on these grants and contributions from State and Federal Government and other public sector agencies. Any reduction in the historical amounts received will adversely affect Council's operating performance and turn the projected surpluses to deficits
- The completion of Council's Asset Revaluations will assist in providing a clear position regarding the asset funding that can then be incorporated within the AMP and LTFP
- The shortfall in asset maintenance and renewals funding identified in the current AMP highlights that Council will be unable to maintain current service levels of their infrastructure assets, especially the large road network

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Section 5 Benchmarking and Comparisons with Other Councils

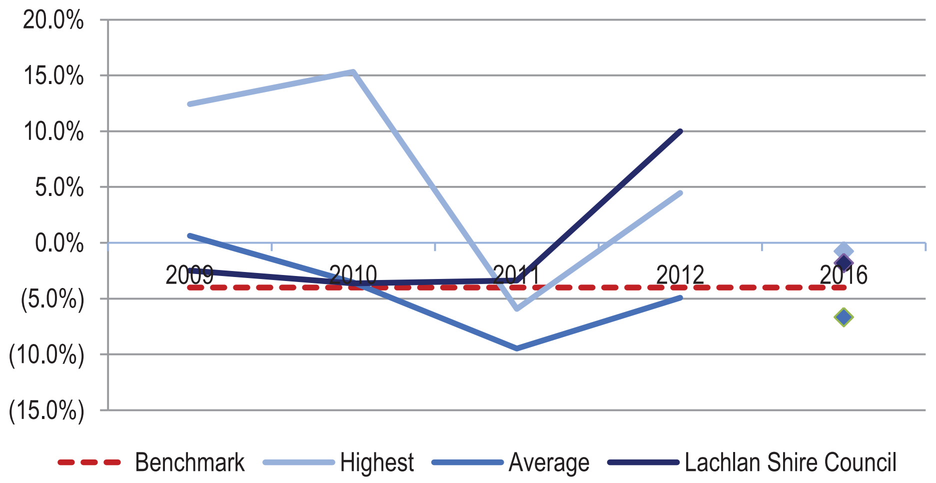
Each council's performance has been assessed against ten key benchmark ratios. This section of the report compares the Council's performance with its peers in the same DLG Group. The Council is in DLG Group 10. There are 25 councils in this group and at the time of preparing this report, we have data for all of these councils.

In Figure 14 to Figure 18, 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 19 to 21 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. We have not included comparisons for the Interest Cover Ratio and Debt Service Cover Ratio due to the fact that Council has not utilised borrowings during the review period and is forecast to continue to in the future.

Financial Flexibility

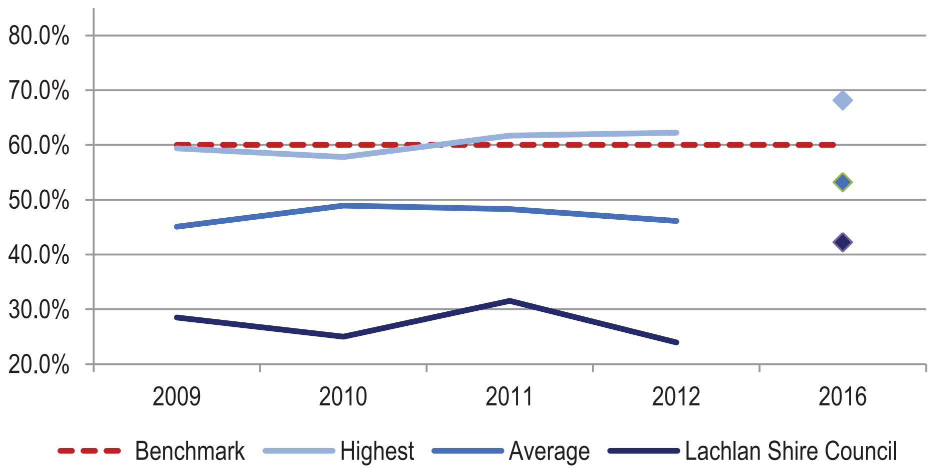
Figure 14 - Operating Ratio Comparison



Council's Operating Ratio has remained above the benchmark in each year and above the group average since 2010. The 2012 ratio is higher than the highest average performer, driven by the increased operating grants and contributions.

Council's projected position is forecast to remain above both the benchmark and group average indicators.

Figure 15 - Own Source Operating Revenue Ratio Comparison

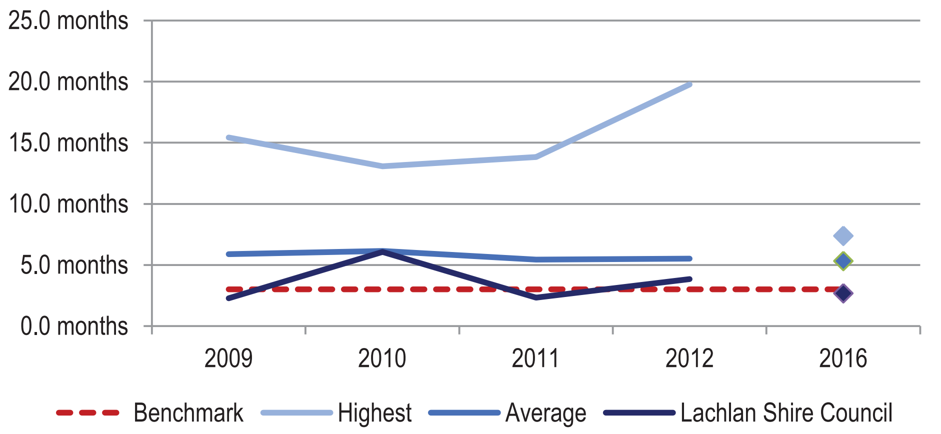


Council's Own Source Operating Ratio confirms that they have relied more heavily on grants and contributions than the group average. The group average is below the benchmark indicating how important external sources of revenues are to councils with demographics that place them in this group.

The forecast position is projected to improve as Council isn't expecting to be so reliant on grants and contributions although they remain below both the group average and the benchmark.

Liquidity

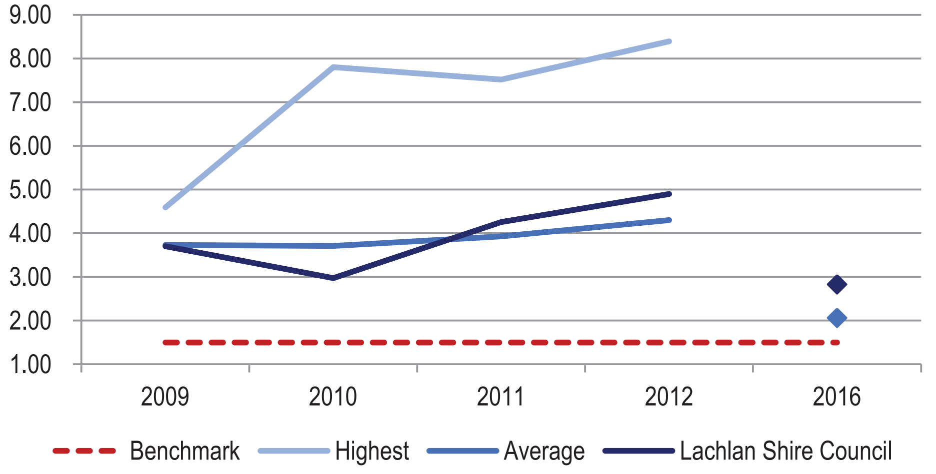
Figure 16 - Cash Expense Ratio Comparison



Council's Cash Expense Ratio has been below the group average in three of the four review years but was above the benchmark in 2010 and 2012.

Council's forecast ratio is projected to be below both the group average and benchmark although a reason for this may be that Council holds the majority of their funds within investments that are not included within this ratio.

Figure 17 - Unrestricted Current Ratio Comparison



Council's Unrestricted Current Ratio has been above the benchmark in each year and the group average in the past two years.

It is projected to decrease in the forecast however it remains above the group average and the benchmark.

Council, along with the group average are forecast to have adequate liquidity to meet ongoing short term liabilities.

Debt Servicing

Council is the only Council within the group that has operated without any borrowings over the four review years therefore we have not included any graphs for the DSCR and Interest Cover Ratio.

Asset Renewal and Capital Works

Figure 18 - Capital Expenditure Ratio Comparison

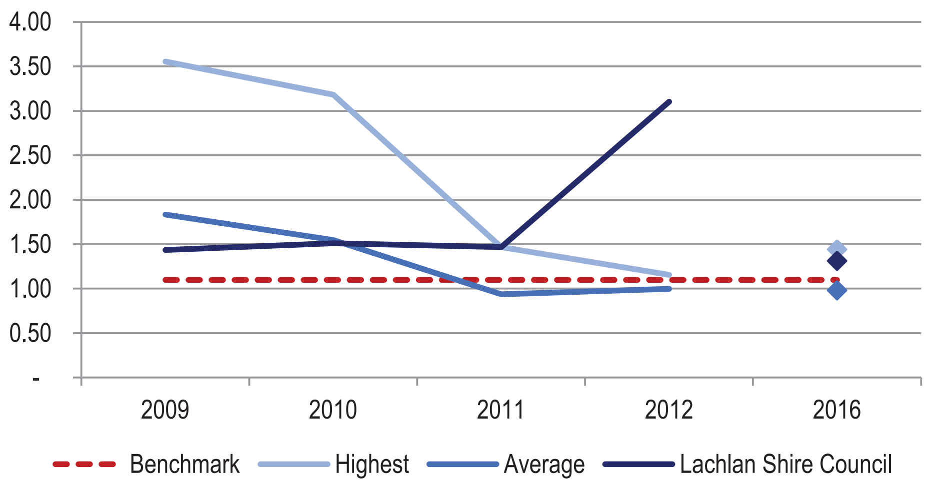


Figure 19 - Asset Maintenance Ratio Comparison

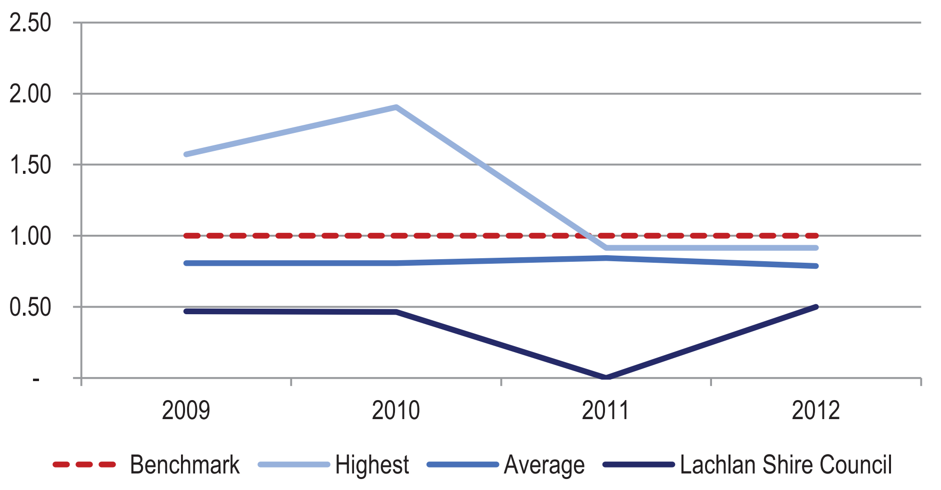


Figure 20 - Infrastructure Backlog Ratio Comparison

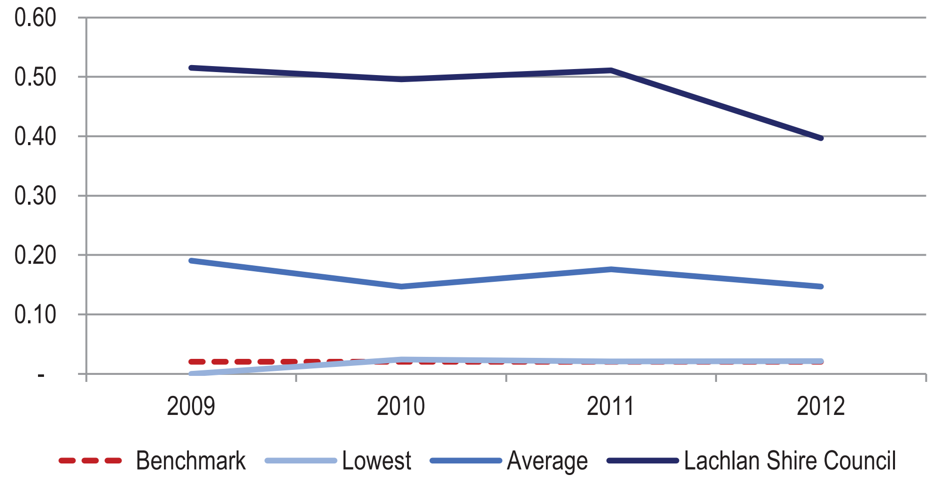
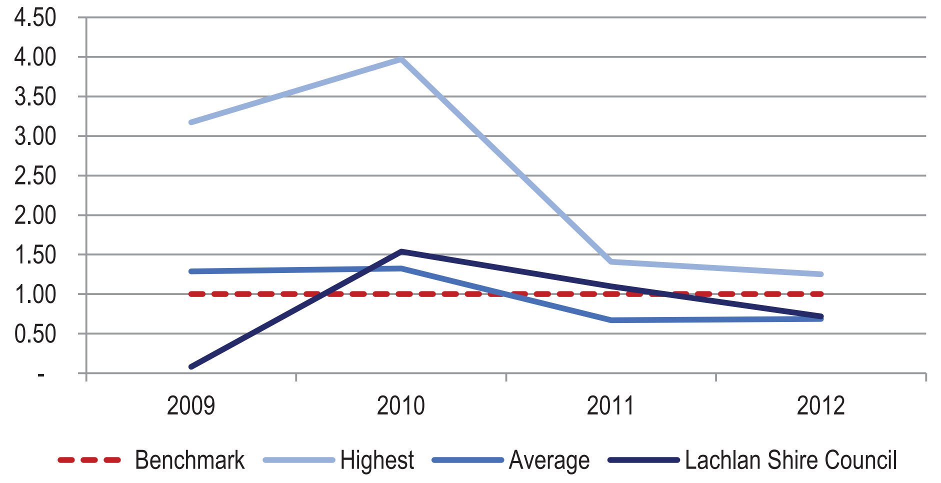


Figure 21 - Building and Infrastructure Asset Renewal Ratio



Council's Capital Expenditure Ratio has been above the group average since 2010 and above benchmark in each year highlighting their strong focus on asset upgrades or additions.

Council has been below the group average and benchmark in each year for the Asset Maintenance Ratio indicating Council needs to improve their allocation for maintenance funding.

Council's Infrastructure Backlog is comparatively large compared to the group average and benchmark indicating the challenge Council has.

The Building and Infrastructure Asset Renewal Ratio has fluctuated over the period and climbed above the benchmark and group average in 2010 but has decreased below the benchmark and was equal to the group average in 2012.

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Section 6 Conclusion and Recommendations

Based on our review of both the historic financial information and the 10 year financial forecast within Council's current version of their LTFP we consider Council to be moderately Sustainable in the short term but Council face increasing pressures in the medium to long term in relation to their infrastructure asset funding.

We base our recommendation on the following key points:

- Council has achieved operating results above the negative 4.0% benchmark in three of the four review years when capital grants and contributions are excluded
- Council has forecast marginal operating surpluses to remain for all 10 years of the LTFP
- Council has focussed on the upgrade and addition of new assets in recent years and this is not Sustainable given Council's large asset base in relation to their revenue base

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

- Council is heavily reliant on grants and contributions to boost their revenues, with 75% of total revenues being received in 2011 and 2012
- Council's Infrastructure Backlog has been above $81m in the last four years and the projected $9.6m shortfall in asset maintenance and renewals funding is only going to increase this figure
- Council remains in the process of finalising their Asset Revaluations, this may negatively impact on the forecast operating results if depreciation expenses increase above the levels within the current LTFP
- A revised focus on asset renewals as opposed to upgrades or new assets is advised to assist with improving the quality of the asset base and reducing the maintenance and renewals funding gap
- Council should investigate all revenue raising options including the possibility of an SRV and the option of applying for LIRS funding in order to assist with their outstanding infrastructure renewals and therefore reducing the Infrastructure Backlog

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Appendix A Historical Financial Information Tables

Table 1- Income Statement

Income Statement ($'000s)	Year ended 30 June				% annual change		
	2012	**2011**	**2010**	**2009**	**2012**	**2011**	**2010**
Revenue							
Rates and annual charges	6,935	6,715	5,944	5,634	3.3%	13.0%	5.5%
User charges and fees	2,851	2,615	1,918	2,894	9.0%	36.3%	(33.7%)
Interest and investment revenue	1,737	1,547	1,208	1,432	12.3%	28.1%	(15.6%)
Grants and contributions for operating purposes	16,500	11,735	11,987	16,339	40.6%	(2.1%)	(26.6%)
Other revenues	526	357	456	513	47.3%	(21.7%)	(11.1%)
Net gain from the disposal of assets	0	688	362	0	(100.0%)	90.1%	N/A
Total revenue	**28,549**	**23,657**	**21,875**	**26,812**	**20.7%**	**8.1%**	**(18.4%)**
Expenses							
Employees	8,476	8,215	8,110	11,950	3.2%	1.3%	(32.1%)
Borrowing costs	0	0	0	0	N/A	N/A	N/A
Materials and contract expenses	7,558	6,755	6,475	6,616	11.9%	4.3%	(2.1%)
Depreciation and amortisation	6,479	7,256	6,930	6,840	(10.7%)	4.7%	1.3%
Other expenses	2,867	2,229	2,193	2,077	28.6%	1.6%	5.6%
Net loss from the disposal of assets	318	0	0	0	N/A	N/A	N/A
Total expenses	**25,698**	**24,455**	**23,708**	**27,483**	**5.1%**	**3.2%**	**(13.7%)**
Operating result	**2,851**	**(798)**	**(1,833)**	**(671)**	**457.3%**	**56.5%**	**(173.2%)**

Table 2 - Items excluded from Income Statement

Excluded items ($'000s)				
	2012	**2011**	**2010**	**2009**
Grants and contributions for capital purposes	12,345	5,932	8,591	3,105
Increase (Decrease) in the fair value of investments	(15)	10	(116)	(1,557)
Borrowing costs (remediation liabilities)	1,178	(72)	109	90

Table 3 - Balance Sheet

Balance Sheet ($'000s)	Year Ended 30 June				% annual change		
	2012	2011	2010	2009	2012	2011	2010
Current assets							
Cash and equivalents	6,147	3,340	8,491	3,915	84.0%	(60.7%)	116.9%
Investments	10,707	15,154	16,330	13,561	(29.3%)	(7.2%)	20.4%
Receivables	4,108	1,635	2,382	2,140	151.3%	(31.4%)	11.3%
Inventories	2,673	2,434	2,338	1,789	9.8%	4.1%	30.7%
Other	100	123	126	194	(18.7%)	(2.4%)	(35.1%)
Total current assets	23,735	22,686	29,667	21,599	4.6%	(23.5%)	37.4%
Non-current assets							
Investments	9,800	8,904	1,000	6,162	10.1%	790.4%	(83.8%)
Receivables	332	254	267	117	30.7%	(4.9%)	128.2%
Inventories	511	337	421	388	51.6%	(20.0%)	8.5%
Infrastructure, property, plant & equipment	232,920	183,228	178,855	172,395	27.1%	2.4%	3.7%
Intangible assets	277	249	0	0	11.2%	N/A	N/A
Total non-current assets	243,840	192,972	180,543	179,062	26.4%	6.9%	0.8%
Total assets	**267,575**	**215,658**	**210,210**	**200,661**	**24.1%**	**2.6%**	**4.8%**
Current liabilities							
Payables	1,628	1,047	2,005	1,197	55.5%	(47.8%)	67.5%
Borrowings	0	8	0	0	(100.0%)	N/A	N/A
Provisions	5,384	5,371	5,116	5,440	0.2%	5.0%	(6.0%)
Total current liabilities	7,012	6,426	7,121	6,637	9.1%	(9.8%)	7.3%
Non-current liabilities							
Provisions	4,838	3,139	3,403	3,017	54.1%	(7.8%)	12.8%
Total non-current liabilities	4,838	3,139	3,403	3,017	54.1%	(7.8%)	12.8%
Total liabilities	**11,850**	**9,565**	**10,524**	**9,654**	**23.9%**	**(9.1%)**	**9.0%**
Net assets	**255,725**	**206,093**	**199,686**	**191,007**	**24.1%**	**3.2%**	**4.5%**

Table 4-Cashflow

Cashflow Statement ($'000s)	Year ended 30 June			
	2012	**2011**	**2010**	**2009**
Cashflows from operating activities	19,998	11,767	12,059	11,337
Cashflows from investing activities	(17,183)	(16,926)	(7,483)	(16,452)
Proceeds from borrowings and advances	0	0	0	0
Repayment of borrowings and advances	0	0	0	0
Cashflows from financing activities	0	0	0	0
Net increase/(decrease) in cash and equivalents	**2,815**	**(5,159)**	**4,576**	**(5,115)**
Cash and equivalents	6,147	3,340	8,491	3,915

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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.

[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.

Sustainability

A local government will be financially sustainable over the long term when it is able to generate sufficient funds to provide the levels of service and infrastructure agreed with its community

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

Building and Infrastructure Backlog Ratio

Benchmark = Less than 0.02x

Ratio = estimated cost to bring assets to a satisfactory condition (from Special Schedule 7) / total infrastructure assets (from Special Schedule 7)

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.