Dungog Shire Council

Financial Assessment, Sustainability and Benchmarking Report

13 March 2013

Prepared by NSW Treasury Corporation for Dungog 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 Dungog Shire Council, the DLG and the Independent Local Government Review Panel. TCorp shall not be liable to Dungog 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 Dungog 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.

When analysing Council's performance over the review period we make the following observations:

- Council has posted operating deficits in each year when capital grants and contributions are excluded until 2012. The 2012 surplus was recorded due to the prepayment of a portion of the Financial Assistance Grant for 2013
- The Unrestricted Current Ratio, Cash Expense Ratio and the level of cash and investments indicate that Council had adequate liquidity
- Council's DSCR and Interest Cover Ratio demonstrate that it could repay its debt obligations

The Council reported $51.9m of Infrastructure Backlog in 2012 which represents 40.2% of its infrastructure asset value of $129.0m. Other observations include:

- Council has not been able to complete the Asset Revaluations process due to a lack of qualified employees to complete the task. This has impacted the completion of the Asset Management Plan (AMP) and its integration with the LTFP.
- As a result of the above, the backlog total has not fluctuated to a large degree with it increasing from $49.1m in 2009 solely due to the buildings and other structures backlog increasing. During this period, the public roads and drainage works totals of $42.7m and $5.0m respectively have remained static indicating an update will be completed in line with the completion of the AMP
- Noting that the completion of the AMP may impact asset maintenance and renewals figures, based on the current figures:
    - Council has spent adequate funds on asset maintenance and capital expenditure over the review period as indicated by the respective cumulative totals against the required spending over the review period
    - Council did not spend adequate funds on asset renewals in 2011 and 2012 as shown by the Building and Infrastructure Renewals Ratio being below benchmark

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

- Council has projected operating deficits in the first eight years of the forecast period followed by two marginal surpluses when capital grants and contributions are excluded

- Council has forecast cash and cash equivalents to steadily increase over the period as indicated by an improving Cash Expense Ratio. This indicates that council should have adequate liquidity throughout the period
- Council's Capital Expenditure Ratio is below the benchmark in seven of the 10 years once Council has finished the capital works linked to a specific capital grant that will be utilised in the first three years of the forecast period

We are not in a position to analyse if Council has the capacity to undertake additional borrowings at the current time. This is because Council needs to complete their AMP and incorporate the asset requirements into their LTFP, before we are able to review an accurate forecast and analyse the possibility of Council utilising further debt facilities.

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

- It is probable that once Council's updated AMP and LTFP are completed following the Asset Revaluations process, Council will be identified as unsustainable
- This assumption is made as we would expect the value of Council's IPP&E to increase after the Asset Revaluations following our experience with other similar sized councils, which in turn is likely to increase deprecation, with Council unable to fund this going forward, further impacting the Infrastructure Backlog

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 and Own Source Operating Revenue Ratio is generally below the group's average
- Council has relatively less capacity to utilise further borrowings than the group average as it is has lower DSCR and Interest Cover Ratio
- Council was in a sufficient liquidity position and was above the group average liquidity level
- Council has performed adequately in terms of its Asset Maintenance Ratio and Capital Expenditure Ratio however they have a comparatively high level of Infrastructure Backlog

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

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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....]

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

Dungog Shire Council LGA	
Locality & Size	
Locality	Hunter
Area	2,252 km^2
DLG Group	10
Demographics	
Population as at 30 June 2011	8,318
% under 18	23%
% between 18 and 59	52%
% over 60	25%
Expected population 2025	9,200
Operations	
Number of employees (FTE)	66
Annual revenue	$13.3m
Infrastructure	
Roads	714 km
Bridges	113
Infrastructure backlog value	$51.9m
Total infrastructure value	$129.0m

Dungog Shire Council Local Government Area (LGA) is located centrally within the Hunter region and is surrounded by Gloucester, Great Lakes, Port Stephens, Maitland, Singleton and Upper Hunter LGAs. It is a one hour drive from Newcastle or less than three hours drive from Sydney.

Within the LGA are the townships of Dungog, Clarence Town, Gresford, Vacy, Martins Creek and Paterson.

The local economy is primarily related to agriculture and tourism with the LGA benefitting from national parks and state forests within its borders. Approximately 40% of the community travel outside of the LGA for work due to the proximity to the lower Hunter employment markets.

Within Council's Infrastructure, Property, Plant and Equipment (IPP&E) as at 30 June 2012 there was:

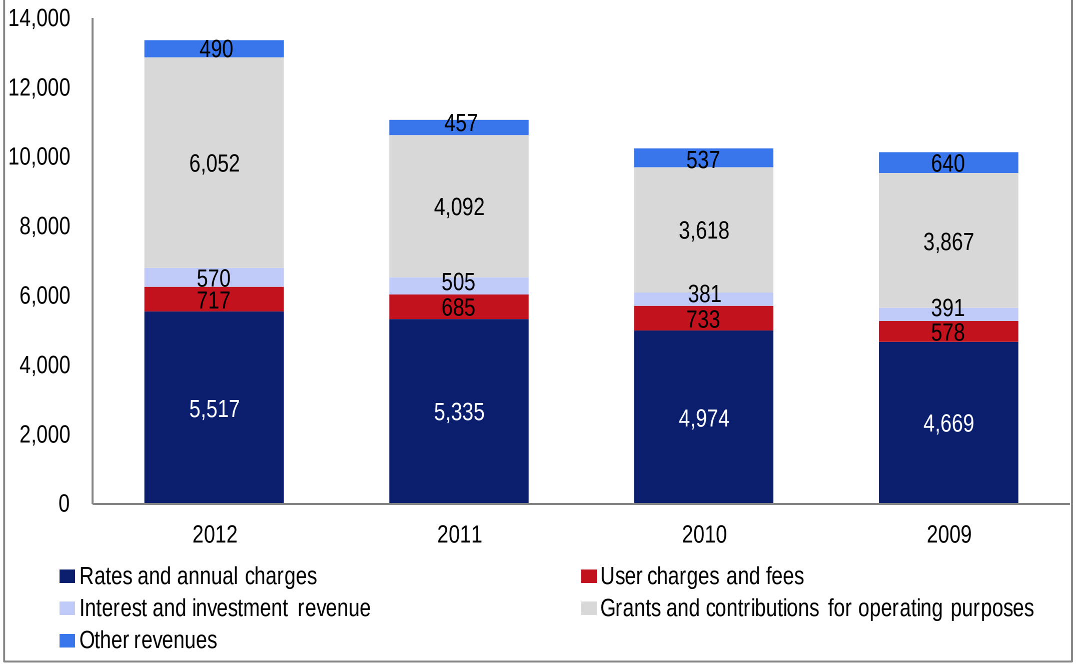
- $119.8m of roads, bridges and footpaths
- $6.5m of specialised buildings
- $1.7m of other structures
- $1.0m of stormwater drainage infrastructure

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

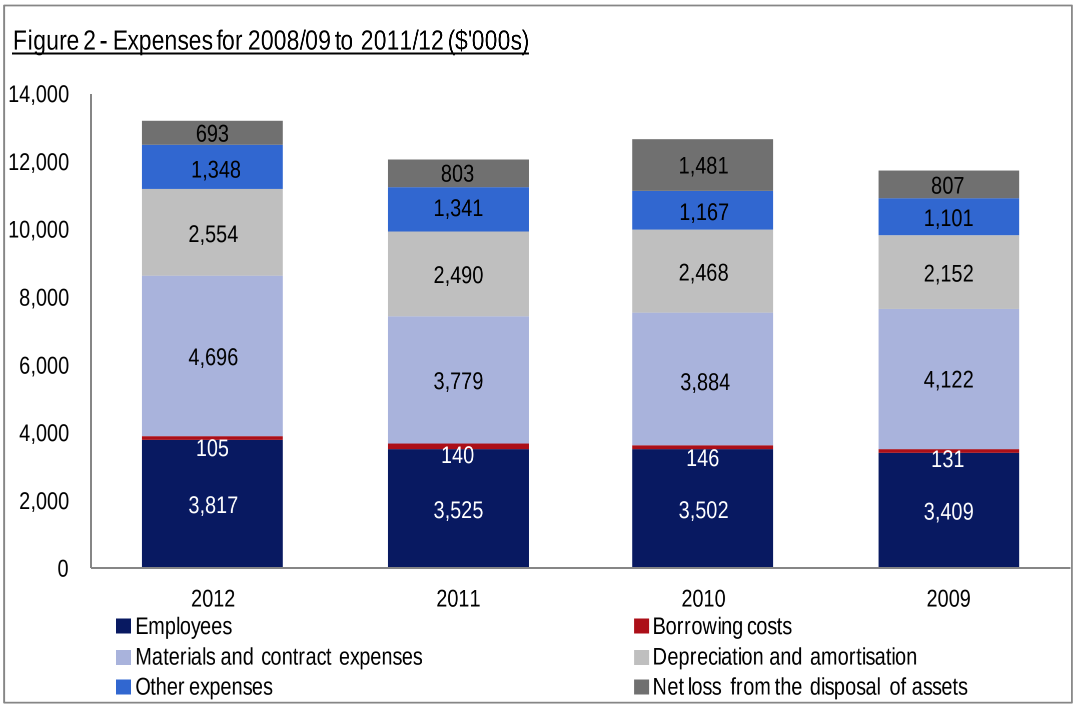
Figure 1 - Revenue Sources for 2008/09 to 2011/12 ($'000s)



Key Observations

- Total operating revenues have increased by $3.2m (31.6%) over the review period to $13.3m in 2012.
- Rates and annual charges have increased year on year at varying rates of between 3.4% p.a. and 7.3% p.a. The 3.4% increase in 2012 was in line with the rate peg while the 2011 increase of 7.3% was due to increased domestic waste annual charges while Council took up adjustment increases in its permissible general revenue of approximately $0.25m due to the 20% cap on farmland rates that had ministerial approval and a prior year catch-up that was applied.
- User charges and fees have increased over the period and represent 5.4% of the total operating revenues in 2012. Planning and building regulation fees of $0.2m was the largest category in 2012.
- Operating grants and contributions have fluctuated over the period but increased by 47.9% in 2012 due to the receipt of the first half of the 2013 Federal Government Financial Assistance Grant (FAG) that provided an additional $0.6m and increased transport/road grants and contributions of $1.0m related to a number of road maintenance programs.
- Other revenues have decreased over the period due to Council receiving road and bridges revenue in 2009 and 2010 but not in 2011 and 2012. These amounts were received following the resolution of contractual disputes over the quality of works done on the road network.

3.2: Expenses



Key Observations

- Total operating expenses have increased by $1.5m (12.7%) over the review period to $13.2m in 2012.
- Employee expenses have been on an upward trend with the highest annual increase in 2012 of 8.3%. This increase was due to an increase in salaries and wages impacted by the annual salary increments and additional overtime paid in order to complete grant funded maintenance.
- Materials and contracts costs were on a downward trend until 2012 when they increased by 24.3%. This increase was also linked to the completion of grant funded maintenance including flood damaged infrastructure works.
- Depreciation expenses have been on an upward trend with roads, bridges and footpath depreciation increasing marginally each year. Council is yet to complete their Asset Revaluation process therefore this is likely to impact this figure once the Revaluations are completed. Councils of a similar size have experienced increases in annual depreciation of between $0.3m and $2.0m over the review period.
- Other expenses have been on an upward trend with contributions to other levels of Government increasing including the waste levy and the NSW rural fire service levy.
- Council has recorded a loss from the disposal of assets in each year and this is included in our analysis as it has been projected to continue in Council's 10 year LTFP forecast. The losses have predominantly related to the disposal of infrastructure assets in each year when they have been replaced. Once the AMP is completed and integrated within the LTFP it is likely that these losses will reduce as the asset data will more accurately depict the depreciation expenses.

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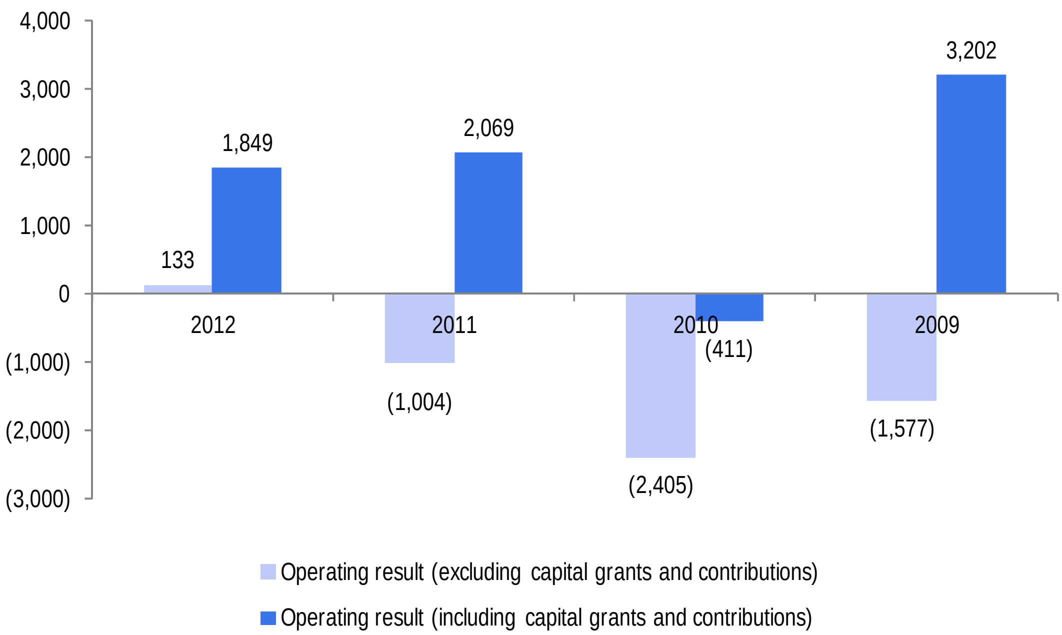
3.3: Operating Results

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 recorded operating deficits in each year up to 2012 when capital grants and contributions are excluded. The 2012 operating surplus has predominantly been achieved due to the receipt of the advance payment of the FAG. Each year has been impacted by the loss on disposal of infrastructure assets.
- Council's depreciation expense has not seen large variations as the Asset Revaluations process has not been completed at the present time. Once this process has been completed the depreciation expense is likely to impact Council's operating results.

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3.4: Financial Management Indicators

Performance Indicators	Year ended 30 June			
	2012	2011	2010	2009
EBITDA ($'000s)	2,792	1,626	209	706
Operating Ratio	1.0%	(9.1%)	(23.5%)	(15.5%)
Interest Cover Ratio	26.59x	11.61x	1.43x	5.39x
Debt Service Cover Ratio	12.19x	5.85x	0.71x	2.66x
Unrestricted Current Ratio	5.07x	4.67x	4.40x	3.74x
Own Source Operating Revenue Ratio	41.4%	42.6%	46.6%	35.2%
Cash Expense Ratio	10.4 months	11.3 months	8.5 months	9.9 months
Net assets ($'000s)	154,476	152,627	147,198	146,806

Key Observations

- Council's underlying operating performance, measured by EBITDA, has improved in the past two years after a low in 2010. The timing differences of the operating grants and contributions contributed to this improvement.
- The Operating Ratio has been below the negative 4% benchmark in each year until 2012 when the advance payment of the 2013 FAG created the surplus result.
- Council has had a varied DSCR and Interest Cover Ratio across the four years. The ratios were below their benchmarks in 2010 due to the low EBITDA but have increased above the respective benchmarks of 2.00x and 4.00x again in 2011 and 2012.
- Council's total borrowings are $1.3m in 2012. This equates to 0.8% of Net Assets.
- The Unrestricted Current Ratio has been above the 1.50x benchmark throughout the review period and has been on an upward trend as Council accumulates cash while it has not been able to complete capital works due to flood damage and a shortage of skilled employees.
- The Own Source Operating Revenue Ratio has been below the benchmark in each year, highlighting Council's reliance on grants and contributions to assist with meeting the costs of their operations.
- The Cash Expense Ratio has marginally increased over the period following varied results but has remained above the 3.0 month benchmark in each year.
- Net Assets have been on an upward trend over the period due to a revaluation of community land in 2011 that increased by $2.9m while there has been a $2.3m increase in the IPP&E asset base over the review period, compared to the written down value of disposed assets and depreciation.

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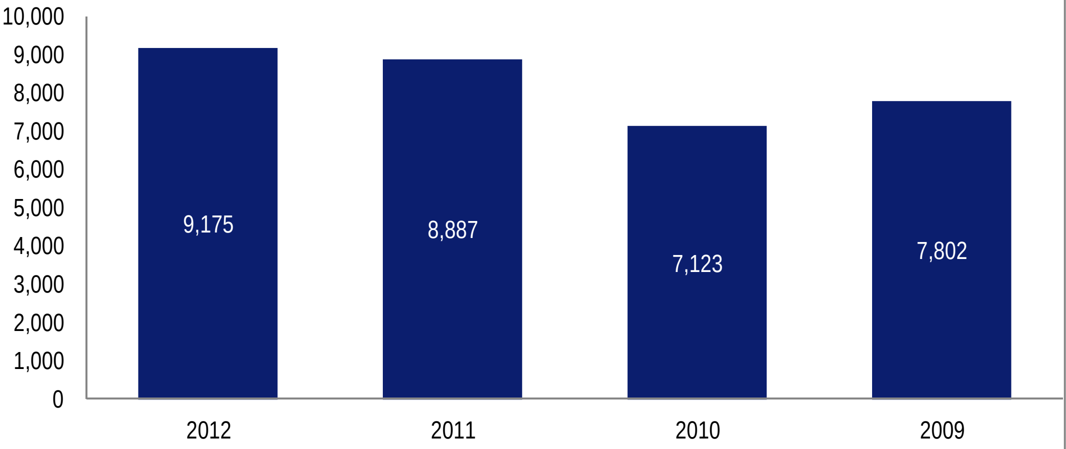
3.5: Statement of Cashflows

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



Key Observations

- Council's cash and cash equivalents have generally been on an upward trend over the period with the operating revenues higher than spending on investing and financing activities in both 2011 and 2012, mainly due to the advance receipt of the FAG.
- Of the $9.7m in cash and investments, $4.5m is externally restricted, $5.1m is internally restricted and $0.1m is unrestricted.
- Council has $0.5m classified as investments in 2012 that are FRNs or Negotiable Certificates of Deposit.
- The level of cash and cash equivalents along with the Unrestricted Current Ratio above the benchmark indicates Council has had sufficient liquidity for the size of its operations.

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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)

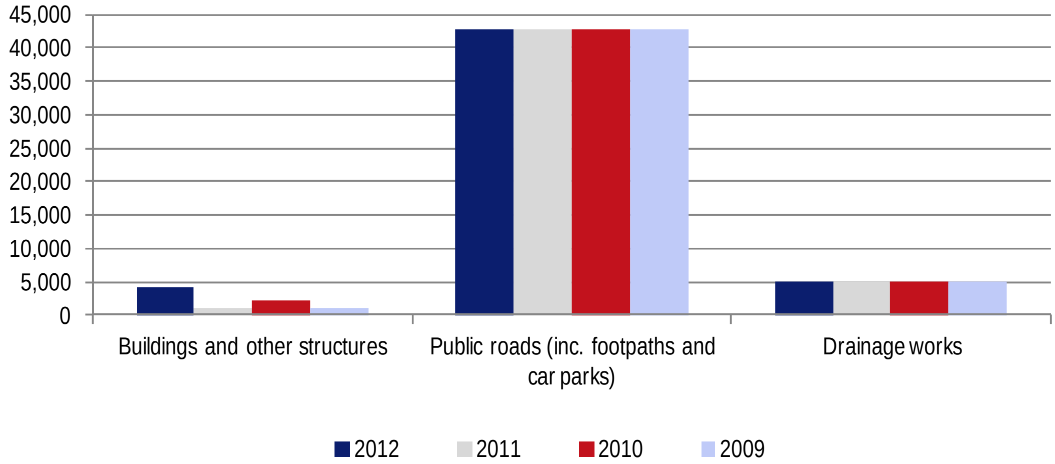
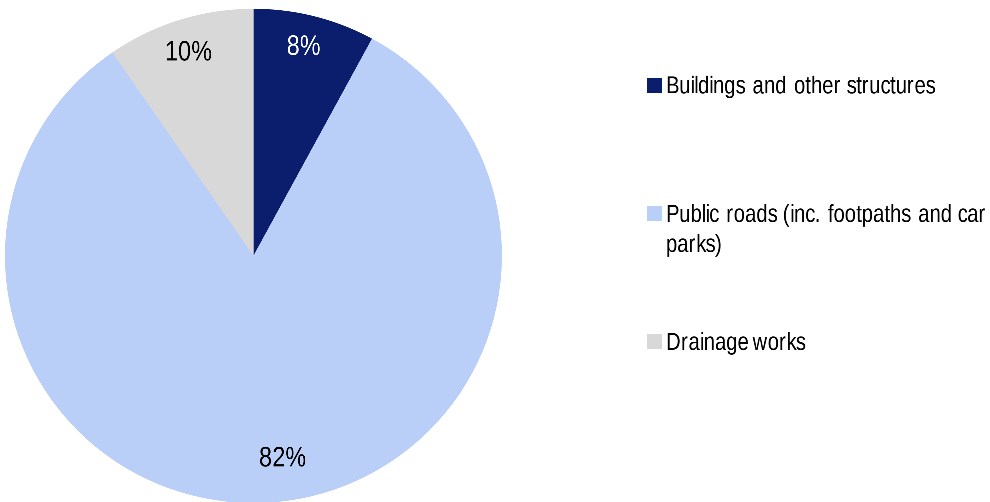


Figure 6 - Infrastructure Backlog Composition for 2011/12



Council's Infrastructure Backlog has increased over the period from $49.1m in 2009 to $51.9m in 2012. The increase has been due to an increase in the buildings and other structures backlog total. Public roads backlog is the largest category with a total of $42.7m.

The public roads and drainage works figures have remained identical in each year as the Asset Revaluations process has not been completed. This is because Council have lost suitably skilled engineering staff and have not been able to replace these employees over the past two years.

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New engineering employees have now been appointed and are building their skills base as they attempt to complete a draft version of the AMP.

3.6(b): Infrastructure Status

Infrastructure Status	Year ended 30 June			
	2012	2011	2010	2009
Bring to satisfactory standard ($'000s)	51,873	48,930	50,385	49,142
Required annual maintenance ($'000s)	2,251	2,151	2,194	2,022
Actual annual maintenance ($'000s)	2,442	2,017	2,103	2,205
Total value of infrastructure assets ($'000s)	129,036	128,190	128,819	129,474
Total assets ($'000s)	160,848	158,044	152,889	152,360
Building and Infrastructure Backlog Ratio	0.40x	0.38x	0.39x	0.38x
Asset Maintenance Ratio	1.08x	0.94x	0.96x	1.09x
Building and Infrastructure Renewals Ratio	0.84x	0.81x	1.21x	2.68x
Capital Expenditure Ratio	1.32x	1.25x	0.68x	1.75x

The Building and Infrastructure Backlog Ratio has remained at a high level in terms of the benchmark of 0.02x over the period. Based on the experience of other Council's once the Asset Revaluation process has been completed the ratio is likely to worsen.

The Asset Maintenance Ratio has remained relatively consistent over the period and close to the 1.00x benchmark highlighting Council has been adequately providing for maintaining the operating standard of their assets.

The Building and Infrastructure Renewals Ratio has been on a downward trend over the period but on average has been above the benchmark.

Council's Capital Expenditure Ratio, which takes into account assets which improve performance or capacity, has remained above the benchmark in every year apart from 2010. This indicates Council has expanded their Net Assets over the period as confirmed in Section 3.4.

Given that Council has not completed its Asset Revaluations, historical depreciation expense is likely to be lower than what it should be. This positively skews the Building and Infrastructure Renewals Ratio and Capital Expenditure Ratio.

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			
	2012	2011	2010	2009
New capital works	611	0	0	1,000
Replacement/refurbishment of existing assets	2,600	5,000	4,000	5,000
Total	3,211	5,000	4,000	6,000

During 2011 and 2012 Council's capital works program included:

- $4.9m spent on roads and bridge infrastructure works
- $0.4m spent on other structures, including sporting grounds, public halls, parks and aged care

3.7: Specific Risks to Council

- Asset Revaluations. As Council has not completed this process, nor completed its AMPs, there is a high level of uncertainty regarding the financial position of Council. Once the AMPs are completed and integrated into the LTFP a more accurate picture will be available of the potential funding gap facing Council in respect of its operations and infrastructure.
- Inability to reduce the Infrastructure Backlog. Historically, Council has been unable to meet the ongoing renewal costs relating to their infrastructure assets. For example the renewal cost for 46 of Council's timber bridges is approximately $30m against an annual turnover of $13.3m. Council also received a number of regional roads to maintain when the State Government reclassified the road network with no roads within the LGA now being classified as state roads. Council continues to try and maximise available grant funding to assist this funding shortfall but this is not enough to enable sufficient funds to be allocated.
- Inability to attract suitably qualified employees. This is highlighted by Council's ongoing issue of appointing engineering staff to complete the overdue AMP. In this particular instance there have been gaps in the engineering team since 2008 despite Council offering higher salaries than neighbouring councils and also offering flexible working hours. The understaffing is leading to efficiency issues with Council not having enough employees to adequately complete the required tasks and responsibilities.
- Limited alternative revenue streams. Council has a small property portfolio and also a small fleet of plant and equipment to generate significant revenues from private works. Along with Gloucester Shire Council, Council is the only LGA without State roads within their boundaries which also limits private and RMS works revenues. This leads Council to have to rely on rates revenue, and grants and contributions.
- Potential impact of the Lower Hunter Water Plan. The proposed Tillegra Dam within the LGA placed significant pressure on Council as they were part of negotiations that ultimately resulted in the dam being rejected in November 2010. A large number of hours were spent in these negotiations and if the updated Lower Hunter Water Plan contains an alternative dam

proposal within the LGA then this would again place a strain on Council's resources and may lead to a further loss of employees.

- Environmental disasters. Council has previously been affected by flooding and was classified as a Natural Disaster area in 2011. Similar to other rural councils impacted by floods, Council receives grant funding to assist with the rehabilitation of infrastructure assets damaged during flooding however these grants do not cover the total cost of the damage with Council's maintenance costs ultimately increasing. The floods also impact the capital works program with scheduled projects having to be delayed.

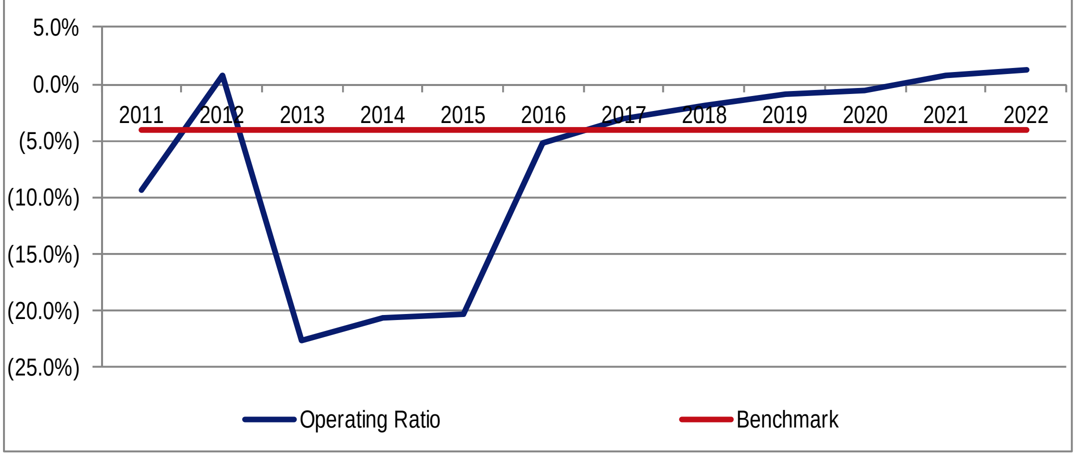
Section 4 Review of Financial Forecasts

The financial forecast model shows the projected financial statements and assumptions for the next 10 years. Council only operate a General Fund although during the review period they had small ongoing operations relating to the Water and Sewer Funds that were transferred to Hunter Water in 2008. These are expected to be wound up upon the finalisation of the Transfer Agreement in the next couple of years with Council due to receive a $0.75m compensation settlement when all conditions of the Transfer Agreement have been met.

As the AMP is yet to be completed, Council's LTFP document has not been completed in full and TCorp has only received the underlying assumptions for the 10 year forecast. Council will complete a fully integrated LTFP once the AMP has been completed and this document will include scenario analysis and KPIs. The scenarios and KPIs have not been completed at the present time due to the incomplete nature of Council's data.

4.1: Operating Results

Figure 7- Operating Ratio for General Fund



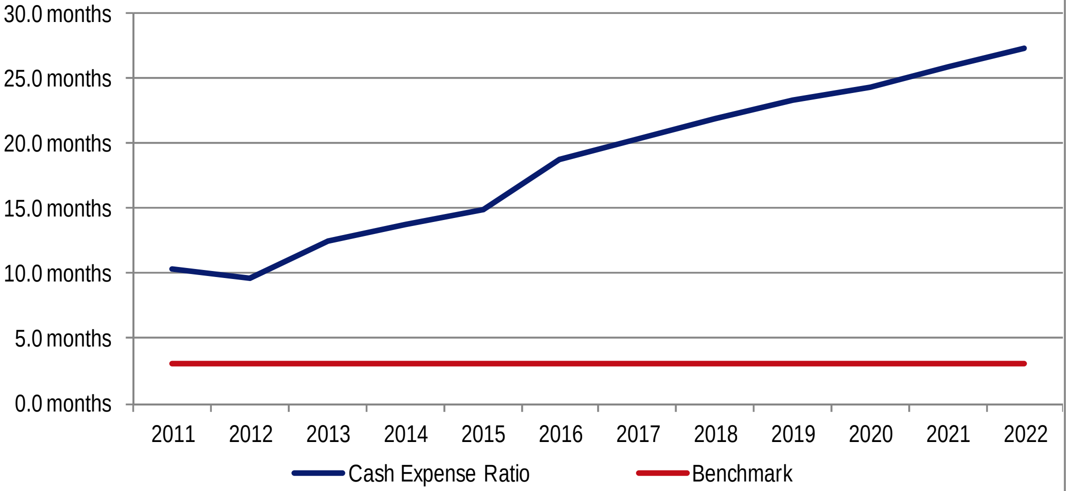
Council has projected that operating deficits will be posted in eight of the 10 years with the three largest deficits to be experienced in 2013 to 2015, with the Operating Ratio forecast to be at a deficit of 22.6% in 2013 . The large difference in these years is a higher forecast loss on the disposal of road assets that has been modelled on historic actual data linked to capital grant funding that will replace road assets. The 2013 decrease is also impacted by lower projected operating grants and contributions, partly due to no prepayment of the FAG.

The Operating Ratio is projected to improve in 2016 as the annual loss from the disposal of assets reduces from $2.4m in 2015 to $0.6m in 2016. The ratio is then projected to improve to a small surplus by 2021 with a 1.3% surplus Operating Ratio in 2022. The marginal annual improvement from 2016 to 2022 is linked to revenues increasing above expenses as depreciation is forecast to marginally decrease in each year, while the value of IPP&E assets is forecast to decrease by $7.6m over the period.

4.2: Financial Management Indicators

Liquidity Ratios

Figure 8 - Cash Expense Ratio for General Fund

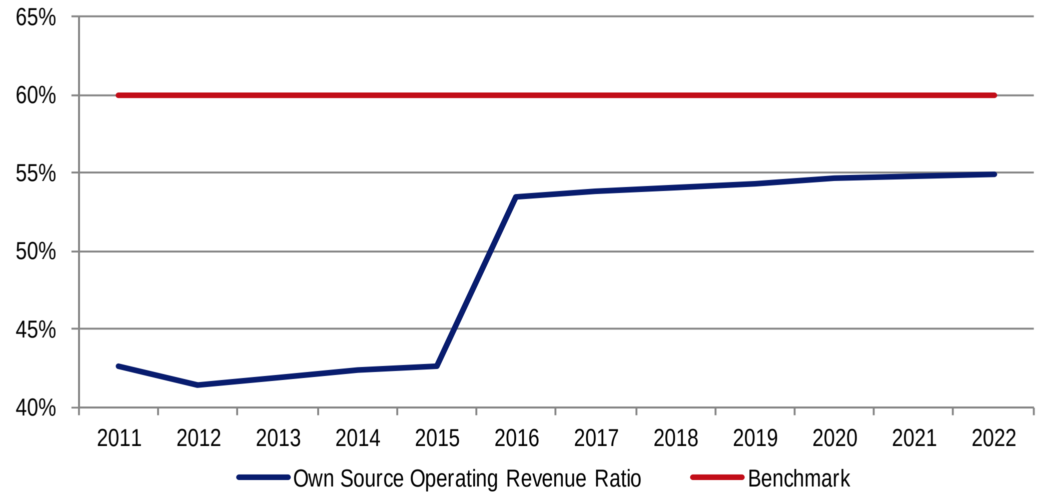


Council has projected that the Cash Expense Ratio will increase from the 2012 position as Council is not forecasting to spend adequate funds on capital expenditure as indicated in Section 4.3.

Council has not calculated a forecast Unrestricted Current Ratio as they propose to complete this once the AMP is integrated into the LTFP.

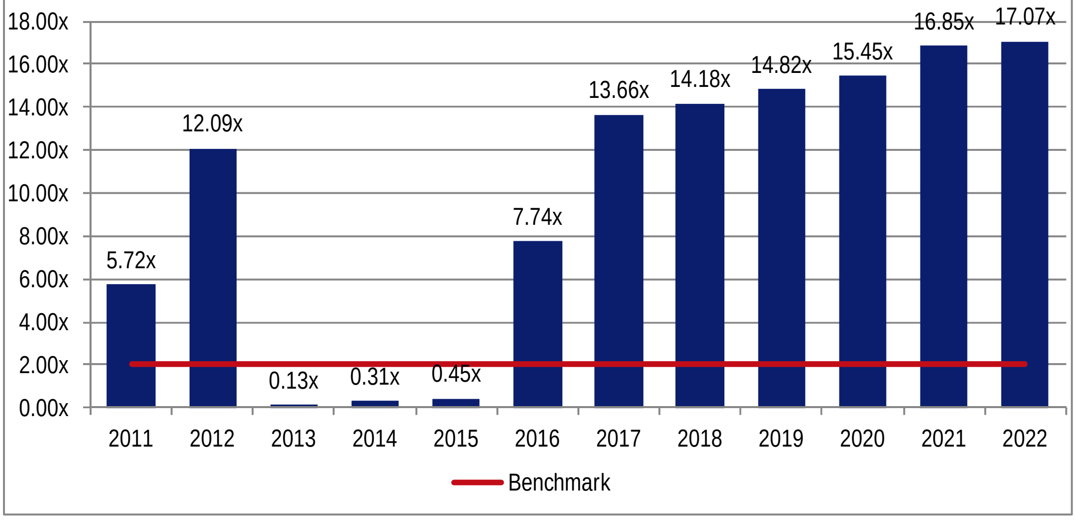
Fiscal Flexibility Ratios

Figure 9 - Own Source Operating Revenue Ratio for General Fund



Council's Own Source Operating Revenue Ratio remains at similar levels to the historical figures between 2013 – 2015 due to the capital grants and contributions being known and included in the forecast. The capital grants and contributions reduced from $4.1m in 2015 to $0.8m in 2016, a level that they are projected to remain at for the remaining years of the forecast. This is the reason for the ratio being skewed upwards from 2016 to 2022.

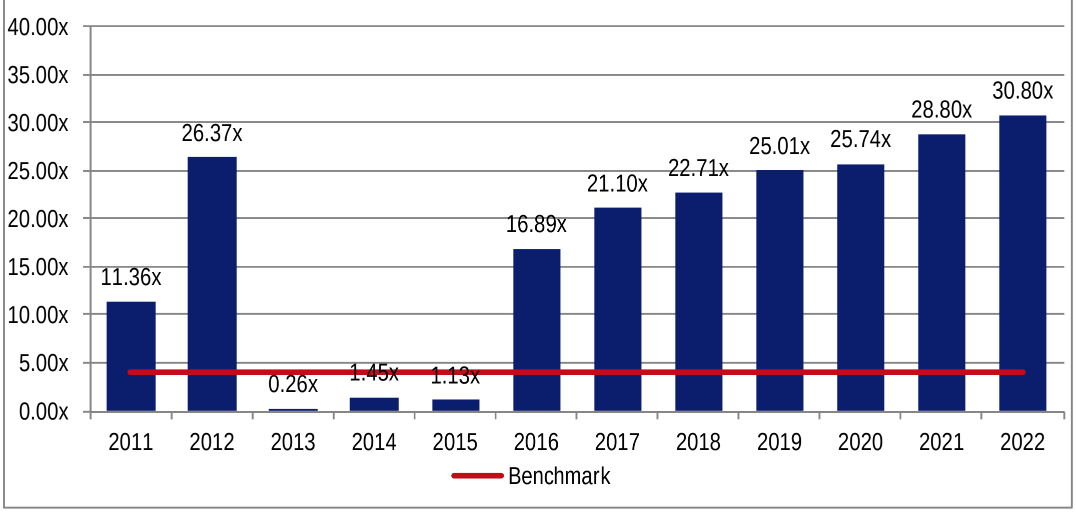
Figure 10 - DSCR for General Fund



The DSCR is projected to decrease below the 2.00x benchmark in the three years when the large net losses from the disposal of assets are forecast. These are book losses therefore Council is projecting a positive cash position to meet the annual repayments of existing borrowings without impacting the accumulated cash and cash equivalents total.

The DSCR increases back above the benchmark as the EBITDA improves as the losses from disposal from assets decrease. The improving position occurs as Council repays their borrowings while they are not projected to utilise new borrowings during the forecast period.

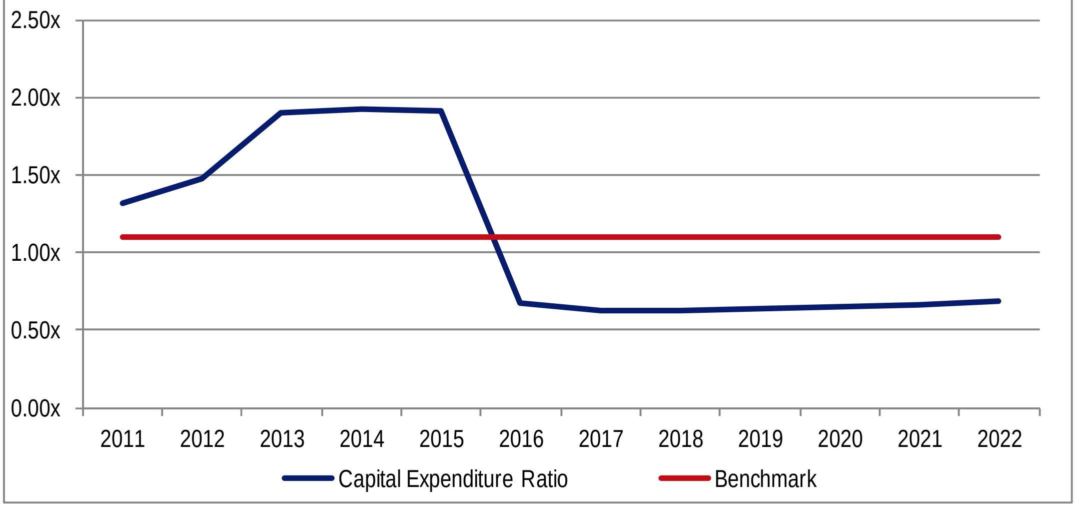
Figure 11 - Interest Cover Ratio for General Fund



The Interest Cover Ratio follows an almost identical pattern to the DSCR with the net losses from the disposal of assets reducing the ratio below the 4.00x benchmark in the same three years at the beginning of the forecast.

4.3: Capital Expenditure

Figure 12 - Capital Expenditure Ratio for General Fund



The forecast Capital Expenditure Ratio is forecast to increase and remain above the 1.10x benchmark in the three years from 2013 to 2015 however these capital works are almost entirely funded from the capital grants that Council will receive including a $13m grant from the State Government for the road between Dungog and Raymond Terrace that Council will receive across these three years.

The ratio decreases below the benchmark from 2016 onwards as Council's capital expenditure reduces in line with the projected capital grants of $0.8m p.a. This highlights that Council relies on the provision of capital grants and contributions to undertake required capital works.

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>

- Existing service levels have been maintained within the LTFP forecast, with scenarios to be added in future versions.
- Rates and annual charges are forecast to increase between 2.9% and 3.6% p.a.
- User charges and fees are forecast to increase between 4.9% and 5.6% p.a. until 2020 and remain static thereafter.
- Interest and investment revenues are forecast to reduce to $0.3m in 2014 and remain at this level thereafter. This does not correlate with the forecast increase in cash and cash equivalents.
- Operating grants and contributions have been forecast at levels below all four review years but are forecast to increase from $2.9m in 2013 to $3.7m in 2022.
- Total employee costs are forecast to increase by 2.9% p.a. with the annual pay award increase within this total at 3.2% p.a. The 2013 total is 4.4% below the 2012 actual figure as 2012 included one-off costs from additional maintenance works.
- Materials and contracts costs are forecast to increase by 3.2% p.a. but the 2013 total is 12.2% below the 2012 actual figure again due to the one-off costs from additional maintenance works.
- Depreciation is based on historic figures due to the Asset Revaluations not yet being complete. It is forecast to remain static until 2015 after which it decreases between 1.7% and 2.4% p.a.
- Other expenses are forecast to increase between 4.4% and 5.7% p.a. mainly due to electricity increases of 16% p.a. and street lighting increases of 14% p.a.
- CPI has been applied in all years at 3% p.a. for all other revenue and expense categories.
- The majority of Council's assumptions appear reasonable however the increasing cash and cash equivalents and reducing forecast capital expenditure should be reviewed, while the reduced operating grants and contributions and depreciation based on historic figures may not be entirely accurate.

4.5: Borrowing Capacity

When analysing the financial capacity of the Council we believe Council should not undertake any additional loan funding in addition to its existing debt facilities. Once Council has completed their AMP, revalued their infrastructure assets to fair value, and integrated this information into its LTFP, Council's capacity to borrow could be re-visited.

4.6: Sustainability

Council has a history of reporting operating deficits when capital grants and contributions are excluded and the prepayment of the 2013 FAG has favourably impacted the 2012 results. Council does have adequate liquidity and a low level of borrowings. The operating deficits have also been impacted by the net losses from the disposal of road assets upon their replacement.

It is difficult to analyse Council's Sustainability in the medium or long term until Council complete their Asset Revaluation process, finalise their AMP and update the LTFP. This process will allow the accurate expenses related to asset maintenance, renewals and expenditure to be recognised.

Reviewing the impact that the Asset Revaluations process has had on other similar sized councils, it is likely that Council will be unsustainable with depreciation expenses likely to increase after the Asset Revaluation and it will further impact the negative outlook of the LTFP. Council is unlikely to be able to fund future asset renewals and subsequently the Infrastructure Backlog will increase. The ongoing required maintenance costs may also increase putting further pressure on Council funds. One positive is that Council may be in a position to amend the accounting of the losses from the disposal of infrastructure assets that have negatively impacted the historic operating result each year, although this may also result in increased annual depreciation expense.

Council has confirmed they do not have the necessary revenue raising options to meet the maintenance and renewal funding costs of their road and bridge infrastructure network going forward and the problems of employing suitable engineering employees is also impacting this issue.

Therefore, in considering the longer term financial Sustainability of the Council we make the following comments:

- Council's long term Sustainability is dependent on Council being able to increase revenues in order to create operating surpluses'. Council has very limited options in this regard with no commercial focussed assets or State roads within the LGA to raise additional revenues
- It is therefore important that Council control its operating expenses with Council's restricted ability to raise its revenue. Council is unlikely to be Sustainable if employee expenses increase each year at the 2012 level of 8.3%
- One option to assist Council revenues is to investigate the possibility of applying for an SRV that would assist in raising rates revenue to meet ongoing asset maintenance and renewals expenses. However, this is likely to have limited impact given the relatively small population within the LGA

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- Council is dependent on State and Federal grants for both operating and capital purposes. Any material adverse change to the levels of grants receivable would severely weaken Council's position
- With Council unable to achieve a break-even operating position at current service levels it is likely that it will become unsustainable and Council will have to review service levels

Section 5 Benchmarking and Comparisons with Other Councils

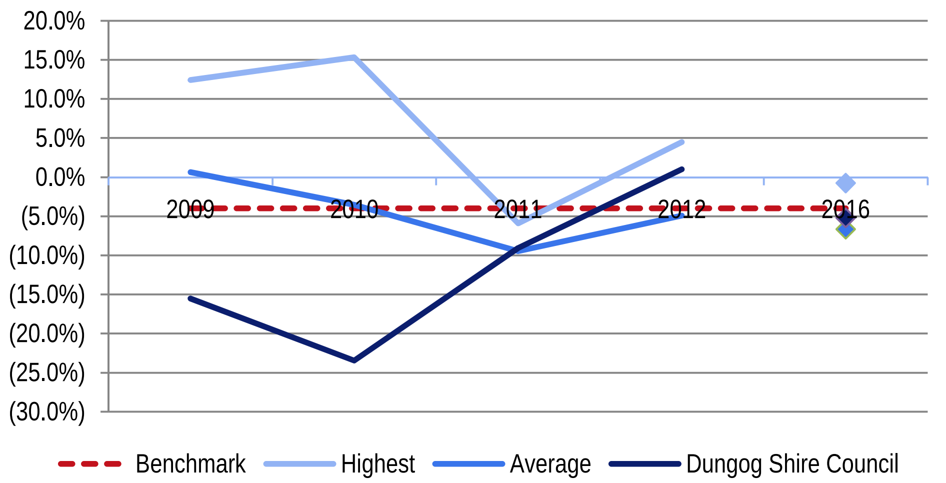
Each council's performance has been assessed against ten key benchmark ratios. The benchmarking assessment has been conducted on a consolidated basis for councils operating more than one fund. This section of the report compares the Council's performance with its peers in the same DLG Group. The Council 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 13 to Figure 19, 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 20 to 22 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. For the Interest Cover Ratio and Debt Service Cover Ratio, we have excluded from the calculations, councils with very high ratios which are a result of low debt levels that skew the ratios.

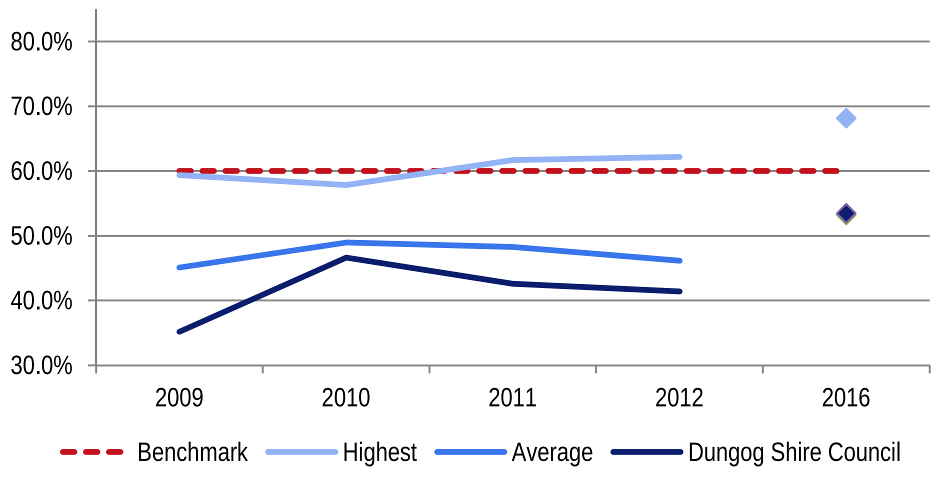
Financial Flexibility

Figure 13 - Operating Ratio Comparison



Council's Operating Ratio was below average until 2011 and the benchmark until 2012. Council has a much improved ratio from 2010 due to lower losses from the disposal of assets and the FAG prepayment that saw the 2012 result increase above the group average and benchmark. The forecast result is projected to return to a level below the benchmark but remain above the group average.

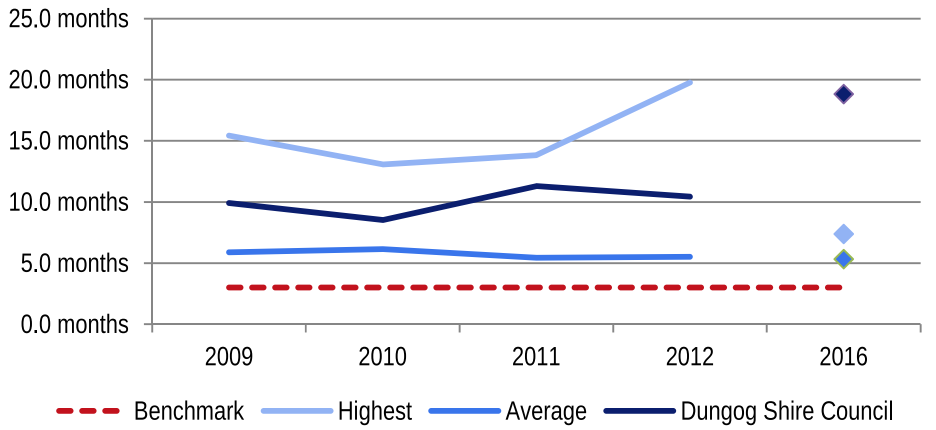
Figure 14 - Own Source Operating Revenue Ratio Comparison



Council's Own Source Operating Revenue Ratio has been below the group average and benchmark in each year, indicating their reliance on grants and contributions to boost their revenue base. The forecast is projected to improve to a level in line with the group average due to the reduced capital grants forecast.

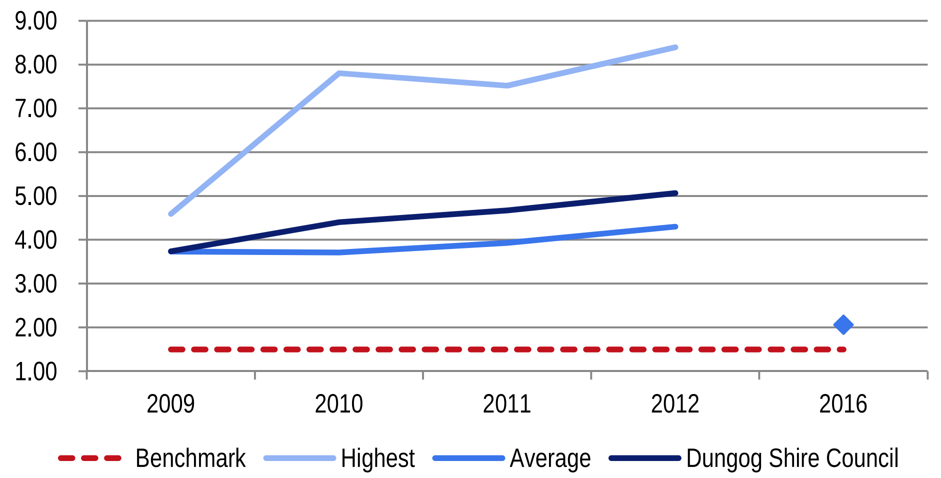
Liquidity

Figure 15 - Cash Expense Ratio Comparison



Council's Cash Expense Ratio has been above the benchmark and group average in each year and is forecast to remain that way. Council holds the majority of their funds in cash and cash equivalents rather than investments and this is part of the reason of the strong ratio results.

Figure 16 - Unrestricted Current Ratio Comparison



Council's Unrestricted Current Ratio has been above the benchmark and group average in each year. Council's LTFP does not currently project this ratio therefore there is no 2016 ratio.

Debt Servicing

Figure 17- Debt Service Cover Ratio Comparison

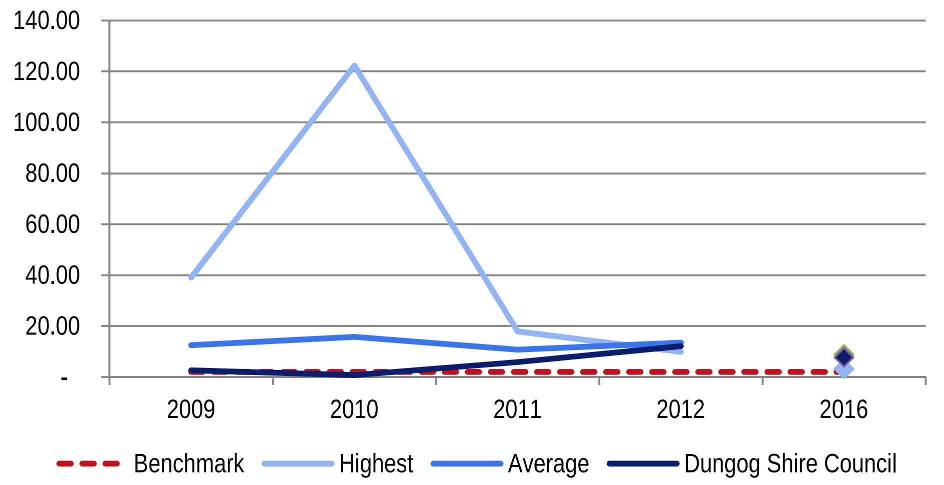
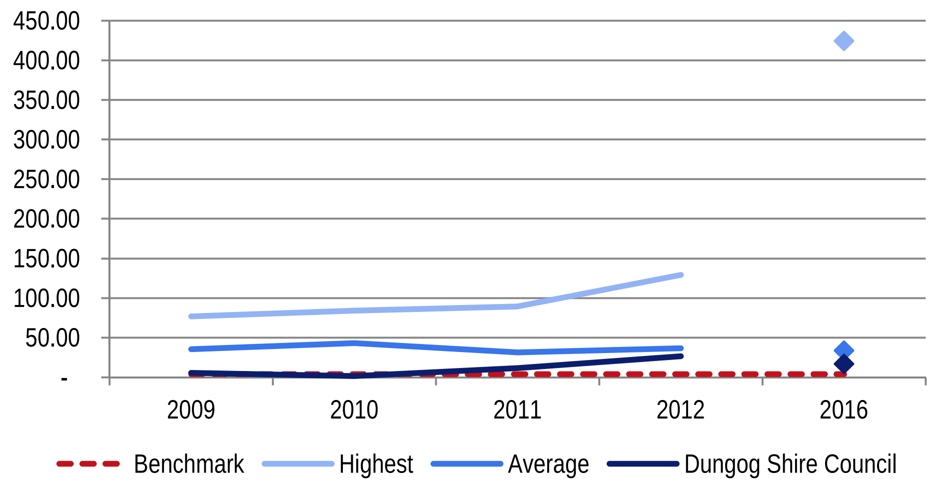


Figure 18 - Interest Cover Ratio Comparison



Council had a below group average DSCR and Interest Cover Ratio but was above the benchmark in each year apart from 2010. This indicates that proportionally Council had less capacity than its peers to utilise further borrowings and this is forecast to remain the position in 2016.

Asset Renewal and Capital Works

Figure 19 - Capital Expenditure Ratio Comparison

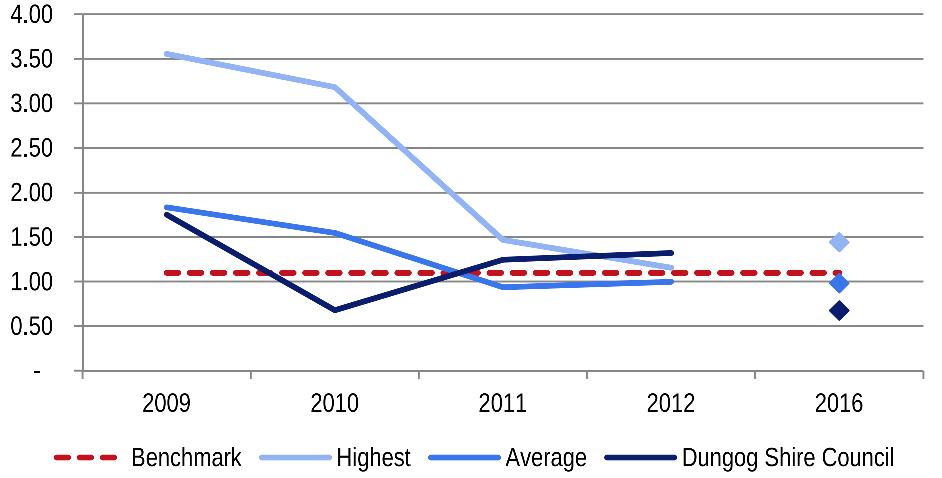


Figure 20 - Asset Maintenance Ratio Comparison

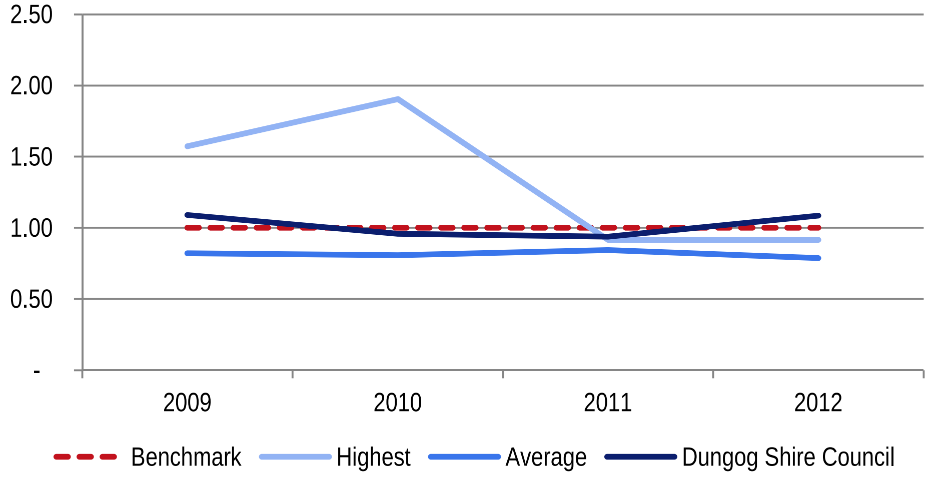


Figure 21 - Infrastructure Backlog Ratio Comparison

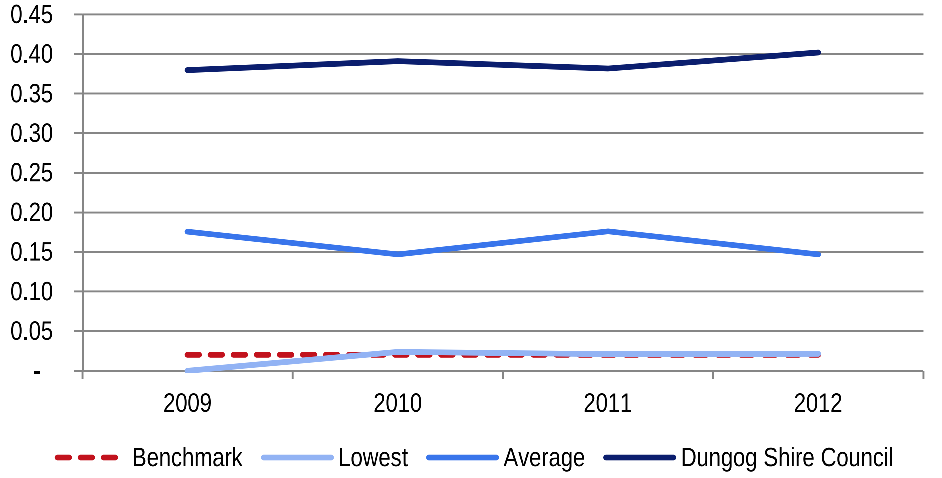
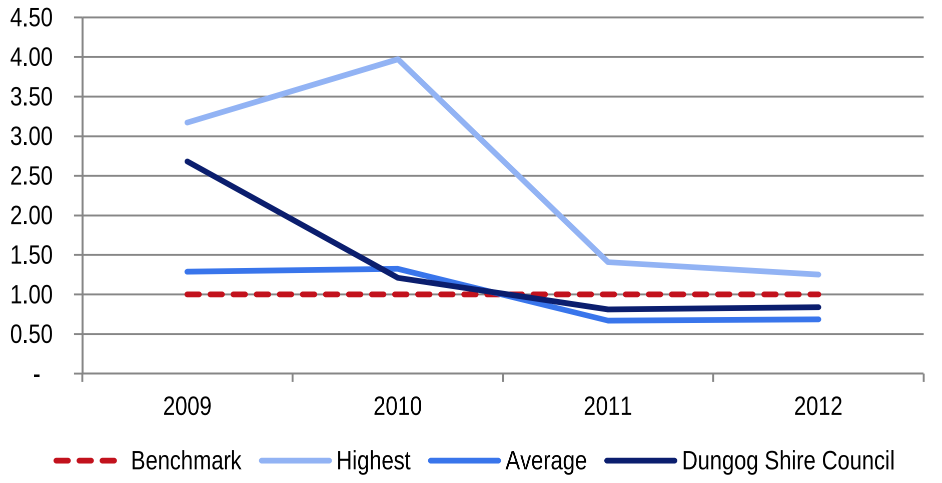


Figure 22 - Building and Infrastructure Asset Renewal Ratio



Council's Capital Expenditure Ratio has been above the benchmark in three of the four review years and has been above the group average in the past two years but is forecast to decrease below both indicators in 2016.

Council has been around the benchmark on asset maintenance spending and above the group average in each year. Council was also a better performer than the highest average performer in both 2011 and 2012.

In relative terms, Council has a larger Infrastructure Backlog when compared to the group average and is significantly above the benchmark in each year.

Council's Building and Infrastructure Asset Renewal Ratio has decreased below the benchmark in 2011 however it remained above the group average in 2011 and 2012. The group average being below the benchmark indicates the limited capacity of councils within this group to adequately spend on asset renewals.

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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 we consider Council's short term financial position to be satisfactory.

It is difficult to assess the medium to long term position until all the IP&R documentation has been completed and all up to date data is integrated within the AMP & LTFP. However, based on our experiences with other councils it is likely that the Asset Revaluations process, completion of AMPs and their integration into the LTFP will detrimentally impact Council's long term Sustainability.

We base our recommendation on the following key points:

- IPP&E values will most probably increase following the Asset Revaluations, inflating annual depreciation, which will impact Council's financial position
- The inability to fund the cost of asset renewals will increase the Infrastructure Backlog, potentially leading to lower quality assets and impact service levels

We would also recommend that the following points be considered:

- The update of the AMP may result in the reduction of the losses on disposal of infrastructure assets when they are replaced. This will positively impact the operating results against the current LTFP, although it could result in offsetting increased depreciation expense
- In a minority of cases the Asset Revaluations process has decreased a council's depreciation expense and Infrastructure Backlog, providing a positive outlook to a council's LTFP forecast. This means that the completion of Council's AMP may not necessarily increase its depreciation expense

New South Wales Treasury Corporation

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	5,517	5,335	4,974	4,669	3.4%	7.3%	6.5%
User charges and fees	717	685	733	578	4.7%	(6.5%)	26.8%
Interest and investment revenue	570	505	381	391	12.9%	32.5%	(2.6%)
Grants and contributions for operating purposes	6,052	4,092	3,618	3,867	47.9%	13.1%	(6.4%)
Other revenues	490	457	537	640	7.2%	(14.9%)	(16.1%)
Total revenue	13,346	11,074	10,243	10,145	20.5%	8.1%	1.0%
Expenses							
Employees	3,817	3,525	3,502	3,409	8.3%	0.7%	2.7%
Borrowing costs	105	140	146	131	(25.0%)	(4.1%)	11.5%
Materials and contract expenses	4,696	3,779	3,884	4,122	24.3%	(2.7%)	(5.8%)
Depreciation and amortisation	2,554	2,490	2,468	2,152	2.6%	0.9%	14.7%
Other expenses	1,348	1,341	1,167	1,101	0.5%	14.9%	6.0%
Net losses from the disposal of assets	693	803	1,481	807	(13.7%)	(45.8%)	83.5%
Total expenses	13,213	12,078	12,648	11,722	9.4%	(4.5%)	7.9%
Operating result	133	(1,004)	(2,405)	(1,577)	113.2%	58.3%	(52.5%)

Table 2 - Items excluded from Income Statement

Excluded items ($'000s)				
	2012	2011	2010	2009
Grants and contributions for capital purposes	1,716	3,073	1,994	4,779
Divestment of water and sewer operations	0	0	0	319

New South Wales Treasury Corporation

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	9,175	8,887	7,123	7,802	3.2%	24.8%	(8.7%)
Investments	500	500	500	500	0.0%	0.0%	0.0%
Receivables	2,449	1,386	1,820	1,080	76.7%	(23.8%)	68.5%
Inventories	1,549	997	955	490	55.4%	4.4%	94.9%
Other	219	217	0	0	0.9%	N/A	N/A
Total current assets	13,892	11,987	10,398	9,872	15.9%	15.3%	5.3%
Non-current assets							
Receivables	75	5	10	16	1400.0%	(50.0%)	(37.5%)
Inventories	22	18	18	18	22.2%	0.0%	0.0%
Infrastructure, property, plant & equipment	146,833	146,014	142,463	142,454	0.6%	2.5%	0.0%
Equity accounted investments	26	20	0	0	30.0%	N/A	N/A
Total non-current assets	146,956	146,057	142,491	142,488	0.6%	2.5%	0.0%
Total assets	160,848	158,044	152,889	152,360	1.8%	3.4%	0.3%
Current liabilities							
Payables	1,360	1,324	1,277	1,396	2.7%	3.7%	(8.5%)
Borrowings	129	116	133	134	11.2%	(12.8%)	(0.7%)
Provisions	1,607	1,527	1,448	1,404	5.2%	5.5%	3.1%
Total current liabilities	3,096	2,967	2,858	2,934	4.3%	3.8%	(2.6%)
Non-current liabilities							
Payables	98	99	100	50	(1.0%)	(1.0%)	100.0%
Borrowings	1,140	1,269	1,380	1,257	(10.2%)	(8.0%)	9.8%
Provisions	2,038	1,082	1,353	1,313	88.4%	(20.0%)	3.0%
Total non-current liabilities	3,276	2,450	2,833	2,620	33.7%	(13.5%)	8.1%
Total liabilities	6,372	5,417	5,691	5,554	17.6%	(4.8%)	2.5%
Net assets	154,476	152,627	147,198	146,806	1.2%	3.7%	0.3%

Table 4-Cashflow

Cashflow Statement ($'000s)	Year ended 30 June			
	2012	2011	2010	2009
Cashflows from operating activities	4,663	5,127	2,781	5,657
Cashflows from investing activities	(4,259)	(3,234)	(3,582)	(5,577)
Proceeds from borrowings and advances	8	9	270	0
Repayment of borrowings and advances	(124)	(138)	(148)	(134)
Cashflows from financing activities	(116)	(129)	122	(134)
Net increase/(decrease) in cash and equivalents	288	1,764	(679)	(54)
Cash and equivalents	9,175	8,887	7,123	7,802

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.

New South Wales Treasury Corporation

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.