Integrated Strategic Financial Analysis (ISFA) - 10 Year (2012/13 to 2021/22)

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Executive Summary

Revenues are being exceeded by costs as Councils across Australia are required to do more with their funds. In NSW, Councils have had their major source of revenue, rates, capped by the State Government. In 1993 the NSW Local Government Act was changed and required Councils to increase the range of Services provided without a mechanism to raise the funds to deliver these services. As a result Councils spent more of their funds on Services and less on property and assets.

The City of Newcastle (TCoN) has suffered from these pressures along with many other NSW Councils that are struggling with financial sustainability. In addition, the Newcastle LGA has a large number of assets to support these services.

Financial Sustainability

Continuing financial sustainability is a key issue facing all NSW local government councils arising from:

- Limits on Increasing rates (rate cap)
- An ageing infrastructure network
- A large numbers of assets
- Increased costs of materials and services
- Cost shifting from other levels of government and
- The service delivery expectations of the wider community.

FiscalStar in a 2009 Local Government Review defined sustainability as:

"Maintaining an investment grade credit rating through achieving three primary goals:

1. A minimum 2.5% budget surplus ratio, so that future ratepayers are not left with excessive share of the cost of capital
2. A maximum 60% Net debt and other financial liabilities to total operating revenue ration s that debt charges remain affordable, and
3. A maximum 2% unsatisfactory infrastructure, unsafe or unsightly."

Secondary goals were:

1. More revenue through own sources than through Government grants
2. Keeping operating expenditure growth less than revenue growth making extra infrastructure renewal monies available for backlogs
3. Having a modest physical asset base.
4. Keeping rates to no more than between 1 and 1.66 times CPI each year and unsustainable was more than 2 times or more than the CPI

Applying its benchmarks FiscalStar found that **37 of the 99 largest Councils needed to increase rates, fees and charges by 80% and 300% over the next 10 years. Of the 99 Councils surveyed in 2009, 37 were unsustainable and a further 16 vulnerable** totalling 53% which were not in the healthy sustainable range.

Of the 18 regional coastal Councils, 12 were unsustainable.

In recent years, TCoN has undertaken extensive Sustainability and Services Reviews to identify possible service rationalisation, cost reduction and sources of additional revenue. As a result, annual Operational Plans have integrated these approved Sustainability Review strategies and savings have been realised. This however has not been enough to provide a sustainable future.

Financial Sustainability - Causes

NSW has suffered rate revenue decline due to rate capping, compared to other Australian states. This helps to account for why so many councils are now unsustainable.

Traditionally, land rates were the main source of revenue for Local Government, however rate capping has severely constrained the rate of growth of this income source. FiscalStar found many councils had a heavy reliance on Government Grants, little spare cash, expenses growing in excess of underlying costs, and insufficient capital works spending to renew ageing assets.

In addition, specific purpose grants from the State Government have fallen as a proportion of Local government revenue from 14.8% in 1974/1975 to only 7.1% in 1997/1998.

The most recently published LGSA survey undertaken for the 2008/2009 financial year shows the total amount of cost shifting for The City of Newcastle as $13,267,099. This represents 7.16% of the total income from operations before capital amounts. This is higher than the average for other urban regional councils (5.44%) and all other NSW council's (5.72%).

Financial Sustainability - Effects

In November 2006 a PricewaterhouseCoopers study revealed **NSW had a backlog of infrastructure renewals of $6.3 billion compared with $0.8 billion in Victoria** and **the under spend per annum was $500 million compared with $81 million in Victoria**. Funding for infrastructure maintenance and renewal has been described as the "**biggest management challenge in Local Government"** (Allan 2006, enquiry into financial sustainability of NSW Local Government).

Analysis of local government in Australia shows that rate income has decreased from 54.1% to 47.2% of total revenue sources from 1974/1975 to 1997/1998 and was only 38.7% in 2009/2010.

For TCoN, the total operating position is declining under the Long Term Financial Plan model. Expenditures are rapidly outstripping operating revenues.

It is evident that the underlying operating position is progressively deteriorating to a point in 2021 when it goes into a negative number. This positional change is approximately $34.7 million over 10 years.

What are the objectives of this plan?

The key objective of this plan is to provide mechanisms which, when combined, can reverse this negative financial position. The Integrated Strategic Financial Analysis (ISFA) will guide the Long Term Financial Plan through:

- Provision of worked options to enable strategic decision making by Council
- Identifying financial and strategic opportunities
- Providing transparency in forecasting Council's financial position
- Analysing the cumulative financial impacts of Council's current plans and policies including implementation of Councils resolutions
- Maintaining a balanced or surplus annual operating budget
- Maintaining a strong cash and liquidity position
- Maintaining adequate cash reserves in accordance with legislation or Policy requirements
- Ensuring robustness of appropriate cost recovery strategies through full pricing and recognition of the true cost of provision of services when setting revenue targets
- Ensuring Council is within industry recognised Financial Health Check indicators
- Ensuring asset renewal and maintenance remain within the sustainable range and
- Identifying current asset holdings and opportunities for rationalisation to assist in addressing Council's maintenance backlog.

The Sustainability Options

This plan explores various options. Each of these options set to achieve long term financial viability for Council including expenditure reductions and increases in revenues. Everything from reductions in employee costs through to savings in services are analysed as well as mechanisms for increasing revenues. A recommendation is offered which includes a combination of expenditure reduction and revenue improvements. If adopted, this will bring Council back into a 2.5% surplus position by 2015.

The sustainability issues facing council are not insurmountable but will require strong support, good governance and financial control.

1. Background

The National Context

There are 565 Local Governments in Australia and this is small by world standards with rates (as land tax) forming only one third of the Nation's property taxes. Local Government accounts for around 6% of general government outlays and 3 to 4% of total taxes collected in Australia. Local Government expenditure as a percentage of GDP is only 2% compared with 15% in other developed countries.

According to the Australian Centre of Excellence for Local Government (ACELG) pressures on Local Government finances have come about because:

- Communities, State and Federal government have come to expect Local Government to undertake a broader range of responsibilities and their revenues have not kept pace with their expenditure requirements.
- Both population increase in coastal areas and decreases in country areas combined with ageing populations have created extra pressures on local government resources.
- Local government assets are ageing and the concern that renewal expenditure is not occurring at the rate necessary to maintain service levels from existing assets.
- The impact of the Australian Accounting Standards in the 1990s which requires Governments to recognise infrastructure (roads, stormwater, drains, and buildings) as assets and depreciate them over their useful lives.
- Property price booms and declines which create volatility in rates payable by many ratepayers without commensurate increases in Local Government Revenues.

According to the ACELG:

- Grants as a share of local government revenue have declined over time
- Local governments' roles have expanded
- Communities typically want all spheres of government to do more for them (and are often not supportive of paying higher taxes to fund such increases)
- There is much greater awareness within local government of the long running cost of its infrastructure related services and responsibilities and the need to balance revenue and expenditure provision and
- Given the size of the sector compared with the other spheres of government, it would be possible to materially improve local government's revenues with a very modest negative impact on the Commonwealth's and/or the states' budgets.

The NSW Context

According to the Urban Taskforce 2012, The Local Government Act of 1993 encouraged Councils to serve people, not just property, but did not give them the revenue base to do so. This accelerated the shift from infrastructure spending to human services with the result that Councils went from the traditional three "Rs" of Roads, Rubbish and rates to the eight "Rs" of:

1. Roads (including footpaths, kerbing, drains and street lighting)
2. Refuse (including recyclable waste collection and disposal)
3. Regulation (eg town planning, land use zoning, development approvals, safety inspections and environmental controls)
4. Recreation (eg parks, sportsgrounds, pools and libraries)
5. Relief (eg community welfare, health, education and transport)
6. Regionalism (eg tourism, and economic development)
7. Retail services (eg Airports and caravan parks)
8. Rate collection

The City of Newcastle Context

The Census population of the City of Newcastle in 2011 was 148,531, living in 65,939 dwellings with an average household size of 2.3. The table below shows the extent of Council's LGA size and its' infrastructure assets.

Newcastle City Council LGA			
Locality and Size		**Infrastructure Cont'd**	
Locality	Hunter	Stormwater pipes	423 km
Area	187 km^2	Playgrounds	115
DLG Group No.	5	Garden beds	589
Demographics		Creeks	67 km
Population	148,531	Bushland	5.7 million sq m
% under 20	23%	Library - general collection books	370,235
% between 18 and 59	56%	Art Gallery - study collection	94 objects
% over 60	21%	Local footpaths	1.2 million sq m
Expected population in 2021	165,600	Bridges	260
Operations		Sea and river walls	10.9 km
Number of employees (FTE)	926	Buildings and structures	591
Annual revenue	$227.7m	Stormwater pits	16,000
Infrastructure		Sports fields	146
Infrastructure backlog value	$112.8m	Trees	105,472
Local Roads	7.5 million sq m	Wetlands	2.1 million sq m
Kerb and gutter	1.5 million m	Library - Local Studies collection	44,634
Bus shelters	124	Art Gallery - permanent collection	5,611 objects
Retaining walls	18 km	Total infrastructure value	$918.5m

Within Council's infrastructure, property, plant and equipment (IPP&E) assets as at 30 June 2011 there were:

- $613.5 million worth of roads, bridges and footpaths
- $181.2 million of specialised buildings
- $98.0 million of stormwater drainage
- $25.1 million of other structures
- $20.0 million of depreciable land improvements and
- $0.7 million of non specialised buildings.

The following tables show the number of Effective Full Time (EFT) employees against Councils service elements:

City Assets	**EFT**
Commercial Enterprise Services	32.4
Financial Services	50.6
Group Management	2
Information Management Services	28.9
Strategic Property and Fleet Management Services	11
Summerhill Waste Management Centre	19
Tourism & Economic Development Services	16
	159.9

City Engagement	
Customer Service Community and Consult Services	29
Government and Council Services	16.5
Group Management	2
Human Resource Services	33.15
	80.65

Future City	
Art Gallery	10.68
Development and Building Services	35.6
Environment and Climate Change Services	7
Group Management	3
Library	52.72
Museum	9.8
Strategic Planning Services	55.42
	174.22

Liveable City	
City Presentation Services	123
Compliance Services	41
Group Management	3
Infrastructure Mgmt Services	54.82
Parks & Recreation Services	135.3
Road & Asset Maintenance Services	232.21
	589.33

Executive Management	
General Manager's Office	2
Group Management	1
Lord Mayor's Office	2
Organisational Performance	8
	13

Total	**1017.1**

Summary

In summary, Councils across Australia represent a small part of GDP but provide a very broad range of services to the community. In NSW revenues are being exceeded by costs as Councils are required to do more with limited funds. With the change in the NSW Local Government Act, the range of Services has increased significantly.

The TCoN has been affected by the same pressures the Local Government Act 1993 imposed on other Councils. In addition to the eight Rs listed above, TCoN has provided services such as:

1. Seniors living
2. Child care
3. Youth venue
4. Museum
5. Regional library
6. Art Gallery
7. Civic Theatre
8. Fort Scratchley
9. Loft (youth services)
10. Community group accommodation
11. Ocean Baths
12. Golf Course
13. Tourists Park
14. Airport

These extra services have been delivered without sufficient revenue sources to cover costs. In addition, the Newcastle LGA has a large number of assets to support these services as shown in the table above.

2. Is NSW Local Government Sustainable?

Before answering this, a definition of Local Government sustainability is required.

2.1 How is Council sustainability defined?

FiscalStar in a 2009 Local Government Review defined sustainability as:

"Maintaining an investment grade credit rating through achieving three primary goals:

- A minimum 2.5% budget surplus ratio, so that future ratepayers are not left with excessive share of the cost of capital
- A maximum 2% unsatisfactory infrastructure, unsafe or unsightly, and
- A maximum 60% Net debt and other financial liabilities to total operating revenue ration s that debt charges remain affordable."

In 2009, FiscalStar used three sustainability indicators (based on these goals) to determine NSW Local Government sustainability as follows:

- Operating Surplus ratio(Operating surplus to revenue from rates, fees and charges)
- Infrastructure backlog ratio (infrastructure renewal backlog to total infrastructure carrying value)
- Net Financial Liabilities Ratio:(Net debt and other financial liabilities to total operating revenue)

The results were as follows:

Sustainability Indicator	Sustainable Benchmark	NSW Local Government Average	NSW Local Government Range
Operating surplus	2.5% to 7.5%	2.00%	29% deficit to 43% surplus
Infrastructure backlog ratio	0% to 2.0%	6.00%	0% to 39%
Net financial liabilities ratio	40% to 80%	4.00%	0% to 193%

Based on this analysis FiscalStar, in 2009, found that of the top 99 NSW Councils:

- 46 were sustainable
- 16 vulnerable and
- 37 unsustainable.

Of the **18 regional coastal Councils, 12 were unsustainable**.

FiscalStar found many councils had a heavy reliance on Government grants, little spare cash, expenses growing in excess of underlying costs, and insufficient capital works spending to renew ageing assets.

Fiscal Star have pointed to the heart of the problem being the backlog of infrastructure in such things as roads, buildings, stormwater drains etc.

2.2 What is causing the sustainability issue?

The lack of funds, combined with expanded services, has caused the sustainability issue. One of the symptoms is large infrastructure backlogs.

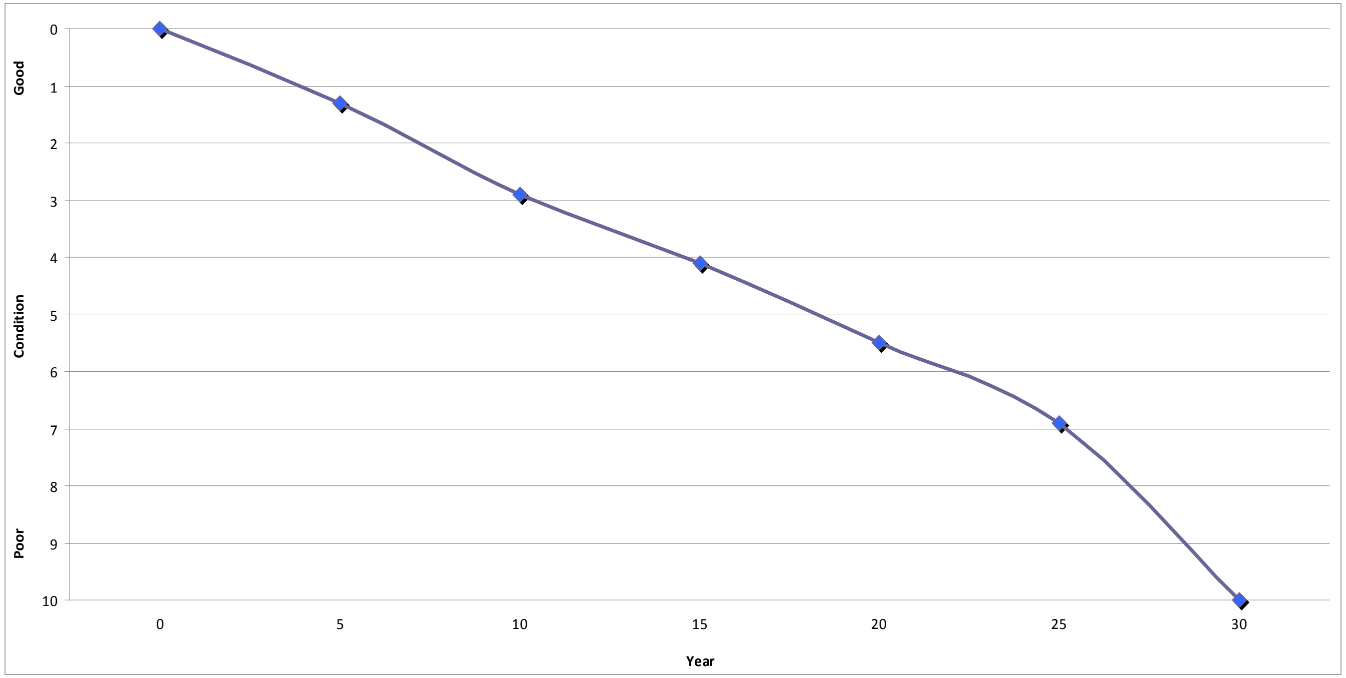
2.2.1 The Infrastructure backlog

This is a very significant issue for many NSW Councils.

What is an 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 stated within Special Schedule 7 that accompanies the council's audited annual financial statements.

An asset degrades over time and at different rates. **This is measured on a 10 point scale** as follows:



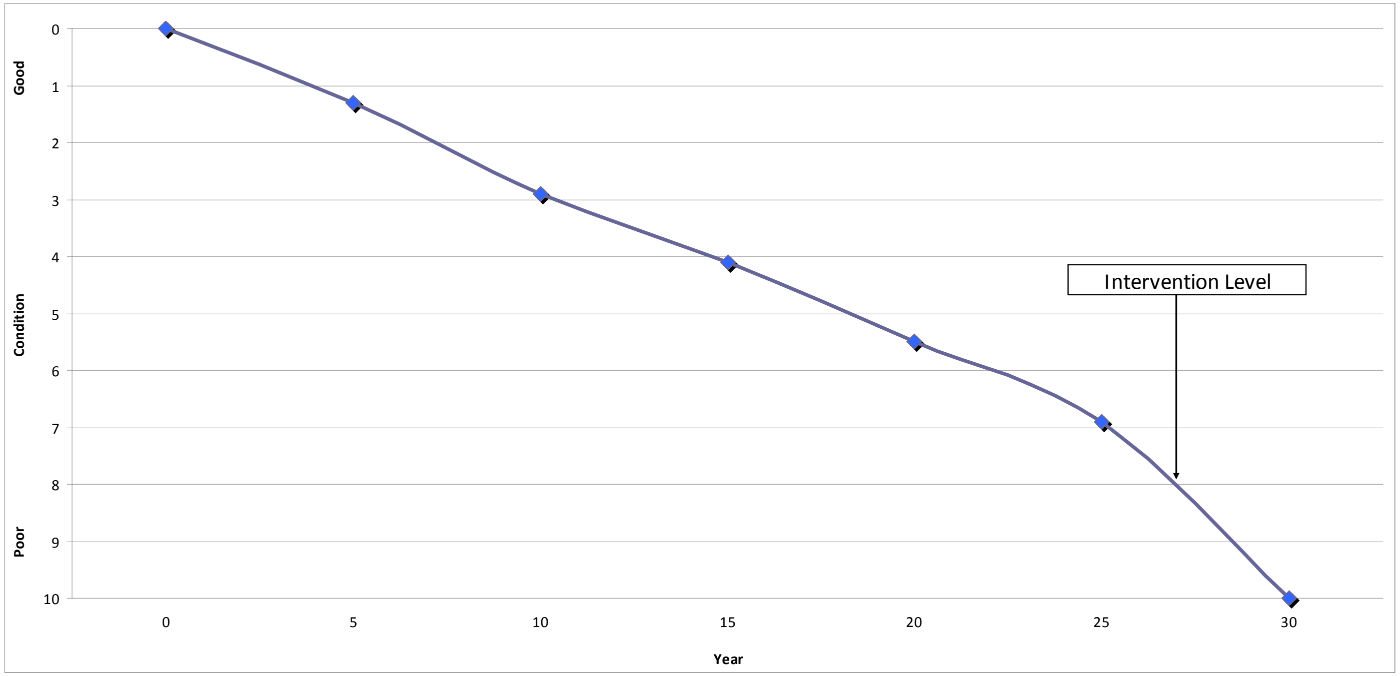
For analysis of the backlog, assets are grouped where the asset has similar behaviours (eg wearing surfaces and pavements as part of the roads group)

The asset groups are defined in the table below:

Group	Category in Group
Roads:	• Wearing surface (regional) • Wearing services (local) • Pavement (regional) • Pavement (local) • Footpath (concrete/block) • Footpath (ash felt) • Kerb and Gutter
Natural assets	• Street tress • Park trees • Urban creeks
Storm Water assets	• Storm water pits • Storm water pipes/culverts
Buildings and Structures	• Buildings (long life greater than 30 years) • Buildings short life (less than 30 years) • Buildings services • Retaining walls • River walls • Bridges and culverts
Recreational assets	• Parks and sporting grounds
Cultural assets	• Cultural assets

The condition of the asset is defined as its point on the **degradation curve**. The present condition is the measure of where an asset is defined on this curve (eg a road in condition 2 is in excellent overall condition, a road in condition 6, is in a "fair to poor overall condition").

There is a point of degradation where the Council will need to intervene and renew the asset. This is called the **intervention level**. (For example the intervention level for roads is 8, as shown below, where an asset is in very poor overall condition, with serviceability being impacted by its' poor condition.



A backlog is the level of overdue renewal and maintenance based upon Councils treatments to date. **Renewal** is the total cost of restoring a physical asset's service level to that which existed originally, applying current standards and technology.

Renewal is not the same as maintenance. **Maintenance** is the annual cost of routine repairs and regular upkeep of a physical asset to ensure that it provides service levels consistent with its expected lifecycle.

How big is the Infrastructure backlog problem in NSW?

In November 2006 a Pricewaterhouse Coopers study revealed **NSW had a backlog of infrastructure renewals of $6.3 billion compared with $0.8 billion in Victoria** and **the under spend per annum was $500 million compared with $81 million in Victoria**. Funding for infrastructure maintenance and renewal has been described as the biggest management challenge in Local Government (Allan 2006, enquiry into financial sustainability of NSW Local Government).

Why has this occurred?

It is evident in NSW, that Councils have been starved of funds since the 1970s when rate capping emerged as a policy. Councils, at this time had relatively simple roles and basic infrastructure per capita. The emphasis was on operations and expanding services over the following decades. Many NSW Councils did this at the expense of renewing their asset base. In addition they expanded the asset base as the services grew. The end result is more degraded assets unsupported by revenue injections.

2.2.2 The Rate Cap

Traditionally land rates were the main source of revenue for Local Government; however rate capping has severely constrained the rate of growth of this income source.

Analysis of local government in Australia shows that rate income has decreased from 54.1% to 47.2% of total revenue sources from 1974/1975 to 1997/1998 and was estimated to be only 38.7% in 2009/2010. In Newcastle this was 52.7 falling to 48.2 in 2011/2012.

Rate Peg

Rate pegging has been in place since 1977.

Under the Local Government Act 1993, the total amount of income that a council can raise from certain rates and charges is limited. **This is called the rate peg percentage**. The rate peg is determined on an annual basis.

Because of rate pegging, a council's overall rates revenue **cannot increase by more than the approved percentage increase**.

If overall land values rise, councils may have to reduce or otherwise adjust the amount of rates levied per dollar so that total income does not grow by more than the approved percentage increase.

Since 2010, IPART is responsible for determining the rate peg that will apply to councils **using a Local Government Cost Index (LGCI)**. The Index assists in calculating the operational costs of councils in New South Wales (NSW).

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 does not directly measure councils' total level of costs. It is a composite index that combines changes in a number of input price indexes over time. The LGCI is similar to the Consumer Price Index (CPI) in this respect.

The **rate peg percentage is calculated by subtracting a determined productivity factor for councils from the Local Government Cost Index**.

For 2011/2012, IPART determined a Local Government Cost Index of 3.0% and a productivity factor of 0.2%, giving a rate peg for 2011/2012 of 2.8%.

The percentage increases in the rate pegging limit over the last **7 years have averaged 3.2%:**

Rates	2005/06	2006/07	2007/08	2008/09	2009/10	2010/11	2011/12	Average
	3.50%	3.60%	3.40%	3.20%	3.50%	2.60%	2.80%	3.20%

Forecasts shown below provide an average increase over the next **5 years is 2.89%:**

Rates and Charges	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
	3.60%	2.80%	2.80%	2.00%	2.50%	3.00%	2.90%	2.30%	2.00%	2.25%	2.40%

Comparing this with other councils in other States the following was observed:

As shown below, (reference ABS) the annual average percentage growth in local government tax revenue and total revenue since 2000/2001 has been lower in NSW than in other states. From this it could be argued that rate pegging has contained the growth in rates in NSW

Annual average percentage increases in revenue 2001/02 - 2010/11:

NSW	4.4%
Victoria	8.2%
Queensland	8.6%
South Australia	7.0%
Western Australia	8.1%

According to IPART there remains great variability in the growth in rates and total revenue among councils. At the upper end, some councils have experienced strong growth, have had a number of high special rate variations, or have increased non-rate revenue (eg user charges and fines).

At the lower end, councils have either not taken up the full rate peg in previous years, have not sought special variations, or do not have the ability to increase income from non-rate sources. It may be that ratepayers in these councils have limited capacity to pay higher rates or charges.

Under the Local Government Act 1993, **councils are able to apply for additional increases** in general income beyond the annual rate peg amount. **This is referred to as a 'Special Rate Variation'**.

Under the **LGA, councils may apply for a single year increase under section 508(2), or a multi-year increase (of between two and seven years) under section 508(A)**.

In 2010, the Government delegated to IPART the responsibility for assessing and determining special rate variation applications, effective from 2011/2012 onwards. Previously, the Minister was responsible for determining special rate variations.

Whist IPART has been delegated responsibility for assessing and determining special variations, the NSW Government, Division of Local Government Department of Premier and Cabinet, has retained responsibility for setting the policy framework under which applications will be assessed. This is reflected in the Government's Special Rate Variation Application Guidelines, which sets out the assessment criteria that IPART must use when assessing applications.

Councils may seek a special rate variation in order to undertake environmental works, fund town improvements, redevelop community and civic facilities, address maintenance backlogs and maintain or improve existing service provision.

Local councils that are seeking special variations to general income above the rate peg amount are required to submit applications to IPART for review and assessment. The council must include details of its intention to apply for a special variation in its draft delivery program and operational plan and must consider any submissions received from the public. If a council's application is approved, IPART will specify the percentage by which the council may increase its general income.

In accordance with the Special Variation Guidelines, IPART must assess special variation applications against the following criteria:

- demonstrated need for the rate increase
- demonstrated community support for the special variation
- reasonable impact on ratepayers
- sustainable financial strategy consistent with the principles of intergenerational equity
- productivity improvements achieved and planned and
- Implementation of the Integrated Planning and Reporting framework.

In order to illustrate this comparison, the following table outlines the IPART rate Local Government Cost Index for all Councils compared to TCoN. The cost index for Newcastle (at 3.42%) is significantly higher than the average for NSW at 2.89%.

				TCoN	Ipart	Variance
Cost items	**TCoN 30/06/2011 Expenditure**	**Effective Wieght (%)**	**Price Change (% Annual average)**	**Contribution to index change (percentage points)**	**Contribution to index change (percentage points)**	**Percentage Points**
Employee benefits and on-costs	101,347,283	36%	3.50			0.25
Plant and equipment leasing (exlcuding waste management)	647,182	0%	3.80			0.01
Operating contracts (excluding waste management	30,711,124	11%	2.10			- 0.20
Legal and accounting services	463,059	0%	2.20			0.03
Office and building cleaning services	75,676	0%	4.90			-
Other business services	14,128,874	5%	3.70			0.04
Insurance	3,337,044	1%	3.30			0.02
Telecommunications, telephone and internet services	953,791	0%	- 0.10	-	-	0.01
Printing publishing and advertising	931,477	0%	- 4.30	-	-	0.01
Motor vehicle parts	67,819	0%	0.60		-	0.01
Motor vehicle repairs and servicing	12,882	0%	- 0.20	-	-	0.01
Automotive fuel	349,567	0%	11.10			0.11
Electricity	4,485,854	2%	10.70			0.15
Gas	56,949	0%	5.70		-	- 0.01
Water and sewerage	902,336	0%	6.33			-
Road, footpath, kerbing, bridge and drain building material	665,771	0%	3.50			0.10
Other building and construction materials	5,805	0%	2.40			0.01
Office supplies	899,561	0%	- 1.00	-	-	-
Emergency Services levies	2,704,375	1%	9.40			0.04
Other expenses	120,759,649	43%	3.20			- 1.08
	283,506,078	**100%**		**3.42**	**2.89**	**- 0.53**

Problems with the rate cap and cost index:

The following are observations relating to the rate cap and Local Government Cost Index theory:

- No two Councils are the same. The rate is averaged over all Councils across NSW and Newcastle's index is much higher than the average due to the range of services it offers.
- A Councils current financial condition is not taken into account before applying the cap.
- The cap does not take into account any infrastructure backlog and councils have to seek a SRV to gain approval to address this.
- The average rate amongst councils varies greatly and
- The rate cap productivity factor discounts council's revenues. Productivity however is measured as a cost saving. Costs are where productivity savings are achieved and then benefit the organisation thereafter. When discounts come off revenues, Councils are penalised thereafter due to loss of that revenues compounding effect. This is regardless of whether efficiency gains are made or not.

In addition, from the table above, NSW has suffered revenue decline due to rate capping compared to other states. This helps to account for why so many councils are now not sustainable.

2.2.3 Falls in other revenues

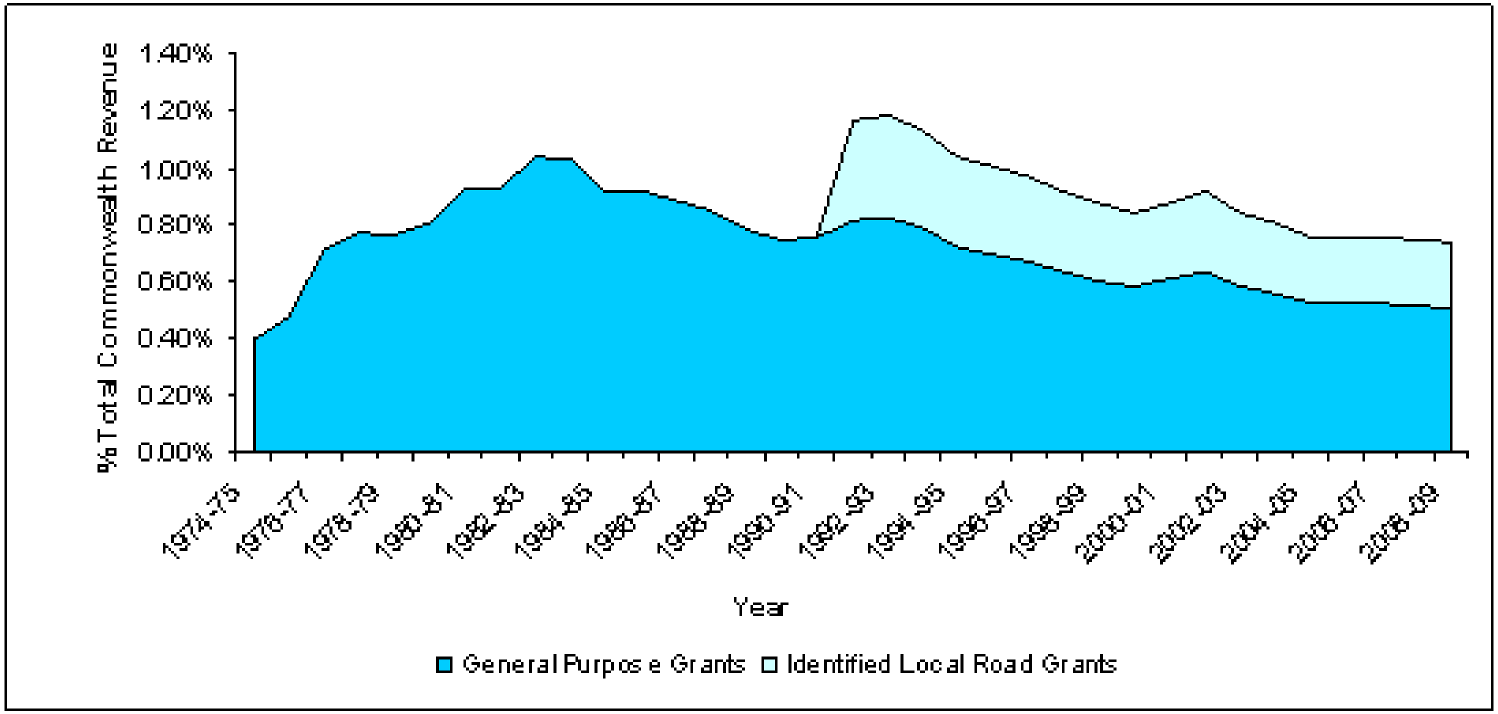
Specific purpose grants from the State Government have fallen as a proportion of Local Government revenue from 14.8% in 1974/1975 to only 7.1% in 1997/1998.

The largest portion of funding from the Commonwealth is distributed to local government annually as the Financial Assistance Grants (FAG). The primary objective of this grant is to address the problems arising from the difference in the relative revenue raising capacities and expenditure responsibilities between the three spheres of government. The FAG is distributed based on the population of the local government area, the relative local road need and relative need based on equalization principles.

The current FAG program does not provide local government with a source of revenue that meets existing demand, nor does it reflect historical growth in demand for local government services. Since it's inception in 1974/1975 the Federal Government has adjusted the FAG based on Consumer Price Index (CPI) and population growth without allowing for the increase in local government responsibilities.

Therefore, over time, this has resulted in a decline of FAGs as a percentage of total Commonwealth revenue. For example, the value of the FAG (including the local roads component) as a proportion of total Commonwealth revenue has fallen from 1.18% in 1993/1994, to 0.97% in 1996/1997 and to just 0.74% by 2008/2009.

The following diagram prepared by ALGA highlights this trend:



To combat the impact of these reductions local government has had to increase the level of user charges. ALGA estimates that average revenue from users as a percentage of operating spending is approximately 37% for local government compared to 4% for the Commonwealth and 12% for state governments. User charges raises equity considerations for the community and therefore increasing user charges further is not an ideal or sustainable solution.

In fact ALGA argues that to truly address the relative revenue raising capacities of the different spheres of government, local government should be provided with access to a higher proportion of the tax collected by the Commonwealth. It suggests that the Financial Assistance Grant should be increased to 1% of total Commonwealth taxation revenue (excluding GST) and that local government should also have access to a proportion of the GST income collected.

In 2005 the Local Government and Shires Associations of NSW (LGSA) commissioned a report to address concerns about the financial capacity of local government to meet growing demand for infrastructure and services. The report titled "*Are Councils Sustainable Independent Inquiry into the Financial Sustainability of NSW Local Government"* was published in 2006 and concluded that significant reform was required to ensure the ongoing viability of local government in NSW. The report supported the ALGA proposal that local government should have a higher proportion of the national tax income.

2.2.4 Cost Shifting

In 2001 the Commonwealth Grants Commission conducted the Review of the Operation of the Local Government (Financial Assistance) Act 1995 in which they concluded that local government is increasingly being drawn into new areas of service provision such as human services but that this is at the expense of traditional property-based services, particularly roads.

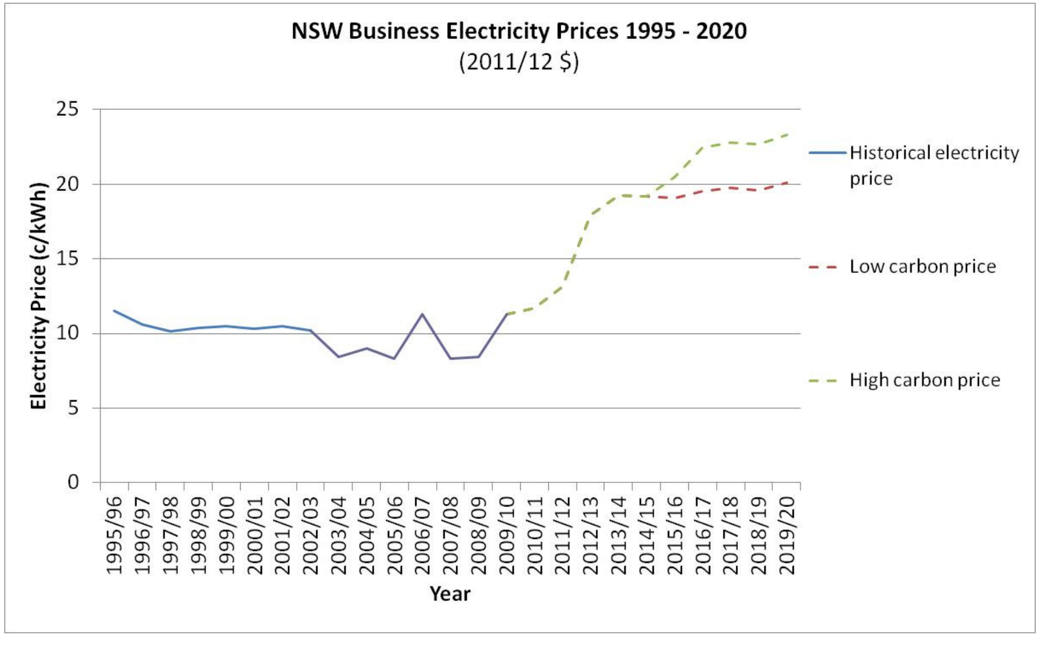
The report cited one of the main reasons why local government functions and responsibilities had increased was Cost Shifting. This is either where a council agrees to provide a service on behalf of a Federal or State Government (with funding subsequently reduced or stopped) or where another tier of government ceases to provide a service and local government, for whatever reason, takes over.

2.2.5 Rising Costs

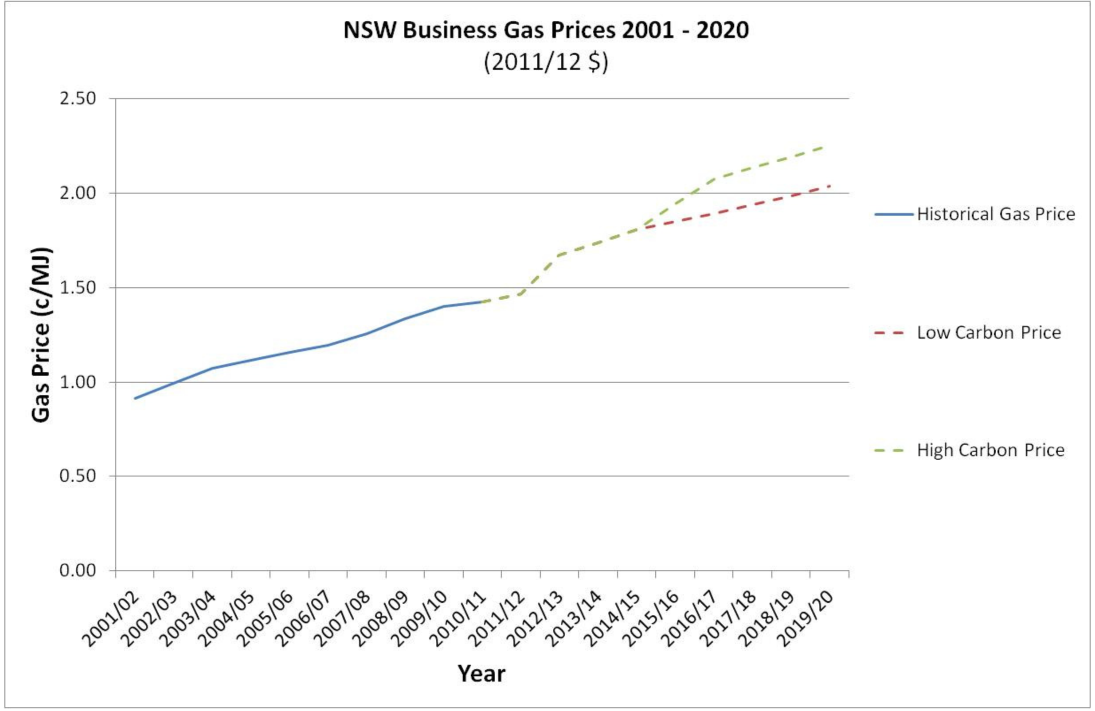
According to the "Institute for Sustainable Futures, UTS December 2011", NSW business energy prices to 2020:

NSW retail electricity prices for business are projected to rise sharply to 2013/2014 due to rising network and wholesale electricity prices as well as the introduction of a carbon price.

Over the decade, electricity prices are set to increase by between 53% (6.97 c/kWh) and 78% (10.2 c/kWh) in real terms from 2011/12 levels, depending on whether a high or a low carbon price eventuates.



Gas prices are projected to increase by between 0.57 c/MJ (39%) and 0.79 c/MJ (54%) on 2011/2012 levels in the low and high carbon price scenarios respectively. The increase is a result of projected rises across all component costs, with rising wholesale costs accounting for 29% of the price rise under the low carbon price scenario and carbon price accounting for 43% of the price rise under the high carbon price scenario.



2.2.6 Employee Costs

Employee costs are aligning with rises in the NSW State Award. There is much inefficiency with this. Firstly where there are private suppliers or competitors we have in some cases gone out of alignment with the market. A recent example is car parks attendants. Council pays approximately $29 per hour for wages and the Award offered by the private sector is approximately $19 per hour.

Work practices, processes and procedures also cause inefficiencies. The lack of integrated systems makes undertaking simple data analysis very complex.

3. The City of Newcastle- is it Sustainable?

In order to determine this, an outline of the current position and forecast of the long term finical position is required through the provision of a Long Term Financial Plan (LTFP).

The City of Newcastle current financial position:

TCorp, in 2012, analysed the TCoN result as follows:

“When analysing Council’s performance over the review period we make the following observations of Councils past three years performance:

- While the Council has incurred operating deficits (excluding grants and contributions for capital purposes), Council’s underlying operating performance (measured using EBITDA) has marginally improved from $19.6 million in 2009 to $21.1 million in 2011
- Council has had sound liquidity as indicated by an Unrestricted Current Ratio above the benchmark in all three years
- Council’s fiscal flexibility is sufficient as indicated by an Own Sourced Operating Revenue Ratio above the benchmark in all three years
- Council’s total borrowings have increased from $38.7 million in 2009 to $53.4 million in 2011
- Council’s ability to service further additional borrowings is reducing with the increasing debt service costs reducing Council’s DSCR and Interest Cover Ratio.

Council’s reported infrastructure backlog of $112.8 million in 2011 represents 12.3% of its infrastructure asset value of $918.5 million. Other TCorp observations include:

- Unlike the majority of councils, buildings and other structures are the largest backlog category at 75.6% of the backlog in 2011
- Over the last three years Council has averaged close to benchmark for its capital investment program, but its expenditure on maintenance has been consistently below required levels
- Since 2010, Council has commenced an expanded capital investment program and has secured approval to a permanent SRV increase of 5% (in addition to the rate peg increase of 3.6%) commencing in the 2013 financial year to fund the rehabilitation and upgrade of nine civic projects that should assist reducing the backlog”.

The City of Newcastle future financial position:

Council's long term financial plans are made up of two components as follows:

1. 10 Year Long Term Financial Plan and
2. 10 year Special Rate Variation Funded Projects Plan (SRV projects)

The following outlines the detail and assumptions behind these plans.

3.1 LTFP (excluding SRV projects)

The LTFP is made up of the adopted Annual Operational Plan and the Four Year Delivery Program. The remaining years are forecast using a number of assumptions outlined in **Appendix A**. The adopted Annual Operational Plan is underpinned by the following financial management strategies and principles:

- Financial stability and sustainability
- Achieving and maintaining a balanced budget philosophy
- Having sufficient cash and available working capital
- Maintaining strong liquidity
- Having sufficient cash reserves to meet statutory and Policy requirements
- Keeping the debt service ratio below industry and Policy
- Continuing to reduce the outstanding infrastructure backlog to maintain all categories of assets at a satisfactory level

The forecast annual Operational Plan needs to be revised annually within the above financial management strategies with appropriate amendments made to meet these financial objectives prior to adoption by Council.

The Long Term Financial Plan in its current state shows shortfalls in funding and in certain years will not meet the key financial management strategies as noted above. It should be noted that this LTFP does not include SRV income or expenditure for the SRV funded projects. This funding and expenditure is outlined in section "3.2 SRV projects".

The table below outlines the LTFP (Excluding SRV funded projects)

From the above it is evident that the underlying base budget is in deficit by $9.5 million in 2012/2013 and this deficit further increased deficit of $37.3 million by 2022. **This position is clearly not sustainable**.

Below is the balance sheet prediction from the Long Term Financial Plan. This balance sheet does not include the Special Rate Variation (SRV) projects which will be outlined in the following section.

The balance sheet shows a strong total equity position for Council. Council has low borrowings which do increase over the 10 years from $64 million to $114 million. Even so, the total equity position after 10 years is still strong at $1.4 billion.

Income and Expenditure Statement

NCC - Long Term Financial Plan

For the year ended 30 June	Notes	2011/12 $'000	2012/13 $'000	2014 $'000	2015 $'000	2016 $'000	2017 $'000	2018 $'000	2019 $'000	2020 $'000	2021 $'000	2022 $'000
Operating Revenue												
Rates & charges		107,020	111,544	115,306	118,535	121,498	125,143	128,772	131,734	134,368	137,392	140,689
User charges & fees		53,363	55,198	56,413	57,971	61,045	64,281	67,688	71,277	75,055	79,034	83,224
Interest		11,796	6,849	6,858	6,636	6,967	7,316	7,681	8,066	8,469	8,892	9,337
Other operating revenues		8,294	10,195	10,592	11,790	12,277	12,784	13,311	13,861	14,433	15,029	15,649
Grants & contributions - Operating		30,724	23,706	24,419	24,998	25,798	26,597	27,262	27,862	28,545	29,287	30,048
Total Operating Revenue		211,197	207,490	213,587	219,930	227,585	236,120	244,716	252,799	260,870	269,634	278,948
Operating Expenses												
Employee costs		89,558	88,453	90,905	92,292	95,291	98,388	101,586	104,887	108,296	111,816	115,450
Borrowing costs		3,922	3,925	4,517	5,107	5,270	5,434	5,570	5,692	5,832	5,983	6,139
Materials & contracts		54,864	41,071	41,896	43,009	46,450	50,166	54,179	58,514	63,195	68,250	73,710
Depreciation & amortisation	1	55,168	57,000	57,000	57,000	58,824	60,648	62,164	63,531	65,088	66,780	68,516
Other operating expenses		30,647	61,411	62,643	64,606	66,674	69,878	73,237	76,757	80,446	84,313	88,365
Total Operating Expenses		234,159	251,859	256,961	262,014	272,509	284,514	296,735	309,382	322,857	337,142	352,181
Total Operating Revenue Less Operating Expenditure		(22,962)	(44,369)	(43,374)	(42,085)	(44,925)	(48,393)	(52,020)	(56,583)	(61,986)	(67,509)	(73,233)
Capital Revenues												
Grants & contributions - Capital	2	11,017	9,079	6,781	6,828	6,958	7,081	7,183	7,275	7,380	7,493	7,610
Proceeds from the sale of Assets		(374)	3,006	949	1,292	2,311	1,846	983	1,229	1,862	1,806	1,485
Total Capital Raising revenue		10,643	12,085	7,729	8,120	9,269	8,927	8,166	8,504	9,242	9,300	9,095
Nett Suplus(deficit) after capital revenue		(12,319)	(32,284)	(35,644)	(33,965)	(35,655)	(39,466)	(43,854)	(48,078)	(52,745)	(58,209)	(64,138)
Add back Depreciation		55,168	57,000	57,000	57,000	58,824	60,648	62,164	63,531	65,088	66,780	68,516
Funding available for capital expenditure		42,849	24,716	21,356	23,035	23,169	21,181	18,310	15,453	12,343	8,571	4,379
Capital Expenses												
Capital Expenditure on Asset renewals	3	57,150	42,947	39,767	41,687	49,936	46,402	43,188	44,997	48,857	46,209	45,489
Total capital spend on renewals		57,150	42,947	39,767	41,687	49,936	46,402	43,188	44,997	48,857	46,209	45,489
Net Transfers from/(to) reserves		10,033	(145)	(11,799)	(10,798)	(2,033)	(3,422)	(6,728)	(3,989)	966	434	(227)
Net Loans Borrowings/(Repayments)		10,000	10,000	10,000	10,000	10,000	10,000	10,000	10,000	10,000	10,000	10,000
Net Overall Funding Surplus/(Deficit)		**5,732**	**(8,376)**	**(20,210)**	**(19,450)**	**(18,801)**	**(18,643)**	**(21,606)**	**(23,533)**	**(25,548)**	**(27,204)**	**(31,338)**
Parking Meter Adjustments												
Halt Meter Expansion and No Weekend Meters City East and City West	**5**		1,143	1,128	2,312	2,324	4,582	4,850	5,132	5,440	5,868	6,044
Net Overall Funding Surplus/ (Deficit) after Parking Meter Adjustments		5,732	(9,519)	(21,339)	(21,762)	(21,125)	(23,224)	(26,456)	(28,665)	(30,988)	(33,072)	(37,382)

Balance Sheet

NCC - Long Term Financial Plan inancial Plan

For the year ended 30 June	2012 $'000	2013 $'000	2014 $'000	2015 $'000	2016 $'000	2017 $'000	2018 $'000	2019 $'000	2020 $'000	2021 $'000	2022 $'000
Current Assets											
Cash and cash equivalents	34,953	26,577	25,203	24,143	22,373	19,375	12,917	7,415	1,740	(3,667)	(8,051)
Investments	74,142	68,822	67,503	65,749	58,972	53,132	48,618	40,766	28,986	15,964	15,549
Receivables	15,795	15,152	15,428	15,845	16,474	17,163	17,874	18,573	19,282	20,041	20,715
Inventory	664	723	739	759	783	807	828	846	867	889	912
Other	524	488	499	513	529	545	559	571	585	600	616
Non current assets classified as held for sale	830	1,000	0	0	0	0	0	0	0	0	0
Total Current Assets	126,908	112,762	109,372	107,009	99,131	91,023	80,795	68,170	51,459	33,828	29,742
Non Current Assets											
Investments	75,354	69,947	68,607	66,824	59,936	54,001	49,413	41,432	29,460	16,225	15,804
Receivables	7,824	7,934	8,109	8,328	8,594	8,861	9,082	9,282	9,509	9,757	10,010
Infrastructure, property, plant and equipment	1,615,168	1,630,287	1,608,813	1,588,702	1,586,314	1,578,499	1,564,243	1,553,631	1,550,425	1,543,245	1,503,212
Investment property	11,436	12,815	12,815	12,815	12,815	12,815	12,815	12,815	12,815	12,815	12,815
Other	24	25	25	26	27	28	28	29	30	30	31
Total Non Current Assets	1,709,806	1,721,009	1,698,370	1,676,695	1,667,686	1,654,203	1,635,581	1,617,189	1,602,239	1,582,072	1,541,872
Total Assets	**1,836,715**	**1,833,771**	**1,807,742**	**1,783,704**	**1,766,817**	**1,745,225**	**1,716,377**	**1,685,359**	**1,653,697**	**1,615,901**	**1,571,614**
Current Liabilities											
Payables	13,548	15,501	15,813	16,233	17,531	18,934	20,449	22,084	23,851	25,759	27,820
Borrowings	2,095	7,089	7,338	8,342	9,015	9,985	10,958	11,917	12,812	13,743	14,101
Provisions	32,640	37,555	38,581	39,202	40,475	41,824	43,218	44,660	46,149	47,690	49,282
Total Current Liabilities	48,282	60,146	61,731	63,777	67,022	70,743	74,625	78,661	82,812	87,192	91,202
Non-Current Liabilities											
Borrowings	62,341	66,121	73,499	79,874	85,575	90,306	94,065	96,864	98,769	99,742	100,357
Provisions	8,455	8,533	8,720	8,956	9,242	9,529	9,767	9,982	10,227	10,492	10,765
Total Non Current Liabilities	70,796	74,654	82,220	88,829	94,817	99,835	103,832	106,846	108,995	110,234	111,123
Total Liabilities	**119,078**	**134,799**	**143,951**	**152,606**	**161,839**	**170,578**	**178,456**	**185,507**	**191,808**	**197,426**	**202,325**
Net Assets	**1,717,636**	**1,698,972**	**1,663,790**	**1,631,098**	**1,604,978**	**1,574,648**	**1,537,920**	**1,499,853**	**1,461,890**	**1,418,474**	**1,369,289**
Equity											
Retained Earnings	1,717,638	1,698,972	1,663,791	1,631,098	1,604,978	1,574,648	1,537,920	1,499,853	1,461,890	1,418,474	1,369,289
Revaluation Reserve	0	0	0	0	0	0	0	0	0	0	0
Total Equity	**1,717,638**	**1,698,972**	**1,663,791**	**1,631,098**	**1,604,978**	**1,574,648**	**1,537,920**	**1,499,853**	**1,461,890**	**1,418,474**	**1,369,289**

The total equity position over the 10 years is decreasing due primarily to the increase in borrowings to fund infrastructure works.

3.2 SRV projects

In order to deliver enhanced and growth assets for the community, The City of Newcastle instigated a program of new projects that were supported by a Special Rate Levy of 5% above the levy cap. These projects have been called the Special Rate Variation Projects or SRV projects for short.

The SRV projects are listed below in priority order. The SRV projects are fully funded and are not dependent on the underlying LTFP as forecast above.

Proposed program of works	$,000
Hunter Street Revitalisation project major works program over 10 years	$16,670
Coastal Revitalisation works program over 10 years	$35,798
Swimming Pool upgrade program over 10 years	$29,826
Libraries upgrade program over 10 years	$42,900
The provision of new cycleways over 10 years	$15,660
Newcastle Art Gallery expansion over 10 years	$21,000
Blackbutt Reserve upgrade over 10 years	$9,850
Implementation of Parking Strategy (On-Street) over 10 years to provide parking spaces more equitably in the Newcastle LGA	$2,795
Total SRV	**$175,319**

The SRV projects are funded and expensed so that these incomes and expenditures are balanced as detailed below. They represent $175.3 million of works which are funded by:

- 5% Special Rate Variation dedicated to SRV projects
- Asset Renewal money (MAPP) which is earmarked for expenditure on the old asset which will now be reallocated to the new asset.
- Extra Government Grant funding
- Section 94 Contributions
- Redundant asset Sales
- Community Contributions
- Sponsorship
- Internal Loans
- Other funding sources

Two recent Council decisions impact on this plan:

- To sell all Councils off street parking stations
- To not expand stages 1b, 2 and 3 of the on street parking plan.

(Note: The revenues forgone due to these decisions affect the operating budget only and not the SRV funds.)

The expenditure for off street parking was included in the asset renewal (MAPP) budget. The expenditures for on street parking affect the internal loans of $1.98 million coming from internal reserves).

The SRV budgets are finely balanced.

It is essential that SRV projects are:

- Delivered on time to meet community expectations
- Delivered within budget. Any overruns will affect the cash flows and the ability to deliver the whole program on time and budget and
- Not committed to until all the funds have been secured.

The table below shows SRV projects income and expenditure which is balanced.

ALL PROJECTS	Prior Years $	2011/12 $	2012/13 $	2013/14 $	2014/15 $	2015/16 $	2016/17 $	2017/18 $	2018/19 $	2019/20 $	2020/21 $	2021/22 $	Total $
CAPITAL INCOME													- -
SRV Forecast Funding	-	- -	5,560,800 -	17,222,208 -	3,014,500 -	10,100,000 -	8,916,500 -	3,085,200 -	2,380,000 -	940,420	-	- -	**51,219,628**
MAPPS Portion of Project	- -	622,887 -	1,186,587 -	2,389,387 -	271,462 -	271,462 -	521,462 -	1,221,462 -	771,462 -	271,462 -	2,250,000	- -	**9,777,633**
Government Grant Funding	- -	1,120,000 -	3,060,000 -	6,715,000 -	1,490,000 -	1,400,000 -	1,580,000 -	2,050,000 -	900,000 -	1,150,000 -	900,000	- -	**20,365,000**
s94 Forecast Contribution	- -	263,000 -	1,050,000 -	1,716,560 -	1,513,000 -	330,000 -	760,000 -	370,000 -	350,000 -	430,000 -	284,000	- -	**7,066,560**
Asset Sales (nominate asset & date)	- -	102,602	- -	1,767,760 -	13,307,957 -	3,800,000 -	11,956,000 -	10,109,800 -	3,805,000 -	11,009,580 -	10,556,000	- -	**66,414,699**
Partnership funding (eg PPP or community contributed works)	-	- -	100,000 -	100,000 -	100,000 -	100,000 -	87,500	-	-	-	-	- -	**487,500**
Reserve (nominate reserve source)	- 898,064 -	2,922,000 -	3,891,000 -	5,125,235 -	1,899,000 -	60,000	- -	1,450,000 -	800,000	-	-	- -	**16,147,235**
Sponsorship	-	-	- -	141,350	-	-	-	-	-	-	-	- -	**141,350**
Fees & Charges (where they are resolved to pay back Capital)	-	-	-	-	-	-	-	-	-	-	-	-	**-**
Loans (External & Internal)	- -	667,000	- -	81,450 -	380,000 -	856,000	- -	1,000,000	-	-	-	- -	**2,984,450**
Other Funding Source (nominate)	-	-	- -	715,351	-	-	-	-	-	-	-	- -	**715,351**
													-
Total Capital Income	**- 898,064 -**	**5,697,489 -**	**14,848,387 -**	**35,974,301 -**	**21,975,919 -**	**16,917,462 -**	**23,821,462 -**	**19,286,462 -**	**9,006,462 -**	**13,801,462 -**	**13,990,000**	**- -**	**175,319,406**
CAPITAL EXPENDITURE													
Hunter Street Revitalisation project major works program over 10 years	-	125,000	850,000	2,605,000	2,530,000	1,905,000	2,255,000	2,375,000	1,625,000	1,200,000	1,200,000		**16,670,000**
Coastal Revitalisation works program over 10 years	140,000	3,060,000	3,226,000	2,792,000	2,850,000	2,955,000	4,455,000	7,220,000	3,930,000	2,950,000	2,360,000		**35,798,000**
Swimming Pool upgrade program over 10 years	-	325,489	2,169,387	10,188,301	12,035,919	3,021,462	21,462	21,462	21,462	21,462	2,000,000		**29,826,406**
Libraries upgrade program over 10 years	-	-	-	100,000	2,300,000	6,500,000	15,360,000	4,640,000	1,200,000	7,100,000	5,700,000		**42,900,000**
The provision of new cycleways over 10 years	-	340,000	2,680,000	2,530,000	380,000	880,000	1,130,000	2,530,000	1,730,000	1,730,000	1,730,000		**15,660,000**
Newcastle Art Gallery expansion over 10 years	758,064	610,000	4,090,000	15,300,000	1,000,000	-	-	-	-	-	-		**21,000,000**
Blackbutt Reserve upgrade over 10 years	-	500,000	1,000,000	1,650,000	500,000	800,000	600,000	2,500,000	500,000	800,000	1,000,000		**9,850,000**
Implementation of Parking Strategy (On-Street) over 10 years	-	667,000	83,000	809,000	380,000	856,000	-	-	-	-	-		**2,795,000**
Implementation of the Parking Strategy (Off-Street) over 10 years	-	70,000	750,000	-	-	-	-	-	-	-	-		**820,000**
													-
Total Capital Expenditure	**898,064**	**5,697,489**	**14,848,387**	**35,974,301**	**21,975,919**	**16,917,462**	**23,821,462**	**19,286,462**	**9,006,462**	**13,801,462**	**13,990,000**	**-**	**175,319,406**

The proposed SRV projects are detailed in Appendix B - I.

The balance sheet below reflects the impacts of the SRV projects. The Total equity position, within 10 years is $1.6 billion.

Balance Sheet

NCC - Long Term Financial Plan inancial Plan

For the year ended 30 June	*2012 $'000*	*2013 $'000*	*2014 $'000*	*2015 $'000*	*2016 $'000*	*2017 $'000*	*2018 $'000*	*2019 $'000*	*2020 $'000*	*2021 $'000*	*2022 $'000*
Current Assets											
Cash and cash equivalents	34,953	34,953	33,915	15,054	17,308	1,128	4,603	12,703	1,345	512	135
Investments	74,142	72,374	74,490	77,937	68,154	61,646	50,026	40,012	32,966	20,961	8,764
Receivables	15,795	15,562	15,862	16,352	17,408	18,049	18,885	19,648	20,357	21,124	21,957
Inventory	664	723	739	759	783	807	828	846	867	889	912
Other	524	488	499	513	529	545	559	571	585	600	616
Non current assets classified as held for sale	830	1,000	0	0	0	0	0	0	0	0	0
Total Current Assets	126,908	125,099	125,505	110,614	104,181	82,177	74,901	73,781	56,120	44,086	32,384
Non Current Assets											
Investments	75,354	73,557	75,708	79,211	69,268	62,654	50,844	40,666	33,505	22,320	14,090
Receivables	7,824	7,934	8,109	8,328	8,594	8,861	9,082	9,282	9,509	9,757	10,010
Infrastructure, property, plant and equipment	1,615,168	1,621,989	1,616,709	1,635,064	1,649,934	1,669,005	1,664,827	1,664,011	1,688,245	1,696,963	1,704,179
Investment property	11,436	12,815	12,815	12,815	12,815	12,815	12,815	12,815	12,815	12,815	12,815
Other	24	25	25	26	27	28	28	29	30	30	31
Total Non Current Assets	1,709,806	1,716,320	1,713,366	1,735,444	1,740,638	1,753,362	1,737,597	1,726,804	1,744,104	1,741,885	1,741,126
Total Assets	**1,836,715**	**1,841,420**	**1,838,871**	**1,846,058**	**1,844,819**	**1,835,539**	**1,812,497**	**1,800,584**	**1,800,224**	**1,785,971**	**1,773,510**
Current Liabilities											
Payables	13,548	15,561	15,876	16,299	17,601	19,007	20,525	22,165	23,936	25,848	27,913
Borrowings	2,095	6,097	7,233	7,458	8,451	9,110	10,066	11,026	11,970	12,848	13,762
Provisions	32,640	37,555	38,581	39,209	40,564	41,936	43,335	44,777	46,266	47,807	49,399
Total Current Liabilities	48,282	59,213	61,690	62,965	66,616	70,052	73,927	77,968	82,172	86,503	91,074
Non-Current Liabilities											
Borrowings	62,341	66,121	73,499	79,874	85,575	90,306	94,065	96,864	98,769	99,742	100,357
Provisions	8,455	8,533	8,720	8,956	9,242	9,529	9,767	9,982	10,227	10,492	10,765
Total Non Current Liabilities	70,796	74,654	82,220	88,829	94,817	99,835	103,832	106,846	108,995	110,234	111,123
Total Liabilities	**119,078**	**133,867**	**143,910**	**151,795**	**161,433**	**169,887**	**177,759**	**184,814**	**191,168**	**196,737**	**202,196**
Net Assets	**1,717,636**	**1,707,553**	**1,694,961**	**1,694,263**	**1,683,386**	**1,665,652**	**1,634,739**	**1,615,770**	**1,609,057**	**1,589,234**	**1,571,313**
Equity											
Retained Earnings	1,717,638	1,707,553	1,694,964	1,694,348	1,683,471	1,665,657	1,634,662	1,615,608	1,608,808	1,588,897	1,570,885
Revaluation Reserve	0	0	0	0	0	0	0	0	0	0	0
Total Equity	**1,717,638**	**1,707,553**	**1,694,964**	**1,694,348**	**1,683,471**	**1,665,657**	**1,634,662**	**1,615,608**	**1,608,808**	**1,588,897**	**1,570,885**

3.3 Summary of forecast assumptions

A detailed outline of assumptions is contained in Appendix A. The following table represents a summary of the LTFP forecast assumptions:

Percentage Increases

	Notes	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Rates & Charges	1	3.60%	3.40%	3.40%	2.00%	2.50%	3.00%	2.90%	2.30%	2.00%	2.25%	2.40%
User Fees & Charges	2	4.53%	11.03%	2.20%	2.76%	5.30%	5.30%	5.30%	5.30%	5.30%	5.30%	5.30%
Interest Income	3	6.00%	5.00%	5.00%	5.00%	5.00%	5.00%	5.00%	5.00%	5.00%	5.00%	5.00%
Grants & Contributions - Operating	4	4.17%	14.65%	3.01%	2.37%	4.13%	4.13%	4.13%	4.13%	4.13%	4.13%	4.13%
Other Operating Revenues	5	0.52%	-45.88%	3.74%	10.17%	3.20%	3.10%	2.50%	2.20%	2.45%	2.60%	2.60%
Grants & contributions - Capital	6	-17.38%	31.65%	-58.36%	3.04%	3.20%	3.10%	2.50%	2.20%	2.45%	2.60%	2.60%
Employee Costs	7	2.15%	3.25%	3.25%	3.25%	3.25%	3.25%	3.25%	3.25%	3.25%	3.25%	3.25%
Materials & Contracts	8	3.50%	33.53%	2.20%	2.70%	3.20%	3.10%	2.50%	2.20%	2.45%	2.60%	2.60%
Borrowings	9	8.00%	8.00%	8.00%	8.00%	8.00%	8.00%	8.00%	8.00%	8.00%	8.00%	8.00%
Depreciation & Amortisation	10	0.60%	0.00%	0.00%	0.00%	3.20%	3.10%	2.50%	2.20%	2.45%	2.60%	2.60%
Other Operating Expenses - Waste	11	0.62%	5.12%	2.20%	2.70%	3.20%	4.81%	4.81%	4.81%	4.81%	4.81%	4.81%
Other Operating Expenses - Residual	12	3.47%	17.16%	2.01%	3.13%	7.43%	6.84%	6.84%	6.84%	6.84%	6.84%	6.84%
CPI	13		0.00%	0.00%	0.00%	3.20%	3.10%	2.50%	2.20%	2.45%	2.60%	2.60%

Notes	
1	Based on CPI delayed for one year discounted for productivity factor of 0.2%
2	Based on current projections
3	Based on expected average return on the portfolio
4	Based on current projections
5	Based on current projections (major decrease due to reduction in lease payments received and decrease in interest on investments)
6	Based on current projections (major decrease due to reductions in grant funding for Major Projects)
7	Employee Costs - based on signed award for years 2012-2014
8	Based on current projections (major increase due to category adjustment of expenditure)
9	Based on current borrowings rates
10	Depreciation - higher than previous increase in 2013 anticipated due to revaluation of infrastructure assets performed in 2011 and 2012
11	Based on current projections followed by average of years 2013 - 2015
12	Based on current projections followed by average of years 2013 - 2015

3.4 Risks with the assumptions

It is important to note that Long Term Financial Plans are inherently uncertain and contain a wide range of assumptions, including assumptions that are outside of Council's control. This may potentially affect the financial results.

These risks to Council's position, which could impact on any result in the future but have not been considered in the model, include:

- **Rate pegging threshold is lower than expected**
- **Grant funding from State and Federal Governments is lower than anticipated**
- **Investment returns are lower than assumed**
- **Contributions, for example s94, do not materialise at the level predicted**
- **Additional cost shifting from other Government agencies without offsetting revenue**
- **Inflation increase against costs higher than anticipated**
- **Legislative changes that may lower income streams or increase expenditure**
- **Natural disasters**

Independent test of assumptions

New South Wales Treasury Corporation (TCorp) is the central financing authority for entities in the New South Wales public sector. It was established in 1983 under the Treasury Corporation Act 1983 (NSW) and its principal objective is "to provide financial services for, or for the benefit of, the Government, public authorities and other public bodies". TCorp has the same legal capacity, powers and authorities as a company under the Corporations Act 2001.

TCorp has compared the TCoN model assumptions versus TCorp's benchmarks for annual increases in the various revenue and expenditure items. Attached in **Appendix C**, TCorp have provided an analysis.

In summary TCorp state:

> ***"Overall the key assumptions within the financial forecasts are considered to be reasonable, although it is noted that the outcome of these assumptions is a deteriorating financial position for Council."***

3.5 How does Newcastle compare with like Councils?

Summary of Councils current and future position

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

- The LTFP assumes the level of services and operations as 'business as usual' apart from the additional revenue and expenditure related to the nine civic capital projects identified as part of the successful SRV.
- Council are forecasting operating deficits each year when capital grants and contributions are excluded and these deficits are forecast to grow from $9.7 million in 2012 to $67.0 million in 2022 (Note this analysis was done prior to parking metre decision).
- The **liquidity position will reduce over the period and will likely result in Council becoming illiquid** if they continue with the scheduled capital expenditure program due to reducing current assets and increasing current liabilities.

4. What are the problems with the long term financial position and why are they significant issues for Council?

The following highlights some of the major issues faced by Council in the short, medium and long term.

4.1 City of Newcastle operating result

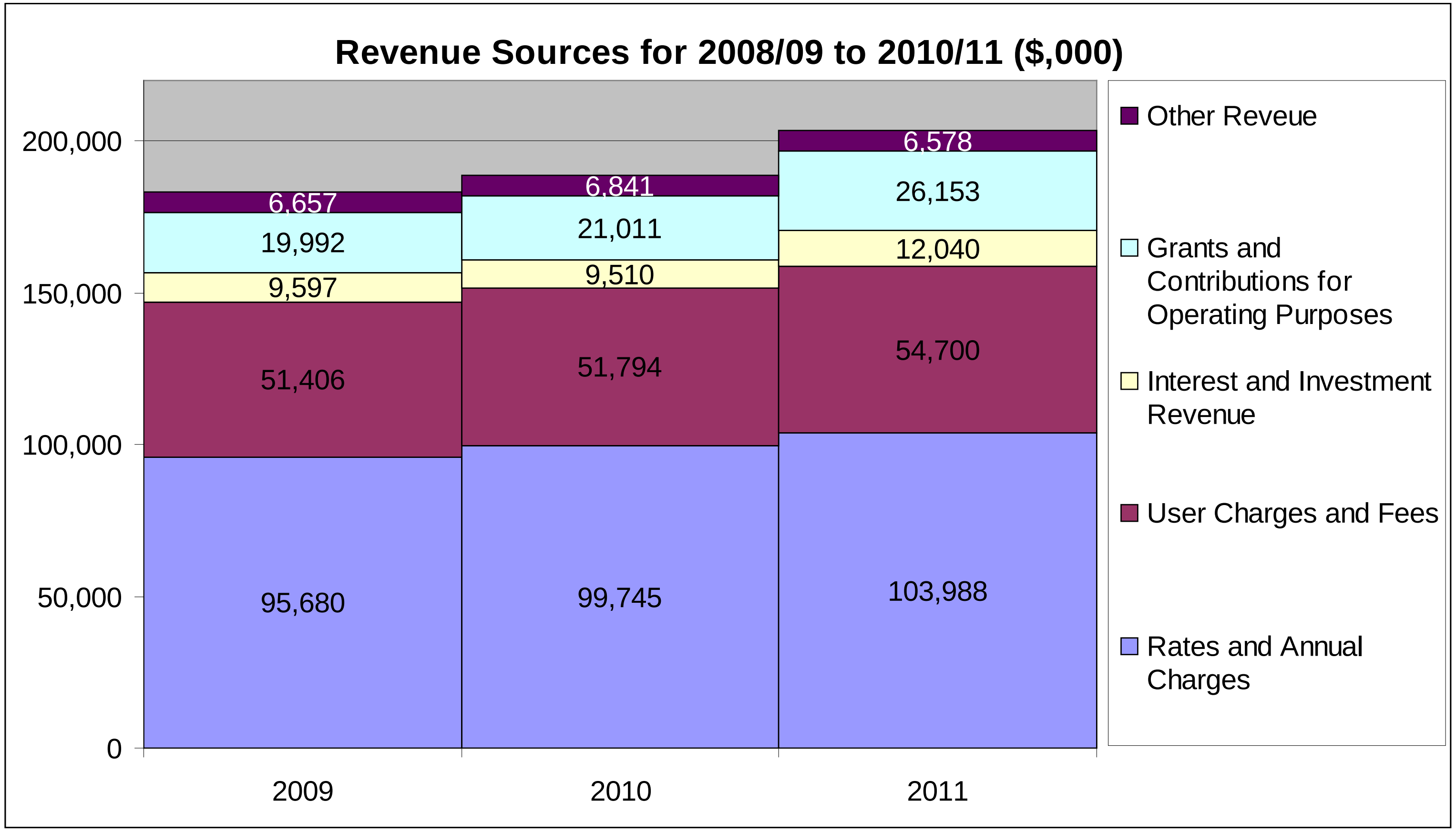
For the purpose of this analysis, depreciation has been backed out of the operating expenses. **Depreciation will be considered separately as an issue of sustainability:**

City of Newcastle Revenue position

In considering the underlying **operational position of Council** the following **revenues have been recognised**:

- Rates and Charges
- User Charges and Fees
- Interest
- Other operating Revenues
- Grants and Contributions – operating

Revenue History



Key Observations

- Rates and annual charges are the main source of revenue for the Council being 51.1% of total revenue in 2011. Rates and annual charges have increased by 4.2% p.a. between 2009 and 2011.

- The maximum allowable rate increase was 3.5% in 2010 and 2.6% in 2011 with the additional revenue attributable to an increase in the number of assessments and increases in valuations. There was also an 11.9% increase in domestic waste management charges which increased total rates and annual charges.

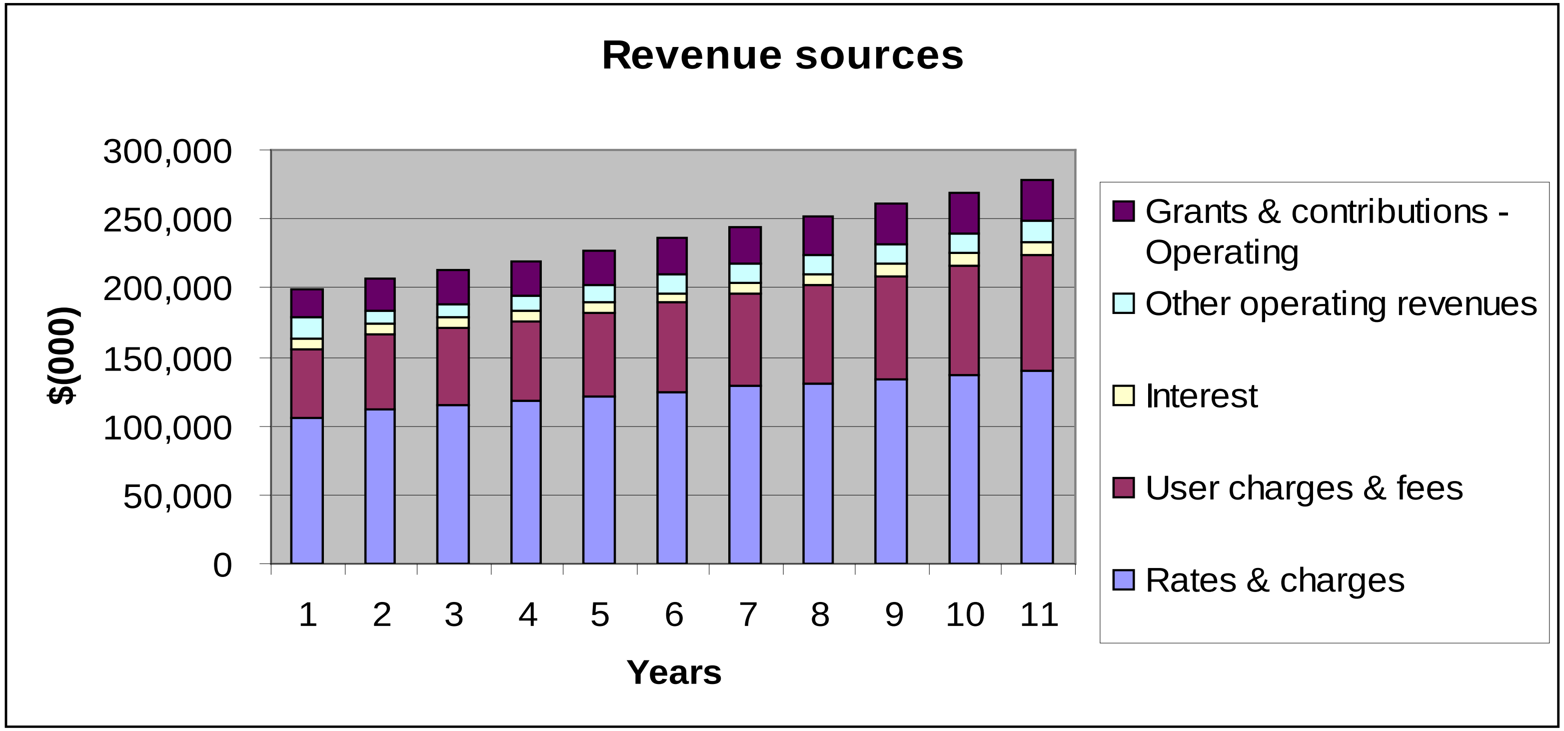
- User fees and charges have increased by 5.6% in 2011 after remaining static in 2010. The main sources of fee revenue in 2011 are tipping fees at $17.6 million and Newcastle Airport revenue at $10.3 million. These increased by $1.0 million and $1.6 million respectively in 2011.

- Interest revenue excluding realised revaluation reserves increased to $12.0 million in 2011, an increase of 25.5% since 2009 due to higher average interest rates and a $30.9 million increase in cash holdings.

- Other revenue of $6.6 million in 2011 includes parking fines of $2.4 million and rental income from investment and other properties of $2.6 million.

- Grants and contributions for operating purposes have increased by 30.8% over the period from 2009 to 2011. In 2011, operating grants and contributions increased by $5.1 million largely due to a once off Natural Disaster Grant of $3.3 million and an increase of $1.0 million in the general purpose Financial Assistance Grant provided by the Federal Government.

Revenue Forecast

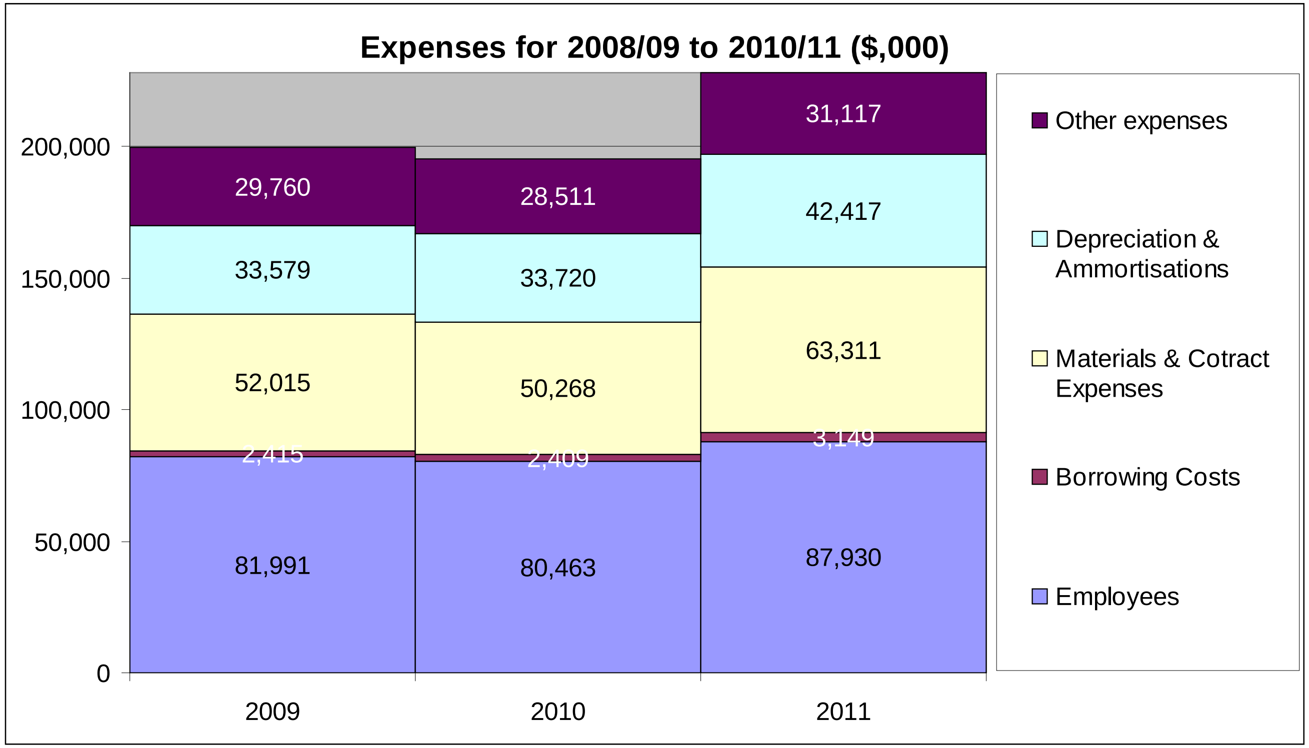


City of Newcastle Expenditure position

From **operating expenditure** side the following has been recognised:

- Employee Costs
- Borrowing Costs
- Depreciation
- Materials and Contracts
- Other operating Expenses

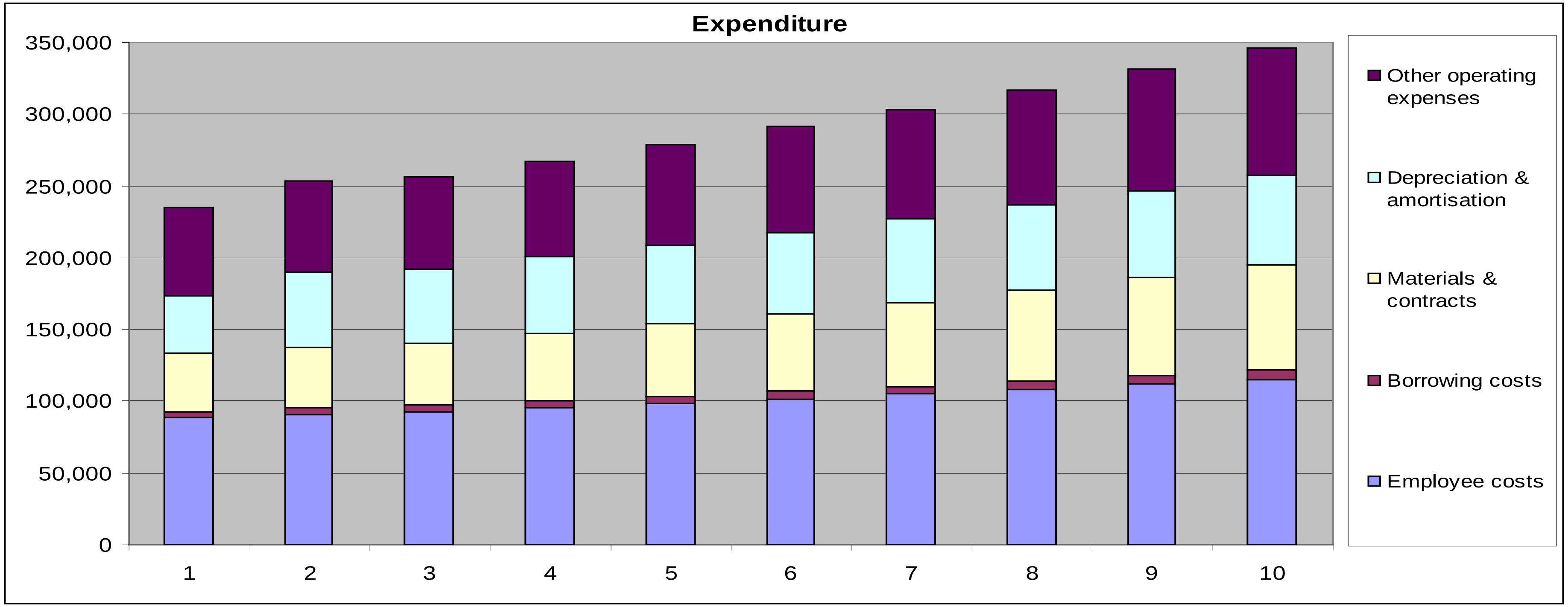
Expenditure History



Key Observations

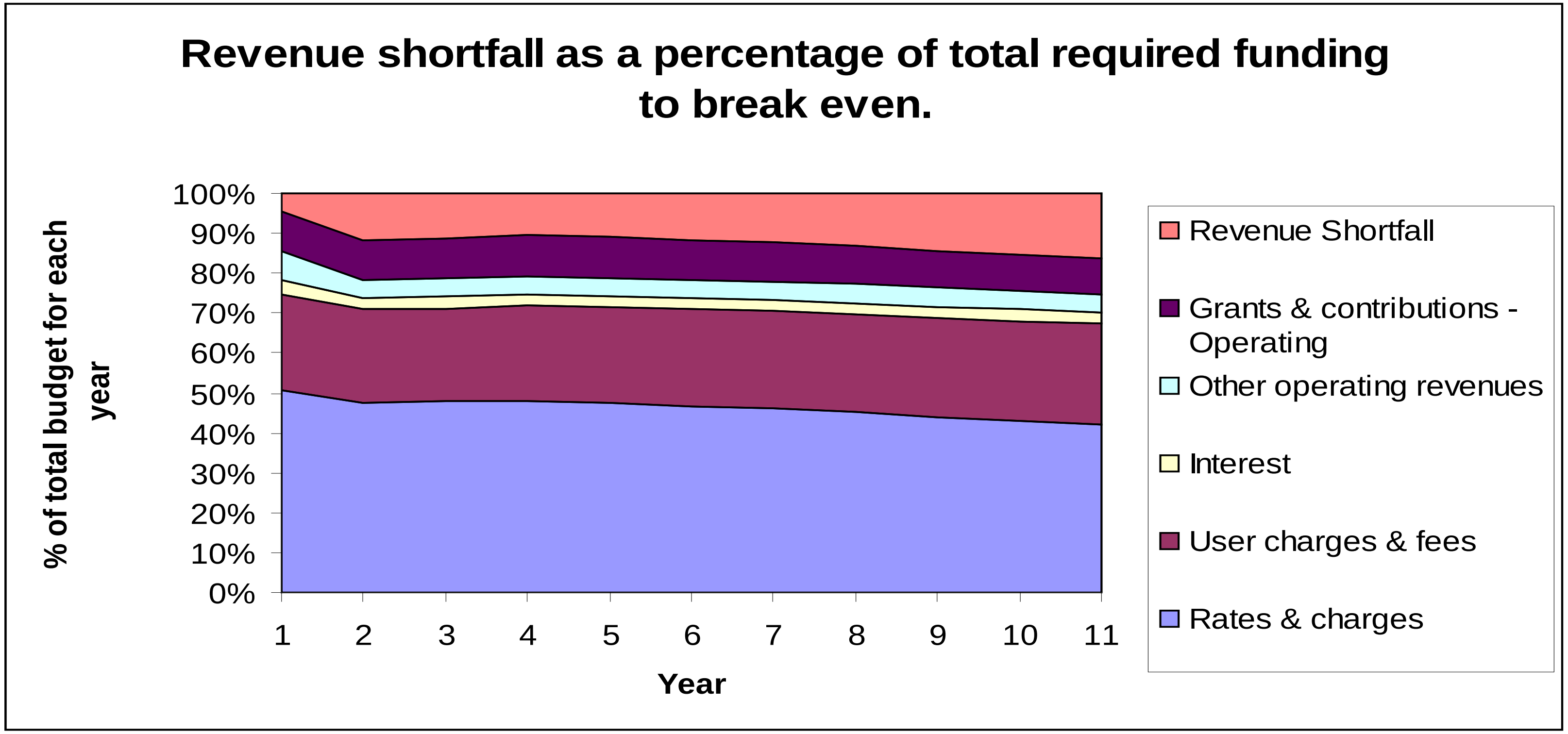
- Employee costs are the largest expense being 38.6% of total expenses in 2011. Employee costs increased 9.3% in 2011 despite a decline in employee headcount from 938 to 926 driven by a rise in salaries and wages of $3.6 million, workers compensation insurance of $1.8 million, employee leave entitlements of $1.4 million and superannuation of $0.8 million.
- Materials and contracts expenses have increased by 21.7% from 2009 to 2011 driven by the 2011 increase of $11.1 million in raw materials and consumables largely attributable to the Major Asset Preservation Program (MAPP) initiated in that year. The MAPP consists of 630 projects covering roads, buildings and structures and the environment with a total project expenditure of $28.5 million.
- Depreciation increased by 25.8% in 2011 following the Asset Revaluations. The increase in road, bridges and footpath infrastructure asset depreciation amounted to $7.5 million.

Expenditure Forecast



Overall Operating Result Key Observations

The graph below shows the revenue shortfall each year as a percentage of the total funding required to balance the budget. As can be observed the funding shortfall is not only getting bigger in real terms it is also larger in terms of the percentage required to balance the budget.



TCorp's observations are as follows:

- Council's net operating result excluding capital grants and contributions has been in deficit over the last three years. The largest deficit in 2011 was due to a 16.7% increase in operating expenses against a 7.7% rise in operating revenue.
- The increase in operating expenses was driven by increases in materials and contract expenses as part of the MAPP, increased employee costs and the higher depreciation charges.
- Council expenses include a non-cash depreciation expense, ($42.4 million in 2011), which has increased by $8.8 million over the past three years following the Asset Revaluations process. Whilst the non cash nature of depreciation can favourably impact on ratios such as EBITDA that focus on cash, depreciation is an important expense as it represents the allocation of the value of an asset over its useful life.

Financial Management Indicators

TCorp measured the following performance indicators:

Performance Indicators	Year ended 30 June		
	2011	**2010**	**2009**
EBITDA ($'000s)	21,099	29,659	19,566
Interest Cover Ratio	6.70x	12.32x	9.07x
Debt Service Cover Ratio	3.18x	5.45x	5.24x
Unrestricted Current Ratio	2.88x	2.99x	2.43x
Own Source Operating Revenue Ratio	70.6%	74.7%	70.0%
Cash Expense Ratio	2.1 months	1.4 months	2.5 months
Net assets ($'000s)	1,400,991	1,734,589	1,565,452

- EBITDA, a measure of Council's underlying performance, increased marginally between 2009 and 2011 after a strong result in 2010. The 2010 result was due to a combination of increased revenues (3.0%) and a reduction in expenses of 2.2% whereas the 2011 result was impacted by increased revenues of 7.7% being offset by a 16.7% increase in expenses. The $20.5 million increase in employee costs, and material and contract expenses were the main drivers of the increased expenses.
- In 2011, the Interest Cover Ratio and the DSCR remain above benchmark indicating the Council has flexibility in regard to carrying further debt although this flexibility is reducing due to increased levels of debt.
- Council's total borrowing shows an increasing trend rising from $38.7 million in 2009 to $53.4 million in 2011, representing 3.8% of net assets.
- The Unrestricted Current Ratio has remained well above the target level of 1.50x over the last three years indicating the Council has had sound liquidity.
- Council's Own Source Operating Revenue Ratio is above the 60.0% benchmark by a minimum of 10.0% over the three years indicating that Council has a sufficient level of fiscal flexibility.
- The Cash Expense Ratio is below the benchmark in all three years however Council utilises the majority of their funds in term deposits and FRNs classified under current investments.
- Net assets declined from $1,734.6 million in 2010 to $1,401.0 million in 2011 due to the Asset Revaluations that resulted in revaluation decrements of $375.1 million in community land, and $20.6m decline in other structures (this was slightly offset by an increase in Council's heritage collection by $51.3 million). Asset values had increased in 2010 from 2009 by $153.5 million from the revaluation of road, bridge, footpath and drainage infrastructure assets.
- When the Asset Revaluations are excluded, there has been marginal rise in the IPP&E asset base of $8.4 million across the three year period.

The table below provides a forecast reflecting these Operating Revenues and Expenses. The depreciation figures have been removed from the analysis for the moment and will be analysed separately.

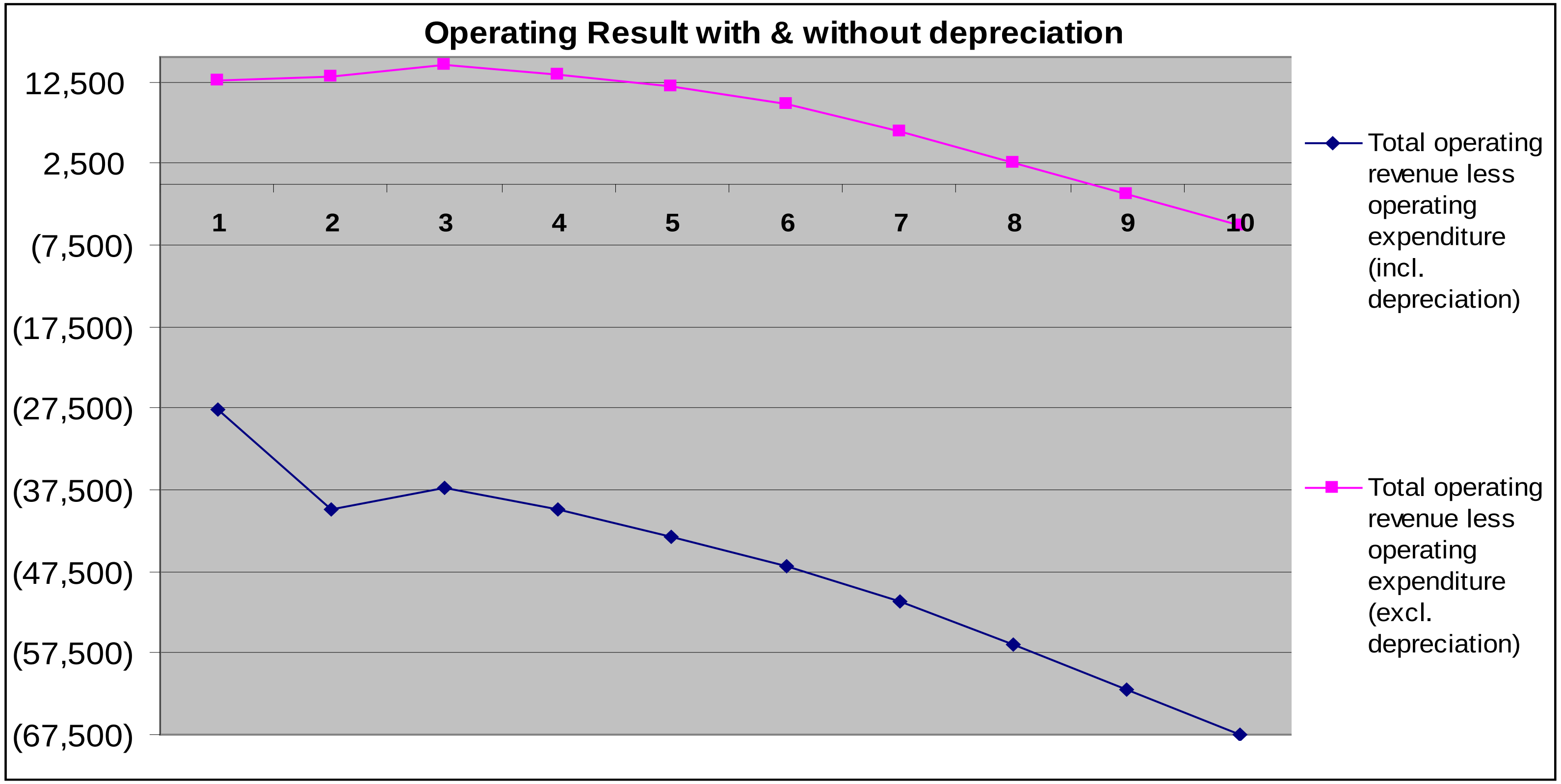
Income and Expenditure Statement												***NCC - Long Term Financial Plan***
For the year ended 30 June	***Notes***	***2011/12 $'000***	***2012/13 $'000***	***2014 $'000***	***2015 $'000***	***2016 $'000***	***2017 $'000***	***2018 $'000***	***2019 $'000***	***2020 $'000***	***2021 $'000***	***2022 $'000***
Operating Revenue												
Rates & charges		107,020	111,544	115,306	118,535	121,498	125,143	128,772	131,734	134,368	137,392	140,689
User charges & fees		53,363	55,198	56,413	57,971	61,045	64,281	67,688	71,277	75,055	79,034	83,224
Interest		11,796	6,849	6,858	6,636	6,967	7,316	7,681	8,066	8,469	8,892	9,337
Other operating revenues		8,294	10,195	10,592	11,790	12,277	12,784	13,311	13,861	14,433	15,029	15,649
Grants & contributions - Operating		30,724	23,706	24,419	24,998	25,798	26,597	27,262	27,862	28,545	29,287	30,048
Total Operating Revenue		211,197	207,490	213,587	219,930	227,585	236,120	244,716	252,799	260,870	269,634	278,948
Operating Expenses												
Employee costs		89,558	88,453	90,905	92,292	95,291	98,388	101,586	104,887	108,296	111,816	115,450
Borrowing costs		3,922	3,925	4,517	5,107	5,270	5,434	5,570	5,692	5,832	5,983	6,139
Materials & contracts		54,864	41,071	41,896	43,009	46,450	50,166	54,179	58,514	63,195	68,250	73,710
Other operating expenses		30,647	61,411	62,643	64,606	66,674	69,878	73,237	76,757	80,446	84,313	88,365
Total Operating Expenses		178,991	194,859	199,961	205,014	213,685	223,866	234,572	245,850	257,769	270,362	283,664
Total Operating Revenue Less Operating Expenditure		32,206	12,631	13,626	14,915	13,899	12,254	10,144	6,949	3,101	(728)	(4,717)

From the above it can be seen that when depreciation is taken out, our current operating revenue to expense position is strong. **The problem is that it declines rapidly.**

Adding back in deprecation the following table illustrates the impact of this non cash item:

Income and Expenditure Statement												***NCC - Long Term Financial Plan***
For the year ended 30 June	***Notes***	***2011/12 $'000***	***2012/13 $'000***	***2014 $'000***	***2015 $'000***	***2016 $'000***	***2017 $'000***	***2018 $'000***	***2019 $'000***	***2020 $'000***	***2021 $'000***	***2022 $'000***
Operating Revenue												
Rates & charges		107,020	111,544	115,306	118,535	121,498	125,143	128,772	131,734	134,368	137,392	140,689
User charges & fees		53,363	55,198	56,413	57,971	61,045	64,281	67,688	71,277	75,055	79,034	83,224
Interest		11,796	6,849	6,858	6,636	6,967	7,316	7,681	8,066	8,469	8,892	9,337
Other operating revenues		8,294	10,195	10,592	11,790	12,277	12,784	13,311	13,861	14,433	15,029	15,649
Grants & contributions - Operating		30,724	23,706	24,419	24,998	25,798	26,597	27,262	27,862	28,545	29,287	30,048
Total Operating Revenue		211,197	207,490	213,587	219,930	227,585	236,120	244,716	252,799	260,870	269,634	278,948
Operating Expenses												
Employee costs		89,558	88,453	90,905	92,292	95,291	98,388	101,586	104,887	108,296	111,816	115,450
Borrowing costs		3,922	3,925	4,517	5,107	5,270	5,434	5,570	5,692	5,832	5,983	6,139
Materials & contracts		54,864	41,071	41,896	43,009	46,450	50,166	54,179	58,514	63,195	68,250	73,710
Depreciation & amortisation	1	55,168	57,000	57,000	57,000	58,824	60,648	62,164	63,531	65,088	66,780	68,516
Other operating expenses		30,647	61,411	62,643	64,606	66,674	69,878	73,237	76,757	80,446	84,313	88,365
Total Operating Expenses		234,159	251,859	256,961	262,014	272,509	284,514	296,735	309,382	322,857	337,142	352,181
Total Operating Revenue Less Operating Expenditure		(22,962)	(44,369)	(43,374)	(42,085)	(44,925)	(48,393)	(52,020)	(56,583)	(61,986)	(67,509)	(73,233)

The above table is shown below in graphical form:



The graph above outlines the impact of these forecasts on the operating surplus/deficit without depreciation (depicted as the pink line) and operating surplus/deficit with depreciation (depicted as the blue line)

As can been seen from the graph the total operating position is declining rapidly under the LTFP model. **Expenditures are rapidly outstripping operating revenues**.

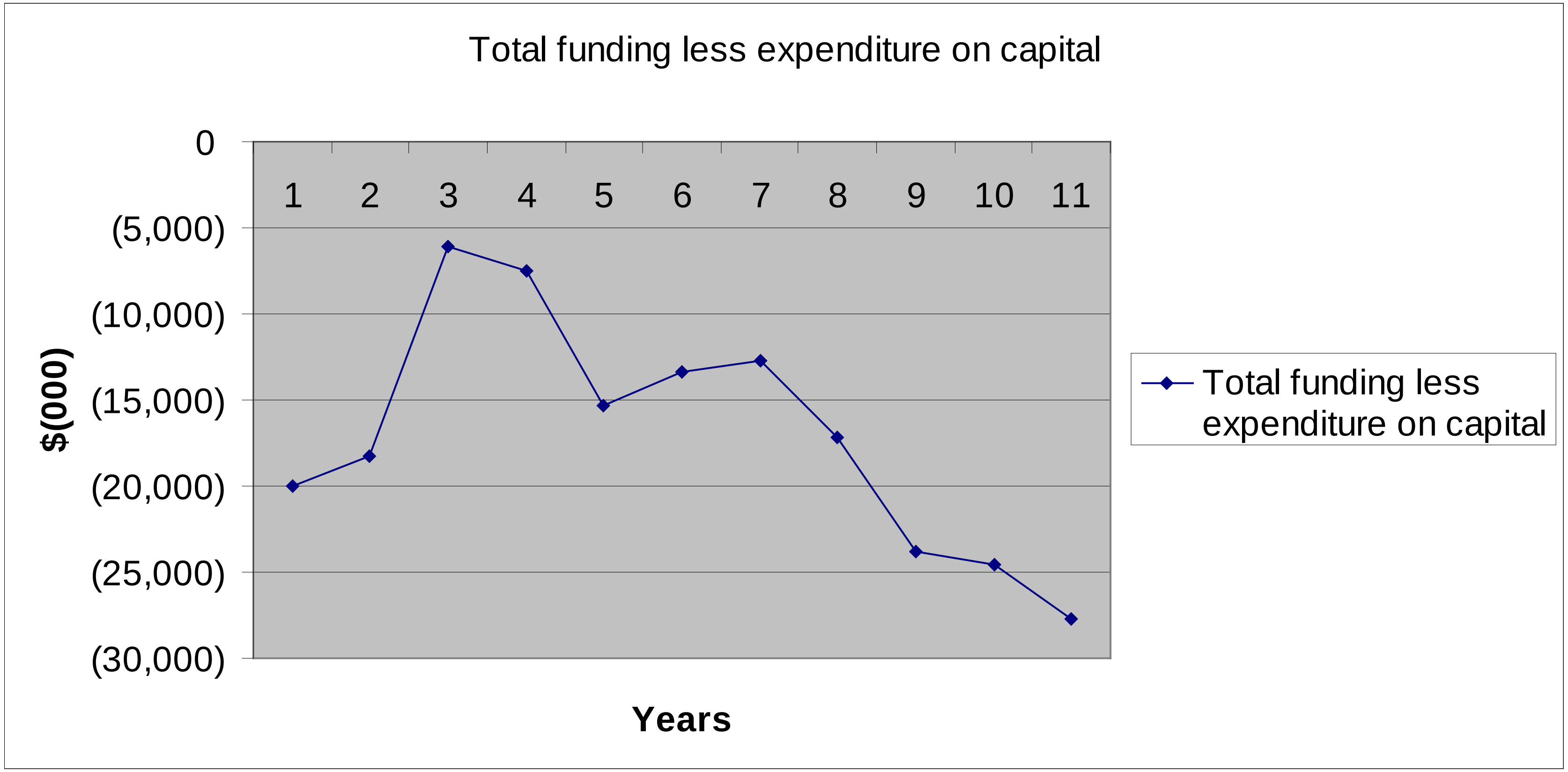
Also it is evident that the underlying operating position is progressively deteriorating to a point in **2021 when it goes into a negative number. This positional change is approximately $34.7 million over 10 years.**

4.2 The City of Newcastle Capital Result

The table below shows that **capital expenditure is outstripping council's capital revenue** (before adding back in depreciation).

It is evident **that Council's strong operating position, before depreciation, is being consumed to fund capital expenditure on assets**. A combination of Councils operating expenditures rising at a greater rate than operating revenues and a large capital expenditure budget insufficiently funded by revenues is causing a double negative impact on the organisation.

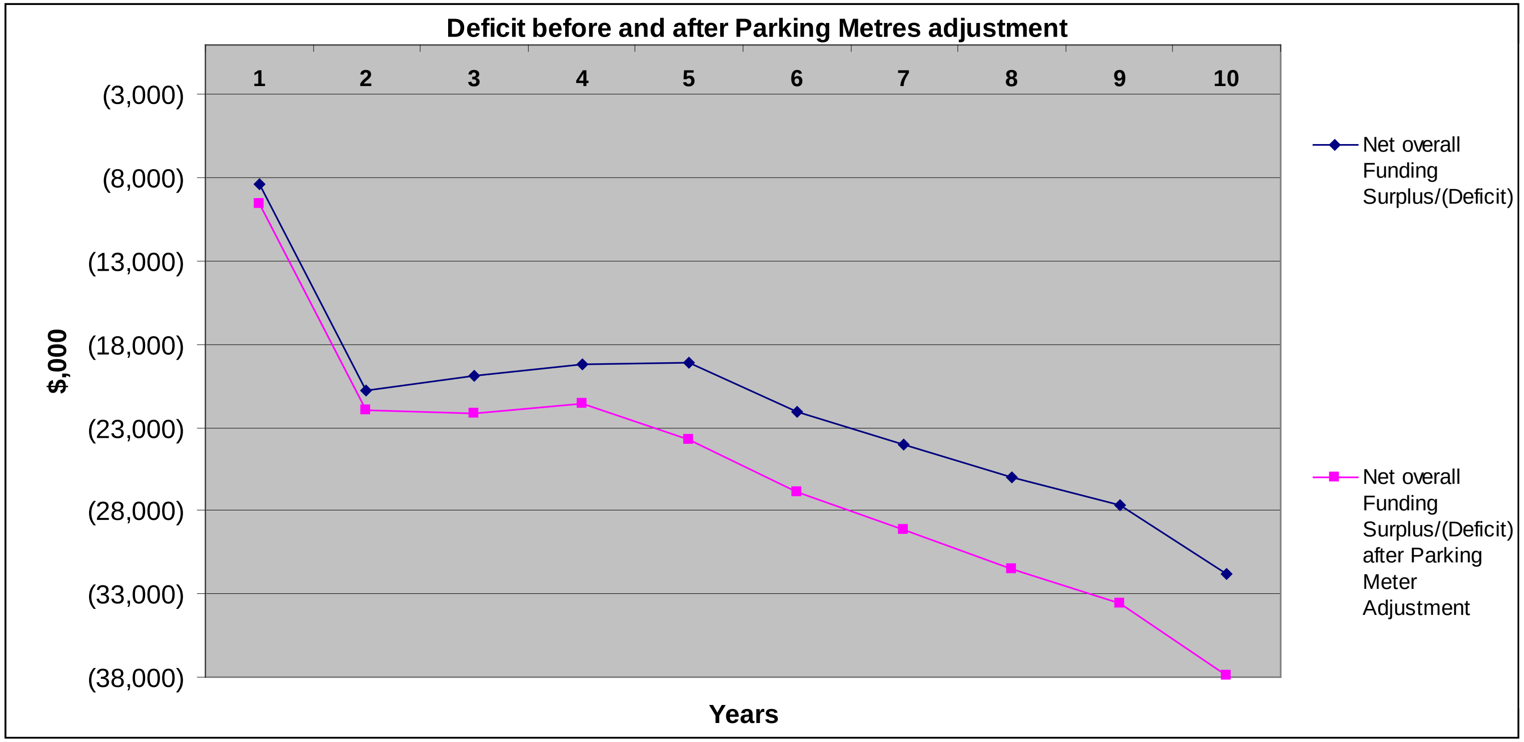
For the year ended 30 June	*Notes*	*2011/12 $'000*	*2012/13 $'000*	*2014 $'000*	*2015 $'000*	*2016 $'000*	*2017 $'000*	*2018 $'000*	*2019 $'000*	*2020 $'000*	*2021 $'000*	*2022 $'000*
Capital Revenues												
Grants & contributions - Capital	2	11,017	9,079	6,781	6,828	6,958	7,081	7,183	7,275	7,380	7,493	7,610
Proceeds from the sale of Assets		(374)	3,006	949	1,292	2,311	1,846	983	1,229	1,862	1,806	1,485
Total Capital Raising revenue		10,643	12,085	7,729	8,120	9,269	8,927	8,166	8,504	9,242	9,300	9,095
Nett Suplus(deficit) after capital revenue		(12,319)	(32,284)	(35,644)	(33,965)	(35,655)	(39,466)	(43,854)	(48,078)	(52,745)	(58,209)	(64,138)
Add back Depreciation		55,168	57,000	57,000	57,000	58,824	60,648	62,164	63,531	65,088	66,780	68,516
Funding available for capital expenditure		42,849	24,716	21,356	23,035	23,169	21,181	18,310	15,453	12,343	8,571	4,379
Capital Expenses												
Capital Expenditure on Asset renewals	3	57,150	42,947	39,767	41,687	49,936	46,402	43,188	44,997	48,857	46,209	45,489
Total capital spend on renewals		57,150	42,947	39,767	41,687	49,936	46,402	43,188	44,997	48,857	46,209	45,489
Total Funding less expenditure on Capital		**(14,301)**	**(18,230)**	**(18,412)**	**(18,652)**	**(26,768)**	**(25,221)**	**(24,878)**	**(29,544)**	**(36,514)**	**(37,637)**	**(41,111)**


Total funding less expenditure on capital
0
(5,000)
(10,000)
(15,000)
(20,000)
(25,000)
(30,000)
$(000)
1
2
3
4
5
6
7
8
9
10
11
Years
Total funding less expenditure on capital

4.3 The City of Newcastle - overall financial result

The Nett overall position is declining over the next 10 years based on a Profit and Loss statement. The before and after position of the parking metre expansion decision made by Council is illustrated in the table and graph below:

For the year ended 30 June	*Notes*	*2011/12 $'000*	*2012/13 $'000*	*2014 $'000*	*2015 $'000*	*2016 $'000*	*2017 $'000*	*2018 $'000*	*2019 $'000*	*2020 $'000*	*2021 $'000*	*2022 $'000*
Net Overall Funding Surplus/(Deficit)		**5,732**	**(8,376)**	**(20,210)**	**(19,450)**	**(18,801)**	**(18,643)**	**(21,606)**	**(23,533)**	**(25,548)**	**(27,204)**	**(31,338)**
Parking Meter Adjustments												
Halt Meter Expansion and No Weekend Meters City East and City West	**5**		1,143	1,128	2,312	2,324	4,582	4,850	5,132	5,440	5,868	6,044
Net Overall Funding Surplus/ (Deficit) after Parking Meter Adjustments		5,732	(9,519)	(21,339)	(21,762)	(21,125)	(23,224)	(26,456)	(28,665)	(30,988)	(33,072)	(37,382)

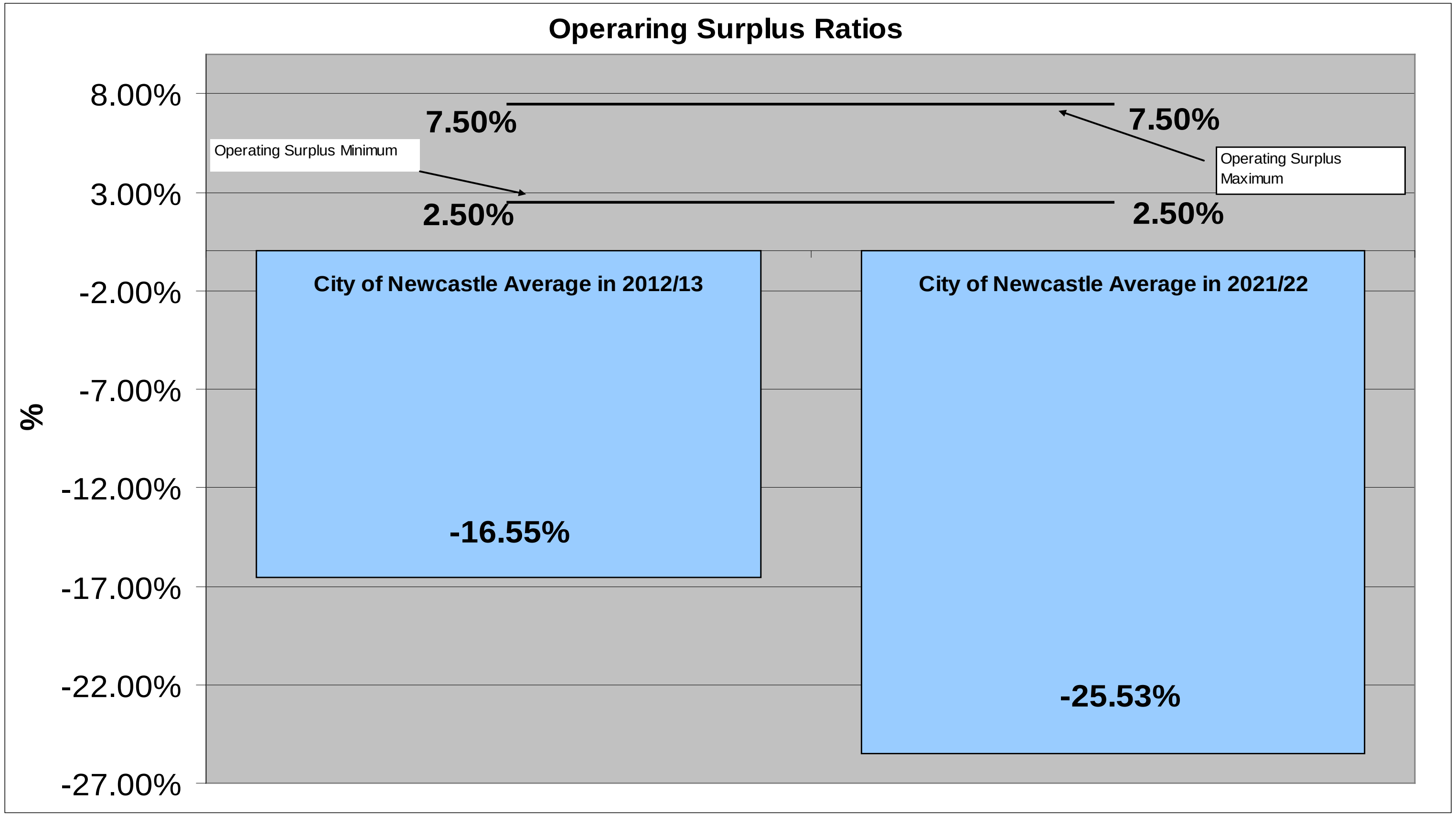


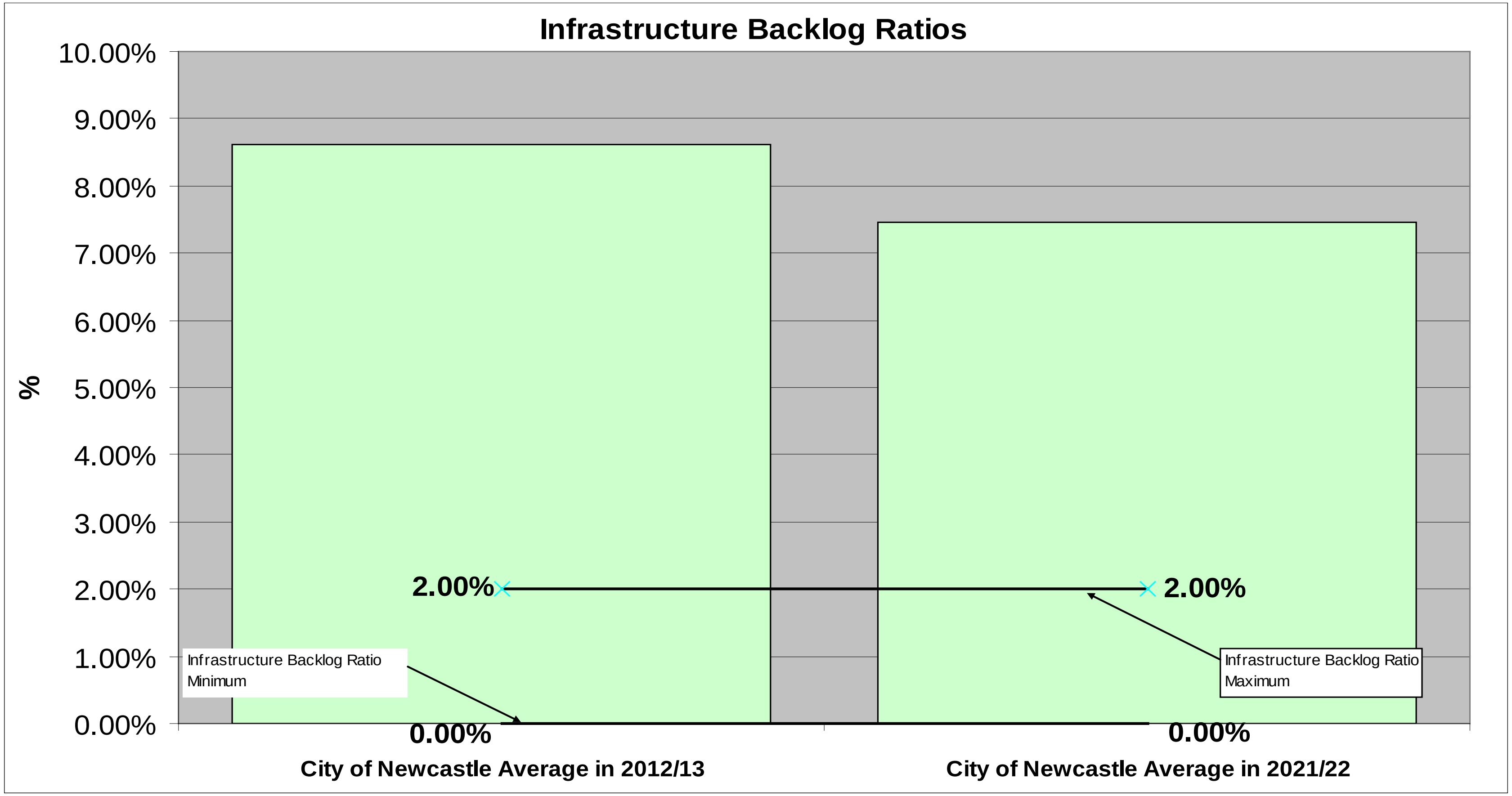
From the graph above, the deficit line moves from minus $9.5 million to $37.38 million within the 10 years or approximately $3 million per year average.

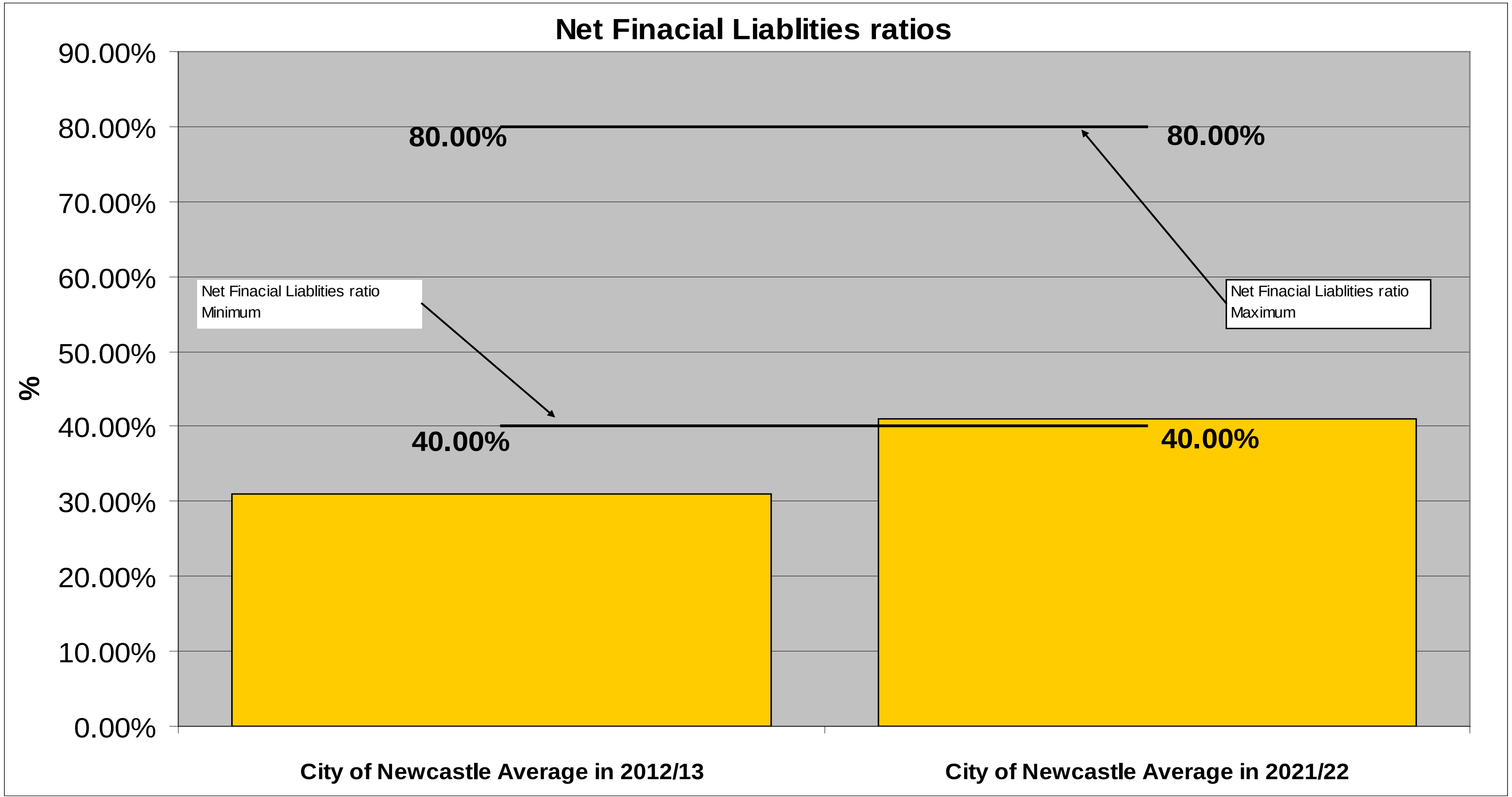
Based on the FiscalStar Sustainability analysis, The City of Newcastle shows the following results:

Sustainability Indicator	Sustainable Benchmark (lower)	Sustainable Benchmark (upper)	City of Newcastle Average in 2012/13	City of Newcastle Average in 2021/22	Percentage change from 2012/13 to 2021/22
Operating Surplus	2.50%	7.50%	-16.55%	-25.53%	-54.24%
Infrastructure backlog ratio	0%	2.00%	8.61%	7.5%	13.42%
Net financial liabilities ratio	40%	80%	31.05%	41%	-31.89%

These are graphed below:




Infrastructure Backlog Ratios
10.00%
9.00%
8.00%
7.00%
6.00%
5.00%
4.00%
3.00%
2.00%
1.00%
0.00%
%
2.00%
2.00%
Infrastructure Backlog Ratio Minimum
Infrastructure Backlog Ratio Maximum
0.00%
0.00%
City of Newcastle Average in 2012/13
City of Newcastle Average in 2021/22



TCorp benchmarked TCoN against 10 benchmark ratios outlined in **Appendix D**.

5. What is causing this problem for Council?

5.1 The Infrastructure Backlog

Infrastructure needs to be:

- Maintained (ie routine repairs)
- Renewed (refurbished or replaced when it deteriorates to an unacceptable level), or
- Enhanced (ie expanded beyond its original capacity)

The backlog is the number and value of assets falling beyond the intervention levels, these assets are in a deteriorated or unacceptable level.

How big is our backlog?

The City of Newcastle has $1.6 billion of Infrastructure, property, plant equipment and investment property on its balance sheet. This equates to a significant amount of infrastructure to replace and maintain, placing considerable pressure each year on Council resources to fund degraded assets.

In 2007 Professor Percy Allan and GHD evaluated that The City of Newcastle had a renewal and maintenance backlog of $134 million. During this time Council spent $12.2 million per year on consequential maintenance and a further $12.1 on asset renewal (total $24.3 million). Based on this policy it was concluded that with Council's existing spending policy that maintenance cost would exceed renewal costs, suggesting under investment in renewals resulting in further degradation and rising costs to maintain. If Council continued this policy from 2007, by 2027 the infrastructure backlog would be $475.1 million (an increase of $341 million).

How was this calculated?

Firstly assets are separated into **asset groups** (eg wearing surfaces or pavements). For each group a condition is determined using a 10 point scale where assets fall below the intervention level on the 10 point scale prescribed for the group.

What should we have spent on infrastructure or asset backlog?

GHD recommended in 2007 we spend:

- **$36.4 million on asset renewal**
- **$8.7 million on consequential maintenance**
- **Total $45.1 million per year**

This would have reduced the asset backlog to zero in five years. After the backlog is reduced then Council should spend $12.5 million thereafter.

This and our current asset backlog is outlined in the table below by asset class.

Asset Class	Asset Category	Asset Condition	Renewals and maitenace backlogs in 2007 (Percy Allan) $'000	Estimated cost to bring to a satisfactory standard (2011) $'000	Estimated cost to bring to a satisfactory standard (2012) $'000	Required Annual Maintenance Expense $'000	Current Annual Maintenance $'000	shortfall(required less current) $'000
Buildings & Structures	Buildings Long Life			70,580	75,505		5,303	
	Buildings Short Life			658	18		810	
	Building Services			12,500	12,500		4,115	
	Retaining Walls			448	448		1,073	
	River Walls			1098	1,097		938	
	Total		**73,000**	**85,284**	**89,568**	**27,053**	**12,239**	**14,814**
Public Roads	Wearing Surface - Regional						618	
	Pavement - Regional						277	
	Wearing Surface - Local			6757	6,792		5,900	
	Pavement - Local			4125	4,173		2,570	
	Footpath - Local			2349	2,380		2,974	
	Kerb & Gutter - Local			27	27		1,873	
	Bridges & Culverts - Local			134	134		92	
	Total		**19,500**	**13,392**	**13,506**	**15,914**	**14,304**	**1,610**
Drainage Works	Stormwater Pits				182		426	
	Stormwater Pipes & Culverts			14,077	14,076		675	
	Total		**33,100**	**14,077**	**14,258**	**3,183**	**1,101**	**2,082**
Natural Assets			**8,000**	**8,000**	**8,000**	**8,000**	**8,000**	**0**
recreational assets			**400**	**400**	**400**	**400**	**400**	**0**
cultural assets			**100**	**100**	**100**	**100**	**100**	**0**
Total Classes	**Total - All Assets**		**134,100**	**121,253**	**125,832**	**54,650**	**36,144**	**18,506**

What do we currently spend?

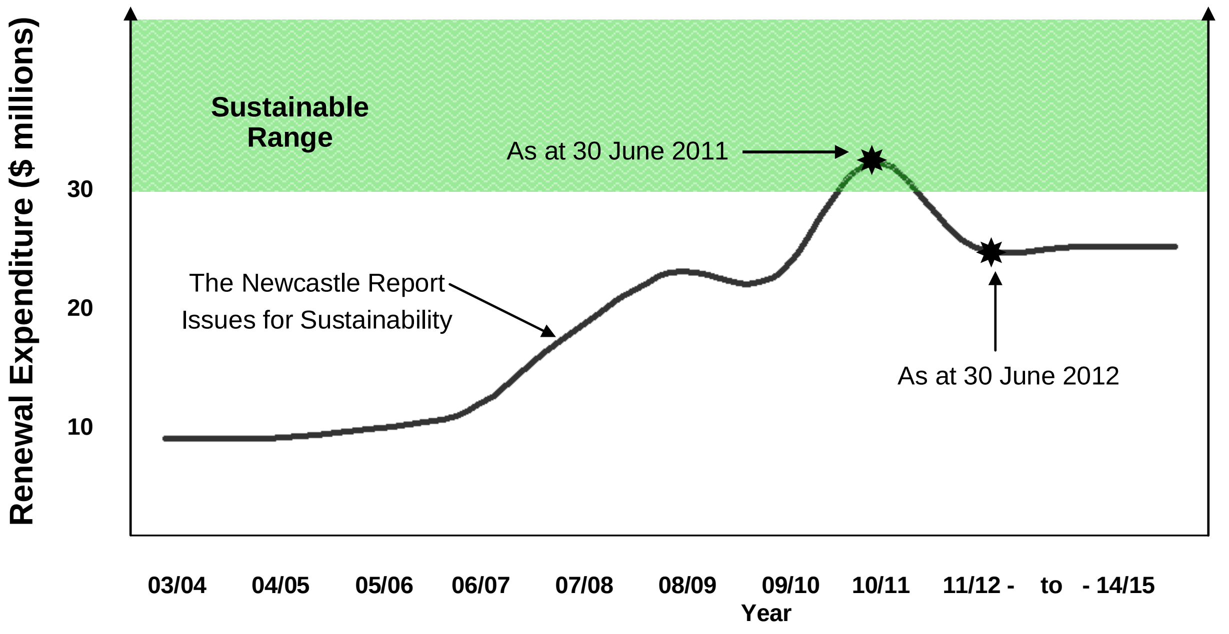
The renewal program is shown below. Projected expenditure for each program for the 10 year financial period is shown below:

For the year ended 30 June renewals expenditure	***2011/12 $'000***	***2012/13 $'000***	***2014 $'000***	***2015 $'000***	***2016 $'000***	***2017 $'000***	***2018 $'000***	***2019 $'000***	***2020 $'000***	***2021 $'000***	***2022 $'000***
Capital Expenditure on Asset renewals	57,150	42,947	39,767	41,687	49,936	46,402	43,188	44,997	48,857	46,209	45,489
Total capital spend on renewals	57,150	42,947	39,767	41,687	49,936	46,402	43,188	44,997	48,857	46,209	45,489

To fund the major asset preservation program and reduce the $134 million infrastructure backlog, Council has increased borrowings to $10 million per annum. The balance of borrowings at 30 June 2011 is estimated at $47 million.

The following graph shows the amount of renewal required in order to maintain assets within the sustainable range. This is shown in green. The amount of funding provided to this task is shown by the line for the years 2003 to 2015. Whilst spending enough to remain sustainable in 2010/2011, this amount has dropped back due to budget shortfalls.

Condition of Public Works



5.2 The Rate Cap

In 2011/12 TCoN raised the following **ordinary rates:**

Rate	*2011/12*	*% Increase 201/11 to 20111/12*	*Number of rate payers 2010/11*	*Number of rate payers 2011/12*	*Increase (decrease) in rate payer number 2011 to 2012*	*Average $ increase(decrease) per rate payer year 2011 to 2012*
Residential	$54,105,121	3.50%	59,748	60,259	511	$23
Farmland	$27,364	-2.30%	17	18	1	-$126
Business	$33,288,323	2.20%	4,726	4,734	8	$141
TOTAL Ordinary rates	**$87,828,060**	**3.50%**	**64,491**	**65,011**	**520**	

In 2011/2012 TCoN raised the following **Special rates for Business Improvement Associations (BIAs):**

Rate	*2011/12*	*% Increase 201/11 to 20111/12*	*Number of rate payers 2010/11*	*Number of rate payers 2011/12*	*Increase (decrease) in rate payer number 2011 to 2012*	*Average $ increase per rate payer year 2011 to 2012*
Town Improvement	$76,316	10.60%	55	55	0	$133
Main street	$1,065,426	6.60%	1,475	1,467	-8	$49
TOTAL Special Rates	**$1,141,742**	**6.80%**	**1,530**	**1,522**	**-8**	

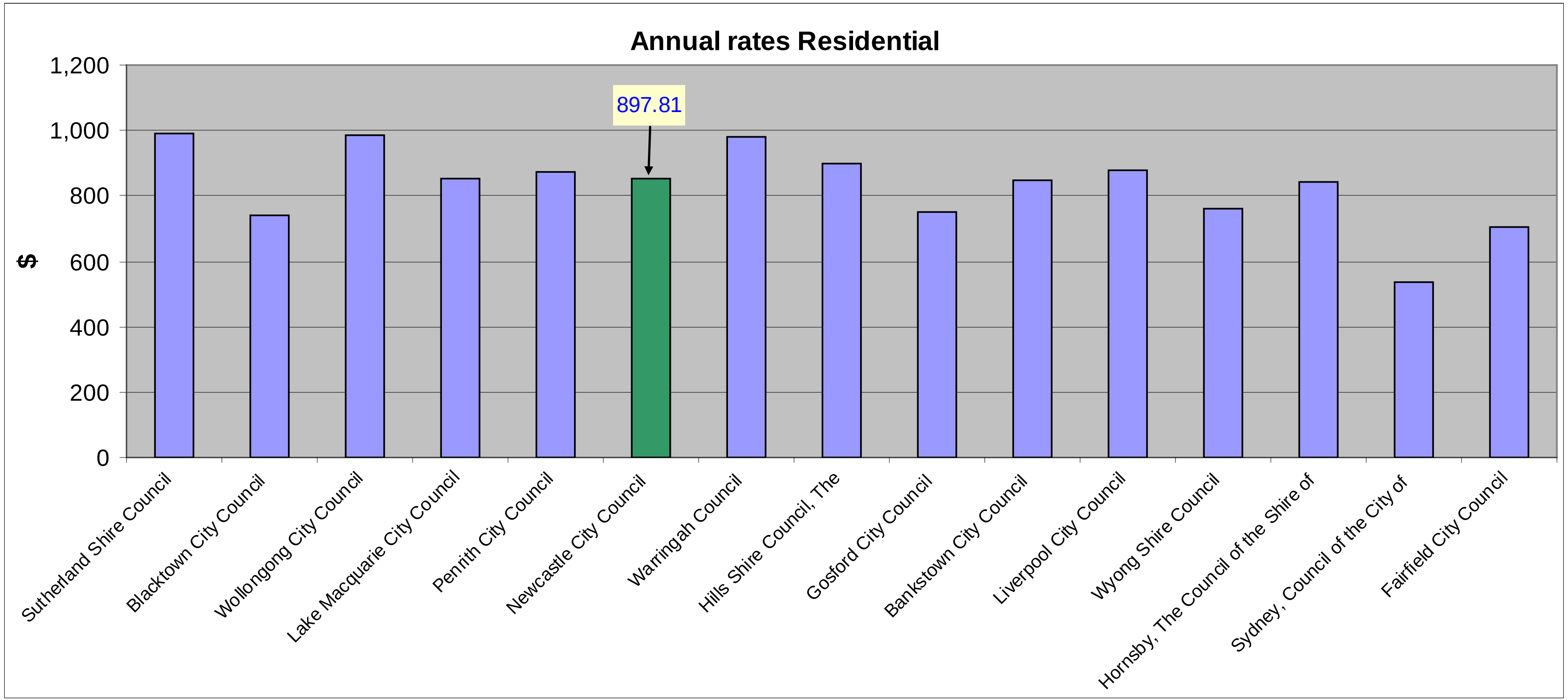
Comparison of Rates

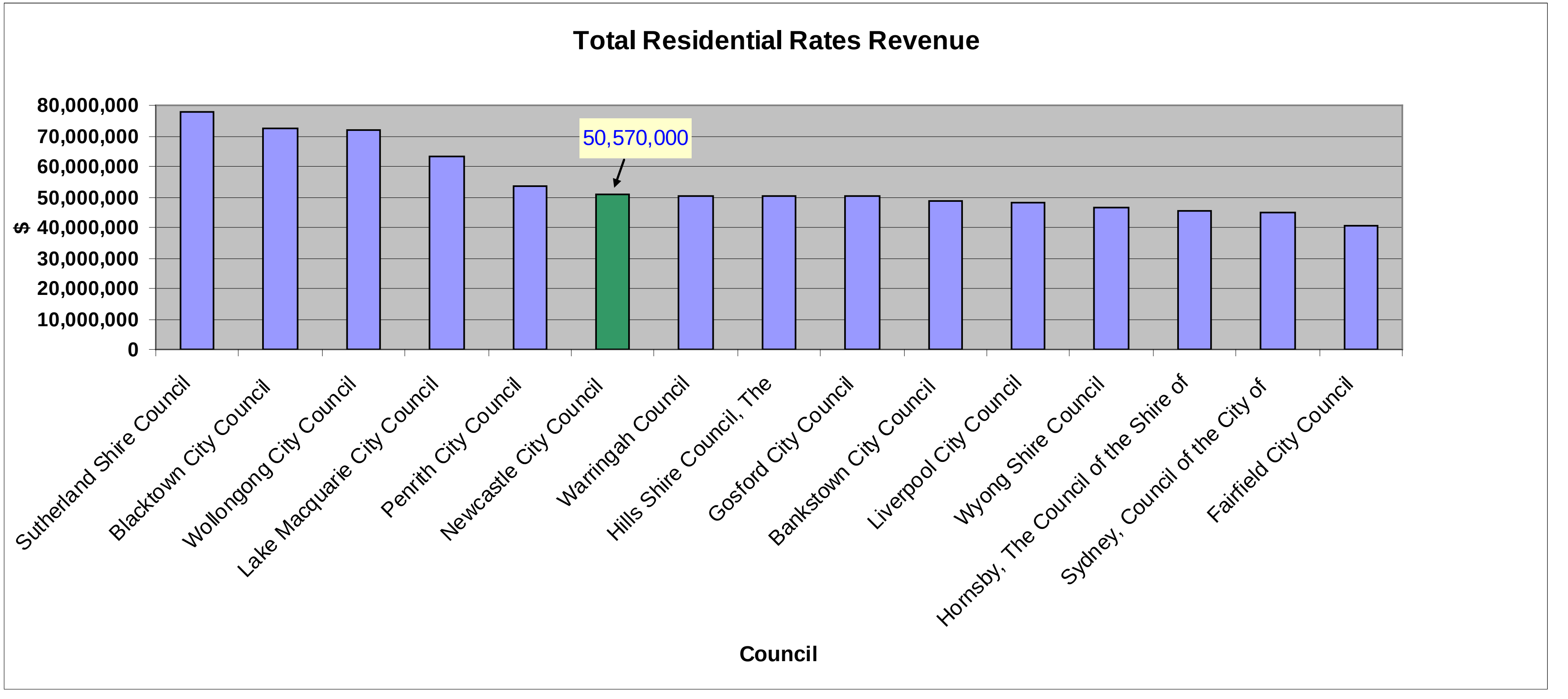
The following table **compares** The City of Newcastle **actual rates with what they could have been if the average increases of other states had been applied** over the last 10 years. The average rate from all States (other than NSW) average annual increase was 7.975%.

Year	Actual Revenue raised by the City of Newcastle through rates	Potential revenue raised if the rate allowable each year was 7.975%	Total rates income forgone
2001/02	$64 m	$64 m	$0
2010/11	$85 m	$138 m	$53 m
Total for the period	$680 m	$1,000 m	$320 m

The table below compares other Group 5 Councils with Newcastle.

Council	Group	Total Residential Rates Revenue	Rateable Residential Properties	Result
Wollongong City Council	5	71,744,000	72,674	$987.20
Tweed Shire Council	5	33,348,000	35,036	$951.82
Lake Macquarie City Council	5	63,435,000	74,215	$854.75
Newcastle City Council	**5**	**50,570,000**	**59,368**	**$851.80**
Coffs Harbour City Council	5	20,352,000	27,714	$734.36
Shoalhaven City Council	5	38,066,000	51,884	$733.68


Annual rates Residential
$
1,200
1,000
800
600
400
200
0
897.81
Sutherland Shire Council
Blacktown City Council
Wollongong City Council
Lake Macquarie City Council
Penrith City Council
Newcastle City Council
Warringah Council
Hills Shire Council, The
Gosford City Council
Bankstown City Council
Liverpool City Council
Wyong Shire Council
Hornsby, The Council of the Shire of
Sydney, Council of the City of
Fairfield City Council



The National Framework

Council indicators for a National Framework have proposed that the following be considered by Councils when analysing rates:

- **Where adopted rate increases that have fluctuated substantially; and**
- **Where rates are at a level that are considerably different to the group median of comparable councils, particularly where councils indicate a long term inability to maintain and renew assets, have persistent underlying operating deficits, and significant debt.**

TCoN rates have not fluctuated greatly over the last 10 years. According to IPART, when compared to other NSW Councils our SRV history has been minimal. In comparing TCoN rates with other Councils the second dot point above describes well the key issues for this Council.

5.3 Impacts on Other Revenues

Waste management service charges

Council is required by legislation to levy annual charges for the provision of waste management services.

Domestic Waste Management Service Charge (DWMSC) – Section 496 of the Local Government 1993 (the Act) requires Council to make and levy an annual charge for the recovery of costs for providing domestic waste management services. For 2011/2012 Council is implementing a number of options aimed at decreasing the amount of waste moved to landfill and increasing recycling across the local government area.

Business Waste Management Service Charge (BWMSC) – Section 501(1) of the Act requires Council to make and levy an annual charge for the provision of waste management services (other than domestic waste management services).

The DWMSC for 2012/13 is expected to reach $7.8 million.

User Charges and Fees

Council's Fees and Charges policy states that all Council fees and charges, not subject to statutory control, are to be reviewed annually before finalising the annual Operational Plan.

The predominant consideration in reviewing fees and charges is full cost recovery on a fee for service (user pays) basis. This principle is only applied where the cost of service provision can be accurately determined and the end user can be easily identified.

Where the user pays principle cannot be applied to determine the fee or charge the alternative is based on the:

- Cost of Council providing the service
- Fee suggested for that service by any relevant body or in any schedule of charges published by the Division of Local Government
- Importance of the service to the community
- Factors specified in the regulations
- Projected CPI increase for the period
- Competitiveness of fees and charges in comparison with those charged by other organisations.

The **table below** outlines the user's fees and charges for 2011/2012.

The significant fees are:

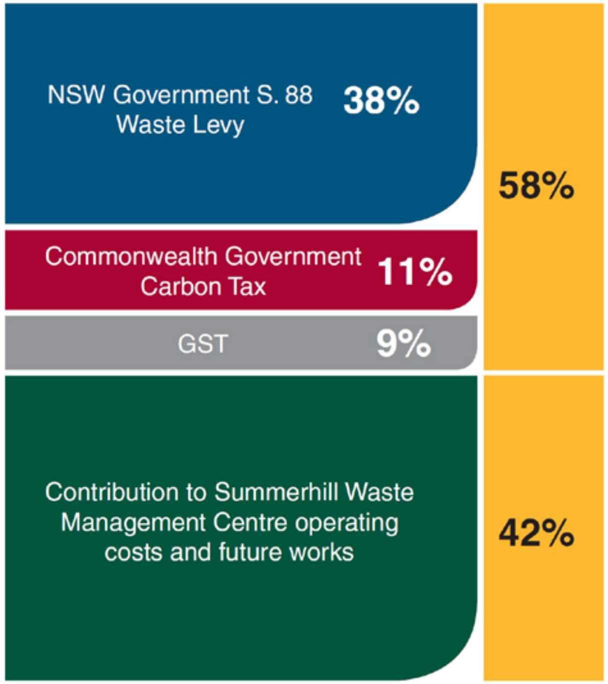
- Waste management Services 3%
- Planning and Building inspection fees 4%
- Tipping Fees and Resource recovery 27%
- Civic Theatre 4%
- Newcastle Airport 20%
- Parking Station/metres 12%

User charges and fees	Actual 2012 $'000	% of total
User charges *(pursuant to s.502)*		
Waste management services (not domestic)	**1,488**	**3%**
Total user charges	**1,488**	**3%**
Fees		
Building services - Other		
Planning and building - Regulatory		
Planning and building - Inspection fee		
- Regulatory/Statutory	**2,076**	**4%**
- Subdivision fees	**478**	**1%**
- Building inspection fee	**406**	**1%**
S603 certificates	**258**	**0%**
Dog control/ registration fees	**161**	**0%**
Licence fees	**258**	**0%**
Local committee's	**422**	**1%**
Inspection fees food shops	**330**	**1%**
Tipping fees/Resource recovery	**14,457**	**27%**
Library fees	**338**	**1%**
Regional Museum	**328**	**1%**
Art Gallery	**156**	**0%**
City Hall	**502**	**1%**
Civic Theatre	**2,026**	**4%**
Parks/Gardens rent	**627**	**1%**
Golf courses	**344**	**1%**
Ocean Baths/Inland pools	**1,024**	**2%**
Newcastle Airport	**10,704**	**20%**
Parking stations/Meter fees	**6,513**	**12%**
Road restorations	**83**	**0%**
Stockton Caravan Park	**1,671**	**3%**
Tourism	**37**	**0%**
RTA works (State Roads not controlled by Council)	**5,802**	**11%**
Professional services	**15**	**0%**
Private works	**265**	**0%**
Childcare	**1,334**	**2%**
Merchant service fee	**97**	**0%**
Fort Scratchley	**285**	**1%**
Reprographics income	**116**	**0%**
Other	**762**	**1%**
Total fees	**51,875**	**97%**
Total user charges and fees	**53,363**	**100%**

The Significant Fees Are:

Tipping fees (27% of total costs)

Whilst the SWMC is expected to collect $24.87 million in fees during 2012/2013 the State and Federal Government charges (Section 88 Levy), Carbon Tax and GST. 58% of the tipping fee is made up of State and Federal government levy and taxes as shown below.

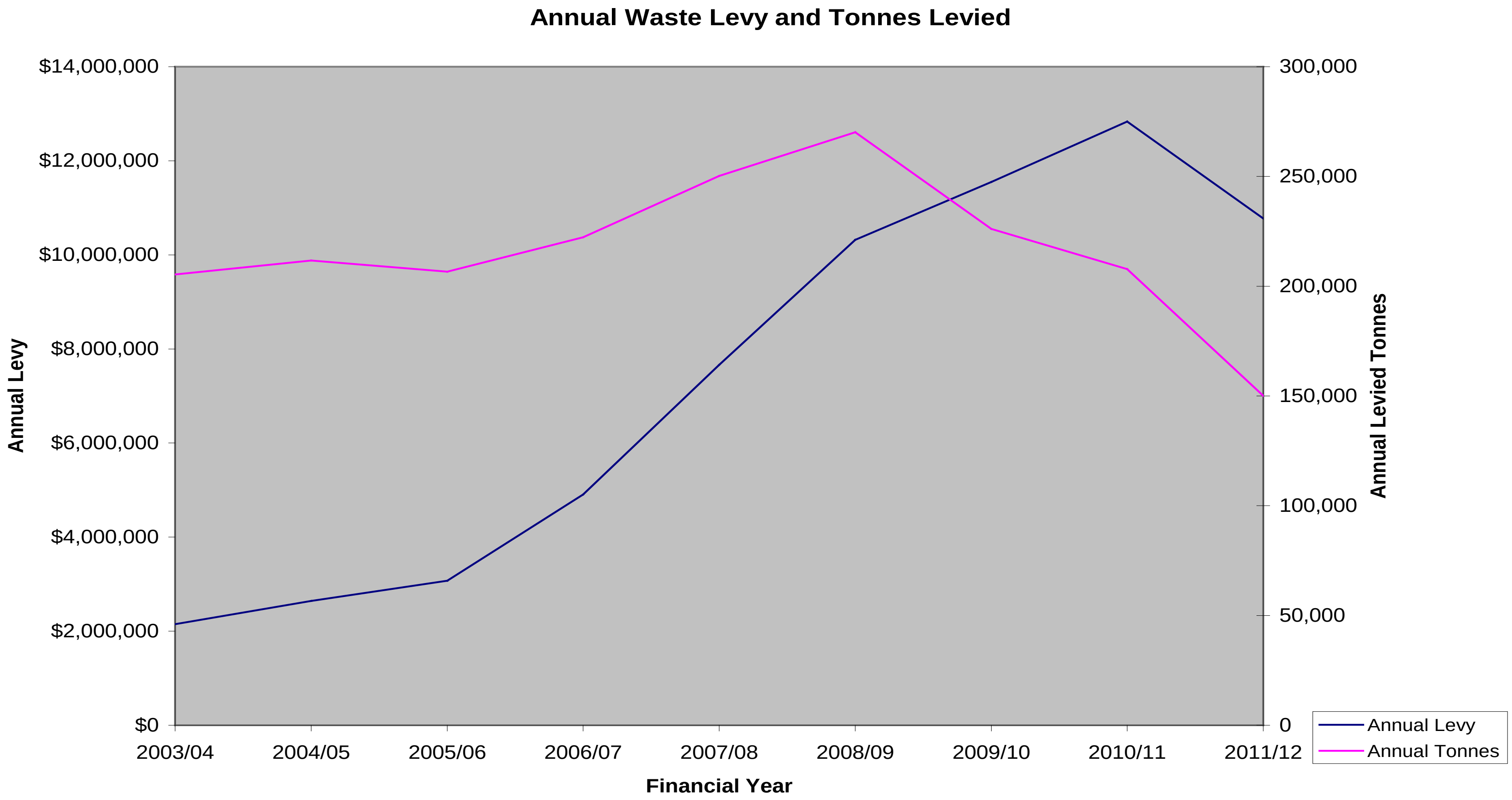


Over the past nine years TCoN has provided **$67.8 million back to the NSW State Government. Employee costs only make up 6.4% of the total expenditure for SWMC**.

The table below shows the payment of the levy against tonnes during these nine years.

Financial Year	Annual Levy Payment ($)	Annual Tonnes Subject to Levy
2003/04	$2,148,587	205,321
2004/05	$2,643,051	211,665
2005/06	$3,071,271	206,639
2006/07	$4,906,498	222,311
2007/08	$7,660,701	250,268
2008/09	$10,320,777	270,146
2009/10	$11,550,926	226,093
2010/11	$12,832,170	207,746
2011/12	$10,772,925	150,152
Total	**$65,906,907**	**1,950,341**
Total inc 2012/13	**$67,852,574**	**1,974,902**

The graph below shows the impact of the levy. The carbon tax and levy have made competition with other smaller facilities (eg Bedminster Plant and Raymond Terrace) more difficult. This has led to more aggressive pricing and a loss of tonnes throughput. This is why Council is now moving swiftly towards developing resource recovery capability.



Newcastle Airport Limited (NAL) (20%)

NAL provides a significant surplus. Council provides loan funding in the form of raised debt which is lent to NAL. In return we receive a 150 basis points credit on the interest rate margin. The full benefit of the surplus is not recognised as a dividend. Under the new model the Airport will pay both Newcastle and Port Stephens Councils a dividend of up to 10%. **Based on forecast growth and an 8% dividend this will provide an income stream back to Council of $36 million over 14 years. ($2.571 million pa)**

Off-Street Parking (12%)

The three Council off-street car parks are being sold. City West has settled and City East will settle in December. The Mall is under negotiation.

The total anticipated capital sale, savings in infrastructure backlog and return on Asset is shown in the table below.

Car parks	Sale price $(millions)	Infrastuture backlog value $(millions)	Forgone suplus before overheads $ (million)	Return on asset value before Overheads (%)
East	$ 4.10	$ 7.50		
West	$ 6.75	$ 8.50		
Mall	$ 4.00	$ 4.50		
Total	$ 14.85	$ 20.50	$ 0.51	3%

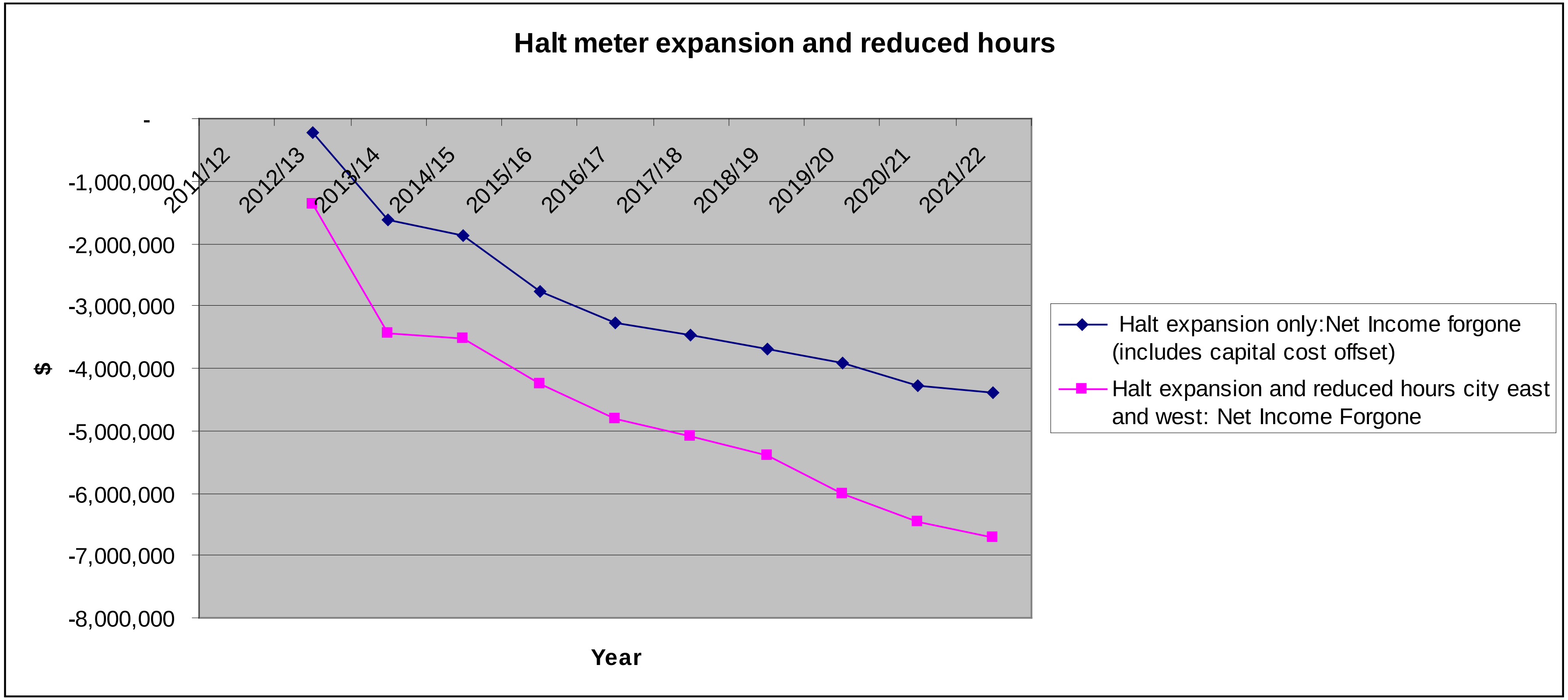
The loss of surplus (before overheads) is anticipated at **$5 million over 10 years**. **The revenue attributed to this is $22 million over 10 years**. These adjustments are already reflected in the revised profit and loss model.

The **savings in infrastructure backlog is estimated at $22 million** which will be used for new capital purposes.

On-Street Parking (12%)

The Council decision to reduce the impacts of on street parking has had the following effects as listed below in the table and graph.

Halt meter expansion/Halt meter expansion and reduced hours city east and west	2011/12	2012/13	2013/14	2014/15	2015/16	2016/17	2017/18	2018/19	2019/20	2020/21	2021/22	Total $
Halt expansion only:Net Income forgone (includes capital cost offset)		-$ 226,455	-$ 1,609,550	-$ 1,878,671	-$ 2,782,393	-$ 3,265,578	-$ 3,467,914	-$ 3,681,150	-$ 3,917,000	-$ 4,268,540	-$ 4,396,596	**-$ 29,493,846**
Halt expansion and reduced hours city east and west: Net Income Forgone		-$ 1,369,456	-$ 3,444,207	-$ 3,532,151	-$ 4,249,665	-$ 4,807,843	-$ 5,088,921	-$ 5,384,837	-$ 6,009,316	-$ 6,467,101	-$ 6,706,715	**-$ 44,932,212**



From the above table and graph, **the LTFP had $44 million income over the 10 years which now comes out of the forecast. This includes $29 million in proposed expansions of 321 metres from years 2013/2014 to 2014/2015.** These adjustments are already reflected in the revised model.

Other operating revenues

Significant other operating revenues are shown below. They include cash **and investments interest of $11.8 million, fines of $3 million and rental income of $3.6 million.**

Interest and Investment Revenue	Actual 2012 $'000	% of total
Interest		
- Overdue rates and charges	**350**	**3%**
- Cash and investments	**11,393**	**97%**
- Other		**0%**
Available for sale revaluation reserves realised	**148**	**1%**
Fair Value adjustments		
- Investments		
- Unrestricted		
Premiums recognised on financial instrument transactions		
Amortisation of discounts and premiums on financial instrument transactions	**(95)**	**-1%**
Total interest and investment revenue	**11,796**	**100%**

Other operating Revenue	Actual 2012 $'000	% of total
Parking fines	**2,760**	**33%**
Other fines	**270**	**3%**
Other charges for overdue rates and charges (legal fees)	**270**	**3%**
Insurance claims	**212**	**3%**
Insurance recovery/bonus	**254**	**3%**
Commissions and Agency fees	**93**	**1%**
Rental Income:		
- Investment property	**1,404**	**17%**
- Other property	**1,204**	**15%**
Investment Recoupment	**1,000**	**12%**
Fair value adjustments - investment properties	**320**	**4%**
Summerhill Waste Management - Electricity Generation	**210**	**3%**
Other	**297**	**4%**
Total other revenue	**8,294**	**100%**

Council's investments contribution over the next ten years declines as the reserves are drawn down to fund the Long Term Financial Plan.

Grants and Contribution Operating

Significant Grants include Financial Assistance Grants ($17.4 million) and Special Purpose Grants ($4.4 million).

Significant Contributions include Section 94 at $0.6 million with RTA ($1.4 million) and Corporate Fitness ($1 million) contributing the most.

Operating Grants	Actual 2012 $'000	% of total
General purpose (Untied)		
- Financial assistance	**10,614**	**46%**
- Financial assistance (In advance)	**6,789**	**29%**
- Pensioner' rate subsidies:		
- General	**1,277**	**6%**
Special purpose		
- Pensioners' rate subsidies		
- DWM	**385**	**2%**
- Community services	**2,081**	**9%**
- Recreation and culture	**644**	**3%**
- Community safety		
- Other	**289**	**1%**
- Natural disaster	**12**	**0%**
- Transport (3x3,Road to Recovery, other transport)	**1,076**	**5%**
Total grants	**23,167**	**100%**
Comprising:		
- Commonwealth funding	**20,509**	**80%**
- State funding	**5,197**	**20%**
- Other Funding		
	25,706	**100%**

Contributions	Actual 2012 $'000	% of total
Developer contributions (S94)		
- S94 management	**19**	**0%**
- Traffic facilities	**11**	**0%**
- Open space	**32**	**1%**
- Community facilities	**75**	**1%**
- Bikeway		
- Studies	**2**	**0%**
- Urban development manager		
- Blue Gum Hills Place	**333**	**7%**
- Transport facilities Blue Gum Hills	**122**	**2%**
- S94A Plan		
Developer contributions - planning agreements		
Paving		
Roads and Drainage		
RTA contributions (Regional/Local, Block Grant)	**1,378**	**27%**
Art Gallery Donations	**5**	**0%**
Regional Museum	**21**	**0%**
Community facilities	**68**	**1%**
Parks and gardens	**14**	**0%**
Library		
Other	**436**	**9%**
Aged housing	**6**	**0%**
Mainstreet programs	**23**	**0%**
Employee's corporate fitness/entitlements	**1,004**	**20%**
Civic and community events	**571**	**11%**
Housing and community amenities	**21**	**0%**
Economic development		
Waste reduction/ diversion incentive	**873**	**17%**
Beach bathing/pools	**4**	**0%**
Total contributions	**5,018**	**100%**
Total grants and contributions	**30,724**	

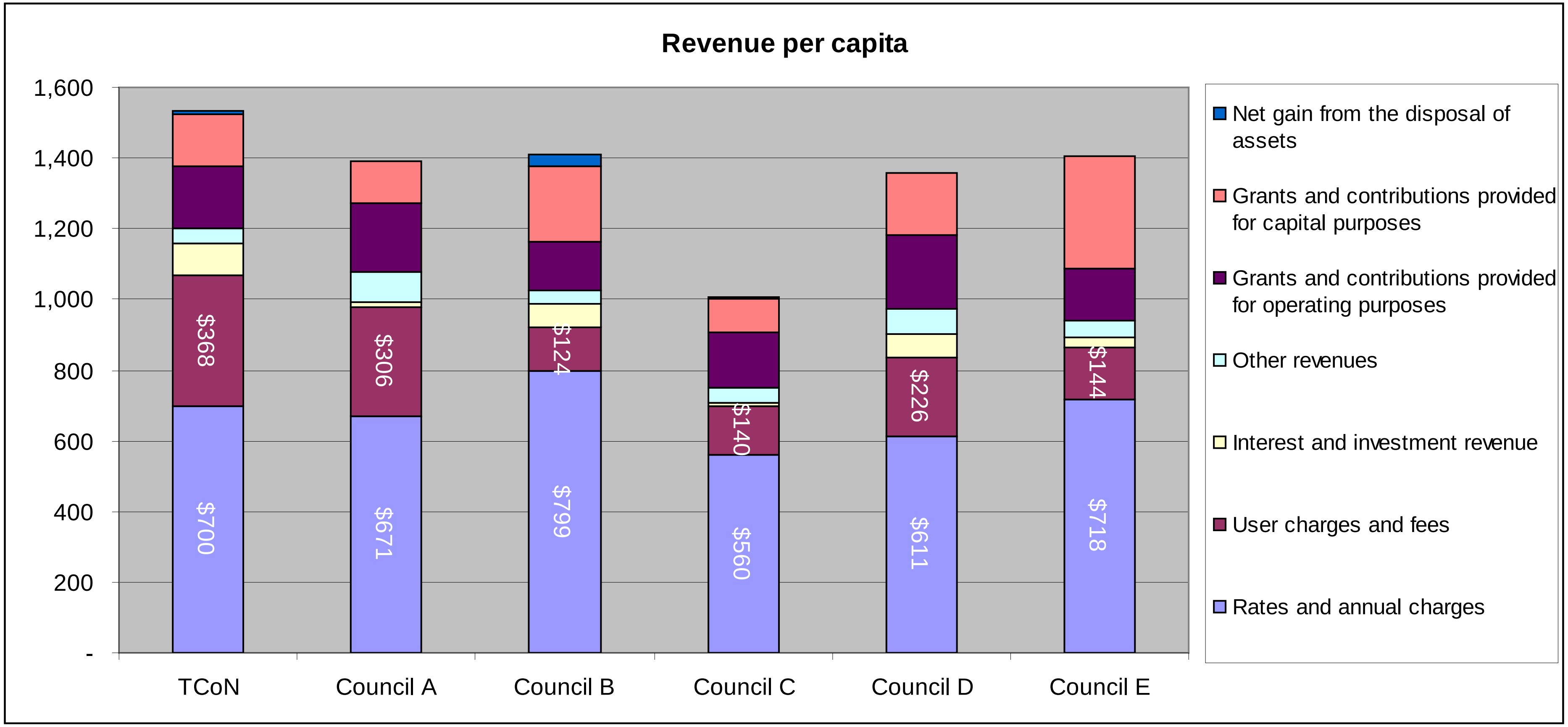
Grants and Contributions - Capital

Capital Grants	Actual 2012 $'000	% of total
General purpose (Untied)		
- Financial assistance		
- Financial assistance (In advance)		
- Pensioner' rate subsidies:		
- General		
Special purpose		
- Pensioners' rate subsidies		
- DWM		
- Community services		
- Recreation and culture	**2,563**	**11%**
- Community safety		
- Other		
- Natural disaster		
- Transport (3x3,Road to Recovery, other transport)	**948**	**4%**
Total grants	**3,511**	**15%**
Comprising:		
- Commonwealth funding	**1,558**	**6%**
- State funding	**1,953**	**8%**
- Other Funding		
	3,511	**14%**

Contributions	Actual 2012 $'000	% of total
Developer contributions (S94)		
- S94 management		
- Traffic facilities		
- Open space		
- Community facilities		
- Bikeway		
- Studies		
- Urban development manager		
- Blue Gum Hills Place		
- Transport facilities Blue Gum Hills		
- S94A Plan	**1,133**	**15%**
Developer contributions - planning agreements		
Paving		
Roads and Drainage	**3,398**	**45%**
RTA contributions (Regional/Local, Block Grant)	**211**	**3%**
Art Gallery Donations	**1,406**	**19%**
Regional Museum	**17**	**0%**
Community facilities	**524**	**7%**
Parks and gardens	**686**	**9%**
Library	**46**	**1%**
Other	**84**	**1%**
Aged housing	**1**	**0%**
Mainstreet programs		
Employee's corporate fitness/entitlements		
Civic and community events		
Housing and community amenities		
Economic development		
Waste reduction/ diversion incentive		
Beach bathing/pools		
Total contributions	**7,506**	**100%**
Total grants and contributions	**11,017**	**28,185**

Income generating efforts compared to other like Councils

In comparing other large like Councils on the East Coast of Australia, the graph below relates to income generating efforts on a per capita basis. For example: Newcastle raises $700 per capita for rates and charges.



From this graph it is evident that Newcastle is in the mid range for its major revenue stream (rates and Charges) and is at the top of the range for User Charges and Fees. This supports the argument that fees and charges are probably at the top of the price sensitivity range.

5.4 Cost Shifting

A recently published LGSA report summarises the results of a survey relating to the 2008/2009 financial year and shows the total amount of cost shifting for The City of Newcastle as $13,267,099. This represents 7.16% of the total income from operations before capital amounts. This is higher than the average for both other urban regional councils (5.44%) and all other NSW council's (5.72%).

The report indicates that the cost shifting ratios published are conservative for several reasons:

- The questions in the survey related to only 23 functions performed by council however others exist and have not been quantified
- Corporate overheads were excluded from the estimates provided by councils so the true cost of providing those services is approximately 10% higher
- Many costs can not be reliably estimated and have therefore been excluded from the survey and
- Capital expenditure was excluded from the survey which would significantly increase costs.

5.5 Rising Operating Costs

Employee Costs and Benefits

A significant operating cost is employee costs and benefits.

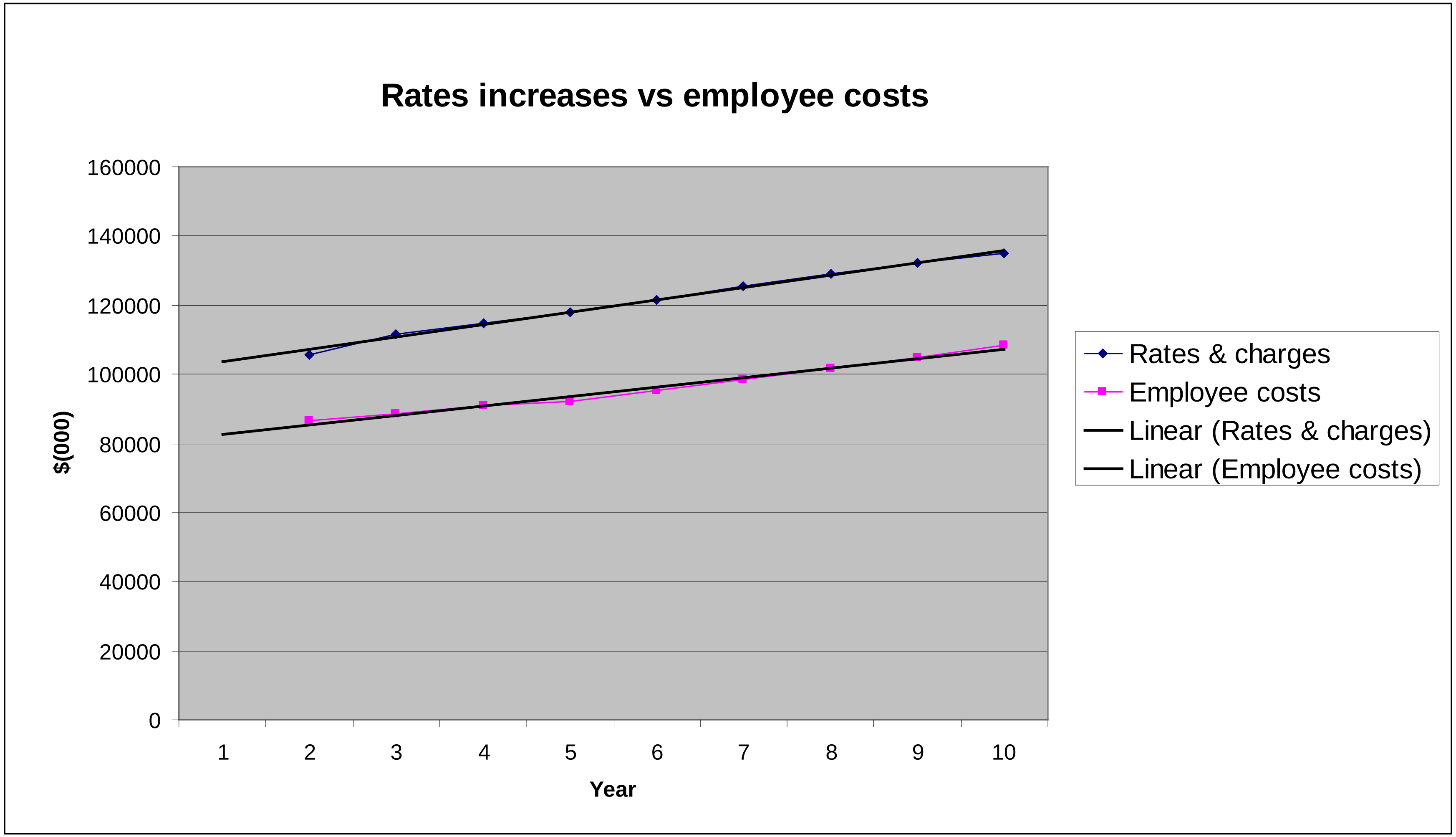
The following table shows the forecast movement in these costs over 10 years:

For the year ended 30 June	*Notes*	*2011/12 $'000*	*2012/13 $'000*	*2014 $'000*	*2015 $'000*	*2016 $'000*	*2017 $'000*	*2018 $'000*	*2019 $'000*	*2020 $'000*	*2021 $'000*	*2022 $'000*
Employee costs		89,558	88,453	90,905	92,292	95,291	98,388	101,586	104,887	108,296	111,816	115,450

The breakdown of the costs is outlined in the following table where salaries and wages make up 71% of these costs.

Employee benefits and on costs	Actual 2012 $'000	% of total
Salaries and wages	**63,857**	**71%**
Travelling	**51**	**0%**
Employee leave entitlements	**13,309**	**15%**
Superannuation	**9,371**	**10%**
Occupational Health and Safety	**1,082**	**1%**
Workers' Compensation Insurance	**3,295**	**4%**
FBT	**517**	**1%**
Training costs (excluding salaries)	**822**	**1%**
Other	**771**	**1%**
Less: Capitalised costs	**(3,516)**	**-4%**
Total employee costs expensed	**89,558**	**100%**

The following table compares rate (income) increases against employee costs:



The above models graph the biggest cost (employee costs) against the biggest revenue (Rates and Charges) in the P&L Statement.

From this it is evident that rates income is moving upward at a faster rate than employee costs. If employee costs were the only consideration in the P&L statement then rates income would be covering them. They are not however.

Materials and Contracts

The table below shows materials and contracts which are a significant expense. This relates predominantly to the development and maintenance of capital assets

Materials and contracts	Actual 2012 $'000	% of total
Raw materials and consumables	**31,813**	**58%**
Contractor and consultancy costs	**20,686**	**38%**
Remuneration of Auditors	**100**	**0%**
Legal fees:		**0%**
- Planning and development	**364**	**1%**
- Other	**738**	**1%**
Operating leases:		**0%**
- Parking meters		**0%**
- Other	**1,163**	**2%**
Total materials and contracts	**54,864**	**100%**

The forecast movement in material sand contracts is shown below:

For the year ended 30 June	*Notes*	*2011/12 $'000*	*2012/13 $'000*	*2014 $'000*	*2015 $'000*	*2016 $'000*	*2017 $'000*	*2018 $'000*	*2019 $'000*	*2020 $'000*	*2021 $'000*	*2022 $'000*
Materials & contracts		54,864	41,071	41,896	43,009	46,450	50,166	54,179	58,514	63,195	68,250	73,710

Borrowing Costs

The following table shows current borrowings:

Borrowing costs	Actual 2012 $'000	% of total
Interest on Overdraft		
Interest on loans	**3,557**	**91%**
Charges on finance leases		**0%**
Charges on hire purchases	**78**	**2%**
Amortisation of discounts and premiums:		**0%**
- Waste management remediation	**287**	**7%**
Less: Capitalised costs		**0%**
Total borrowing costs expensed	**3,922**	**100%**

Council's loan liability as at 30 June 2011 will amount to $47 million. Council may consider seeking Division of Local Government approval for future loan borrowing programs.

Council's loan borrowings strategy underpins its continuing support of addressing asset renewal and maintenance backlog in line with the Strategic Asset Management Plan through escalated programs. All borrowings will be consistent with Council's adopted Borrowing Policy and Strategy, including monitoring against the policy threshold of a debt service ratio of 4%.

All new loans will be raised from appropriate financial institutions and be secured by a charge on the income of Council.

Depreciation, Amortisation and Impairment

The table below shows depreciation, amortisation and impairment. From the table depreciation is shown form an accounting perspective.

Depreciation, amortisation and impairment	Actual 2012 $'000	% of total
Intangibles - software	-	0%
Plant and equipment	5,385	10%
Office equipment	958	2%
Furniture and fittings	244	0%
Land improvements (depreciable)	2,378	4%
Buildings	-	0%
- Specialised	9,329	17%
Other structures	4,104	7%
Infrastructure	-	0%
- roads, bridges and footpaths	26,749	48%
- storm water drainage	5,077	9%
Other assets	-	0%
- Heritage collections	12	0%
- Library books	1,146	2%
- Other	1	0%
Waste management asset	105	0%
Less: Capitalised costs	(320)	-1%
		0%
Total depreciation and total impairment	55,168	100%

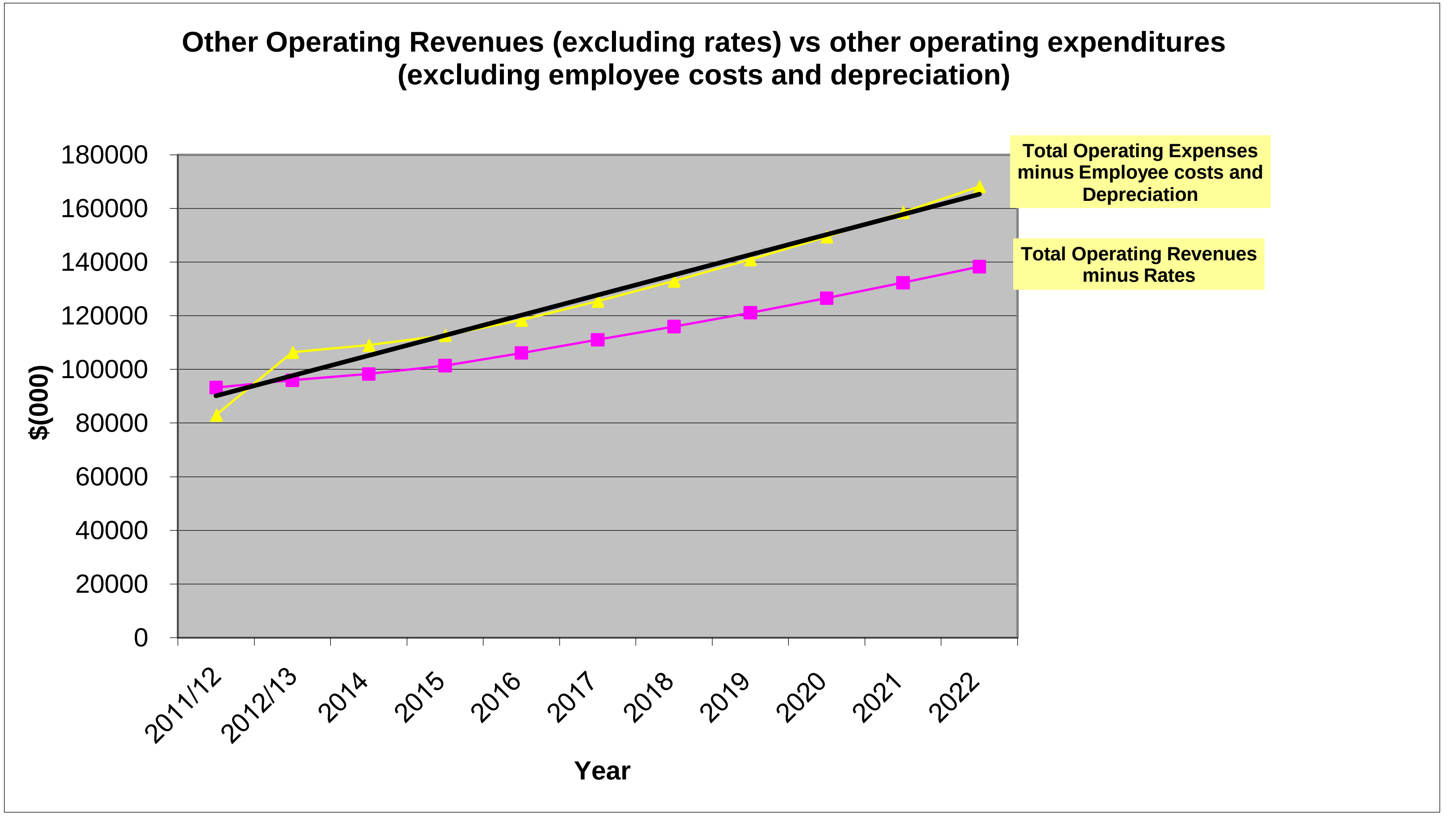
Other Operating Expenses

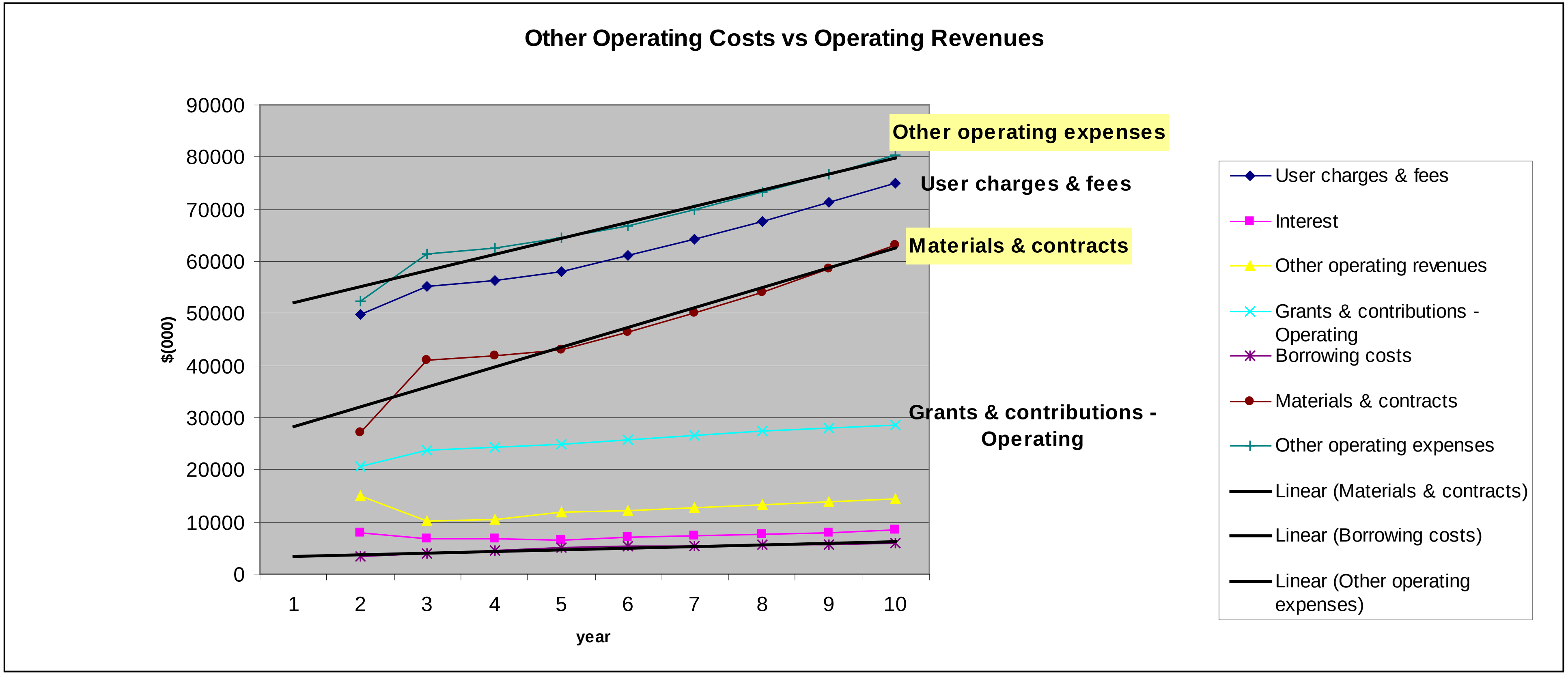
The table below shows other expenses. This table combines other expenses which are more difficult to categorise. The largest expense in this grouping is NSW Waste Levy at $10.8 million. (This is referred to in Section 5.3 of this document).

Other expenses	Actual 2012 $'000	% of total
Other expenses for the year including the following:		
Bad and doubtful debts	451	1%
Mayoral allowance	71	0%
Councillors' fees and allowances	316	1%
Councillors' expenses (incl. Lord Mayor)	109	0%
Street lighting	3,458	11%
Electricity	2,141	7%
Telephone	1,190	4%
Water	706	2%
Contributions and donations	44	0%
Emergency services levy	2,745	9%
Bank charges	478	2%
S355 Local committee working expenses	745	2%
Insurance	3,286	11%
Newcastle Airport	3,476	11%
Planning levy		0%
Fair value adjustments - investment properties		0%
Fair value adjustments - investment		0%
NSW Government Waste Levy	10,862	35%
Election costs	28	0%
Other	541	2%
Total other expenses from continuing operations	**30,647**	**100%**

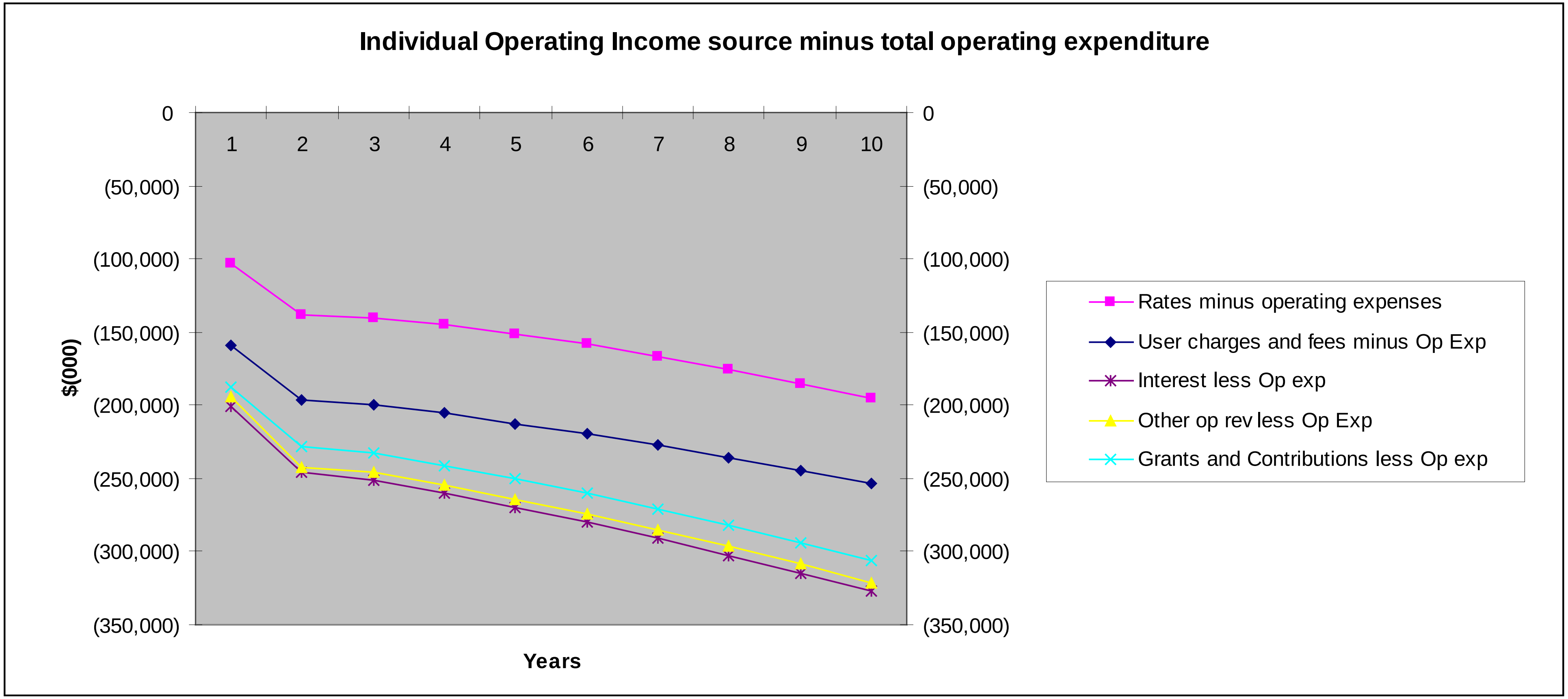
5.6 Analysis of Councils Revenues and expenses

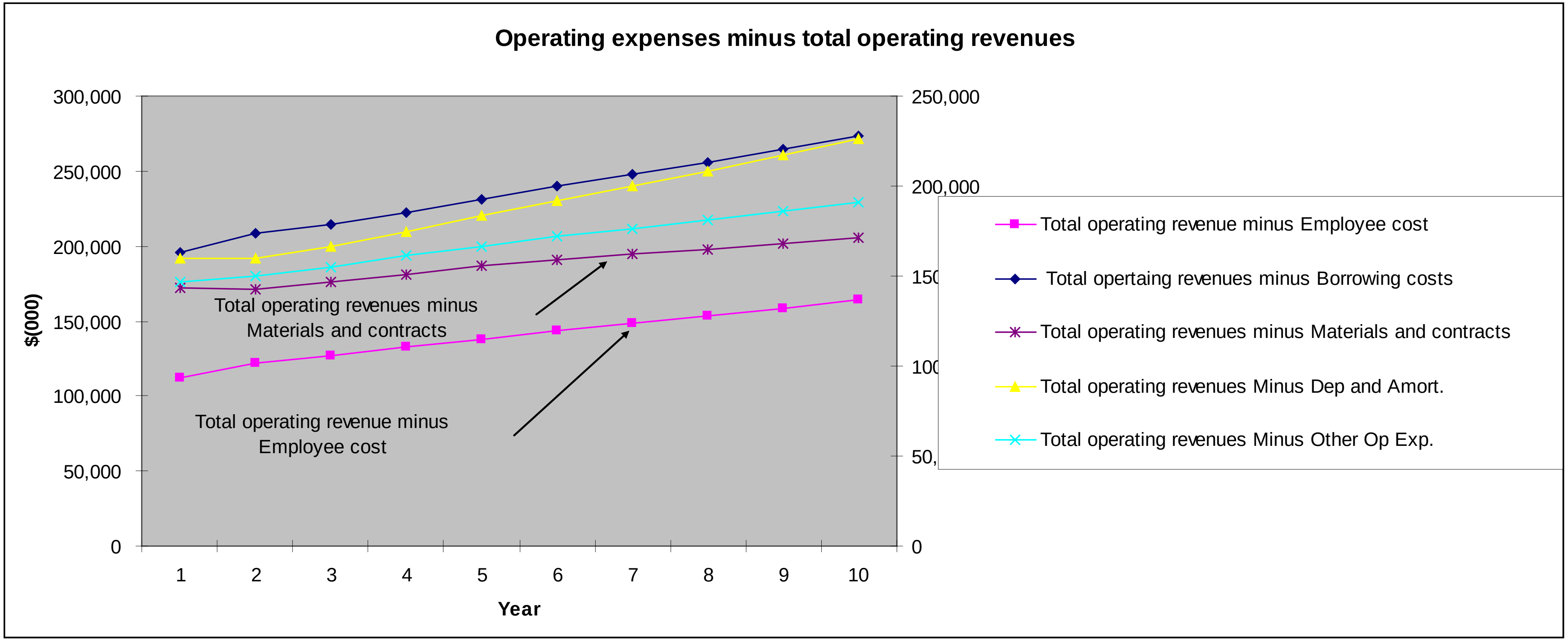
The graph below shows the impact of modeling all operating revenues (excluding rates) against all operating costs (excluding depreciation and employee costs). The graph clearly shows the other than rate revenue (such as user charges and fees, grants and contributions) does not cover the other than employee and depreciation costs (such as materials and contracts and other). The two lines break even in 2012/2013 and then trend apart in opposite directions over the next 10 years.





The graph above shows that the two biggest costs rising disproportionally against revenues are other operating expenditures and materials and contracts.


Individual Operating Income source minus total operating expenditure
0
(50,000)
(100,000)
(150,000)
(200,000)
(250,000)
(300,000)
(350,000)
$(000)
1
2
3
4
5
6
7
8
9
10
Years
Rates minus operating expenses
User charges and fees minus Op Exp
Interest less Op exp
Other op rev less Op Exp
Grants and Contributions less Op exp



For the graph above the lower the line the more impact it has on the profit and loss statement. (ie employee costs have the biggest impact from an expense perspective and second biggest impact is material and contracts. The flatter the curve on the line means that the greater the impact this expense has on the profit and loss as time goes on (ie materials and contracts is flatter the employee costs). In real terms there is $59 million difference in employee costs and materials and contracts in year one and in year 10 the gap between the two lines reduces to $49 million. This means that on average materials and contracts is going up $1 million per year faster than employee costs.

6. What is needed to fix the problem?

Council needs to urgently revise its LTFP. This plan needs to consider the long term and integrate various intervention measures necessary to guide Council back into a sustainable position. This report has been constructed in order to guide the creation of a **new Long Term Financial Plan. This report is referred to as the "10 Year Integrated Strategic Financial Analysis".**

6.1 The purpose of the draft 10 Year Integrated Strategic Financial Analysis (ISFA) (2013/14 to 2021/22)

The purpose of the ISFA is to provide Council with a mechanism to analyse Councils revenues and costs against their delivery obligations and develop intervention options to provide a pathway to sustainability.

This analysis is done within the context of finite economic and financial resources. The plan considers:

- Sustainability measures
- Service levels and
- Infrastructure renewals and replacement.

The plan recognises internal and external revenue sources and forecasts all costs over a 10 year horizon.

6.2 What are the ISFA Objectives?

The objectives of the ISFA in guiding the Long Term Financial Plan will be to:

- Provide worked options to enable strategic decision making by Council
- Ensure Council's long term financial sustainability
- Identify financial and strategic opportunities
- Provide transparency in forecasting Council's financial position
- Analyse the cumulative financial impacts of Council's current plans and policies including implementation of Councils resolutions
- Maintain service levels expected by the community
- Maintain a balanced annual operating budget
- Maintain a strong cash and liquidity position
- Maintain adequate cash reserves in accordance with legislation or Policy requirements
- Ensure robustness of appropriate cost recovery strategies through full pricing and recognition of the true cost of provision of services when setting revenue targets
- Ensure Council is within industry recognised Financial Health Check indicators
- Ensure asset renewal and maintenance remain within the sustainable range, and
- Identify current asset holdings and opportunities for rationalisation to assist in addressing Council's maintenance backlog.

7. Sustainability Options

The following section investigates sustainability options. The options have been modelled as stand alone. (That is each option is taken in turn to determine its impact on the total budget and the reduction impacts on the deficit.) The Hybrid options consider combinations of these options used together to produce a deficit reduction result. For example, costs reductions used with revenue improvements. In order to save $1 million per annum, large reductions in service elements or assets are required for example, the cessation of services.

It is important to note that there is a danger of double counting when options are combined.

7.1 Expenditure Reduction Options

These options consider expenditure reductions across Council.

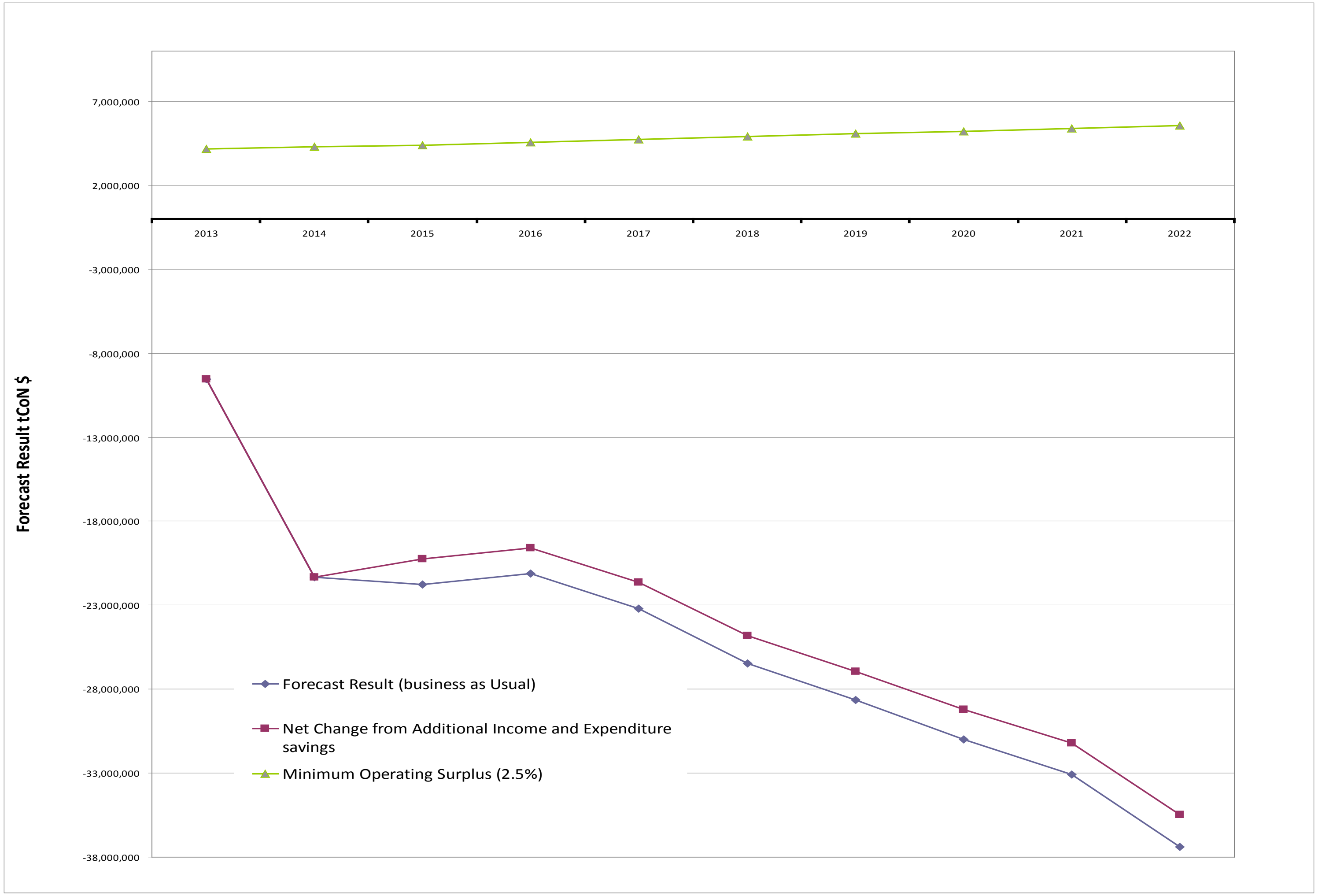
7.1.1 Implement new computer system - Enterprise Resource Planning (ERP)

Council has undertaken a significant project which involves replacing our **unintegrated "best of breed" systems with an integrated "out of the box" solution** that will see Councils extensively stand alone system with a central platform. This option sees potential savings in stage 1 and 2 of $1.5 million by year 3 (2015/16).

How could these savings be achieved?

Once the ERP is in place the opportunity for financial self help and Information Management Service (IMS) self help across the sections will be easier. A further opportunity to outsource the server provision will create more staffing efficiencies. A benefits realisation program will need to follow the ERP project.

The following graph shows the impact of this option.



Financial Year:	2012/13	2013/14	2014/15	2015/16	2016/17	2017/18	2018/19	2019/20	2020/21	2021/22	Total
Improvement on Deficit	-	-	- 1,500,000	- 1,552,500	- 1,606,838	- 1,663,077	- 1,721,285	- 1,781,529	- 1,843,883	- 1,908,419	- 13,577,530

This option provides financial benefit to the budget, but is not enough to deliver a surplus.

7.1.2 Service unit savings

This option involves the following steps:

Under this option a number of service units would be considered for:

1. Cessation, or
2. Reduction

There are 15 service elements in the model.

How could these savings be achieved?

An example of a potential **service element cessation** would be Beresfield Golf Course.

In this example $150,000 loss would be addressed through the following steps:

1. Test grounds maintenance outsourcing for contestability
2. Produce a DA for the adjacent land
3. Determine post 1 and 2 above if the service was making a margin after 1 year
4. Proceed to sell or maintain
5. End result $150,000 saving ongoing

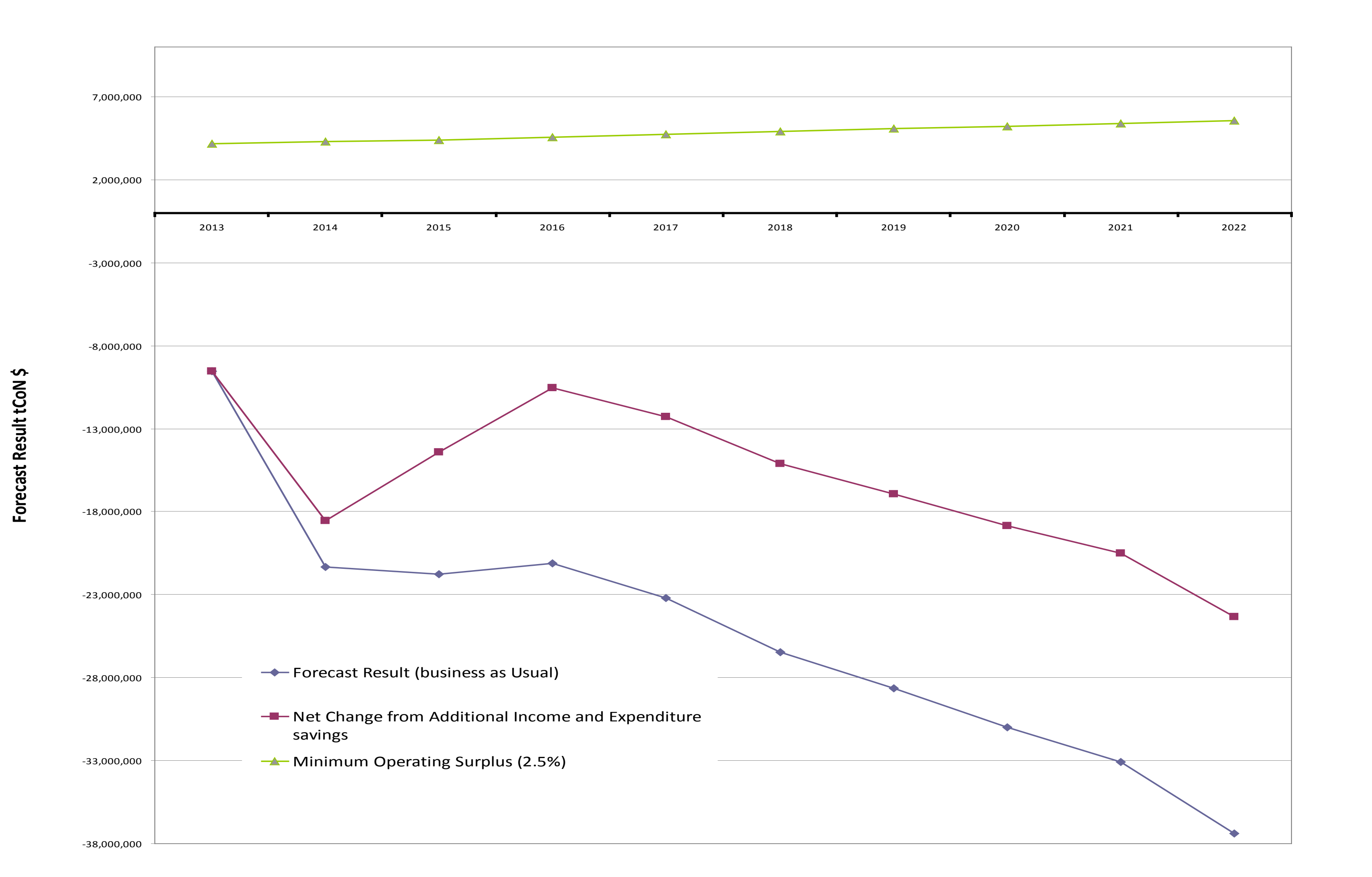
An example of service element reduction could be Tourism and Economic Development Services. This could be achieved by:

1. Transferring the elements of the service to the private sector or an independent tourism sector
2. Outsourcing some of the service element.
3. The potential savings on this example could be: $1 million by 2014 and an addition $500,000 by 2015.

A variety of alternates have been considered so they are similar to the examples above and staged over 3 years with savings in total as follows:

- Year 1 - $2.8 million
- Year 2 - $4.0 million
- Year 3 - $3.0 million

These have been staged in such away that alternates and decisions can be modelled and made.



Financial Year:	2012/13	2013/14	2014/15	2015/16	2016/17	2017/18	2018/19	2019/20	2020/21	2021/22	Total
Improvement on Deficit	- -	2,800,000 -	7,366,750 -	10,576,024 -	10,950,319 -	11,337,921 -	11,739,307 -	12,154,968 -	12,585,418 -	13,063,446 -	92,574,152

7.1.3 Annual budget savings

One option involves the following steps:

1. Reduce operating expenditure by 5% in year one. This is achieved by taking the year 0 budget and applying CPI. The second step it reduce the CPI increased budget by 5%.
2. In years two to ten the same process is applied to the year one budget. This time 3% is taken off the expenditure.

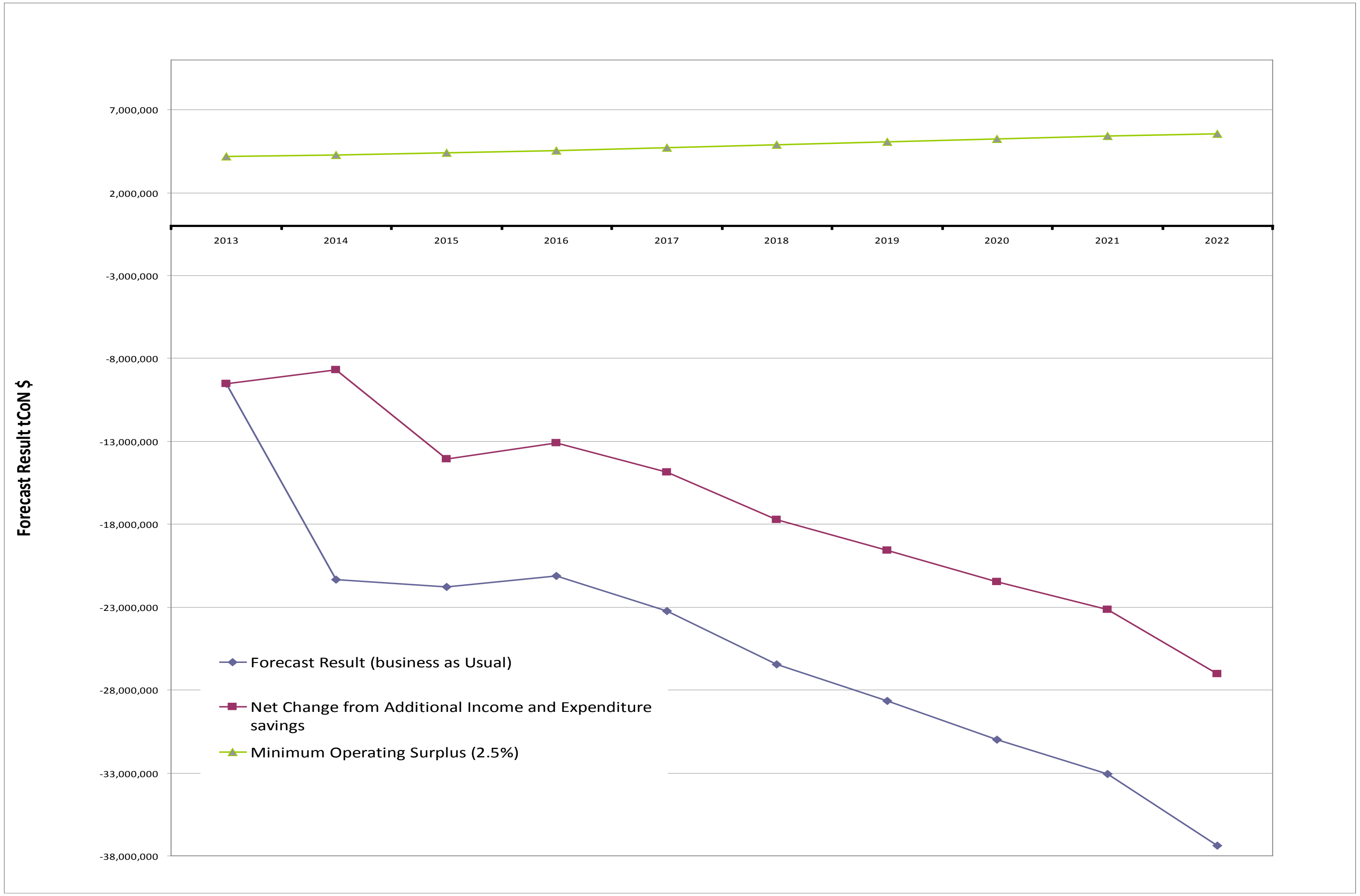
A **second option** would be to save 10.25% over the first two years as detailed in Section 8.

How could these savings be achieved?

During each budget cycle the Service Unit Manager and Director would agree and sign off on a savings target. The Service Unit Manager and Director would be held accountable to achieving that target. If budgets fell short of their target other savings would have to be found.

The following graph shows the impact of this option.

From the graph it can be seen that there are substantial savings in year one to ten, they are not sufficient to sustain a surplus in the organisation.



Financial Year:	2012/13	2013/14	2014/15	2015/16	2016/17	2017/18	2018/19	2019/20	2020/21	2021/22	Total
Improvement on Deficit	- -	12,651,519 -	7,703,501 -	8,013,330 -	8,368,445 -	8,730,918 -	9,106,536 -	9,506,505 -	9,930,417 -	10,376,786 -	84,387,958

7.1.4 MAPPS 5% reduction

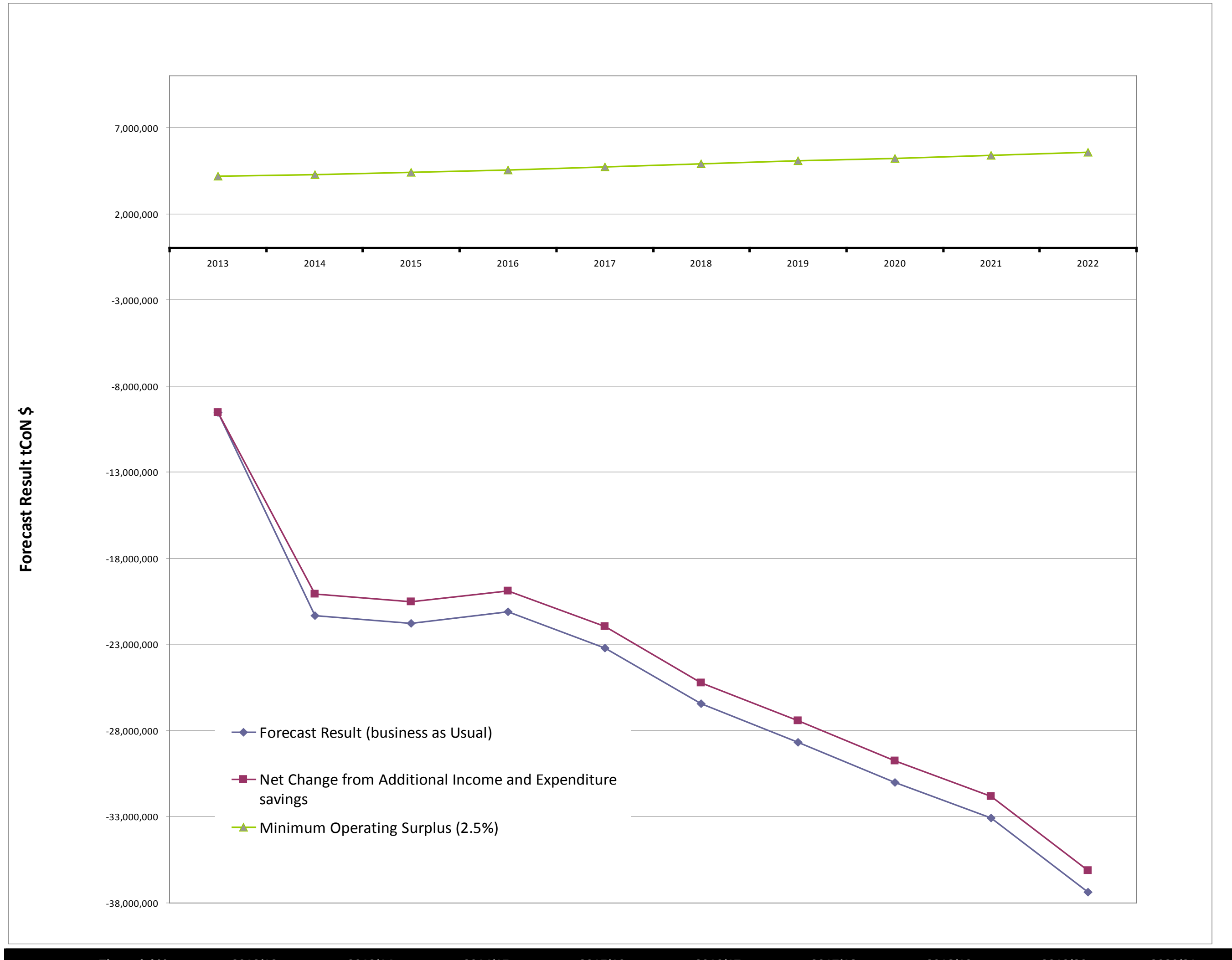
This option involves the following steps:

This option considers reducing the asset maintenance and asset renewal funding by 5% in year one and then maintaining this lower level of renewal.

How could these savings be achieved?

This will be a process of reducing the annual MAPPS budget by $2.5 million per year. This can only be achieved through asset disposal. If the budget for MAPPS is reduced without asset disposal, the infrastructure backlog will significantly increase over 10 years.

The following graph shows the impact of this option.



Financial Year:	2012/13	2013/14	2014/15	2015/16	2016/17	2017/18	2018/19	2019/20	2020/21	2021/22	Total
Improvement on Deficit	- -	1,249,800 -	1,249,800 -	1,249,800 -	1,249,800 -	1,249,800 -	1,249,800 -	1,249,800 -	1,249,800 -	1,249,800 -	11,248,200

The graph shows the minimum impact of this strategy. In addition, the strategy would be delaying the inevitable that the infrastructure backlog will grow further. Once this happens the catch up cost will be significant and possibly insurmountable. The only way this can be achieved is reducing the backlog to start with either through asset sales or capital to renew.

7.1.5 MAPPS 10% reduction

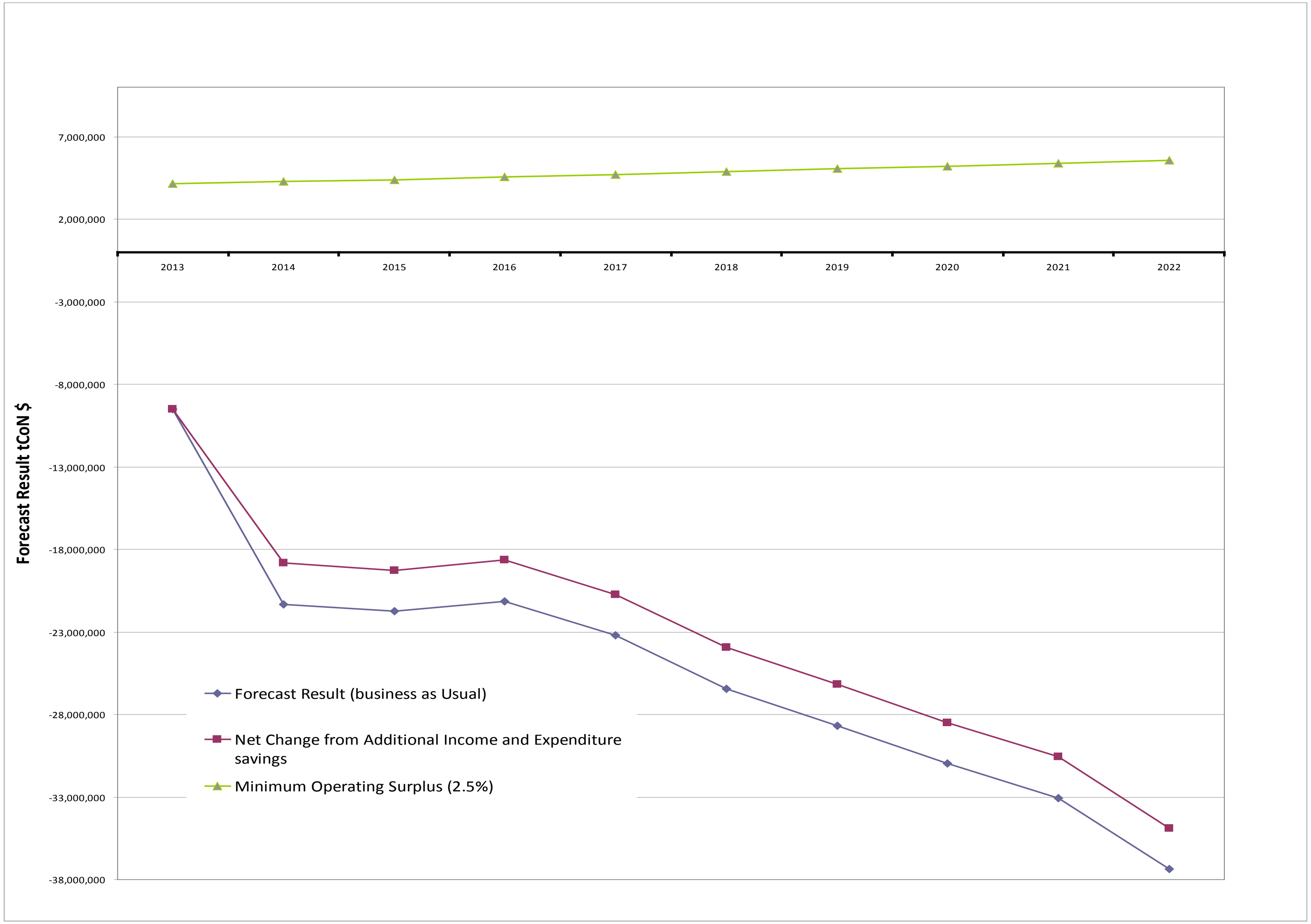
This option involves the following steps:

The MAPPS program is predominantly allocated to the infrastructure backlog. If this budget is reduced more assets will not be renewed at their intervention level. This will result in more assets moving into the backlog. The cost of renewal then goes up and the backlog becomes larger. This will provide a short term benefit to the budget but will result in intergenerational inequity.

How will these savings be achieved?

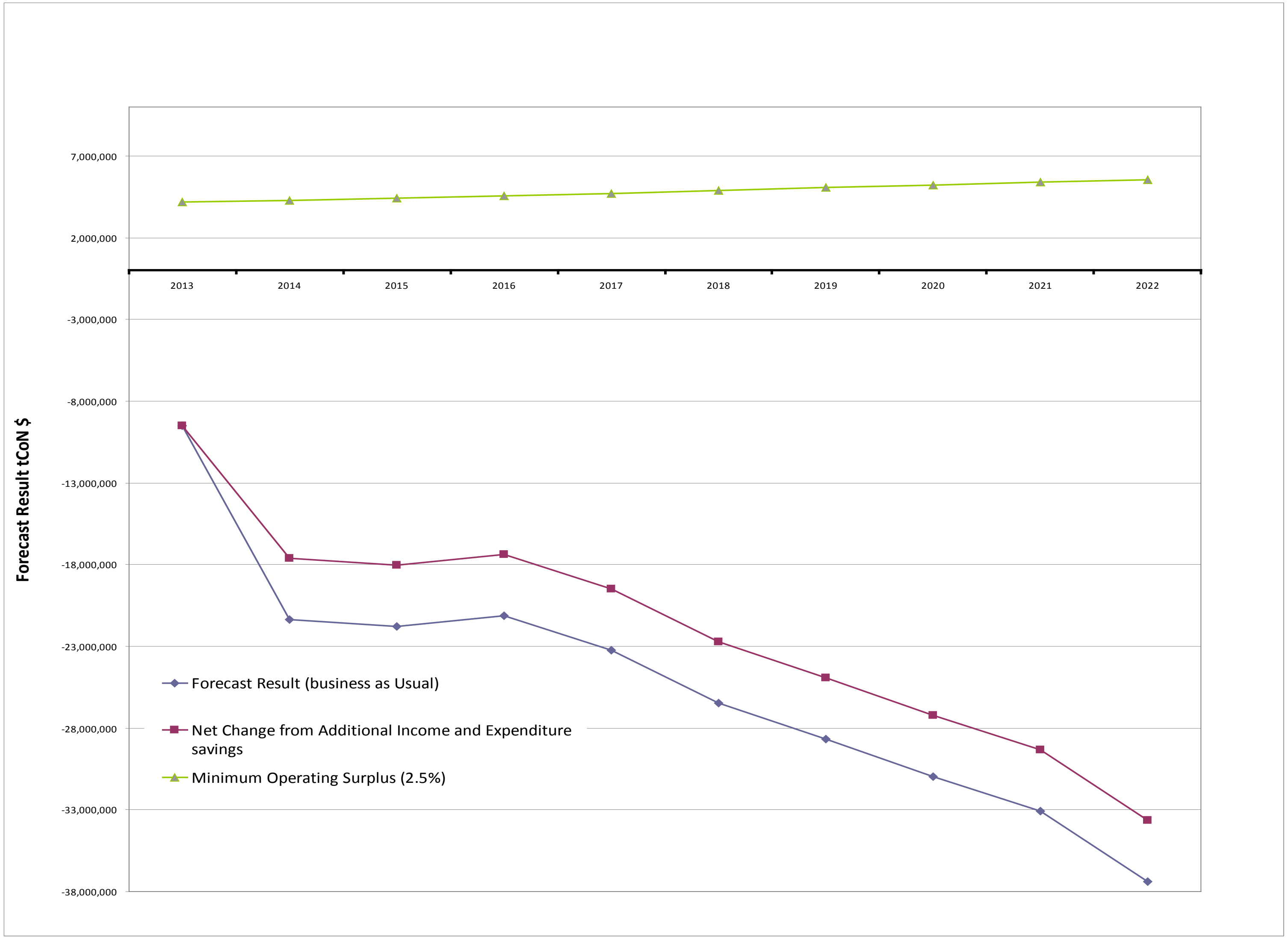
They will be achieved through cutting the MAPPS budget. This would have impacts on materials and staffing levels. Council would approve this through the budget process.

The impacts of this are graphed below. It's important to note that the infrastructure backlog will grow and hence expenses in the future, when these issues are addressed, will increase.



Financial Year:	2012/13	2013/14	2014/15	2015/16	2016/17	2017/18	2018/19	2019/20	2020/21	2021/22	Total
Improvement on Deficit	- -	2,499,600 -	2,499,600 -	2,499,600 -	2,499,600 -	2,499,600 -	2,499,600 -	2,499,600 -	2,499,600 -	2,499,600 -	22,496,400

The graph below shows what a 15% reduction in MAPPS would look like (this is simply adding the 5 and 10 % options together).



Financial Year:	2012/13	2013/14	2014/15	2015/16	2016/17	2017/18	2018/19	2019/20	2020/21	2021/22	Total
Improvement on Deficit	- -	3,749,400 -	3,749,400 -	3,749,400 -	3,749,400 -	3,749,400 -	3,749,400 -	3,749,400 -	3,749,400 -	3,749,400 -	33,744,600

7.1.6 Employee costs savings

This option involves the following steps:

There are three different scenarios modelled as follows:

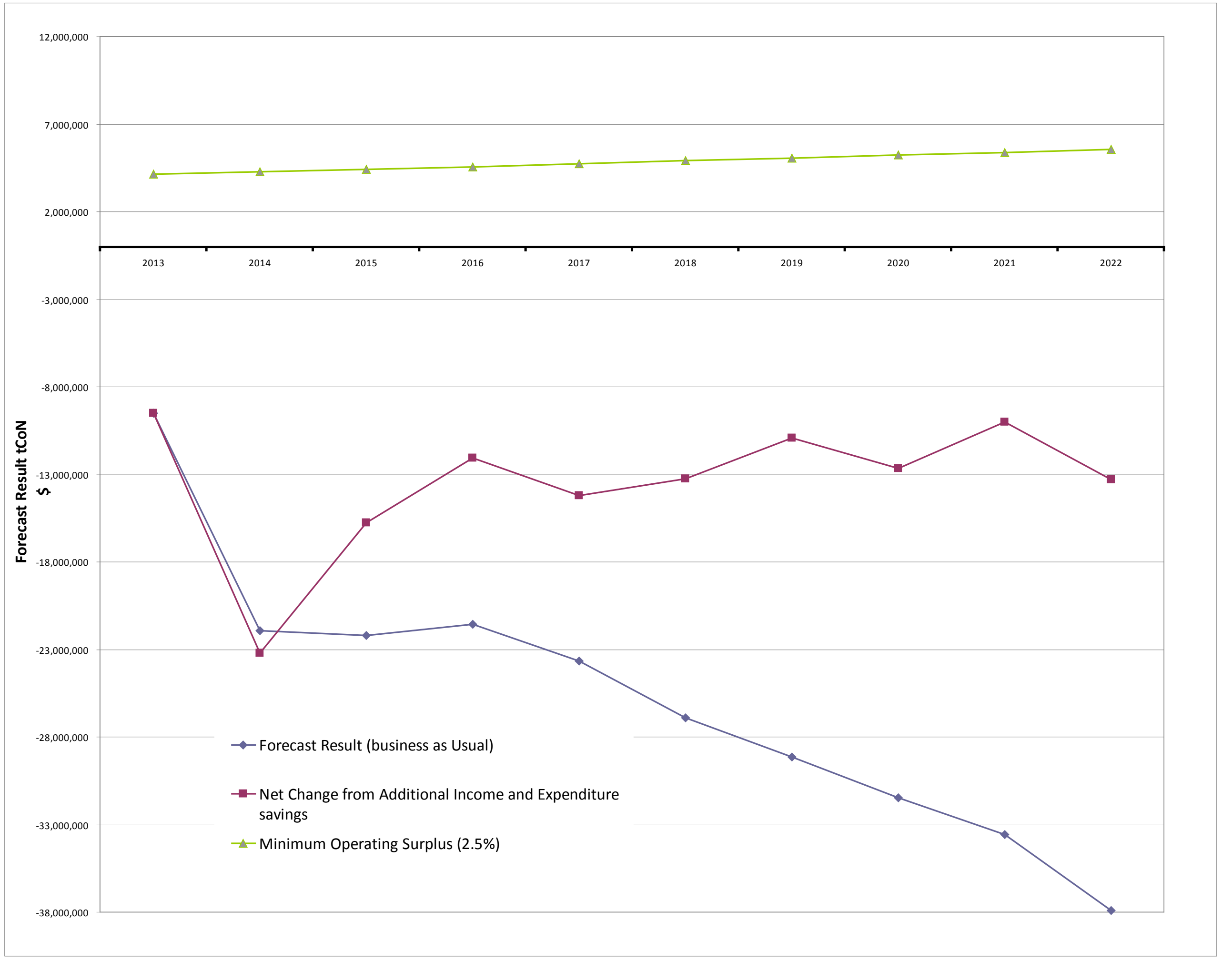
- The first is to progressively reduce employee costs over 10 years. This option yields $123 million and would involve approximately 290 staff over the 10 years. This involves approximately a 30% reduction in the workforce.

- The second is to reduce employee costs by $130 million in 10 years, and

- The third is to reduce employee costs by $4.5 million over two years and then hold the reduced EFT down by this number for the remainder of the 10 years. This would yield $135 million over 10 years.

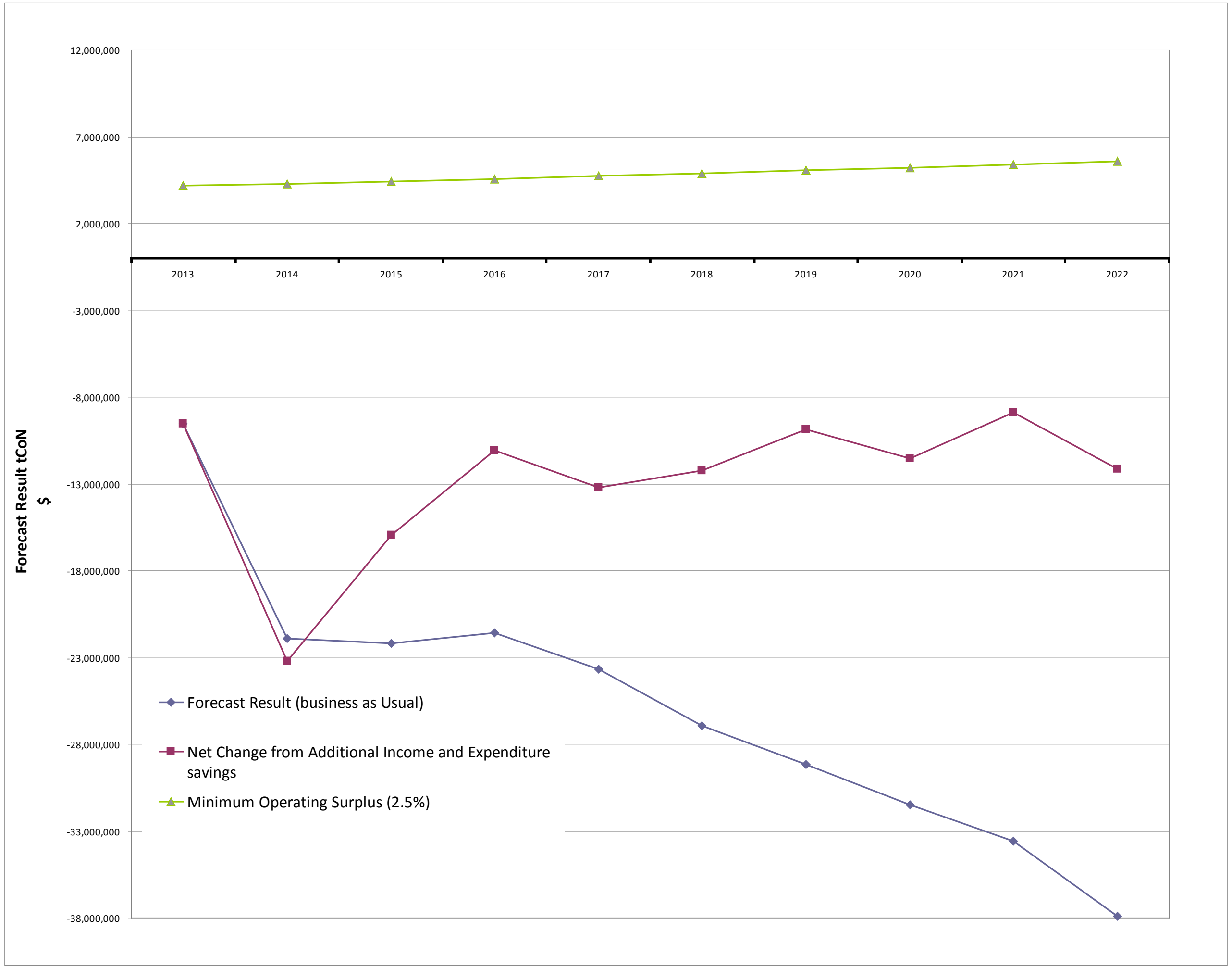
The three options are modelled in sequence below:

(1) $123 million



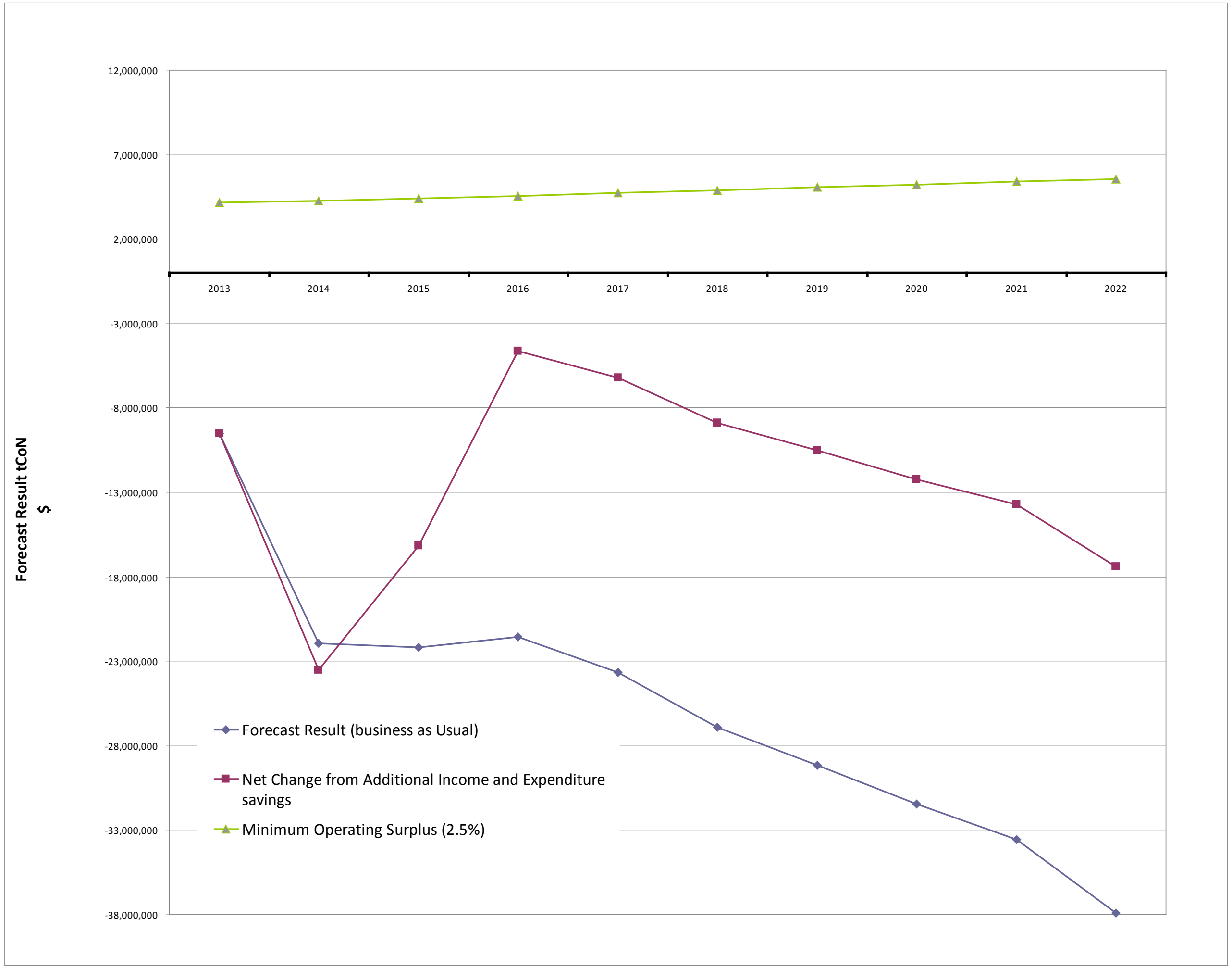
Financial Year:	2012/13	2013/14	2014/15	2015/16	2016/17	2017/18	2018/19	2019/20	2020/21	2021/22	Total
Improvement on Deficit	-	1,278,313	- 6,412,726	- 9,512,140	- 9,458,797	- 13,651,940	- 18,225,628	- 18,821,782	- 23,563,490	- 24,597,603	- 122,965,793

(2) $130 million



Financial Year:	2012/13	2013/14	2014/15	2015/16	2016/17	2017/18	2018/19	2019/20	2020/21	2021/22	Total
Improvement on Deficit	-	1,278,313	- 6,251,059	- 10,480,969	- 10,459,113	- 14,684,766	- 19,292,021	- 19,922,833	- 24,700,325	- 25,771,385	- 130,284,159

(3) $4.5 million reduction employee costs in two years yielding $135 million over 10 years



Financial Year:	2012/13	2013/14	2014/15	2015/16	2016/17	2017/18	2018/19	2019/20	2020/21	2021/22	Total
Improvement on Deficit	-	1,597,891	- 6,028,180	- 16,910,471	- 17,460,061	- 18,027,513	- 18,613,407	- 19,218,343	- 19,842,939	- 20,487,835	- 134,990,858

How could these savings be achieved?

The savings could only be achieved through:

- Efficiencies brought about by changed work practices (eg cross skilling)
- Outsourcing - only where the costs of service is lower
- Reduction in whole services (eg Beresfield Golf Course)
- Reduction in partial service
- Reduction in hours (eg 48/52)
- Providing employee redundancy (any redundancy would have a cost of payout in the first year followed by savings in subsequent years. This model has used and average redundancy cost of $100,000 and savings annually of $80,000).
- Natural attrition of staff. The current natural attrition rate is 6%.

Example of potential employee savings in the parks service:

Council maintains approximately 1200 Ha of bushland and park lands. Park land falls into two groups: reserves which have no assets (eg park benches, toilets etc) and parks which may have one or more of these assets.

There are 11 field maintenance groups. Each group has two teams. A team is made up of field supervisor, senior field worker and field worker. The table in **Appendix C** outlines the labour, plant and capital costs of each team as follows:

- Labour $187,000
- Stores and materials $7,000
- Capital $154,000

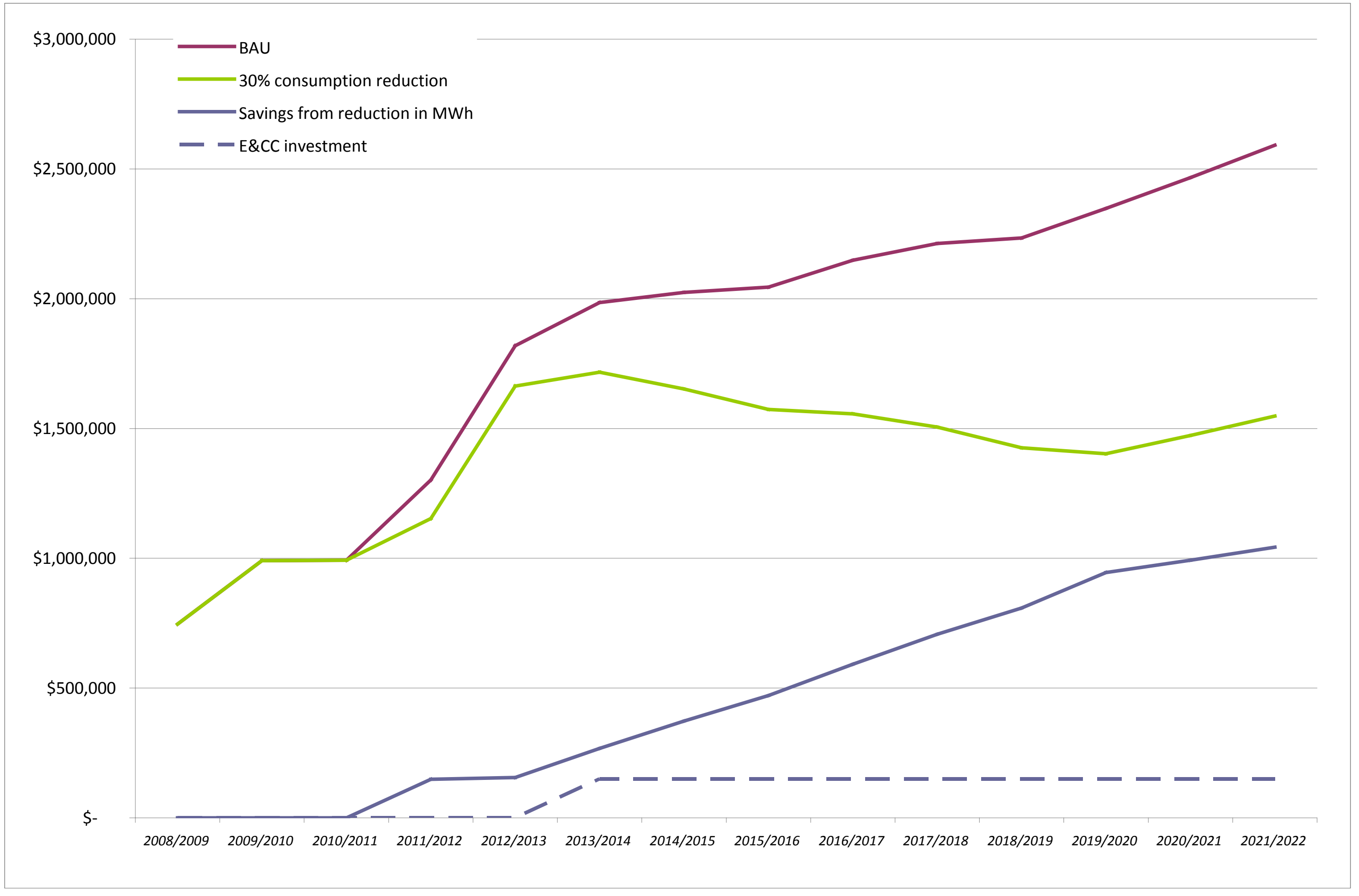
Each team maintains approximately 45 Ha of parkland.

Council could consider the following options:

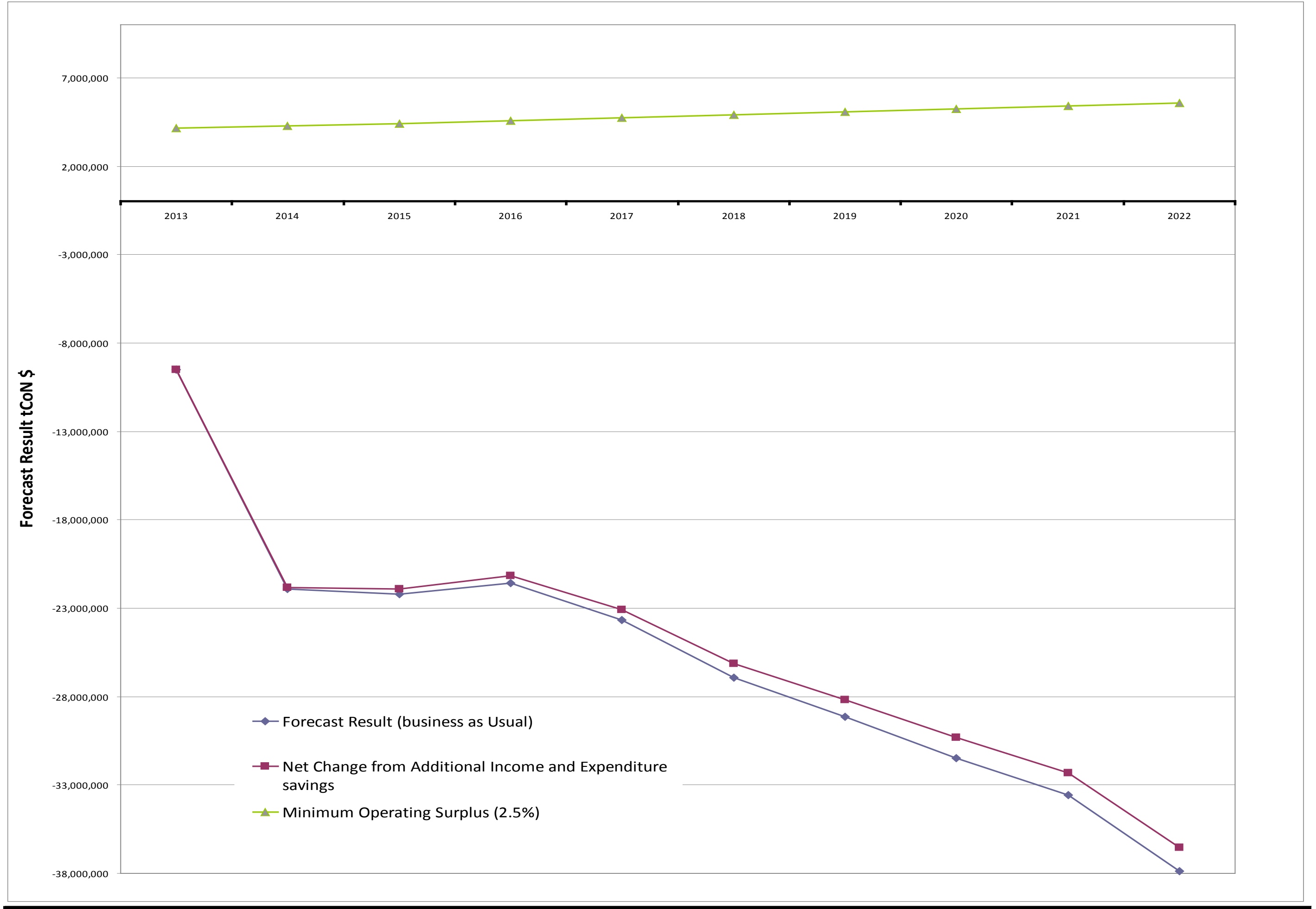
- Not mow the 45 Ha and drop a whole team and its cost from the budget.
- Dispose of the 45 Ha and drop a whole team and its cost from the budget
- Through contestability, open the 45 Ha mowing area to market competition. Let the contract to mow the 45 Ha to either a private company or an in-house bid based on the winning bid.

7.1.7 Implement utility savings (energy/water)

As outlined in the report utility costs are going up significantly. The graph below shows what will happen to costs for energy if the TCoN continues to consume at the current rate. This is shown by the magenta line. The green line shows what would happen to costs if Council were able to achieve a 30% savings.



The impact of these savings is shown in the graph below:



Financial Year:	2012/13	2013/14	2014/15	2015/16	2016/17	2017/18	2018/19	2019/20	2020/21	2021/22	Total
Improvement on Deficit	-	- 96,651	- 260,171	- 417,264	- 603,224	- 785,044	- 949,289	- 1,159,326	- 1,260,110	- 1,365,448	- 6,896,527

How could this be achieved?

This could be achieved with low levels of capital improvement and better management of systems such as automatic energy shut down systems after certain hours and undertaking cleaning services at different times. Each year a service unit would have an energy budget to manage. That would include the reduction target. An investment budget would also be made available to technology devises to restrict usage hours. The forecast is net of any capital amounts.

7.1.8 Asset savings

The City of Newcastle has a significant buildings and structures asset base. There are 591 buildings and structures with a total value of $445 million out of a total infrastructure value of $1,615 million or 28%.

They also constitute a significant proportion of the backlog at $89.6 million out of a total backlog of $125.8 million or 71%.

Operational savings can be achieved by reducing the number of assets Council owns. These savings include:

- Maintenance
- Renewal expenditure
- Depreciation
- Overhead

How could this be achieved?

Assuming 10% or $45 million of this asset base could be disposed, any sales revenue could be allocated to reduce Councils infrastructure backlog. Once the backlog is taken care of and the number of assets reduced, the amount of maintenance depreciation and renewal monies can be reduced. This will flow over into employee and materials costs savings as well.

There are a number of ways savings can be achieved on assets as follows:

Buildings:

- Retain but close (eg Community Hall)
- Retain and lease the entire building (eg Clarendon Hotel)
- Demolish and sell site (eg Fred Ash Warehouse to State Courts)
- Value add and sell site (eg rezoning, DA, Lynches Prawn site)
- Sell in an as is condition (eg old Wallsend Library)

Structures:

- Reduce numbers (eg park benches, toilet facilities)

Open space:

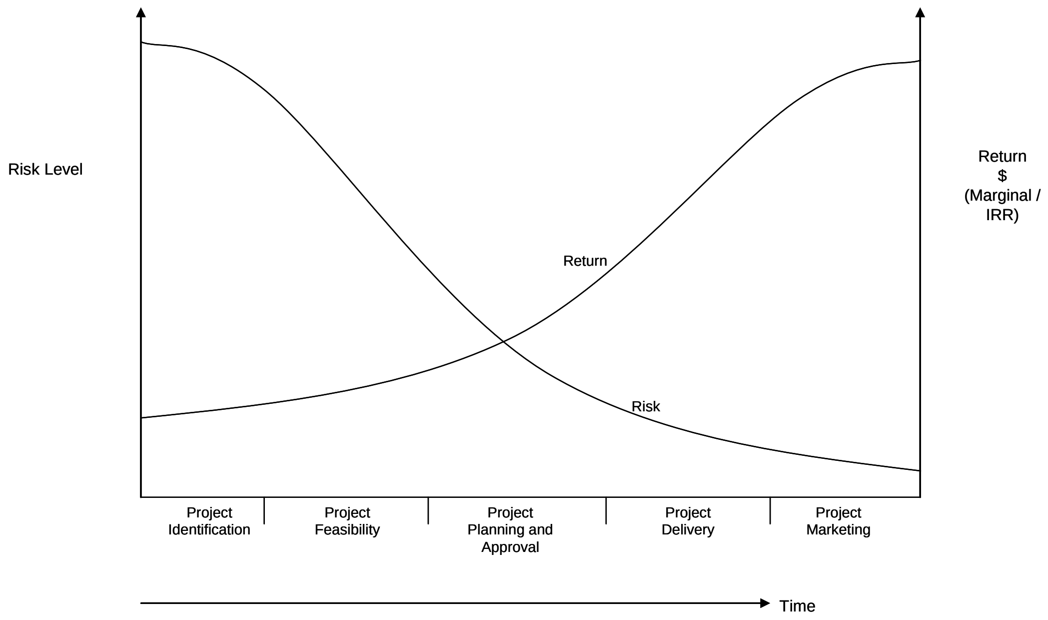
- Where open space is operational land then dispose
- Value add then dispose of operational land
- Identify Community land for reclassification to operational and then dispose
- Community land gifting and
- Community land that is no longer serviced and maintained to parkland condition (eg allow to become green space)

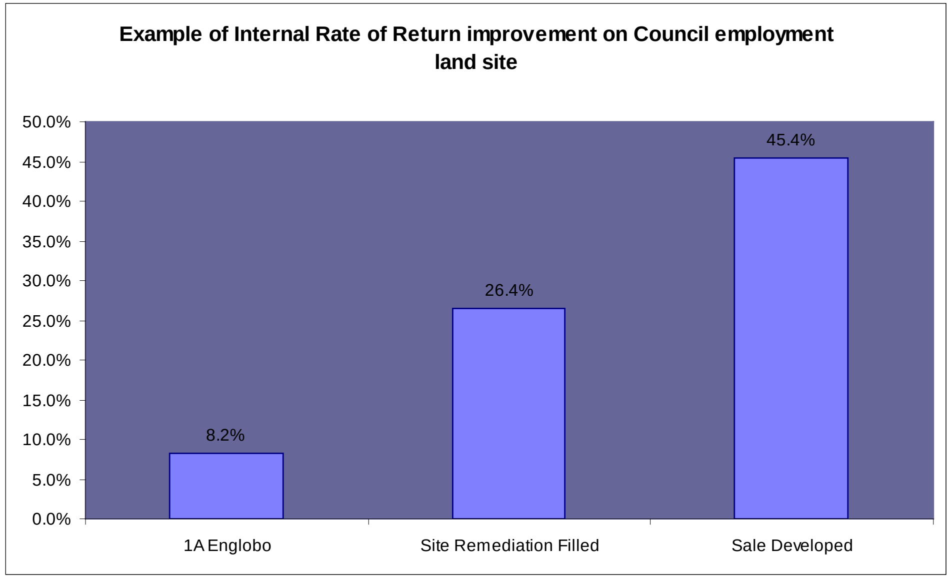
Below is a table of some of Councils largest buildings and structures. The list shows assets which are underway in terms of value add and disposal.

Asset Description	Estimated Cost to bring to Satisfactory Standard ($,000)	Rationalisation ($,000)
Newcastle - City Hall	27,120	
Civic West - Parking Station	8,500	**8,500**
Court House - Parking Station	* 7,500	*** 7,500**
The Mall - Parking Station	* 7,500	*** 7,500**
Frederick Ash Store - Burwood St	4,510	**4,510**
Lambton Swim Centre - Olympic Pool	3,920	
Civic Arcade	3,825	**3,825**
Mayfield Swim Centre - Olympic	2,160	
Stockton Swim Centre - Olympic	2,160	
Beresfield Swim Centre - Olympic	2,160	
Wallsend Swim Centre - Olympic	2,160	
Total	71,515	**31,835**
Total of all building and structures backlog	**85,284**	
Top 11 as a % of backlog	**84%**	**37%**

Note: The swimming centre upgrades are for filtration units only.

The diagrams below show the value potentially added on a parcel of land. The risk and return graph shows how that when a project is de-risked the value can increase. The Internal Rate of Return graph shows the potential value add of the underlying land value pre and post the de-risking process.

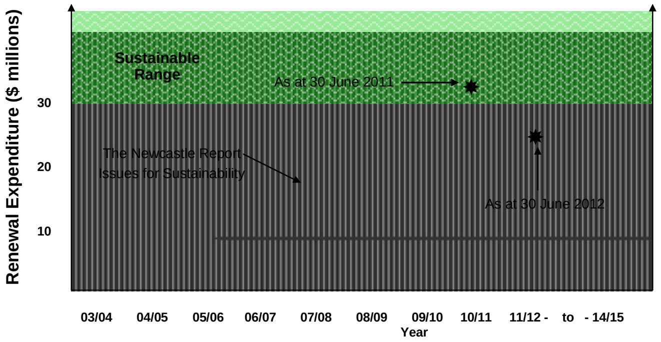




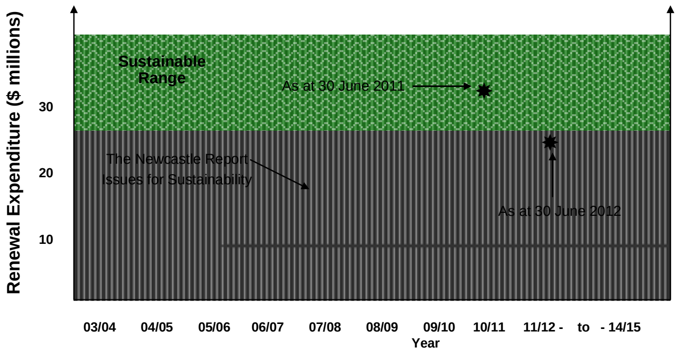
The other impact of asset disposal is the renewal or MAPPS budget becomes more effective at reducing the backlog.

The graphs below show sustainable range of maintenance and asset renewal comes down in scale once assets are disposed. The backlog will be more effectively addressed by the money spent and will reduce rather than increase.

Condition of Public Works (sustainable range pre asset disposal)



Condition of Public Works (post asset disposal)



7.2 Revenue Increase Options

All these options, with the exception of the pools entry fee, result in increased revenues.

7.2.1 Increase non-rate operating revenues

This option to improve revenues involves the following:

- City Hall would break even in 2014 with a net increase of $0.5 million annually
- Civic theatre to improve financial performance by $0.25 million in year two
- Airport Dividends received at a forecast 10% showing $3.2 million yield per year or at 8% at $2.5 million yield p.a
- Fort Scratchley entry and possible entry fees for other cultural venues
- SWMC improving margin by $0.5 million within one year
- BIAs become self funding with a year ($0.05 million)

How would this be achieved?

City Hall

This could be achieved by leasing out the space of City Hall where Council was simply a tenant of the building lease holder. As an example: Leasing may involve activities such as lawyer’s offices.

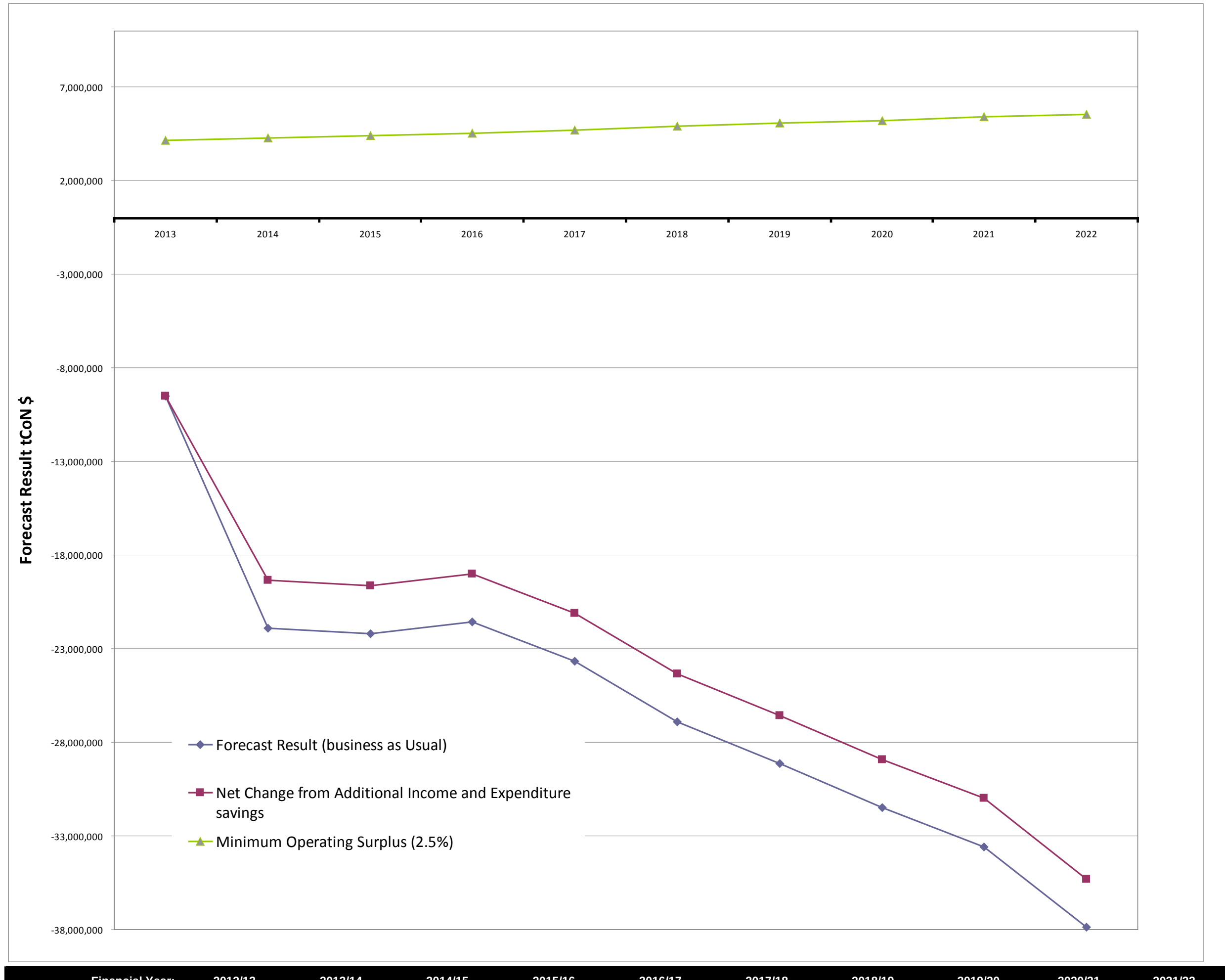
Civic Theatre

Income can be increased with the in-house operation of the Bars and a potential new tenant for the Brasserie restaurant.

Airport

Newcastle Airport Limited is well advanced towards implementing a restructure process which will enable dividends and potentially equity sell down for both Port Stephens and The City of Newcastle Councils.

The graph below shows the impact of an 8% dividend from the Airports profits.



Financial Year:	2012/13	2013/14	2014/15	2015/16	2016/17	2017/18	2018/19	2019/20	2020/21	2021/22	Total
Improvement on Deficit	- -	2,571,429 -	2,571,429 -	2,571,429 -	2,571,429 -	2,571,429 -	2,571,429 -	2,571,429 -	2,571,429 -	2,571,429 -	23,142,857

Fort Scratchley and other cultural venues

Increased revenues could be considered at sites such as the Art Gallery and Museum. A cost benefit analysis based on reduced numbers of entrants would need to be undertaken.

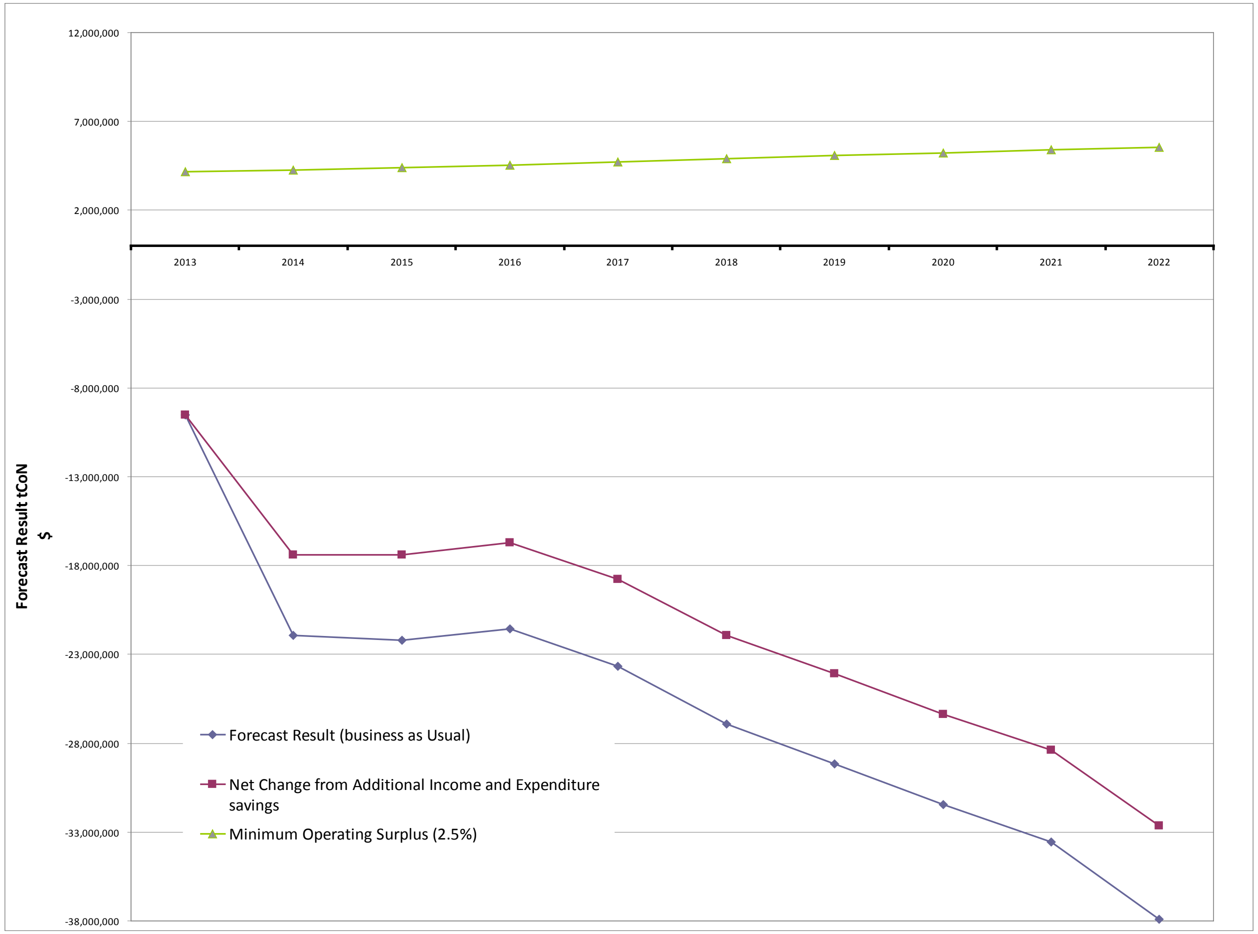
Summerhill Waste Management Centre

Improved performance of SMWC with the introduction of inert resource recovery within year one.

Business Improvement Association

Council currently pays for the BIA Co-ordinator. This cost could be recovered under the section 355 levy which currently provides funding to the BIA's.

The graph below shows the impact of these combined options.



Financial Year:	2012/13	2013/14	2014/15	2015/16	2016/17	2017/18	2018/19	2019/20	2020/21	2021/22	Total
Improvement on Deficit	-	- 4,514,286	- 4,809,786	- 4,865,628	- 4,923,425	- 4,983,245	- 5,045,159	- 5,109,239	- 5,175,563	- 5,244,207	- 44,670,538

7.2.2 Special Rate Variation(s) to support operations

Three options were modelled as follows:

- Two Section S508(A) over seven years
- One Section 508(2) over one year

The mechanism and definition of these options is outlined in section 2.2.2.

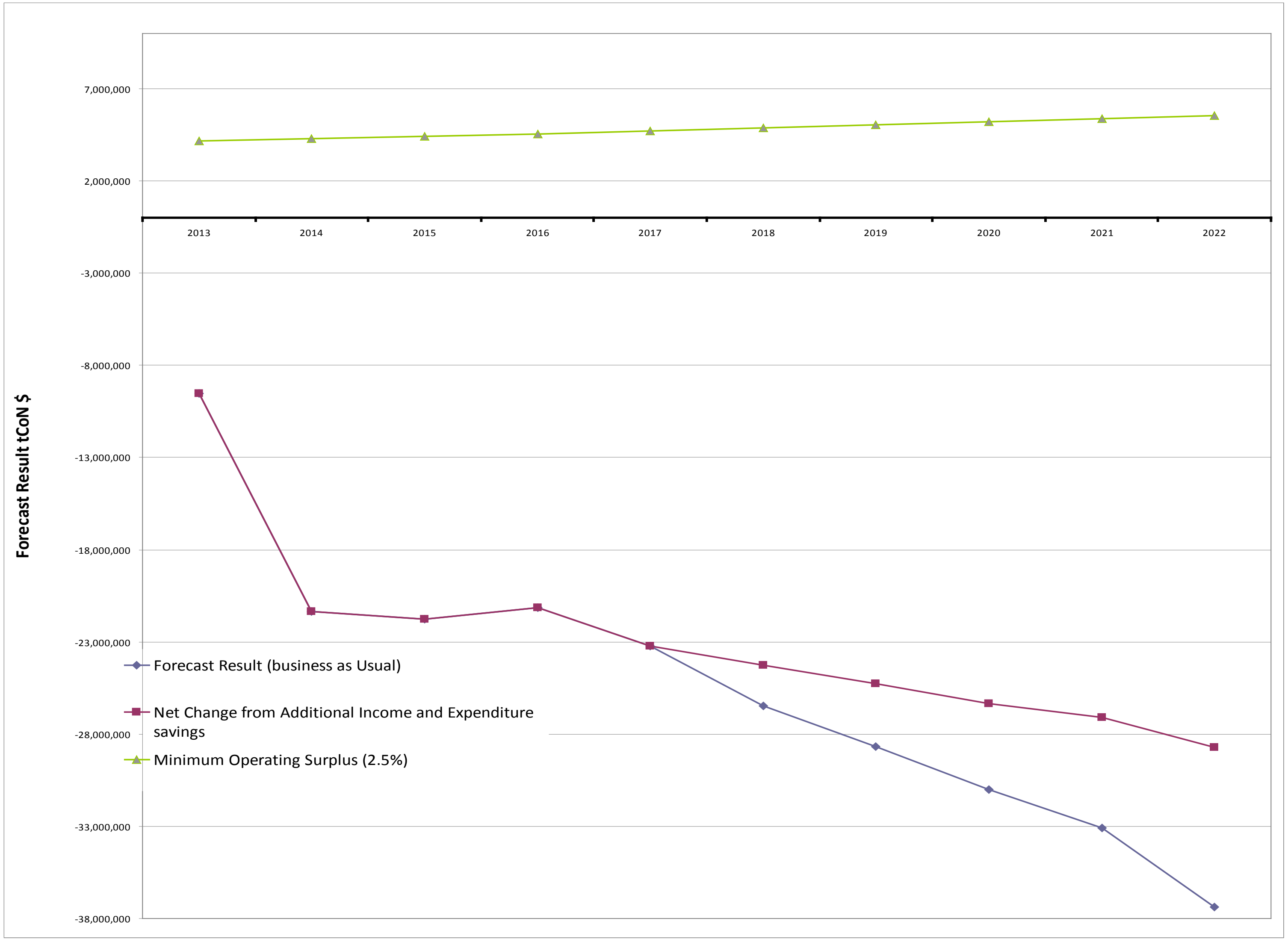
508(A) Option 1

This model shows the following increases in rates:

- 2018 2%
- 2019 1%
- 2020 1%
- 2021 1%
- 2022 2%

This represents a small increase in rates over a number of years above the cap. It should be noted that 508(A) allows a special rate for seven years. The above only includes four years and could include another three years of 1% increases post the life of this 10 year plan.

This option is graphed below.



Financial Year:	2012/13	2013/14	2014/15	2015/16	2016/17	2017/18	2018/19	2019/20	2020/21	2021/22	Total
Improvement on Deficit	-	-	-	-	-	- 2,195,779	- 3,397,969	- 4,655,620	- 5,985,754	- 8,659,828	- 24,894,950

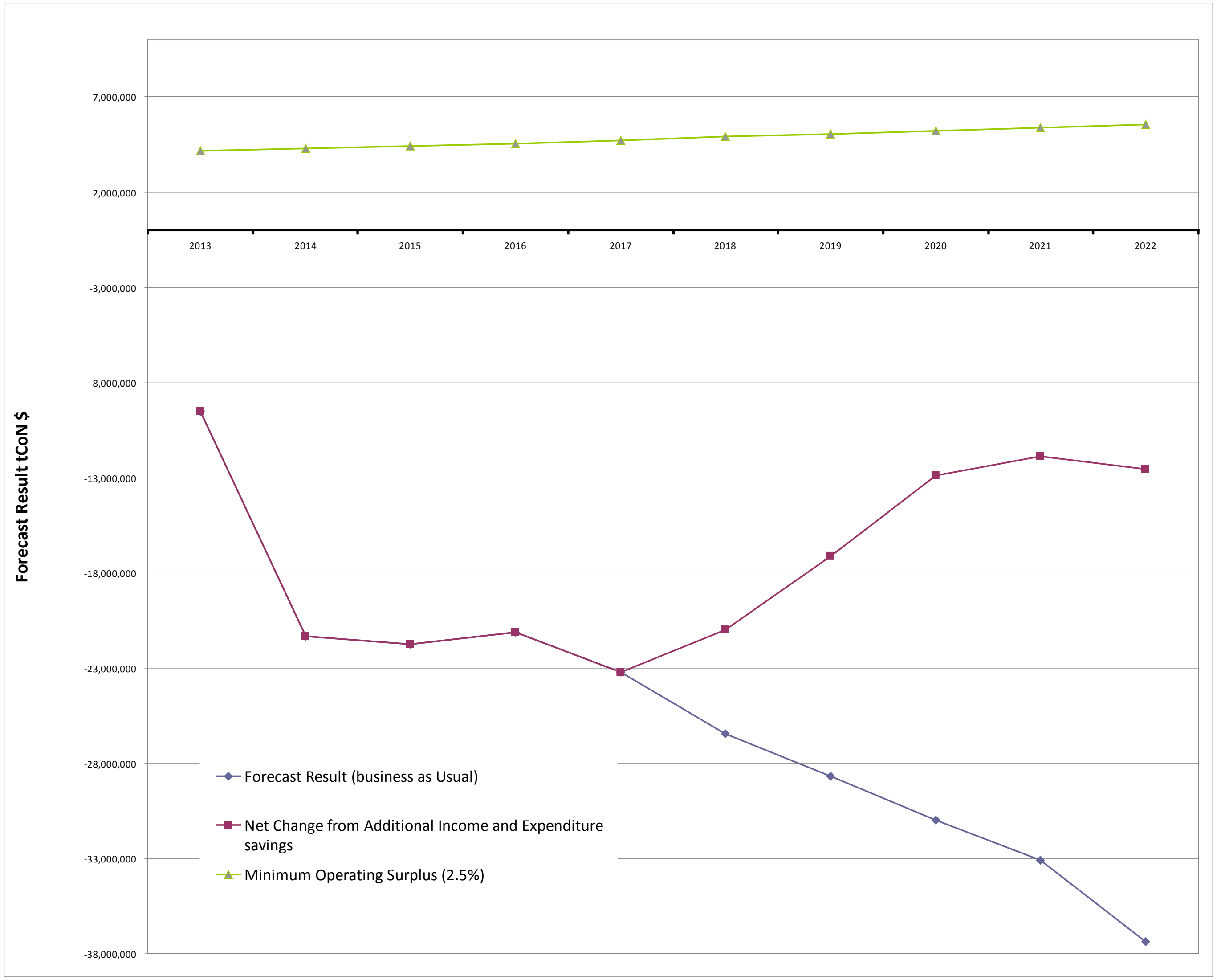
508(A) Option 2

This model shows the following increases in rates:

- 2017 5%
- 2018 5%
- 2019 5%
- 2020 2%

This model represents a moderate special rate over four years.

This impact is graphed below.



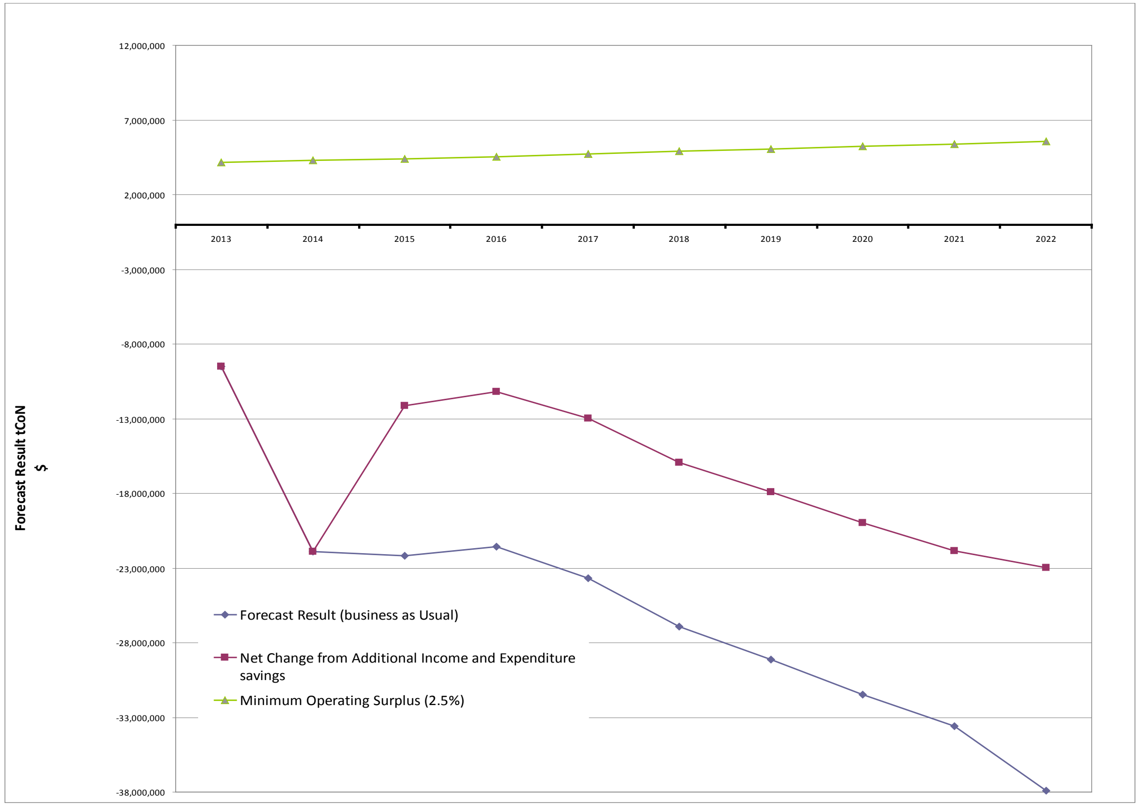
Financial Year:	2012/13	2013/14	2014/15	2015/16	2016/17	2017/18	2018/19	2019/20	2020/21	2021/22	Total
Improvement on Deficit	-	-	-	-	-	- 5,478,831	- 11,516,502	- 18,090,041	- 21,211,961	- 24,834,352	- 81,131,688

508(2) Option 3

This model shows the following increases in rates in one year as follows:

- 2015 10%

This model represents an increase in one year of 10% which then stays on the base indefinitely.



Financial Year:	2012/13	2013/14	2014/15	2015/16	2016/17	2017/18	2018/19	2019/20	2020/21	2021/22	Total
Improvement on Deficit	-	-	- 10,057,200	- 10,358,916	- 10,690,401	- 11,000,423	- 11,253,433	- 11,478,501	- 11,736,768	- 14,923,300	- 91,498,942

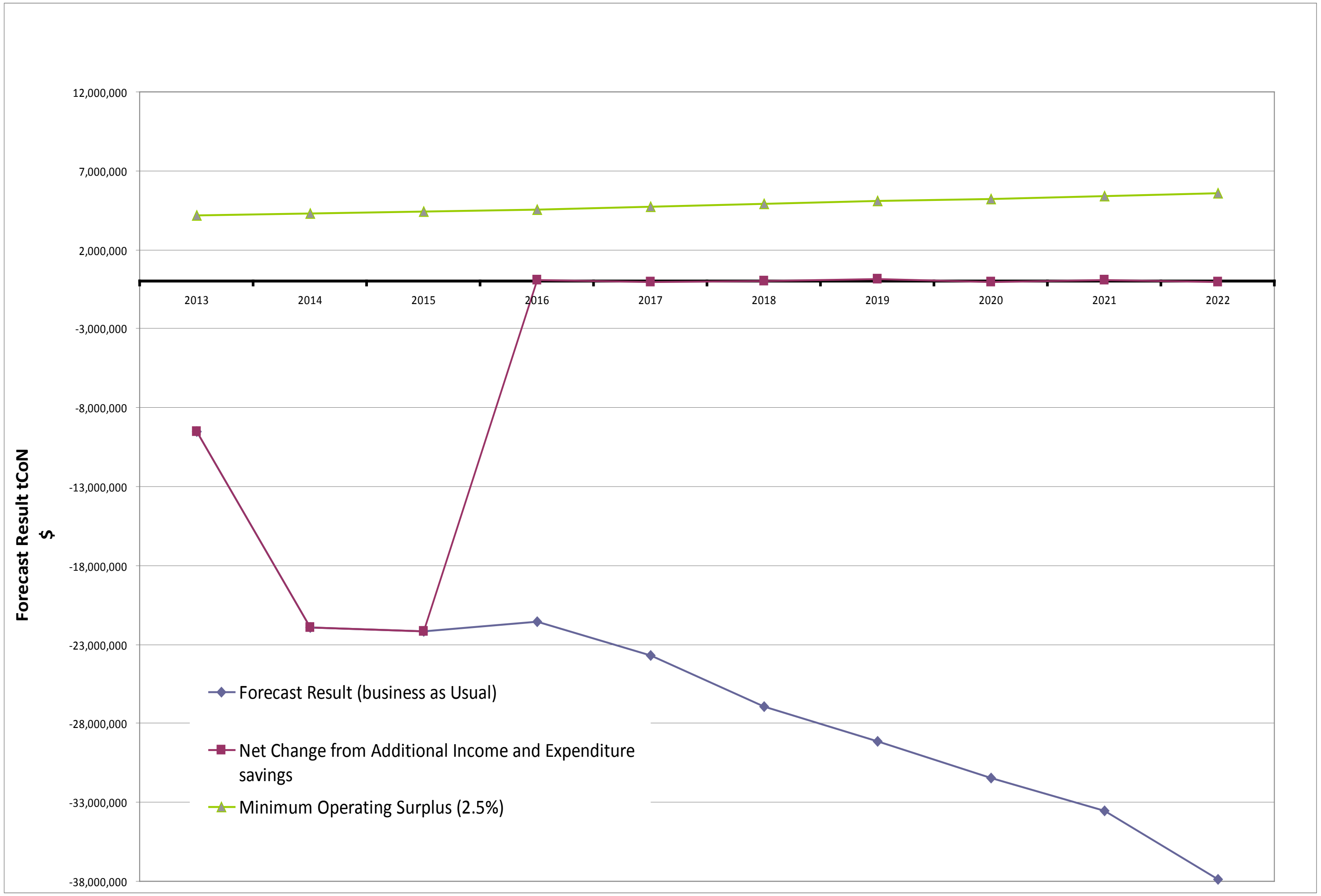
What would be required, in terms of rate increases, to remove the deficit?

The amount required initially to bring the budget back in surplus is very large. Then over the following years minor variations above the cap are required.

The following SRV Model S508 (A) would be required over the following years on top of the cap.

2015	21%
2016	1%
2017	2%
2018	1.2%
2019	1.1%
2020	1.0%
2021	2.2%

This is demonstrated in the graph below.



Financial Year:	2012/13	2013/14	2014/15	2015/16	2016/17	2017/18	2018/19	2019/20	2020/21	2021/22	Total
Improvement on Deficit	-	-	- -	21,648,123 -	23,619,133 -	26,968,003 -	29,264,935 -	31,440,972 -	33,639,350 -	37,833,402 -	204,413,919

How would these be achieved?

These options would meet the following IPART tests in accordance with the Special Variation Guidelines. IPART must assess special variation applications against the following criteria:

- Demonstrated need for the rate increase
- Demonstrated community support for the special variation
- Reasonable impact on ratepayers
- Sustainable financial strategy consistent with the principles of intergenerational equity
- Productivity improvements achieved and planned and
- Implementation of the Integrated Planning and Reporting framework.

7.3 Income Reduction Impacts

These models show the cessation of fees for parking (two hours free across the city) and pools entry.

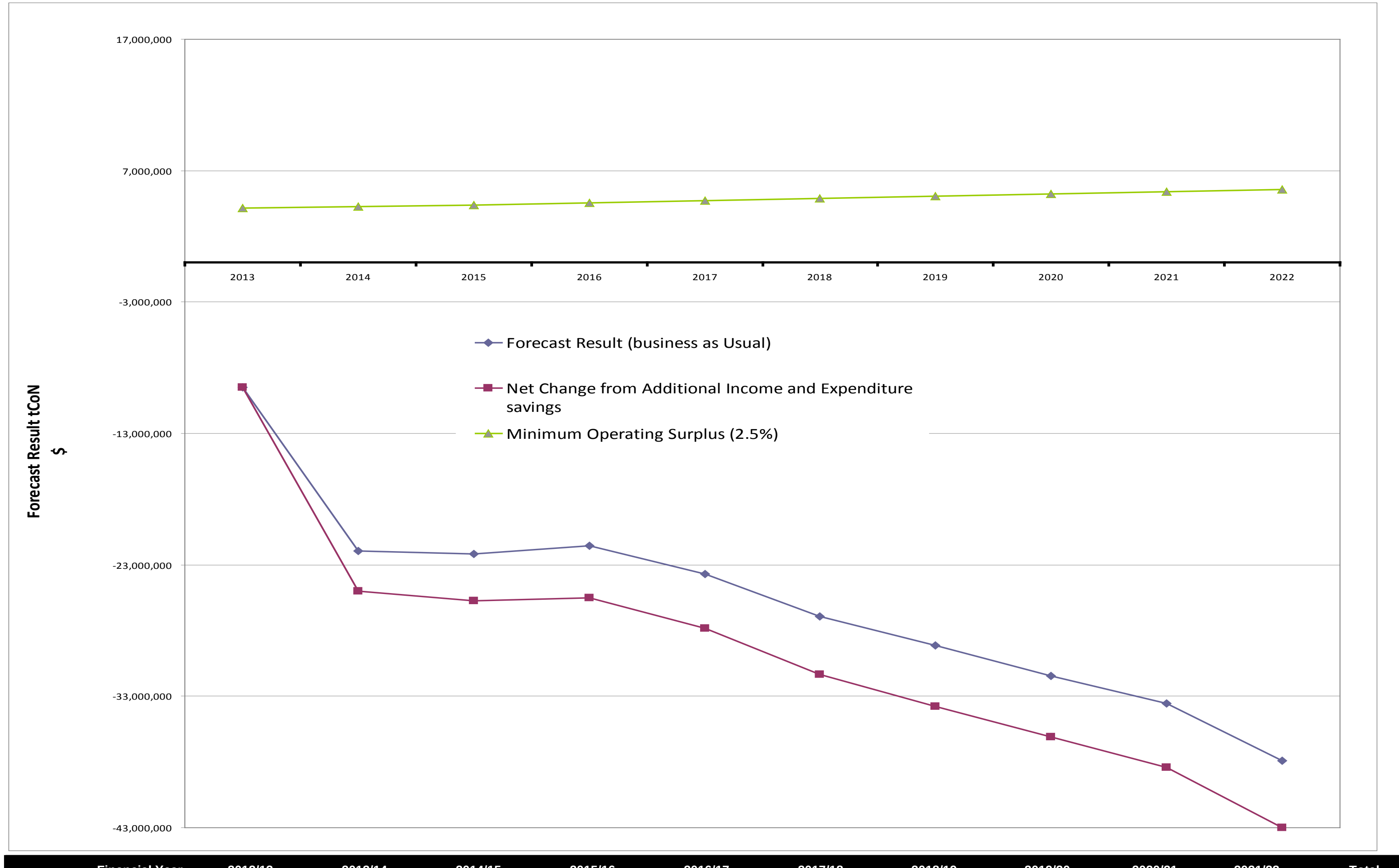
It should be noted that if Council chooses any of these options the base deficit curve drops and will need to be used as the base underlying deficit for any of the expenditure reduction strategies or income improvement strategies.

The following models have been constructed to show the further impacts of income reduction. These are as follows:

7.3.1 Income reduction – 2 hours free parking across the City

A recent Council resolution requested Management to investigate the impact of two hour free parking across the City.

The impact of this request is illustrated in the graph below.

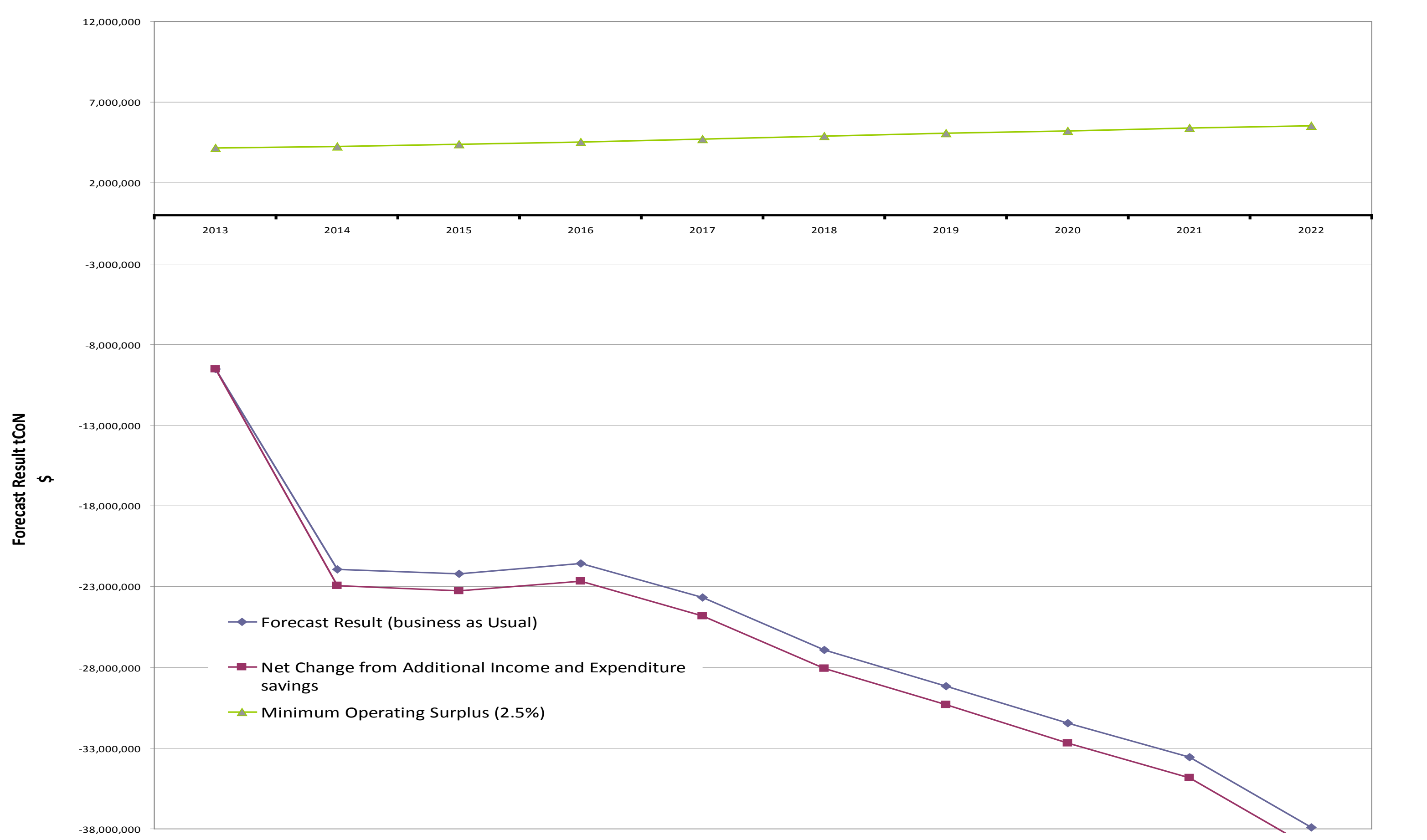


Financial Year:	2012/13	2013/14	2014/15	2015/16	2016/17	2017/18	2018/19	2019/20	2020/21	2021/22	Total
Decline in Deficit	-	3,085,437	3,520,395	3,973,346	4,178,713	4,394,641	4,621,667	4,616,465	4,854,353	5,104,436	38,349,453

7.3.2 Income reduction – pools free entry

A recent Council Notice of Motion Resolution sought to provide free entry to inland pools.

The impact of this request is illustrated in the graph below.



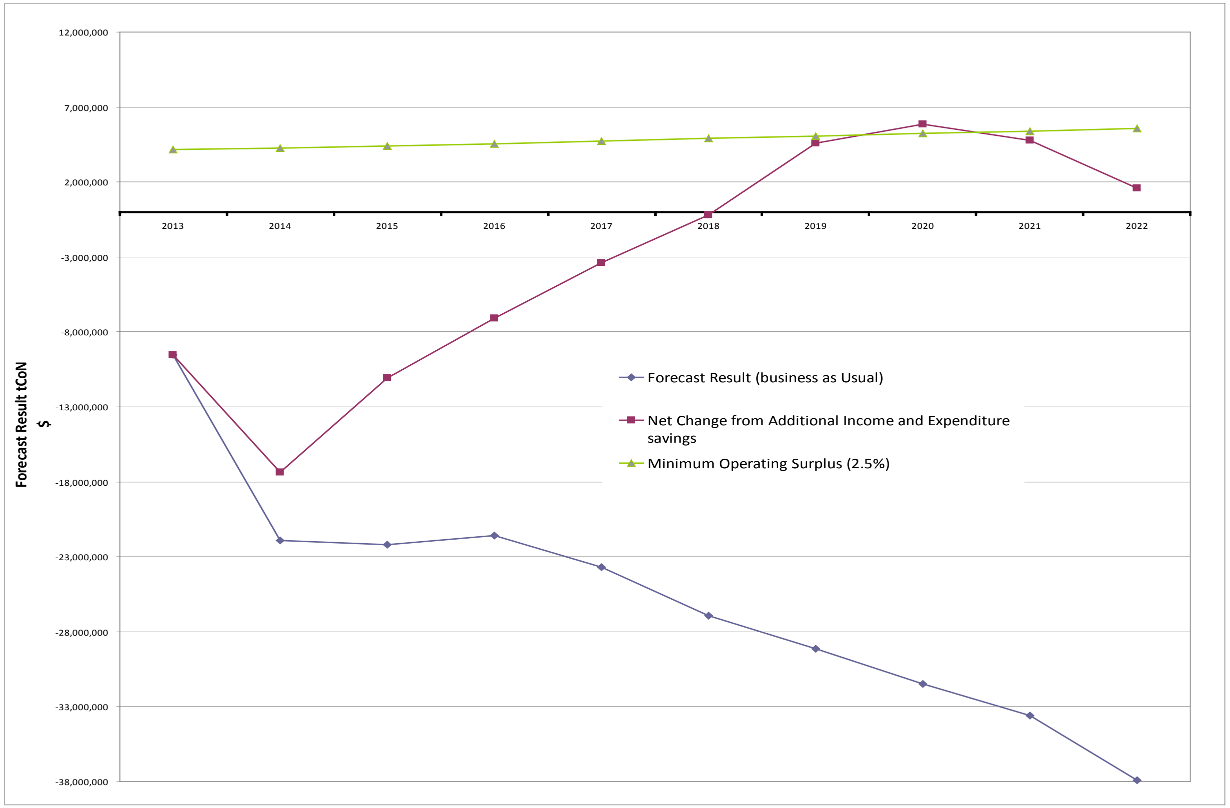
Financial Year:	2012/13	2013/14	2014/15	2015/16	2016/17	2017/18	2018/19	2019/20	2020/21	2021/22	Total
Decline in Deficit	-	1,023,433	1,054,136	1,085,760	1,118,333	1,151,883	1,186,439	1,222,032	1,258,693	1,296,454	10,397,163

7.4 Hybrid (Expenditure/Revenue) Options

7.4.1 Option 1

This Option involves achieving post ERP implementation savings, 11 service element savings, achieving breakeven on income producing entities and adopting a SRV over 4 years. This model sees the organisation reach sustainability by 2017/2018.

This is graphed below.



Financial Year:	2012/13	2013/14	2014/15	2015/16	2016/17	2017/18	2018/19	2019/20	2020/21	2021/22	Total
Improvement on Deficit	-	- 4,550,000	- 11,134,250	- 14,475,386	- 20,295,104	- 26,722,198	- 33,725,622	- 37,306,074	- 38,358,356	- 39,473,616	- 226,040,605

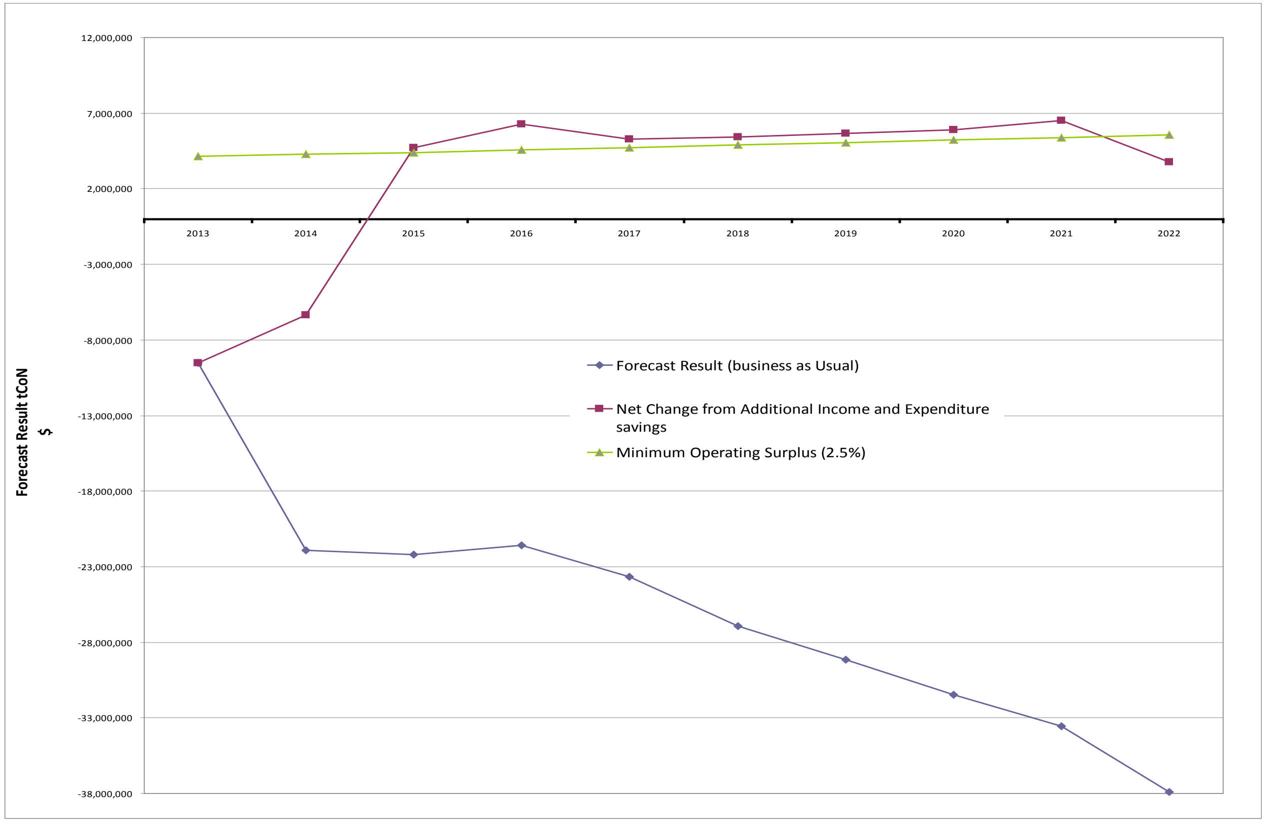
7.4.2 Option 2

This Option involves achieving:

- Post ERP savings;
- 5% operational budget expenditure reductions (reduction over two years which has a cumulative impact of 10.25%);
- 8% Airport dividends; and
- SRV over five years.

This model sees the organisation reach sustainability by 2015/2016.

This option is graphed below.



Financial Year:	2012/13	2013/14	2014/15	2015/16	2016/17	2017/18	2018/19	2019/20	2020/21	2021/22	Total
Improvement on Deficit	- -	15,561,025 -	26,887,157 -	27,859,746 -	28,981,710 -	32,353,659 -	34,795,882 -	37,359,122 -	40,064,339 -	41,659,245 -	285,521,886

7.4.3 Option 3

This Option takes into account reduction in income if two hour free-parking is implemented across the entire precinct and some additional options needed to offset them.

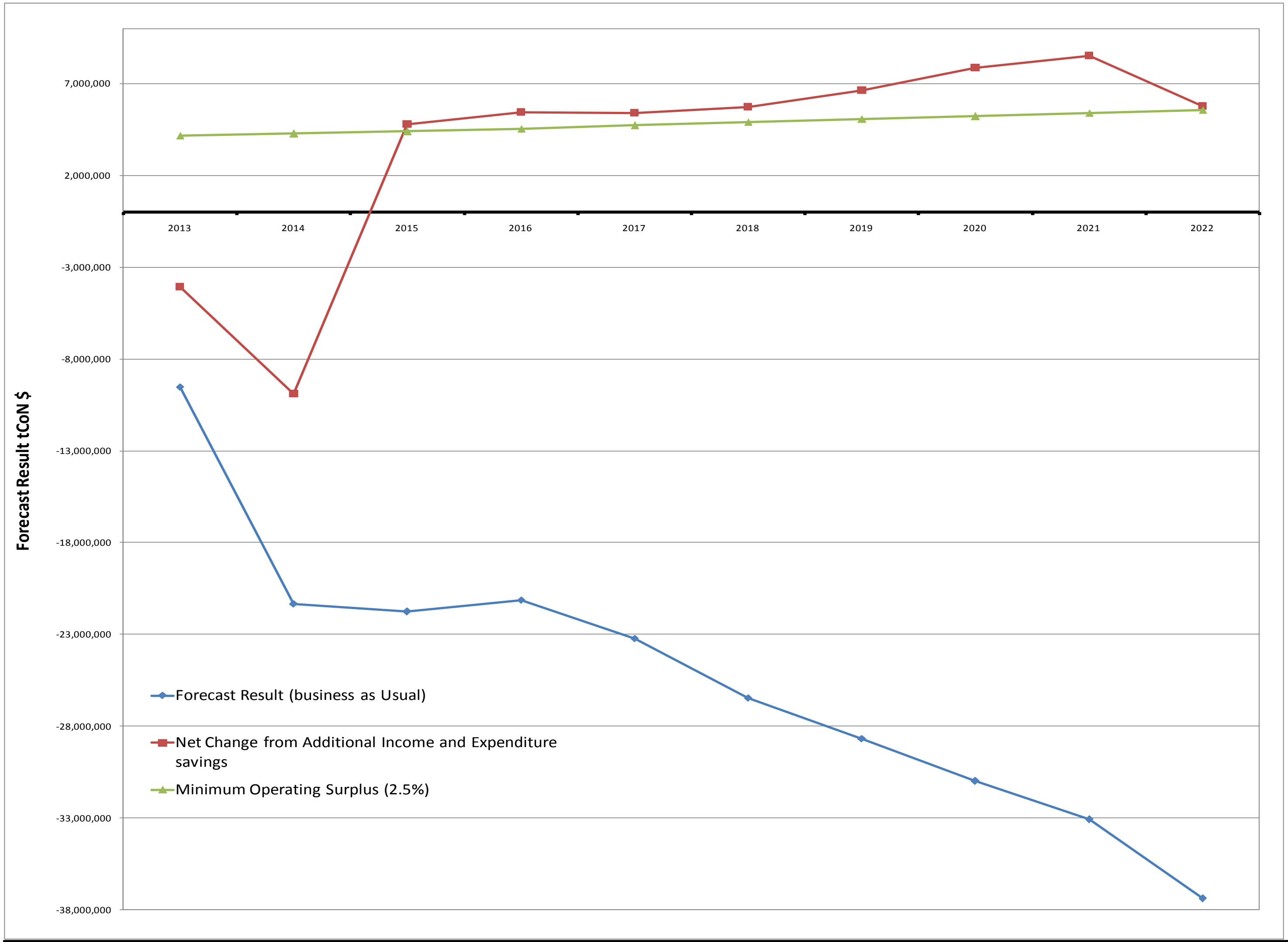
Financial Year:	2012/13	2013/14	2014/15	2015/16	2016/17	2017/18	2018/19	2019/20	2020/21	2021/22	Total
Reduction in Income	-	3,085,437	3,520,395	3,973,346	4,178,713	4,394,641	4,621,667	4,616,465	4,854,353	5,104,436	38,349,453

This involves achieving:

- Post ERP savings
- 5% operational budget expenditure reductions (reduction over two years which has a cumulative impact of 10.25%)
- 8% Airport dividends and
- SRV over seven years (10.5%).

This model sees the organisation reach sustainability by 2015/2016.

This option is graphed below.



Financial Year:	2012/13	2013/14	2014/15	2015/16	2016/17	2017/18	2018/19	2019/20	2020/21	2021/22	Total
Improvement on Deficit	- 5,454,626	- 11,460,432	- 26,535,845	- 26,558,800	- 28,629,810	- 32,176,081	- 35,292,005	- 38,836,403	- 41,585,714	- 43,161,719	- 289,691,435

7.4.4 Option 4

This Option also takes into account the income reduction if two hour free-parking is implemented across the entire precinct from the 1 July 2013.

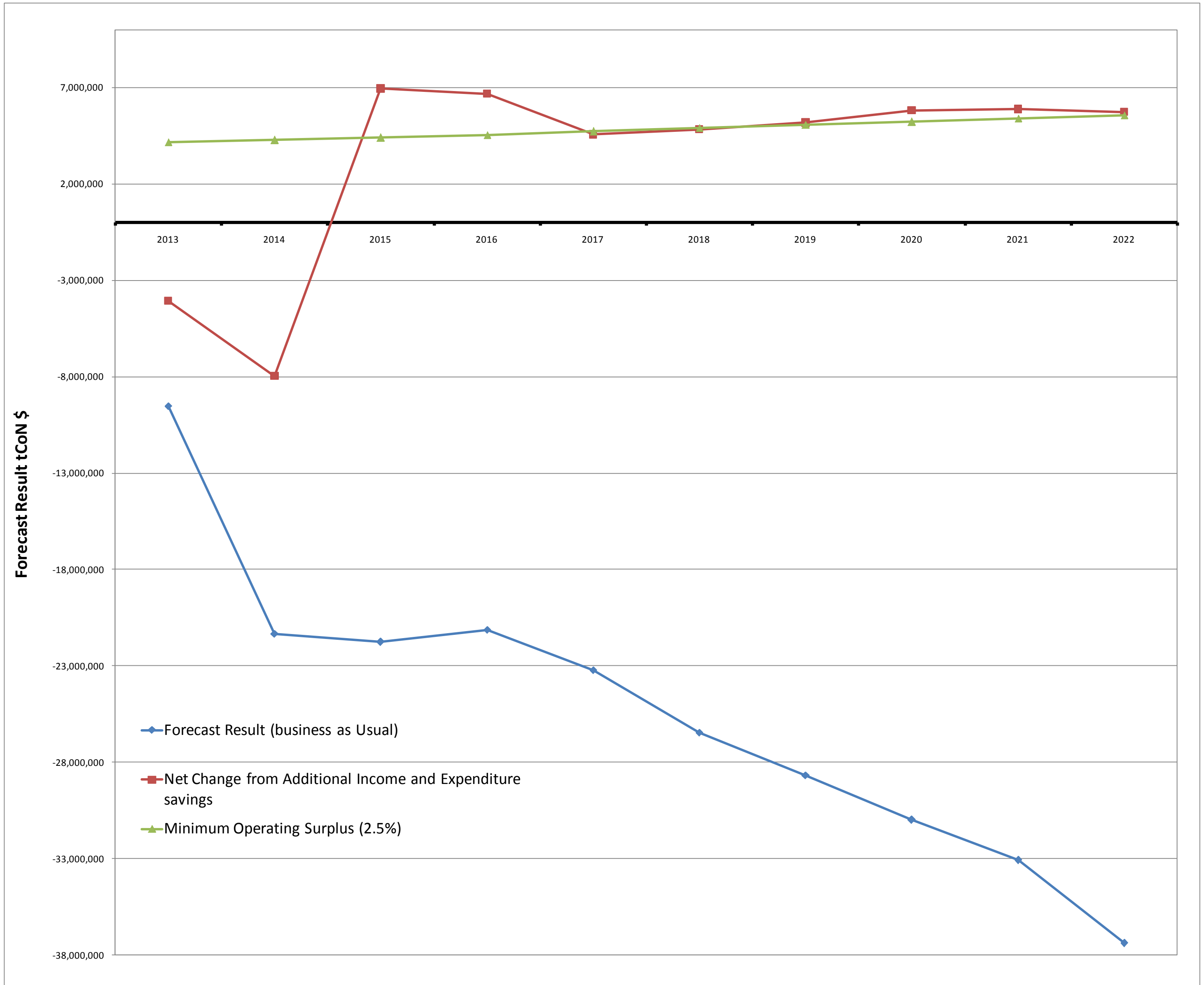
Financial Year:	2012/13	2013/14	2014/15	2015/16	2016/17	2017/18	2018/19	2019/20	2020/21	2021/22	Total
Reduction in Income	-	3,085,437	3,520,395	3,973,346	4,178,713	4,394,641	4,621,667	4,616,465	4,854,353	5,104,436	38,349,453

Deficit reduction will be achieved using:

- Post ERP savings
- 6% operational budget expenditure reductions (reduction over two years which has a cumulative impact of 12.36%)
- 8% Airport dividends and
- SRV over five years (6.5%).

This model sees the organisation reach sustainability by 2015/2016.

This option is graphed below.



Financial Year:	2012/13	2013/14	2014/15	2015/16	2016/17	2017/18	2018/19	2019/20	2020/21	2021/22	Total
Reduction in Income	- 5,454,626	- 13,369,780	- 28,703,972	- 27,790,839	- 27,784,122	- 31,286,434	- 33,838,042	- 36,799,048	- 38,948,073	- 43,104,669	- 287,079,605

8. Recommended Option

The following option is recommended. (This option assumes that two hour free parking across the city does not continue past January 2013)

Hybrid Option 2

The Hybrid Option 2 offers a combination of organisation efficiencies and savings in the first two years, improved financial performance of commercial venues and a special rate variation from financial year 2017/2018.

This option has the following features:

Post ERP Savings

These saving are $2 million in year 2014/2015. They will need to be achieved through efficiency and staff number gains following the implementation of the new enterprise system in 2015. The total value of these savings over **10 years is $13.5 million.**

Energy Savings

By setting a target each year for energy savings, changing practice and implementing simple technology a forecast annual $0.268 million savings will occur by 2014. The total savings for the **10 year period is $6.4 million.**

5% Budget cuts over two years

This initiative has a cumulative impact of **10.25% over two years and results in a total saving s of $189.7 million over 10 years**. The budget savings will be accomplished through:

- Service reduction
- Service level variation
- Contract market testing
- Sustainably savings not yet achieved
- Service review savings not yet achieved
- EFT reductions and
- Material costs reductions.

In order for this to be achieved each Director and Manager will be given a maximum budget allocation for each year and the mangers will provide initiatives to achieve these savings. Any service level or service change will require a Council Resolution. The detailed plan will be provided to Council through the budget process and the creation of the next Long Term Financial Plan.

Maintenance savings and capital raising from asset disposal

Based on an asset disposal program there will be maintenance and operational savings. In addition there will be capital raised through the sales. This capital should be put into a concerted effort to remove the asset backlog over the next 5 years. The **total raised for the 10 year period is $5.3 million**.

City Hall

City Hall will need to breakeven by 2015. This will be achieved through higher levels of bookings, better utilisation of rooms including leasing out some of the rooms to commercial tenants. The total additional income raised over **the 10 years will be $5 million**.

Civic Theatre

The Civic Theatre will provide improved financial performance by an additional $250,000 by 2014. This will result in **$2.2 million increased revenue over the 10 year** period.

NAL Dividends

The Newcastle Airport is currently being restructured. Once complete the Airport will pay both Port Stephens and Newcastle Councils a dividend on profits. This dividend will be up to 10% per annum. A conservative 8% has been forecast in this plan. **This return will provide $23 million over 10 years**.

Fort Scratchley, Museum and Art Gallery

Entry fees will need to be applied to raise an additional $250,000 by 2014. **This will achieve $2.5 million over the 10 years**.

Summerhill Waste Management Centre

The improved position will be required by 2014 by $0.5 million per annum. **This will raise an additional $5.1 million in 10 years**.

BIAs

Business Improvement Associations are rate funded. This service should be full cost recovery. **This will cost recover $0.5 million over 10 years**.

Child Care Services

Child care services will pay leases or costs will be reduced through disposal depending on the outcome of the Service Review. The income or savings to be achieved will be $0.5 million by 2014. **The total for the 10 year period will be $5 million**.

Special Rate Variation

A SRV will need to be applied for and granted by 2017/2018. The SRV will be a S508 (A) maximum seven years.

The following increases above the rate cap will need to be achieved over five years:

- 2018 2%
- 2019 1%
- 2020 1%
- 2021 1%
- 2022 2%

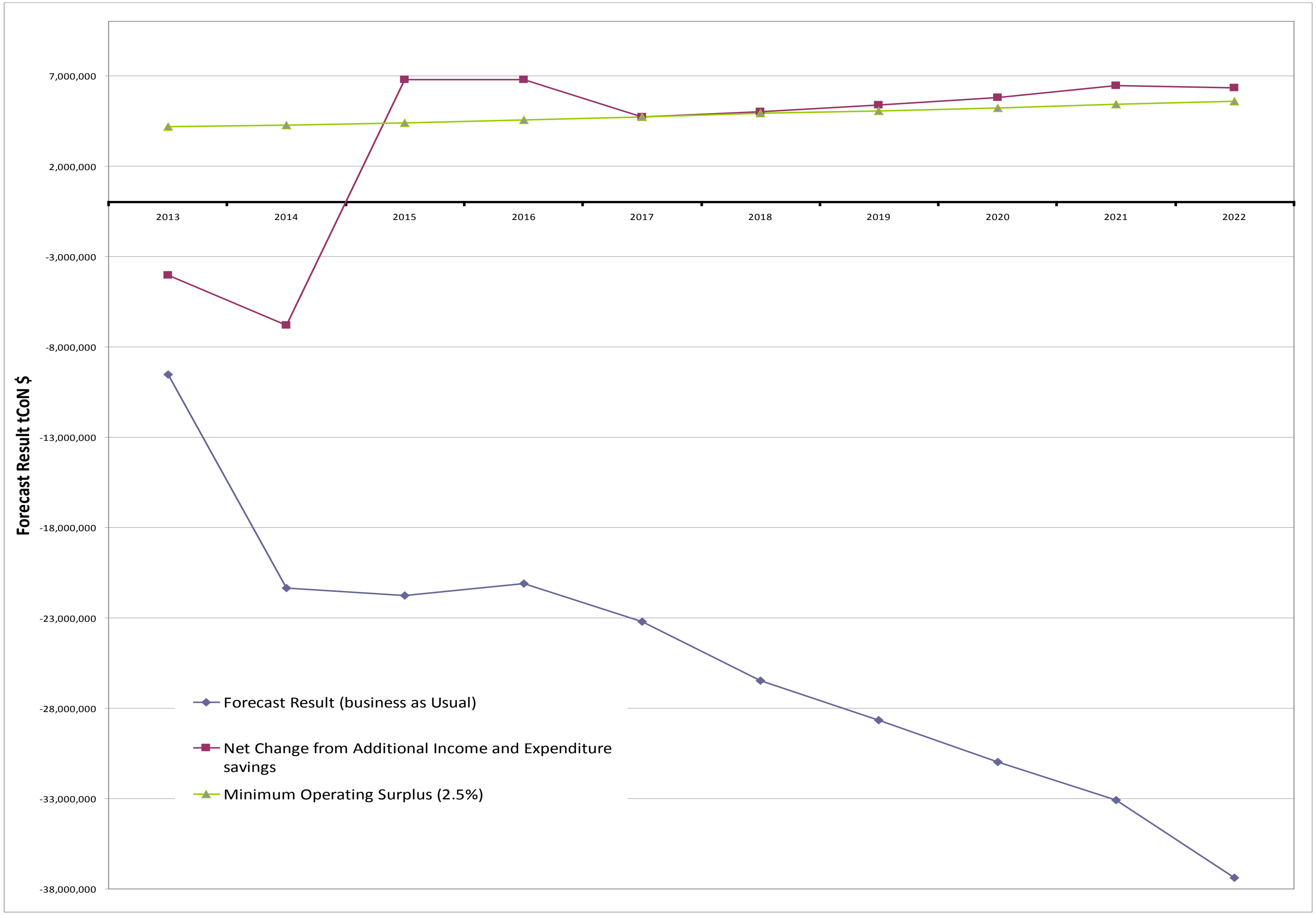
This will raise $24.8 million over 10 years.

Summary

The following table outlines the incomes and saving necessary in $ year by year in order to meet the target outlined.

	2012/13 $'000	*2014 $'000*	*2015 $'000*	*2016 $'000*	*2017 $'000*	*2018 $'000*	*2019 $'000*	*2020 $'000*	*2021 $'000*	*2022 $'000*	**Total**
Savings	5,455	10,509	23,392	22,647	22,528	23,718	24,946	26,280	27,567	28,926	215,967
Additional Income	-	3,621	4,167	4,223	4,281	6,537	7,801	9,123	10,519	13,262	73,854
Total	5,455	14,130	27,559	26,870	26,809	30,255	32,747	35,402	38,086	42,188	289,821

The forecast surplus (deficit) line for the next 10 years is outlined below along with a reconstituted profit and loss statement.



Financial Year:	2012/13	2013/14	2014/15	2015/16	2016/17	2017/18	2018/19	2019/20	2020/21	2021/22	Total
Improvement on Deficit	- 5,454,626	- 14,545,869	- 28,526,954	- 27,909,420	- 27,922,837	- 31,445,638	- 34,017,991	- 36,755,991	- 39,525,542	- 43,716,097	- 289,820,965

Income and Expenditure Statement

NCC - Long Term Financial Plan

For the year ended 30 June	Notes	2012/13 $'000	2014 $'000	2015 $'000	2016 $'000	2017 $'000	2018 $'000	2019 $'000	2020 $'000	2021 $'000	2022 $'000
Operating Revenue											
Rates & charges		111,544	114,727	118,106	121,059	124,691	130,502	134,656	138,538	142,881	148,841
User charges & fees		55,198	57,963	60,085	63,232	66,545	70,032	73,702	77,565	81,632	85,913
Interest		6,849	6,858	6,636	6,967	7,316	7,681	8,066	8,469	8,892	9,337
Other operating revenues		10,195	13,163	14,362	14,848	15,355	15,883	16,432	17,004	17,600	18,221
Grants & contributions - Operating		23,706	24,419	24,998	25,798	26,597	27,262	27,862	28,545	29,287	30,048
Total Operating Revenue		207,490	217,130	224,186	231,904	240,504	251,361	260,718	270,122	280,293	292,359
Operating Expenses											
Employee costs		88,453	86,482	81,978	84,638	87,385	90,221	93,149	96,172	99,293	102,515
Borrowing costs		3,925	4,517	5,107	5,270	5,434	5,570	5,692	5,832	5,983	6,139
Materials & contracts		41,071	39,843	38,909	42,022	45,383	49,014	52,935	57,170	61,744	66,683
Depreciation & amortisation	1	40,230	53,069	51,769	53,426	55,082	56,459	57,701	59,115	60,652	62,229
Other operating expenses		61,556	59,599	58,179	59,865	62,577	65,432	68,451	71,576	74,972	78,531
Total Operating Expenses		235,235	243,510	235,941	245,221	255,861	266,695	277,928	289,865	302,644	316,097
Total Operating Revenue Less Operating Expenditure		(27,745)	(26,381)	(11,755)	(13,317)	(15,357)	(15,335)	(17,210)	(19,743)	(22,351)	(23,738)
Capital Revenues											
Grants & contributions - Capital	2	9,079	6,781	6,828	6,958	7,081	7,183	7,275	7,380	7,493	7,610
Proceeds from the sale of Assets		8,606	1,853	4,292	3,572	1,846	983	1,229	1,862	1,806	1,485
Total Capital Raising revenue		17,685	8,634	11,120	10,530	8,927	8,166	8,504	9,242	9,300	9,095
Nett Suplus(deficit) after capital revenue		(10,060)	(17,747)	(636)	(2,787)	(6,430)	(7,169)	(8,706)	(10,501)	(13,051)	(14,642)
Add back Depreciation		40,230	53,069	51,769	53,426	55,082	56,459	57,701	59,115	60,652	62,229
Funding available for capital expenditure		30,171	35,322	51,133	50,639	48,652	49,290	48,995	48,614	47,600	47,586
Capital Expenses											
Capital Expenditure on Asset renewals	3	42,947	39,767	41,687	49,936	46,402	43,188	44,997	48,857	46,209	45,489
Total capital spend on renewals		42,947	39,767	41,687	49,936	46,402	43,188	44,997	48,857	46,209	45,489
Net Transfers from/(to) reserves		(145)	(11,799)	(10,798)	(2,033)	(3,422)	(6,728)	(3,989)	966	434	(227)
Net Loans Borrowings/(Repayments)		10,000	10,000	10,000	10,000	10,000	10,000	10,000	10,000	10,000	10,000
Net Overall Funding Surplus/(Deficit)		**(2,921)**	**(6,244)**	**8,649**	**8,669**	**8,828**	**9,374**	**10,009**	**10,723**	**11,825**	**11,870**
Parking Meter Adjustments											
Halt Meter Expansion and No Weekend Meters City East and City West	**5**	1,143	1,128	2,312	2,324	4,582	4,850	5,132	5,440	5,868	6,044
Net Overall Funding Surplus/ (Deficit) after Parking Meter Adjustments		**(4,064)**	**(7,372)**	**6,336**	**6,345**	**4,246**	**4,524**	**4,877**	**5,282**	**5,957**	**5,825**

Appendix A

Assumptions used in constructing the LTFP Model

The adopted 2012/2013 Operational Plan is the base budget for the Long Term Financial Plan. The plan also incorporates the four year Delivery Program. These documents were adopted by Council on 21 June 2011. Council also adopted the 2011/2012 – 2015 Delivery Program.

The following assumptions have been used as the basis for the 10 year the Long Term Financial Plan.

A.1 General Assumptions

A.1.1 Population

The Community Strategic Plan details expected population growth to 2030. The Australian Bureau of Statistics Census of Population and Housing 2006 and 2011 statistics show the number of total **dwellings to be 65,939** with a **population of 148,531** (this is up from 141,753 population (0.96% per year) and 63,409 (0.8% per year) dwellings in 2006).

It is predicted The City of Newcastle will have a population **165,600 in 2021, representing an estimated average annual growth rate of 1%**.

A.1.2 Inflation

The CPI is a measure of the price movements of a standard basket of consumer goods. In the Local Government environment, however, CPI alone is not a sufficient measure of the rise in costs. The Long Term Financial Plan includes other assumptions to provide a more accurate reflection of the estimated rise in costs. Where these have been used they have been detailed accordingly.

Unless otherwise indicated, the CPI index forecasts have been used as the basis of preparation of the Long Term Financial Plan. These index values are:

CPI Forecast	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
	3.00%	3.00%	2.20%	2.70%	3.20%	3.10%	2.50%	2.20%	2.45%	2.60%	2.60%

Term Australian Economic Forecast

A.1.3 Cash reserves

Reserve funding is made in accordance with Council's Reserves Policy and accompanying plans.

The cash reserves consist of a combination of statutory reserves underpinned by legislation and non-statutory reserves. The Policy position on the non-statutory reserves are supported by Council's adopted Reserves Policy as well as existing and future resolutions made by Council on funding restrictions.

A.1.4 Borrowings

All borrowings are made in accordance with the standards set by the Division of Local Government's Minister's Borrowing Order and Council's Borrowing Policy and Strategy which underpin the requirements of the *Local Government Act 1993* and the *Local Government (General) Regulations 2005*.

Council's resolution of 21 June 2011 included a commitment for Council to seek to rationalise its borrowings.

Planned borrowings for The City of Newcastle for future years are:

Borrowings(planned)	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
	$10m	$10m	$10m	$10m	$10m	$10m	$10m	$10m	$10m	$10m	$10m

All new loans would be raised from appropriate financial institutions and be secured by charge on the income of Council.

Council has notified the DLG of its intent to borrow **$10 million to fund capital expansion works at Newcastle Airport Limited**. The borrowing has been excluded from the Long Term Financial Plan as there will be no additional cost to ratepayers or impact on the balance sheet.

A.2 Operating Revenue Assumptions and Forecasts

A.2.1 Rates and annual charges

Currently, councils are subject to the NSW State Government's allowable maximum annual increase in rates (rate pegging) with allowances made for the addition or reclassification of properties.

The following scenarios have been included:

Ordinary rates

- Set at CPI rate (base) adjusted for the industry productivity factor
- Special variation of 5% from 2012/2013 for the SRV projects listed above.

Rates & Charges	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
	3.60%	2.80%	2.00%	2.50%	3.00%	3.20%	2.90%	2.30%	2.00%	2.25%	2.40%

Annual charges

- Waste Management Service Charges (WMSC) - the domestic and business waste management service charges are estimated to increase over the life of the Long Term Financial Plan and reflect the actual cost of the provision of the service. Included in the service charge is the NSW State Government Waste Levy as set by the Department of Environment, Climate Change and Water. The levy per tonne of waste is anticipated to steadily increase over the life of the Long Term Financial Plan.

  The WMSC also reflects the anticipated approval by the Department of Climate Change and Water for the extension of the current waste licence at Summerhill Waste Management Centre to 2034.

  It is also assumed that a Waste Recovery Centre will be operational from 2011/2012.

- Stormwater Management Service Charges (SWMSC) - the stormwater management service charge funds enhanced stormwater related works and services program.

DWMS	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
	0.62%	5.12%	2.20%	2.70%	3.20%	4.81%	4.81%	4.81%	4.81%	4.81%	4.81%

A.2.2 User fees and charges

The Revenue Policy requires all non-statutory fees and charges to be reviewed annually and on a full cost recovery basis. It is assumed that price increases will continue on this basis.

User fees and charges	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
	4.53%	11.03%	2.20%	2.76%	5.30%	5.30%	5.30%	5.30%	5.30%	5.30%	5.30%

This is made up of:

Fees, charges and other income	2012/13	2013/14	2014/15	2015/16	2016/17	2017/18	2018/19	2019/20	2020/21
User fees and charges:									
Waste Collection	5.00%	5.00%	5.00%	5.00%	5.00%	5.00%	5.00%	5.00%	5.00%
Parking Stations and Meters	2.42%	2.40%	2.60%	2.50%	2.50%	2.50%	2.50%	2.50%	2.50%
Stockton Caravan Park	41.71%	3.37%	3.26%	3.30%	3.30%	3.30%	3.30%	3.30%	3.30%
Other user fees and charges	7.72%	5.58%	5.08%	6.13%	6.13%	6.13%	6.13%	6.13%	6.13%
Other income	5.95%	.62%	1.06%	2.54%	3.45%	2.50%	2.20%	2.45%	2.60%

A.2.3 Interest on investments

Investments are placed and managed in accordance with the standards set by the Division of Local Government Minister's Investment Order, Council's Investment Policy and Strategy which underpin the requirements of the *Local Government Act 1993* and the *Local Government (General) Regulations 2005* Investment returns have been based on current portfolio returns with due consideration of Westpac's long term projection of interest rates.

Interest	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
	6.00%	5.00%	5.00%	5.00%	5.00%	5.00%	5.00%	5.00%	5.00%	5.00%	5.00%

A.2.4 Other revenues

A.2.5 Grants and contributions (operating)

Grants include tied and special purpose grants. Generally, all grants are indexed by the CPI. The major component of grants is the Federal Assistance Grant. Contributions consist of operating and capital components.

Grants and contributions - operating	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
	4.17%	14.65%	3.01%	2.37%	4.13%	4.13%	4.13%	4.13%	4.13%	4.13%	4.13%

A.3 Operating Expenditure (expenditure assumptions and forecasts)

A.3.1 Employee costs and benefits

Salaries and Wages

Wages and salaries costs consist of two components:

1. Award increases under the City of Newcastle Enterprise Agreement and the Local Government (State) Award
2. Salary review process increases, including position and job re-evaluations

Staffing levels are based on the Workforce Management Plans in line with service level expectations.

A3.2 Retirement benefit obligations

The Council contributes, on behalf of its employees, to the following superannuation funds:

1. Statutory superannuation guarantee contribution (various funds)
2. Defined Benefits Local Government Superannuation Scheme (Scheme)

For the Defined Benefits Fund, rates of increase have been based on an actuarial assessment by the Fund Managers. In recent years, the Scheme advised Council that as a result of the impact of the global financial crisis which is a significant deficiency of assets over liabilities. As at 30 June 2010, this deficit applicable to The City of Newcastle was approx $8.65 million.

Employee costs	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
	2.15%	3.25%	3.25%	3.25%	3.25%	3.25%	3.25%	3.25%	3.25%	3.25%	3.25%

A.3.2 Borrowing costs

Borrowing costs are based on an approximate 200 basis points above the investment return rate to compensate for commercial risk. Refer to borrowings Section 6.2.5 above for policy and additional borrowings summary.

Borrowing costs	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
	8.00%	8.00%	8.00%	8.00%	8.00%	8.00%	8.00%	8.00%	8.00%	8.00%	8.00%

A.3.3 Materials, contracts and other operating costs

Increases for materials, contracts and other operating costs are generally based on CPI movements, except for local government election costs which occur every four years.

Street lighting and electricity costs are forecast to rise above CPI during the years 2012 – 2014 due to an increase approved by IPART for a rise in the costs of electricity.

Included in expenditure is the NSW State Government Waste Levy as set by the Department of Environment, Climate Change and Water. The levy will increase over the life of the Long Term Financial Plan.

Materials and Contracts	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
	3.50%	33.53%	2.20%	2.70%	3.20%	3.10%	2.50%	2.20%	2.45%	2.60%	2.60%

Materials, contracts and other operating costs	2012/13	2013/14	2014/15	2015/16	2016/17	2017/18	2018/19	2019/20	2020/21
Street lighting and electricity	18.20%	2.90%	2.60%	2.54%	2.54%	2.54%	2.54%	2.54%	2.54%
NSW State Government Waste Levy	16.69%	15.10%	13.87%	15.00%	15.00%	15.00%	15.00%	15.00%	15.00%
Materials and contracts	2.40%	2.40%	2.60%	5.00%	5.00%	5.00%	5.00%	5.00%	5.00%
Other operating costs	1.54%	5.51%	0.57%	2.54%	2.54%	2.54%	2.54%	2.54%	2.54%

All maintenance costs are included in the operating costs. Maintenance is defined as the cost of upkeep and repair to an asset so it does not deteriorate prematurely.

A.3.4 Depreciation and impairment

Depreciation and impairment is based on the Asset Management Strategy and includes consideration of future asset acquisitions, disposals and potential revaluations as required by Australian Accounting Standards and the Division of Local Government's Code of Accounting Practice and Financial Reporting.

A.4 Capital Revenue

A.4.1 Capital grants and contributions

Grants and contributions-capital	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
	-17.38%	31.65%	-58.36%	3.04%	3.40%	3.10%	2.50%	2.20%	2.45%	2.60%	2.60%

Capital grants and contributions vary from year to year subject to applications for grants and the level of contributions from subdivision developers.

A.4.2 Asset sales

No asset rationalisation has been incorporated into the adopted Operational Plan.

Asset sales incorporated into the SRV funding sources have been recommended by the Asset Advisory Board. All proposed asset sales will need Council approval.

All asset sales, including where applicable, asset rationalisation, will be detailed in the Asset Management Plans with monies received used for capital asset replacement or renewal in accordance with adopted Reserves and Restricted Assets Policy.

A.5 Capital Expenditure

A.5.1. Capital expenditure on assets

Planned capital expenditures are based on corporate capital projects, major asset preservation program renewals and city projects.

Capital expenditure is defined as Asset Renewal, Asset Enhancement and asset growth or expansion. These are defined as follows:

- **Asset Renewal:** The cost of restoring an asset to its original service capacity using current standards and technology. (eg recladding the City Hall)
- **Asset Enhancement:** The cost of expanding and asset beyond its original service capacity (eg expanding the city Art Gallery)
- **Asset Growth:** The costs of expanding Councils stock of Assets (eg a new cycleway)

Appendix B:

SRV Projects

B.1 Hunter Street Revitalisation Project

Hunter Street Revitalisation includes 44 priority actions identified for delivery at an additional cost of **$16.67 million over 10 years**.

B.2 Coastal Revitalisation Project

The Coastal Revitalisation project costing **$35.79 million** includes the following works:

- Stockton improvements (Corroba oval, dune stabilisation, sports club, tourist park expansion, tree planting, cycle routes etc)
- Nobbys improvements
- Shortland Esplanade and Newcastle baths improvements
- King Edward Park improvements
- Bar Beach improvements
- Dixon Park improvements
- Merewether improvements

B.3 Swimming Pool Upgrade Program

The proposed Swimming Pool upgrade program includes the construction of a Newcastle Regional Aquatic and Leisure Centre at total cost of **$27.5 million**.

B.4 Libraries Upgrade

The libraries upgrade includes the building of new libraries with modern facilities and rationalising old properties valued at **$42.9 million**.

B.5 Cycleways Program

Cycleways works include provision for new and upgrades to existing cycleways and shared pathways at an estimated cost of **$15.66 million**.

B.6 Newcastle Art Gallery Expansion

The Newcastle Art Gallery expansion project will increase display space for exhibitions and the permanent collection. Increased space will be provided for collection storage and technical/conservation workshop facilities. New features will include a café and function space/boardroom facilities. Enhanced plant and equipment works to improve the environmental conditions for storage of art works, security and fire facilities are also planned.

The Newcastle Art Gallery expansion project also includes the development of education workshop space, space for artist in residence and storerooms. The total estimated cost of the Newcastle Art Gallery expansion is **$21 million**.

B.7 Blackbutt Reserve Upgrade

Stage 1 of the Blackbutt Reserve upgrade includes the construction of a playground and toilet block, kiosk, education centre and BBQ shade shelters at Carnley Avenue.

Stage 2 includes the construction of an administration building, carpark, playground, BBQ shade shelters, a boardwalk and new toilet block at Richley Reserve.

A lookout platform is also planned for construction at Lookout Road with construction of a toilet block at the Main Ridge. The project also includes refurbishment of exhibits as well as upgrades to shared pathways. The estimated cost of the Blackbutt Reserve update is **$9.85 million**.

B.8 Parking Strategy

The overall objective of the strategy is to ration available parking spaces in an equitable manner to:

- Provide a mix of free and paid time-restricted parking in core retail areas
- Decrease parking costs with distance from activity centres/attractions
- Reflect convenience factors for on-street parking by pricing on-street parking slightly higher than off street parking
- Improve the mix of parking options available at off-street parking stations
- Disposal of Council owned parking stations which currently due to age and condition require significant ongoing maintenance.

B.9 Major Asset Preservation Program

The major asset preservation program is broken down into three programs. Projected expenditure for each program for the 10 year financial period is shown below:

MAPS Program	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Roads	$9.456m	$9.456m	$9.456m	$9.456m	$9.456m	$9.456m	$9.456m	$9.456m	$9.456m	$9.456m	$9.456m
Buildings and structures	$9.1m	$9.1m	$9.1m	$9.1m	$9.1m	$9.1m	$9.1m	$9.1m	$9.1m	$9.1m	$9.1m
environment	$6.44m	$6.44m	$6.44m	$6.44m	$6.44m	$6.44m	$6.44m	$6.44m	$6.44m	$6.44m	$6.44m
Total	**$25M**	**$25M**	**$25M**	**$25M**	**$25M**	**$25M**	**$25M**	**$25M**	**$25M**	**$25M**	**$25M**

To fund the major asset preservation program and reduce the $139 million infrastructure backlog, Council has increased borrowings to $10 million per annum. The balance of borrowings at 30 June 2011 is estimated at $47 million.

The impact of any of these factors would need to be included in the annual Operational Plan process.

Appendix C

The following are extracts from TCorps report on TCoN financial position:

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%
- The LTFP assumes the level of services and operations as 'business as usual' apart from the additional revenue and expenditure related to the nine civic capital projects identified as part of the successful SRV
- Other operating revenues are forecast to increase by 15.3% and 32.5% in 2015 and 2016
- Materials and contracts are forecast to increase by 51.0% in 2013 and by 8.0% in each year from 2016 to 2022. Council has stated that the 2012 adopted budget figure was under budgeted and that the increase from 2013 onwards reflects the projected cost increases more accurately
- Other operating expenses are forecast to increase by 17.2% in 2013, predominantly due to the increased waste levy and then increase between 2.0% and 7.2% in the remaining year through to 2022
- Council has reclassified the waste levy into other expenses as opposed to materials and contracts where it had historically been accounted for
- Council's total cash and investments are forecast to decrease from $184.4 million in 2012 to $23 million in 2022
- To assist the funding of the nine civic capital projects relating to the SRV funding, Council are forecasting to sell under-utilised or redundant assets at a value of $45.2 million that are included within the cumulative asset sales of $68.2 million within the forecast. This includes two of the three parking stations that Council own, with the sale of these completing in the 2013 financial year.

Appendix D

The following are extracts from TCorps report on TCoN financial position:

TCorp Benchmarking and Comparisons with Other Councils

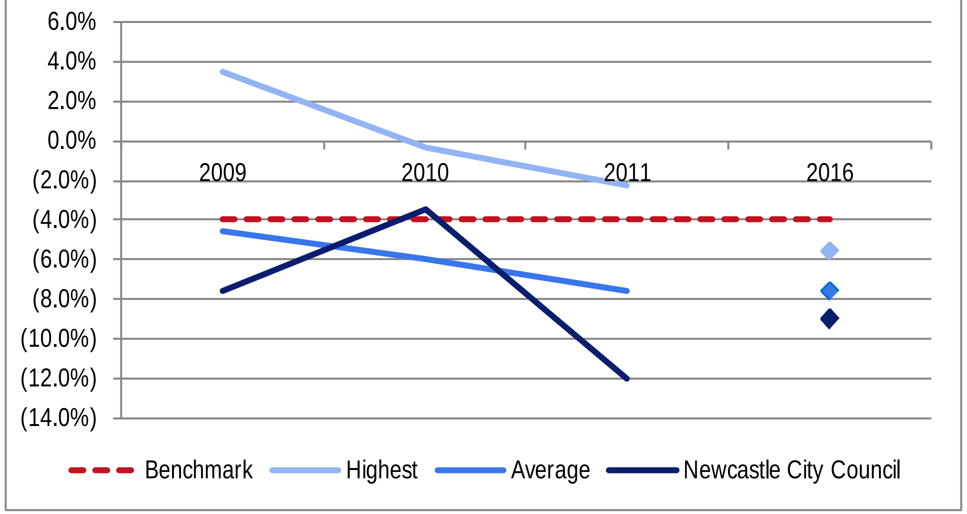
Each council's performance has been assessed against ten key benchmark ratios. This section of the report compares the Council's performance with its peers in the same DLG Group. The Council is in DLG Group Five and there are six councils in this group.

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

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

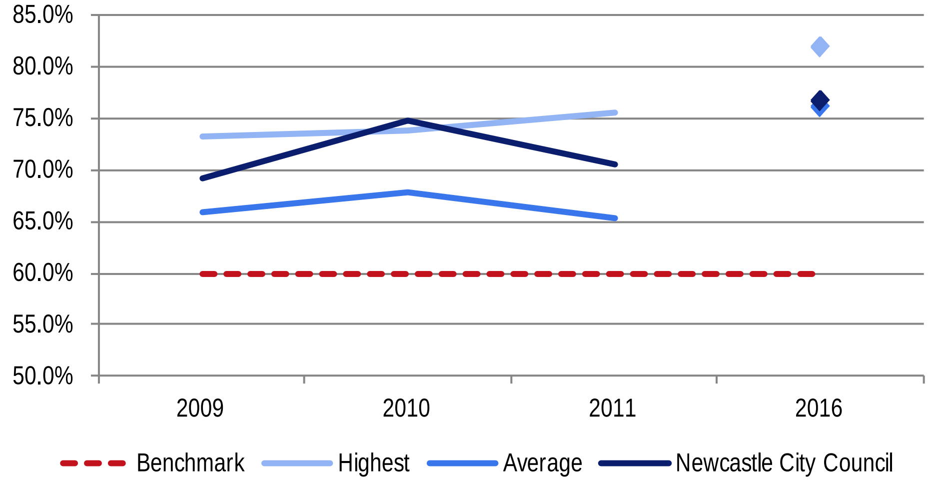
Financial Flexibility

Figure 15 - Operating Ratio Comparison



Council's Operating Ratio was below the benchmark and group average in two of the past three years. Consistent with other councils in the group, it experienced a decline in operating results in 2011 due to increased depreciation expense. The results are forecast to improve in the medium term but remain below the benchmark (and deteriorate significantly post 2016).

Figure 16 - Own Source Operating Revenue Ratio Comparison



Council's Own Source Operating Revenue Ratio was above the group average and the benchmark. The ratio is forecast to improve further in the medium term in line with the group average.

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

Liquidity

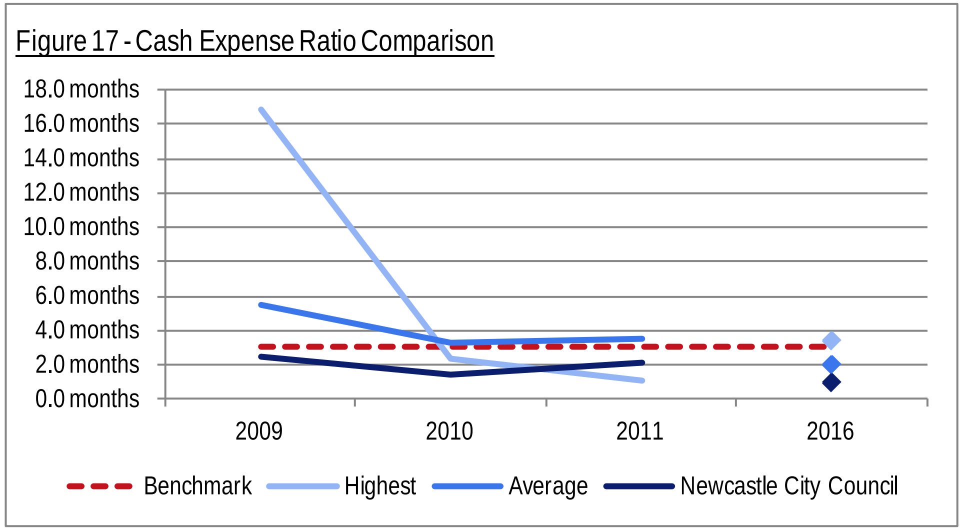


Figure 17 - Cash Expense Ratio Comparison
18.0 months
16.0 months
14.0 months
12.0 months
10.0 months
8.0 months
6.0 months
4.0 months
2.0 months
0.0 months
2009
2010
2011
2016
Benchmark
Highest
Average
Newcastle City Council

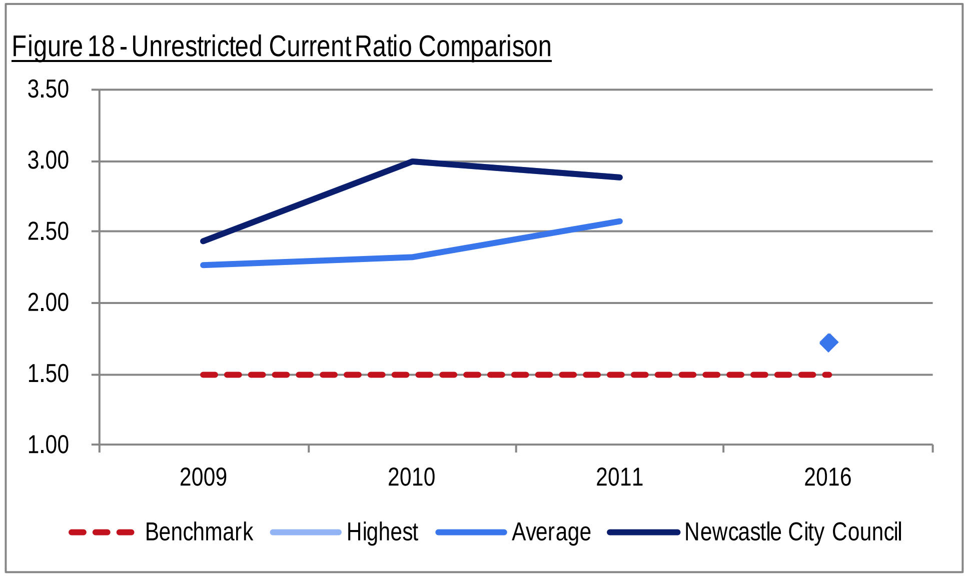
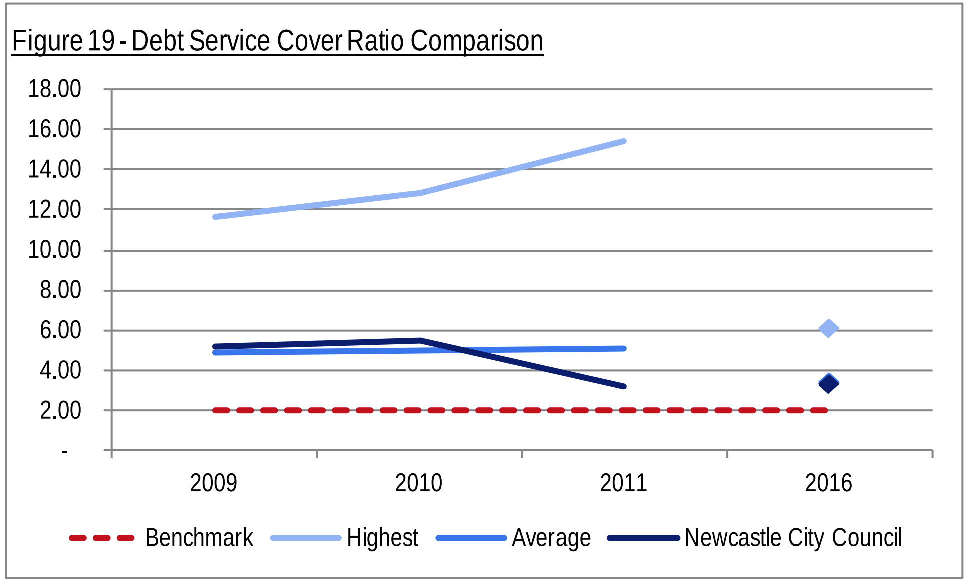
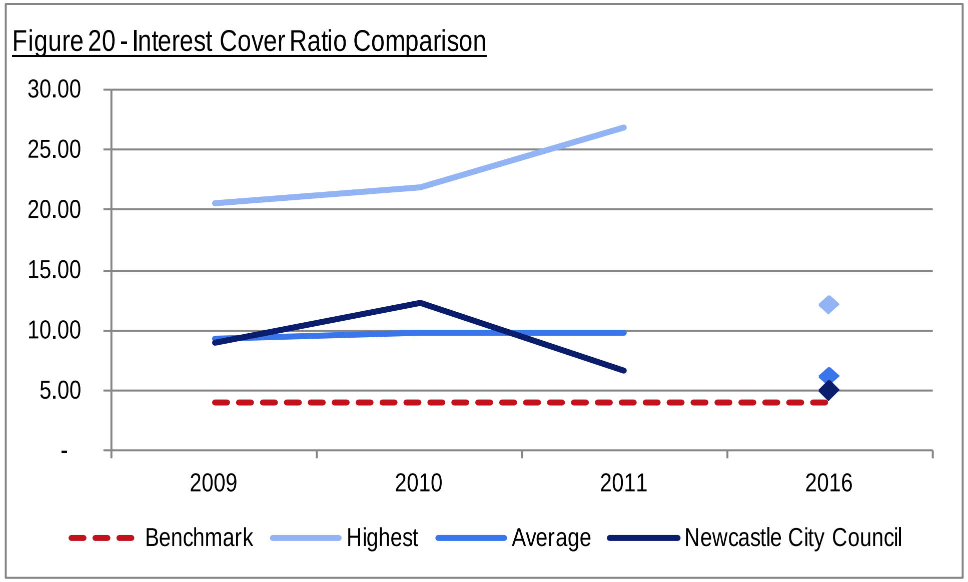


Figure 18 - Unrestricted Current Ratio Comparison
3.50
3.00
2.50
2.00
1.50
1.00
2009
2010
2011
2016
Benchmark
Highest
Average
Newcastle City Council

On average over the past three years, the Council's liquidity position has been sound. Council has the highest Unrestricted Current Ratio in the group though they have not provided a forecast Unrestricted Current Ratio.

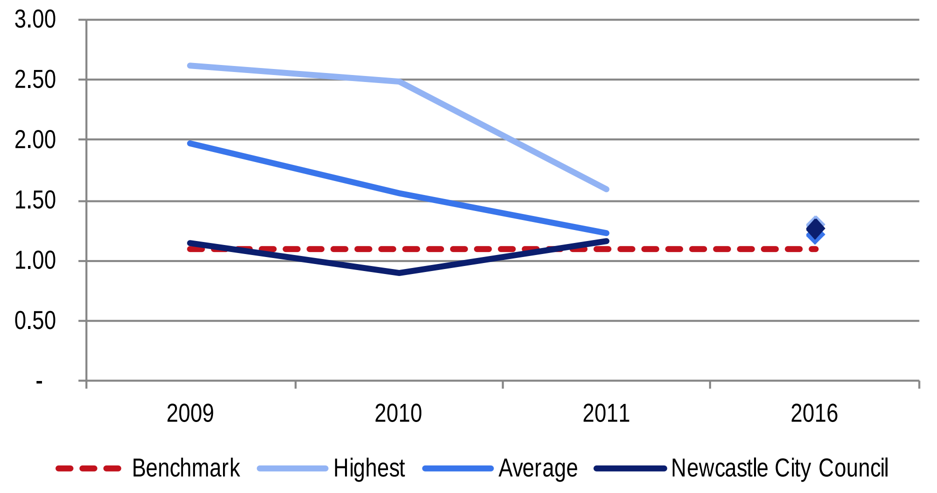
Debt Servicing





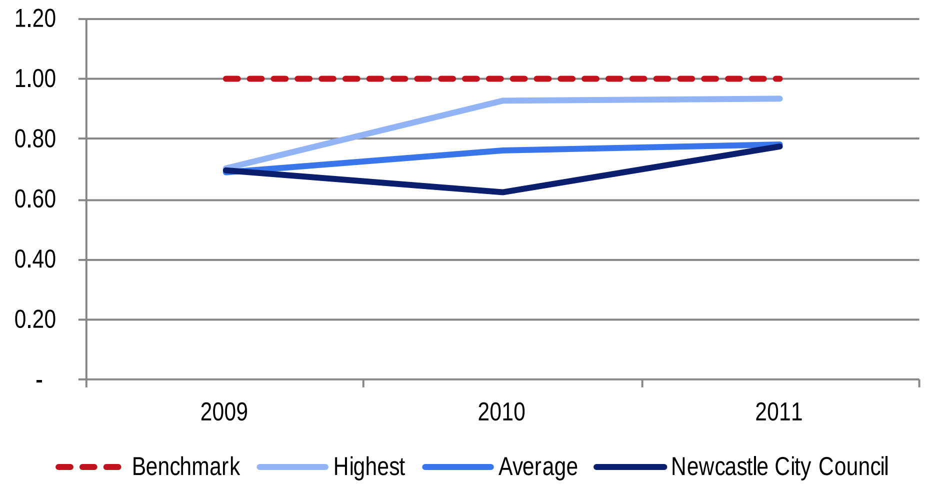
Over the review period, Council was above benchmark in respect of its Debt Service Cover Ratio (DSCR) and Interest Cover Ratio's but these ratios are forecast to marginally deteriorate in the medium term to be close to the benchmark.

Figure 21 - Capital Expenditure Ratio Comparison



Asset Renewal and Capital Works

Figure 22 - Asset Maintenance Ratio Comparison



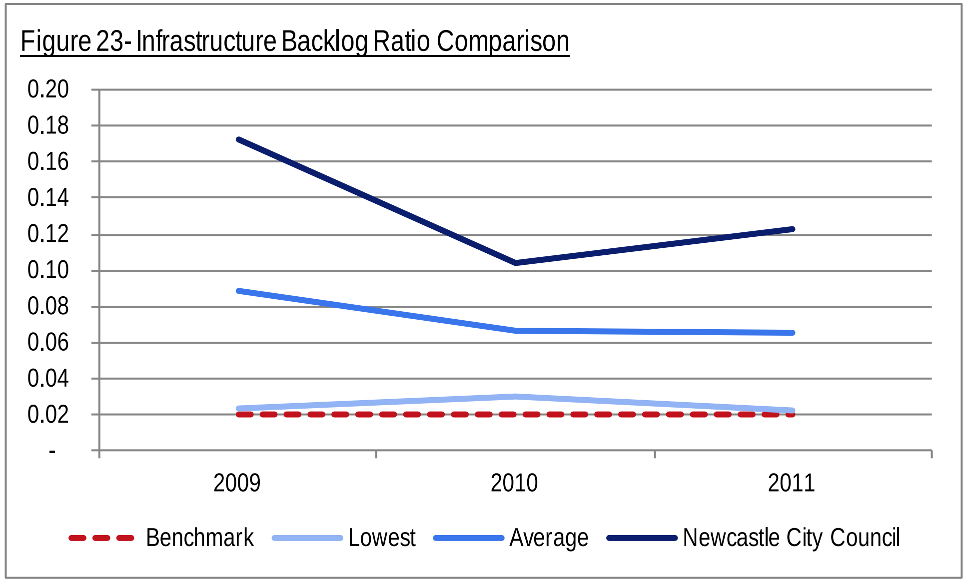


Figure 23- Infrastructure Backlog Ratio Comparison
0.20
0.18
0.16
0.14
0.12
0.10
0.08
0.06
0.04
0.02
-
2009
2010
2011
Benchmark
Lowest
Average
Newcastle City Council

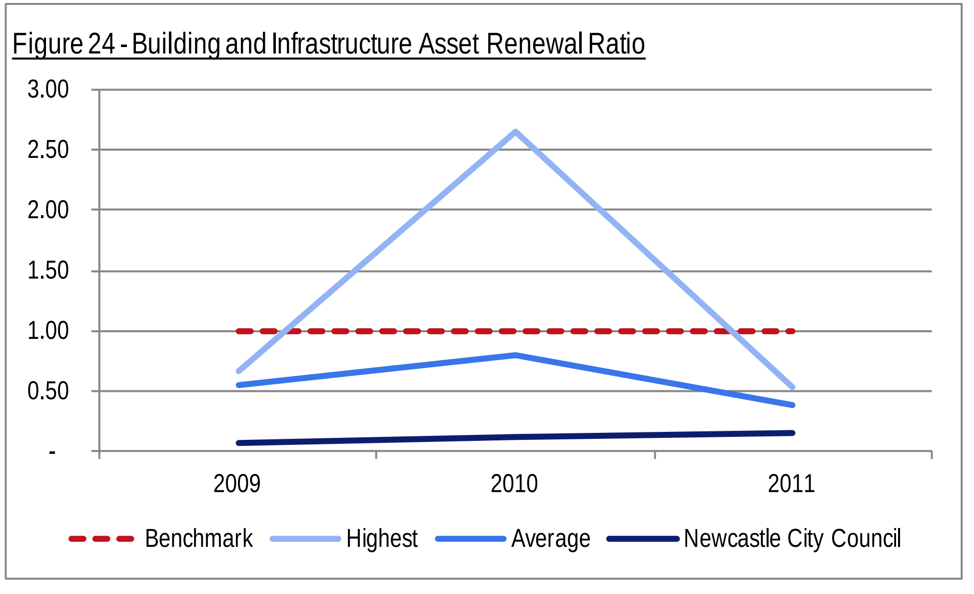


Figure 24 - Building and Infrastructure Asset Renewal Ratio
3.00
2.50
2.00
1.50
1.00
0.50
-
2009
2010
2011
Benchmark
Highest
Average
Newcastle City Council

Overall, the Council has a much higher Infrastructure Backlog than other councils in the group. It is also below the group average and benchmark in terms of spending on asset maintenance. The Council's Building and Infrastructure Asset Renewal Ratio is well below the group average and benchmark. The Council's Capital Expenditure Ratio has been below the group average, though it has been around the benchmark and is forecast to remain around the benchmark in the medium term.

Overall the Council has a high Infrastructure Backlog and has spent less on building and infrastructure asset renewal and asset maintenance than required. This is likely to increase the Infrastructure Backlog further in the future if this issue is not addressed.

TCorp's Conclusions

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

- Council's DSCR and Interest Cover Ratio has remained above the benchmark in recent years indicating the capacity to manage the additional borrowings.
- Council's liquidity position has been sound, as indicated by a strong Unrestricted Current Ratio.
- Council's financial flexibility is adequate as highlighted by the Own Source Operating Revenue Ratio.
- While Council's Infrastructure Backlog is relatively large it is predominantly buildings related and they have successfully managed to keep the roads and drainage backlog to a manageable level. Having the backlog within buildings is seen as less of a negative as these assets are saleable should Council need to undertake an asset rationalisation exercise.

Council management are aware of the current position and the challenges that the Council faces in the medium to long term. This recommendation is made with the following points to be reviewed by the newly elected Council in conjunction with the Management Team:

- The current LTFP and capital expenditure program is likely to lead to Council becoming illiquid by 2019.
- A review of the LTFP assumptions should be undertaken to identify a sustainable way forward, whether that be by identifying new revenue sources, revising service levels, or rescheduling capital expenditure and associated borrowings to ensure that all liabilities are able to be met as required.
- The additional borrowings currently scheduled within the LTFP of $92.2 million from 2014 to 2022, contribute to Council's potential future liquidity issues. If the liquidity issues scheduled in 2019 were addressed but the scheduled additional borrowings were still utilised then Council will not be in a position to meet the increasing repayments by 2022.

Historical Financial Information Tables constructed by TCorp:

Income Statement

Income Statement ($'000s)	**Year ended 30 June**			**% annual change**	
	2011	**2010**	**2009**	**2011**	**2010**
Revenue					
Rates and annual charges	103,988	99,745	95,680	4.3%	4.2%
User charges and fees	54,700	51,794	51,406	5.6%	0.8%
Interest and investment revenue	12,040	9,510	9,597	26.6%	(0.9%)
Grants and contributions for operating purposes	26,153	21,011	19,992	24.5%	5.1%
Other revenues	6,576	6,841	6,657	(3.9%)	2.8%
Total revenue	**203,457**	**188,901**	**183,332**	**7.7%**	**3.0%**
Employees	87,930	80,463	81,991	9.3%	(1.9%)
Borrowing costs	3,148	2,408	2,415	30.7%	(0.3%)
Materials and contract expenses	63,311	50,268	52,015	25.9%	(3.4%)
Depreciation and amortisation	42,417	33,720	33,579	25.8%	0.4%
Other expenses	31,117	28,511	29,760	9.1%	(4.2%)
Total expenses	**227,923**	**195,370**	**199,760**	**16.7%**	**(2.2%)**
Operating result	**(24,466)**	**(6,469)**	**(16,428)**	**278.2%**	**(60.6%)**

Items excluded from Income Statement

Excluded items ($'000s)			
	2011	**2010**	**2009**
Grants and contributions for capital purposes	21,266	13,962	26,913
Revaluation reserves realised	1,478	0	0
Net gain/(loss) from disposal of assets	1,462	6,158	(17)
Investment recoupment (Other revenues)	0	0	2,345
Fair value adjustments - investment property	0	615	0
Fair value adjustments - investments	0	0	(10,131)

Balance Sheet

Balance Sheet ($'000s)	Year Ended 30 June			% annual change	
	2011	2010	2009	2011	2010
Current assets					
Cash and equivalents	31,769	18,957	33,498	67.6%	(43.4%)
Investments	65,941	76,868	43,899	(14.2%)	75.1%
Receivables	15,775	16,081	15,560	(1.9%)	3.3%
Inventories	745	732	692	1.8%	5.8%
Other	395	620	450	(36.3%)	37.8%
Non-current assets classified as held for sale	4,445	830	891	435.5%	(6.8%)
Total current assets	119,070	114,088	94,990	4.4%	20.1%
Non-current assets					
Investments	88,801	84,476	78,184	5.1%	8.0%
Receivables	7,968	8,100	7,735	(1.6%)	4.7%
Infrastructure, property, plant & equipment	1,291,982	1,622,204	1,472,854	(20.4%)	10.1%
Investment property	12,815	12,815	12,200	0.0%	5.0%
Intangible Assets	451	0	0	N/A	N/A
Other	22	24	28	(8.3%)	(14.3%)
Total non-current assets	1,402,039	1,727,619	1,571,001	(18.8%)	10.0%
Total assets	**1,521,109**	**1,841,707**	**1,665,991**	**(17.4%)**	**10.5%**
Current liabilities					
Payables	24,216	18,709	15,565	29.4%	20.2%
Borrowings	2,687	3,162	2,709	(15.0%)	16.7%
Provisions	33,782	33,720	37,849	0.2%	(10.9%)
Total current liabilities	60,685	55,591	56,123	9.2%	(0.9%)
Non-current liabilities					
Borrowings	50,664	43,384	36,000	16.8%	20.5%
Provisions	8,769	8,143	8,416	7.7%	(3.2%)
Total non-current liabilities	59,433	51,527	44,416	15.3%	16.0%
Total liabilities	**120,118**	**107,118**	**100,539**	**12.1%**	**6.5%**
Net assets	**1,400,991**	**1,734,589**	**1,565,452**	**(19.2%)**	**10.8%**

Cashflow

Cashflow Statement ($'000s)	Year ended 30 June		
	2011	**2010**	**2009**
Cash flows from operating activities	37,957	34,544	44,939
Cash flows from investing activities	(31,950)	(56,922)	(38,892)
Proceeds from borrowings and advances	10,284	10,873	7,068
Repayment of borrowings and advances	(3,479)	(3,036)	(1,765)
Cash flows from financing activities	6,805	7,837	5,303
Net increase/(decrease) in cash and equivalents	**12,812**	**(14,541)**	**11,350**
Cash and equivalents	31,769	18,957	33,498

Glossary of Terms

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 engageing 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.

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.

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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

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 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.

Integrated Planning and Reporting (IP&R) Framework

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

Local Government Cost Index (LGCI)

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

Net Assets

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

Roads and Maritime Services (RMS)

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

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

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

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

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

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

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

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

The applications are reviewed and approved by IPART.

Ratio Explanations

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

Building and Infrastructure Renewals Ratio
Benchmark = Greater than 1.0x
Ratio = Asset renewals / depreciation of building and infrastructure assets
This ratio compares the proportion spent on infrastructure asset renewals and the asset's deterioration measured by its accounting depreciation. Asset renewal represents the replacement or refurbishment of existing assets to an equivalent capacity or performance as opposed to the acquisition of new assets or the refurbishment of old assets that increase capacity or performance.

Cash Expense Cover Ratio
Benchmark = Greater than 3.0 months
Ratio = current year's cash and cash equivalents / (total expenses – depreciation – interest costs) *12
This liquidity ratio indicates the number of months a council can continue paying for its immediate expenses without additional cash inflow.

Capital Expenditure Ratio
Benchmark = Greater than 1.1x
Ratio = annual capital expenditure / annual depreciation
This indicates the extent to which a council is forecasting to expand its asset base with capital expenditure spent on both new assets, and replacement and renewal of existing assets.

Debt Service Cover Ratio (DSCR)
Benchmark = Greater than 2.0x
Ratio = operating results before interest and depreciation (EBITDA) / principal repayments (from the statement of cash flows) + borrowing interest costs (from the income statement)
This ratio measures the availability of cash to service debt including interest, principal and lease payments

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, building, other structures and depreciable land improvement assets (from note 9a)
This ratio shows what proportion the backlog is against total value of a council's infrastructure.

Interest Cover Ratio
Benchmark = Greater than 4.0x
Ratio = EBITDA / interest expense (from the income statement)
This ratio indicates the extent to which a council can service its interest bearing debt and take on additional borrowings. It measures the burden of the current interest expense upon a council's operating cash.

Operating Ratio
Benchmark = Better than negative 4%
Ratio = (operating revenue excluding capital grants and contributions – operating expenses) / operating revenue excluding capital grants and contributions
This ratio measures a council's ability to contain operating expenditure within operating revenue.

Own Source Operating Revenue Ratio
Benchmark = Greater than 60%
Ratio = rates, utilities and charges / total operating revenue (inclusive of capital grants and contributions)
This ratio measures the level of a council's fiscal flexibility. It is the degree of reliance on external funding sources such as operating grants and contributions. A council's financial flexibility improves the higher the level of its own source revenue.

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

Ratio = Current assets less all external restrictions / current liabilities less specific purpose liabilities
Restrictions placed on various funding sources (eg 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.