Holroyd City Council

Financial Assessment and Sustainability Report

Date:	16 January 2015

Disclaimer

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1 Executive Summary

In April 2013 TCorp provided Holroyd City Council (the Council) with a Financial Assessment, Sustainability and Benchmarking Report.

In the report TCorp made the following observations:

- Over the review period, revenue increased year on year between 4.8% and 9.7% p.a.
- Expenses increased by 15.3% in 2011 driven by an 81.6% increase in depreciation and 18.2% in 2012 with a further increase in depreciation alongside increased employee and materials & contract expenses.
- Council had sufficient liquidity over the review period.
- Council reported $49.4m in Infrastructure Backlog in 2012.
- Council reported operating deficits when capital grants and contributions are excluded that increased from $1.0m in 2010 to $14.8m in 2012.
- The 2012 Long Term Financial Plan (LTFP) forecast operating deficits each year with the operating result projected to improve from 2015 when a 6 year SRV was proposed at 6% above the annual rate peg.
- Council had forecast sufficient liquidity and financial flexibility.
- Council had not included sufficient capital expenditure to maintain infrastructure at its current service levels for the long term.

TCorp's report stated that "*Based on our review of both the historic financial information and the 10 year financial forecast within Council's LTFP we consider Council's financial position is weak in the short term and is likely to deteriorate*". This resulted in TCorp assigning Council with a Financial Sustainability Rating (FSR) of Weak and Outlook of Neutral.

Following receipt of the report Council has successfully applied for a five year SRV and also completed a major review of their infrastructure assets and linked depreciation methodology. This has enabled Council to update the integration of their LTFP & AMPs. The review completed by Council focused on re-assessing the useful lives of assets and has resulted in significant adjustments to depreciation expense. Council's auditors have signed off on amendments to the depreciation expenses for the 2013 and 2014 financial years. Council has provided TCorp with adjusted numbers for the 2012 and 2011 financial years which have been used in preparing this report. Using these numbers provides a more comparable analysis of Council's financial results to be undertaken, but it is noted that the numbers used in 2012 and 2011 have not been audited.

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

- Council's operating performance is forecast to improve to a break-even result by 2018 when capital grants and contributions are excluded.
- Operating results with marginal variations from break-even are forecast in the subsequent six years.
- Council's own source operating revenue is forecast to remain at a strong level, assisted by the increased rates revenue from the SRV.

- Council's liquidity is forecast to remain adequate with their Unrestricted Current Ratio remaining above the benchmark in each year.
- Council has forecast significant levels of capital expenditure for new and renewal assets over the next 20 years to maintain service levels and provide buildings and infrastructure for the increasing population.

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

- The approved SRV is expected to contribute in assisting Council to achieve an ongoing break-even operating result.
- The SRV should also assist in Council having sufficient funds to maintain their current infrastructure assets each year as well as assist with capital expenditure on new assets.
- The review of Council's infrastructure assets and the subsequent decrease in Council's annual depreciation expense is a major factor assisting the forecast break-even operating position.
- Council's capital expenditure on new and renewal assets appears high with an average Capital Expenditure Ratio of 1.70x and Buildings and Infrastructure Asset Renewals Ratio of 1.40x across the 10 year forecast. Council has however confirmed that following approval of the five year SRV, a 20 year capital works plan including Section 94 plan infrastructure works was created totalling $300m to enable the LGA to manage the ongoing population increases expected within the area.
- In line with the 20 year capital works plan, significant increases in capital grants and contributions are forecast relating to the Section 94 developer contributions.

Based on our review of both the historic financial information and the 10 year financial forecast within Council's LTFP we consider Council to be in an improved position when compared to the analysis within our April 2013 report. Council's current Financial Sustainability Rating (FSR) is Moderate when analysing the five year historic financials between 2010 and 2014 with an Outlook of Positive.

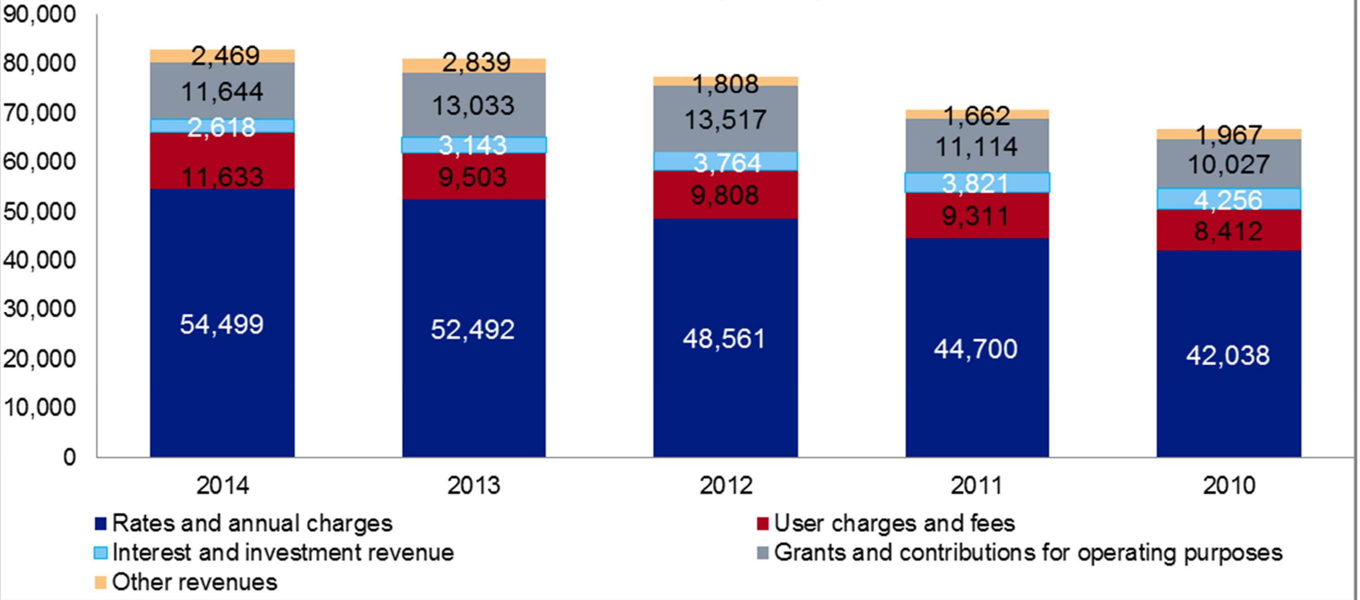
A Positive Outlook indicates that a Council's FSR is likely to improve in the short term (i.e. within the next three years). Should this improvement occur in Holroyd City Council's FSR as projected in the LTFP, then the FSR would improve to Sound.

2 Review of Financial Performance and Position

TCorp has updated its review based on the 2014 annual audited accounts of the Council

2.1 Revenue

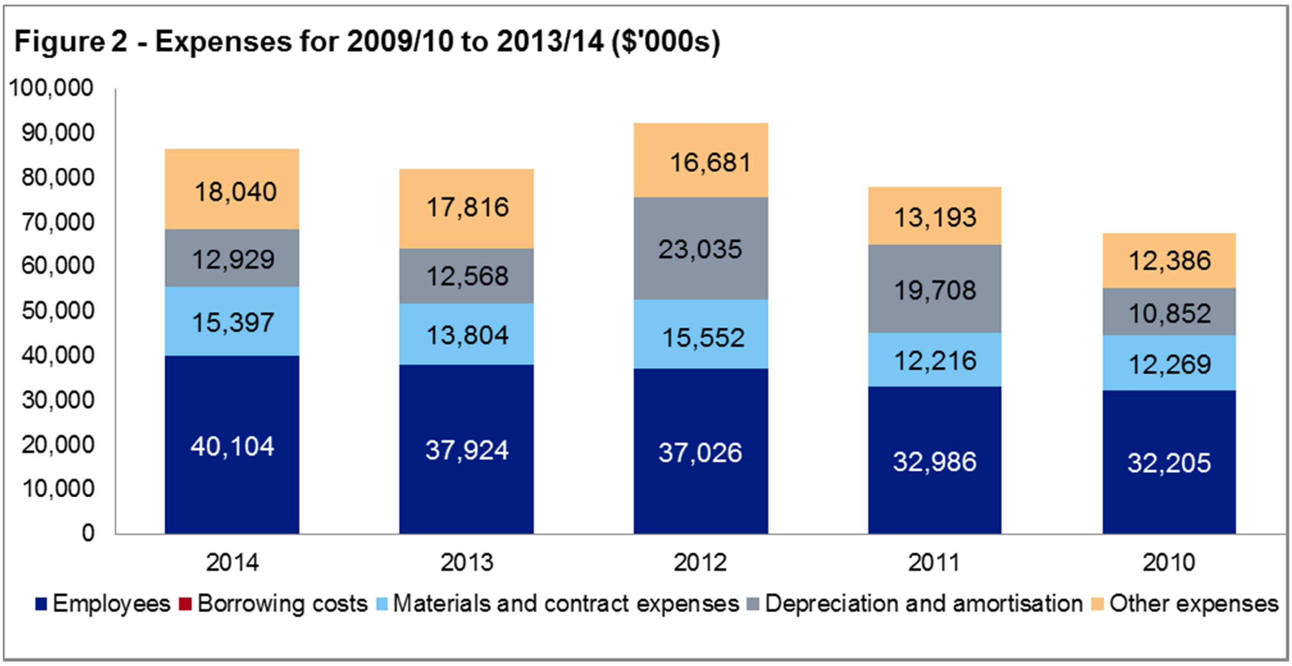
Figure 1 - Revenue Sources for 2009/10 to 2013/14 ($'000s)



Key Observations

- Council's total revenue has continued to increase year-on-year in 2013 and 2014 although at a reduced rate of 4.6% and 2.3% p.a. respectively. Over the five year review period it increased by $16.2m (24.2%) to $82.9m.
- Rates and annual charges have increased 3.8% in 2014, the lowest annual increase over the 5 year period. Council has had a five year SRV approved that equates to a 44.2% increase, beginning in 2014/15.
- User charges and fees increased by 22.4% in 2014 due to an increase in child care / family day care fees of $1.4m to $4.9m that were boosted by the new Pemulwuy childcare centre and an increase of $0.7m to $1.6m for town planning fees linked to increased housing demand.
- Interest and investment income has declined year on year with a 16.7% decrease in 2014. This decrease is aligned with the reduction in the RBA cash rate reducing to 2.50%. Council has detailed their average investment return was 4.7% in 2014 compared to 5.5% in 2013.
- The 2014 operating grants and contributions reduced from 2013 because of the timing of the Financial Assistance Grant (FAG) payments that resulted in only 6 months FAG being received in 2014.
- Other revenue has been varied over the 5 year period and is predominantly made up of parking fines which amounted to $1.5m in 2014.

2.2 Expenses



Key Observations

- Total expenses increased by $18.7m (27.7%) over the review period with a 0.3% increase in 2013 followed by a 5.3% increase in 2014.
- Employee expenses have increased by $3.1m between 2012 and 2014 with a 5.7% increase in 2014. This has been driven by an additional 15 FTE employees due in part to Council opening a childcare centre in Pemulwuy. In 2014 the number of FTE employees noted has increased to 520 with casual staff included for the first time and 2013 FTE numbers being restated to 505.
- Council has remained debt free since 2010 therefore does not have any borrowing costs.
- Materials and contract expenses have fluctuated somewhat with an 11.2% decrease in 2013 followed by an 11.5% increase in 2014. The decrease in 2013 was mainly due to a reduction in legal costs of $0.7m that were abnormally high in 2012 due to building contract issues relating to the Pemulwuy child care centre. Council has stated the 2014 increase has occurred as a result of increased spending on raw materials and consumables of $1.3m and contractor and consultancy costs of $0.5m. These increases related to a rise in development applications, project evaluations including the Local Environment Plan along with security and cleaning services relating to the new childcare centre in Pemulwuy. Operating Council's sporting facilities including the three swimming pools in the LGA along with parks and entertainment facilities were also contributors.
- Following the review of Council's depreciation expenses, the 2011 and 2012 figures have been amended to reflect the adjusted depreciation amounts for the infrastructure assets. The original depreciation totals for 2011 and 2012 were $19.7m and $23.0m respectively which has resulted in savings of $7.1m and $10.4m. The review that Council has completed in 2013 was based on a reassessment of the useful lives and residual values of assets and resulted in an adjustment of $152.5m to correct prior period overstatement of depreciation. This was offset by a $23.0m loss on the revaluation of infrastructure assets. Council's depreciation expense has therefore been

relatively consistent over the last four years. In 2014 the total depreciation expense of $12.9m equates to 1.8% of Council's infrastructure assets.

- Other expenses have continued to increase year-on-year with waste disposal tipping fees driving the increase. This expense equates to $9.0m (50%) of other expenses and increased by $0.7m (7.8%) in 2014.

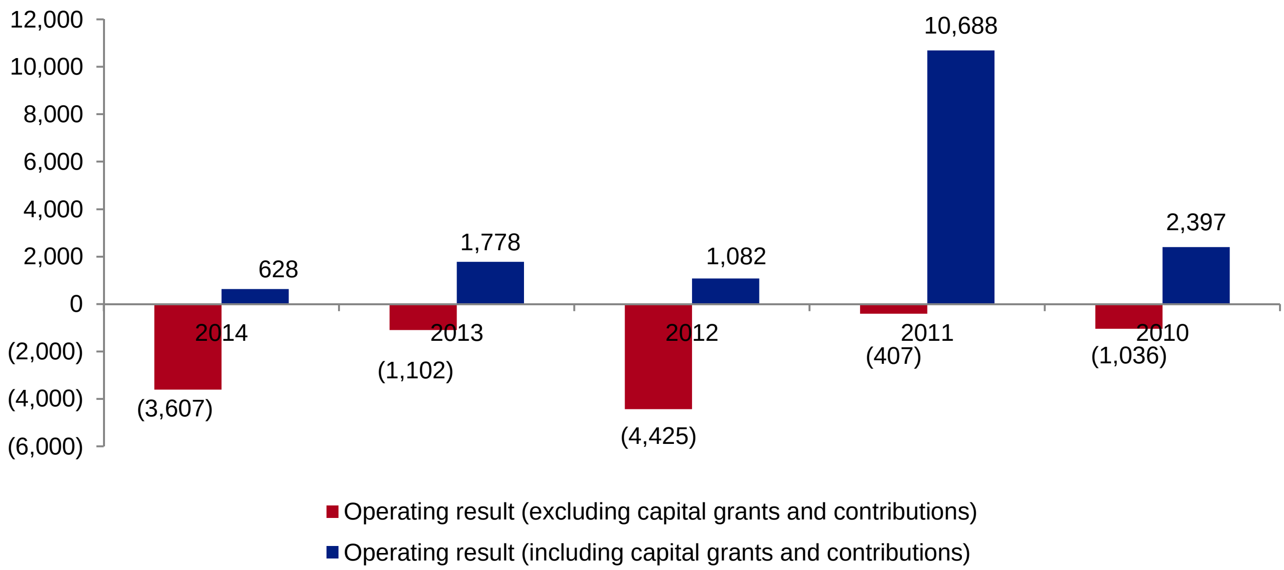
2.3 Operating Results

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

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

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

Figure 3 - Operating Results for 2009/10 to 2013/14 ($'000s)



Key Observations

- Operating deficits have been posted in each year when capital grants and contributions are excluded however the 2011 and 2012 results have been considerably improved following the revision of the depreciation expenses.
- The 2013 deficit decreased to $1.1m because of total operating expenses only increasing by 0.3% during the year against an increase in total revenues of 4.6%. This marginal increase in expenses was due in part to the $1.8m decrease in materials and contracts expense.
- The 2014 deficit increased to $3.6m due to total operating expenses increasing by 5.3% against a 2.3% increase in total revenues with the increase in employee expenses alone being larger than the total revenue increase in this year.

2.4 Financial Management Indicators

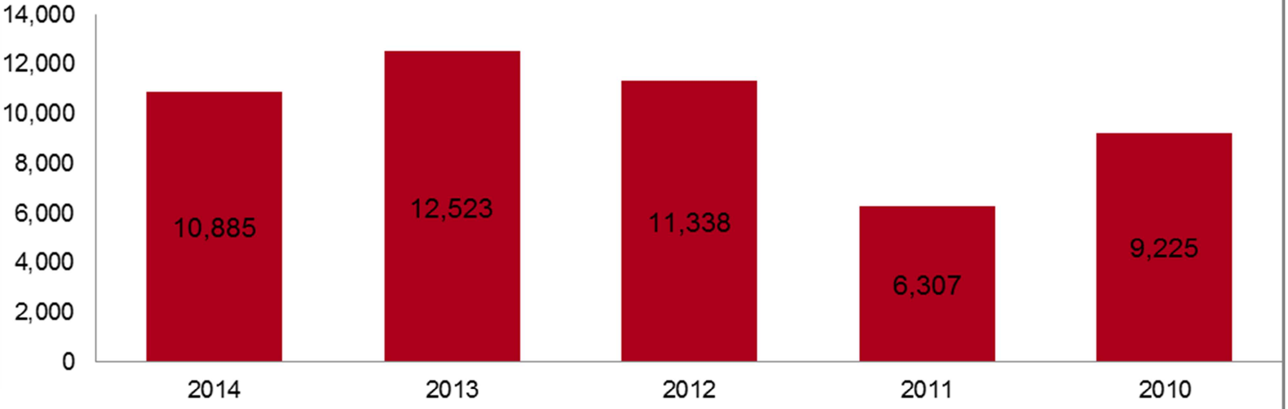
Performance Indicators	Year ended 30 June				
	2014	2013	2012	2011	2010
EBITDA ($'000s)	9,322	11,466	8,199	12,213	9,840
Operating Ratio	(4.4%)	(1.4%)	(5.7%)	(0.6%)	(1.6%)
Interest Cover Ratio	N/A	N/A	N/A	N/A	410.00x
Debt Service Cover Ratio	N/A	N/A	N/A	N/A	12.93x
Unrestricted Current Ratio	2.58x	3.00x	3.43x	6.84x	6.55x
Own Sourced Revenue Ratio	75.9%	73.9%	70.4%	66.1%	71.9%
Cash Expense Ratio	1.8 months	2.2 months	2.0 months	1.3 months	1.9 months
Net assets ($'000s)	987,603	985,175	853,326	861,859	970,439

Key Observations

- EBITDA, representing Council's underlying operating performance, has fluctuated each year in line with the variation in the operating losses posted.
- Council is yet to achieve an operating surplus or break-even position therefore their Operating Ratio is negative in each year. The deterioration in the 2014 operating result has moved the Operating Ratio outside the negative 4% benchmark and Council need to aim for a minimum break-even operating result.
- The Unrestricted Current Ratio has been on a downward trend however remains comfortably above the 1.5x benchmark.
- Council's Own Sourced Revenue Ratio has improved each year since 2011, above the benchmark. Council is therefore not reliant on external sources of funds. This ratio is likely to improve further following the approval of the five year SRV from 2014/15.
- The Cash Expense Ratio has remained below the 3.0 month benchmark in each year. This is because Council utilises term deposits and other investments to maximise their return on investment. These products are classified as investments as opposed to cash and cash equivalents and are why this ratio is below the benchmark.
- Council's Net Assets have fluctuated over the review period but have increased by 1.8% in total. The decrease in 2011 was due to an accounting adjustment relating to community land reducing the value of that land by $182.4m. This was offset by a $45.6m increase in other structures following their revaluation. The $131.8m increase in 2013 was mainly due to further revaluations and adjustments relating to Council's building and infrastructure assets that also amended the depreciation for 2011 and 2012 as previously detailed.

2.5 Statement of Cashflows

Figure 4 - Cash and Cash Equivalents for 2009/10 to 2013/14 ($'000s)



Key Observations

- Council's cash and cash equivalents have remained at a relatively stable level over the majority of the five year period. The majority of Council's funds remained in term deposits.
- Overall cash, cash equivalents, and investments have increased from $50.8m in 2010 to $56.2m in 2014. Of the $56.2m, $25.5m is externally restricted, $17.7m is internally restricted and $13.0m is unrestricted.
- Within the investments portfolio of $45.4m valued at 30 June 2014, $12.0m is in current term deposits, $17.4m is in Negotiable Certificates of Deposit (NCDs) and FRNs and $16.0m is in non-current term deposits.

2.6 Capital Expenditure

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

2.6.1 Infrastructure Backlog

Figure 5 - Infrastructure Backlog for 2009/10 to 2013/14($'000s)

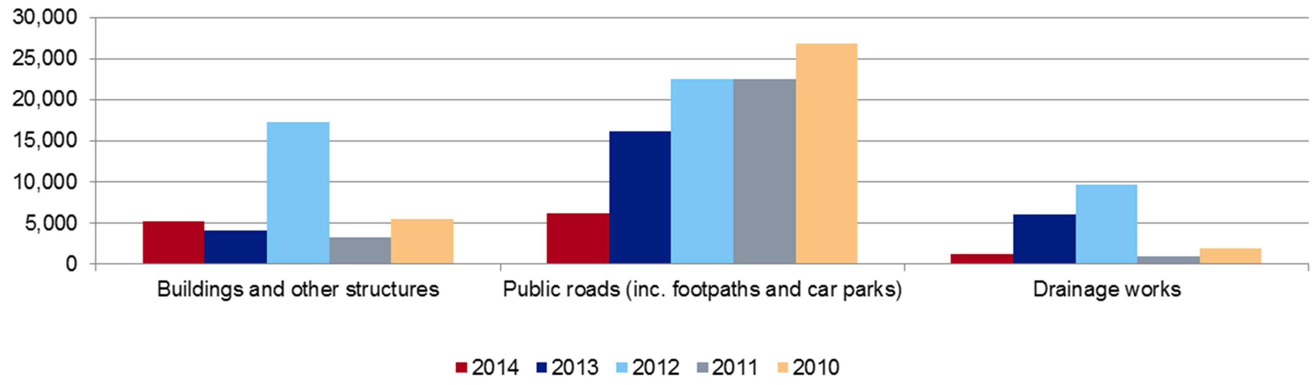
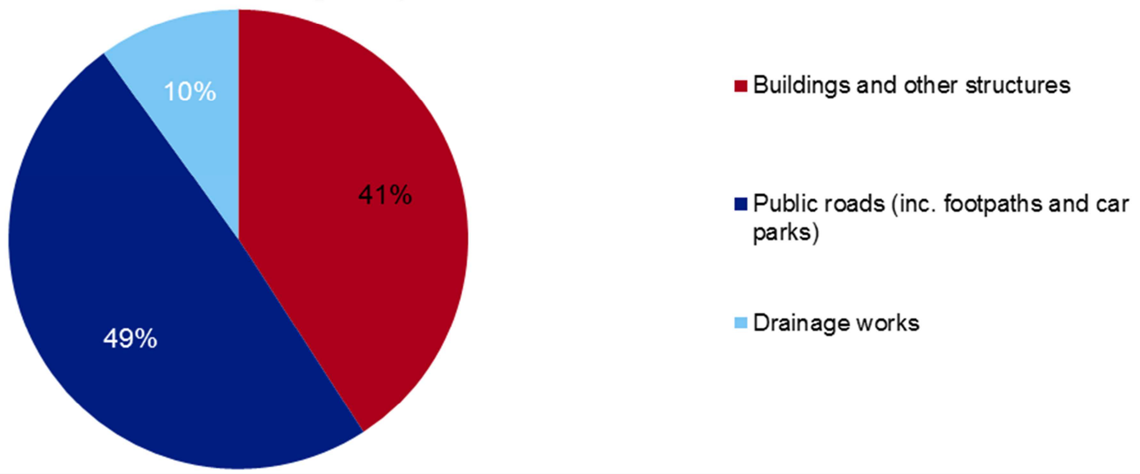


Figure 6 - Infrastructure Backlog Composition for 2013/14



Council's Infrastructure Backlog has decreased significantly from $49.4m in 2012 to $12.7m in 2014. The decrease in public road backlog from $22.5m to $6.2m has been the main reason for the decrease and this is in line with the information received from Council regarding the reassessment of their road assets since TCorp completed the original 2013 assessment.

The backlog originally increased to $49.4m in 2012 from a review of Council's AMP and related to increases in buildings, other structures and drainage works.

2.6.2 Infrastructure Status

Infrastructure status	Year ended 30 June				
	2014	2013	2012	2011	2010
Bring to satisfactory standard ($'000s)	12,679	26,319	49,445	26,627	34,178
Required annual maintenance ($'000s)	5,282	5,317	4,872	5,669	8,008
Actual annual maintenance ($'000s)	4,018	4,274	2,389	3,591	5,835
Total value infrastructure assets ($'000s)	706,738	692,067	585,195	595,424	546,364
Total assets ($'000s)	1,016,166	1,014,513	881,553	890,288	996,246
Infrastructure Backlog Ratio	0.02x	0.04x	0.08x	0.04x	0.06x
Asset Maintenance Ratio	0.76x	0.80x	0.49x	0.63x	0.73x
Building and infrastructure asset renewal ratio	0.61x	0.64x	0.83x	1.26x	0.90x
Capital Expenditure Ratio	0.85x	1.37x	1.49x	1.30x	1.25x

The Building and Infrastructure Backlog Ratio has reduced from the high in 2012 due to the revaluation of road assets detailed in section 2.6.1 along with a decrease in the drainage works backlog from $9.7m in 2012 to $1.3m in 2014.

The Asset Maintenance Ratio and Building and Infrastructure Asset Renewals Ratio (BIARR) have remained below their 1.00x benchmark in each year with the BIARR continuing its downward trend since 2011. The required annual maintenance total has fluctuated over the years as Council has refined its AMPs. The weaker ratios indicate that Council has not invested enough to be able to maintain the operating standard of their assets or renew them to a satisfactory standard.

Council's Capital Expenditure Ratio has been above the benchmark in each year with the exception of 2014. The 2011 and 2012 ratio were above benchmark when the adjusted depreciation is taken into consideration. The five year average is 1.25x.

2.6.3 Capital Program

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

Capital Program ($'000s)	Year ended 30 June				
	2014	2013	2012	2011	2010
New capital works	1,843	5,621	4,397	135	306
Replacement/refurbishment of existing assets	9,853	12,094	11,067	17,240	13,735
Total	11,696	17,715	15,464	17,375	14,041

Council's major capital works in 2013 and 2014 include:

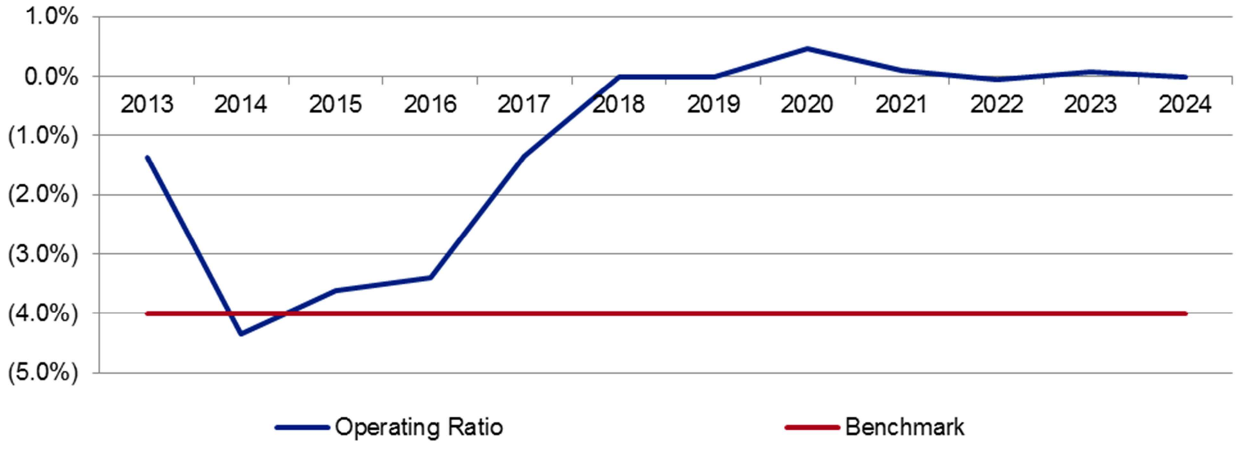
- $7m spent on Pemulwuy Children's Centre that opened in 2013.
- $6m spend on Council owned vehicles including garbage disposal trucks, park maintenance machinery and other Council owned automobiles and other plant and equipment.
- $9m on various road renewals, footpath renewals and bridge renewal works.
- $0.9m on drainage renewals.
- $2.2m on facilities renewals including buildings, parks and recreational assets.

3 Review of Financial Forecasts

The revised financial forecast model shows the projected financial statements and assumptions for the next 10 years. As the Council operates only one fund we have focused our review on this General Fund.

3.1 Operating Results

Figure 7- Operating Ratio for General Fund



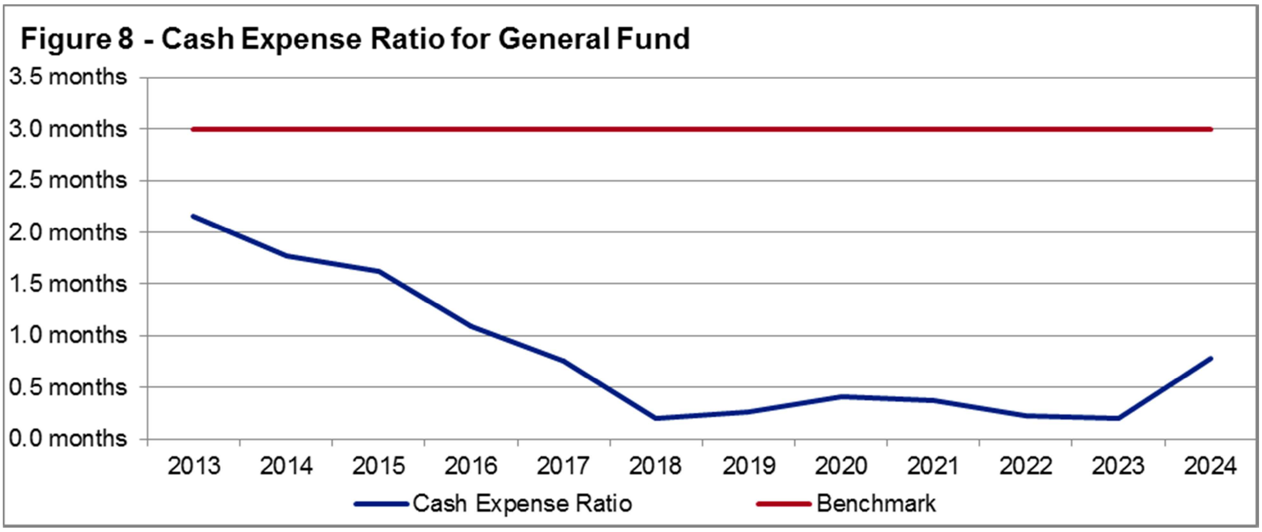
Council's Operating Ratio is forecast to improve above benchmark in 2015 and improve to a breakeven position by 2018 where it remains for five of the remaining six years, with the $0.6m 2020 surplus the exception to the breakeven results.

The improvement in the ratio coincides with the beginning of the five year SRV that began in 2015. It is also assisted by a number of above CPI increases in a number of revenue items in 2015 that are expected to remain at the 2015 levels or improve in the subsequent forecast years.

The final year of the SRV is 2019 and the operating result is projected to remain at the breakeven level because interest and investment revenue is forecast to decrease as the SRV funds are fully utilised to cover the increase in the associated materials and contracts expenses, while other expenses are also projected to increase by 7.8%. The SRV is to be permanently retained in the rate base.

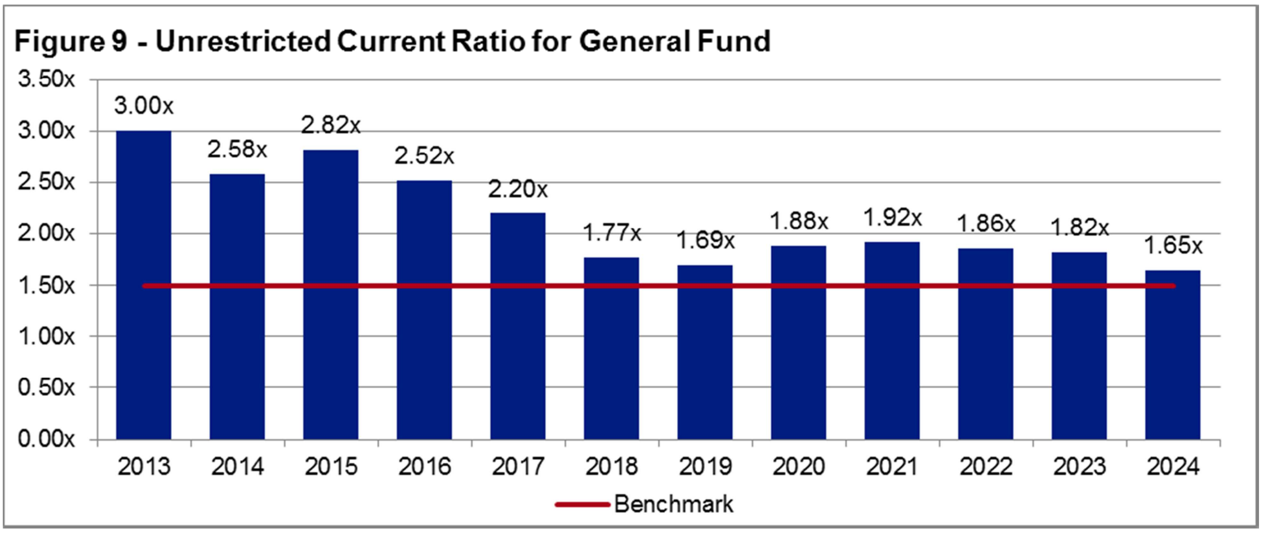
3.2 Financial Management Indicators

Liquidity Ratios



Council continues to invest the majority of its funds into investments with durations greater than three months. The Cash Expense Ratio does not include these funds as it is measuring the level of funds that would be immediately available should another financial crisis occur similar to the Global Financial Crisis.

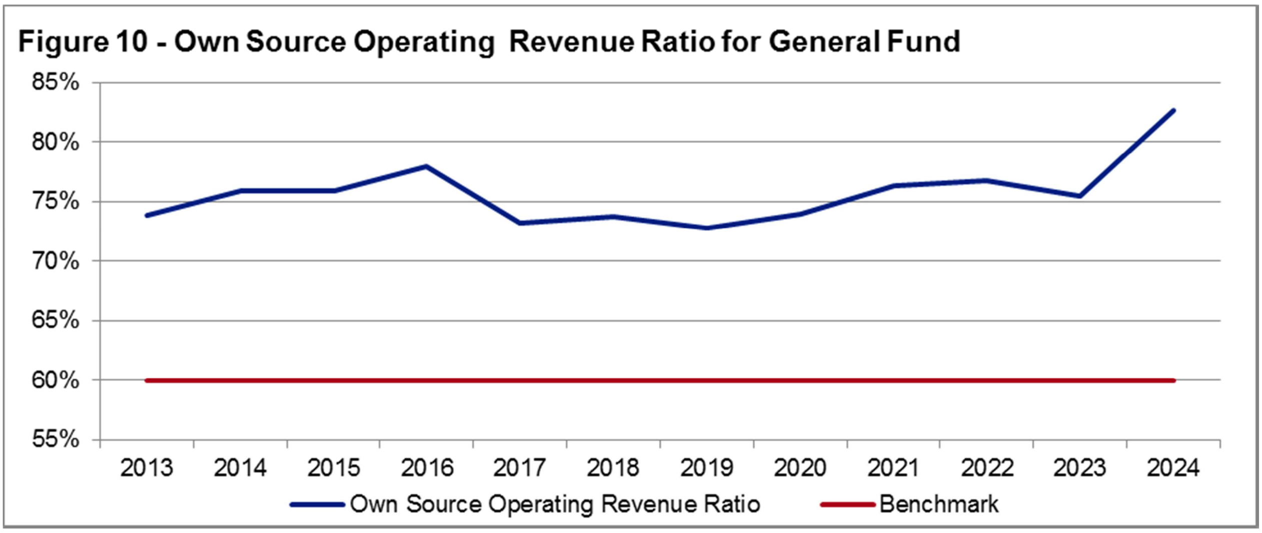
This therefore provides a ratio result below the 3.0 month benchmark in each year with the ratio decreasing over the 10 year period from 1.8 months in 2014 to 0.2 months in 2018 before a marginal increase to 0.8 months in 2024. This is because Council has forecast cash and cash equivalents to reduce during the 10 years of the LTFP with investments remaining static, while operating expenses are forecast to increase over the 10 year period.



The Unrestricted Current Ratio is forecast to remain above the benchmark for the duration of the forecast although it is forecast to reduce below 2.0x from 2018 onwards. Current assets are forecast to decrease from $61.2m in 2014 to $53.8m in 2024 due to the decrease in cash and cash equivalents while current liabilities are forecast to increase from $27.5m in 2014 to $33.7m in 2024.

Overall, Council's cash and cash equivalents and investments combined indicate a sound liquidity position however the cash and cash equivalents are below a level that TCorp would ideally recommend as highlighted by the low Cash Expense Ratio.

Fiscal Flexibility Ratios

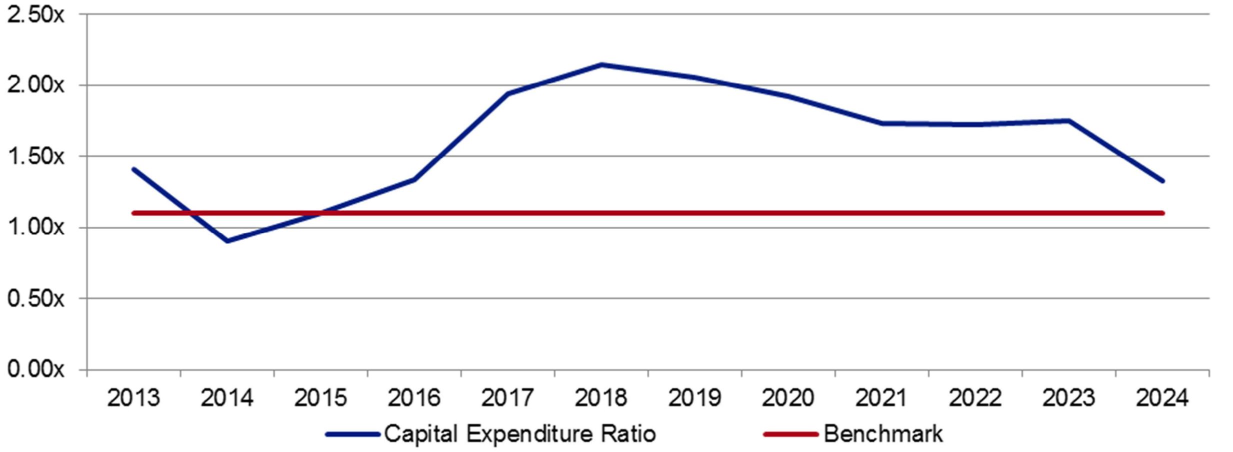


The majority of Council's revenue is generated from rates and annual charges, and user charges and fees. This indicates Council is not heavily reliant on external sources of funding. This results in a ratio that is forecast to remain comfortably above the benchmark and above 70% in each year of the LTFP. The five year SRV from 2015 will assist to keep the own source operating revenue at these levels while the decrease in 2017 is due to an $8.0m increase in capital grants and contributions forecast in that year.

Council has not utilised any borrowings since 2010 but does have capacity to use debt of up to $38.4m should it be required to assist in the financing of any infrastructure assets based on a Debt Service Cover Ratio above 2.00x.

3.3 Capital Expenditure

Figure 11 - Capital Expenditure Ratio for General Fund



The Capital Expenditure Ratio increases to the benchmark in 2015 and remains above the benchmark in the following nine years. Over the 10 year period Council is forecast to spend $277.3m on capex compared to the 10 year forecast total depreciation of $162.6m.

Council has a high population growth rate which has seen a 10.5% increase between 2006 and 2011 and it is forecast to increase by a further 42.8% in the 20 years to 2031. Council has detailed that following approval of the five year SRV, a 20 year capital works plan including Section 94 plan infrastructure works totalling $300m has been created to enable the LGA to manage the ongoing population increases experienced within the area.

The works cover such projects as land acquisition, new roads drainage and buildings to facilitate the rapid growth of the LGA, car park developments, drainage refits, an aquatic health and wellness centre, (costing an expected $32m over 2017 to 2019 years), sporting facilities upgrade and the continuing works on roads, footpaths, buildings (17 childcare centres, youth and community centres) and parks.

The maintenance of assets & infrastructure at sustainable levels i.e. maintaining current service levels was a priority of the community when they were consulted in relation to the SRV. With the strong forecast increase in population, maintaining current service levels while accommodating for the increased population results in Council's expectation of the Capital Expenditure Ratio and Building and Infrastructure Asset Renewals Ratio being at above average levels for the next 20 years.

The Capital Expenditure Ratio average is 1.70x for the 10 year period while the Building and Infrastructure Asset Renewals Ratio average is 1.40x. Council expect these ratios to remain above the benchmarks from 2024 – 2034 but at lower levels than the period of the current LTFP.

3.4 Financial Model Assumption Review

Council has used its own assumptions in developing their forecasts.

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

TCorp's benchmarks:

- Rates and annual charges: TCorp notes that the Local Government Cost Index (LGCI) increased by 3.4% in the year to September 2011, 2.8% in 2012, and 3.6% in 2013 and 3.4% in 2014. In December 2013 IPART announced that the rate peg to apply in the 2014/15 financial year will be 2.3%. Beyond 2015 TCorp has assessed a general benchmark for rates and annual charges to increase by mid-range LGCI annual increases of 3.0%.
- IPART developed the LGCI to use for setting the maximum allowable increase in general income for local government in NSW (rate peg). The LGCI is the measure of movement in the unit costs incurred by NSW council activities funded from the general rate base.
- Interest and investment revenue: annual return of 5%
- All other revenue items: the estimated annual CPI increase of 2.5%
- Employee costs: 3.5% (estimated CPI+1%)
- All other expenses: the estimated annual CPI increase of 2.5%

Key Observations and Risks

- The LTFP has been based on maintaining the existing standard of services to the community and incorporates the five year SRV that was approved by IPART in June 2014 to assist in maintaining these services and related assets along with providing assistance with longer term sustainability from 2014/2015. This SRV includes an 8% p.a. increase for three years followed by a 7% p.a. increase for the next two years. The cumulative increase over this period is 44.2%.
- Council has forecast a $2.7m (23.0%) increase in user charges and fees driven by a full year of childcare fees from the new centre at Pemulwuy and increased planning fees that are expected to increase by 80% due to increased development applications in the Holroyd LGA.
- Interest and investment revenue is forecast to increase by $0.5m (17.8%) with additional cash and cash equivalents held as the SRV income is received. The model does include projected cash rate rises in the second half of 2015 and into 2016 however with the benefit of current economic data it appears that a rate cut rather than a rate rise could be the RBA's next move to counteract soft domestic data. A 5.0% return on invested funds has been forecast for each year which is in line with the returns in 2013 and 2014.
- Council has also forecast a $1.8m (73.4%) increase in other revenues with parking fines and infringement notices contributing to the increase as Council has introduced electronic scanning devices and employed an additional three FTE parking patrol officers in 2015. Council has stated that this will bring them in line with other urban councils in terms of technology and ability to manage this area of their business.
- Grants and contributions for operating purposes are forecast to decrease by 6.3% in 2015 and remain below the 2014 total until 2023. Council is expecting a decrease in the region of $1.9m in child care/family day care specific purpose grants in 2015 following these being cancelled by the

Federal Government – this is part of the reason for the increase in the user charges and fees detailed above. This will be offset to an extent by the regularised payments of the FAG that could increase by up to $2.0m compared to 2014. The FAG increasing at this level will actually result in operating grants and contributions being $1.0m higher than actually forecast.

- Materials and contracts expense is forecast to increase by $4.1m (26.8%) in 2015 in line with the increased spend on maintenance and renewals, partly funded by the new SRV revenue. Council also sees continued increases in expenses relating to the operating and maintaining of parks, entertainment and sporting facilities including the three swimming pools in the LGA and the related ancillary cost of this additional spend in subcontractor and consultancy fees.
- Other expenses are forecast to increase by 9.2% in 2015 with residual waste disposal tipping fees (outsourced to SITA) expected to continue to increase at high levels – they have increased 14% in the first half of the year. IT, insurance and energy costs are also projected to increase above CPI.
- Depreciation is forecast in line with Council's Asset Management Plans however these have not been reviewed by TCorp. With the significant increase in the asset base, depreciation is forecast to grow in each year from $12.9m in 2014 to $20.1m in 2024.
- All other revenue and expenses are forecast to increase by 3.0% p.a.

3.5 Sustainability

Based on the information received and the revised LTFP, TCorp believes Council to currently be in a Moderate Sustainability position. The Outlook for Council for the next three years is Positive.

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

- The amended depreciation figures for 2011 and 2012 have assisted in improving the Financial Sustainability Rating (FSR) to Moderate in conjunction with the operating results for 2013 and 2014.
- The approved five year SRV is forecast to assist Council to achieve a break-even operating result by 2018. An operating result in line with a break-even position is forecast for the remaining six years of the forecast.
- Council's Own Source Operating Revenue Ratio is forecast to remain above benchmark in all 10 years of the forecast period.
- Council has forecast increased expenditure on the maintenance of its existing assets.
- Capital expenditure is forecast to be adequately spent on new and renewal assets so that Council's asset base will be maintained and grow over the 10 year period.
- Council has forecast a strong increase in capital grants and contributions from 2017 to 2023 compared to historical amounts received. These are forecast to assist with the 20 year capital works plan. If forecast growth does not occur then lower levels of grants will be received and some projects will be delayed or possibly withdrawn.
- While Council has not forecast the requirement for any borrowings, there is capacity to utilise debt to assist with asset purchases or renewals if required.

4 Conclusion and Recommendations

Based on our review of both the historic financial information and the 10 year financial forecast within Council's LTFP we consider Council to be in an improved position when compared to the analysis within our April 2013 report. Council's current Financial Sustainability Rating (FSR) is Moderate when analysing the five year historic financials between 2010 and 2014 with an Outlook of Positive. This is due to Council's forecast improvement in their operating performance.

We base our conclusion on the following key points:

- Council's review of its infrastructure assets has significantly decreased the annual depreciation expense. The review that Council has completed was based on a reassessment of the useful lives and residual values of assets. This has reduced the annual operating expenses and improved the operating result and forecast performance.
- Council has successfully applied for a five year SRV that will add 44.2% to the rate revenue over the five years. This increase will be permanently integrated into Council's rates and will assist in funding future asset renewals and capital works and improve overall financial performance.
- These two factors should assist Council to achieve sustainable break-even operating results within the next five years.

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

- Council has forecast significant capital expenditure across their LTFP and this is reflected in a high Capital Expenditure Ratio and Buildings and Infrastructure Renewals Ratio across the 10 years of the forecast. Council has confirmed that following approval of the five year SRV, they have created a 20 year capital works plan including Section 94 plan infrastructure works which totals $300m to enable the LGA to manage the ongoing population increases experienced within the area.
- A significant increase in capital grants and contributions has been forecast to assist with funding the 20 year capital works plan and if these are not received as forecast then some expenditure may not be required or will need to be delayed or possibly withdrawn. Council will need to closely monitor this extensive program of capital investment.

Appendix A Historical Financial Information Tables

Table 1-Income Statement

Income statement	Year ended 30 June					% annual change			
	2014	2013	2012	2011	2010	2014	2013	2012	2011
Revenue									
Rates and annual charges	54,499	52,492	48,561	44,700	42,038	3.8%	8.1%	8.6%	6.3%
User charges and fees	11,633	9,503	9,808	9,311	8,412	22.4%	(3.1%)	5.3%	10.7%
Interest and investment revenue	2,618	3,143	3,764	3,821	4,256	(16.7%)	(16.5%)	(1.5%)	(10.2%)
Grants and contributions for operating purposes	11,644	13,033	13,517	11,114	10,027	(10.7%)	(3.6%)	21.6%	10.8%
Other revenues	2,469	2,839	1,808	1,662	1,967	(13.0%)	57.0%	8.8%	(15.5%)
Total revenue	**82,863**	**81,010**	**77,458**	**70,608**	**66,700**	**2.3%**	**4.6%**	**9.7%**	**5.9%**
Expenses									
Employees	40,104	37,924	37,026	32,986	32,205	5.7%	2.4%	12.2%	2.4%
Borrowing costs	0	0	0	0	24	N/A	N/A	N/A	(100.0%)
Materials and contract expenses	15,397	13,804	15,552	12,216	12,269	11.5%	(11.2%)	27.3%	(0.4%)
Depreciation and amortisation	12,929	12,568	12,624	12,620	10,852	2.9%	(0.4%)	0.0%	16.3%
Other expenses	18,040	17,816	16,681	13,193	12,386	1.3%	6.8%	26.4%	6.5%
Total expenses	**86,470**	**82,112**	**81,883**	**71,015**	**67,736**	**5.3%**	**0.3%**	**15.3%**	**4.8%**
Operating result (excluding capital grants and contributions)	**(3,607)**	**(1,102)**	**(4,425)**	**(407)**	**(1,036)**	**(227.3%)**	**75.1%**	**(987.2%)**	**60.7%**
Operating result (including capital grants and contributions)	**628**	**1,778**	**1,082**	**10,688**	**2,397**	**(64.7%)**	**64.3%**	**(89.9%)**	**345.9%**

Table 2 - Items excluded from Income Statement

Excluded items	2014	2013	2012	2011	2010
Grants and contributions for capital purposes	4,235	2,880	5,507	11,095	3,433
Fair valuation movements in investments	106	178	29	(222)	(1,256)
Net share of interests in joint ventures and associated entities	25	259	346	356	120
Net gain from the disposal of assets	165	145	218	106	265
Other revenues - write back of duplicate payment	0	0	830	0	0

Table 3 – Employee Numbers

	2014	2013	2012	2011	2010
Full Time Equivalent Employees at year end	520	505	454	446	443

Table 4 – Balance Sheet

Balance sheet ($'000s)	Year ended 30 June					% annual change			
	2014	2013	2012	2011	2010	2014	2013	2012	2011
Current assets									
Cash and cash equivalents	10,885	12,523	11,338	6,307	9,225	(13.1%)	10.5%	79.8%	(31.6%)
Investments	29,358	28,251	44,991	53,696	41,567	3.9%	(37.2%)	(16.2%)	29.2%
Receivables	4,650	4,937	3,785	4,135	4,450	(5.8%)	30.4%	(8.5%)	(7.1%)
Inventories	283	303	278	2,205	2,186	(6.6%)	9.0%	(87.4%)	0.9%
Other	0	103	102	139	38	(100.0%)	1.0%	(26.6%)	265.8%
Total current assets	45,176	46,117	60,494	66,482	57,466	(2.0%)	(23.8%)	(9.0%)	15.7%
Non-current assets									
Investments	16,000	13,000	0	0	0	23.1%	N/A	N/A	N/A
Receivables	342	280	324	493	456	22.1%	(13.6%)	(34.3%)	8.1%
Infrastructure, property, plant & equipment	953,007	953,500	817,449	820,195	932,882	(0.1%)	16.6%	(0.3%)	(12.1%)
Investments accounted for using the equity method	1,641	1,616	1,357	1,011	655	1.5%	19.1%	34.2%	54.4%
Investment property	0	0	1,929	1,235	3,992	N/A	(100.0%)	56.2%	(69.1%)
Intangible assets	0	0	0	872	795	N/A	N/A	(100.0%)	9.7%
Total non-current assets	970,990	968,396	821,059	823,806	938,780	0.3%	17.9%	(0.3%)	(12.2%)
Total assets	**1,016,166**	**1,014,513**	**881,553**	**890,288**	**996,246**	**0.2%**	**15.1%**	**(1.0%)**	**(10.6%)**

Balance sheet ($'000s)	Year ended 30 June					% annual change			
	2014	2013	2012	2011	2010	2014	2013	2012	2011
Current liabilities									
Payables	16,859	17,757	17,385	18,913	16,314	(5.1%)	2.1%	(8.1%)	15.9%
Borrowings	0	0	0	0	0	N/A	N/A	N/A	N/A
Provisions	10,616	10,594	9,583	9,033	8,849	0.2%	10.5%	6.1%	2.1%
Total current liabilities	27,475	28,351	26,968	27,946	25,163	(3.1%)	5.1%	(3.5%)	11.1%
Non-current liabilities									
Borrowings	0	0	0	0	0	N/A	N/A	N/A	N/A
Provisions	1,088	987	1,259	483	644	10.2%	(21.6%)	160.7%	(25.0%)
Total non-current liabilities	1,088	987	1,259	483	644	10.2%	(21.6%)	160.7%	(25.0%)
Total liabilities	**28,563**	**29,338**	**28,227**	**28,429**	**25,807**	**(2.6%)**	**3.9%**	**(0.7%)**	**10.2%**
Net assets	**987,603**	**985,175**	**853,326**	**861,859**	**970,439**	**0.2%**	**15.5%**	**(1.0%)**	**(11.2%)**

Table 5 - Cashflow

Cash Flow Statement ($'000s)	Year ended 30 June				
	2014	2013	2012	2011	2010
Cash flows from operating activities	12,717	14,052	12,127	23,359	17,507
Cash flows from investing activities	(14,355)	(12,867)	(7,096)	(26,277)	(8,169)
Proceeds from borrowings and advances	0	0	0	0	0
Repayment of borrowings and advances	0	0	0	0	(737)
Cash flows from financing activities	0	0	0	0	(737)
Net increase/(decrease) in cash and equivalents	**(1,638)**	**1,185**	**5,031**	**(2,918)**	**8,601**

Appendix B Glossary

Asset Revaluations

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

Collateralised Debt Obligation (CDO)

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

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

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

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

Office of Local Government (OLG)

OLG (previously DLG) is an Office in the Planning and Environment cluster and is responsible for local government across NSW. OLG’s organisational purpose is “to strengthen the local government sector” and its organisational outcome is “successful councils engaging and supporting their communities”. Operating within several strategic objectives OLG has a policy, legislative, investigative and program focus in matters ranging from local government finance, infrastructure, governance, performance, collaboration and community engagement. OLG 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.

[1] IPART “Revenue Framework for Local Government” December 2009 p.83
[2] DLG “Recognition of certain assets at fair value” March 2009

Financial Sustainability Rating (FSR)
The FSR is an assessment of a council's capacity to meet its financial commitments in the short, medium and long term. The FSR for each Council has been determined based on the review and consideration of a Council's historical performance against a set of benchmark indicators. The rating methodology consists of seven FSR categories. The FSR is calculated using weighted benchmarks according to the relative importance of each benchmark in terms of a Council's financial capacity and sustainability.

Grants and Contributions for Capital Purposes

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

Grants and Contributions for Operating Purposes

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

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

Independent Commission Against Corruption (ICAC)

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

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

Independent Pricing and Regulatory Tribunal (IPART)

IPART has four main functions relating to the 152 local councils in NSW. Each year, IPART determines the rate peg, or the allowable annual increase in general income for councils. They also review and determine council applications for increases in general income above the rate peg, known as "Special Rate Variations". They approve increases in council minimum rates.

They also review council development contributions plans that propose contribution levels that exceed caps set by the Government.

Infrastructure Backlog

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

Integrated Planning and Reporting (IP&R) Framework

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

Local Government Cost Index (LGCI)

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

Net Assets

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

Roads and Maritime Services (RMS)

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

Outlook

The Outlook assigned to Council is TCorp's assessment of the potential movement of Council's FSR within the next three years. The outlook methodology consists of three categories. A positive Outlook indicates that a Council's FSR is likely to improve in the short term, whilst a Neutral Outlook indicates that the FSR is likely to remain unchanged. A Negative Outlook indicates that a Council's FSR is more likely to deteriorate and is a sign of a general weakening in performance and sustainability.

Section 64 Contribution

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

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

Section 94 Contribution

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

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

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

Special Rate Variation (SRV)

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

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

The applications are reviewed and approved by IPART.

Sustainability

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

Ratio Explanations

Asset Maintenance Ratio

Benchmark = Greater than 1.0x

Ratio = actual asset maintenance / required asset maintenance

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

Building and Infrastructure Renewals Ratio

Benchmark = Greater than 1.0x

Ratio = Asset renewals / depreciation of building and infrastructure assets

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

Cash Expense Cover Ratio

Benchmark = Greater than 3.0 months

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

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

Capital Expenditure Ratio

Benchmark = Greater than 1.1x

Ratio = annual capital expenditure / annual depreciation

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

Debt Service Cover Ratio (DSCR)

Benchmark = Greater than 2.0x

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

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

Building and Infrastructure Backlog Ratio

Benchmark = Less than 0.02x

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

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

Interest Cover Ratio

Benchmark = Greater than 4.0x

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

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

Operating Ratio

Benchmark = Better than negative 4%

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

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

Own Source Operating Revenue Ratio

Benchmark = Greater than 60%

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

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

Unrestricted Current Ratio

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

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

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

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