New South Wales
Treasury Corporation

Tumbarumba Shire Council

Financial Assessment, Sustainability and Benchmarking Report

3 April 2013

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

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Disclaimer

This report has been prepared by New South Wales Treasury Corporation (TCorp) in accordance with the appointment of TCorp by the Division of Local Government (DLG) as detailed in TCorp's letters of 22 December 2011 and 28 May 2012. The report has been prepared to assist the DLG and the Independent Local Government Review Panel in its consideration of the Sustainability of each local government area in NSW.

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

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

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

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Section 1 Executive Summary

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

TCorp's approach has been to:

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

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

- Council consistently recorded operating surpluses in each of the last four years, trending upwards for the last three years
- Council's EBITDA has doubled over the four year period to $5.8m
- Cash and cash equivalents have increased over the review period

The Council reported $5.4m of infrastructure backlog in 2012 which represents 4.3% of its infrastructure asset value of $124.4m. Other observations include:

- Road assets is the largest category of Infrastructure Backlog at 35.0% and drainage works account for 27.0% of the total Backlog
- The Backlog has decreased by 67.8% since 2009 due to considerable flood restoration works in 2012 and 2011.

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

- Council's Operating Ratio is forecast to be generally above benchmark
- The Own Source Revenue Ratio is forecast to be below benchmark
- Council's Interest Cover Ratio, Debt Service Cover Ratio, Unrestricted Current Ratio and Cash Expense Ratio are all forecast to be above benchmark
- Council's long run Capital Expenditure Ratio forecast is an average of 0.8x p.a, which would not be sufficient to keep infrastructure assets in their satisfactory condition.

In our view, the Council has the capacity to undertake additional borrowings of up to $5.3m. This is based on the following analysis:

- Based on a benchmark of DSCR>2.0x, up to $5.3m could be borrowed in addition to any existing borrowings
- This scenario has been calculated by basing borrowing capacity on a 10 year amortising loan at 7.5% p.a.

In considering the longer term financial Sustainability of the Council we consider Council to be in a sound position. Our key observations are:

- Council has built up cash reserves which could be used to fund its forecast capital expenditure program and reduce the Infrastructure Backlog
- Council's LTFP takes a conservative approach to forecasting its operating and capital grant revenue but despite this, Council continues to forecast operating surpluses which may therefore be marginally understated
- The long term Sustainability of the Council is dependent on Council continuing to receive operating grants and contributions from both the State and Federal government to support its operations
- Council's forecast capital expenditure program is below benchmark from 2016

In respect of the Benchmarking analysis TCorp has compared the Council's key ratios with other councils in DLG Group 9. The key observations are:

- Council's current Operating Ratio performance has been strong with above benchmark and group average levels. This is forecast to decline marginally over the medium term but remain above both the group's average and at or near benchmark
- The Council is forecast to be in a strong liquidity position with both the Cash Expense Ratio and the Unrestricted Current Ratio above benchmark by 2016
- The Council has a sound level of debt servicing capacity with DSCR and Interest Cover Ratio above benchmark. Council could support further debt financing if required
- The Council has focused on asset renewal and this has reduced the Infrastructure Backlog. The Council will need to continue to focus on its capital expenditure as it is currently projected to fall below the benchmark level by 2016

Section 2 Introduction

2.1: Purpose of Report

This report provides the Council with an independent assessment of their financial capacity, Sustainability and performance measured against a peer group of councils. It will complement Council's internal due diligence, the IP&R system of the Council and the DLG, together with the work being undertaken by the Independent Local Government Review Panel.

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

The key areas focused on are:

- The financial capacity of the Council
- The long term Sustainability of the Council
- The financial performance of the Council in comparison to a range of similar councils and measured against prudent benchmarks

2.2: Scope and Methodology

TCorp's approach was to:

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

In undertaking its work, TCorp relied on:

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

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

- Council agrees with the findings of the report

Definition of Sustainability

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

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

Benchmark Ratios

In conducting our review of the Councils' financial performance, forecasts and Sustainability we have measured performance against a set of benchmarks. These benchmarks are listed below.

Benchmarks do not necessarily represent a pass or fail in respect of any particular area. One-off projects or events can impact a council's performance against a benchmark for a short period. Other factors such as the trends in results against the benchmarks are critical as well as the overall performance against all the benchmarks.

As councils can have significant differences in their size and population densities, it is important to note that one benchmark does not fit all. For example, the Cash Expense Ratio should be greater for smaller councils than larger councils as a protection against variation in performance and financial shocks. Therefore these benchmarks are intended as a guide to performance.

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

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

2.3: Overview of the Local Government Area

Tumbarumba Shire Council	
Locality and Size	
Locality	Murray
Area	4,391.8km²
DLG Group No.	9
Demographics	
Population	3,358
% under 20	24.1%
% between 20 and 59	56.2%
% over 60	19.7%
Expected population in 2021	3,400
Operations	
Number of employees (FTE)	98
Annual revenue	$22.0m
Infrastructure	
Roads	476.2km
Bridges	41
Infrastructure backlog value	$5.4m
Total infrastructure value	$124.4m

The Shire's main economic activity is agriculture, followed by timber plantation and the processing industry is a key employer. Hyne and Son Pty Ltd operates a newly constructed mill at Tumbarumba, being the largest softwood processing mill in the southern hemisphere.

Horticulture, viticulture and tourism add to the economic strength of the area. The reputation of the region's cool climate wines continues to grow, with the achievement of numerous awards in the wine industry.

Other key employers are Tumbarumba Shire Council, Snowy Hydro, the National Parks and Wildlife Service, Mannus Correctional Centre and Murrumbidgee Local Health District which provides health services across the Shire. South of Tooma is the catchment of Upper Murray Health and Community Services operated from Corryong.

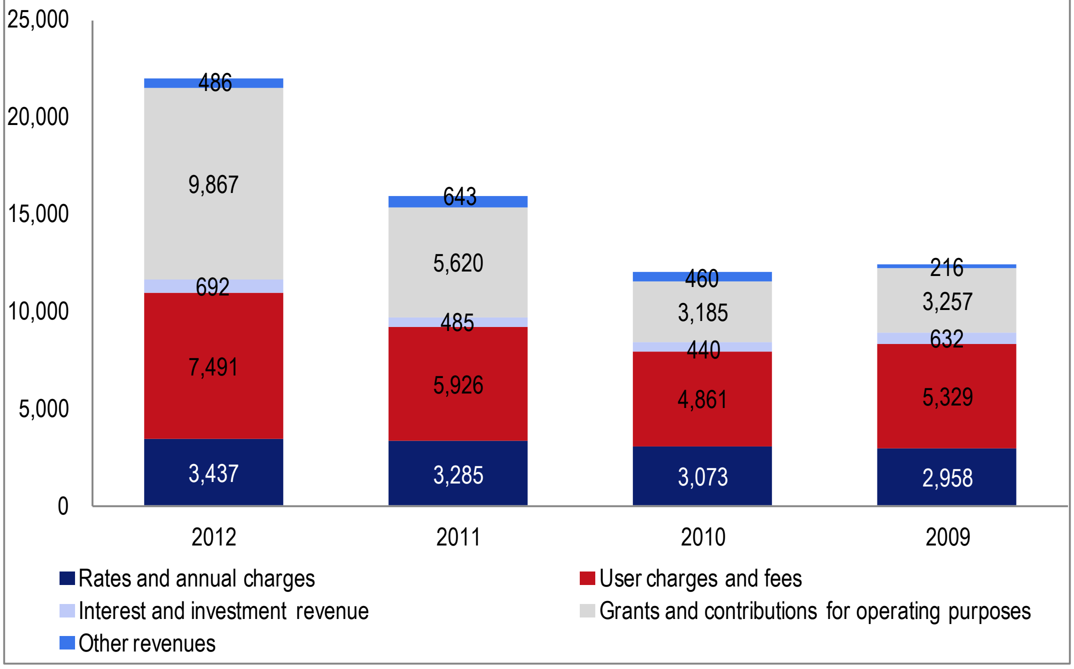
Council operates a number of shared services with neighbouring councils. This occurs in areas such as waste management, library services and road maintenance works.

Section 3 Review of Financial Performance and Position

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

3.1: Revenue

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

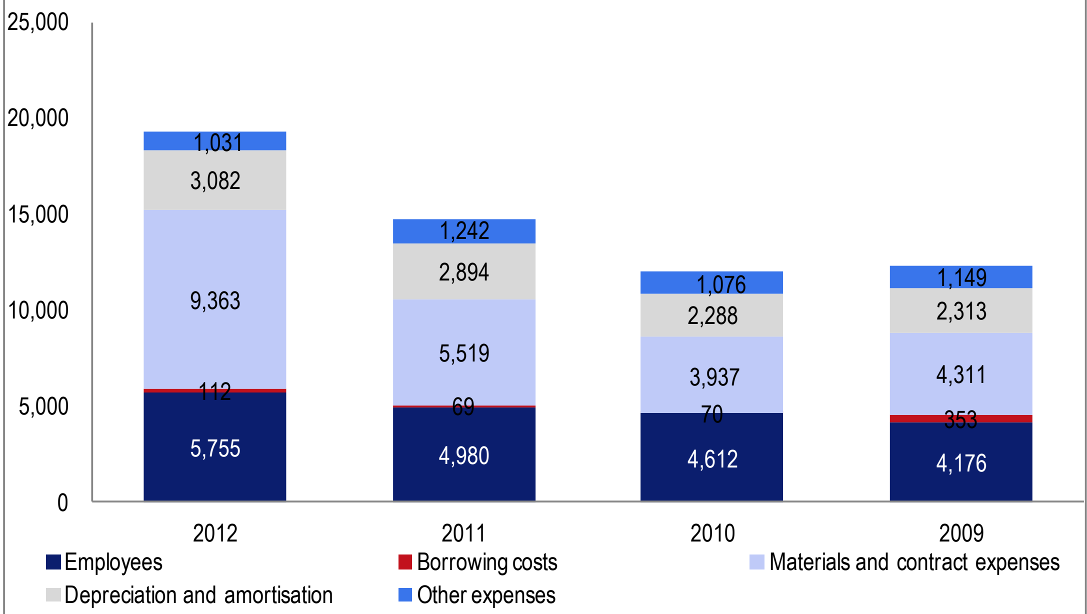


Key Observations

- Total revenue, excluding capital grants and contributions, increased by 77.3% over the four year period to $22.0m in 2012.
- Rates and annual charges have increased by 16.2% ($0.5m) since 2009. On a compounded annual basis, average growth has been 5.1% p.a. Rate growth of 3.1%p.a has been in line with standard rate peg. Annual charges have increased at a faster rate of 8.4% p.a, driven by increases in water supply charges and sewerage charges.
- User fees and charges have grown over the four year period with an overall increase of 40.6% ($2.2m) since 2009. On a compounded annual basis, average growth has been 12.0% p.a. RMS charges vary from year to year and can lead to volatile results. 2012 results benefited from RMS fees of $5.2m ($4.6m in 2011) in addition to acquisition and the first full year of Carcoola children centre fees totalling $0.6m
- Grants and contributions increased by 27.6% ($3.9m) in 2012 due to the Federal Government bringing forward $0.5m of the 2013 Financial Assistance Grant allocation to all NSW councils and RMS grants increasing by $2.9m as a result of flood damage funding from floods in the Shire in 2011 and 2012.

3.2: Expenses

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



Key Observations

- Council's total expenses increased by 57.2% ($7.0m) from 2009 to $19.3m in 2012. On a compounded annual basis, growth was 16.3% p.a.
- Full time equivalent employees increased from 79 in 2009 to 98 in 2012 as a result of Council acquiring the Carcoola childcare centre in 2012. On a per employee basis, total employee costs increased by 3.6% p.a. on a compounded annual basis since 2009.
- Materials and contracts expenses increased with RMS works, and were also impacted by restoration works following floods. Council's costs for RMS works are offset by revenue, while works to bring flood damaged assets back to their prior condition are offset by grants.
- Depreciation charges increased over the review period from $2.3m in 2009 to $3.1m in 2012, with the major increase in 2011 following the Asset Revaluations process which increased the value of Council's infrastructure assets.
- Other expenses include insurance and electricity.

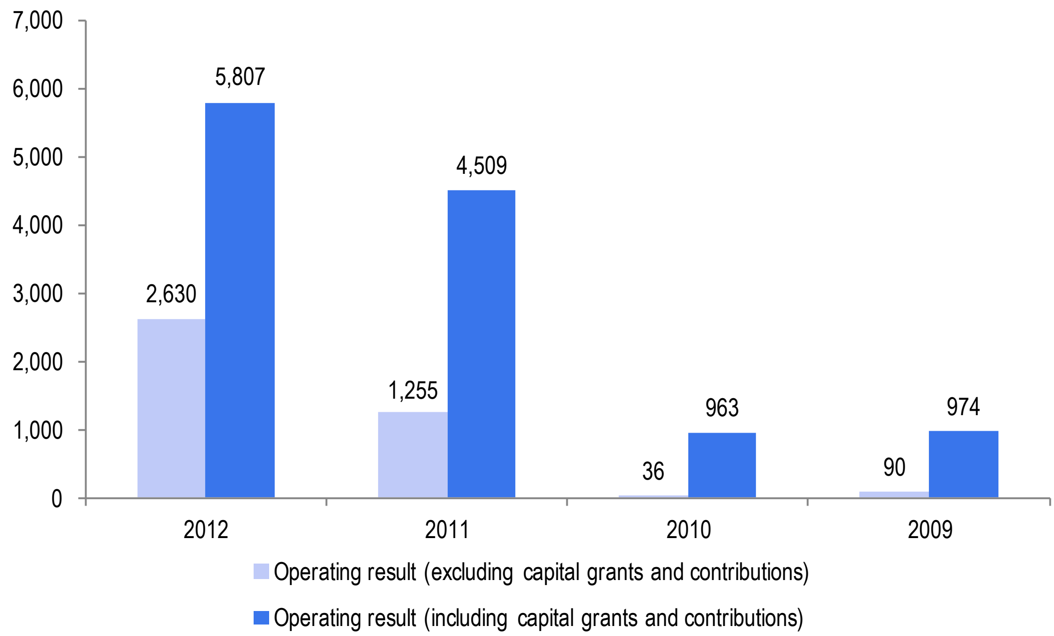
3.3: Operating Results

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

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

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

Figure 3 - Operating Results for 2008/09 to 2011/12 ($'000s)



Key Observations

- Council consistently recorded operating surpluses in each of the last four years, trending upwards for the last three years. Council results were positively affected in 2012 through the early receipt of operating grants from the 2013 financial year.
- Council expenses include a non-cash depreciation expense, ($3.1m in 2012), which has increased by $0.8m over the past three years following the Asset Revaluations process. Whilst the non cash nature of depreciation can favourably impact on ratios such as EBITDA that focus on cash, depreciation is an important expense as it represents the allocation of the value of an asset over its useful life.

3.4: Financial Management Indicators

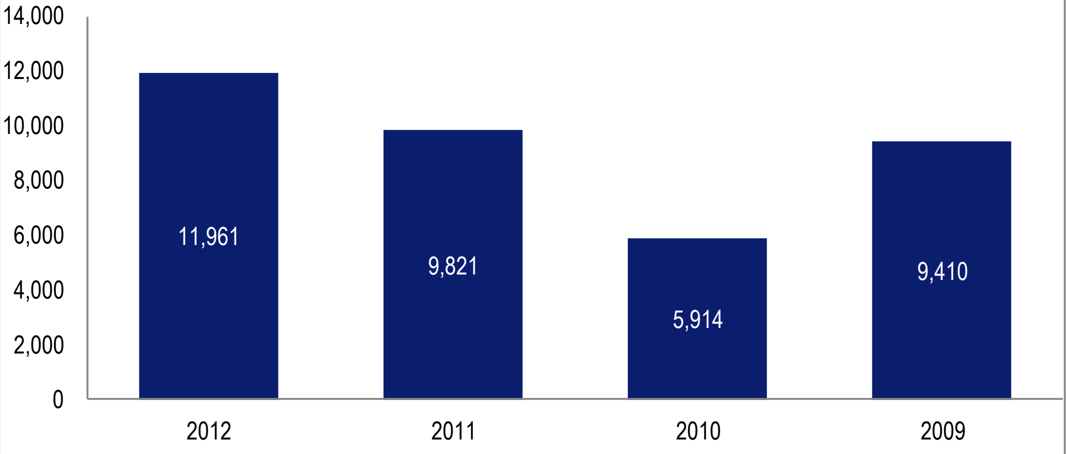
Performance Indicators	Year ended 30 June			
	2012	**2011**	**2010**	**2009**
EBITDA ($'000s)	5,824	4,218	2,394	2,756
Operating Ratio	12.0%	7.9%	0.3%	0.7%
Interest Cover Ratio	52.00x	61.13x	34.20x	7.81x
Debt Service Cover Ratio	27.87x	27.75x	16.07x	6.42x
Unrestricted Current Ratio	5.27x	4.71x	5.39x	3.21x
Own Sourced Operating Revenue Ratio	43.5%	47.9%	61.3%	62.4%
Cash Expense Ratio	8.9 months	10.0 months	7.4 months	11.7 months
Net Assets ($'000s)	158,357	146,546	142,187	104,914

Key Observations

- Council's EBITDA has increased over the four year period.
- The Unrestricted Current Ratio and Cash Expense Ratio have been well above the benchmarks in all four years indicating liquidity is sufficient.
- The Own Source Operating Revenue Ratio has been well below the benchmark the last two years, reflecting Council's increased grant revenue from RMS, for flood-restorations and advanced operating grant payments.
- Net Assets have increased by $53.4m between 2009 and 2012 due to the Asset Revaluations which increased the value of Council's infrastructure assets.
- The Asset Revaluations over the last four years have resulted in some volatility in Net Assets. Consequently, in the short term, the value of Net Assets is not necessarily an informative indicator of performance. In the medium to long term however, this is a key indicator of a Council's capacity to add value to its operations. Over time, Net Assets should increase at least in line with inflation plus an allowance for increased population and/or improved or increased services. Declining Net Assets is a key indicator of the Council's assets not being able to sustain the ongoing operations of Council.
- When the Asset Revaluations are excluded, the underlying trend in all four years has been an expanding Infrastructure, Property, Plant and Equipment (IPP&E) asset base with asset purchases being larger than the combined value of disposed assets and annual depreciation. Over the last four years this amounted to a $9.0m net increase in IPP&E.

3.5: Statement of Cashflows

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



Key Observations

- Cash and cash equivalents have increased over the review period. Council does not hold any investments.
- The Unrestricted Current Ratio indicated Council had sufficient liquidity.
- Within the $11.9.0m in total cash and cash equivalents, $4.9m was externally restricted, $6.9m was internally restricted and $0.1m was unrestricted.

3.6: Capital Expenditure

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

3.6(a): Infrastructure Backlog

Figure 5 - Infrastructure Backlog for 2008/09 to 2011/12($'000s)

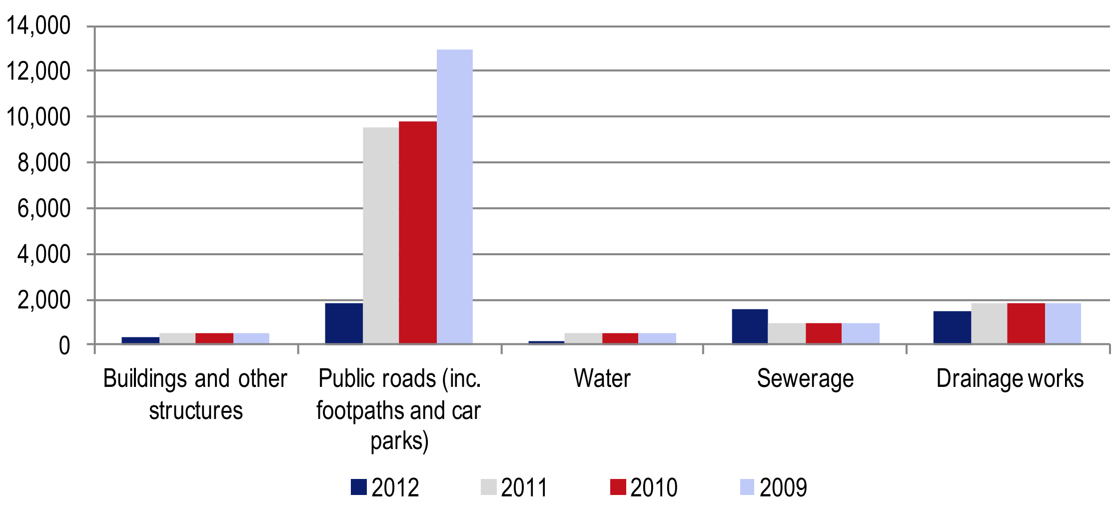
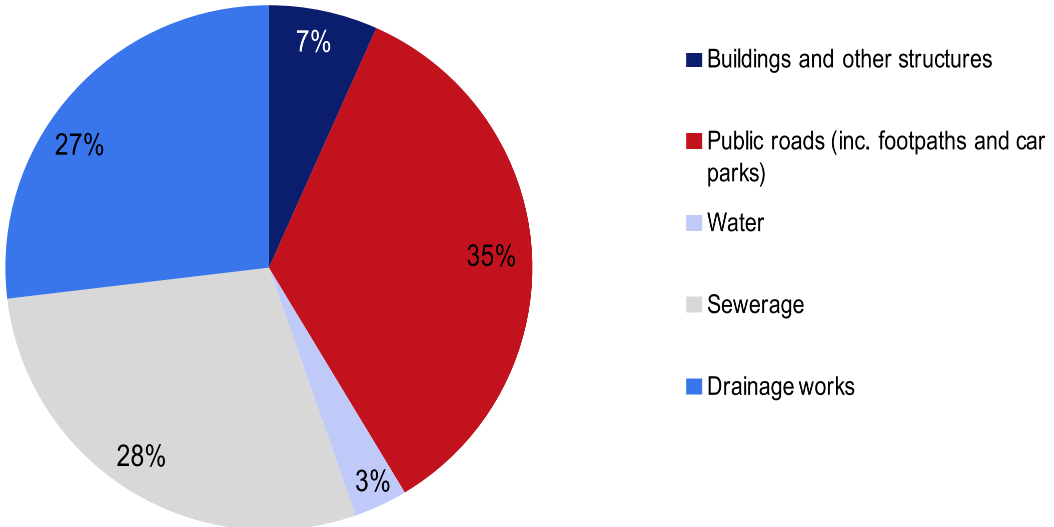


Figure 6 - Infrastructure Backlog Composition for 2011/12



The Council reported $5.4m of Infrastructure Backlog in 2012 which represents 4.3% of its infrastructure asset value of $124.4m.

Road asset is the largest category of the Infrastructure Backlog at 35.0% and drainage works account for 27.0%. The backlog has decreased significantly since 2009 due to considerable flood restoration works in 2012 and 2011. In recent years Council adopted a new Asset Management system which better enables Council to allocate its resources towards maintaining and improving its assets with better planning.

3.6(b): Infrastructure Status

Infrastructure Status	Year ended 30 June			
	2012	**2011**	**2010**	**2009**
Bring to satisfactory standard ($'000s)	5,398	13,407	13,648	16,770
Required annual maintenance ($'000s)	5,543	4,030	3,692	4,207
Actual annual maintenance ($'000s)	5,763	4,871	5,934	5,451
Total value infrastructure assets ($'000s)	124,380	115,355	111,968	68,030
Total assets ($'000s)	163,144	151,220	145,168	109,094
Infrastructure Backlog Ratio	0.04x	0.12x	0.12x	0.25x
Asset Maintenance Ratio	1.04x	1.21x	1.61x	1.30x
Building and infrastructure asset renewal ratio	1.76x	1.11x	1.13x	1.23x
Capital Expenditure Ratio	2.05x	1.90x	1.69x	1.70x

The Building and Infrastructure Renewals Ratio and Asset Maintenance Ratio both indicate that Council has been spending more than the required amounts on asset renewal and maintenance. A continuation of this level of spending will likely see the Infrastructure Backlog continuing to move towards zero.

3.6(c): Capital Program

The following figures are sourced from the Council's Annual Financial Statements at Special Schedule No. 8 and are not audited. New capital works are major non-recurrent projects. Council commenced the separate reporting of new capital works and replacement/refurbishment of existing assets in 2012 so numbers are not available for earlier years.

Capital Program ($'000s)	Year ended 30 June			
	2012	**2011**	**2010**	**2009**
New capital works	3,175	4,256	2,317	4,232
Replacement/refurbishment of existing assets	4,481	0	0	0
Total	**7,656**	**4,256**	**2,317**	**4,232**

Major capital works completed in 2012 included;

Roads:
- Natural disaster recovery flood damage works $1.5m
- Sealing and stabilisation of roads $1.0m
- Completion of the Tumbarumba water treatment plant $1.2m

Plant & Equipment:
- Replace vehicles, trucks and road building equipment $1.4m

Land Improvements:
- Land Development for residential estate $0.6m

3.7: Specific Risks to Council

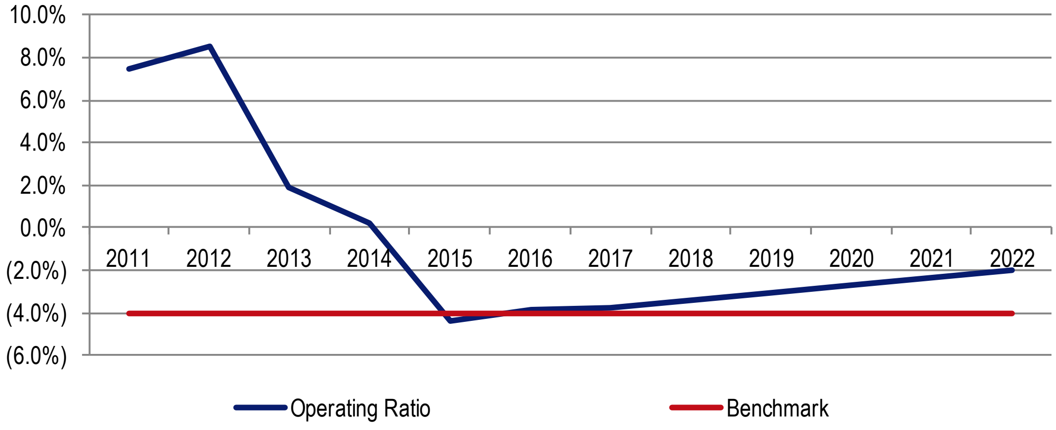
- Population. The LGA has a small and ageing population with growth in population size largely dependent on macroeconomic factors. Funding the increasing needs of an ageing population may require a changed focus from Council in future years. Council already promotes reaching out to elderly residents through provision of community transport, social outings, grocery delivery and home maintenance services.
- Freight on roads. In recent years there has been an increase in freight vehicles on the roads. More modern and bigger trucks combined with wet weather can cause significant deterioration in the local road network.
- Natural disasters. The LGA has been affected by flood events in recent years. As a result Council has had to prioritise repair work at the expense of other projects which are deferred in Council's delivery program. Council relies on grants and contributions from other levels of government particularly RMS, for repair works.

Section 4 Review of Financial Forecasts

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

4.1: Operating Results

Figure 7 - Operating Ratio for General Fund



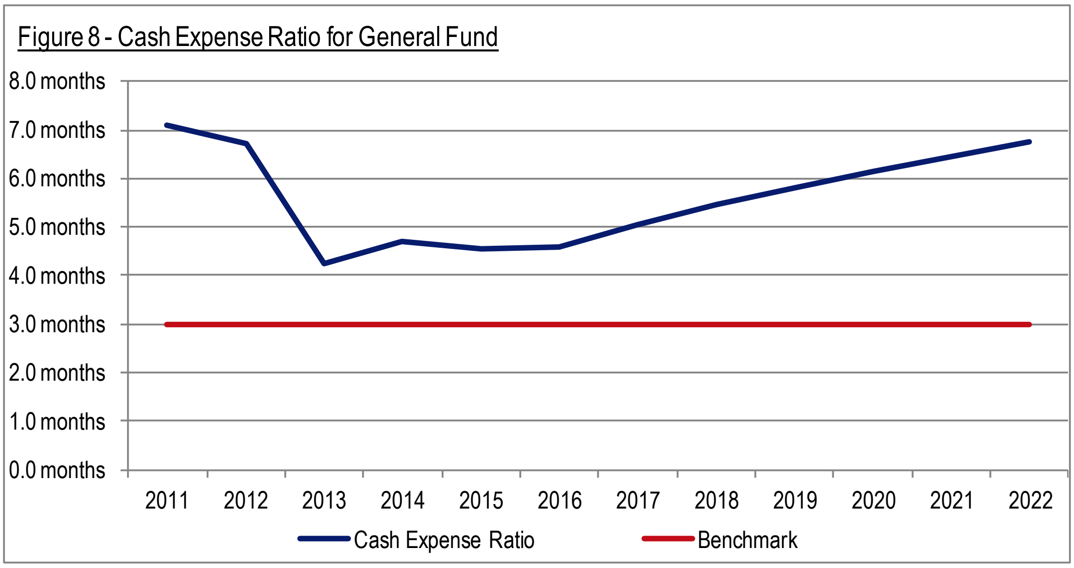
Council's Operating Ratio in the first two years of the LTFP to 2015 is impacted by higher Financial Assistance Grants and more restoration works. The ratio drops in 2014 and 2015 as Council projects a decline in RMS fees but forecasts a continuation of the same level of expense growth.

RMS user charges and fees, grants and material and contracts costs are higher as a result of flood restoration works to repair roads and infrastructure damaged from the previous three flood events, which were considered as repair expenses rather than capital work.

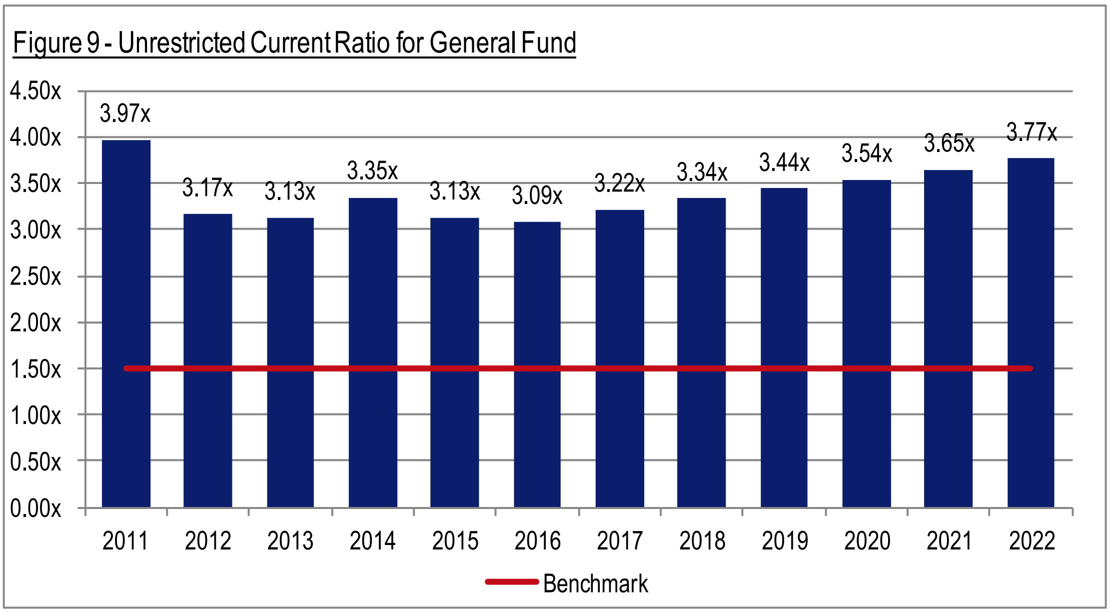
The spike in the Operating Ratio in 2012 and decline in 2013 is largely due to the significant prepayment of Financial Assistance Grants by the Federal government in 2012 which is not forecast to re-occur in 2013.

4.2: Financial Management Indicators

Liquidity Ratios



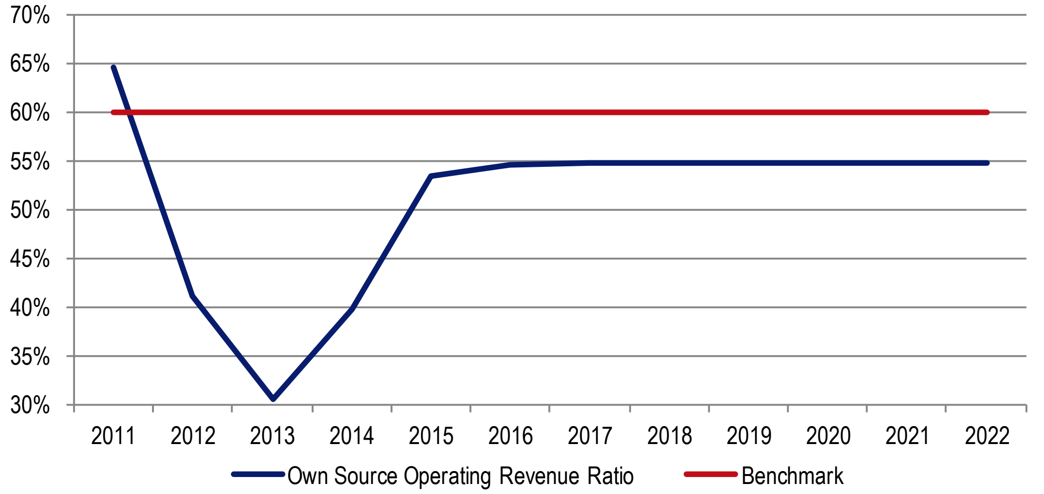
The Cash Expense Ratio remains above the benchmark each year of the forecast and is improving. Based on the above forecast Council would be in a strong liquidity position and may consider allocating investments to term deposits to attract higher interest rates and generate increased investment income.



The Unrestricted Current Ratio remains above benchmark each year.

Fiscal Flexibility Ratios

Figure 10 - Own Source Operating Revenue Ratio for General Fund



Own Source Operating Revenue Ratio for Council is forecast at 55% from 2015. The Ratio fluctuates significantly from 2011 to 2014 due to capital grant funding for restoration works. In particular, works to replace Mannus Dam, destroyed in the October 2010 flood event, is scheduled to occur during 2013.

The Own Source Operating Revenue Ratio is below benchmark reflecting Council's dependence on external grants and contributions. Being a large rural LGA with a sparse and dispersed population, Council does not have many opportunities to improve this ratio significantly.

Figure 11 - DSCR for General Fund

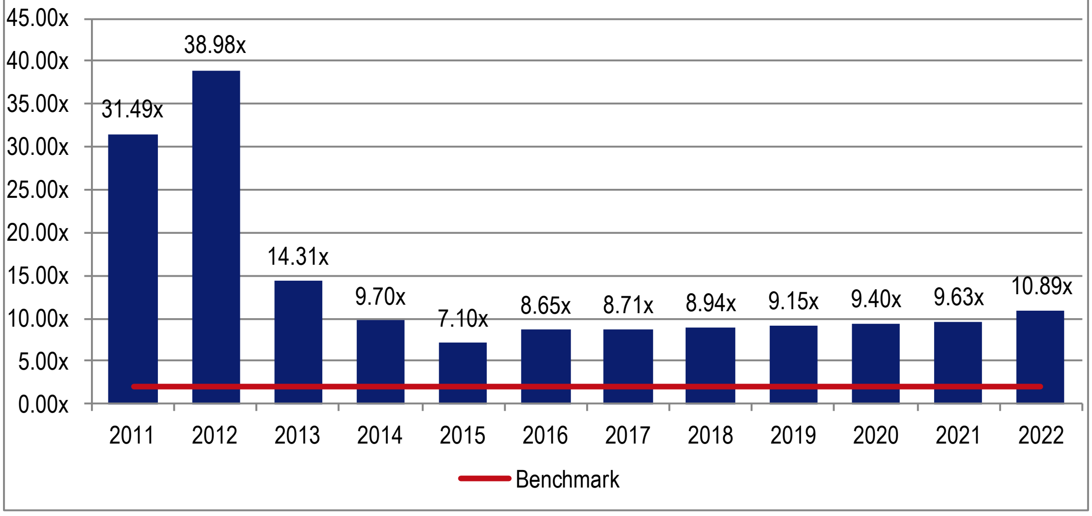
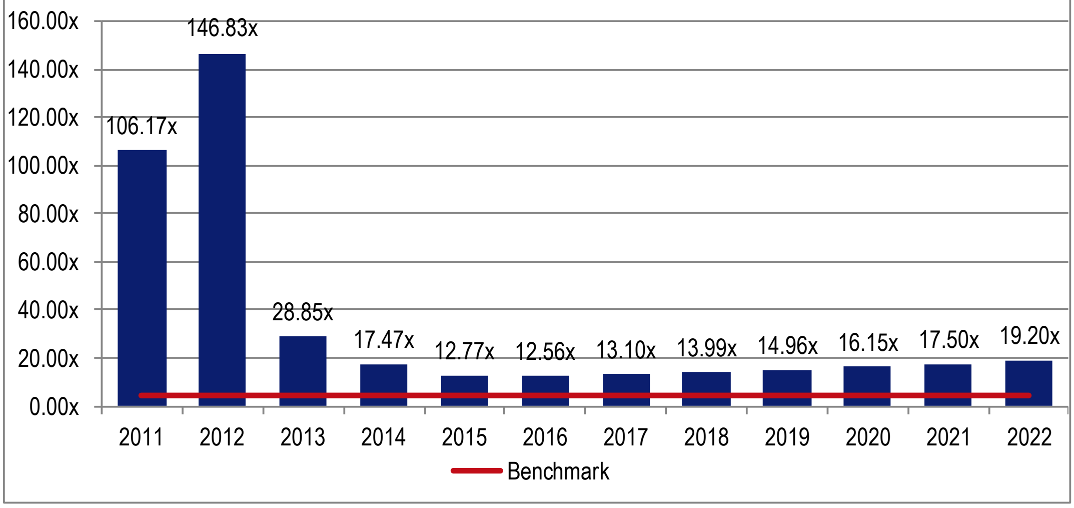


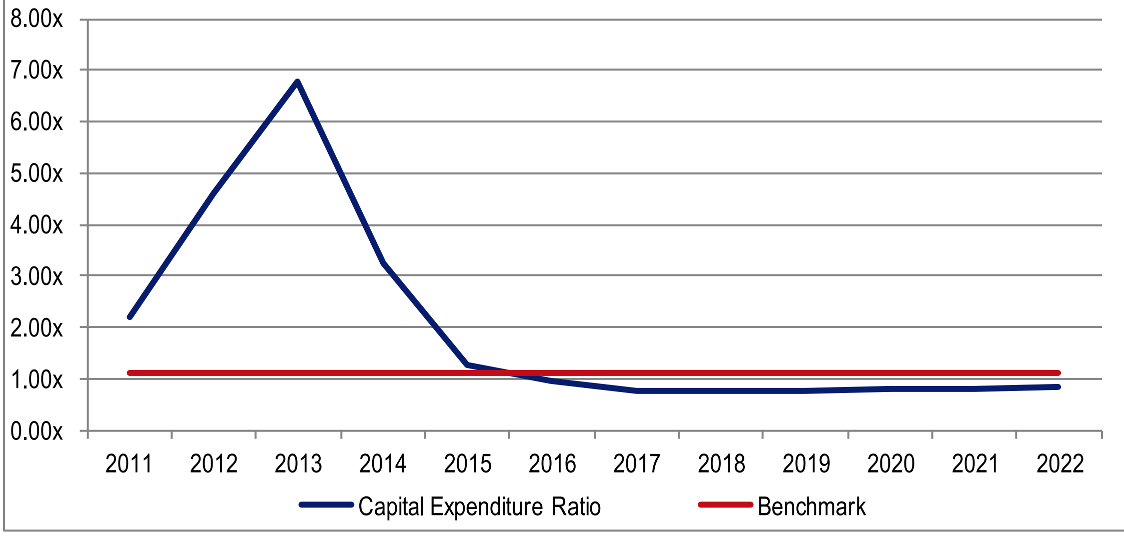
Figure 12 - Interest Cover Ratio for General Fund



The Unrestricted Current Ratio and Interest Cover Ratio remains above benchmark each year. Based on these Ratios, Council has an ability to service an increased level of debt, if required.

4.3: Capital Expenditure

Figure 13 - Capital Expenditure Ratio for General Fund



Council's Capital Expenditure Ratio for the General Fund peaks in 2013 due to the Mannus Dam project work. Council's long run forecast of an average of 0.8x p.a would not be sufficient to keep infrastructure assets in their current satisfactory condition when measured against the benchmark..

Planned capital expenditure projects until 2016 include

Project	Cost and funding source
Tumbarumba Retirement Village 8 Units	$2.5m Loan plus Council's funds
Establish Visitor Information centre in Khancoban	$0.6m Loan
Mannus Dam Restoration	$6.4m grant
Local and regional roads reseals and reconstruction	$2.8m Council's funds
The Parade CBD Upgrade	$1.4m Loan plus Council's funds
Major Road Repairs funded by Natural Disaster Assistance	$6.5m grant
Repair & Reconstruct Bald Hill	$5.0m grant
Renew Sewerage Treatment plant	$9.0m 50/50 grant/Council

4.4: Financial Model Assumption Review

Councils have used their own assumptions in developing their forecasts.

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

TCorp's benchmarks:

- Rates and annual charges: TCorp notes that the LGCI increased by 3.4% in the year to September 2011, and in December 2011, IPART announced that the rate peg to apply in the 2012/13 financial year will be 3.6%. Beyond 2013 TCorp has assessed a general benchmark for rates and annual charges to increase by mid-range LGCI annual increases of 3.0%
- Interest and investment revenue: annual return of 5.0%
- All other revenue items: the estimated annual CPI increase of 2.5%
- Employee costs: 3.5% (estimated CPI+1.0%)
- All other expenses: the estimated annual CPI increase of 2.5%

<u>Key Observations and Risks</u>

- Council's forecasts are impacted by flood restoration works and RMS projects until 2015. This period results in large fluctuations in many of Council's key revenue and expense lines in 2013 and 2014.
- Rates and annual charges are forecast to increase by 3.0% p.a.
- From 2014 onwards, user fees and charges are forecast to increase by 2.8% p.a.
- Grants and contributions for operating purposes are forecast to decline from $3.9m in 2012 to $3.4m in 2013 before increasing by an average of 3.1% p.a. from 2014 onwards.
- Employee expenses are forecast to increase by 3.2% p.a
- Materials and contract expenses fluctuate in the early years of the LTFP due to flood restoration works and grow by 14.5% ($0.8m) in 2014, with an average growth of 3.1% p.a thereafter.
- TCorp find the key assumptions underpinning the LTFP reasonable.
- The LTFP assumes current service levels are maintained.

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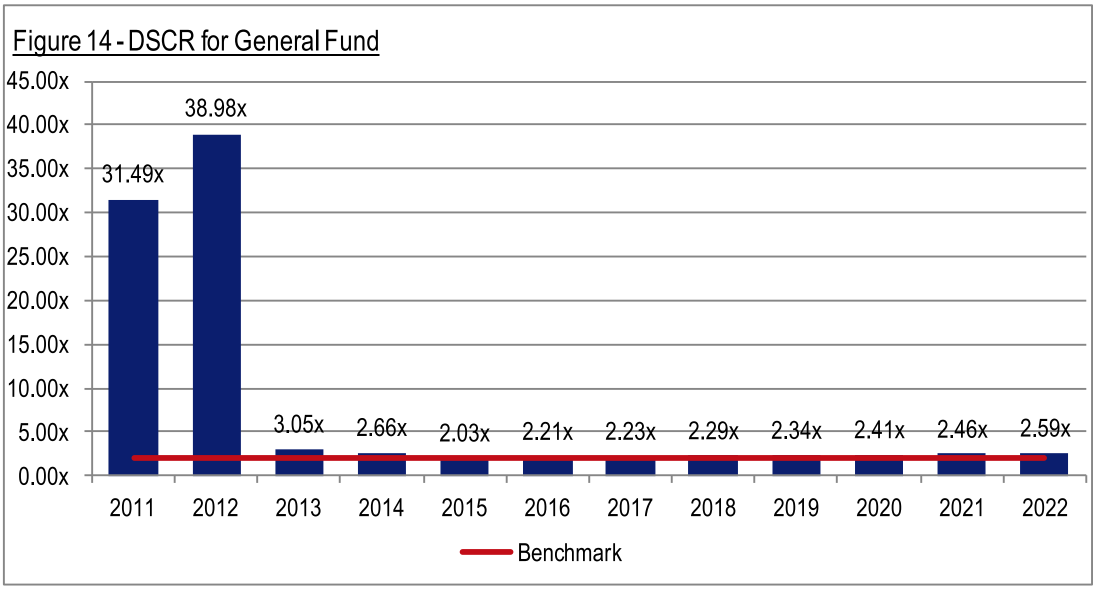
4.5: Borrowing Capacity

When analysing the financial capacity of the Council we believe Council would be able to incorporate loan funding if required. Some comments and observations are:



- Based on a benchmark of DSCR>2x, up to \$5.3m could be borrowed in addition to any existing borrowings
- This scenario has been calculated by basing borrowing capacity on a 10 year amortising loan at 7.5% p.a.

4.6 Sustainability

Despite the significant challenges Council faces being a large rural LGA with a low population density, Council management have run a fiscally responsible operation which at this time appears to support a Sustainable position in the long term.

In recent years Council adopted a new Asset Management system which better enables Council to plan and allocate its resources towards maintaining and improving its assets. Council's Asset Management Plan is reasonably well developed, however Council's forecast capital expenditure is below benchmark and, needs to be reviewed and linked to its LTFP.

Council has provided agreed levels of service with the residents while building up satisfactory cash reserves over the last number of years. The planned expenditure of these reserves over the next 10 years will enable sufficient capital expenditure to keep infrastructure assets in their current satisfactory condition.

Other areas where management have shown foresight for longer term Sustainability include:

- Keeping staff numbers and salaries and wages static
- Joint tendering with neighbouring Councils to increase efficiency
- Regional cooperation through shared services and organisations such as REROC
- Infrastructure management has been sound with Council having completed a program to replace all wooden bridges in the LGA with concrete bridges
- Council's Infrastructure Backlog has been consistently decreasing through restoration work

In considering the longer term financial Sustainability of the Council we consider Council to be in a sound position. We make the following additional comments:

- Council has built up cash reserves which could be used to fund its forecast capital expenditure program and reduce the Infrastructure Backlog
- Council's LTFP takes a conservative approach to forecasting its operating and capital grant revenue which may understate its forecast operating surpluses and capital expenditure program particularly after 2015
- The long term Sustainability of the Council is dependent on Council continuing to receive operating grants and contributions from both the State and Federal government to support its operations
- Council's forecast Capital Expenditure Ratio is below benchmark from 2016

Section 5 Benchmarking and Comparisons with Other Councils

Each council's performance has been assessed against ten key benchmark ratios. The benchmarking assessment has been conducted on a consolidated basis for councils operating more than one fund. This section of the report compares the Council's performance with its peers in the same DLG Group. The Council is in DLG Group 9. There are 21 councils in this group and at the time of preparing this report, we have data for all of these councils.

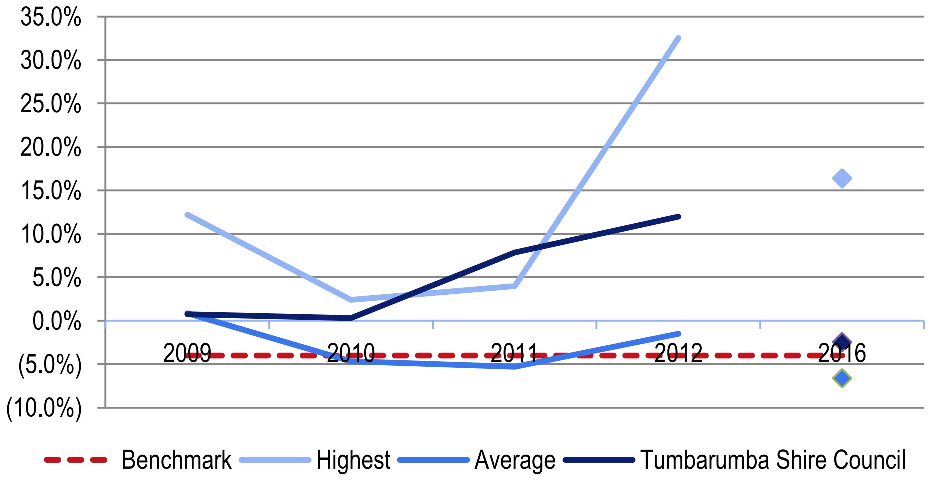
In Figure 15 to Figure 21, the graphs compare the historical performance of Council with the benchmark for that ratio, with the average for the Group, with the highest performance (or lowest performance in the case of the Infrastructure Backlog Ratio where a low ratio is an indicator of strong performance), 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. For the Interest Cover Ratio and Debt Service Cover Ratio, we have excluded from the calculations, councils with very high ratios which are a result of low debt levels that skew the ratios.

Please note that this section of the report has been prepared separately to the LIRS financial assessment and includes the latest information at the time of preparation which includes data from the 2012 financial year.

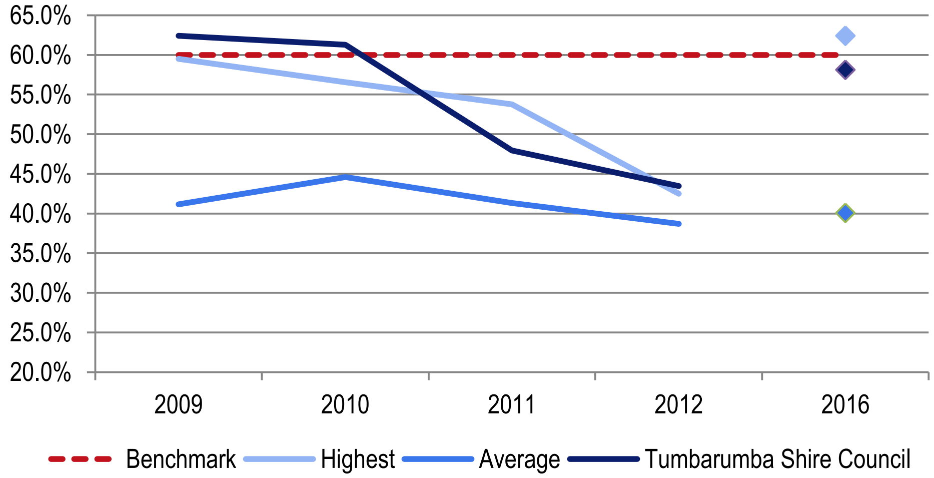
Financial Flexibility

Figure 15 - Operating Ratio Comparison



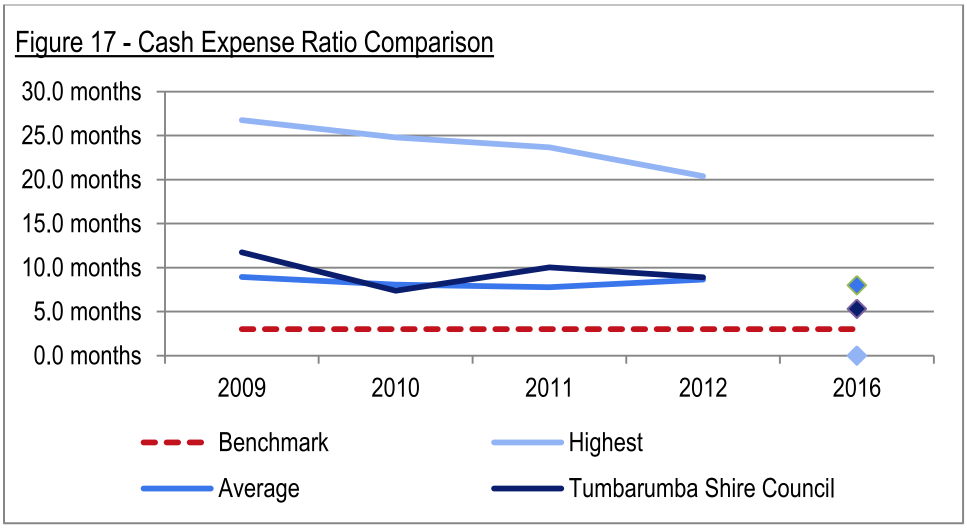
New South Wales Treasury Corporation

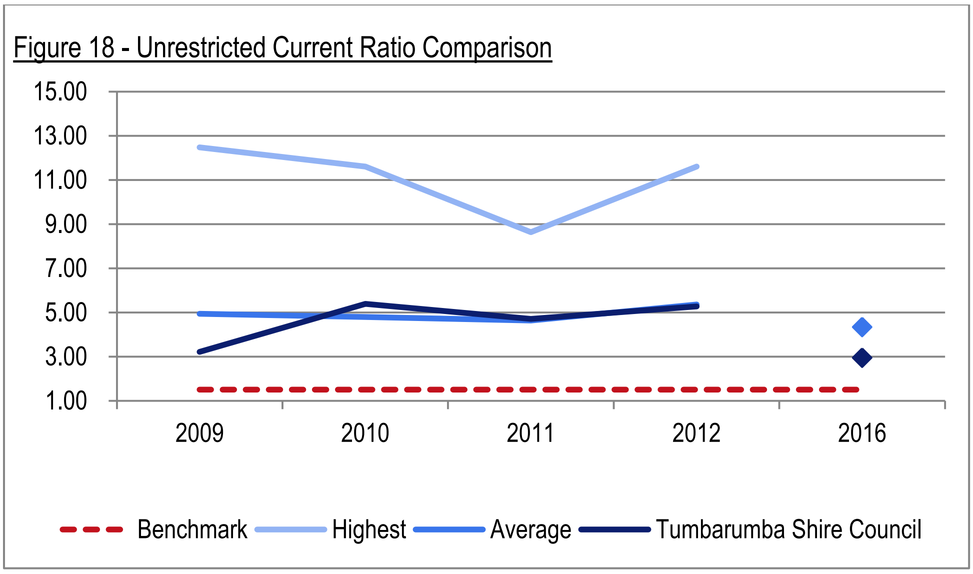
Figure 16 - Own Source Operating Revenue Ratio Comparison



Council's current Operating Ratio performance against benchmark and the group average is strong. The Council is forecast to have moderate flexibility in the medium term with the operating ratio forecast to fall but remain above average and the benchmark. This is mainly due to the current LTFP forecasting declining RMS fees. With grants also currently projected at lower levels in the medium term, the Council's own source operating ratio is set to increase in the medium term.

Liquidity





The Council's liquidity is strong with both the Cash Expense Ratio and the Unrestricted Current Ratio currently at or above benchmark and the group average, and is forecast to be above benchmark in 2016.

Debt Servicing

Figure 19 - Debt Service Cover Ratio Comparison

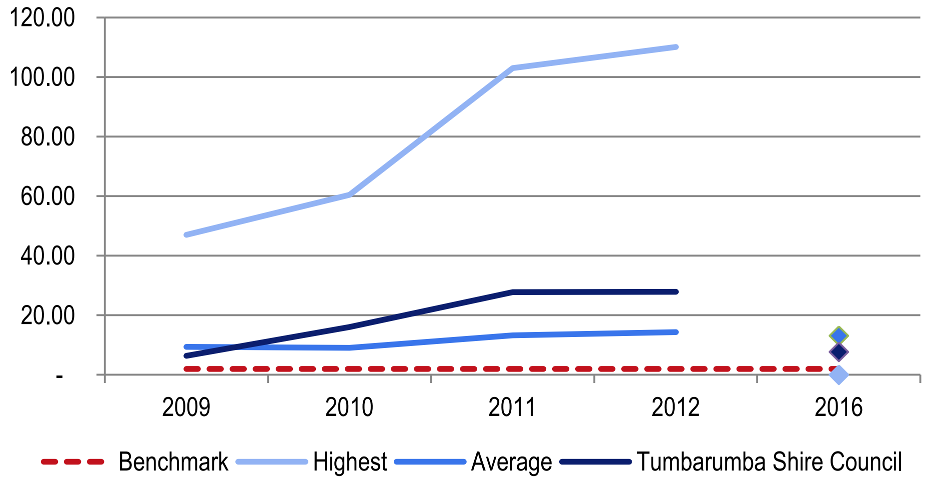
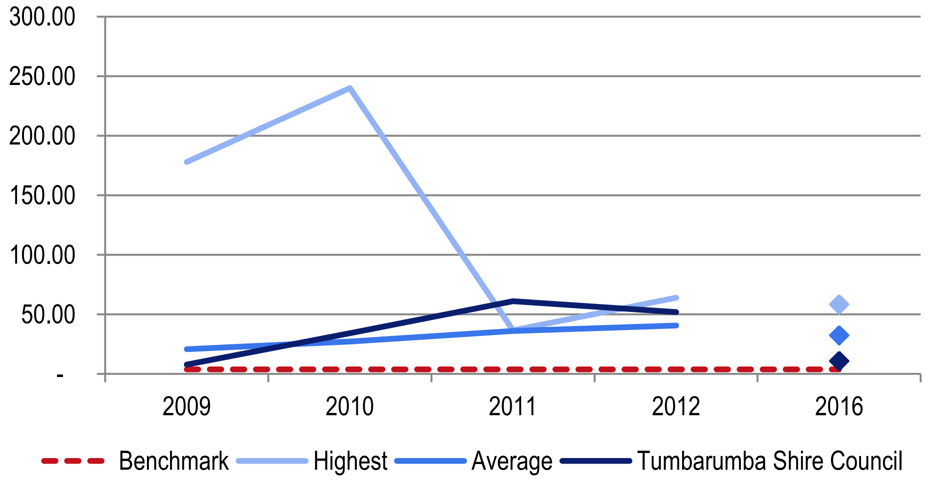


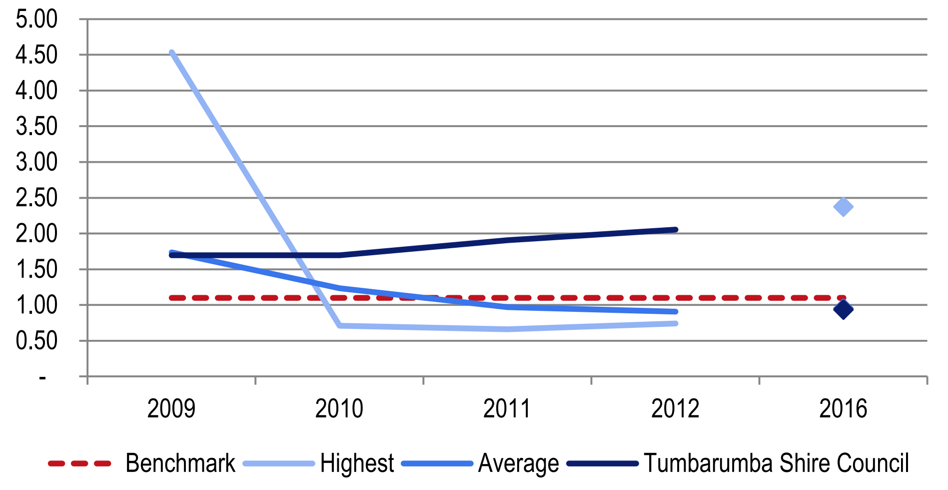
Figure 20 - Interest Cover Ratio Comparison



The Council has sound debt servicing capacity with both the DSCR and interest cover ratio remaining above benchmarks over the review period. The Council can support further debt financing if required.

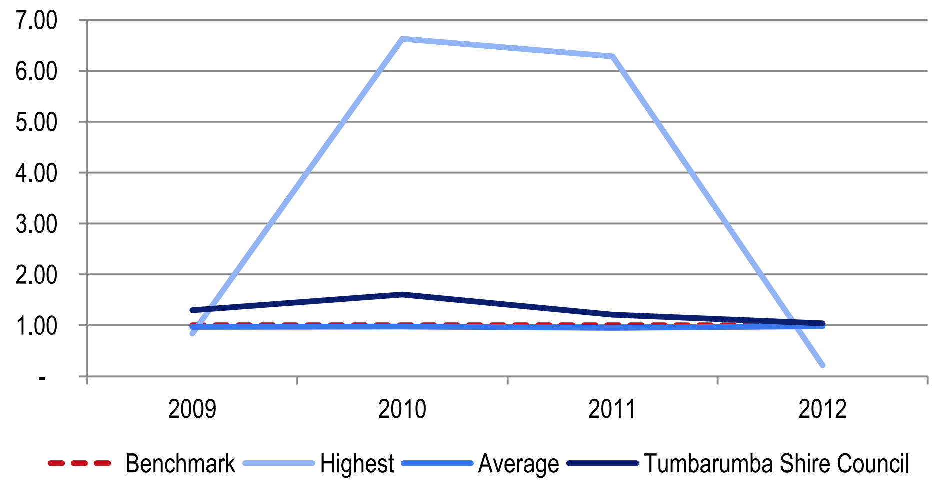
Asset Renewal and Capital Works

Figure 21 - Capital Expenditure Ratio Comparison



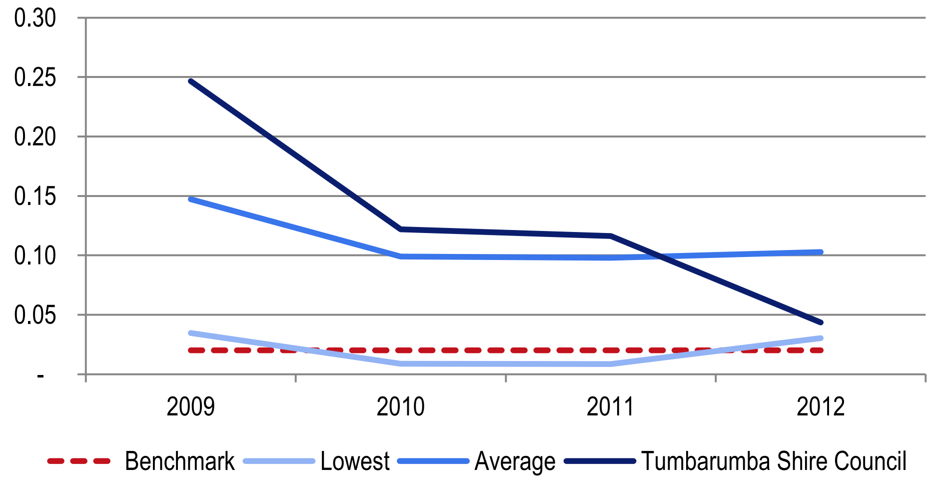
The Council has strong forecast capital expenditure at present with the Mannus Dam project but this is expected to fall just below benchmark by 2016. Since 2009 Council's performance in this area has been amongst the best in its Group.

Figure 22 - Asset Maintenance Ratio Comparison



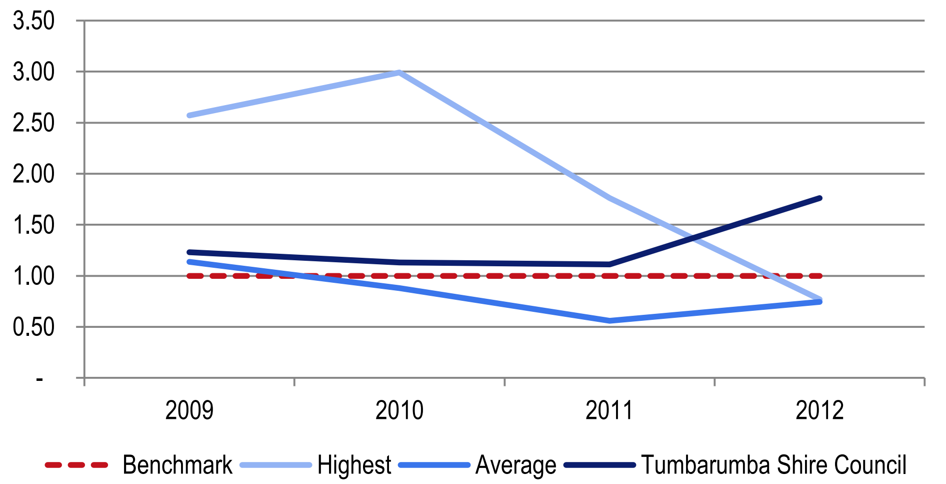
The Council's Asset Maintenance Ratio is consistent with both the benchmark and average.

Figure 23 - Infrastructure Backlog Ratio Comparison



The Infrastructure Backlog Ratio has fallen significantly and is below average but slightly above the benchmark in 2012. This has been assisted by the restoration work completed after flood events.

Figure 24 - Building and Infrastructure Asset Renewal Ratio



The Council's asset renewal is above average and benchmark which is mainly due to the restoration work completed after the floods.

Section 6 Conclusion and Recommendations

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

We base our recommendation on the following key points:

- Council reported operating surpluses each year over the review period and these are forecast to continue
- Salaries and wages have remained static
- Council has had very strong levels of liquidity throughout the period as indicated by its Unrestricted Current Ratio being well above the benchmark
- Council's cash reserves will better enable asset renewal in the long term
- Council has close to zero Infrastructure Backlog

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

- Council's forecast capital expenditure would not be sufficient to keep infrastructure assets in their current satisfactory condition and needs to be reviewed and linked in with Council's Asset Management Plan

New South Wales Treasury Corporation

Appendix A Historical Financial Information Tables

Table 1- Income Statement

Income Statement ($'000s)	Year ended 30 June				% annual change		
	2012	2011	2010	2009	2012	2011	2010
Revenue							
Rates and annual charges	3,437	3,285	3,073	2,958	4.6%	6.9%	3.9%
User charges and fees	7,491	5,926	4,861	5,329	26.4%	21.9%	(8.8%)
Interest and investment revenue	692	485	440	632	42.7%	10.2%	(30.4%)
Grants and contributions for operating purposes	9,867	5,620	3,185	3,257	75.6%	76.5%	(2.2%)
Other revenues	486	643	460	216	(24.4%)	39.8%	113.0%
Total revenue	**21,973**	**15,959**	**12,019**	**12,392**	**37.7%**	**32.8%**	**(3.0%)**
Expenses							
Employees	5,755	4,980	4,612	4,176	15.6%	8.0%	10.4%
Borrowing costs	112	69	70	353	62.3%	(1.4%)	(80.2%)
Materials and contract expenses	9,363	5,519	3,937	4,311	69.7%	40.2%	(8.7%)
Depreciation and amortisation	3,082	2,894	2,288	2,313	6.5%	26.5%	(1.1%)
Other expenses	1,031	1,242	1,076	1,149	(17.0%)	15.4%	(6.4%)
Total expenses	**19,343**	**14,704**	**11,983**	**12,302**	**31.5%**	**22.7%**	**(2.6%)**
Operating result (excluding capital grants and contributions)	**2,630**	**1,255**	**36**	**90**	109.6%	3386.1%	(60.0%)
Operating result (including capital grants and contributions)	**5,807**	**4,509**	**963**	**974**	28.8%	368.2%	(1.1%)

Table 2 - Items excluded from Income Statement

Excluded items	2012	2011	2010	2009
Grants and contributions for capital purposes	3,177	3,254	927	884
Net gain from the disposal of assets	0	232	219	247

New South Wales Treasury Corporation

Table 3 - Balance Sheet

Balance Sheet ($'000s)	Year Ended 30 June				% annual change		
	2012	2011	2010	2009	2012	2011	2010
Current assets							
Cash and cash equivalents	11,961	9,821	5,914	9,410	21.8%	66.1%	(37.2%)
Investments	0	689	0	0	(100.0%)	N/A	N/A
Receivables	4,357	4,015	3,903	2,166	8.5%	2.9%	80.2%
Inventories	493	272	361	494	81.3%	(24.7%)	(26.9%)
Other	29	39	19	37	(25.6%)	105.3%	(48.6%)
Total current assets	16,840	14,836	10,197	12,107	13.5%	45.5%	(15.8%)
Non-current assets							
Investments	0	0	575	319	N/A	(100.0%)	80.3%
Receivables	81	81	123	0	0.0%	(34.1%)	N/A
Inventories	0	0	0	0	N/A	N/A	N/A
Infrastructure, property, plant & equipment	146,223	136,303	133,842	96,164	7.3%	1.8%	39.2%
Investment property	0	0	431	504	N/A	(100.0%)	(14.5%)
Total non-current assets	146,304	136,384	134,971	96,987	7.3%	1.0%	39.2%
Total assets	**163,144**	**151,220**	**145,168**	**109,094**	**7.9%**	**4.2%**	**33.1%**
Current liabilities							
Payables	1,610	1,534	697	1,757	5.0%	120.1%	(60.3%)
Borrowings	108	102	78	80	5.9%	30.8%	(2.5%)
Provisions	1,312	1,220	1,179	1,206	7.5%	3.5%	(2.2%)
Total current liabilities	3,030	2,856	1,954	3,043	6.1%	46.2%	(35.8%)
Non-current liabilities							
Borrowings	1,504	1,607	764	841	(6.4%)	110.3%	(9.2%)
Provisions	253	211	263	296	19.9%	(19.8%)	(11.1%)
Total non-current liabilities	1,757	1,818	1,027	1,137	(3.4%)	77.0%	(9.7%)
Total liabilities	**4,787**	**4,674**	**2,981**	**4,180**	**2.4%**	**56.8%**	**(28.7%)**
Net assets	**158,357**	**146,546**	**142,187**	**104,914**	**8.1%**	**3.1%**	**35.5%**

Table 4-Cashflow

Cash Flow Statement ($'000s)	**Year ended 30 June**			
	2012	**2011**	**2010**	**2009**
Cash flows from operating activities	8,176	7,626	70	3,977
Cash flows from investing activities	(5,939)	(4,586)	(3,487)	(2,462)
Proceeds from borrowings and advances	0	950	0	0
Repayment of borrowings and advances	(97)	(83)	(79)	(76)
Cash flows from financing activities	(97)	867	(79)	(76)
Net increase/(decrease) in cash and equivalents	**2,140**	**3,907**	**(3,496)**	**1,439**
Cash and equivalents	11,961	9,821	5,914	9,410

Appendix B Glossary

Asset Revaluations

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

Collateralised Debt Obligation (CDO)

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

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

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

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

Division of Local Government (DLG)

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

Depreciation of Infrastructure Assets

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

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

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

EBITDA

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

Grants and Contributions for Capital Purposes

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

Grants and Contributions for Operating Purposes

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

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

Independent Commission Against Corruption (ICAC)

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

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

Independent Pricing and Regulatory Tribunal (IPART)

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

Infrastructure Backlog

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

Integrated Planning and Reporting (IP&R) Framework

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

Local Government Cost Index (LGCI)

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

Net Assets

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

Roads and Maritime Services (RMS)

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

Section 64 Contribution

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

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

Section 94 Contribution

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

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

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

Special Rate Variation (SRV)

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

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

The applications are reviewed and approved by IPART.

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.