New South Wales
Treasury Corporation

Blacktown City Council

Financial Assessment, Sustainability and Benchmarking Report

26 April 2013

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

New South Wales
Treasury Corporation

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 Blacktown City Council, the DLG and the Independent Local Government Review Panel. TCorp shall not be liable to Blacktown City 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.

New South Wales
Treasury Corporation

Index

Section 1 Executive Summary

This report provides an independent assessment of Blacktown City 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 although 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:

- Total revenue, excluding capital grants and contributions, increased by 19.1% over the four year period to $238.0m in 2012
- EBITDA has grown by $13.4m since 2009, with a 27.5% ($10.4m) increase recorded in 2012 following positive growth in rates and annual charges alongside operating grants and contributions

The Council reported $52.6m of Infrastructure Backlog in 2012 which represents 3.1% of its infrastructure asset value of $1,700.9m. Other observations include:

- Infrastructure Backlog in 2012 was 87.4% ($46.0m) related to public roads (including footpaths and car parks)
- The Backlog has declined by 55.0% since 2009 as Council continued to develop the methodologies used in their AMP
- The Capital Expenditure Ratio has been significantly above benchmark in each of the past four years
- Based on the Infrastructure Backlog Ratio, Asset Maintenance Ratio, and Building and Infrastructure Asset Renewal Ratio, Council has not been spending sufficiently on asset maintenance and renewal

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

- The Operating Ratio is forecast to improve towards benchmark levels by 2021 due to growth in newly rateable properties
- Council forecasts to have current cash reserves of less than one month's cash expenses during the LTFP. This does not take into account Council's level of investments, and Council project growth in these assets from $268.2m in 2012 to $513.1m by 2022
- Council has no debt and do not project any debt being taken over the period of the LTFP, therefore DSCR and Interest Cover Ratios are not relevant forecasts in this review

In our view, the Council has the capacity to undertake additional borrowings of up to $125.0m if required. This is based on a 10 year amortising loan at an interest rate of 7.50% p.a.

We consider Council to be moderately Sustainable in the medium term. In respect of the long term Sustainability of the Council, our key observations are:

- Council's historical financial position has been satisfactory
- Council's current LTFP shows improving operating results, and sound liquidity
- Council demonstrated that it has begun integrating the cost of implementing the AMP with its LTFP. Further refinements to asset valuation techniques and the AMP will continue to improve its LTFP
- The LTFP does not include sufficient levels of planned capital expenditure to maintain existing assets at an acceptable standard, or allowance for growth. This potential shortfall is one of the key risks facing the Council's long term Sustainability

In respect of our Benchmarking analysis we have compared the Council's key ratios with other councils in DLG Group 3. Our key observations are:

- Council's financial flexibility as indicated by the Operating Ratio and Own Source Operating Revenue Ratio was below peer group.
- Council's liquidity position was mixed, with above average Unrestricted Current Ratio but below average Cash Expense Ratio due to the investment of funds in longer dated deposits.
- Council has operated debt free over the past four years. On average, councils from the group used borrowing and had a sound debt servicing capacity.
- In the last three years, Council has generally outperformed the peer group in terms of level of Infrastructure Backlog, maintenance of assets and capital expenditure. Council's performance in terms of renewal of assets was weak compared to the benchmark and the group average.

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 their internal due diligence, and 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
- Asset Management Plan (AMP)
- Council's IP&R documents
- Discussions with Council officers
- Other publicly available information such as information published on the IPART website

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

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

Definition of Sustainability

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

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

Benchmark Ratios

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

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

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

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

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

2.3: Overview of the Local Government Area

Blacktown City Council	
Locality and Size	
Locality	Sydney Western Suburbs
Area	240.1km²
DLG Group No.	3
Demographics	
Population	301,099
% under 20	30.9%
% between 20 and 59	55.6%
% over 60	13.5%
Expected population in 2021	366,600
Operations	
Number of employees (FTE)	1,336
Annual revenue	$238.0m
Infrastructure	
Roads	1,173km
Bridges	104
Infrastructure backlog value	$52.6m
Total infrastructure value	$1,700.9m

Blacktown is the most populous Local Government Area in NSW with its population comprising 15.0% of Western Sydney's total population.

Access into and out of Blacktown is provided by transport links including the Western railway line between Sydney, Penrith and Richmond; the Great Western Highway, Richmond Road; plus the M2, M4, and M7 Motorways.

With regard to industry, the largest contribution is made by the manufacturing industry, with approximately $2.0b, or 18.0% of the total Gross Regional Product of Blacktown City. Other significant contributors to Gross Regional Product were the Wholesale Trade (9.3%), Transport, Postal & Warehousing (7.8%), Education & Training (5.7%) and Financial & Insurance Services (5.4%) sectors.

Blacktown City was one of only seven cities within Australia given funding under the Australian Government's $94m Solar Cities initiative, the Blacktown Solar City consortium worked with industry, businesses and the local community to rethink the way they produce and use energy. The Blacktown Solar City project hit its final year in 2012 and was deemed a success by households, business and local government.

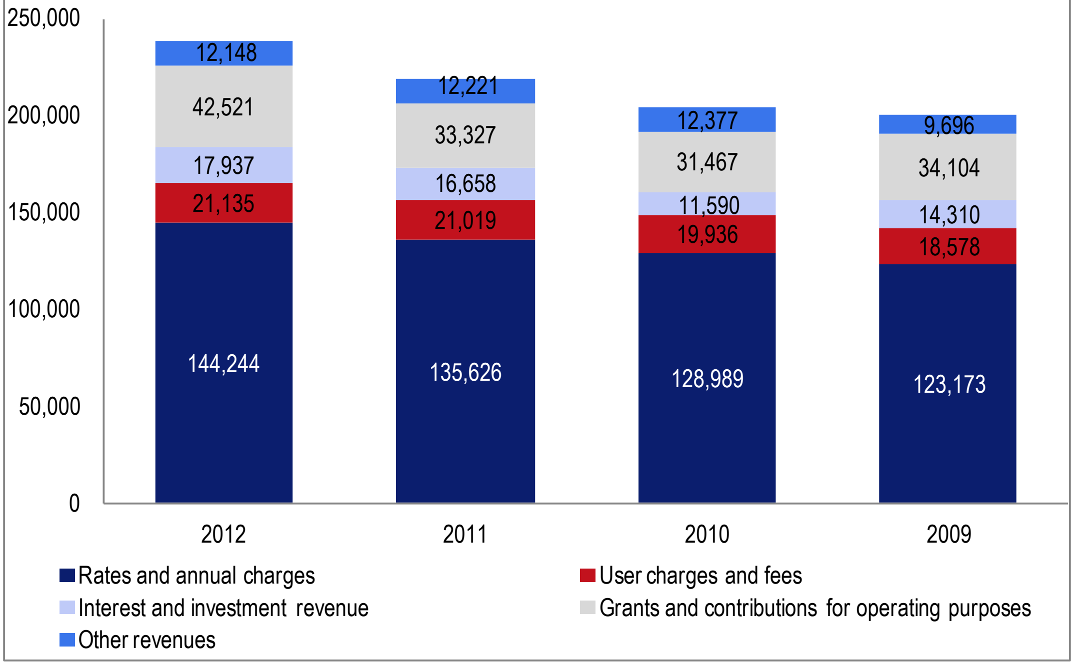
New South Wales
Treasury Corporation

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)

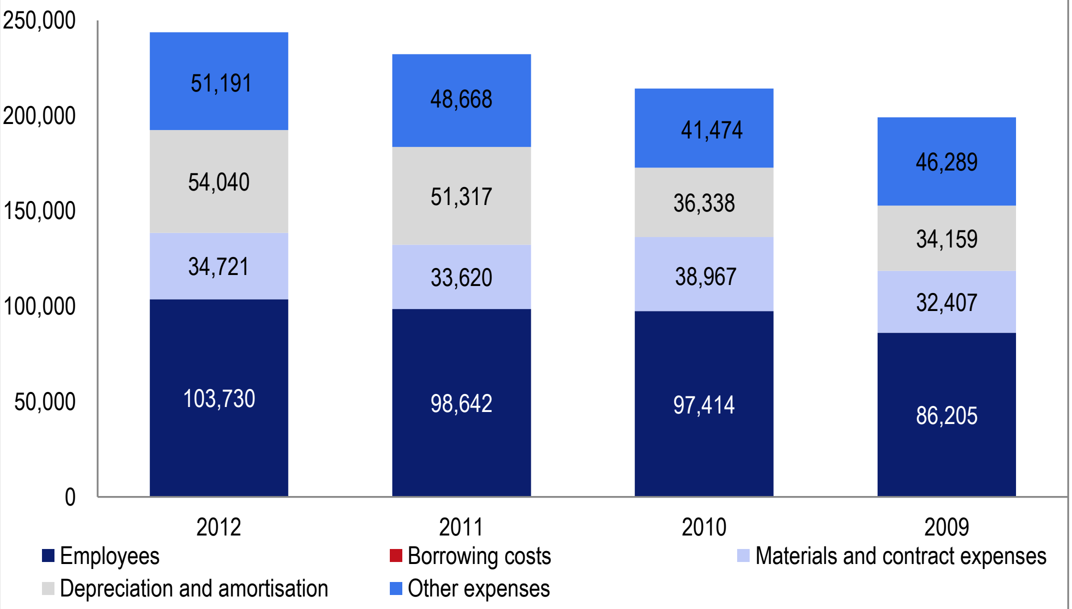


Key Observations

- Total revenue, excluding capital grants and contributions, increased by 19.1% over the four year period to $237.9m in 2012.
- Rates and annual charges have increased by 17.1% ($21.1m) since 2009. On a compounded annual basis, average growth has been 5.4% p.a. Revenue growth above the standard rate peg is consistent with population growth in the area. In 2012, rates and annual charges increased by 6.4% ($8.6m) driven by a 16.3% ($4.0m) increase in domestic waste management service charges following government levy increases.
- User fees and charges have grown over the four year period with an overall increase of 13.8% ($2.6m) since 2009. On a compounded annual basis, average growth has been 4.6% p.a. The largest contributors in 2012 were child care and pre-school fees of $6.5m and swimming pool fees of $4.4m.
- Grants and contributions increased by 27.6% ($9.2m) in 2012 primarily due to the Federal Government bringing forward one-half of the 2013 Financial Assistance Grant allocation to all NSW Councils.
- Other revenues have marginally declined since 2010, with main components such as rental income, fines, and recreation and leisure all static year on year.

3.2: Expenses

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



Key Observations

- Council's total expenses increased by 22.4% ($44.6m) from 2009 to $243.7m in 2012. On a compounded annual basis, growth was 7.0% p.a.
- FTEs increased from 1,318 in 2009 to 1,336 in 2012. On a per employee basis, total employee costs increased by 5.8% on a compounded annual basis since 2009. This reflects the general growth in wage levels and in particular employee leave entitlements, which increased by an average of 7.7% p.a. ($3.5m) over the review period.
- Borrowing costs have been zero since 2009 as Council currently has a no debt policy.
- Materials and contracts expenses increased by 2.3% on a compound annual basis to 2012 as Council has maintained expenditure on materials and consumables and contractor costs to static levels year on year.
- A revision of the AMP in 2011, in particular the remaining useful lives of infrastructure assets, resulted in the annual depreciation charge increasing by $15.0m to $51.3m in that year alone.
- Other expenses have grown by 3.4% p.a. on a compounded annual basis, from $46.3m in 2009 to $51.2 m in 2012. Growth has been driven by rising tipping fees, which have increased by $10.1m to $20.2m in 2012.

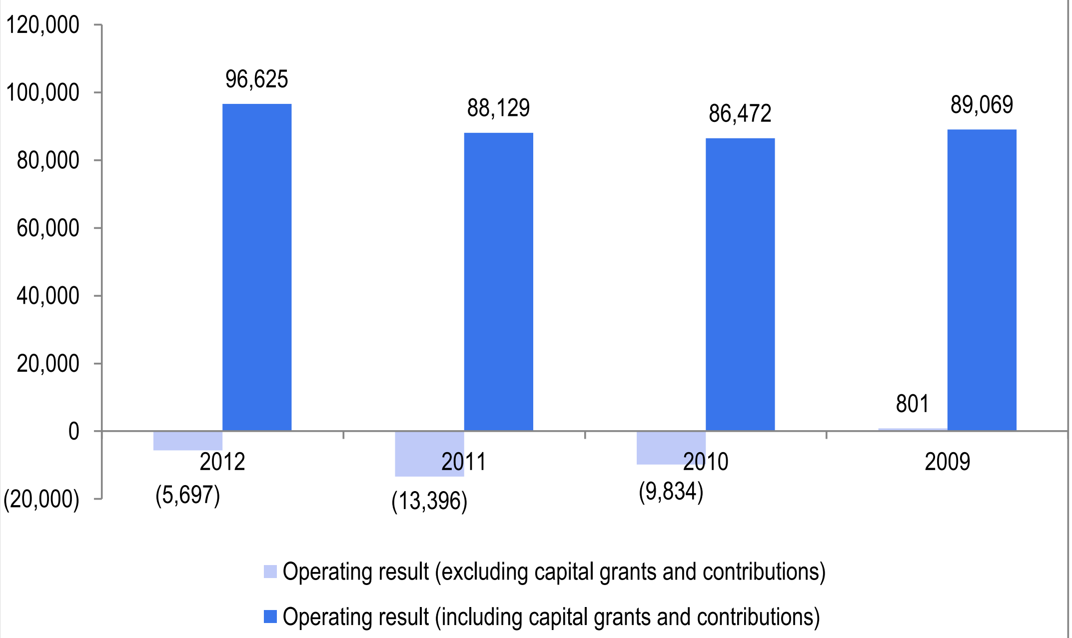
3.3: Operating Results

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 has no control over (e.g. impairments).

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

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

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



Key Observations

- Council has recorded operating deficits (excluding capital grants and contributions) in the last three years.
- Council expenses include a non-cash depreciation expense, ($54.0m in 2012), which has increased by $19.9m since 2009 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 ($'000s)	48,343	37,921	26,504	34,960
Operating Ratio	(2.4%)	(6.1%)	(4.8%)	0.4%
Interest Cover Ratio	N/A	N/A	N/A	N/A
Debt Service Cover Ratio	N/A	N/A	N/A	N/A
Unrestricted Current Ratio	4.26x	5.23x	4.77x	5.21x
Own sourced revenue	48.6%	48.9%	49.5%	49.2%
Cash expense ratio	1.0 months	0.9 months	4.4 months	2.2 months
Net assets ($'000s)	2,702,901	2,607,973	2,753,351	2,560,679

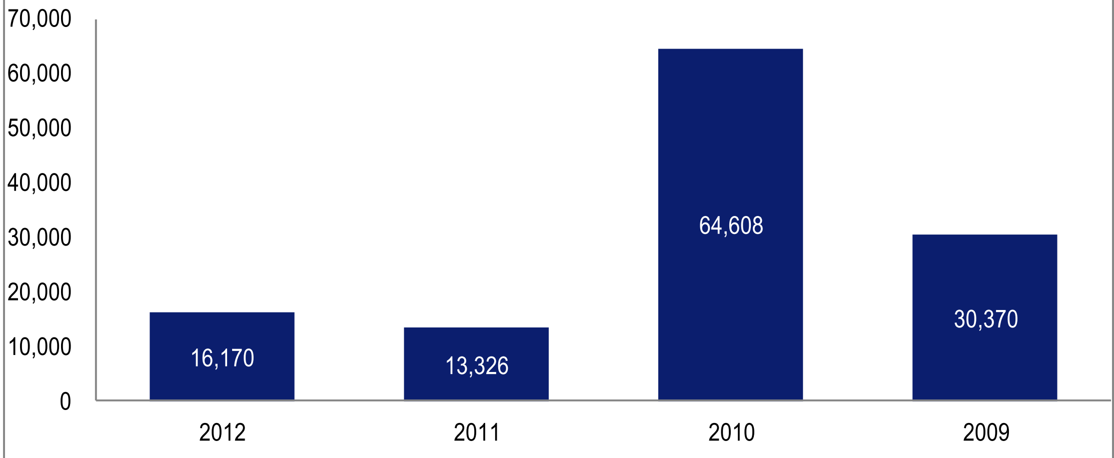
Key Observations

- EBITDA has grown by $13.4m since 2009, and a 27.5% ($10.4m) increase was recorded in 2012 following growth in revenues, particularly in domestic waste management charges and operating grants.
- The Operating Ratio declined to a deficit in 2010 mainly due to the increased employee costs in this year and then increased depreciation charges in 2011, however has improved above benchmark in 2012.
- The Unrestricted Current Ratio has been well above the benchmark of 1.50x over the review period, indicating Council has strong liquidity.
- The Own Sourced Operating Revenue Ratio has been below benchmark in each of the last 4 years. Capital Contributions have been higher than usual for Council, as development of lands has resulted in increased developer contributions. When these are excluded, the Own Sourced Operating Revenue Ratio is above benchmark.
- When the Asset Revaluations are excluded, the underlying trend in recent years has been a substantial increase in the infrastructure, property, plant, and equipment (IPP&E) asset base with asset purchases being greater than the combined value of disposed assets and annual depreciation. Over the review period the Infrastructure, Property, Plant and Equipment (IPP&E) asset base has increased, with asset purchases being $335.1m greater than the combined value of disposed assets and annual depreciation. It should be noted that over this period, Council reported a total of $148.7m in land under roads asset additions, which are treated as an IPP&E asset additions for accounting purposes.
- Council has no outstanding borrowings.

3.5: Statement of Cashflows

Key Observations

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



- Council's cash and cash equivalents decreased in 2011 following the transfer from cash of $51.3m to investment securities.
- In total, Council has cash and investments of $284.4m in 2012 of which $142.3m is externally restricted, $121.5m is internally restricted and $20.6m is unrestricted.
- Council had no exposures to CDO, linked notes or FRNs. Council's investment portfolio suffered no capital losses in recent years.
- Overall the cash balances along with the Unrestricted Current Ratio indicate that Council had sufficient resources to meet their day to day obligations.

3.6: Capital Expenditure

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

3.6(a): Infrastructure Backlog

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

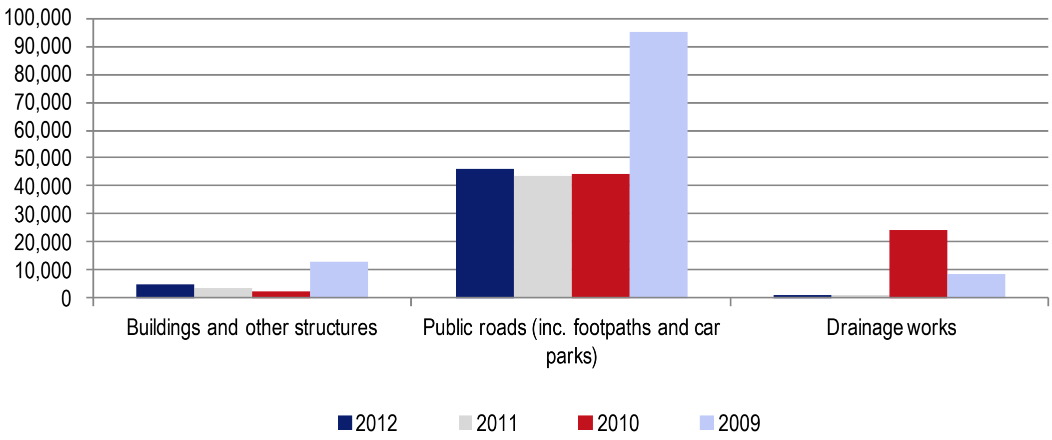
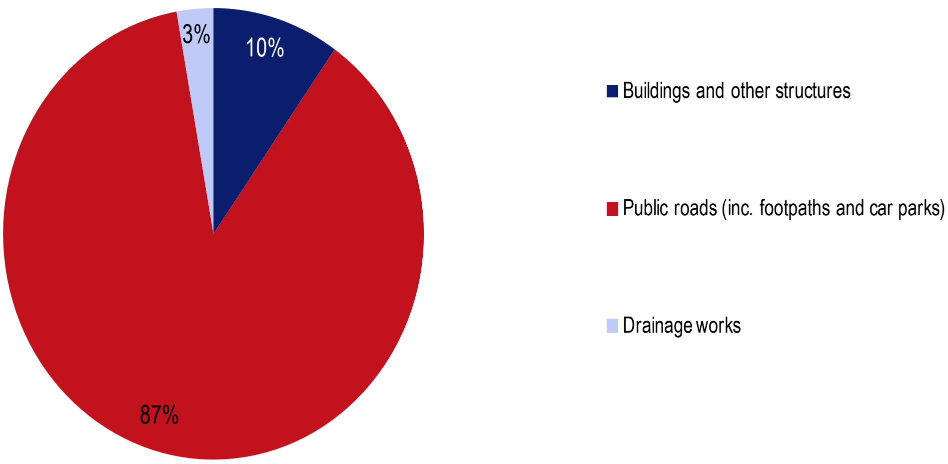


Figure 6 - Infrastructure Backlog Composition for 2011/12



Council reported a $52.6m Infrastructure Backlog in 2012, of which 87.4% ($46.0m) related to public roads (inc. footpaths and car parks). The backlog has declined by 55.0% since 2009 as Council continue to develop the methodologies used in their AMP

3.6(b): Infrastructure Status

Infrastructure Status	Year ended 30 June			
	2012	2011	2010	2009
Bring to satisfactory standard ($'000s)	52,625	48,755	70,689	116,865
Required annual maintenance ($'000s)	31,199	29,779	38,362	52,875
Actual annual maintenance ($'000s)	28,485	26,683	28,591	31,851
Total value infrastructure assets ($'000s)	1,700,942	1,679,964	1,617,993	672,545
Total assets ($'000s)	2,791,226	2,681,220	2,819,914	2,619,900
Infrastructure Backlog Ratio	0.03x	0.03x	0.04x	0.17x
Asset Maintenance Ratio	0.91x	0.90x	0.75x	0.60x
Building and Infrastructure Asset Renewal Ratio	0.34x	0.33x	0.38x	0.48x
Capital Expenditure Ratio	2.71x	2.44x	3.05x	3.84x

The Infrastructure Backlog Ratio has been decreasing, and the Asset Maintenance Ratio has been on an upward trend but neither has met their respective benchmarks over the review period. This indicates that Council has not been spending enough on asset maintenance.

Council's Building and Infrastructure Renewals Ratio has also been consistently below the benchmark of 1.0x which indicates Council is spending at levels below the required amount on asset renewal.

The Capital Expenditure Ratio, which takes into account assets which improve performance or capacity, has been above benchmark in each of the past four years. This is reflective of the growing developer investments for capital works but it should be noted that a significant proportion of this capital expenditure is largely attributable to significant land under roads asset additions during the review period. Land under road additions have occurred annually and ranged from $37.2m in 2009 to $45.3m in 2012. Excluding land under road additions, the Capital Expenditure Ratio would be 1.87x in 2012.

3.6(c): Capital Program

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

Capital Program ($'000s)	Year ended 30 June			
	2012	2011	2010	2009
New capital works	21,485	26,000	27,000	36,000
Replacement/refurbishment of existing assets	21,485	18,000	18,000	18,000
Total	**42,970**	**44,000**	**45,000**	**54,000**

The capital works in 2012 included:

Drainage	$3.2m
Reseal	$3.6m
Regional Roads	$1.7m
Failed Pavements	$3.2m
Road works	$2.6m
Roads to Recovery Program	$2.0m
Traffic Facilities	$0.7m
CBD / Commercial Centres Embellishment Works	$1.2m
Path Paving & Minor Works	$0.5m
Parks Construction	$2.1m
Major Parks and Reserves Improvements	$8.2m
Buildings Construction	$10.6m
Playground Equipment	$0.8m
Field Lighting	$0.1m
Other	$2.6m
Total	**$43.1m**

3.7: Specific Risks to Council

- Land acquisition for new development areas. Council is required to acquire land for the future development of subdivisions in the LGA. Council is exposed to the cost of these acquisitions until such a time as a property developer acquires the land from Council. The risk that Council will be left holding these assets for longer than anticipated is mitigated by the projected population growth and dwelling increases in the LGA.
- Changes in developer contributions policy. This is a particularly relevant issue for Council because of a number of expected new developments. During 2010, the NSW Government made a number of amendments to the framework for contributions plans, imposing caps on the amount that councils can levy developers. The cap is $20,000 for established areas and $30,000 for 'greenfield' areas. This could result in Council bearing increasing costs for development works in the future.
- The LTFP does not forecast sufficient planned capital expenditure to maintain existing assets at an acceptable standard, or allowance for growth. This potential shortfall is one of the key risks facing the Council's long term Sustainability.

New South Wales
Treasury Corporation

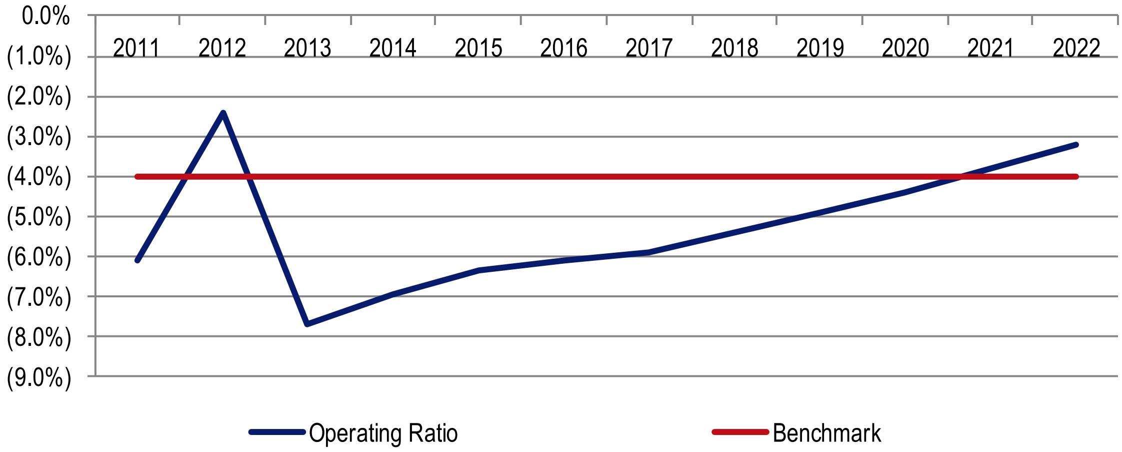
Section 4 Review of Financial Forecasts

The financial forecast model shows the projected financial statements and assumptions for the next 10 years.

Council only operate a General Fund. The 'Base Case' scenario within Council's LTFP has been analysed. Council's LTFP includes six different scenarios including a Base, Optimistic, Pessimistic and Balanced Case along with a variation of the Base Case and a variation of the Balanced Case.

4.1: Operating Results

Figure 7 - Operating Ratio for General Fund

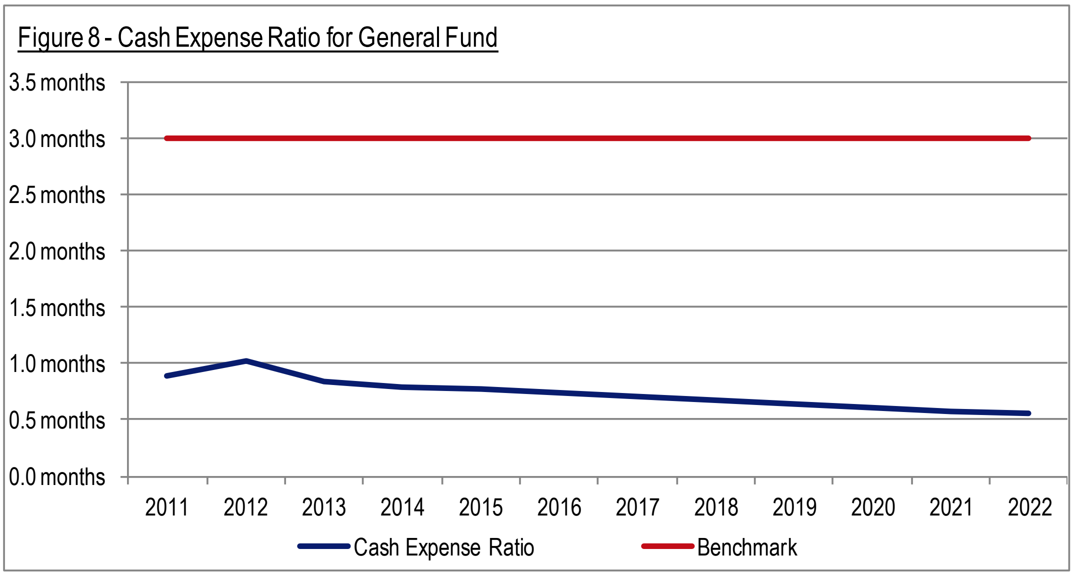


Operating Ratio is forecast to fall below benchmark in 2013 as Council forecasts operating grants and contributions to decrease by 36.0% ($15.3m), other revenues by 46.7% ($5.7m) and interest revenues by 35.3% ($6.4m). This is off-set to an extent by a forecast 40.5% ($8.6m) increase in user charges and fees. Council completed their LTFP in 2011, and based their assumptions on the results from that year, which were lower than actual results in 2012.

The Operating Ratio is then forecast to improve towards benchmark by 2021 due to growth in newly rateable properties, which has had a positive impact on the projected rates and domestic waste revenues.

4.2: Financial Management Indicators

Liquidity Ratios

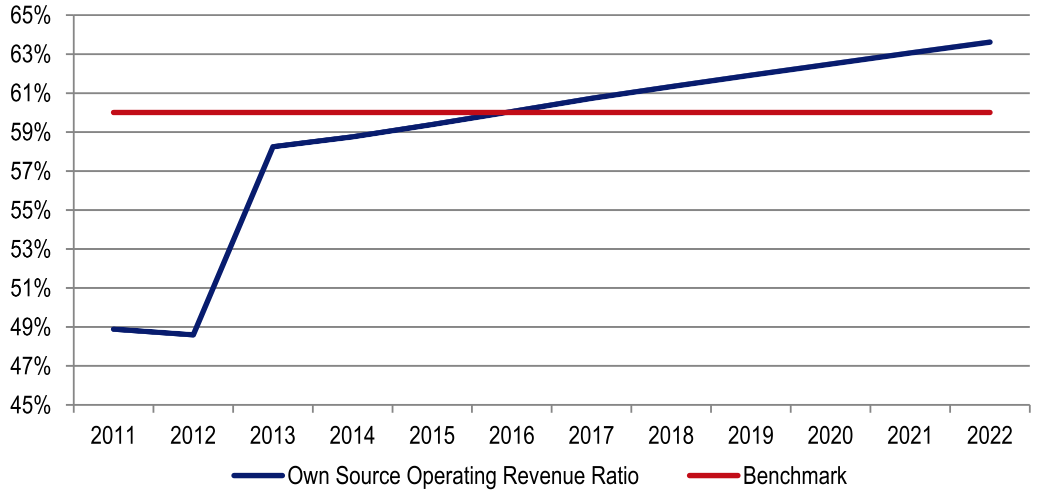


The decline in the Cash Expense Ratio over the life of the forecast is driven by a flat cash balance forecast.

The graph indicates that Council expects to have cash reserves of less than month's cash expenses during LTFP. The ratio does not take into account Council's level of investments, and Council projects growth in these assets from $250.6m in investment assets in 2013 to $523.6m by 2022.

Fiscal Flexibility Ratios

Figure 10 - Own Source Operating Revenue Ratio for General Fund

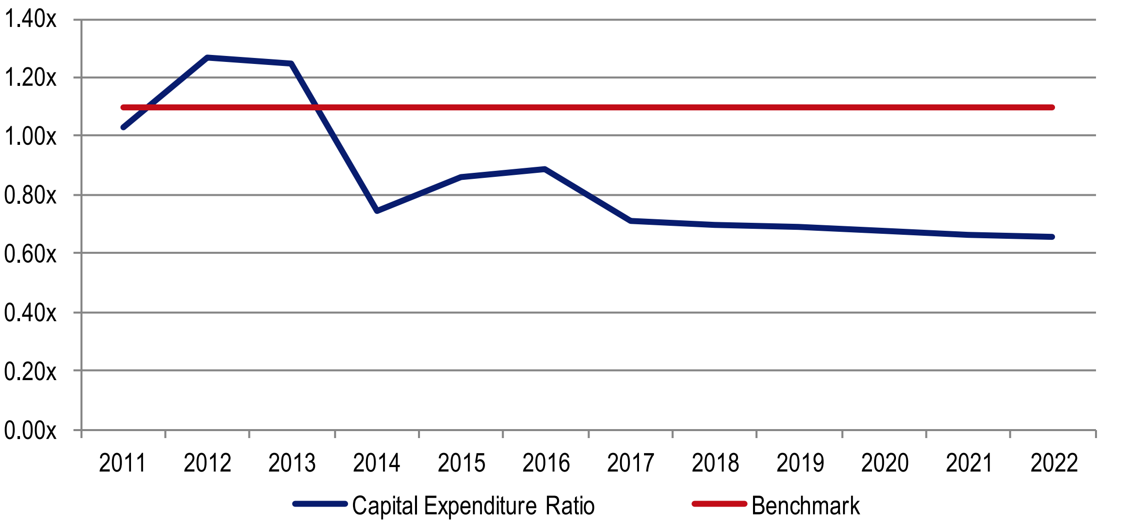


Own Sourced Operating Revenue is forecast to rise from 49.0% in 2012 to 58.0% in 2013, primarily due to capital grants and contributions falling from $102.3m in 2012 to $88.5m in 2013 as Council forecast fewer section 94 contributions from developers. The ratio improves over the forecast period as rates and annual charges are forecast to increase at a faster rate than all of the other revenue categories.

Council currently have no debt and do not project any debt being taken over the LTFP, therefore DSCR and Interest Cover Ratios are not relevant in this case.

4.3: Capital Expenditure

Figure 13 - Capital Expenditure Ratio for General Fund



The Capital Expenditure Ratio is below benchmark from 2013 and on a downward trend. Recent AMP amendments resulted in depreciation increasing by 41.2% in 2011, which has impacted capital expenditure requirements significantly.

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:

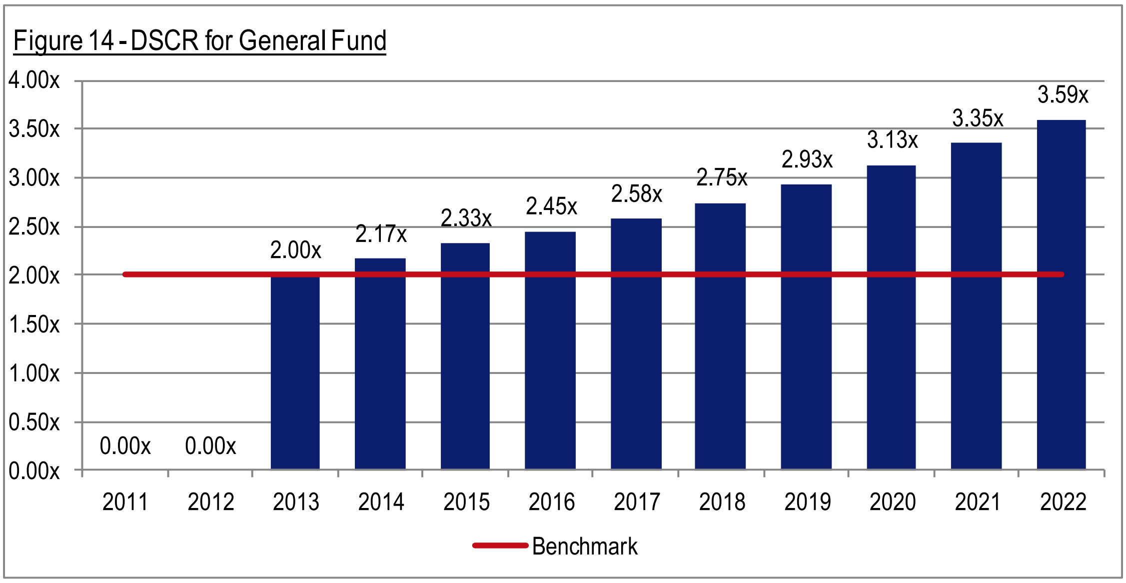
- Rates and annual charges: TCorp notes that the LGCI increased by 3.4% in the year to September 2011, and in December 2011, IPART announced that the rate peg to apply in the 2012/13 financial year will be 3.6%. Beyond 2013 TCorp has assessed a general benchmark for rates and annual charges to increase 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>

- Rates and annual charges are forecast to grow by 5.0% p.a. for the LTFP. This is above the rate peg due to Blacktown's expected population growth over the coming years that add 0.75% p.a. to the forecast 3.0% p.a. increase for the rate peg while there is also a 10.0% p.a. increase in waste related charges factored in.
- Interest received is forecast to grow at an average rate of 9.0% p.a. over the LTFP as Council keep cash at a constant level and putting growing reserves in investments.
- Employee costs are forecast to grow at a rate of 4.0% p.a. for the life of the forecast.
- Materials and contracts expenses are forecast to grow at a rate of 5.0% p.a. due to private works.
- Other expenses are forecast to grow at a rate of 6.0% p.a. as Council factors rising electricity costs into the forecasts.
- Overall the assumptions that underpin the financial forecasts are considered to be reasonable although capital expenditure forecasts are below benchmark levels and will need to be reviewed in order to reflect updated versions of the AMP and maintain asset quality.

4.5: Borrowing Capacity

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



- Based on a benchmark of DSCR>2x, up to $125.0m could be borrowed. At these levels, Council could eliminate its Infrastructure Backlog very quickly if this was a priority
- This scenario has been calculated by basing borrowing capacity on a 10 year amortising loan at an interest rate of 7.50% p.a.

4.6 Sustainability

Based on historical performance and LTFP forecasts, Council is in a moderately Sustainable position.

Operations

In terms of operational performance, Council has shown positive signs of operational Sustainability, with EBITDA trends and Operating Ratios at acceptable levels.

Council provides for over 301,099 residents with 366,660 expected by 2021. This 21.8% forecast rise in population will have an impact on Council's infrastructure and could result in pressure on the existing Infrastructure Backlog.

Environment

In addition to operational and financial Sustainability, community focus is shifting towards environmental sustainability. Blacktown was one of seven Australian cities (including Adelaide, Perth and Alice Springs) chosen to become a Solar city.

Households reduced energy consumption with 15,000 Energy Efficient Packs distributed, over 3,500 home energy audits conducted and 139 contracts signed for residential ceiling insulation. There are also 417kW of solar generated through residential PV installations.

In local business, 100 kilowatt solar electricity system was installed at the Cadbury Schweppes facility and 110kW installed at Coca Cola Amatil facility, a 28.8 kW at Mount Druitt Community Hub and the most recent addition in commercial PV was the 50 kilowatt installed at Veolia Environmental Services.

Financial

We consider Council to be moderately Sustainable in the medium term. In considering the longer term financial Sustainability of the Council we make the following comments:

- Council's historical financial position has been satisfactory
- Council's current LTFP shows improving operating results, and sound liquidity
- Council demonstrated that it has begun integrating the cost of implementing the AMP with its LTFP. Further refinements to asset valuation techniques and the AMP will continue to improve its LTFP

The following concerns should be considered:

- Council needs to address their underspending on assets as shown by their Infrastructure Backlog Ratio, Asset Maintenance Ratio and Building and Infrastructure Asset Renewal Ratio to improve their Sustainability
- The LTFP has insufficient planned Capital Expenditure to maintain existing assets at an acceptable standard plus any allowance for growth. This potential shortfall is a key risk facing the Council's long term Sustainability

Section 5 Benchmarking and Comparisons with Other Councils

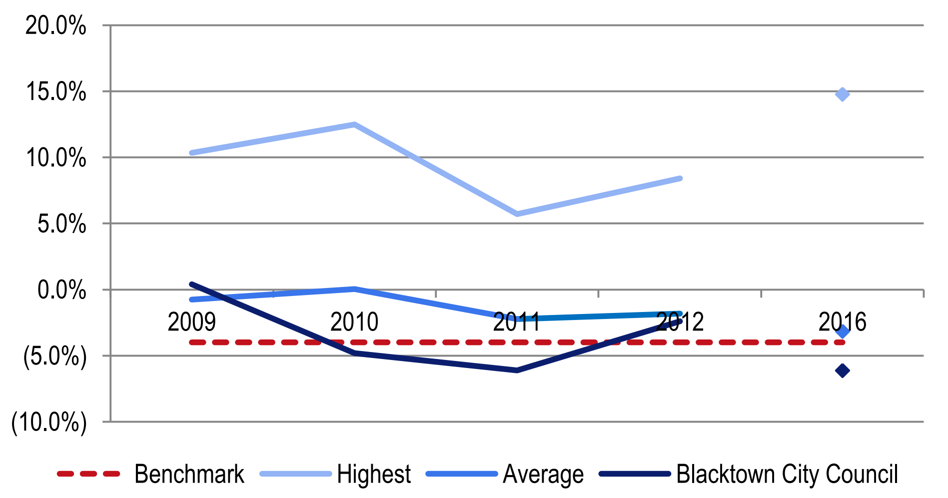
Each council's performance has been assessed against ten key benchmark ratios. The benchmarking assessment has been conducted on a consolidated basis for councils operating more than one fund. This section of the report compares the Council's performance with its peers in the same DLG Group. The Council is in DLG Group 3. There are 17 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 24, 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.

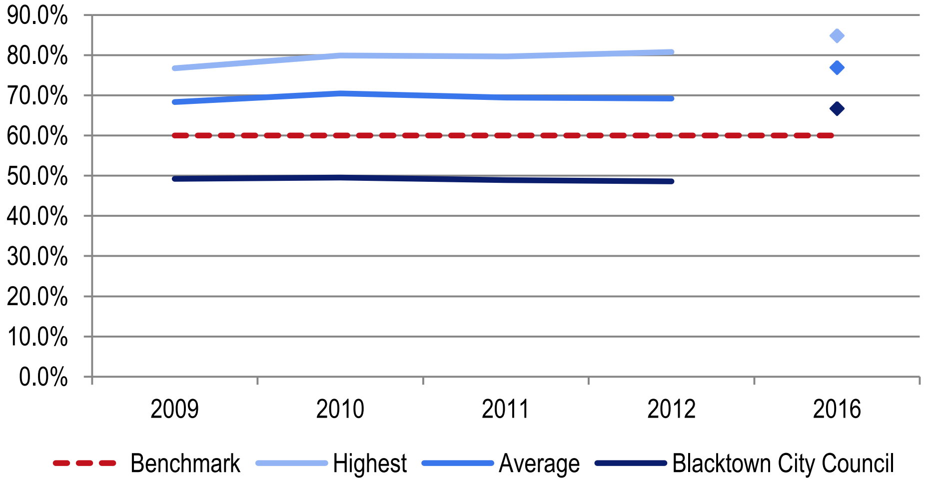
Financial Flexibility

Figure 15 - Operating Ratio Comparison



Council's Operating Ratio outperformed the benchmark in two of the past four years and was below the group average in three of the past four years. Over the medium term, Council's ratio is forecast to decline and be below the benchmark and the peer group.

Figure 16 - Own Source Operating Revenue Ratio Comparison



Council's Own Source Operating Revenue Ratio was consistently below the group average and the benchmark over the review period. Over the medium term, Council's ratio is forecast to improve and be above the benchmark but below the peer group.

Liquidity

Figure 17 - Cash Expense Ratio Comparison

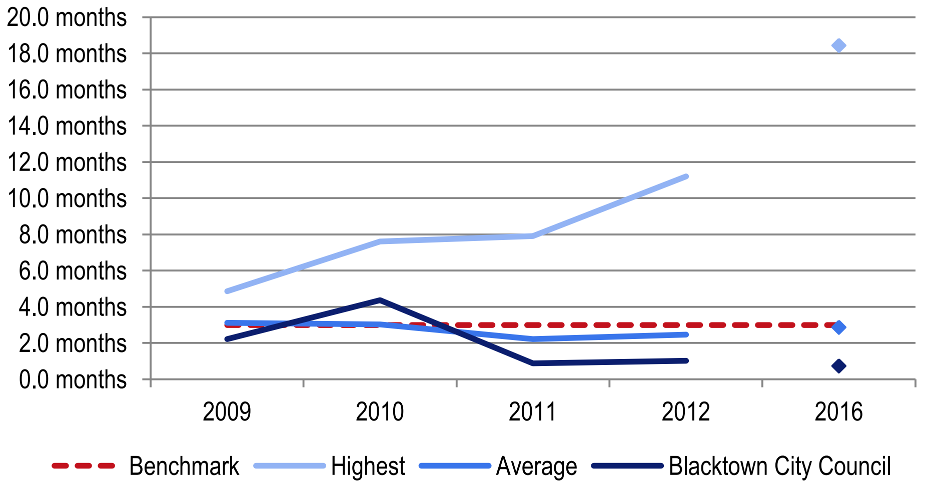
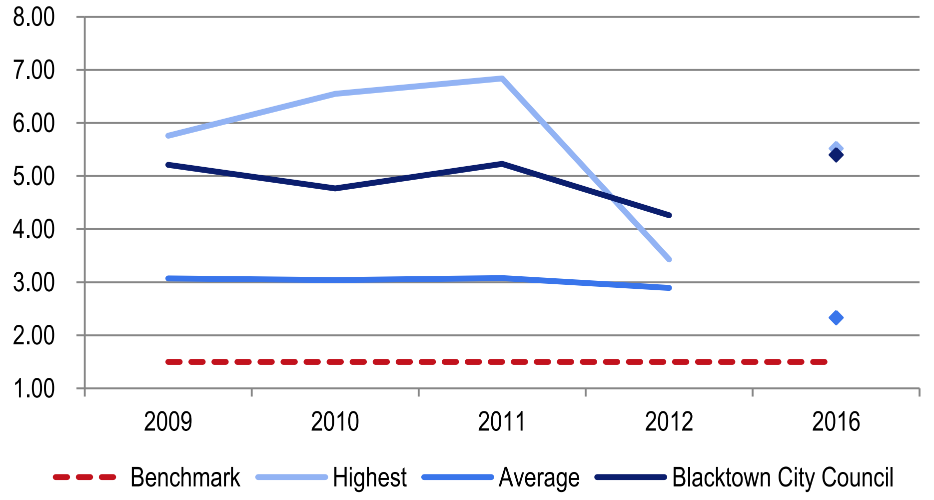


Figure 18 - Unrestricted Current Ratio Comparison



Council's Cash Expense Ratio was below the benchmark and the group average in three of the past four years. Though, Council has sufficient liquidity as it maintained most of its cash reserves in investments. Council's Unrestricted Current Ratio consistently outperformed the benchmark and the peer group over the review period.

Over the medium term, Council's liquidity ratios are forecast to remain mixed compared to the group average because Council invests its funds in longer dated investments.

Debt Servicing

Figure 19 - Debt Service Cover Ratio Comparison

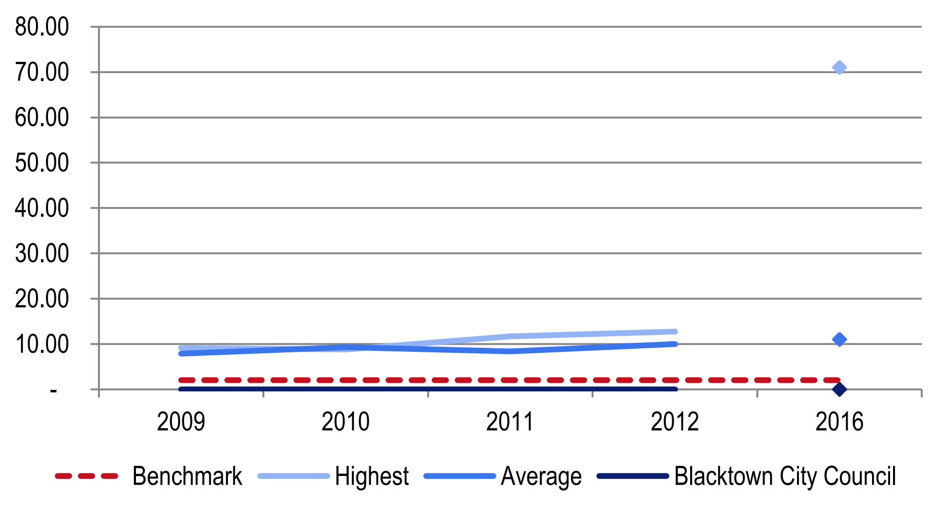
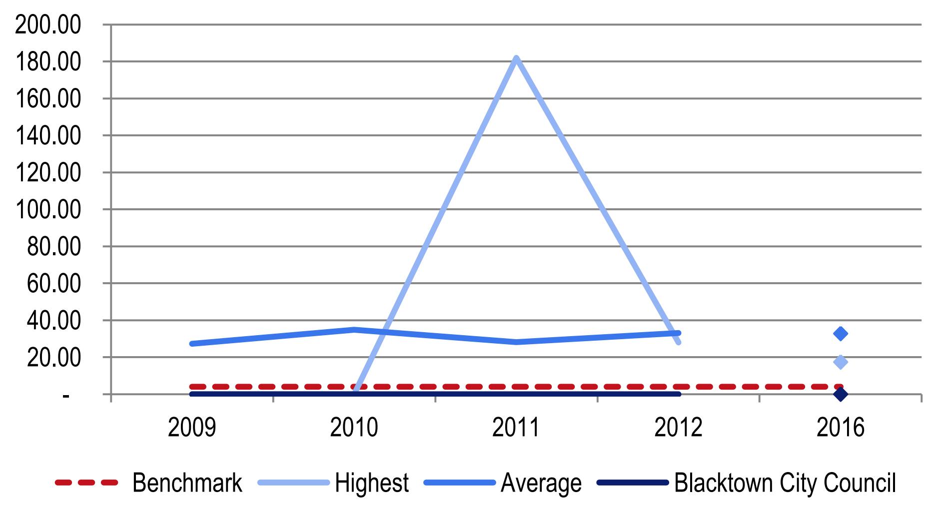


Figure 20 - Interest Cover Ratio Comparison



Council has operated debt free over the past four years and does not forecast to add borrowings over the medium term. On average, councils from this group have used borrowings over the review period and their debt servicing capacity was sound with above benchmark DSCR and Interest Cover Ratio.

Asset Renewal and Capital Works

Figure 21 - Capital Expenditure Ratio Comparison

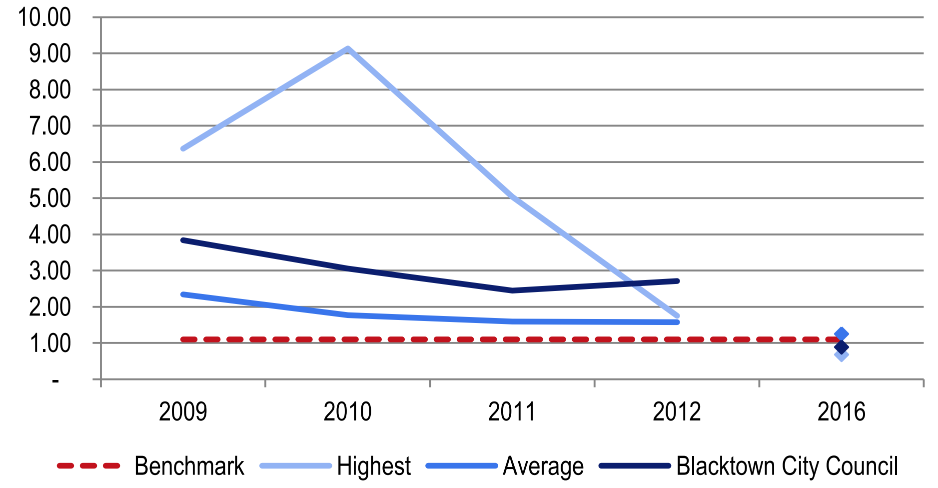


Figure 22 - Asset Maintenance Ratio Comparison

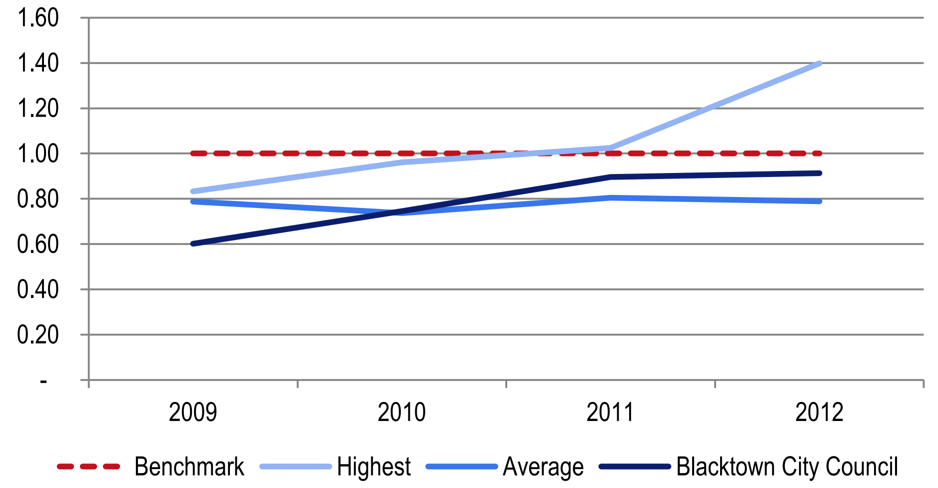


Figure 23- Infrastructure Backlog Ratio Comparison

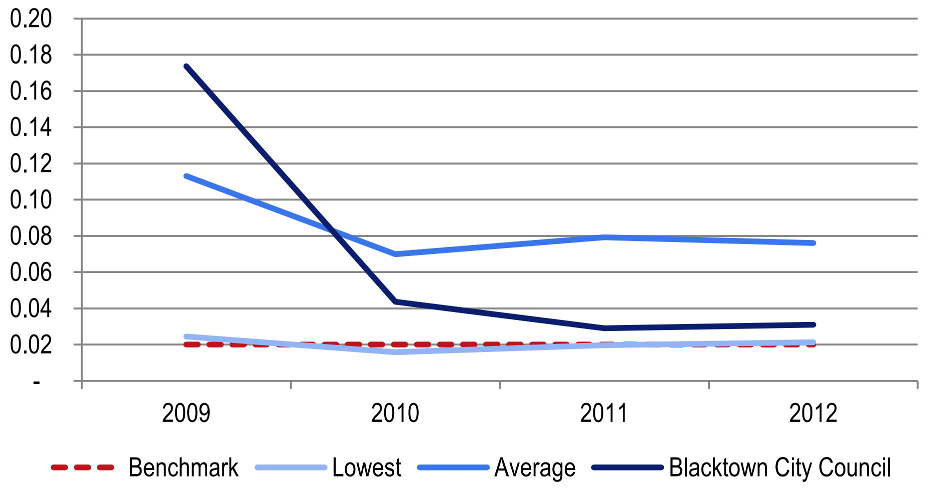
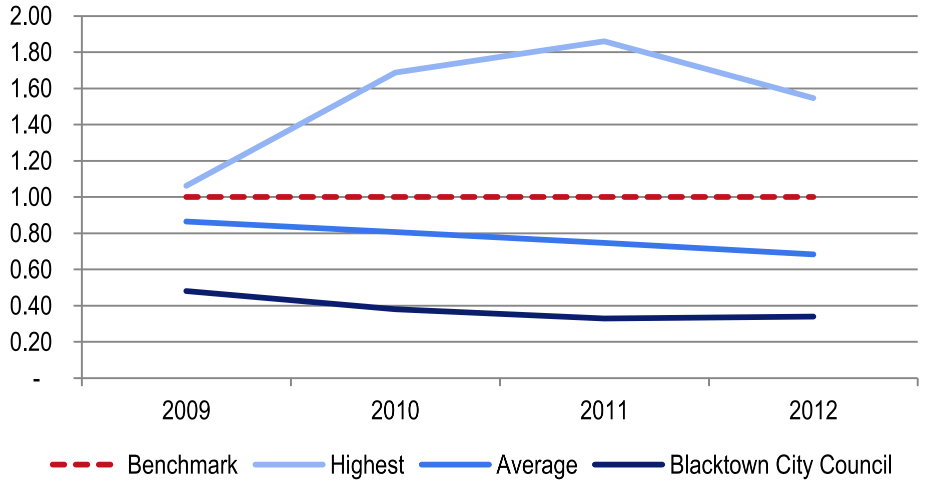


Figure 24 - Building and Infrastructure Asset Renewal Ratio



Council's level of Infrastructure Backlog has been below the group's average level in three of the past four years. Council's spending on maintenance of assets was above the group average in three of the past years.

Council's Capital Expenditure Ratio consistently outperformed the benchmark and the peer group. Over the medium term, Council's capital expenditure is forecast to decline and be below the benchmark and the group average.

Council's Building and Infrastructure Asset Renewal Ratio was consistently well below the benchmark and the group average.

Section 6 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 moderately Sustainable and is expected to remain at this level in the medium term.

We base our recommendation on the following key points:

- EBITDA has grown by $13.4m since 2009, and a 27.5% ($10.4m) increase was recorded in 2012 following growth in revenues, particularly in interest income and operating grants.
- Council has sound levels of cash and investments and capacity for taking on additional debt if required

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

- Council's current Infrastructure Backlog of $52.6m is significant and Council has the financial resources to address this Backlog
- Council provides for over 301,099 residents with 366,660 expected by 2021. This 21.8% forecast rise in population will have an impact on Council's infrastructure and could result in pressure on the existing Infrastructure Backlog so addressing the Backlog in the medium term would assist Council's capacity to deal with its increasing population

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	144,244	135,626	128,989	123,173	6.4%	5.1%	4.7%
User charges and fees	21,135	21,019	19,936	18,578	0.6%	5.4%	7.3%
Interest and investment revenue	17,937	16,658	11,590	14,310	7.7%	43.7%	(19.0%)
Grants and contributions for operating purposes	42,521	33,327	31,467	34,104	27.6%	5.9%	(7.7%)
Other revenues	12,148	12,221	12,377	9,696	(0.6%)	(1.3%)	27.7%
Total revenue	**237,985**	**218,851**	**204,359**	**199,861**	**8.7%**	**7.1%**	**2.3%**
Expenses							
Employees	103,730	98,642	97,414	86,205	5.2%	1.3%	13.0%
Borrowing costs	0	0	0	0	N/A	N/A	N/A
Materials and contract expenses	34,721	33,620	38,967	32,407	3.3%	(13.7%)	20.2%
Depreciation and amortisation	54,040	51,317	36,338	34,159	5.3%	41.2%	6.4%
Other expenses	51,191	48,668	41,474	46,289	5.2%	17.3%	(10.4%)
Total expenses	**243,682**	**232,247**	**214,193**	**199,060**	**4.9%**	**8.4%**	**7.6%**
Operating result (excluding capital grants and contributions)	**(5,697)**	**(13,396)**	**(9,834)**	**801**	57.5%	(36.2%)	(1327.7%)
Operating result (including capital grants and contributions)	**96,625**	**88,129**	**86,472**	**89,069**	9.6%	1.9%	(2.9%)

Table 2 - Items excluded from Income Statement

Excluded items	2012	2011	2010	2009
Grants and contributions for capital purposes	102,322	101,525	96,306	88,268
Minority interest	543	637	1,073	19
Net gain from the disposal of assets	1,690	139	1,893	1,226

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	16,170	13,326	64,608	30,370	21.3%	(79.4%)	112.7%
Investments	223,226	197,500	165,000	189,865	13.0%	19.7%	(13.1%)
Receivables	21,360	19,509	14,761	12,215	9.5%	32.2%	20.8%
Inventories	27,327	25,296	23,855	22,375	8.0%	6.0%	6.6%
Other	146	143	183	244	2.1%	(21.9%)	(25.0%)
Total current assets	288,229	255,774	268,407	255,069	12.7%	(4.7%)	5.2%
Non-current assets							
Investments	45,000	60,350	20,000	10,000	(25.4%)	201.8%	100.0%
Receivables	1,395	1,501	1,571	1,671	(7.1%)	(4.5%)	(6.0%)
Intangible Assets	467	0	0	0	N/A	N/A	N/A
Investments accounted for using the equity method	4,538	3,995	3,358	2,285	13.6%	19.0%	47.0%
Infrastructure, property, plant & equipment	2,419,987	2,327,700	2,490,893	2,313,285	4.0%	(6.6%)	7.7%
Investment property	31,610	31,900	35,685	37,590	(0.9%)	(10.6%)	(5.1%)
Total non-current assets	2,502,997	2,425,446	2,551,507	2,364,831	3.2%	(4.9%)	7.9%
Total assets	**2,791,226**	**2,681,220**	**2,819,914**	**2,619,900**	**4.1%**	**(4.9%)**	**7.6%**
Current liabilities							
Payables	33,153	27,183	25,243	23,037	22.0%	7.7%	9.6%
Borrowings	0	0	0	0	N/A	N/A	N/A
Provisions	50,137	41,718	37,314	32,666	20.2%	11.8%	14.2%
Total current liabilities	83,290	68,901	62,557	55,703	20.9%	10.1%	12.3%
Non-current liabilities							
Borrowings	0	0	0	0	N/A	N/A	N/A
Provisions	5,035	4,346	4,006	3,518	15.9%	8.5%	13.9%
Total non-current liabilities	5,035	4,346	4,006	3,518	15.9%	8.5%	13.9%
Total liabilities	**88,325**	**73,247**	**66,563**	**59,221**	**20.6%**	**10.0%**	**12.4%**
Net assets	**2,702,901**	**2,607,973**	**2,753,351**	**2,560,679**	**3.6%**	**(5.3%)**	**7.5%**

Table 4-Cashflow

Cash Flow Statement ($'000s)	Year ended 30 June			
	2012	**2011**	**2010**	**2009**
Cash flows from operating activities	78,794	73,601	65,955	74,855
Cash flows from investing activities	(75,950)	(124,883)	(31,717)	(68,970)
Proceeds from borrowings and advances	0	0	0	0
Repayment of borrowings and advances	0	0	0	0
Cash flows from financing activities	0	0	0	0
Net increase/(decrease) in cash and equivalents	**2,844**	**(51,282)**	**34,238**	**5,885**
Cash and equivalents	16,170	13,326	64,608	30,370

New South Wales Treasury Corporation

Appendix B Glossary

Asset Revaluations

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

Collateralised Debt Obligation (CDO)

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

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

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

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

Division of Local Government (DLG)

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

Depreciation of Infrastructure Assets

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

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

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

EBITDA

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

Grants and Contributions for Capital Purposes

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

Grants and Contributions for Operating Purposes

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

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

Independent Commission Against Corruption (ICAC)

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

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

Independent Pricing and Regulatory Tribunal (IPART)

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

Infrastructure Backlog

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

Integrated Planning and Reporting (IP&R) Framework

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

Local Government Cost Index (LGCI)

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

Net Assets

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

Roads and Maritime Services (RMS)

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

Section 64 Contribution

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

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

Section 94 Contribution

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

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

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

Special Rate Variation (SRV)

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

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

The applications are reviewed and approved by IPART.

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.