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4.5: Borrowing Capacity

When analysing the financial capacity of the Council we believe Council will not be able to incorporate additional loan funding in addition to the LIRS loan facilities. Although Council has strong debt servicing abilities, as indicated by its high forecast DSCR and Interest Cover Ratios, its cash and investment levels are forecast to be exhausted by 2016.

This is a serious liquidity issue which Council needs to consider, develop options and remodel. Should Council consider adjusting its capital expenditure program to an affordable level, source additional operating cash flow or reduce operating cash expense, then additional borrowing could be considered.

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Section 5 Benchmarking and Comparisons with Other Councils

[This section still being finalised]

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 reasonably sound financial position if its liquidity issues in the forecast medium term are resolved. Both past performance and the financial forecasts support our findings that Council has sufficient financial capacity to service the additional borrowings proposed under its LIRS applications.

As noted in our report, the forecast analysis has been focussed on the General Fund where the LIRS application relates to, whereas the historical analysis has focused on the consolidated audited accounts.

We based our recommendation on the following key points:

- Council has sufficient capacity to manage the additional $7.1m debt highlighted by a DSCR and Interest Cover Ratio above the benchmarks in all 10 years of its financial forecast
- Council has a high level of own sourced income and is not heavily reliant on grants and contributions compared to most Councils
- Council has a low level of borrowings of 0.5% of the General Fund's net assets

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

- Council's forecast that it may face liquidity issues in the medium to long term. This is indicated by very low Unrestricted Current Ratio and Cash Expense Ratio which falls to negative levels in later years. This can be improved if the currently high capital expenditure forecasts are revised to a level more consistent with benchmark requirements
- Council's financial performance has shown areas of improvement over the period from 2009 to 2011. Whilst management is aware of the financial issues noted in this report that Council faces over the medium term, management will need the strong support of Council to implement solutions to these problems to ensure that Council remains financially sound over the medium to long term

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Appendix A Historical Financial Information Tables

Table 1- Income Statement

Income Statement ($'000s)	Year ended 30 June			% annual change	
	2011	2010	2009	2011	2010
Revenue					
Rates and annual charges	119,020	113,233	102,235	5.1%	10.8%
User charges and fees	53,675	51,679	49,012	3.9%	5.4%
Interest and investment revenue	8,905	8,522	1,817	4.5%	369.0%
Grants and contributions for operating purposes	23,546	23,330	23,264	0.9%	0.3%
Other revenues	2,680	5,451	2,900	(50.8%)	88.0%
Total revenue	**207,826**	**202,215**	**179,228**	**2.8%**	**12.8%**
Employees	74,877	76,462	70,082	(2.1%)	9.1%
Borrowing costs	12,260	9,621	9,306	27.4%	3.4%
Materials and contract expenses	42,950	46,324	48,420	(7.3%)	(4.3%)
Depreciation and amortisation	53,594	59,902	50,331	(10.5%)	19.0%
Other expenses	40,017	40,025	27,600	(0.0%)	45.0%
Total expenses	**223,698**	**232,334**	**205,739**	**(3.7%)**	**12.9%**
Operating result	**(15,872)**	**(30,119)**	**(26,511)**	**47.3%**	**(13.6%)**

Table 2 - Items excluded from Income Statement

Excluded items ($'000s)			
	2011	2010	2009
Grants and contributions for capital purposes	43,406	29,423	17,699
Net gain/(loss) from the disposal of assets	(1,493)	131	11,267

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Table 3 - Balance Sheet

Balance Sheet ($'000s)	Year Ended 30 June			% annual change	
	2011	2010	2009	2011	2010
Current assets					
Cash and equivalents	51,799	49,202	18,572	5.3%	164.9%
Investments	69,447	73,976	77,605	(6.1%)	(4.7%)
Receivables	35,979	37,592	31,124	(4.3%)	20.8%
Inventories	2,088	2,169	2,119	(3.7%)	2.4%
Other	366	414	811	(11.6%)	(49.0%)
Total current assets	159,679	163,353	130,231	(2.2%)	25.4%
Non-current assets					
Investments	16,992	4,164	4,239	308.1%	(1.8%)
Receivables	1,422	1,330	1,330	6.9%	0.0%
Intangible assets	2,515	3,266	4,318	(23.0%)	(24.4%)
Infrastructure, property, plant & equipment	2,037,332	1,917,686	1,713,712	6.2%	11.9%
Total non-current assets	2,058,261	1,926,446	1,723,599	6.8%	11.8%
Total assets	**2,217,940**	**2,089,799**	**1,853,830**	**6.1%**	**12.7%**
Current liabilities					
Payables	46,989	52,615	31,456	(10.7%)	67.3%
Borrowings	10,818	10,708	8,100	1.0%	32.2%
Provisions	28,742	32,486	26,282	(11.5%)	23.6%
Total current liabilities	86,549	95,809	65,838	(9.7%)	45.5%
Non-current liabilities					
Payables	52	40	37	30.0%	8.1%
Borrowings	179,444	163,812	107,389	9.5%	52.5%
Provisions	50,528	35,218	29,538	43.5%	19.2%
Total non-current liabilities	230,024	199,070	136,964	15.5%	45.3%
Total liabilities	**316,573**	**294,879**	**202,802**	**7.4%**	**45.4%**
Net assets	**1,901,367**	**1,794,920**	**1,651,028**	**5.9%**	**8.7%**

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Table 4-Cashflow

Cashflow Statement ($'000s)	Year ended 30 June		
	2011	2010	2009
Cashflows from operating activities	80,708	66,688	42,248
Cashflows from investing activities	(93,854)	(95,088)	(27,783)
Proceeds from borrowings and advances	26,450	70,339	573
Repayment of borrowings and advances	(10,708)	(11,308)	(8,173)
Cashflows from financing activities	15,742	59,031	(7,600)
Net increase/(decrease) in cash and equivalents	**2,596**	**30,631**	**6,865**
Cash and equivalents	51,799	49,202	18,572

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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

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

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

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cases this has led to significantly higher depreciation charges, and will contribute to higher reported operating deficits.

EBITDA

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

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

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unaudited and stated within Special Schedule 7 that accompanies the council's audited annual financial statements.

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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.

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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

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Treasury Corporation

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

Infrastructure Backlog Ratio

Benchmark = Less than 0.02x

Ratio = estimated cost to bring assets to a satisfactory condition (from Special Schedule 7) / total infrastructure, building, other structures and depreciable land improvement assets (from note 9a)

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

Interest Cover Ratio

Benchmark = Greater than 4.0x

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

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

Operating Ratio

Benchmark = Better than negative 4%

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

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

Own Source Operating Revenue Ratio

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Benchmark = Greater than 60%

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

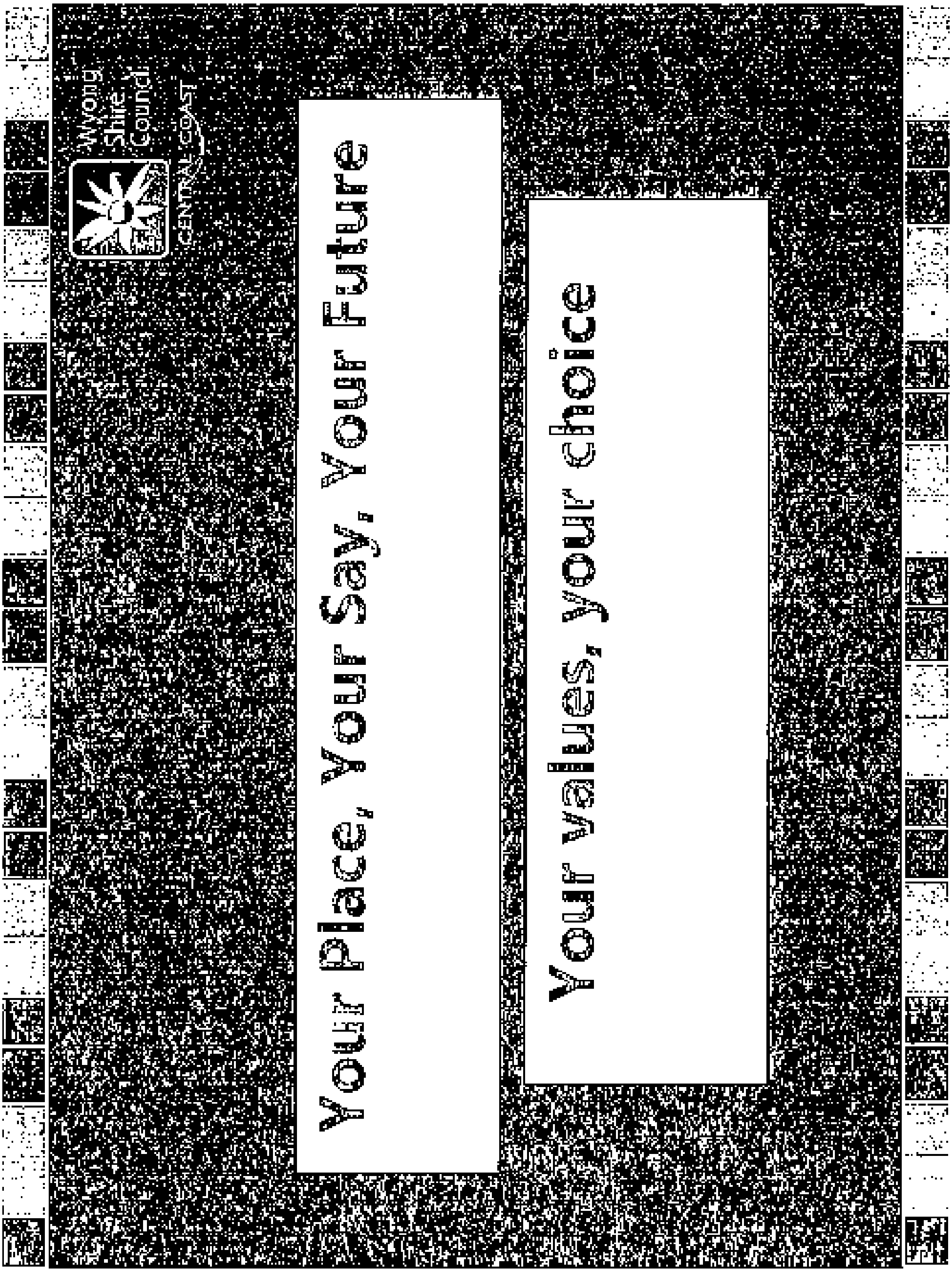
This ratio measures the level of a council's fiscal flexibility. It is the degree of reliance on external funding sources such as operating grants and contributions. A council's financial flexibility improves the higher the level of its own source revenue.

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.


Wyong Shire Council
CENTRAL COAST
Your Place, Your Say, Your Future
Your values, your choice

Today we will:

- Briefly consider the situation with regard to services, long term financial planning and community aspirations.
- Understand existing community input on what we value.
- Identify the services we think are most important for our future
- Identify the most important activity areas, or groups of services

Wyong Shire Council
CENTRAL COAST

The Question Council wants to answer

- What level of service meets the needs and aspirations of the community while achieving the best balance between:
  - Cost and willingness to pay
  - Long term financial sustainability
  - Impact on current and future residents and ratepayers

Wyong Shire Council

Understanding your needs & wants

- So we can all pursue the quality of life we seek
- So Council can better plan services for the future
- So we can ensure the best use of the ratepayer's dollar.
- So everyone knows what can be done & what can't

Wyong Shire Council
CENTRAL COAST

At this workshop we will:

- Consider what Council's financial position means for you.
- Gain your input to understand what you value
- Identify what services you think are most important
- Identify what areas (groups of services) are most important to you

Wyong Shire Council

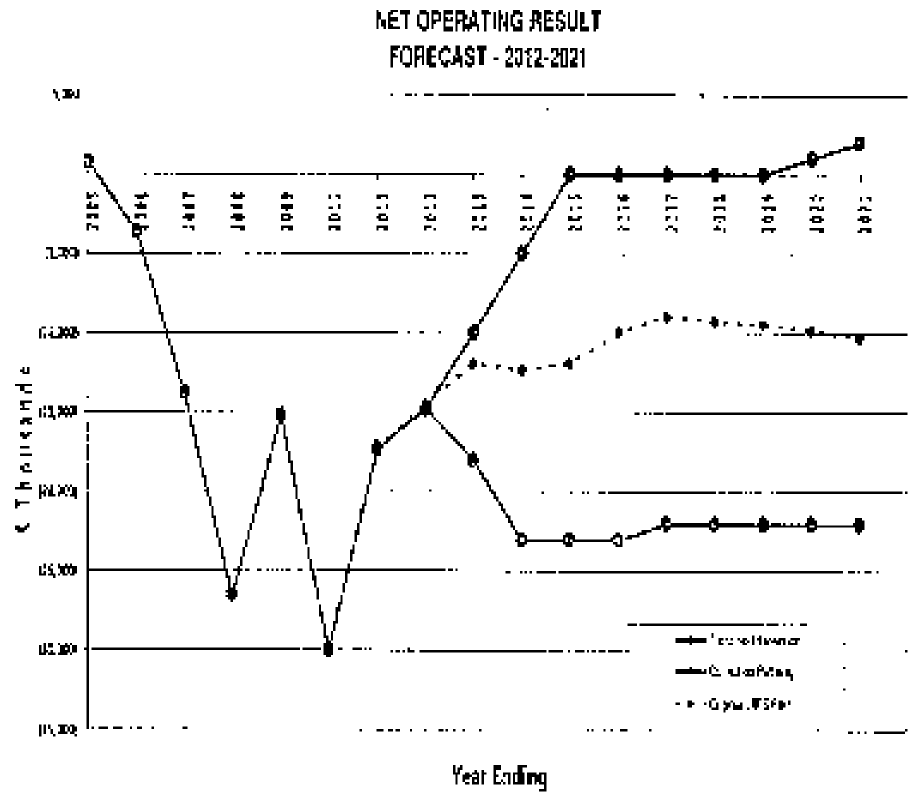
Outline

- **PART 1**
  - Council's current financial position
  - Our actions to regain financial sustainability
- **PART 2**
  - Workshop: Your say on Council's services

Wyong Shire Council
CENTRAL COAST

Financial Opportunities and Challenges

- Net Operating result
- Information technology
- Cost shifting from other levels of government
- Corporate Measures and reporting
- Partnerships
- Central Cost Water Corporation



Wyong Shire Council

Balancing the Budget

- Council is working towards a healthy financial future for Wyong Shire.
- Council has more money going out than coming in for daily operations.
- Assets need to be kept up-to-date
- Council is committed to an operating result of break even by 2014./15

Wyong Shire Council

Keeping costs down.

- Reduced the deficit from $30million to <$15million in 18 months.
- $2.165m one-off reduced fleet costs
- $1.0m annually- reduced staff costs
- $300k annually- reduced legal costs
- $250k annually- reduced use of consultants

Wyong Shire Council

Keeping costs down.

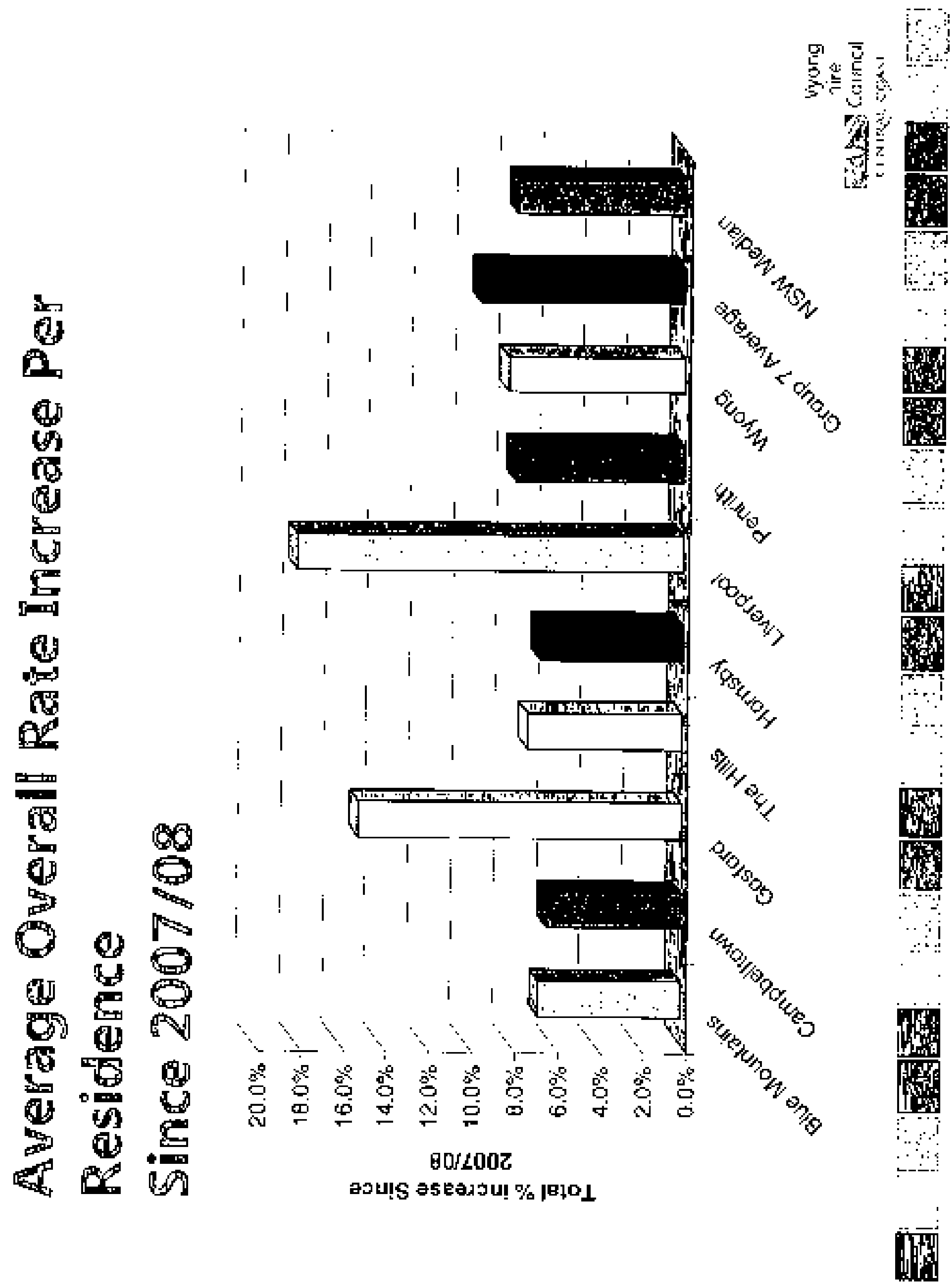
- Reduced road patching costs from $118 m2 to $21m2
- In-field technology to improve productivity
- Energy cost savings- lighting and air conditioning in the Civic Centre and other Council buildings.
- Myriad of other tiny improvements

Wyong Shire Council

Competing Needs

- Materials spend low against other Councils
- Borrowing costs very high against NSW
- Depreciation costs high vs others
- Asset replacement way behind.
- Roads need $140m to catch up

Wyong Shire Council


Average Overall Rate Increase Per Residence Since 2007/08
Total % increase Since 2007/08
20.0%
18.0%
16.0%
14.0%
12.0%
10.0%
8.0%
6.0%
4.0%
2.0%
0.0%
Blue Mountains
Campbelltown
Gosford
The Hills
Hornsby
Liverpool
Penrith
Wyong
Group 7 Average
NSW Median

What Next?

- Council still has $15m deficit to tackle. Something's gotta give.
- We need your help to reach break-even.
- What Council services do you value ?
- Remember – better/more services = cost
- A Service Standard Review

Wyong Shire Council

What do we want to know?

- Which Council services do you think are really necessary for your life's needs?
- What qualities in those services are needed?
- How much are you willing to pay?
- Would you discard some for better quality in others?
- Which one would you exchange?

Wyong Shire Council
CENTRAL COAST

What Happens Next?
Working with the Community to:-

- Review the values and priority areas
- Develop scenarios for different levels of service.
- Identify the scenario that strikes the best balance between what you want & our capacity to pay for it.
- Councillors will then plan how to proceed.
- Maintaining or increasing current services levels will need to be funded in some way.

Wyong Shire Council

Your role is vital to:

- Help us understand what our community values (Phase 1 – May 2012)
- Help us prioritise the range of services Council provides (Phase 1 – May 2012)
- Help decide which service mix provides the best balance for our community (Phase 2- October/November 2012)

Wyong Shire Council

Considering what you have just seen and heard...

- Did anything strike you as interesting, significant, surprising?
- Is there anything you strongly agree with? Why?
- Is there anything you strongly disagree with? Why?

Wyong Shire Council

Now we will...

- Look at the Principal Activities, or groups of services
- Identify some success factors
- Identify the services within those Principal Activities that best deliver success
- Identify the Principal Activities that are most significant to you and your lifestyle

Wyong Shire Council
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