YARRA CITY COUNCIL

DRAFT LONG TERM FINANCIAL PLAN 2017/18–2026/27

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1. INTRODUCTION

This Long Term Financial Strategy (LTFS) has been developed and updates the strategy adopted by Council in 2016-17. The scenario presented is considered the most achievable option for Council to support Council's financial sustainability into the future.

The main scenario parameters are detailed below:

- Rate increase at the ESC rate cap level (2%) for the life of the LTFS;
- Full cost recovery of waste services via a new proposed waste service charge
- Debt redemption as a first priority
- Cash backing reserves as a second priority
- Efficiency target of $500k recurrent expenditure savings built into each year

The scenario relies on the proposed waste service charge being introduced. It is proposed to introduce the waste service charge in order to improve Council's short to medium term financial sustainability, and to enable Council to be able to respond to emerging priorities from our community in the longer term. If the waste service charge is not implemented, Council will be required to reduce services and/or service levels, or reduce the capital expenditure program in the next budget cycle.

The LTFS is a living document subject to ongoing review.

2. OBJECTIVE

Council prepares a Long Term Financial Strategy (LTFS) over a 10 year period to provide financial management and guidance to support service delivery and the capital works program. This document outlines the key assumptions and provides an overview of each key element of the LTFS.

Strong financial management will be evidenced by Council fully renewing its assets as required and generating cash liquidity to meet operational requirements. The Operating Budget will also deliver sufficient cash surplus to enable timely asset renewal and a reasonable level of funding to be available for New/ Upgrade Capital Works and New Initiatives in Operations.

3. MANAGEMENT OF THE LTFS

The LTFS is managed within a framework of key financial indicators together with profiled cash management. These items are drawn together to provide a strategy for the long term sustainability and solvency of Council's operation.

The key lead indicators are:

- Liquidity
- Unrestricted Cash
- Net Result
- Indebtedness

Other indicators are:

- Debt Commitment
- Self-Financing
- Renewal Gap
- Capital Replacement

Descriptions of each of these indicators together with the target range sought is provided in Appendix 1 – Key Financial Indicators Described (Page 17).

The framework also includes key assumptions that underpin the financial analysis. The assumptions are outlined in Appendix 2 – Cashflow Parameter Assumptions (Page 19).

Historical assumptions have been reviewed and a number of amendments have been required particularly in the management of liquidity. The changes made reflect the changing operating environment at Yarra for example rate capping has significantly reduced Council's revenue over the life of the LTFS and Council has less control via rates to respond to financial shocks. Council also has a $32.5m loan due to be repaid in 2020-21.

A critical element of the assumptions is the allocated expenditure to the Capital Works Program. This assumes 100% of the capital program will be delivered in cash terms over the long term.

This LTFS also proposes to establish a set of financial principles that provide advice on Council's financial strategy. These are detailed in Appendix 3.

4. FINANCIAL POSITION BACKGROUND

Council's current financial position (predicted 30 June 2017) is constrained and cash management is very tight. In general, Council is performing satisfactorily against benchmark ratio levels established by the Auditor General with the exception of cash related ratios. The Unrestricted Cash ratio is currently low, however this improves significantly by the end of the LTFS. The Liquidity ratio is also low in early years, however improves in the latter half of the LTFS.

Council is faced with a myriad of requests from community and it has very limited capacity in discretionary funds to respond to these needs, unless the proposed waste service charge is introduced. If the proposed waste service charge is not introduced Council will be required to reduce services and/or service levels, or reduce capital expenditure.

Council is adequately meeting its asset renewal obligations within the LTFS.

Council borrowed funds in November 2014 via the MAV Local Government Funding Vehicle Bond sponsored by the MAV. This seven year loan of $32.5 million provided funding for payment of the Defined Benefit Superannuation debt, purchase of 345 Bridge Rd, purchase of the Connie Benn Centre and an energy performance contract. This loan is an interest only fixed term loan. A major strategy in this current LTFS is to redeem this debt when it is due. An additional loan of $13.5 million is due to be drawn down in 2016-17. This loan is funded on a principal and interest basis and will be repaid by the end of the LTFS.

5. 2017-18 BUDGET POSITION

The 2017-18 Operating Budget provides for a cash surplus that is used to fund Council's Capital Works Program. The Operating Budget supports more than 100 services to the community and the Capital Works Program is critical to Council's ability to maintain, enhance and build assets to also service community need.

Despite a deliberate plan to grow overall cash holdings in recent years, Council had insufficient cash to balance the budget due to a range of external factors. In 2017-18 a new waste service charge is proposed, bringing in an additional $8.5 million in 2017-18, and $102 million across the LTFS. This is essentially a measure to restore the 10 year LTFS to its original position prior to rate capping being introduced, which had a $98m impact of foregone revenue over the life of the 10 year plan. This additional revenue will support the repayment of borrowings, as well as the ongoing provision of services. It will improve Council's short to medium term financial sustainability, and enable Council to be able to respond to emerging priorities from our community in the longer term. The end of year cash position at 30 June 2018 is expected to be $26.75 million (assuming 100% of the capital budget is spent).

The Open Space Reserve has been fully acquitted during 2015-16 with funds being applied to a general reserve, however these are not fully cash backed.

5.1 CASH HOLDINGS

Council's total cash holding at 30 June 2016 was $22.5 million with $20.18 million applicable for general reserve obligations.

5.1.1 WORKING CAPITAL

At 30 June 2017, it is estimated that Council requires around $50 million in cash at the end of each financial year to manage its working capital ratio. This balance needs to be higher if the general reserve (currently $20 million) is to be cash backed.

5.1.2 OPEN SPACE RESERVE

The Open Space Reserve was fully acquitted as at 2015-16 (as reflected in the 2015-16 Annual Report). The change to policy has resulted in the Open Space Reserve being fully acquitted and any remaining funds were transferred to a general reserve, however this is not fully cash backed. The balance of the General Reserve is $20 million.

6. STRATEGIC ACTIONS

In drafting this LTFS a number of strategies have been implemented to seek to build a more complete picture of Council's financial position and to provide better alignment with Council's goals.

6.1 IMPROVING COUNCIL'S WORKING CAPITAL

With the proposed introduction of the waste service charge, Council will redress the shortfall in the cash balance to ensure minimum operating cash is available.

6.2 RELEASE OF GENERAL RESERVE FUNDS

Council has a stated goal of seeking to acquire open space and the 2016-17 LTFS aligned the acquisition of strategic open space assets with rationalisation of existing Council assets and asset sales income. This is still a goal in the medium to long term.

A further update to the Open Space Policy will provide Council with an effective funding source for development of its existing open space. It is anticipated that this expenditure will be equal to the income raised. There will be no increase in the obligation and therefore the financial obligation to the Reserve will not grow. If Open Space contributions exceed capital expenditure than the Reserve, additional funds will need to be added to the Reserve balance.

6.3 RATE CAPPING

In 2016-17 rate capping was introduced with details of the scheme provided by the Essential Services Commission. An allowance has been made for rate increases as foreshadowed by the ESC together with an allowance for growth via Supplementary Rates and the proposed Waste Services charge.

The Minister for Local Government, The Hon. Natalie Hutchins, announced the rate capping level for 2017-18 on 16 December 2016 at 2%.

Predicted future rate increases are outlined below.

Table 1 PREDICTED ESC RATE INCREASES

LTFS	Year 1	Year 2	Year 3	Year 4	Year 5	Year 6	Year 7	Year 8	Year 9	Year 10
	2017-18	2018-19	2019-20	2020-21	2021-22	2022-23	2023-24	2024-25	2025-26	2026-27
Predicted Rate Cap	2%	2%	2%	2%	2%	2%	2%	2%	2%	2%

If the rate cap increases are less than predicted, Council will be required to reduce services and/or service levels and/or reduce the capital works program, if additional revenue sources are not available.

6.4 PROPOSED WASTE SERVICE CHARGE

The City of Yarra is one of six Councils in Victoria that does not levy separate waste/recycling charge. However many councils do levy garbage/recycling charges which are included on the rates notice. The level of these charges must be linked to the cost of service. The Local Government Act excludes garbage/recycling charges from the rate cap, at the moment. This may not always be the case, with the Local Government Act currently under review.

Growth in multi-unit development is resulting in above average increases in the waste area. In the last 12 months there has been a 4.54% increase in average waste collection numbers and 6.05% for recycling. Waste tipping fees are predicted to grow by 6.33% (Landfill Levy 8.15% and Gate Fees by 3.25%).

Council provides a range of services which could be charged for including the weekly kerbside garbage and recycling collections, commercial (domestic type), waste and recycling collection and the ‘at call’ hard and green waste collections. All residential properties receive the garbage and recycling service with approximately 1,600 (out of a total of 7,558) of commercial industrial properties receiving the service.

This LTFS includes the proposed introduction of a waste services charge as part of the 2017-18 budget. This provides $102 million over the LTFS. The charge is expected to increase by 4% per annum from a base rate of $8.5 million.

This LTFS has been developed on the assumption that a proposed Waste Charge is introduced in Year 1 (2017-18). Given the significant movement in waste costs predicted over time it will be critical from a financial perspective to isolate these costs from the rate cap.

6.5 LOAN BORROWINGS

The introduction of rate capping and debt requiring to be repaid in the short term has had a significant impact on the LTFS and greatly exacerbated Council’s already tight financial position. Existing debt is serviced by a $32.5 million interest only loan, due to be repaid in 2020-21 and a $13.5 million principal and interest loan due to be repaid by the end of this 10 year LTFS.

The Victorian Auditor-General has indicated through its recommendation on financial ratios that Indebtedness (Non-current liabilities/Own sourced revenue) above 40% places Council in the medium risk category and 60% in the high risk category.

The LTFS includes a significant principal repayment starting from Year 1 for the interest only loan. It is anticipated that all debt will be paid by the end of 2026-27. This is dependent upon the proposed waste charge being introduced.

The indebtedness ratio is 22.2% at 30 June 2018.

Debt Commitment ratio remains low risk for the life of the LTFS as a result of moving to a principal and interest approach to debt financing, and is a crucial strategy should borrowings be required in the future.

Further borrowing may need to occur to provide Council with a capacity to access contingency funds should the need arise e.g. a further call on the Defined Benefit Superannuation obligation, and especially so if the proposed waste charge is not introduced.

6.6 LEASING AND RATIONALISATION OF MOTOR VEHICLE AND UTILITY FLEET

Council's motor vehicle and utility fleet is currently partially purchased and managed directly by Council, and partially leased. As a result an annual capital allocation is required to pay for the changeover cost of some of these vehicles. In the 2016-17 Budget the net capital allocation was $0.5 million.

Additional leasing will be further considered during 2017-18 as a possible cost reduction model.

6.7 DISPOSAL OF SURPLUS ASSETS AND ENHANCING RETURNS

A more pro-active and entrepreneurial approach to disposal of redundant laneways, investigation of increasing returns and potential for disposal of some assets needs to be pursued. Disposal of some assets to fund new requirements is considered appropriate and the most effective use of community resources. In addition to the receipt of a cash injection from the sale a saving is also made on maintenance and asset renewal costs.

It is also recommended that assets surplus to requirements be carefully considered as opportunities for open space creation where relevant or disposal to fund the purchase of other assets.

Opportunities to seek improved returns from building assets that are not fully applied for community use are currently being investigated. It is anticipated that improved financial returns can be achieved from a number of buildings by being more entrepreneurial in property management and improve the use of assets. This will assist Council's overall financial position.

A further separate report on the Property Strategy will be presented to Council in 2017-18.

6.8 FEES AND CHARGES POLICY

It is proposed that Council adopt a strong fees and charges policy that provides a variety of categories of fees and charges from full costing to part subsidy/investment in services. The calculation of fees would mirror the cost of service provision and only where appropriate and in compliance with competitive neutrality the fee would be subsidised.

In general, fees should follow the trend in labour costs so that the ratio of subsidy from rates is maintained. There will be circumstances where movement of fees above or below the trend figure is justified. Individual fees should consider cost recovery, competition and ability to generate return on investment. The fees and charges policy would guide the preparation of the Schedule of Fees and Charges.

This LTFS assumes Fees and Charges are generally increased in line with the movement in labour costs based on the principle of cost recovery where appropriate and practical.

6.9 NEW SERVICES

Council is committed to the introduction of the following new service:

- *North Fitzroy Hub* will operate from partway through 2016-17 and with a full year operation from 2017-18. It is anticipated that an additional $800K for a full year operation will be required and this has been allowed for in the LTFS.

6.10 NEW POPULATION AND DEVELOPMENT

Yarra is experiencing a significant increase in new property and population.

Residential dwelling growth is expected to be around 2% pa from 2016 through to 2021 and then decline slightly with growth increasing by about 1.6%.

Table 2 Forecast population, households and dwellings

City of Yarra	Forecast year				
Summary	**2016**	**2021**	**2026**	**2031**	**2036**
Population	88,120	95,911	103,191	110,512	117,036
Change in population (5yrs)	9,107	7,790	7,280	7,321	6,524
Average annual change	2.21	1.71	1.47	1.38	1.15
Households	39,431	43,178	46,741	50,267	53,452
Average household size	2.19	2.18	2.17	2.17	2.16
Population in non-private dwellings	1,604	1,604	1,604	1,604	1,604
Dwellings	41,921	46,103	49,981	53,757	57,166
Dwelling occupancy rate	94.06	93.66	93.52	93.51	93.50

Population and household forecasts, 2011 to 2036, prepared by .id the population experts, August 2013. http://www.id.com.au

The LTFS provides for <u>no net growth in labour costs</u> to accommodate the increased population and dwellings being serviced. Requirements to fulfil statutory obligations or increased customer demand must be sourced from within the existing workforce allocation.

6.11 ENHANCED DEBT MANAGEMENT

A significant task to improve debt management is being driven by the organisation. This involves the review of historical debt across all aspects of Council's operations.

Further key initiatives are the establishment of four instalment rate payments (removing the annual payment option) as the minimum standard of payment and the introduction of a credit card surcharge fee.

These two debt management initiatives have been incorporated into this LTFS.

6.12 LEGAL CASES

An allocation has been made within the LTFS to accommodate estimated legal fees (at the same funding level as 2016-17), however no allocation has been made for potential settlement costs.

6.13 INTRODUCTION OF ENHANCED PARKING ENFORCEMENT

Two key recommendations from the Parking Service Review were for Council to consider the introduction of enhanced enforcement on Sundays for key locations across the City and to introduce consistent signage given that some activity centres have inconsistent signage deriving from pre-amalgamation. Parking is at a premium in the City and both these measures will assist with parking management. Parking revenue continues to be an important source of income for Council.

6.14 LEISURE CENTRES IMPROVED RETURNS

An extensive Service Review has been undertaken into the operation of Council's Leisure Centres. A number of strategic opportunities exist to improve Council's overall financial return from these operations while also enhancing services to the community. However some of these initiatives will require capital funding to achieve improved returns.

6.15 ASSET RENEWAL AND NEW AND UPGRADE EXPENDITURE

Information from the Asset Management Plans inform Council's capital expenditure priorities.

As part of the preparation of this LTFS the cost of renewal works has been indexed to reflect the future cost of works in years 2-10 of the LTFS.

New assets are being driven by a number of regular programs derived from Strategies and Plans. These include water sensitive urban design, reduction in potable water e.g. Edinburgh Gardens, Activity Centre enhancements generating new road works, public toilets and LATMs. These types of assets also create an additional maintenance requirement of approximately 1% per annum going forward**.**

This LTFS indicates that funds available for New and Upgrade Capital Expenditure and New Initiatives in Operations will be very low ($5.44 million) in 2017-18 and remain relatively low in the short to medium term of the LTFS. Renewal of assets is prioritised to enhance financial sustainability.

Estimated Capital Expenditure as outlined in Table 3

Capital Cashflow	Year 1	Year 2	Year 3	Year 4	Year 5	Year 6	Year 7	Year 8	Year 9	Year 10
	2017-18	2018-19	2019-20	2020-21	2021-22	2022-23	2023-24	2024-25	2025-26	2026-27
	$'000	$'000	$'000	$'000	$'000	$'000	$'000	$'000	$'000	$'000
Renewal	24,605	25,814	25,559	23,666	25,177	26,832	27,508	29,675	30,003	30,619
Upgrade	539	6,224	7,907	10,865	4,795	3,428	1,990	2,120	2,820	1,825
New	4,896	820	200	1,461	8,028	8,500	10,037	8,531	8,309	9,511
Carry-forwards	3,000	-	-	-	-	-	-	-	-	-
Total	**33,040**	**32,858**	**33,666**	**35,992**	**38,000**	**38,760**	**39,535**	**40,326**	**41,132**	**41,955**

7. KNOWN MATTERS TO BE QUANTIFIED

Council has a number of initiatives underway to gather efficiencies and improve its financial position including Service Reviews, Revenue Strategies and reviews of Strategies and Plans. Generally, it is too early in the development of these initiatives to incorporate these outcomes.

7.1 FUTURE INITIATIVES

A number of other key issues have also been identified as being likely to have a significant impact on the LTFS but are unquantified at this time. These include:

Fitzroy Town Hall – future use

Gasworks site including Indoor Sports Stadium and Depot relocation (no allowance in LTFS)

Richmond Secondary College impact

Amcor Community Facilities - Modelling is being undertaken of the likely impact of the Amcor development on Council's financial position and initial estimates are a cost neutral position. Given the uncertainty of the assumptions at this time no amendment to the LTFS has been made.

7.2 CONTINGENT LIABILITIES

A number of issues have been identified that have the potential to result in a financial impact on Council. As these issues are uncertain no specific allowance within the LTFS has been made. These matters include:

- Future calls from the Local Government Defined Benefits Scheme.
- Legal costs.
- Council has received a $500K grant for the Lourdes development which will be required to be repaid if this development does not proceed or the grant reallocated.
- Costs associated with changes arising from the reform of the HACC service and NDIS.

The LTFS will be regularly updated to incorporate these matters when information allows.

8 FINANCIAL SCENARIOS AND OUTCOMES

8.1 KEY OUTCOMES

Key outcomes are outlined below:

Table 4 Summary of LTFS (Cash Flows)

Cashflow Statement	Year 1	Year 2	Year 3	Year 4	Year 5	Year 6	Year 7	Year 8	Year 9	Year 10
	2017-18	2018-19	2019-20	2020-21	2021-22	2022-23	2023-24	2024-25	2025-26	2026-27
	$'000	$'000	$'000	$'000	$'000	$'000	$'000	$'000	$'000	$'000
Cash Flows from Operating Activities										
Receipts										
Rates	112,708	117,166	121,289	125,500	129,803	134,200	138,693	143,284	147,975	152,769
Statutory Fees & Fines	27,107	27,378	27,926	28,484	28,960	29,435	29,910	30,385	30,860	31,335
User Fees and other Fines	26,387	26,651	27,184	27,728	28,216	28,703	29,191	29,678	30,166	30,653
Grants Capital	1,195	1,207	1,231	1,256	1,269	1,281	1,294	1,307	1,320	1,333
Grants Operating	12,023	13,225	14,548	16,003	16,163	16,324	16,488	16,652	16,819	16,987
Contributions	4,300	4,300	4,300	4,300	4,300	4,300	4,300	4,300	4,300	4,300
Reimbursements	1,640	1,699	1,819	1,942	2,004	2,024	2,045	2,065	2,086	2,107
Interest	500	500	500	500	-	-	-	-	-	-
Other Receipts	1,207	1,294	1,345	1,418	1,432	1,447	1,461	1,476	1,490	1,505
Total Receipts	**187,067**	**193,420**	**200,142**	**207,131**	**212,146**	**217,714**	**223,380**	**229,147**	**235,016**	**240,989**
Payments										
Payments to suppliers	(69,085)	(69,754)	(71,110)	(72,493)	(73,198)	(73,910)	(74,629)	(75,355)	(76,089)	(76,830)
Payments to employees (including redundancies)	(80,142)	(82,058)	(83,677)	(85,330)	(87,030)	(88,730)	(90,430)	(92,130)	(93,830)	(95,530)
Total Payments	**(149,227)**	**(151,812)**	**(154,787)**	**(157,823)**	**(160,228)**	**(162,640)**	**(165,059)**	**(167,485)**	**(169,919)**	**(172,360)**
Net cash provided by (used in) operating activities	**37,840**	**41,608**	**45,355**	**49,308**	**51,918**	**55,074**	**58,321**	**61,662**	**65,097**	**68,629**
Cash Flows from Investing Activities										
Payments for property,plant and equipment,infrastructure	(33,040)	(32,858)	(33,666)	(35,992)	(38,000)	(38,760)	(39,535)	(40,326)	(41,132)	(41,955)
Proceeds from sale of property,plant and equipment,infrastructure	800	697	692	687	682	675	670	665	660	655
Net cash provided by (used in) investing activities	**(32,240)**	**(32,161)**	**(32,974)**	**(35,305)**	**(37,318)**	**(38,085)**	**(38,865)**	**(39,661)**	**(40,472)**	**(41,300)**
Cash Flows from financing activities										
Finance Costs	(2,139)	(2,088)	(2,035)	(1,980)	(410)	(349)	(286)	(219)	(149)	(76)
Repayment of interest bearing loans and borrowings	(7,591)	(7,982)	(8,389)	(8,811)	(5,713)	(1,369)	(1,433)	(1,500)	(1,569)	(1,642)
Net cash provided by (used in) financing activities	**(9,730)**	**(10,070)**	**(10,424)**	**(10,791)**	**(6,123)**	**(1,718)**	**(1,719)**	**(1,719)**	**(1,719)**	**(1,719)**
Net increase (decrease) in cash and cash equivalents	(4,130)	(623)	1,957	3,212	8,477	15,271	17,738	20,282	22,905	25,611
Cash and cash equivalents at the beginning of financial year	30,877	26,747	26,124	28,081	31,293	39,770	55,041	72,778	93,061	115,966
Cash and cash equivalents at end of financial year	**26,747**	**26,124**	**28,081**	**31,293**	**39,770**	**55,041**	**72,778**	**93,061**	**115,966**	**141,577**

This LTFS includes the proposed introduction of a waste service charge which improves cash flow and allows for debt repayment. Debt levels are relatively high. This LFTS provides Council with the capacity to fund its day to day operations and provide a reasonable cash surplus to enable a high level of self-financing of its capital works program and new initiatives.

The following table outlines key financial indicators, suggested long term target ratios for Yarra and performance as outlined in the LTFS. Graphical representations of these indicators are shown below the following table. The target range for the indicators have been developed considering the Victorian Auditor General's financial sustainability indicators (subject to change)

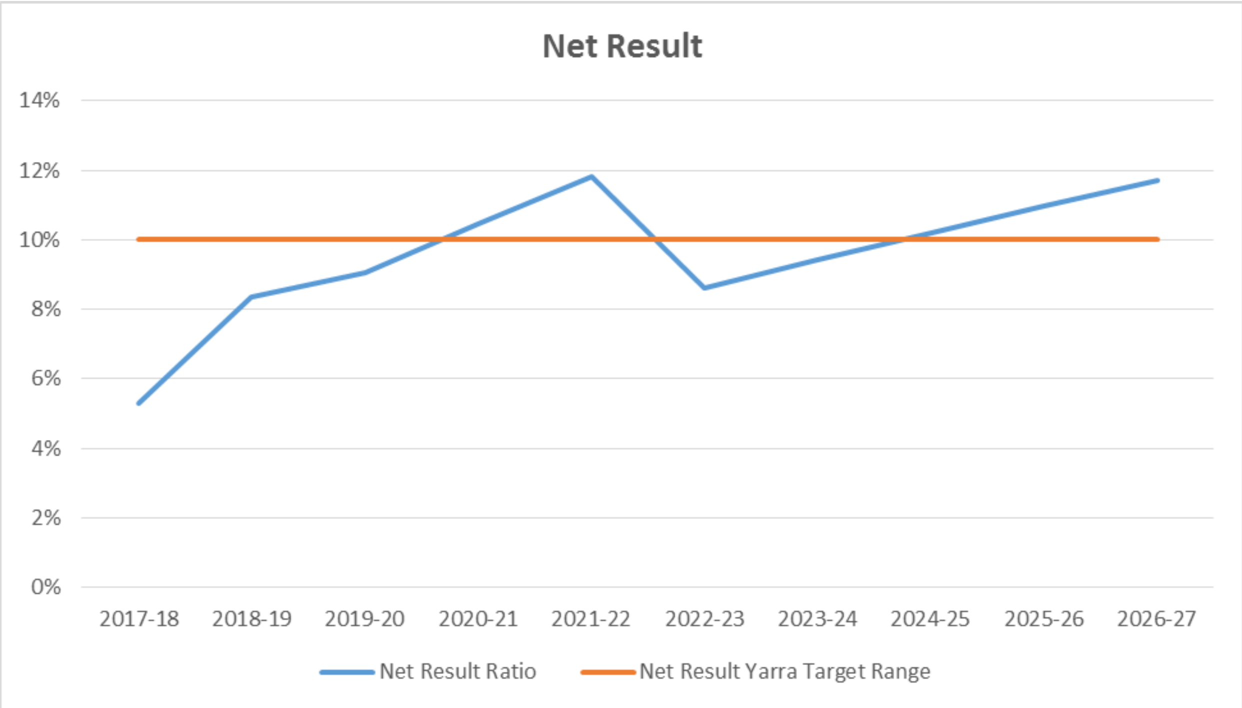
Further improvement to the City's financial position is required to attain the long term targets for financial sustainability.

Table 5 Estimated Key Financial Indicators

LTFS	Yarra Target	Year 1 2017-18	Year 2 2018-19	Year 3 2019-20	Year 4 2020-21	Year 5 2021-22	Year 6 2022-23	Year 7 2023-24	Year 8 2024-25	Year 9 2025-26	Year 10 2026-27
Net Result	>10%	5%	8%	9%	10%	12%	9%	9%	10%	11%	12%
Liquidity	>1.5	1.17	1.08	1.08	1.14	1.11	1.40	1.78	2.20	2.67	3.18
Unrestricted Cash	>75%	4%	15%	19%	25%	48%	84%	125%	171%	221%	285%
Debt Commitment	<5%	2%	2%	2%	2%	0%	0%	0%	0%	0%	0%
Indebtedness	<30%	29%	22%	17%	12%	5%	4%	3%	2%	2%	1%
Self Financing	>25%	90%	117%	129%	138%	140%	112%	117%	122%	127%	132%
Renewal Gap	>1.1	1.8	1.4	1.5	1.4	1.3	1.8	1.8	1.8	1.6	1.6
Capital Replacement	>1.5	1.8	1.6	1.5	1.5	1.5	1.6	1.6	1.6	1.6	1.6

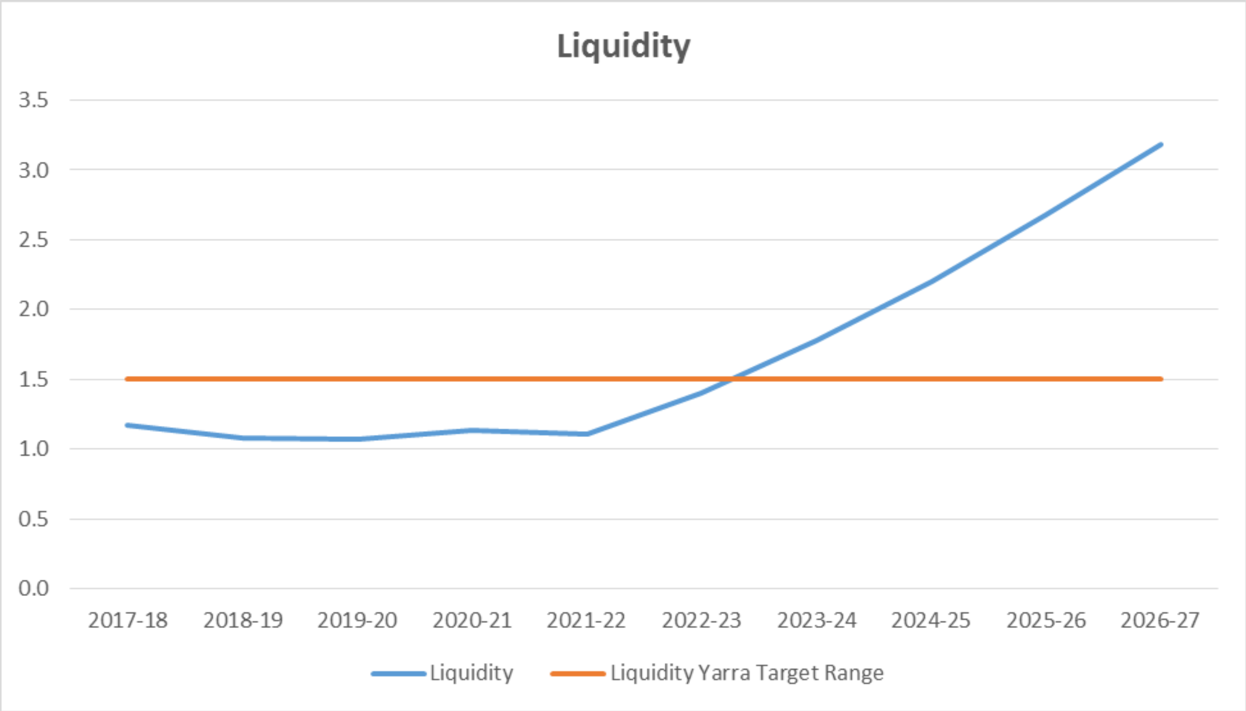
GRAPHS:

Graph 1 – Net Result



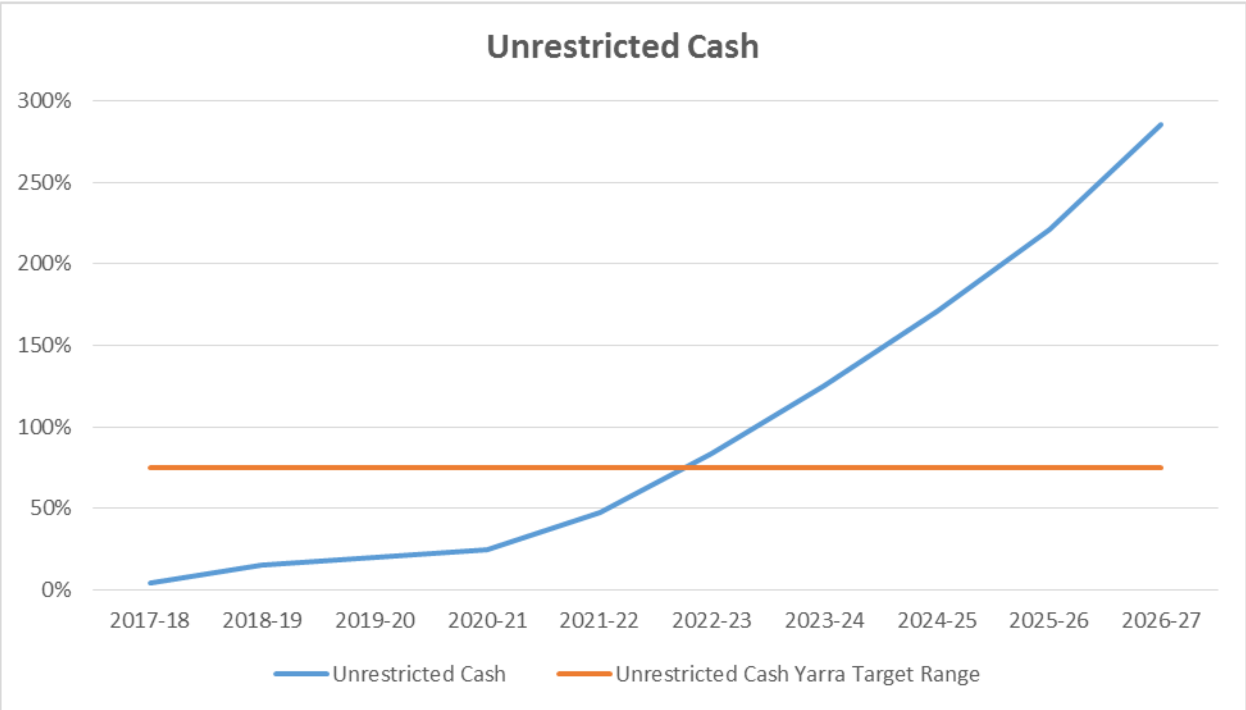
An indicator of the sustainable operating result required to enable Council to continue to provide core services and meet its objectives. Ideally the blue line should exceed the target orange line.

Graph 2 – Liquidity



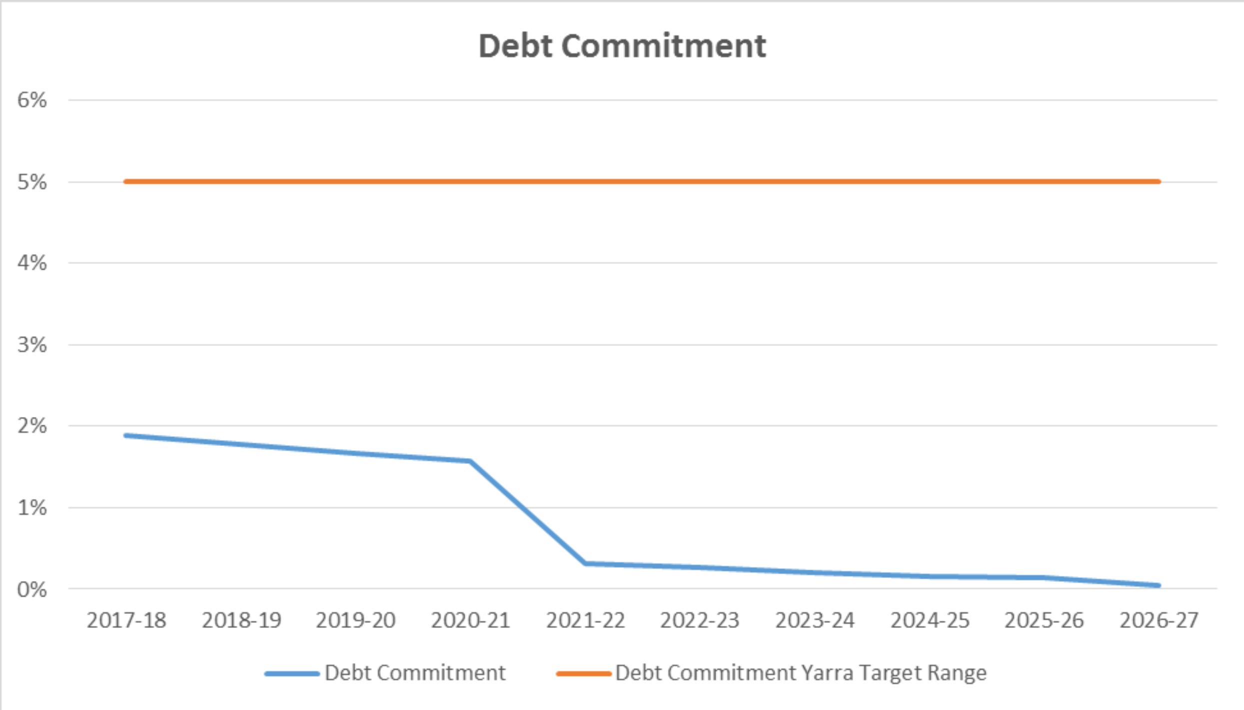
To assess Council's ability to meet current commitments. Ideally the blue line should exceed the target orange line.

Graph 3 – Unrestricted Cash



To assess Council's freely available cash level. Ideally the blue line should exceed the orange line.

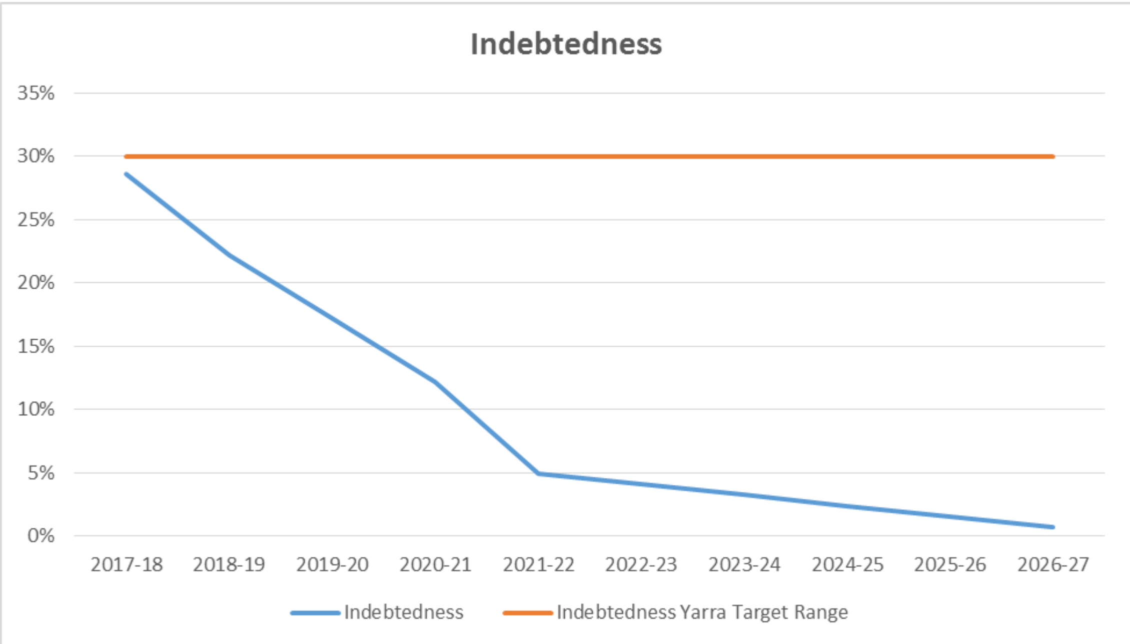
Graph 4 – Debt Commitment



To identify Council's debt redemption strategy. Ideally the blue line should **not** exceed the target orange line.

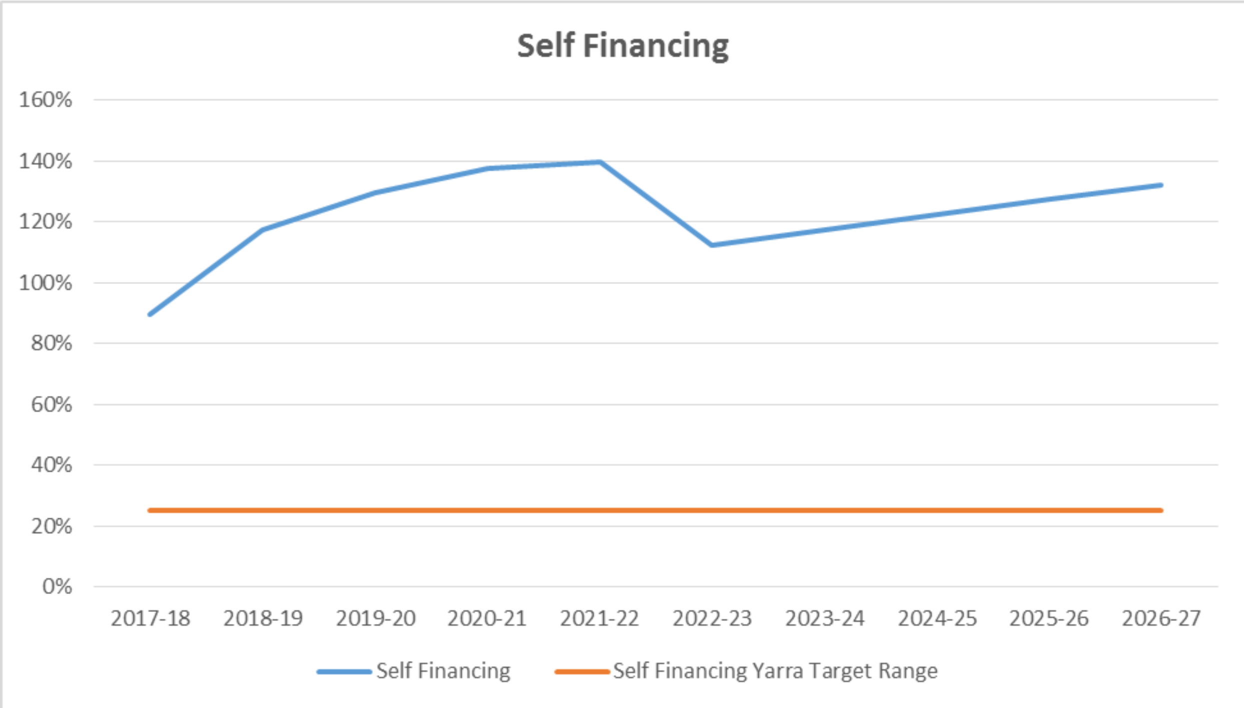
The reason for the decrease in Debt Commitment in Year 6 is due to an additional principal repayment

Graph 5 – Indebtedness



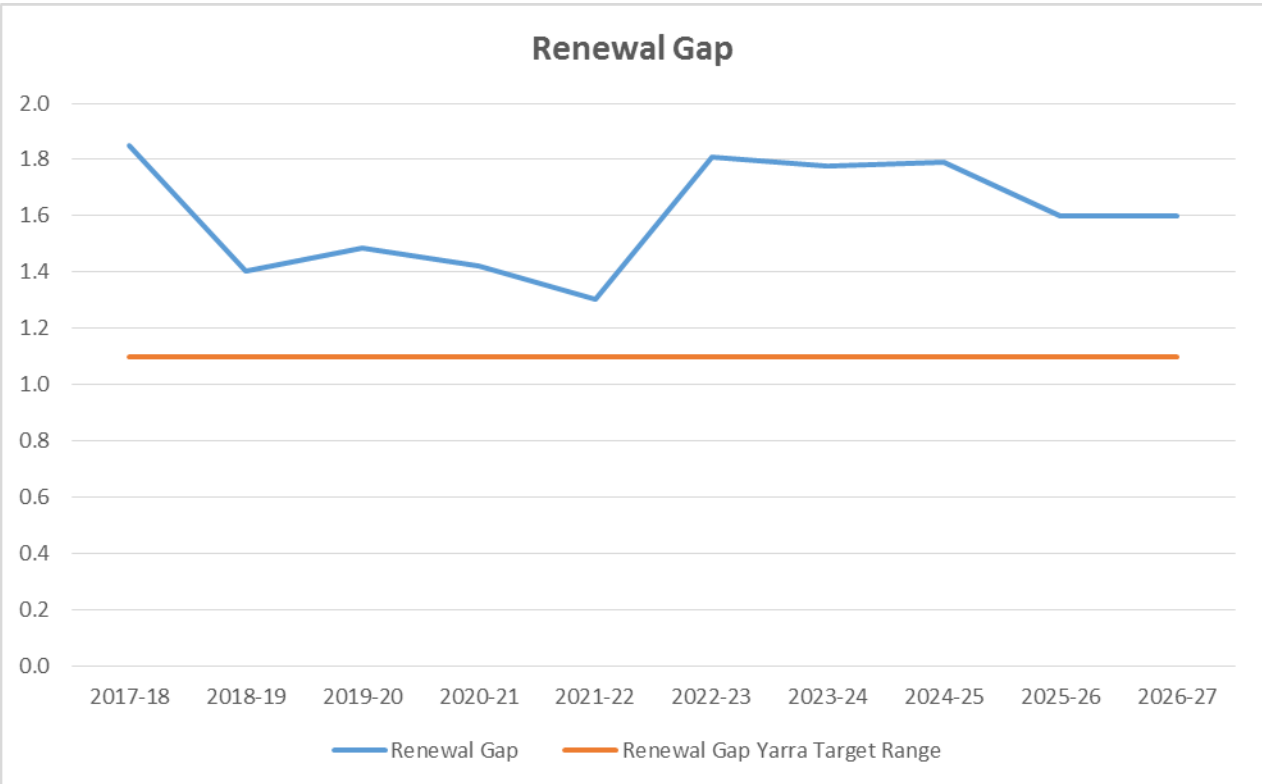
To identify reliance on debt to fund capital programs. Ideally the blue line should **not** exceed the target orange line.

Graph 6 – Self Financing



To identify reliance on debt to fund capital programs. Ideally the blue line should exceed the target orange line.

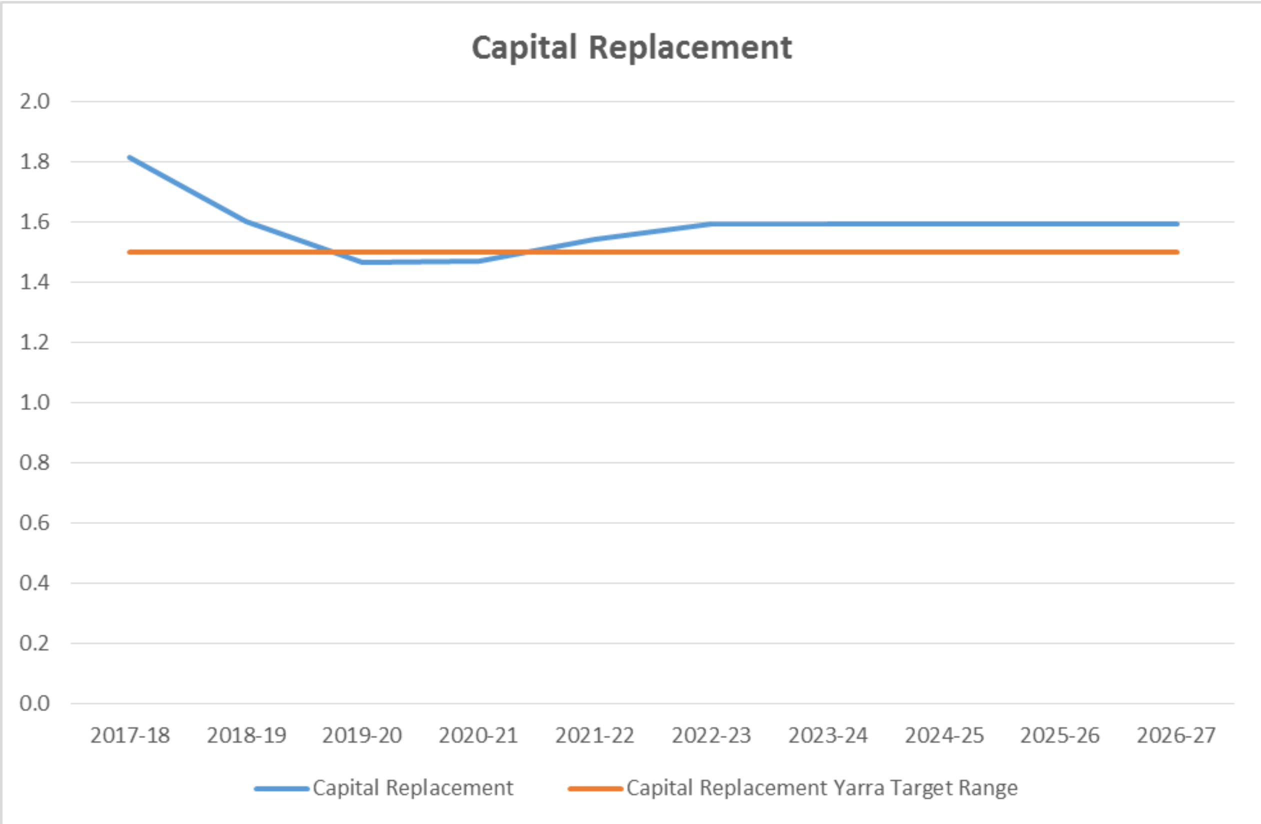
Graph 7 – Renewal Gap



To assess Council's ability to renew assets as required. Ideally the blue line should exceed the target orange line.

The renewal gap appears to be trending positively however anecdotal evidence suggests that asset renewal is not meeting community expectations in all circumstances e.g. leisure centre infrastructure.

Graph 8 – Capital Replacement



Measures the replacement of assets is consistent with their consumption. Ideally the blue line should exceed the target orange line.

The challenge for Council will be to improve its overall financial sustainability by improving the performance of the key financial indicators.

APPENDIX 1 KEY FINANCIAL INDICATORS DESCRIBED

Indicator	**Description**	**Long Term Target Range for Yarra**
Adjusted Underlying Result	An indicator of the sustainable operating result required to enable Council to continue to provide core services and meet its objectives. <u>Adjusted underlying surplus</u> Adjusted underlying revenue A positive result indicates a surplus. VAGO High Risk = less than negative 10% Medium Risk = Negative 10% to zero Low Risk = Greater than 10%	More than 10%
Liquidity	To assess Council's ability to meet current commitments. <u>Current assets</u> Current liabilities A percentage higher than 100% means that there is more cash and liquid assets than short term liabilities VAGO High Risk = less than 75% Medium Risk = 75% to less than 100% Low Risk = greater than 100%	Greater than 150%
Unrestricted Cash	To assess Council's freely available cash level. <u>Unrestricted cash</u> Current liabilities VAGO High Risk = less than 10% Low Risk more than 10% Target based on Local Government Performance and Reporting Indicators	Greater than 75%
Debt Commitment	To identify Council's debt redemption strategy. <u>Debt servicing and redemption costs</u> Rate Revenue Debt redemption includes loan and finance lease principal and interest as a percentage of rate revenue Local Government Performance and Reporting Indicators	Less than 5%
Indebtedness	Indicates reliance on debt to fund capital programs. <u>Non-current liabilities</u> Own sourced revenue The higher the percentage the less able to cover non-current liabilities from revenue generated by Council	Less than 30%

Indicator	**Description**	**Long Term Target Range for Yarra**
	VAGO High Risk = more than 60% Medium Risk = 40% - 60% Low Risk = less than 40%	
Self-Financing	Indicates reliance on debt to fund capital programs. <u>Net operating cash flows</u> Underlying revenue VAGO High Risk Less than 10% Medium Risk 10% - 20% Low Risk = Greater than 20%	Greater than 25%
Investment Renewal Gap	To assess Council's ability to renew assets as required. <u>Asset renewal expenditure</u> Depreciation A percentage greater than 100 indicates that Council is maintaining its existing assets. If there has been a past gap in renewal a percentage of greater than 100 is desirable. VAGO High Risk = less than 50% Medium Risk = 50% - 100% Low Risk = greater than 100%	Greater than 110%
Capital Replacement	Measures the replacement of assets is consistent with their consumption. <u>Capital expenditure</u> Depreciation VAGO High Risk Less than 100% Medium Risk 100% - 150% Low Risk Greater than 150%	Greater than 150%

Target ranges have been assessed with reference to the VAGO and Local Government Performance and Reporting Indicators.

APPENDIX 2 CASHFLOW PARAMETER ASSUMPTIONS

CATEGORY	2017 LTFS	2018 LTFS	YR 3 -10 LTFS	REASON
Rate Revenue	99.5% plus prev year opening debtor balance	99.5% plus prev year opening debtor balance	99.5% plus prev year opening debtor balance	Current collection rate. Opening debt stable or improving.
Parking Enforcement	90% Plus 10% parking debt	90% Plus 10% parking debt	90% Plus 10% parking debt	Current trend based on collection for infringements. Other income from meters and permits is cash.
Other charges fees & fines (debtors)	97.5% Plus 10% opening debt	97.5% Plus 10 % opening debt	97.5% Plus 10 % opening debt	Opening debt relatively stable number.
Employee Costs	97.5%	97.5%	97.5%	Current staffing trend at near full employment.
Government Grants	100%	100%	100%	Collection history.
Capital Works Program	100% including carry forward	100% including carry forward	100% including carry forward	Historical trend.
Payments to Suppliers	100%	100%	100%	Variation in Balance Sheet holdings of payables and accruals.

APPENDIX 3 FINANCIAL STRATEGY PRINCIPLES

The Financial Strategy Principles provide the framework for the development of Council's Long Term Financial Strategy, and annual Budget development. The principles enable consistent and informed decision-making by the Council.

The Financial Strategy Principles are outlined below:

Balanced and Sustainable Budget

Council will:

- Implement a sustainable budget and conservative financial strategy that caters for short and long-term requirements
- Achieve a Liquidity Ratio of +150% to ensure the maintenance of the required level of cash to meet operational requirements and strengthen this position over the years of the LTFS. (aspirational target)
- Maximise the level of grants and subsidies received from Victorian and Commonwealth governments to achieve a better share of government taxes for the community.
- Debt servicing and debt redemption will be maintained within the financial capacity of Council reflected in a cap on indebtedness (P&I) of less than 40%
- Direct funds from asset sales to the purchase of new, upgrade assets or re-establishment of working capital
- Trust Funds and Statutory Reserves will be fully cash backed at 30 June each year (aspirational target)

Asset management

Council will

- Provide well-maintained community assets that are fit for their purpose and provide best possible community benefit. Council will commit an appropriate level of expenditure on asset renewal and give priority to asset renewal over new assets.
- Ensure that the community has access to required community infrastructure, located to meet community needs within a framework of city wide priorities and designed with regard to current and future needs.
- Fund capital expenditure in a prudent, ethical and responsible manner. Council will seek and accept external funding contributions to a project where the acceptance of the funding will not compromise Council's principles or objectives.
- Manage, acquire and dispose of property in the best interest of the community. Council recognises the importance of efficient use of property holdings over the long term to support community wellbeing.

APPENDIX 4 OPERATING AND CAPITAL ACTIVITIES

Income Statement	Year 1	Year 2	Year 3	Year 4	Year 5	Year 6	Year 7	Year 8	Year 9	Year 10
	2017-18	2018-19	2019-20	2020-21	2021-22	2022-23	2023-24	2024-25	2025-26	2026-27
	$'000	$'000	$'000	$'000	$'000	$'000	$'000	$'000	$'000	$'000
Revenue										
Rates - general	(113,658)	(117,711)	(121,852)	(126,083)	(130,406)	(134,823)	(139,336)	(143,948)	(148,660)	(153,476)
Grants-Capital	(1,195)	(1,207)	(1,231)	(1,256)	(1,269)	(1,281)	(1,294)	(1,307)	(1,320)	(1,333)
Grants-Operating	(12,023)	(13,225)	(14,548)	(16,003)	(16,163)	(16,324)	(16,488)	(16,652)	(16,819)	(16,987)
Contributions - cash	(4,300)	(4,300)	(4,300)	(4,300)	(4,300)	(4,300)	(4,300)	(4,300)	(4,300)	(4,300)
Statutory fees and fines	(28,534)	(28,819)	(29,395)	(29,984)	(30,484)	(30,984)	(31,484)	(31,984)	(32,484)	(32,984)
User fees	(27,064)	(27,334)	(27,881)	(28,439)	(28,939)	(29,439)	(29,939)	(30,439)	(30,939)	(31,439)
Reimbursements	(1,640)	(1,699)	(1,819)	(1,942)	(2,004)	(2,024)	(2,045)	(2,065)	(2,086)	(2,107)
Interest	(500)	(500)	(500)	(500)	-	-	-	-	-	-
Other revenue	(1,207)	(1,294)	(1,345)	(1,418)	(1,432)	(1,447)	(1,461)	(1,476)	(1,490)	(1,505)
Total Revenue	**(190,121)**	**(196,089)**	**(202,871)**	**(209,924)**	**(214,996)**	**(220,622)**	**(226,346)**	**(232,171)**	**(238,098)**	**(244,131)**
Expenses										
Employee Costs	80,639	82,252	83,897	85,575	87,286	89,032	90,813	92,629	94,481	96,371
Materials & services	69,085	69,754	71,110	72,493	73,198	73,910	74,629	75,355	76,089	76,830
Bad and doubtful debts	2,010	1,980	1,950	1,920	1,980	2,040	2,100	2,160	2,220	2,280
Depreciation & amortisation	20,664	22,432	22,881	23,338	23,838	24,338	24,838	25,338	25,838	26,338
Finance costs	2,139	2,088	2,035	1,980	410	349	286	219	149	76
Total Expenses	**174,537**	**178,506**	**181,873**	**185,305**	**186,712**	**189,669**	**192,665**	**195,701**	**198,777**	**201,895**
Adjustments										
WDV of assets sold	500	500	500	500	500	500	500	500	500	500
Proceeds from sales	(800)	(697)	(692)	(687)	(682)	(675)	(670)	(667)	(660)	(655)
Net gain/(loss) on disposal of property, infrastructure, plant and equipment	**(300)**	**(197)**	**(192)**	**(187)**	**(182)**	**(175)**	**(170)**	**(167)**	**(160)**	**(155)**
Net (Surplus)/Deficit	**(15,884)**	**(17,780)**	**(21,190)**	**(24,806)**	**(28,466)**	**(31,128)**	**(33,851)**	**(36,637)**	**(39,481)**	**(42,391)**
Net Asset Revaluation Increment	(50,339)	-	(52,204)	-	(52,726)	-	(53,253)	-	(53,786)	-
Comprehensive Result	**(66,223)**	**(17,780)**	**(73,394)**	**(24,806)**	**(81,192)**	**(31,128)**	**(87,104)**	**(36,637)**	**(93,267)**	**(42,391)**

OPERATING ACTIVITIES REVENUE

RATE REVENUE

Council no longer has control over its rate revenue as it is limited in future years by the direction imposed by the Minister for Local Government under rate capping. Current estimates are outlined below:

Table 6 Rates & Charges Estimates

LTFS	Year 1	Year 2	Year 3	Year 4	Year 5	Year 6	Year 7	Year 8	Year 9	Year 10
	2017-18	2018-19	2019-20	2020-21	2021-22	2022-23	2023-24	2024-25	2025-26	2026-27
	$'000	$'000	$'000	$'000	$'000	$'000	$'000	$'000	$'000	$'000
Rate Revenue	104,058	107,771	111,558	115,421	119,362	123,381	127,481	131,662	135,927	140,278
Supplementary Rates	1,100	1,100	1,100	1,100	1,100	1,100	1,100	1,100	1,100	1,100
Waste Service Charge	8,500	8,840	9,194	9,561	9,944	10,342	10,755	11,185	11,633	12,098
Total Rates & Charges	**113,658**	**117,711**	**121,852**	**126,083**	**130,406**	**134,823**	**139,336**	**143,948**	**148,660**	**153,476**

Supplementary Rates are additional rate income raised as a result of growth in new or extended properties or by change of land use under the planning scheme.

FEES AND CHARGES

Fees and Charges assist Council to offset the cost of some service delivery directly with the user rather than funding through rate income. If fees and charges income reflects the movement in Council costs and particularly wages costs this will generally mean that the user will continue to contribute the same proportion of the costs. Hence the movement of average wages has been used to predict these costs.

Statutory Charges are not within Council's control and these generally do not reflect movements in staff costs but at CPI. Some statutory charges are also not indexed e.g. statutory planning and as result ad hoc adjustments to fees occur.

PARKING REVENUE

Parking revenue is a reflection of the statutory charges established by the State Government and also reflects the growing pressure on parking space within the City. Parking revenue can be influenced by many external factors such as economic conditions, clearway policy and fuel prices. A conservative approach to growth in this revenue source has been applied, recognising that it will continue to grow.

Table 7 Predicted trend in parking revenue

LTFS	Year 1	Year 2	Year 3	Year 4	Year 5	Year 6	Year 7	Year 8	Year 9	Year 10
	2017-18	2018-19	2019-20	2020-21	2021-22	2022-23	2023-24	2024-25	2025-26	2026-27
	$'000	$'000	$'000	$'000	$'000	$'000	$'000	$'000	$'000	$'000
Parking Revenue	28,534	28,819	29,395	29,984	30,484	30,984	31,484	31,984	32,484	32,984

Note these amounts include the introduction of sensor technology in Year 1 and 2.

Council's income from parking enforcement, permits and parking meter income is significant at $28.6 million (2016-17 budget) of total income or 16% of total revenue. Parking Revenue should improve following the implementation of the New Parking Technology during 2017-18 & 2018-19. An assumption on the increase in revenue has been built into year 1.

GOVERNMENT GRANTS - OPERATING

These grants are received from Commonwealth and State Governments in support of programs. The largest grant is the Victorian Grants Commission allocation of Commonwealth money. Council's entitlement to the Victorian Grants Commission is an "as of right" entitlement and no significant shift in allocation is expected. This grant has been frozen by the Commonwealth Government in previous years and has not been subject to CPI adjustment. This changes from 2017-18. Any increase will relate to changes in Yarra's population.

INTEREST INCOME

Interest income is based on predicted cash flow, cash balances and CPI.

OPERATING ACTIVITIES EXPENSES

EMPLOYEE COSTS

Employee benefits include all labour related expenditure including agency staff. Costs here are governed by Council's Enterprise Bargaining Agreement that is due for negotiation now and will influence the 2017-18 financial year (Year 1 of the LTFS). From years 2-10 an estimate has been provided that is based on predicted average weekly earnings increases. Any restructuring of the workforce will need to be managed within the existing labour allocations with restructuring costs to be absorbed plus an allowance is also made for movement in banding entitlements.

No allowance has been made been made for the impact of expected population and dwelling growth on the labour budget.

No allowance has been made for further contributions to the Local Government Defined Benefits Scheme (Vision Super).

CONTRACTS

Contract costs generally increase in excess of CPI inflation reflecting the growth in average weekly wages and material costs.

MATERIALS AND SERVICES

These relate to a range of goods and services including utilities, insurance, consultants, legal fees, telecommunications and maintenance.

A reduction of $500,000 in materials and services as an efficiency dividend is included in 2017-18 and extended through years 2-10.

Legal fees are a significant component of Material and Services and these costs are often outside Council's control. Increased development pressure is also generating increases in legal costs associated with VCAT appeals.

Council's contribution to community through its annual and service grants is a large proportion of this cost (Total community grants budget in 2017-18 is $1.9 million plus other contributions of $1.46 million).

The State Government also imposes a Waste Levy on Council to encourage enhanced environmental practice across the State and historically has been increasing at around 10% per annum.

DEPRECIATION

Depreciation is forecast to increase by 2% per annum from year 2.

DOUBTFUL DEBTS

Doubtful debts are forecast to decrease across the LTFS.

GAIN/LOSS ON SALE OF ASSETS

An amount of $0.3 million has been allowed for loss on sale of assets in 2017-18, reducing to $0.2 million in 2018-19. This remains stable for the remainder of the LTFS.

CAPITAL WORKS PROGRAM

Table 8 Capital Works Program

Capital Works	Year 1	Year 2	Year 3	Year 4	Year 5	Year 6	Year 7	Year 8	Year 9	Year 10
	2017-18	2018-19	2019-20	2020-21	2021-22	2022-23	2023-24	2024-25	2025-26	2026-27
	$'000	$'000	$'000	$'000	$'000	$'000	$'000	$'000	$'000	$'000
Renewal	24,605	25,814	25,559	23,666	25,177	26,832	27,508	29,675	30,003	30,619
Upgrade	539	6,224	7,907	10,865	4,795	3,428	1,990	2,120	2,820	1,825
New	4,896	820	200	1,461	8,028	8,500	10,037	8,531	8,309	9,511
Carry-forwards	3,000	-	-	-	-	-	-	-	-	-
Total	**33,040**	**32,858**	**33,666**	**35,992**	**38,000**	**38,760**	**39,535**	**40,326**	**41,132**	**41,955**

These numbers also incorporate an update to the definition used for upgrade. Renewal of assets now includes improvements that bring existing assets to today's equivalent capacity or performance capability. For example replacement of a kitchen to today's standard. Upgrade of an asset is restricted to increase in asset capacity. Accordingly the mix of New, Upgrade and Renewal categories in each year has changed since the program was last presented to Council. This change assists to provide a more accurate representation of renewal expenditure which is an important financial indicator.

A review of classification of expenditure between Operating and Capital is also proposed. Currently a large transfer from Capital to Operating occurs as part of the end of year accounting adjustment and review of budget definitions will reduce this variance and better reflect the division of expenditure.

ASSET RENEWAL CAPITAL WORKS

Asset renewal has been incorporated with the LTFS in accordance with the adopted asset management plans. These include:

- Roads (including drainage)
- Buildings
- Open Space 2008 and under review
- Drainage to be separated and under review

Asset renewal expenditure has been indexed for CPI.

Information Technology requirements are based on the Information Systems Strategy. This Strategy is due for renewal in 2017.

Renewal expenditure has been reduced to reflect the move to leasing of motor vehicles.

In general Council's asset renewal requirements are being met however a renewal gap remains.

NEW AND UPGRADE CAPITAL WORKS

The New and Upgrade Capital Works program has been based on assessments undertaken for the 2017-18 Budget preparation.

APPENDIX 5 BALANCE SHEET ACTIVITIES

Balance Sheet	Year 1	Year 2	Year 3	Year 4	Year 5	Year 6	Year 7	Year 8	Year 9	Year 10
	2017-18	2018-19	2019-20	2020-21	2021-22	2022-23	2023-24	2024-25	2025-26	2026-27
	$'000	$'000	$'000	$'000	$'000	$'000	$'000	$'000	$'000	$'000
Current Assets										
Cash and cash equivalents	26,747	26,124	28,081	31,293	39,770	55,041	72,779	93,061	115,966	141,577
Trade and other receivables	14,335	15,023	15,802	16,675	17,545	18,413	19,279	20,143	21,006	21,868
Accrued Income	280	280	280	280	280	280	280	280	280	280
Prepayments	1,163	1,163	1,163	1,163	1,163	1,163	1,163	1,163	1,163	1,163
Inventories	130	130	130	130	130	130	130	130	130	130
Non Current assets classified as held for sale	696	696	696	696	696	696	696	696	696	696
Total Current Assets	43,350	43,416	46,152	50,237	59,584	75,723	94,327	115,473	139,241	165,714
Non-Current Assets										
Trade and other receivables	255	255	255	255	255	255	255	255	255	255
Property, plant and equipment, infrastructure	1,748,914	1758841	1821329.5	1833484	1899872	1913794	1981244	1995732	2064312	2079429
Total Non-Current Assets	**1,749,169**	**1,759,096**	**1,821,585**	**1,833,739**	**1,900,127**	**1,914,049**	**1,981,499**	**1,995,987**	**2,064,567**	**2,079,684**
Total Assets	**1,792,519**	**1,802,512**	**1,867,737**	**1,883,976**	**1,959,711**	**1,989,772**	**2,075,826**	**2,111,460**	**2,203,808**	**2,245,398**
Current Liabilities										
Trade and other payables	17,311	17,311	17,311	17,311	17,311	17,311	17,311	17,311	17,311	17,311
Trust funds and deposits	6,195	6,195	6,195	6,195	6,195	6,195	6,195	6,195	6,195	6,195
Income in advance	223	223	223	223	223	223	223	223	223	223
Provisions	15,215	15,409	15,629	15,874	16,130	16,432	16,815	17,314	17,965	18,806
Interest bearing loans and borrowings	1,142	1,195	1,250	5,713	1,369	1,433	1,500	1,569	1,642	0
Total Current Liabilities	**40,086**	**40,333**	**40,608**	**45,316**	**41,228**	**41,594**	**42,044**	**42,612**	**43,336**	**42,535**
Non-Current Liabilities										
Provisions	1,416	1,416	1,416	1,416	1,416	1,416	1,416	1,416	1,416	1,416
Other Liab	585	585	585	585	585	585	585	585	585	585
Interest bearing loans and borrowings	37,267	29,233	20,788	7,514	6,144	4,711	3,212	1,642	0	0
Total Non-Current Liabilities	**39,268**	**31,234**	**22,789**	**9,515**	**8,145**	**6,712**	**5,213**	**3,643**	**2,001**	**2,001**
Total Liabilities	**79,354**	**71,566**	**63,397**	**54,831**	**49,374**	**48,306**	**47,256**	**46,256**	**45,337**	**44,536**
Net Assets	**1,713,165**	**1,730,946**	**1,804,339**	**1,829,145**	**1,910,337**	**1,941,466**	**2,028,569**	**2,065,204**	**2,158,471**	**2,200,862**
Equity										
Accumulated surplus	607,014	624,794	645,984	670,790	699,256	730,384	764,235	800,872	840,353	882,744
Reserves	1,106,152	1,106,152	1,158,356	1,158,356	1,211,082	1,211,082	1,264,335	1,264,335	1,318,121	1,318,121
Total Equity	**1,713,166**	**1,730,946**	**1,804,340**	**1,829,146**	**1,910,338**	**1,941,466**	**2,028,570**	**2,065,207**	**2,158,474**	**2,200,865**

BALANCE SHEET ASSETS

RECEIVABLES

Receivables (net) are forecast to be $14.3 million in 2017-18. This is anticipated to increase by 5% on average each year across the LTFS.

INVENTORY, ACCRUED INCOME, REPAYMENTS AND ASSETS HELD FOR SALE

The remaining current asset items have been left at forecast 2016-17 levels.

PROPERTY, INFRASTRUCTURE AND PLANT AND EQUIPMENT

Property, infrastructure and plant and equipment is based on forecasts for additions and disposals net of depreciation. An escalation factor of 5.0% has been allowed every two years from 2017-18 for the asset revaluation increment.

INVESTMENTS IN ASSOCIATES, OTHER RECEIVEABLES AND FINANCIAL ASSETS

The remaining non-current asset items have been left at forecast 2016-17 levels.

BALANCE SHEET LIABILITIES

PAYABLES

Payables are forecast to be $17.3 million in 2017-18 and remaining stable across the LTFS.

TRUST FUNDS

Trust funds are forecast to be $6.2 million in 2017-18 and remaining stable across the LTFS.

EMPLOYEE PROVISIONS (CURRENT AND NON-CURRENT)

Employee provisions are forecast to be $16.6 million in 2017-18 increasing to $20.2 million over the 10 year period.

INTEREST BEARING LOANS AND BORROWINGS

Loans are based on repayment schedules for two loans of $32.5 million and $13.5 million both repayable within the life of this LTFS.

OPEN SPACE RESERVE

The open space reserve is forecast to be fully acquitted during the 2017-18 financial year. This will continue through the 10 year period.