District Council of Franklin Harbour

Long Term Financial Plan 2021 - 2030

May 2021

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1. INTRODUCTION

The purpose of this Long Term Financial Plan ("LTFP") is to express, in financial terms, the activities that the District Council of Franklin Harbour ("Council") proposes to undertake over the medium to longer term to achieve its stated objectives as outlined in its Strategic Management Plan.

It is a guide for future action based on the longer-term impact of revenue and expenditure proposals. The aggregation of future intended outlays and anticipated revenues enables the accumulating overall financial implications to be readily identified and if warranted, for proposed future activities to be revised.

Long-term financial plans are particularly important for local governments as they are responsible for managing a high level of long-lived assets relative to their income base. A council may have long-periods with modest levels of asset renewal requirements and then other periods when very significant outlays are necessary. All councils need to generate revenue in an equitable manner over time and ensure they have capacity to finance peaks in asset management and other outlays when, and including by way of borrowings where, necessary.

The preparation of a LTFP generates improved information to guide decisions about the mix and timing of outlays on operating activities and additional assets and the funding implications of these. Without a soundly based LTFP, an organisation with significant asset management responsibilities is unlikely to have sufficient data to determine sustainable service levels and affordable asset stockholding strategies, appropriate revenue targets or optimal treasury management.

2. RELEVANT LEGISLATION

Local Government (Financial Management) Regulations 2011

5—Long-term financial plans

(1) A long-term financial plan developed and adopted for the purposes of section 122(1a)(a) of the Act must include—

- *(b) a summary of proposed operating and capital investment activities presented in a manner consistent with the note in the Model Financial Statements entitled Uniform Presentation of Finances; and*
- *(c) estimates and target ranges adopted by the council for each year of the long-term financial plan with respect to an operating surplus ratio, a net financial liabilities ratio and an asset sustainability ratio presented in a manner consistent with the note in the Model Financial Statements entitled Financial Indicators.*

(2) A long-term financial plan must be accompanied by a statement which sets out—

- *(a) the purpose of the long-term financial plan; and*
- *(b) the basis on which it has been prepared; and*
- *(c) the key conclusions which may be drawn from the estimates, proposals and other information in the plan.*

The information that follows satisfies the above regulations.

3. FINANCIAL STRATEGY

The LTFP is based on Councils current operating service levels as well as projected capital renewal expenditure obtained from Councils Asset Management Plan.

- Community Wastewater Management Schemes ("CWMS") charges are set at an appropriate level to ensure whole of life costs are recovered.

  There are currently two types of charges designed to achieve this being:

  - A service charge of $150 per unit per annum
  - A capital charge of $367 per unit per annum

  The capital charge is aimed at recouping the original construction cost of the Cowell CWMS and is being used to repay the debt incurred at the time of construction.

  The service charge is aimed at recouping the whole of life costs of running and renewing the Cowell CWMS as it wears out. In 2018-19 the service charge was reduced from $442 per unit per annum to $150 in recognition of the out of pocket expenses being incurred by rate payers required to enable them to connect to the mains. The intention was for this to be a short term arrangement with the service charge to be reinstated to the previous level in due course.

  Council have discussed this matter at length and feel that a phasing in strategy needs to be employed to return the service charge to the level required to recoup the whole of life costs of the Cowell CWMS. The Local Government Act requires this to happen. If the service charge were not increased to the previous level, then this would mean the shortfall in revenue required to cover the whole of life costs of the CWMS would be covered most likely from general rate revenue which would be seen as unfair to those ratepayers who do not receive the benefits of the CWMS.

  Accordingly, the long term financial plan has been prepared on the understanding that the service charge will be increased by $50 per annum plus CPI for each year within the five year period commencing 30 June 2023 and ending 30 June 2028.

- Additional revenue is included in the LTFP as a result of a number of initiatives that are outlined in the following table:

Revenue Stream	2021-22	2022-23	2023-24	2022-25
Marina rent/berth sales	12,000	24,000	30,000	36,000
Marina Café rent	8,500	15,000	15,000	15,000
Rate increase due to population growth	10,000	10,000	10,000	10,000
Port Gibbon Cabins x2	39,072	51,840	54,432	57,154
Camping fees	25,000	25,000	25,000	25,000
Additional camping Point Gibbon/ Rangeview	8,000	15,000	17,500	20,000
Forecast per Annum increase	**102,572**	**140,840**	**151,932**	**163,154**

  These estimates are believed to be conservative with the possibility existing that even larger revenue streams may eventuate once the foreshore redevelopment project is completed.

3. FINANCIAL STRATEGY con't

- Waste management user charges are set at an appropriate level to ensure the full cost of providing these services is recovered from those who benefit from the service.
- Council will continue to review service delivery to the community to identify any further opportunities to reduce operating costs due to increased operating efficiencies. This will be an ongoing objective for management to ensure the maximum benefit to the community per dollar of rates.
- Council will not undertake any further construction of upgraded or new assets over the next 10 years unless additional revenue is identified that will fund such upgrades. By committing to this strategy, Council will be able to allocate resources to replacing existing assets in a timely manner as well as minimising any increases in operating costs associated with additional assets. Should an upgrade program be agreed to, then a complete re-work of the LTFP will be undertaken to confirm Council will remain in a financially sustainable position after the completion of these works.
- Grant revenue will be targeted in a strategic manner. This means that grant revenue to build new assets would only be pursued and accepted if the new assets were deemed to have strategic significance, particularly, if additional funding was to be contributed by Council. Where an operating grant is sought and additional Council funds are required to be contributed, then careful consideration will be given to long-run benefits and costs. This will ensure activities that may better fit Council's strategic objectives are not being delayed in lieu of the activity being funded by the grant.
- The LTFP will be revised as part of the Annual Business Planning process each year.

4. KEY ASSUMPTIONS

The following assumptions have been built into the forecast calculations:

- The content of the LTFP is based on real (2020-21) dollar values for all future years to facilitate comparisons between years.
- Forecast debt and cash reserves in future years have been discounted by 1.8% p.a. in recognition of the fact that inflation reduces the real value of financial assets and liabilities.
- Commonwealth Financial Assistance Grant ("FAGs") revenue is not expected to vary over the planning period. Timing of receipt of FAGs revenue has been assumed to be quarterly four times each year.
- Capital and maintenance expenditure on road renewal and plant and equipment matches expenditure requirements from the 10 year renewal programs.
- Capital expenditure renewal levels have been set to ensure assets are renewed in a timely manner that is consistent with Councils Asset Management Plan.
- Commonwealth Roads to Recovery funding is maintained at current levels throughout the planning period.
- Investment income has been calculated at 1.5% p.a. on the previous year's closing cash balance.

5. LONG TERM FINANCIAL SUSTAINABILITY – KEY FINANCIAL INDICATORS

Indicator 1 - Operating Surplus Ratio ("OSR")

The operating surplus ratio expresses the operating surplus (deficit) as a percentage of operating income.

Calculated as: (operating revenue minus operating expense) divided by operating revenue.

The OSR is used to confirm that Council can cover its operating expenditure and depreciation charge from its operating revenue. A negative result indicates that Council is not doing so.

Throughout the life of the plan, Council aims to achieve an operating result of within the range of 0% to 10% of operating revenue.

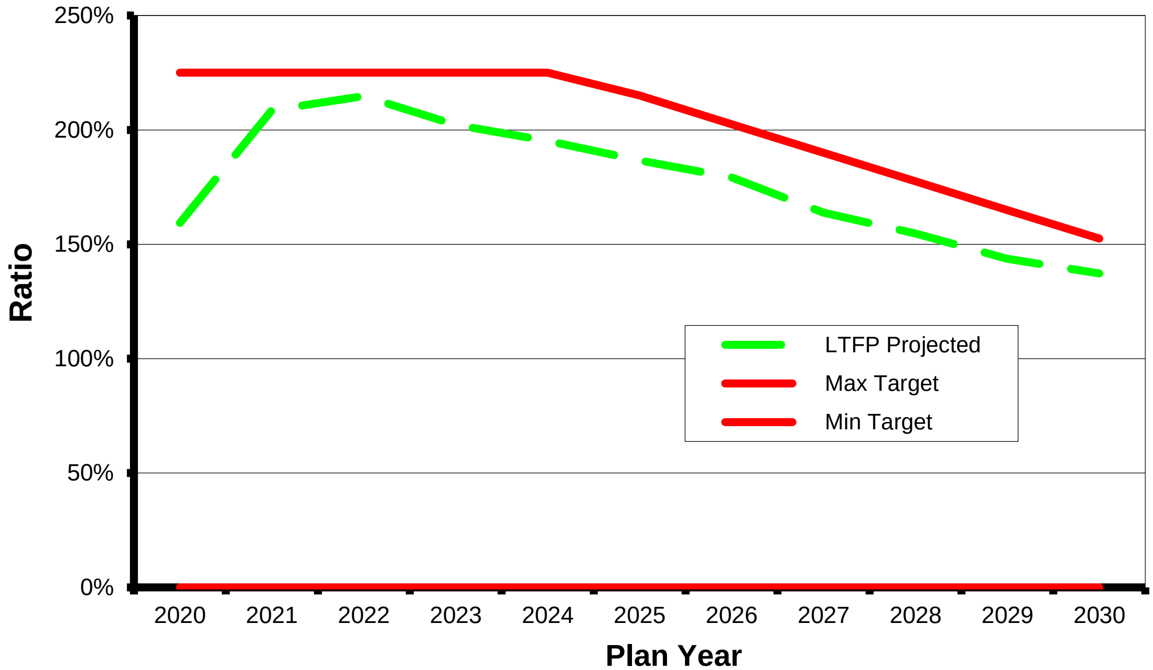
The above graph indicates that Council is in a strong operating position with operating income exceeding operating expenditure throughout the life of the plan.

The forecast surplus funds are a significant contributor to the reduction in the forecast net financial liabilities as demonstrated in the section that follows.

Indicator 2 - Net Financial Liabilities Ratio (NFLR)

Net financial liabilities is a comprehensive measure of the indebtedness of the Council as it includes items such as employee long-service leave entitlements and other amounts payable as well as taking account of the level of Council's available cash and investments. Specifically, Net Financial Liabilities equals total liabilities less financial assets, where financial assets for this purpose includes cash, cash equivalents, trade and other receivables, and other financial assets, but excludes equity held in Council businesses, inventories and land held for resale.

Council have set a maximum debt level of 225% of operating revenue for the first four years of the plan. Subsequent years upper limits have been progressively reduced at a rate consistent with the impact the financial strategy will have on the reduction of Net Financial Liabilities.



The following table of data informs the above graph:

	2020	2021	2022	2023	2024	2025	2026	2027	2028	2029	2030
Net Financial Liabilities	6,976	8,755	8,802	8,428	8,216	7,938	7,679	7,117	6,725	6,242	5,965
Total Operating revenue	4,377	4,197	4,099	4,168	4,210	4,253	4,284	4,347	4,347	4,347	4,347
NFLR	**159%**	**209%**	**215%**	**202%**	**195%**	**187%**	**179%**	**164%**	**155%**	**144%**	**137%**

At first glance it appears that Council has an excessive level of Net Financial Liabilities (NFL) forecast for the year ending 30 June 2022 when NFL peaks at $8.8M

There are a number of mitigating circumstances that need to be understood when assessing the manageability of such a high level of liabilities, being:

- The level of debt included in NFL that specifically relates to the construction of the Cowell CWMS in 2016-17. This has a dedicated revenue stream that is repaying this component of NFL.
- A notional provision of $2.3M is carried in the liabilities section of Councils balance sheet included in relation to deposits held on 17 licenses to occupy issued to various parties residing in the Cowell Cottages complex. The provision is carried to reflect the unlikely event where every resident leaves the complex at the same time and Council were required to repay all of the deposits at once. In reality this would never happen.

  Further to this there is an unrecognised financial asset being the actual license which would be available for resale should a resident leave.

  Finally, the current written down value of the land and buildings included in the non-current assets section of the balance sheet is $2.8M. In reality should this property ever need to be sold the market value would likely be well in excess of this amount.

The following analysis will demonstrate that the forecast level of NFL is manageable and that the financial strategy outlined in section 3 of this plan is consistently reducing NFL over time.

<u>Break down of NFL as of 30 June 2022:</u>

CWMS related Borrowings	$2.8M
Cowell Cottages Provision	$2.3M
Other Borrowings	**$3.7M**
Total NFL	$8.8M

Other Borrowings as a percentage of Operating Revenue = 90%

<u>Break down of NFL as of 30 June 2030:</u>

CWMS related Borrowings	$1.0M
Cowell Cottages Provision	$2.3M
Other Borrowings	**$2.6M**
Total NFL	$5.9M

Other Borrowings as a percentage of Operating Revenue = 60%

When assessing the level of other borrowings, it can be seen that even when NFL peak at $8.8M the underlying real level of borrowings to be repaid is only $3.7M or 90% of operating revenue. This is lower that the accepted ceiling level of NFLR of 100% used as a guideline by the local government sector in more normal circumstances.

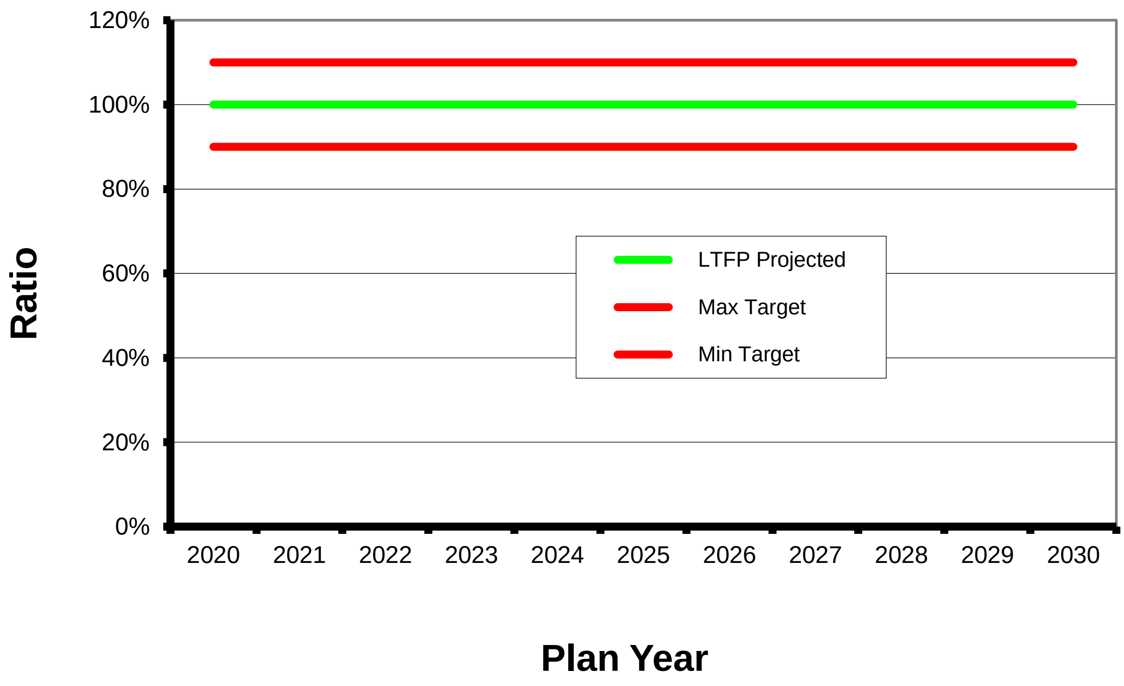
When considering NFL as of 30 June 2030 it can be seen that the financial strategy is having the desired effect as NFL reduces to $5.9M, with the other borrowings component reducing to $2.6M producing a NFLR of 60% that is well below the industry ceiling of 100%.

Indicator 3 - Asset Renewal Ratio ("ARR")

The ARR indicates the extent to which existing non-financial assets are being renewed and replaced, compared with what is needed to cost-effectively maintain service levels. It is calculated by measuring capital expenditure on renewal or replacement of assets, relative to the optimal level of such expenditure determined by Councils asset management data.

If capital expenditure on renewing or replacing existing assets is at least equal to the level proposed by Councils asset data, then a Council is ensuring optimal timing of replacement of physical assets to maintain service levels. Any material underspending on renewal and replacement over the medium term is likely to adversely impact on the achievement of preferred, affordable service levels and could potentially progressively undermine a Council's financial sustainability.

It is important to understand the difference between new/upgraded assets and renewal/ replacement assets. Only expenditure on renewal/replacement is included in the calculation of the asset renewal funding ratio. Minimal capital expenditure has been included in this plan to fund the construction of new assets from the year ending 30 June 2023 onwards. Refer further below for a full definition of new/upgraded assets and renewal/replacement assets.



The above graph demonstrates that Council is intending to fund capital renewals as identified in its asset renewal work programs.

Summary of Council’s Long-term Sustainability based on LTFP forecasts

The above key financial indicators point to Council operating in a sustainable manner over the life of the LTFP.

The OSR indicates Council is covering its operating expenses including depreciation over the life of the LTFP.

The LTFP funds capital renewal requirements as calculated based on Councils existing asset data. The ARR demonstrates that Council is replacing its infrastructure in a timely manner.

This report has clearly demonstrated that the financial strategy that underpins the LTFP is effective, thereby enabling the forecast NFLR is to reduce significantly over the life of this plan.

It is intended to update the LTFP annually as part of the annual business planning process.

6. STATEMENT OF UNIFORM PRESENTATION OF FINANCES

The Statement of Uniform Presentation of Finances together with the results of the Key Financial Indicators provides a summarised report that focuses on Council's finances at a strategic level.

Readers are strongly encouraged to take the time to comprehend how this report is structured and what the implications of the various lines of this report are for the Key Financial Indicator calculations.

The Statement of Uniform Presentation of Finances highlights the operating surplus / (deficit) measure which is considered the most critical indicator of a Council's financial performance.

The last line or rather the result of this report is the movement in Net Financial Liabilities (net lending / borrowing) for the year based on Council's planned capital and operating budgets for that year.

Achieving a zero result on the net lending / (borrowing) measure in any one year essentially means that the Council has met all of its expenditure (both operating and capital) from the current year's income (with income including amounts received specifically for new / upgraded assets).

New / Upgraded vs Renewal / Replacement of Assets

A clear understanding of the difference between expenditure incurred to renew or replace existing assets and expenditure incurred to create new or upgraded assets is essential in order to understand the strategic relevance of the Statement of Uniform Presentation of Finances.

A **new asset** is additional to Council's previous asset complement.

For example, roads constructed as part of a Council owned subdivision are new assets. Similarly, laying footpaths in areas where they did not previously exist are also new assets.

An **upgraded asset** replaces a previously existing asset with enhanced capability or functionality.

Renewal or replacement of an asset occurs where a previously existing asset is replaced without enhancement of the service capability except where this is incidental and unavoidable.

It is possible for capital expenditure to be a combination of renewal as well as upgrade. This is particularly prevalent in this Council region due to the increased volume of B-double traffic experienced in recent times. This has required existing roads to be rebuilt to higher standards.

For example, the replacement of a road that was initially a 6 metre wide sheeted surface with an 8 metre width sheeted surface can be considered part replacement and part upgrade.

The important point to understand is that if Council is not able to replace its existing assets in a timely manner, then new assets should not be built unless essential. By building new assets Council is effectively building new liabilities as the assets usually do not generate revenue (e.g. roads), cannot be sold and will need to be maintained and eventually replaced.

Uniform Presentation of Finances	2020 Year 0 Actual $'000	2021 Year 1 Budget $'000	2022 Year 2 Plan $'000	2023 Year 3 Plan $'000	2024 Year 4 Plan $'000	2025 Year 5 Plan $'000	2026 Year 6 Plan $'000	2027 Year 7 Plan $'000	2028 Year 8 Plan $'000	2029 Year 9 Plan $'000	2030 Year 10 Plan $'000
Operating Revenues	4,377	4,197	4,099	4,168	4,210	4,253	4,284	4,347	4,347	4,347	4,347
less Operating Expenses	3,759	4,023	3,990	4,007	4,086	4,077	4,065	4,055	4,033	4,020	4,005
Operating Surplus/(Deficit) before Capital Amounts	**618**	**174**	**109**	**161**	**124**	**176**	**219**	**292**	**313**	**327**	**342**
LESS: Net Outlays on Existing Assets											
Capital Expenditure on Renewal or Replacement of Existing Assets	2,119	1,134	1,198	1,195	1,406	1,324	1,406	1,127	1,360	1,233	1,443
less Depreciation, Amortisation & Impairment	(988)	(982)	(1,158)	(1,205)	(1,205)	(1,205)	(1,205)	(1,205)	(1,205)	(1,205)	(1,205)
less Proceeds from Sale of Replaced Assets	(58)	(140)	(91)	(92)	(185)	(121)	(145)	(101)	(153)	(110)	(108)
Net Outlays on Existing Assets	**1,073**	**12**	**(51)**	**(102)**	**16**	**(2)**	**56**	**(179)**	**2**	**(82)**	**130**
LESS: Net Outlays on New or Upgraded Assets											
Capital Expenditure on New/Upgraded Assets	2,917	7,035	1,900	0	0	0	0	0	0	0	0
less Amounts Specifically for New/Upgraded Assets	(2,215)	(5,093)	(1,583)	0	0	0	0	0	0	0	0
less Proceeds from Sale of Surplus Assets	(270)	0	0	0	0	0	0	0	0	0	0
Net Outlays on New or Upgraded Assets	**432**	**1,942**	**317**	**0**	**0**	**0**	**0**	**0**	**0**	**0**	**0**
EQUALS: Net Lending / (Borrowing) for Financial Year	**(887)**	**(1,780)**	**(158)**	**264**	**108**	**178**	**163**	**471**	**311**	**409**	**212**

Conclusion

The ‘Net Lending / (Borrowings) for the Financial Year’, represents the movement in Councils’ net financial liabilities from one year to the next.

If the result for any given year is in brackets, then this identifies the amount of cash that is required to fund the capital and operating expenditure budgets after considering all available cash inflows for the year. Such a result would lead to an increase in borrowings.

Alternatively, any amounts that are not in brackets identify the amount of money that is surplus to Councils needs for the year as the forecast cash inflows would be greater than the forecast operating and capital expenditure requirements. Such a result would lead to a decrease in borrowings.

When reviewing the financial years ending 30 June 2020 to 30 June 2022 the uniform presentation of finances report shows that Councils net financial liabilities increase (as demonstrated by the results being in brackets) over this period as more cash is being spent than received in these years. When comparing this to the NFLR graph earlier in this report it is noted that the NFLR trends upwards during these years.

Conversely from the financial year ending 30 June 2023 onwards the uniform presentation of finances report shows that net financial liabilities reduce (as demonstrated by the positive results) over this period as less cash is being spent than received in these years. When comparing this to the NFLR graph earlier in this report it is noted that the NFLR trends downwards throughout these years.

Explanation / Examples of Components of Summary of Financial Position

Operating Revenue and Expenditure: represent the totals from the relevant lines of the Statement of Comprehensive Income (operating statement) for the year being reported on.

Capital Expenditure on renewal and replacement of Existing Assets: e.g., roads reseal, replacement tractor, building renovations, replacement computer hardware.

Proceeds from sale of replaced assets: e.g., trade in value of a tractor or motor vehicle being replaced.

Capital Expenditure on New and Upgraded Assets: e.g., constructing a new building, constructing a new catchment pond, purchasing a piece of machinery that was not previously on hand.

Amounts specifically for new or upgraded Assets: e.g., capital grants to partly fund a new CWMS, funds received to build new footpaths that did not previously exist.

Proceeds from Sale of Surplus Assets: proceeds from the sale of a council building that was no longer required, sale of surplus land.

REFERENCE MATERIAL

IPWEA Practice Note 6 – Long-term Financial Planning.

LGA Information Paper 9 – Local Government Financial Indicators

LGA Information Paper 12 – Targets for Local Government Financial Indicators

South Australian Local Government Model Financial Statements