10-YEAR FINANCIAL MANAGEMENT PLAN

KING ISLAND COUNCIL

INTRODUCTION

This long-term financial management plan is one of a number of a number of prescribed plans, strategies and policies required under the *Local Government Act 1993* (The Act), including:

- A strategic plan (s.66)
- An annual plan (s.71)
- Financial management strategies (s.70A)
- Long-term strategic asset management plans (s.70B)
- Asset management policies (s.70C)
- Asset management strategies (s.70D)

The Act requires the long-term financial management plan to be consistent with the strategic plan and the long-term strategic asset management plans.

PURPOSE

The purpose of the plan is to enable Councillors, staff and the community to take a long-term view of how Council's finances are best managed and planned to generate the revenue needed to meet annual service delivery and operational costs and long-term infrastructure maintenance and asset renewal costs.

The plan is also to assist Council achieve:

- equitable and efficient revenue raising, including intergenerational equity;
- compliant, prudent and transparent financial management; and
- long-term financial sustainability, including the ability to respond to and recover from unexpected financial impacts.

The plan provides a framework for Council's consideration of its annual plans and budgets and periodic reviews and updates of its strategic plan and asset management plans.

CONTEXT – KING ISLAND ECONOMY, JOBS AND POPULATION

Compared to most Tasmanian councils, King Island Council has a small, low growth property base on which to generate rate income. This constrains Council's capacity to raise rate revenue to deliver its core services, meet ever-increasing regulatory compliance obligations, and fund infrastructure and asset renewals.

The financial sustainability of Council is dependent on the sustainability of the Island's economy and State and Federal government policy.

The Island's economy is driven by its agriculture, fishing, mining and tourism industries, business services and government services, the size and scale of which are beyond Council's powers to control.

History shows that industry and business closures or marginal economic conditions can significantly impact Council's rate base and its capacity to raise revenue without necessarily reducing Council's infrastructure, service delivery and compliance commitments and costs.

Closures of the Scheelite mine in the early 1990s and the King Island Abattoir in 2009 are real world examples of events that negatively impacted the local economy, employment and population with flow-on impacts on Council's financial position.

The unpredictability of such events requires Council to closely monitor potential economic and social changes and be in a strong financial position to respond to and manage the change.

Council will seek to maintain a reasonable level of cash reserves to accommodate impacts on revenues and expenditures with a minimum of disruption. Council will also work with State and Commonwealth Governments to secure fair and equitable assistance.

Council will also continue to support the Island's existing industries which underpin the economy and its rate base as well as new appropriate and sustainable private and public investments to grow the economy and rate base to improve Council's financial sustainability.

BACKGROUND – FINANCIAL PERFORMANCE

Council uses two accounting methods to measure its annual financial performance. The first is the underlying statutory operating result (surplus/deficit), which includes depreciation. The second is the net underlying cash result.

Council's recent budgets have projected an underlying statutory deficit of between $450,000 in 2019/20 and $700,000 in 2018/19. A significant proportion of the deficit is due to waste management environmental compliance environmental compliance requirements and depreciation.

Council set a target in the latter half of 2020 to work to avoid deficit cash results from its operations. A cash surplus of $123,000 is forecast for 2019/20, which is a substantial improvement on the budgeted cash deficit of $432,759.

To offset the inability to fund depreciation from operational results, Council will seek grants to fund major infrastructure projects. In years in which grants are received for capital projects, a surplus operating result may be achieved.

10-YEAR ASSET MANAGEMENT PLAN

Council's draft Roads & Infrastructure Asset Management Plan sets out the 10-year commitments needed to maintain these assets in the most cost-effective manner and to upgrade and add new assets to meet demand.

The strategies in this financial plan provide for the continued investment in asset maintenance, renewal and replacement.

10-YEAR FINANCIAL MANAGEMENT PLAN

1. STATUTORY FINANCIAL COMPLIANCE

As a public authority, Council has obligations to manage and report its finances in accordance with the Act, accounting standards, audit requirements and other regulatory requirements such as those associated with grant funding.

Council also has a suite of financial policies to manage matters such as rates and charges, investments, financial reserves, financial IT systems, debt recovery, prevention of fraud, risk management and other related matters. The policies are subject to regular monitoring and review.

2. REVENUE SOURCES

2.1. GENERAL RATES

General rates are a property tax and the principal means Council has to raise revenue. Rates represent approximately 30% of Council's total revenue.

Council levies rates on the basis of a property's Assessed Annual Value (AAV) set by the Tasmanian Valuer-General, which are subject to periodic revaluations and adjustments.

Council ensures it only raises sufficient rate revenue to fund, together with other revenue sources, its legislative compliance obligations and its infrastructure, services and operational commitments. Council will also minimise increases by continuing to find and implement cost savings and efficiencies, including opportunities to resource share with the community and other councils.

It is important that Council maintains a stable and predictable approach to setting rates to enable ratepayers to plan and manage their finances with certainty and to ensure rate income keeps pace with general inflationary price increases as well as additional commitments imposed through government regulation or additional spending to meet community needs.

2.2. SERVICE RATES OR SPECIAL CHARGES

Service rates are a user charge applied by Council for delivery of a particular service such as waste collection. Service rates represent approximately 6% of Council's total revenue.

Service rates are calculated on a fee for service basis. Council will progressively consider this approach for all waste management services, consistent with the circular economy principle recommended in the King Island Waste Management Strategy 2019-2029.

In the event Council provides a service which is also provided by a private competitor, it must be charged at market rates.

2.3. USER AND STATUTORY CHARGES

User charges include aircraft landing fees at the airport, fees set in facility lease agreements with sporting and recreation groups, and commercial leases.

The user pays principle usually applies when setting rates. However, in the case of airport charges, Council takes into account the level of passenger and freight movements, the viability of full cost recovery fees, and the economic and social benefits the airport generates for the community.

Similarly, sporting and recreation lease charges are set at amounts that take into account the level of volunteer support provided by lessees and the social and economic benefits the community derives from these activities being available to existing and potential participants.

User charges represent approximately 10% of Council's total revenue.

Statutory charges include fees prescribed in legislation and regulation associated with a wide range of services, including planning, development and building permits, dog licences, public health and food safety licences and so on.

Statutory charges raise approximately 2% of Council's total revenue.

2.4. GENERAL PURPOSE GRANTS

The annual Federal Assistant Grant (FAG) is allocated to all councils as general-purpose, untied funding. Each council's allocation is based on a horizontal fiscal equalisation methodology implemented by the State Grants Commission in accordance with Commonwealth legislation.

While a component of the grant is set on a per capita basis, the major portion is calculated on measurable revenue and expenditure adjustments to achieve nominal equalisation between councils.

As Council faces significant revenue and expenditure disadvantages because of the island's size and isolation, the equalisation methodology generates a FAG contribution that represents 15% of its total revenue, which is higher than most other councils.

While the grant is untied, Council prioritises its allocation to address these disadvantages rather than initiate new projects or programs unrelated to the equalisation methodology.

While Council makes submissions to assist the State Grants Commission's deliberations, actual allocations are beyond Councils control and can materially impact its total revenue and spending capacity. It is for this reason Council needs to maintain a positive rate revenue raising effort and minimise potential risks should Commonwealth Government funding policies change.

2.5. ROAD GRANTS

Council, along with other councils, also receives annual road infrastructure funding under the Commonwealth Government's Roads to Recovery Program. This represents 6% of Council's total revenue.

These grants are an important source of revenue and are allocated to the maintenance, renewal and upgrade of Council's road and bridge infrastructure.

2.6. CAPITAL AND SPECIFIC PURPOSE GRANTS

Council also submits grant applications under State and Commonwealth Government programs and can receive one-off grants for specific purposes for projects or service programs. These grants should not be relied upon to achieve a sustainable balanced budget or to deliver core infrastructure asset and service delivery functions. Caution also needs to be exercised to ensure one-off grants do not create ongoing obligations that cannot be funded from Council's core rate, user charges and general-purpose grant revenue.

2.7. INTEREST ON INVESTMENTS AND OVERDUE RATE PAYMENTS

Interest derived from cash-at-bank and cash reserves provides another source of revenue for Council. It is difficult to estimate interest income over the 10-year period as it depends on the actual cash position during each financial year and applicable interest rates at the time, which vary according to prevailing market conditions.

Cash and investment balances are managed to meet anticipated expenditure commitments and ensure all current liabilities can be met as required.

Longer term investment of reserves not required for short term liquidity are made in accordance with Council's investments policy and aim to achieve the best possible return while ensuring the security of the funds. Income from these investments provide predictable returns and are incorporated in annual budget considerations.

Council also receives a small amount of income from interest and penalties paid on overdue rates and charges.

Overall, interest income provides less than 2% of Council's revenue.

2.8. DIVIDENDS

Council is a part-owner of the Tasmanian Water and Sewerage Corporation (TasWater) along with other Tasmanian councils and may receive a dividend in proportion to its contributed assets. Dividends are determined by the TasWater Board and vary according to TasWater's annual financial position and dividend policy.

Past dividend payments have reduced from $100,000 in 2018/19 to $30,000 in 2019/20 and zero in 2020/21, due to the impact of the COVID-19 emergency. It is expected there will be future dividend payments over the next 10-years but the quantum is difficult to estimate.

2.9. LOANS

The general purpose of loan borrowings is to fund major strategic infrastructure assets that provide long-term economic, social and environmental benefit for the community. Council's most recent loan borrowing was to fund an upgrade of the passenger terminal at the airport.

Council's small rate base and a generally low growth economy requires a cautious approach to loan borrowings over the next 10-years. A low or zero interest rate environment potentially enables Council to borrow and fund asset management and improvement priorities in its long-term infrastructure asset plan. Consideration of such a strategic borrowing program needs to include the capacity of the community to fund the repayment over the term of the loan and the ability of the community to fund maintenance and renewal of the asset during its expected life.

Consideration also needs to be given to managing the risks associated with an increase in interest rates, in which case a low debt environment would provide Council with a more secure and certain financial position.

2.10. PRIVATE WORKS

Council earns substantial revenue from private civil construction and maintenance works, including a contract with the State Government to maintain the state road network on the Island. As Council is competing with the private sector for this work, its charges reflect full cost recovery plus a market-driven profit margin. The profits are used to fund public works and services.

Revenue from private works represents approximately 20% of Council's total revenue.

2.11. OTHER REVENUE

The State Government provides Council with revenue collected from light vehicle registrations on the island. This represents approximately 7% of Council's total revenue. Council revenue is raised from a road user charge paid by the Naracoopa Sand Mine.

From time to time, Council may derive revenue from the sale of property or surplus plant and machinery. While Council owns four residential properties, no major property sales are planned during the 10-year period. However, it remains an option available to Council should the need arise and one-off funds generated would be included in the appropriate annual budget.

3. EXPENSES

In the delivery of Council functions, the major areas of expenditure are: employee costs; materials, contracts and other costs; and, State Government levies. Council's accounts also include depreciation, which is non-cash book entry.

3.1. EMPLOYEE COSTS

Council has a very small number of employees compared to most other Tasmanian councils. Given continued low growth in Council's rate base, it is expected that employee numbers will be generally maintained at this level over the next 10-years.

Employee costs include all salaries and wages and all employment related expenses including payroll tax, employer superannuation, leave entitlements, fringe benefit tax, workers compensation insurance and professional development. The total employee cost is expected to generally increase in line with inflation over the 10-year period.

3.2. MATERIALS, CONTRACTS AND OTHER COSTS

This category includes the purchase of consumables, payments to contractors for the provision of services, insurances, utility services, such as telecommunications, water, sewerage, and electricity; and finance costs.

Cost increases for these items are generally expected to be in line with inflation over the next 10-years.

3.3. STATE GOVERNMENT LEVIES

Council is required to pay the State Government land tax and state fire levies. State fire levies are collected from ratepayers on behalf of the State Fire Commission and represent approximately 1.5% of revenue collected. Council has no control over the extent of levies imposed by the Government.

3.4. DEPRECIATION

Depreciation is a non-cash item in Council's budget and recognises the value of an asset over its estimated useful life. Market valuations of major assets, including roads and the airport, are obtained from independent specialists.

Council calculates depreciation of its existing assets in accordance with national local government accounting standards and includes it in Council's underlying statutory operating result (surplus or deficit).

Depreciation is an indicative measure of the expense provision needed for asset renewal in any given year and is applied, in part, to indicate a council's financial sustainability.

Depreciation is not, however, an accurate measure of actual expenditure needed for asset renewal or replacement. Council's Asset Management Plans provide a more reliable estimate of expenditure required for inclusion in its annual budgets.

Council sources funds for its asset management commitments from rate income, fees and charges, grants and loan borrowings.

3.5. CAPITAL WORKS

Council adopts an annual capital works program to renew or replace infrastructure and other assets. This is to maintain the asset base and a consistent level of service.

Council aims to allocate sufficient resources to the program to meet commitments identified in the long-term asset management plan.

FINANCIAL MANAGEMENT

The aims of Council's Financial Management Plan are:

- to tightly manage revenue and expenses to ensure a balanced budget with sufficient cash-at-bank and in reserves to meet its debts, as and when they fall due;
- to fund asset renewals; and
- to manage the financial impacts from unexpected events.

This is challenging given Council's limited rate base, the Island's low growth economy and the ever-increasing regulation and compliance obligations imposed on Council.

The long-term strategies in this plan will assist Council in meeting this challenge.

Council will also establish, maintain and progressively update a model of Council's finances over a rolling 10-year timeframe. The model is to test and project financial results to be derived from detailed application of the strategies.

The model will project underlying statutory results, operating cash results and key indicators such as a net financial liabilities ratio and an indebtedness ratio.

The model results will form part of Council's consideration of each annual budget.