

29 April 2021

The Acting General Manager
Wingecarribee Shire Council
PO Box 141
Moss Vale NSW 2577

Dear Sir,

Review of Council Finances

In accordance with an engagement agreement dated 23 March 2021 we have been commissioned to undertake a review of Council's finances, specifically:

- a. Undertake an independent desktop review of the Council's financial position, resourcing strategy, maintenance of basic infrastructure, rates of depreciation versus asset replacement and the capacity to deliver projects identified in the Community Strategic Plan (more particularly the Operational Plan and Delivery Program).
- b. Special Rate Variation Approval May 2016 - A general review of expenditure under Council's two SRV's (Infrastructure Component & Continuation of Environment Levy) to ensure compliance with approvals.
- c. Civic Centre Refurbishment Project – A review of expenditure and confirmation that the project funding has been approved by the elected body.

Our review has been conducted with assistance of the Council's Finance Team. We would like to commend the CFO and his team for their valuable assistance in providing the necessary information and documentation during the course of the review and responding to queries in a timely manner.

From a governance perspective we have relied on Council resolutions and reports presented to Council. We have not considered reports, discussions or decisions that may have been part of Councillor workshops or private briefings.

A summary of our findings is available on pages 2-3 and recommendations arising from our review are included on page 20.

We would be happy to respond to any questions in relation to this review

Yours faithfully



Robert Finch
Finch Consulting

1. Executive Summary:

The Wingecarribee Shire Council was suspended by the NSW Minister for Local Government on 12 March 2021. Mr Viv May PSM was appointed Interim Administrator for a three-month period.

In a Council minute of 17 March, the Interim Administrator advised the community that he would request the Acting General Manager to commission a desktop review of Council's financial position. Since that date the terms of engagement have been expanded to include a review of the Special Rate Variation and Civic Centre expenditure.

A summary of our findings is as follows:

PAST FINANCIAL PERFORMANCE (Page 5)

- Council's audited Financial Statements for the last five years reported consolidated Operating Surpluses (before capital grants and contributions). A disaggregation of these results by Fund reveals that whilst Water and Sewer funds recorded surpluses, the General Fund recorded Operating Deficits over the same period.
- Past operating results in the General Fund have restricted Council's capacity to fully fund asset replacement and renewal and achieve published benchmarks for asset renewals. Published Infrastructure condition indicators reveal that the condition of key infrastructure assets has also declined over this five year period.
- Financial sustainability and the capacity to maintain and renew infrastructure was recognised by Council in 2016 and prompted a successful application to IPART for a Special Rate Variation (SRV) which would increase general rate revenue by 45% over five years and fund projects outlined in the 2017-2027 Resourcing Strategy.
- Delays in the delivery of maintenance and capital programs has contributed to Council not fully achieving the goals of the Resourcing Strategy.

CURRENT FINANCIAL POSITION (Page 10)

- The audited Financial Statements for the year ended 30 June 2020 demonstrate that Council's current financial position is sound.
- Key financial performance indicators are all generally close to or better than benchmark. As at 30 June 2020 the level of borrowings for the General Fund was relatively low and the Sewer Fund has manageable debt levels.
- Cash and Investment balances before funding reserves are relatively positive. However, Council's approach to authorising and funding Internal Restrictions should be reviewed to ensure adequate working capital balances.
- Under current market conditions, Councils investment portfolio is achieving minimal returns and therefore a policy review and utilisation of professional advice should be considered.

PROJECTED FINANCIAL PERFORMANCE AND RESOURCING (Page 12)

- Council's future direction is governed by the Resourcing Strategy 2017-2027 plan, which incorporates the Long Term Financial Plan, Workforce Plan and Strategic Asset Management Plan. The Workforce Plan and Asset Management Plan require updating to align with the Long Term Financial Plan.
- The Long Term Financial Plan is projecting that both General and Sewer Funds will achieve operating surpluses for the next five years, whereas the Water fund will operate in deficit. We understand that the 2021/22 draft budget will address this issue.
- Council is planning to expend over \$295m on capital projects over the next four years to be funded by a combination of grants, loans, developer contributions and Council funds.
- Over 50% of the funding for capital works in the next four years will be derived from cash surpluses and reserves. The utilisation of funds from this source will have a significant impact on the level of reserves held by the Water and Sewer Fund which will need to be carefully managed.
- It is intended to raise \$49m in new loans as part funding of capital projects. Whilst the level of loan raising is significant the future debt service cover ratio will remain within acceptable benchmarks.
- The planned capital and maintenance expenditure program will have a positive impact on achieving relevant asset renewal and maintenance benchmarks.

SPECIAL RATE VARIATION (SRV) – (Page 16)

- We are of the view that the SRV has been levied in accordance with the IPART Determination and the environmental levy component of the SRV for 2019-20 has been treated in accordance with the intent of both Council and IPART.
- For reasons outlined in this report, Council has not fully achieved the planned capital and operating expenditure targets nor the reduction in operating deficits proposed in the IPART Determination. The shortfall in expenditure on SRV projects of \$5.2m has been set aside in the Investing in Our Future reserve.
- Revenue from the Environmental Levy and has been expended on appropriate environmental projects over the last four years and the under expenditure of \$61,000 in 2019/20 has been appropriately transferred to the Environment Levy Restriction.

CIVIC CENTRE PROJECT (Page 19)

- Total actual and planned expenditure on the Civic Centre project, including fit out, library rebovations, solar and landscaping expenditure is expected to reach \$10.7m.
- The Office of Local Government Expenditure Review Guidelines require Council to submit an Expenditure Review (business case) before commencing the project. The Expenditure Review document lodged by Council, the week before acceptance of the prime tender for the project, was not tabled for consideration or approval of the elected Council.
- Governance oversight and management reporting on this significant and potentially contentious project between 2016 and 2019 lacked transparency.
- Whilst reporting to the elected Council on expenditure and funding approval may not have been fully open and transparent in the earlier years, it is apparent from our review that the elected body approved the total expenditure of the Civic Centre project via adoption of Operating Plans and approval of Revotes.

2. Past Operating Performance

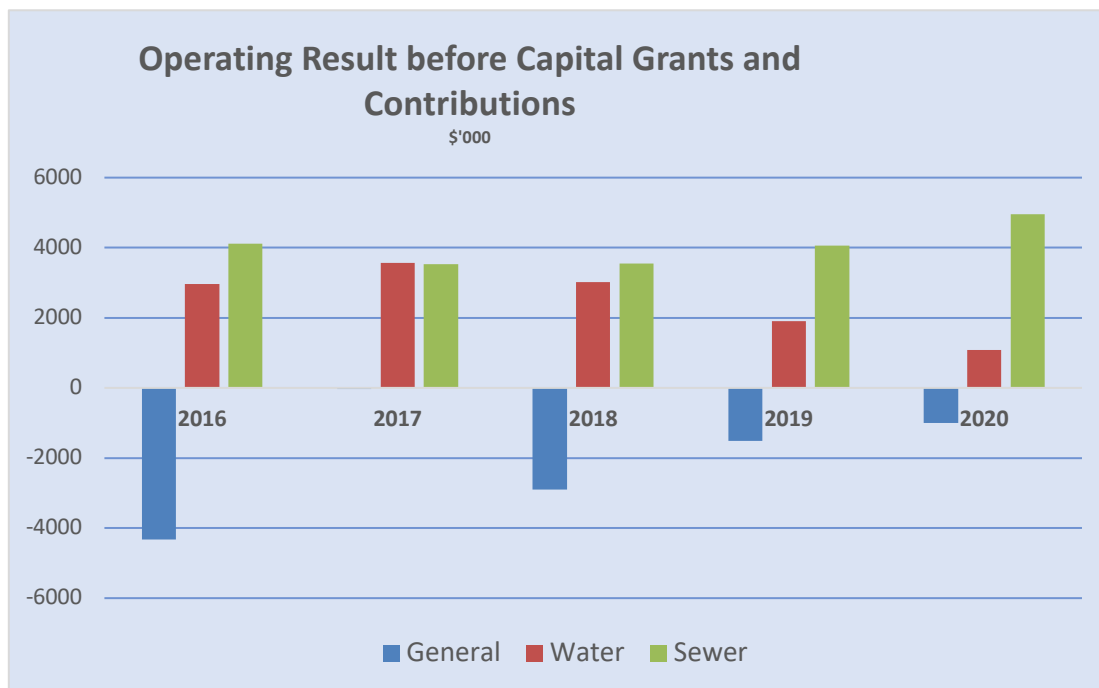
In assessing Council’s past financial performance we have relied upon the annual audited Financial Statements and associated Special Schedules.

The Financial Statements indicate that the Council has recorded modest consolidated Operating Surpluses (before capital funding) for the past five financial years:

Consolidated Operating Result Before Capital Grants and Contributions \$'000				
2016	2017	2018	2019	2020
2,735	7,056	3,671	4,442	5,041

The audited Financial Reports are consolidated accounts for the General, Water and Sewer Funds. The Water and Sewer Funds are restricted funds to the extent that their financial resources cannot be utilised to fund General Fund operations or capital projects without Ministerial approval.

The financial performance of the Water and Sewer funds appears to be reasonably sound over this period with positive operating results. However, General Fund recorded the following deficits over the last five years.



Council’s inability to achieve operating surpluses in the General Fund, particularly in the earlier years has hampered its capacity to fully fund depreciation and thus set aside sufficient funds to meet the cost of renewal of depreciating assets or acquisition of new asset at the same rate that assets are depreciating.

This historical financial performance was recognised by the community and Council in 2016 and prompted the need for an application for a Special Rate Variation (SRV) in order to achieve financial sustainability and fund infrastructure replacement. Further commentary in relation to the application of the SRV is included later in this report.

Operating Revenues

The ability to generate “own source” revenue remains a challenge for many rural councils, who are more reliant on external funding from grants. In 2018-19 the Audit Office reported that 68% of rural Councils did not achieve the own source operating revenue benchmark of >60%. For the last five years Council has exceeded this benchmark.

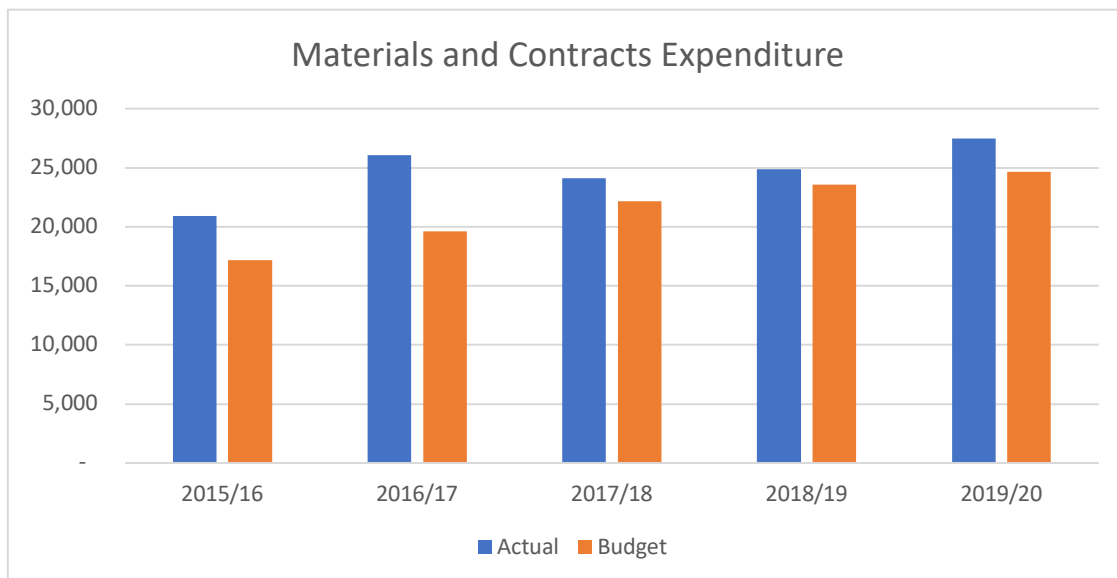
Income from general fund rates and annual charges has grown by 44% due to implementation of the Special Rates Variation and an 8.5% increase in the number of rate assessments. The 2019 average ordinary residential rate of \$1,637 compares with the NSW comparative group average of \$1,128.

Water Fund combined rates and user charges has grown by 21% over the last five years and Sewer Fund rates and user charges grew by 29% in the same period. Water fund increases were attributable to a combination of increases in charges and consumption patterns impacted by the drought.

Positive growth in own source revenue has assisted in placing council on a sound financial footing.

Operating Expenditures

Consolidated operating expenditures, excluding depreciation, have grown by 19% over the last five years mainly due to a 32% increase in the “Material and Contracts” category. Expenditure in this category exceeded budget by a total of \$16.3m over this period.



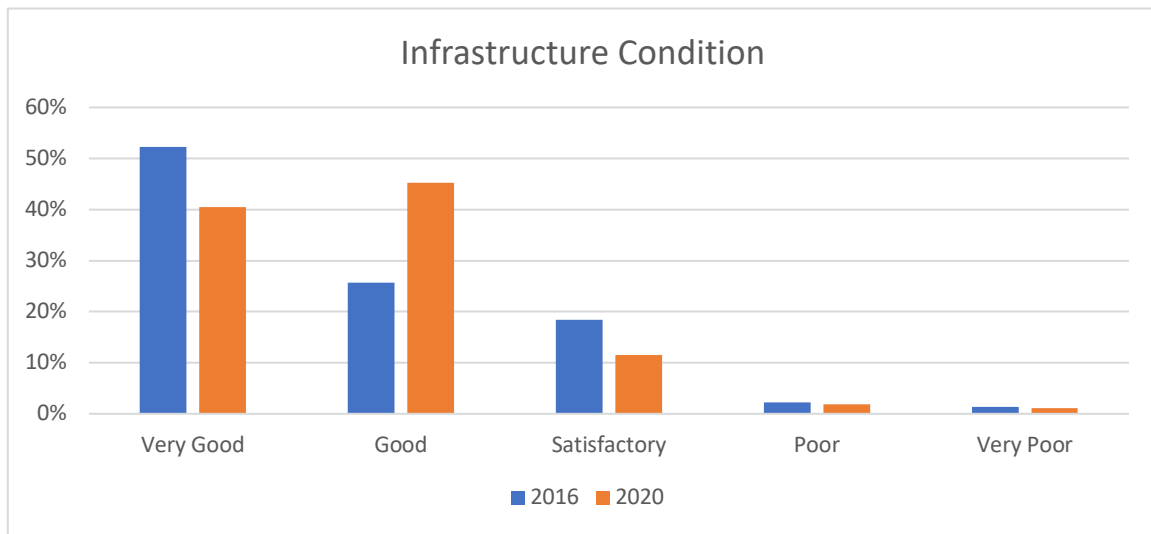
The increase in materials and contracts can be attributed to expenditure not considered as part of the original adopted budget relating to; bushfire response programs and works, significant storm damage remediation works, the ongoing use of contract staff due to long term vacancies within Council staffing structure, and changes in the accounting treatment for certain classes of transactions.

Employment benefits and oncosts (before capitalisation) have grown by 19.6% since 2015/16 reflecting the growth of equivalent fulltime staff (EFT) of 17.8% since 2015/16, but the expenditure was within budget expectations. As at June 2020, Council had a population of 107 per EFT compared with OLG published group average of 109 for 2018/19.

INFRASTRUCTURE ASSET CONDITION

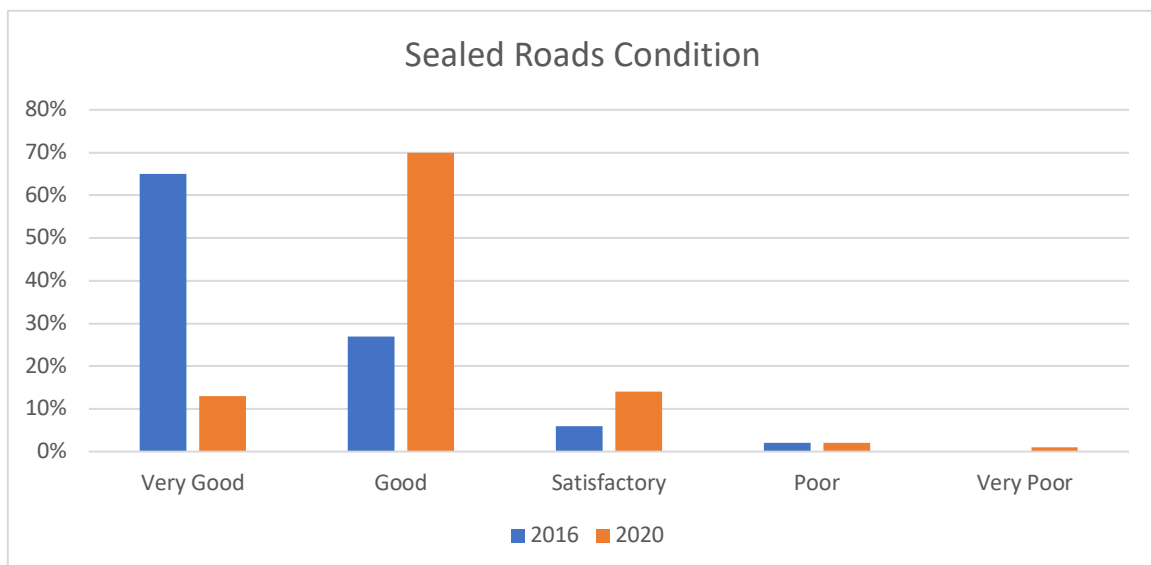
As part of the annual reporting process, Council is required report on the condition of infrastructure assets.

Whilst we acknowledge that these condition assessments are not subject to audit and are to some extent subjective, they do provide an indicator of the success of asset maintenance renewal programs.



The above graph shows that the condition of assets in the “very good” category has slipped to the “good” category over the last five years.

The gross replacement cost of sealed roads \$452m represents 44% of the gross replacement cost of all depreciable general fund infrastructure assets.



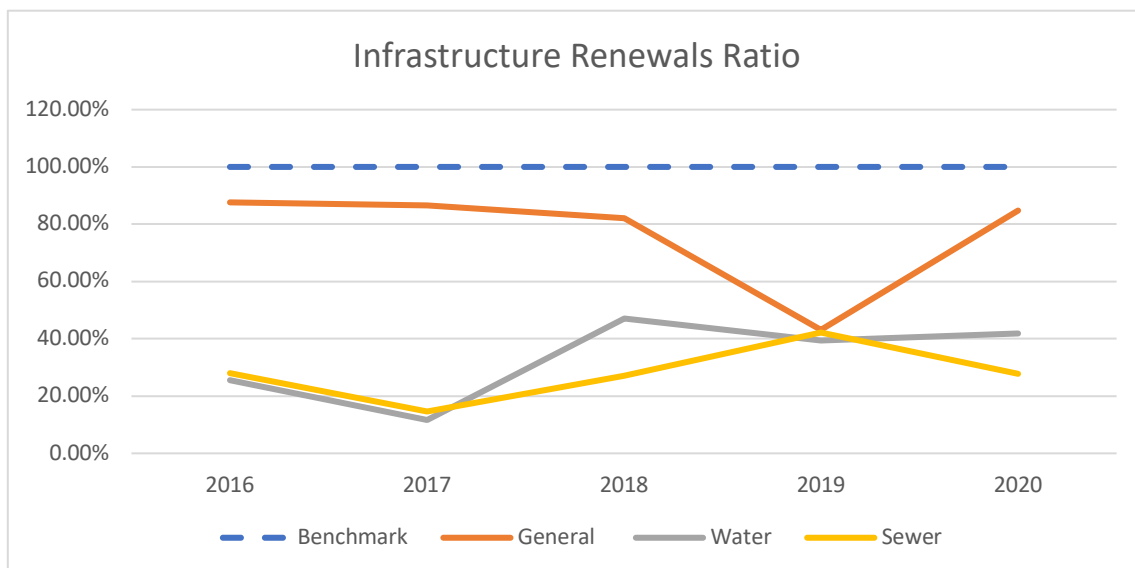
The above graph shows that the condition of sealed roads has also deteriorated in the “very good” category with slippage to the “good” category.

The condition indicators for Water and Sewerage infrastructure assets in 2020 show no substantial change from the indicators set in 2016.

BUILDINGS AND INFRASTRUCTURE RENEWAL

As part of the annual reporting compliance process, Council is required to report a Building an Infrastructure Renewals Ratio. This ratio is an assessment of the rate that these assets are being renewed relative to the rate at which they are depreciating. It is important to note that “renewals” represent the replacement and/or refurbishment of existing assets to an equivalent capacity as opposed to the acquisition of new assets (or the refurbishment of old assets that increases capacity or performance).

The benchmarks reported by Council for the last five years are summarised in the follow graph.



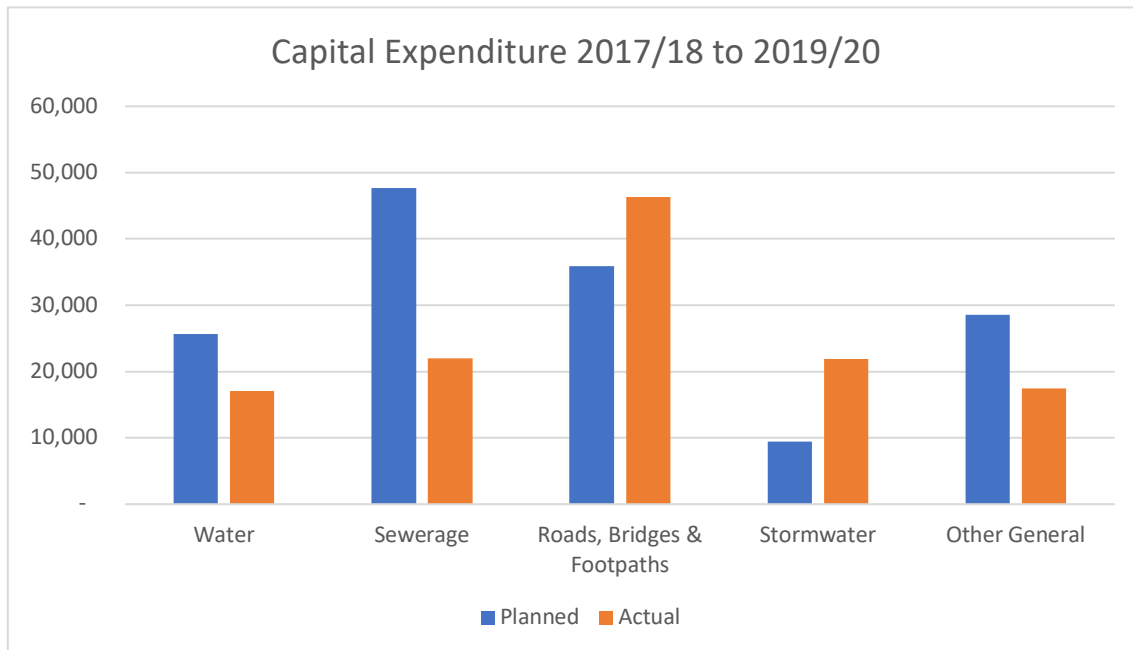
Water and Sewer fund renewal ratios suggest a poor rate of renewal, however it is relevant to consider that long life below ground infrastructure are usually only renewed at the end of the life cycle, so it is essential that these funds hold strong reserves to fund eventual replacement.

Councils 2017-2027 Resourcing Strategy expected that the 100% benchmark, on both a consolidated and general fund basis, would have been achieved by 2018 to 2020 and maintained at an average above 90% up to 2027. Delays in the asset renewal program, particularly water and sewer have contributed to the failure to fully achieve these objectives. It is also relevant to note that the ratio excludes capital works-in-progress.

Whilst the renewal ratio has not achieved benchmark in the last five years, new assets or refurbished assets, that have increased performance or capacity, have grown substantially to the extent that the combination of new and renewed assets, including work-in-progress, has considerably exceeded the rate of depreciation in those years. A significant component of new assets has derived from the dedication of infrastructure from developers.

CAPITAL EXPENDITURE BUDGETS

Over the last three years planned capital expenditure varied significantly from the actual result for key infrastructure categories. viz



The inability to achieve planned expenditure in Water and Sewer funds is reflected in the relatively poor infrastructure renewal ratio described earlier.

Over this three year period, Council has received over \$80m in capital grants and developer contributions in excess of budget expectations. The General Fund component of this extra funding has contributed to expenditure exceeding budget in the Roads, Bridges and Stormwater categories.

Whilst expenditure from unplanned grant funding has been positive, it appears to have been at the expense of Council's capacity to achieve planned project completion within the expected time frame. This fact is reflected in the substantial budget "carry overs" or revotes each year. The following table demonstrates the extent of this issue over the last three years.

REVOTES From	2018/18 \$'000	2018/19 \$'000	2019/20 \$'000
General Fund	15,552	37,122	19,356
Water Fund	5,494	3,179	6,019
Sewer Fund	1,628	4,971	7,682
Total	22,674	45,272	33,057

We note that Council has recently established a dedicated Project Delivery Branch to improve efficiencies in managing projects.

3. Current Financial Position

The audited Financial Statements for the year ended 30 June 2020 disclose important key performance indicators that reflect the financial standing of the Council.

NET CURRENT ASSETS

The Net Current Asset balance is an important financial performance indicator because it is a measure of Council's capacity to fund its day to day working capital needs, meet liabilities or unexpected expenditures arising in the next twelve months and also to fund reserves.

Included in current assets is cash that is externally restricted. External restrictions include unexpended grants, contributions and loans for specific purposes and are therefore not available to fund day to day working capital needs.

Council may also elect to set aside cash in reserves (Internal Restrictions) to fund future projects. Where cash is internally restricted, it is not available to fund working capital unless Council resolves to utilise such reserves accordingly.

As at 30 June 2020, our assessment of the working capital balance of Council was as follows:

Working Capital	General Fund	Water Fund	Sewer Fund
	\$'000	\$'000	\$'000
General Fund NCA			
Current Assets	83,001	67,641	58,355
Current Liabilities	(22,475)	(2,121)	(4,214)
ELEs and Payables > 12 Mnths	6,512	379	749
Adjusted Net Current Assets	67,038	65,899	54,890
External Restrictions	27,312	18,245	18,117
Unrestricted NCA	39,726	47,654	36,773
Internal Restrictions (Reserves)	40,569	-	0
Available to fund Working Capital	(843)	47,654	36,773

The above table demonstrates that the general fund had has a very tight working capital balance after funding internal restrictions.

An alternative approach in assessing working capital needs is to consider the utilisation of cash and investments. As at 30 June 2020, Council had \$67.9m in current cash and investments. After deducting both external and internal restriction, this balance reduces to \$81,000 which we believe is insufficient to fund working capital needs.

We are therefore of the view that Council may not have had the financial capacity to fully fund internal restriction (reserves) in 2020 or that internal restrictions in 2020 were being partly funded by cash needed for working capital.

It is our view that a growing council of the size of Wingecarribee should maintain a working capital balance of at least \$5m before funding internal restrictions.

Council management utilises different methodology to determine working capital needs. For example, Council does not rely on working capital to fund the repayment of loans within the next twelve months as these repayments are funded in the budget for that year, however we believe that the methodology used above, whilst conservative, should be considered as an alternative approach in assessing the funding available for internal restrictions.

As Council may resolve to utilise the \$40m set aside in internal restrictions for other purposes or return the funds to consolidated revenue, it is relevant to consider the Unrestricted Current Ratio published in the 2020 Financial Statements. This is a measure of net current assets, less external restrictions and specific purpose liabilities and at 5.72 is well in excess of the benchmark of 1.5 and thus indicates a sound financial position.

The establishment or removal of internal restrictions should be subject to a resolution of the elected Council. Council does not have an internal restrictions policy and not all Restrictions have been subject to a resolution of Council.

DEBT SERVICE COVER RATIO

The audited Financial Statements as at 30 June 2020 show that Council had loan borrowings totalling \$20.9m, a reduction of \$4.3m on the previous year. Many of these loans are close to full amortisation and this fact is reflected in the debt service cover ratio.

The debt service cover ratio measures the operating cash to service debt including interest, principal and lease payments. The accepted benchmark is a ratio greater than two times.

Council's General Fund had a ratio of 9.07x and Sewer fund had a ratio of 3.63x, an improvement on the previous year. The Water fund carried no debt as at 30 Jun 2020.

These ratios demonstrate that Council has positive borrowing capacity, although the level of future debt for the Sewer fund would need to be carefully managed.

INVESTMENTS

As at 30 June 2020, Council had \$183m held in cash and investments with 96% held in term deposits. The average yield on these investments is now below 1% with current rollovers attracting rates below 0.5%.

Council adopted an Investment Policy in July 2017 which provided for investment in alternative products subject to a risk management framework. The policy also allows for the appointment of a licenced investment advisor.

Many councils in NSW experienced significant investment losses during the Global Financial Crisis and Council was no exception having lost \$11.1m but eventually recovering \$9.7m in 2016/17. This incident has undoubtedly resulted in Council adopting a conservative investment profile. However, in the light of current market conditions, it would be timely to review the policy and consider the appointment of an investment advisor to improve portfolio performance.

GOVERNANCE AND ADMINISTRATION

During the process of this review, we noted that Council' financial systems appeared to be effective and efficient and statutory reporting obligations were met within appropriate time frames.

The elected Council's monitoring of financial performance is measured through the budget approval process and quarterly budget reporting.

In this regard, we noted that Operational Plan and Quarterly Budget Reviews tendered to focus on consolidated financial results and that the operating performance of each fund was not immediately apparent. We believe that this reporting framework would be enhanced by disclosing operating results by fund.

4. Projected Financial Performance and Resourcing

Councils Resourcing Strategy 2017-2027 incorporates several key planning documents:

- Long Term Financial Plan
- Workforce Plan
- Strategic Asset Management Plan

These planning documents were the culmination of the Fit for the Future assessment, community consultation program in 2015 and IPART application for a Special Rate Variation in 2016 and set the scene for the future development of the Shire.

We reviewed these documents to assess their application over recent years and to determine Council capacity to resource future plans.

In reviewing the Workforce plan and the Strategic Asset Management Plan, we noted that they had not been updated since inception, although it is acknowledged that there is only a statutory requirement to renew the Resourcing Strategy every four years .

In 2015/16 staff turnover rate was approximately 19 per cent. This is higher than the industry average of approximately seven per cent. The Workforce Plan identified proposed strategies to satisfy the workforce gap analysis. We have seen no evidence of the review of outcomes or evidence of ongoing monitoring, particularly at the elected Council level.

The Strategic Asset Management Plan provides an assessment of the "Level of Service" of relevant assets classes. We noted that many of the "current performance" indicators were described as "yet to be measured or assessed" or "policy to be developed". We have seen no evidence of review and confirmation of assumptions for this plan.

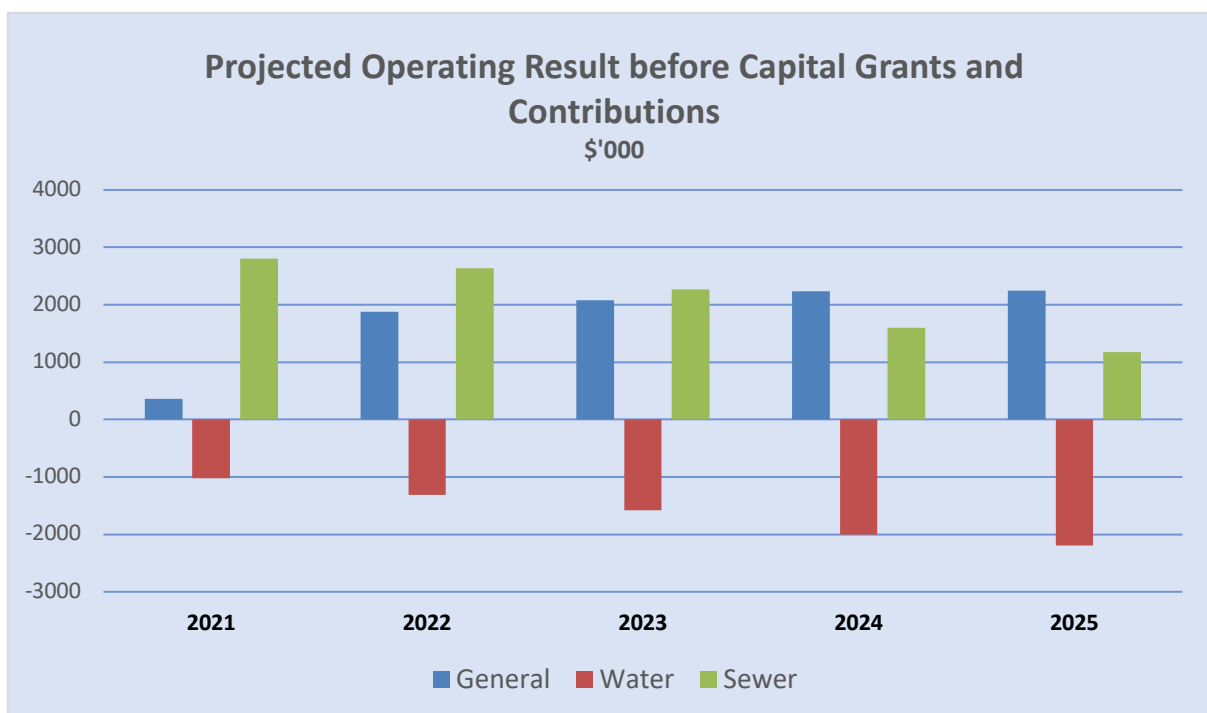
The Long Term Financial Plan is typically updated annually as part of Council's annual budget process, however future years are not necessarily aligned with other two key planning documents.

In response to our comments in relation to updating of the Resourcing Strategy, Management has advised that the delay in the local government elections has put back plans for community consultation and subsequent renewal of the Resourcing Strategy.

As indicated earlier, Council has established a dedicated Project Delivery Branch and we understand that asset management practice areas have significantly improved in the last 2-3 years. As the Resourcing Strategy is the overarching planning document in the asset management program, regular updating, monitoring and performance reviews at a governance level should assist this Branch in satisfying governance accountability.

Projected Financial Operating Results

The Long Term Financial Plan (LTFP) discloses the expected operating results by fund for the next five years.



It is positive to note that the LTFP predicts that general fund will achieve operating surpluses over this period, however the Water Fund is predicted to move from a position of positive operating surpluses over the last five years to operating deficits over the next five years. This significant change is mainly due to limited growth in revenue from User charges and Fees and significant growth in employee benefits and material and contract costs.

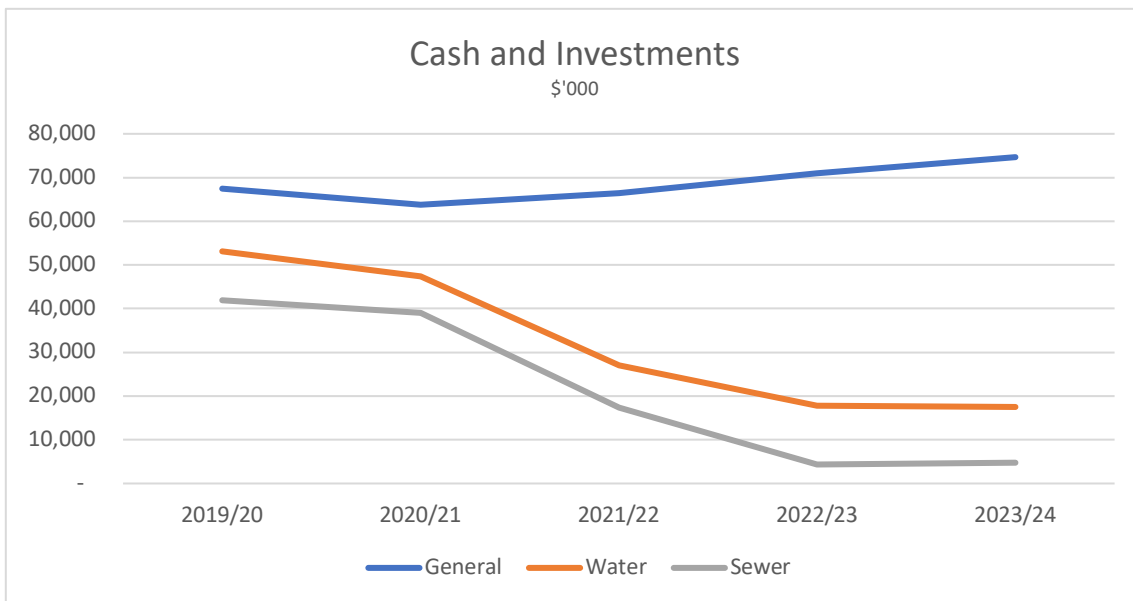
A review of the Water Fund LTFP would be appropriate with the objective of returning the planned deficits to surpluses.

Future Capital Projects and Funding

The LTFP 2020-30 proposes that over the next four years Council will expend \$295m on capital projects. The source of funding for this expenditure is shown in the following table.

FUNDING SOURCE	General \$'000	Water \$'000	Sewer \$'000
Cash Surpluses and Reserves	99,096	37,360	49,062
Capital Grants	15,365	-	6,600
Loans	10,260	15,750	23,000
Developer Contributions	67	18,800	19,258
Total Capital Expenditure	124,788	71,910	97,920

It is significant to note the level of funding from cash operating surpluses and reserves. The utilisation of reserves has the following impact on the level of projected cash and investment balances.



The extensive asset renewal program for Water and Sewer Fund will see a significant depletion in cash reserves, particularly the Sewer fund. By 2023/24 the Sewer Fund is expected to have only \$4.7m in cash and Investments of which \$1.7m will be externally restricted resulting in a tight working capital balance or limited reserves.

The main impact on the Sewer fund arises from the planned upgrade to three sewerage treatment plant at a cost of \$85m. Council’s Integrated Water Cycle Management Strategy 2018 provides technical justification for these upgrades. Council originally anticipated State Government funding of up to 30% towards this project, however approved funding of only \$6.6m is now anticipated thus placing more reliance on Sewer fund reserves and loans.

New loans will also be a funding source over the next four years and thus will impact on the debt service cover ratio described above, however these ratios will remain within acceptable benchmarks.

By way of further explanation, an average of 3% of general fund revenue from rates, user and annual charges will be utilised fund loan interest and principal repayments. In the Sewer fund this percentage increases to an average of 11% over the next four years.

We believe that both General and Water Fund have additional borrowing capacity should the need arise, subject to an appropriate assessment of Council’s ability to service the debt.

UNFUNDED PROJECTS

Councils Operational Plan 2020/21 lists unfunded projects amounting to \$418m. This total is now reduced to \$333m as the sewerage treatment plant project was incorrectly disclosed as unfunded.

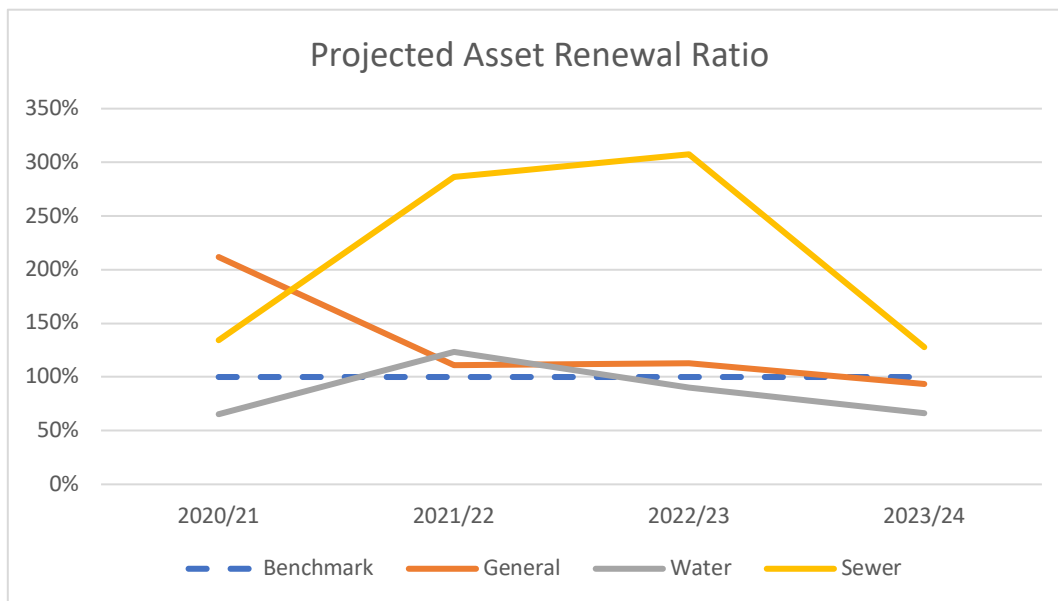
We understand that the Unfunded Projects Lists comprises projects that are regionally significant and as such funding is to be sought from all tiers of government.

Unfunded projects amounting to \$322m relate to the General Fund. The General funds sound rating base will assist the fund in maintaining the existing level of reserves and together with additional borrowing capacity will allow the Council to maintain the rate of asset renewal or consider further projects on the unfunded project list.

IMPACT ON RENEWALS RATIO

As reported above Council has been unable to achieve the 100% benchmark for Asset Renewals over the five years to 2019/20.

The proposed capital expenditure program for next four year will have the following impact on the Asset Renewals ratio.



The Asset Maintenance ratio should also achieve benchmarks over this period.

5. Special Rate Variation (SRV)

BACKGROUND

In 2016, Council applied for a multi-year special variation under section 508A of the Local Government Act. The council requested increases of 8.55% for 2016-17 and 9.25% in each of 2017-18 and 2018-19 with an increase of 12.15% in 2019-20, a cumulative increase of 45.30%. It applied for the increase to remain permanently in the rate base. This increase includes additional revenue to replace the 3.5% environmental levy that will expire on 30 June 2019.

The application was sort for the following projects:

- The continuation of the Wingecarribee Our Future Environment program.
- Increased infrastructure maintenance and renewals for roads, buildings, drainage and parks.
- Asset upgrades for roads and drainage.
- Improve the council's financial sustainability.

The Independent Pricing and Regulatory Tribunal of NSW (IPART), which is responsible for setting the amount by which councils may increase their general income, approved Council's application in May 2016 subject to the following conditions:

1. The council uses the additional income from the special variation for the purposes of improving financial sustainability and reducing infrastructure backlogs as outlined in the council's application and listed in Appendix A of the Determination.
2. The council reports in its annual report for each year from 2016-17 to 2025-26 on:
 - the actual revenues, expenses and operating balance against the projected revenues, expenses and operating balance, as outlined in the Long Term Financial Plan provided in the council's application, and summarised in Appendix B of the determination.
 - any significant variations from its proposed expenditure as forecast in the current Long Term Financial Plan and any corrective action taken or to be taken to address any such variation
 - Expenditure consistent with the council's application and listed in Appendix A of the Determination, and the reasons for any significant differences from the proposed expenditure, and
 - the outcomes achieved as a result of the actual program of expenditure.

Part of our brief is to undertake general review of expenditure under Council's SRV's (Infrastructure Component & Continuation of Environment Levy) to ensure compliance with approvals. Our findings are as follows.

SRV INCOME

In conjunction with the audit of the annual financial statements, the Audit Office undertakes an audit of the Permissible Income Yield for General Rates. The Audit Office has issued unqualified opinions since commencement of the SRV thus providing assurance that the levy was rated in accordance with the IPART determination.

The environmental levy, which expired on 30 June 2019, was not part of the permissible income audit until 2019-20. There has been conjecture among ratepayers in relation to the percentage increase that should apply to the environment levy 2019/20 and beyond. Some ratepayers argue that the environmental component of the SRV should be permanently fixed at 3.5% of general rate income, thus resulting in an increase of \$450,000PA on the income raised by the Environmental Levy in 2018/19.

This argument does not take into consideration that the IPART Determination is based on increases in general income, and that the percentage increase will vary from year to year based on the number and value of rate assessments. Councils SRV application and the IPART Determination also clearly indicate that the revenue from the SRV will allow \$9.4m to be expended on the Our Future Environment program between 2019/20 and 2025/26. The \$9.4m in equivalent revenue arises from applying 2.5% assumed rate peg increase to the Environment Levy base of 2018/19. If the argument that 3.5% of general income should be permanently applied, the total revenue over this period would amount to approximately \$13m. We believe that this was not the intent of Council nor IPART in making the Determination.

Management tabled a report to Council on 28 October 2020 which clarified the debate on this issue. We believe that report to be a correct interpretation of the facts. The report was noted without qualification by the elected body.

EXPENDITURE FUNDED BY SRV

Council is required to report annually on the actual revenues, expenses and operating result compared with the Long Term Financial Plan (LTFP) detailed in the IPART Determination.

The following table compares the proposed operating and capital expenditure disclosed in the LTFP compared with the actual expenditure disclosed in Council's Annual Reports.

	2016-17	2017-18	2018-19	2019-20	4 Year Total
Operating Expenditure					
Per IPART Determination (LTFP)	596,000	1,188,000	2,079,000	3,915,000	7,778,000
Actual Per Annual Report	514,161	1,134,031	1,555,567	3,615,184	6,818,943
GAIN (SHORTFALL)	(81,839)	(53,969)	(523,433)	(299,816)	(959,057)
Capital Expenditure					
Per IPART Determination (LTFP)	1,726,000	3,737,000	5,774,000	8,142,000	19,379,000
Actual Per Annual Report	1,220,596	3,248,860	4,742,974	5,882,561	15,094,991
GAIN (SHORTFALL)	(505,404)	(488,140)	(1,031,026)	(2,259,439)	(4,284,009)
Total Expenditure Shortfall	(587,243)	(542,109)	(1,554,459)	(2,559,255)	(5,243,066)

2019-20 actual Operating Expenditure includes environment expenditure.

This table discloses that Council did not fully achieve the LTFP objectives in most years since the commencement of the SRV. The total shortfall in operating and capital expenditure of \$5.2m represents approximately 19.3% of additional SRV revenue of \$27.1m (above the assumed rate peg increase) generated over the last four years.

Management has advised that the shortfall described above is primarily due to:

- Project savings (expenditure below budget)
- Delays in project delivery
- Delay in the development of maintenance plans

Even though the Annual Reports disclose a shortfall in SRV capital expenditure, it is relevant to note that additional capital expenditure on roads, drainage, buildings and parks over the last four years, compared with the base year of 2015/16, exceeded the planned SRV capital expenditure for those years. This additional capital expenditure was partly due to additional unplanned funding from grants and developer contributions.

It should be noted that the unexpended component of SRV funding has been set aside as an internal restriction in the “Investing in our Future” reserve.

OUR FUTURE ENVIRONMENT PROGRAM

Revenue generated by the Environment Levy between 2016-17 and 2018-19 and part SRV for 2019/20, and the associated expenditure as disclosed in the Annual Reports is shown in the following table.

Environment Levy	2016-17	2017-18	2018-19	2019-20	4 Year Total
Income From Environment Levy	1,141,000	1,186,000	1,247,000		4,864,000
Income from SRV				1,290,000	
Environment Expenditure	1,294,258	1,191,882	1,255,390	1,228,976	4,970,506
Variation	(153,258)	(5,882)	(8,390)	61,024	(106,506)

This table demonstrates that, 2016/17 and 2018/18 income from the Environmental Levy has been fully expended. The 2019/20 underspend of \$61,024 has been transferred to the Environment Levy restriction.

We have reviewed the expenditure totals disclosed in the Annual Reports for 2018/19 and 2019/20 and confirm that they agree with Council’s ledger system and the expenditure categories within the ledger satisfy the intent of the Levy.

OPERATING RESULT

Council application for an SRV was partly based on generating additional income to reduce or eliminate general fund budget deficits.

The actual General Fund operating result over the last four years fell short of planned operating result in the LTFP.

Operating Result	2016-17	2017-18	2018-19	2019-20	4 Year Total
Per IPART Determination (LTFP)	(2,555,000)	(467,000)	1,519,000	3,513,000	2,010,000
Actual Net Operating Result #	(37,000)	(2,906,000)	(1,512,000)	(1,008,000)	(5,463,000)
GAIN (SHORTFALL)	2,518,000	(2,439,000)	(3,031,000)	(4,521,000)	(7,473,000)

General Fund Operating Result excluding Capital Grants and Contributions

Our earlier comments in this report regarding the reasons for excess expenditure in materials and contracts has contributed to the variation between planned and actual operating results.

REPORTING

As indicated above, it is a condition of the IPART Determination that Council provide specific information in the Annual Reports in relation to the application of the SRV. Our review of the Annual Reports for the relevant years indicates that Council has complied with most of the reporting requirement, however the reports do not appear to disclose the requirement that Council report on “*any corrective action taken or to be taken to address any significant variation*” from proposed expenditure.

6. Civic Centre

EXPENDITURE AND VOTE APPROVAL

We have been asked to undertake a review of expenditure on the Civic Centre and confirm that the project funding has been approved by the elected body. Our findings are as follows.

The refurbishment of the Civic Centre has been on Council projects agenda since 2014/15 with interim expenditure totalling \$724,000 between 2014/15 and 2016/17.

The Resourcing Strategy 2017-2027 (Strategic Asset Management Plan page 61 of 71) indicates planned capital expenditure on the Civic Centre of \$3m in 2017-18, \$2.2m in 2018-19 and nil in future years. In addition, an approved revote amount of \$821,662 was carried over from 2016/17 bringing total planned expenditure on the project to \$6m.

The Resource Strategy and the associated Operational Plan 2017/18 was adopted by Council on 14 June 2017.

Subsequent to the adoption of the Operational Plan 2017/18, Council employed MDA Australia to provide cost estimates for the project (inclusive of all functional requirements) which resulted in projected costs increasing to \$8.4m. The additional funding (\$2.4m) to cover this increase cost was included in the adopted 2018/19 Operational Plan as a line item in the capital works program. There was no information in the document providing reasons for the increased costs.

Management has advised that a further allocation of funds totalling \$846,000 was included in the adopted 2019/20 Operational Plan. This amount was included in a total allocation of \$2.23m to cover the Civic Centre and four other building projects.

We note from our reading of the Operational Plans from 2017/18 to 2019/20, that it is not immediately obvious that the cost had increased significantly from the original estimate. This is due to the fact that capital budget allocations in the Operational Plans are only for the current year and revotes from prior year(s) are considered and adopted some months after the adoption of the budget. Neither reporting process discloses Life to Date costs and estimates.

We also noted that in the substantive and detailed narrative incorporated in the operational plans, including the highlighting of key infrastructure projects, there was only limited reference to the Civic Centre project despite the growth in anticipated costs and potential community concerns about the merit of the project.

On 11 Dec 2019, following an open and competitive tender process, Council accepted a tender from Matrix Group for the prime building contract for \$6.8M. The tabled report disclosed that the total estimated cost of the project was \$9.26m (this amount excluded expenditure of \$724,000 prior to 2017/18 on design fees and preliminary expenses).

It was only at this stage of the project that we observed clear written disclosure of the total expected cost of the project, albeit in a closed session of Council. We were advised by Management that Councillors were also advised of the changes in budget required for the project through Councillor briefing sessions delivered in relation to the Annual Budget, which we understand were also in closed session.

On 9 December 2020, Council resolved to modify the scope of the project and increase the budget allocation by a further \$850,000 bringing total projected costs to \$10.8m.

It is positive to note that since February 2020, expenditure on major capital projects over \$5m have been reported separately to the Finance Committee through the quarterly budget review process. The report tabled at the Finance Committee meeting of 11 Feb 2020 clearly indicated the approved budget amount of \$9.26m and expenditure to date.

Funding of the project is derived from the following sources:

Civic Centre Reserve	\$5,348,000
Investing in Our Future Reserve	\$ 779,000
Land Rental Charge Reserve	\$ 673,000
GF Consolidated Revenue	\$ 460,000
Loan Borrowings	<u>\$2,850,000</u>
TOTAL	\$10,110,000

Additional fit out, library, solar and landscaping expenditure to finalise the project is estimated at approximately \$600,000, to be funded from the adopted budget.

Whilst reporting to the elected Council on expenditure and funding approval may not have been fully open and transparent in the earlier years, it is apparent from our review that the elected body approved the total expenditure of the Civic Centre project via adoption of Operating Plans and approval of Revotes.

PROJECT GOVERNANCE OVERSITE

Civic Centre Refurbishment Advisory Committee

In November 2016 Council resolved to form the Civic Centre Refurbishment Advisory Committee. The Committee comprising three councillors and relevant members of staff. The role of the Committee was to “provide advice and recommendations to the Council in respect to the scope of the project plan for the refurbishment of Council’s Civic Centre including review of detailed designs and estimates.”

We are advised that Committee met in 2017 and 2018, but no formal minutes were maintained and we have not sited any formal recommendations from the Committee to Council. We understand that staff attending these meetings are no longer employed by the Council and therefore we have been unable to confirm the deliberations of this Committee.

Capital Expenditure Review

Under the NSW Office of Local Government (OLG) Capital Expenditure Guidelines for projects over \$1m, or projects greater than 10% of Council’s Annual Rate Revenue (which ever is greater), Council is required to complete a Capital Expenditure Review (Business Case) and notify the OLG prior to commencement of the project, unless the project falls within an exempt category, such as roads and bridges.

Council awarded the Tender for the Civic Centre Refurbishment project to Matrix Group Co on 11 December 2019, however the Capital Expenditure Review document was only lodged with the OLG on 5 Dec 2019 and approval was not received from the OLG until 21 April 2020.

It is acknowledged that the guidelines do not state timelines for submission of the Review other than providing notification “prior to commencement of the project”, however it is reasonable to expect that timely lodgement of the Review, in order to receive confirmation prior to accepting a major tender, would be appropriate.

The Capital Expenditure Review document provides a detailed business case for the refurbishment for the Civic Centre including merits of the project, relevant costings and funding sources. Unfortunately, the document was not tabled at a Council meeting nor was Council asked to approve of the document before lodgement with the OLG. We understand that whilst staff believe that it would have been appropriate for the Council to consider this document in conjunction with the Tender recommendation, the former Council Executive took a contrary position.

Development Application

Council lodged a development application on 22 June 2018 and was approved by Council 14 Nov 2018. An updated DA for the modifications approved on 9 Dec 2020 was assessed by the Independent Advisory Planning Assessment panel on 7 April 2021 and was formally endorsed by Council on 21 April.

7. Recommendations

As a result of issues identified during the review, we suggest that Council consider the following recommendations:

- a) Revisit the Long Term Financial Plan for the Water and Sewerage funds to ensure financial sustainability over the longer term.
- b) Adopt a Reserves policy that ensures a minimum of \$5m is available as unrestricted cash to fund working capital requirements before setting aside funds as Internal Restrictions.
- c) Ensure that the establishment and funding of Internal Restrictions is supported by Council resolutions.
- d) Consider rationalising the number of Internal Restrictions.
- e) Modify the budget reporting framework to ensure that there is clear disclosure of operating results by fund.
- f) Ensure appropriate governance oversight and risk monitoring of major projects.
- g) Review and update the existing Investment Policy and consider the appointment of an investment advisor to improve portfolio performance.
- h) Regularly review and update the Resourcing Strategy to reflect current community expectations and changes in long term planning.
- i) Review the process and scale of revotes with a view to incorporating the financial impact of delays in projects into the following years original budget rather than approving significant project revotes after the original budget has been adopted.
- j) Prepare OLG Capital Expenditure Reviews in a timely manner and table for approval by the elected Council.
- k) Review the allocation of projects to be funded from the SRV with a view to satisfying the IPART Determination expenditure expectations.