Southern Midlands Council

Financial Management Strategy 2018/19 to 2026/2027

(3rd Revision)

(Incorporating Long-term Financial Management Plan)

(as adopted by Council – April 2018)

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1. Executive Summary

The Financial Management Strategy & Long Term Financial Management Plan (FMS) has been prepared to provide the Southern Midlands Council with direction and context for decision making in the allocation, management and use of Council's financial resources.

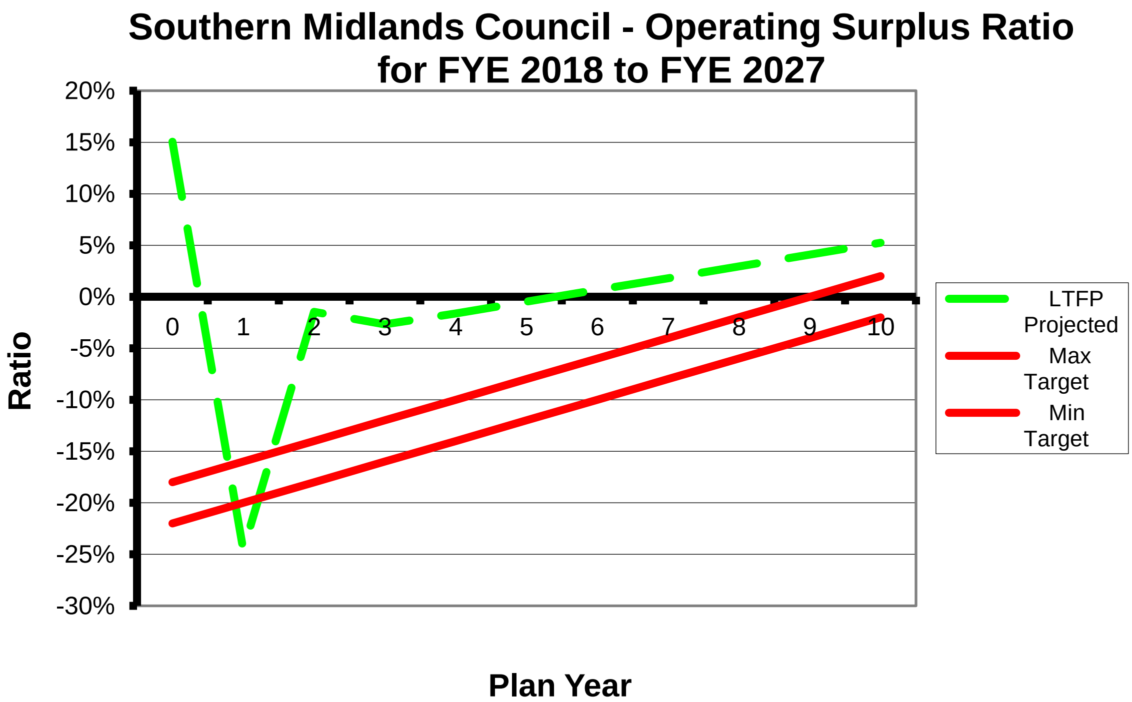
The strategy has been prepared to guide Council in its financial decision-making ensuring that the following principles are followed;

- The community's finances will be managed responsibly to enhance the wellbeing of residents
- Council will maintain community wealth to ensure that the wealth enjoyed by today's generation may also be enjoyed by tomorrow's generation
- Council's financial position will be robust enough to recover from unanticipated events, and absorb the volatility inherent in revenues and expenses
- Resources will be allocated to those activities that generate community benefit.

The following targets have been set out in the strategy and have been determined to be an appropriate measure of financial sustainability:-

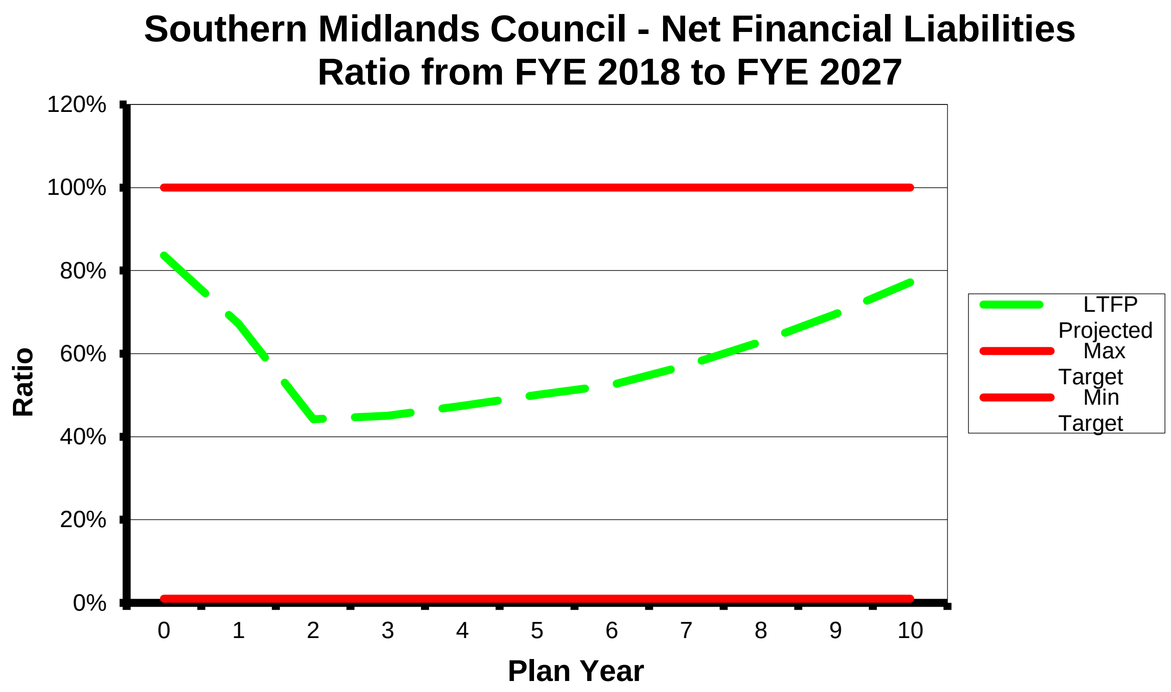
- To achieve and maintain a break-even position at the end of the 10-year strategy (i.e. a resultant minimum operating surplus ratio of 0%).
- To achieve a net financial liabilities ratio within the range of 0% to 100%.

The targeted operating surplus ratio of 0% is achieved prior to the conclusion of the ten-year period. The reduction in the 2017/18 financial year is as a result of receiving 50% of the Commonwealth's Financial Assistance Grant for 2017/18 in the 2016/17 financial year. Improvement is made from the period 2018/19 through to 2026/27 as the Australian Government has resumed indexation of the Financial Assistance Grants.



The targeted net financial liabilities ratio within the targeted range of 0% to 100% is achieved in all years. This will be maintained for the life of the strategy.

The forecast ratio for the period of the Strategy is demonstrated in the following table:-



1.1 Introduction

The FMS has been developed to provide the Southern Midlands Council with a strategic framework when developing budgets for the next ten-year period. The key objectives of the FMS are to:

a) Provide direction and context for decision making in the allocation, management and use of the Southern Midlands Council's financial resources;
b) Guide Council in the development of a ten year financial plan and determine financial boundaries for the delivery of operational and capital plans;
c) Use ratepayer's money, together with other funding available, wisely to provide prioritised services and improve financial sustainability and asset management; and
d) demonstrate and maintain financial sustainability in the medium and long term whilst achieving the strategic objectives of Council.

The FMS includes consolidation of controlled entities.

In preparing the FMS, the following principles of sound financial management have been complied with:

- Prudent management of financial risks relevant to debt, assets and liabilities
- Provision of reasonable stability in the level of rate burden
- Consideration of the financial effects of Council decisions on future generations
- Full, accurate and timely disclosure of financial information.

It is important to note that the FMS is not about deciding on what Council will spend on individual projects. The FMS is about the various financial strategies that will effectively determine the amount of funds that Council will have at its discretion to allocate in future years.

The FMS is a guiding document to consider when developing budget estimates, rather than a document that is dictating future decisions of Council. The long-term financial estimates in this strategy will be revisited and updated regularly to reflect any strategies that arise from the Council planning process. This current version will continue to provide a framework for financial planning and will be further revised and expanded each year.

The FMS is to be reviewed each year following the preparation and endorsement of the Annual Financial Report and prior to the commencement of the Annual Plan and Budget Estimates for the coming year.

If Council follows the general thrust of the document when setting the 'Annual Plan and Budget Estimates', the organisation will demonstrate financial sustainability into the future.

2. Financial Principles

The following principles serve to guide Council in setting its financial management strategies. They are given practical effect through strategies. Strategies are measured by the setting of medium term targets.

2.1 The community's finances will be managed responsibly to enhance the wellbeing of residents

Council will ensure it only raises the revenue it needs, and does so in the most efficient and equitable manner possible. Council will manage community funds according to affordable best practice standards and ensure information regarding its financial management decisions is accessible to the community. Council will ensure it only delivers those services that cannot be delivered more efficiently and effectively by other providers.

2.2 Council will maintain community wealth to ensure that the wealth enjoyed by today's generation may also be enjoyed by tomorrow's generation

Council will seek to achieve equity across generations by recognising that each generation must pay its way with respect to recurrent expenses being met from recurrent revenue (the full cost of the service it consumes).

Council will invest sustainably in community assets to maintain (and potentially enhance) service levels.

2.3 Council's financial position will be robust enough to recover from unanticipated events, and absorb the volatility inherent in revenues and expenses

Council will ensure it accumulates and maintains sufficient financial resources and has the borrowing capacity to deal with volatility and unexpected events.

Council's operational budget will be flexible enough to ensure that changes and volatility in revenues and expenses as a result of the changing economic environment can be absorbed.

2.4 Resources will be allocated to those activities that generate community benefit.

Council will ensure that robust and transparent processes are in place for the allocation and prioritisation of resources through budgetary decision-making, as well as for choosing the most effective methods for delivering specific services and projects. Strategies will include a vigorous cost-benefit analysis in preparing and assessing proposals.

Council will recognise its service obligations to the Southern Midlands community in its decision-making.

3. Financial Management Strategies

The following financial strategies portray the strategic direction in which Council's financial decisions are based including borrowing, infrastructure, and service delivery.

3.1 Financial Indicators

Council targets to achieve a consistent and gradual improvement in the Comprehensive Income Statement.

3.2 Rating Strategy

Council targets to achieve a break-even position and ensure it only raises the revenue it needs, and does so in the most efficient and equitable manner possible. Council must balance its service levels with the needs and expectations of the community and set appropriate levels of tax to adequately fulfil its roles and responsibilities.

The following factors influence the level of rates and charges:-

- Distribution and level of Commonwealth and state funding
- Socio-economic profile of the area (capacity to pay)
- User-pays policies
- Level and range of services
- Current economic environment

In determining its rates each year Council gives consideration to the current economic climate and the capacity of the community to pay for services.

3.3 Rating Structure

Council has established a rating structure comprising of two-key elements – general and service rates.

The general rates are levied based on the Assessed Annual Value (AAV) of properties as determined by the Valuer-General. Property values generally reflect the capacity of the ratepayer to pay.

The service rates currently cover waste management services. This user pay component is designed to reflect payment based on usage of services provided by Council.

Council will endeavour to strike a balance between the two elements to provide equity in the distribution of the rate burden across the municipality.

3.4 Asset Management Strategy

The key objective of Council's Asset Management Strategy is to maintain Councils existing assets at desired condition levels. If funding is not sufficiently allocated to asset renewal then Council's investment in those assets will reduce along with the capacity to deliver services to the community.

Council has an Asset Management Policy to ensure that adequate provisions are made for the long-term maintenance and replacement of Council's infrastructure and built assets by:-

- Ensuring that services and infrastructure are provided in a sustainable manner, with the appropriate levels of service to the community and the environment.
- Safeguarding our assets by implementing appropriate asset management strategies and ensuring financial resources are adequately provided for those assets.
- Creating an environment whereby there is clear awareness throughout the Council at both the elected and employee level, on the importance of maintaining our assets to an acceptable standard
- Meeting legislative requirements for asset management.
- Ensuring resources and operational capabilities are identified and responsibility for asset management is appropriately resourced
- Demonstrating transparent and responsible asset management processes that align with local government industry standards
- Undertaking a continuous cycle of review to ensure that asset management outputs match the changing needs of the Council and the community.

Council's Asset Management Strategy is based on the knowledge provided by various Asset Management Plans which set out capital expenditure requirements in future years.

3.5 Investment Strategy

Cash reserves require careful management to both achieve optimum investment incomes and to ensure that cash is available when needed for the planned expenditures. Funds will be invested in a manner that allows them to earn interest for as long as possible while retaining flexibility in accessing those funds for Council purposes.

Council's Annual Plan and Budget Estimates and Financial Management Strategy will be used to provide direction on the term of investments to be placed. Council will ensure that enough funds are on hand at 30 June each year to ensure that all current liabilities can be met.

Council will ensure that its investment portfolio maximises its return on investments while maintaining an acceptable level of risk.

3.6 Borrowing Strategy

Borrowings are an effective mechanism of linking the payment for assets (via debt repayments) to successive Council populations who receive benefits over the life of that asset. This matching concept is frequently referred to as 'inter-generational equity'.

Council will only borrow for capital expenditure, which will improve services to ratepayers. Borrowings may be used by Council as a funding source for new capital works projects. Asset renewals will be funded internally from cash reserves and cash provided by operating activities (mainly from depreciation).

In considering new debt Council will consider the impact of borrowing costs on the sustainability of operating positions and its capacity to repay the debt. Council will maintain enough borrowing capacity to ensure that it has the capacity to deal with significant unexpected events.

When borrowing Council shall raise all external borrowings at the most competitive rates available and from sources available as defined by legislation.

3.7 Reserves

Any material favourable budget variations realised in a given financial year be specifically quarantined and reserved.

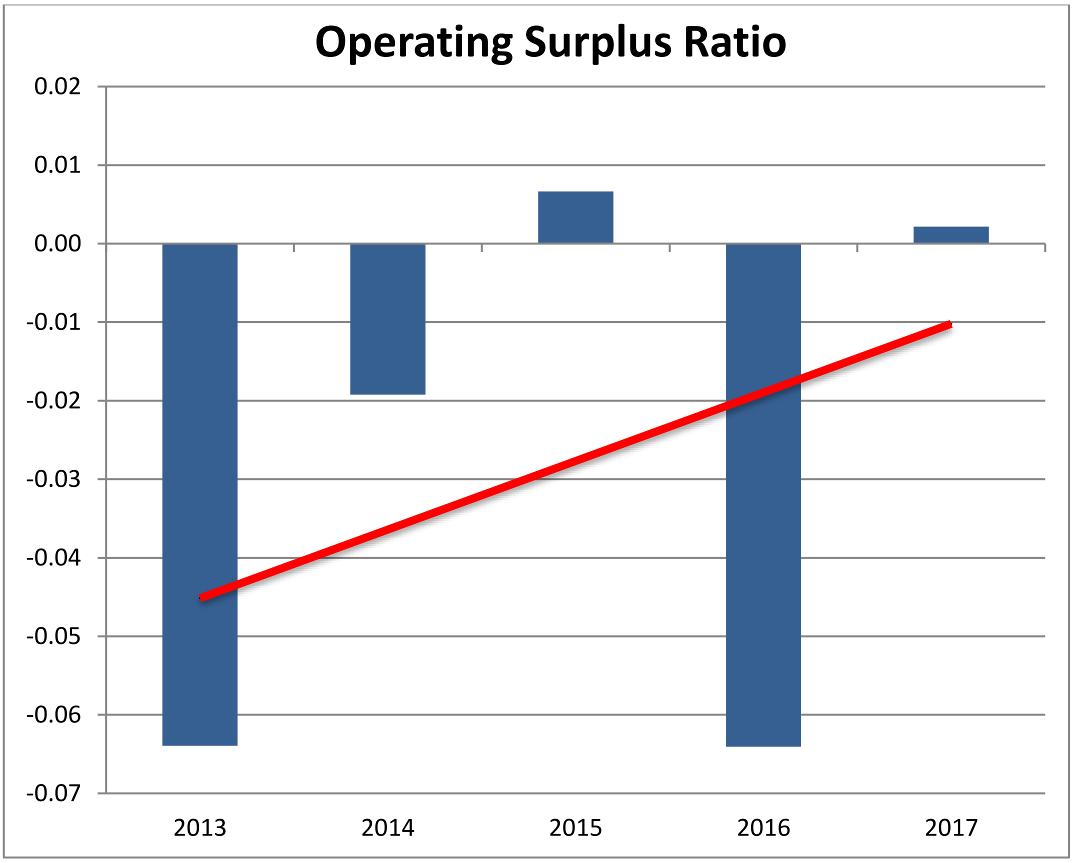
4. Financial Performance

The following graphs summarise key ratios highlighting important aspects of Council's financial performance over the past five years.

Graphs which show forecasts for the period 2012/13 to 2016/17 are in the following section.

4.1 Operating Surplus Ratio

The operating surplus ratio serves as an overall measure of operating effectiveness. A result less than 0.00 indicates an operating deficit. It is accepted that best practice dictates that operating deficits cannot be sustained in the longer term.

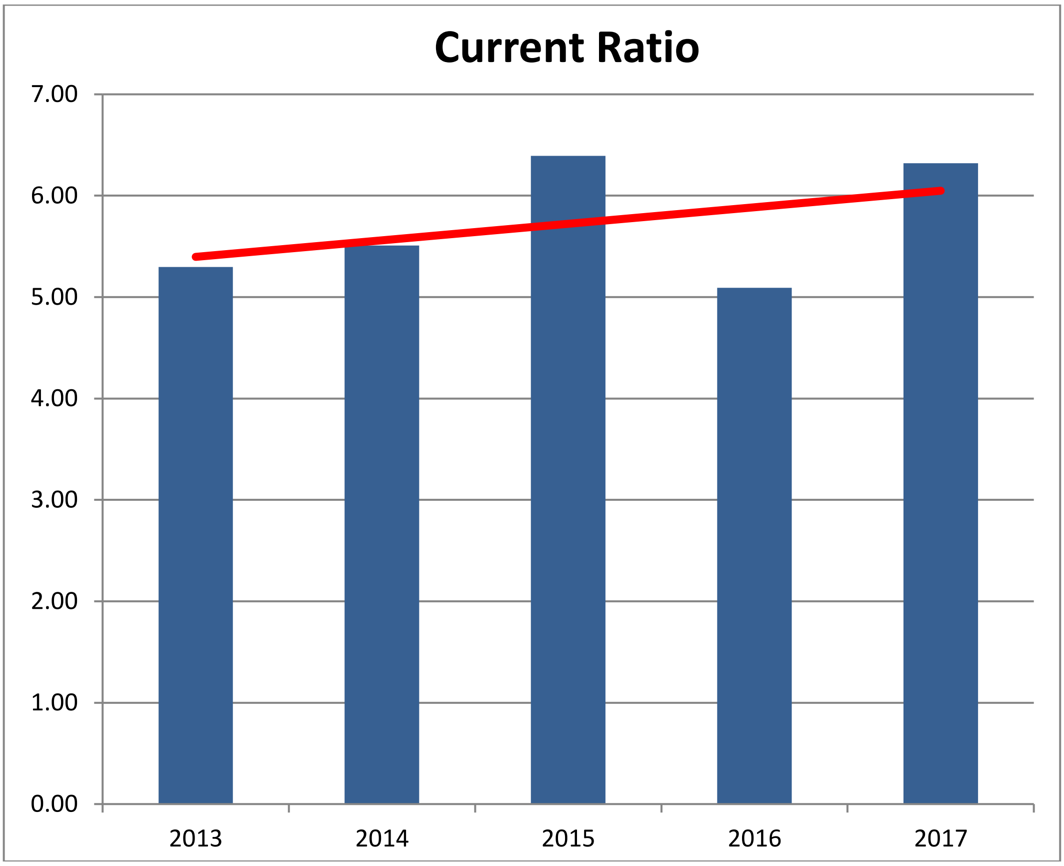


The operating surplus benchmark for Council is 0.00 which is the point where operating revenues equal operating expenditures. An operating margin below the benchmark would indicate that Council might not be generating sufficient revenue to fulfil its operating requirements.

4.2 Current Ratio

The current ratio measures the liquidity, or cash, position of Council. That is, Council's ability to meet its debt obligations as they fall due. A ratio of 1.00 or more indicates that there is enough cash and liquid assets to cover short-term liabilities.

Influencing factors are planning and budgetary control, timing of cash flows and credit policies and collection of debts.

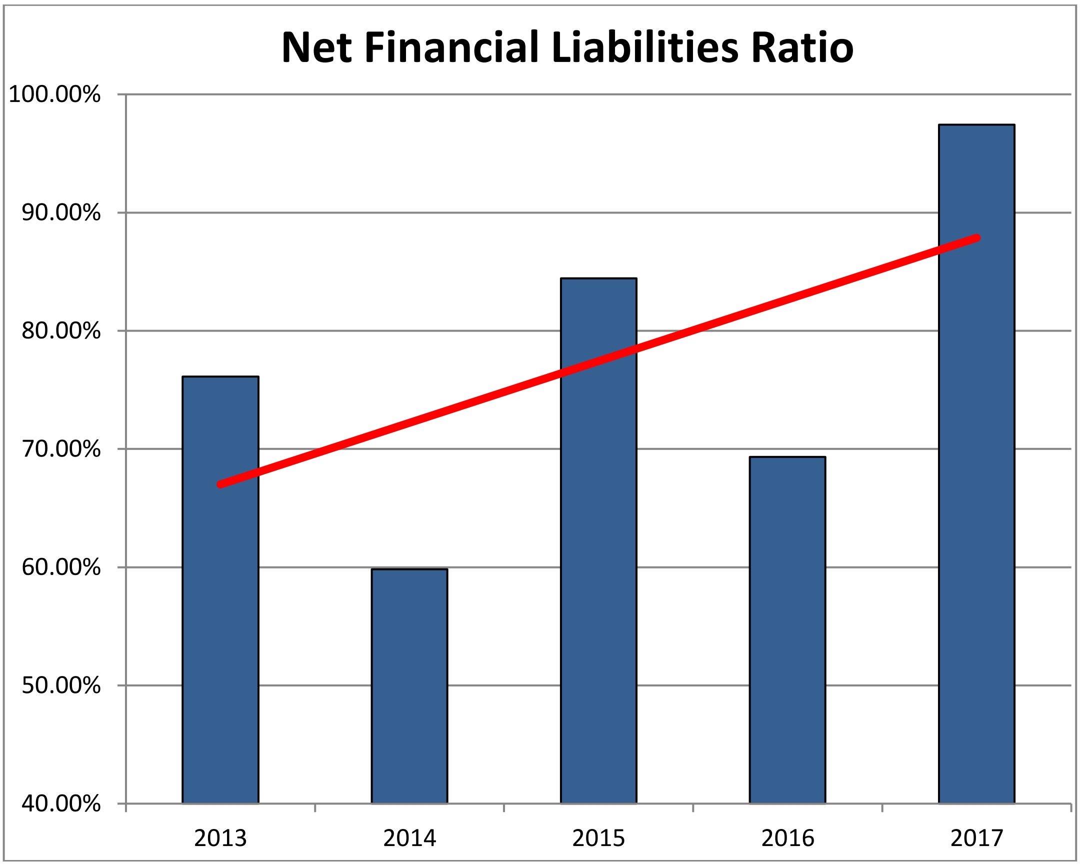


The benchmark proposed is 1.5, which indicates that Council has more cash and liquid assets than short-term liabilities if achieved.

In all years Council's ratio has been substantially greater than the benchmark indicating that Council has been able to meet all short-term liabilities comfortably.

4.3 Net Financial Liabilities Ratio

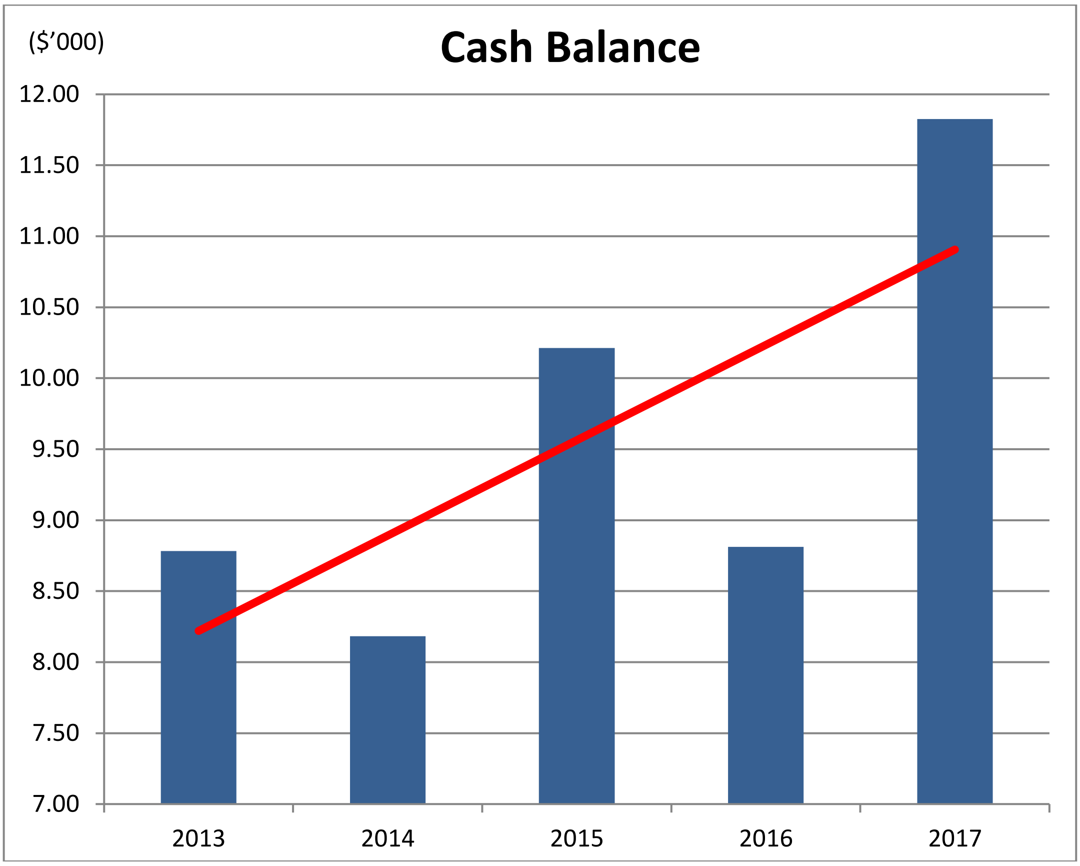
The Net financial liabilities ratio indicates the extent to which net financial liabilities could be met from operating income. It is a calculation of net financial liabilities divided by operating income.



4.4 Cash Balance

Cash represents money on hand at the end of each year. Some of this cash is restricted and must be used to meet long service leave obligations, grant funding obligations and to meet general working capital requirements at the beginning of the new financial year (for example to pay accounts payable as at 30 June).

The benchmark of $1.50 million is in excess of unspent grant funding.



5. Financial Projections

The financial statements included in the FMS portray the projected long-term financial position of the Southern Midlands Council over the next ten years.

The FMS presents financial statements, as follows:

- Comprehensive Income Statement
- Statement of Cash Flows
- Statement of Financial Position

The statements are prepared on current knowledge and will no doubt be affected by various events that will occur in future years. It is important that the long-term financial projections in this strategy be revisited and updated on an annual basis.

The model is a guiding document to be used during the budget deliberation process. If the general thrust of the document is followed Council will maintain financial sustainability.

5.1 Modelling Methodology

Following each Statement are descriptions of the assumptions specifically applied to produce the long-term estimates. On a more overall sense however, it is worthwhile detailing the approach to the modelling process as broad percentages have not been universally applied.

The forecast budget result for 30 June 2018 has been used as the base point used for modelling.

Whilst the FMS uses the more specific assumptions as detailed in the pages that follow, it will not remove the ongoing desire of Council to achieve operational efficiencies. The FMS is intended to establish a framework that Council can benchmark its performance and strive to exceed the targets set. Where further efficiencies can be achieved, funds will be dedicated to asset renewal or maintenance where applicable.

5.2 Summary Model Assumptions

5.2.1 Comprehensive Income Statement

The above statement has been prepared by setting percentage increases for the various classes of expenditure and income and then reviewing each general ledger account for areas where a variance to this pattern is likely to occur.

1. Rates - average real rate increases of up to 1.50% per annum over the life of the strategy.
2. Charges - average increase of up to 2.50% per annum over the life of the strategy allowing for the following adjustments:

    - User fees and charges reduced in YE 2019 by $176K to reflect closure of the Visitor Centre in October 2010.
    - User fees and charges reduced by a further $160K in YE 2020 due to planned privatisation of the Callington Mill milling operation.
    - User fees and charges increased by $130K in YE 2020 to recognise commencement of the new Aquatic Centre operation.

3. Commercial Revenue – this income relates to the consolidation of Council subsidiaries (i.e. Heritage Building Solutions Pty Ltd & HESC Ltd) – remain constant over the life of the strategy.
4. Grants – Financial Assistance Grant (FAG) for YE 2017 includes 50% of the 2017-18 entitlement which was received in advance. The continuing life of the strategy is then indexed at a rate of 2.00% per annum.
5. Grants – Non FAG – YE 2018 - as per budget. YE 2019 - $377K Roads to Recovery (balance of the 2014-19 program) plus $800K State Government (instalment 2 of $2.0 million) YE 2020 - $450K Roads (new program) which is included in each of the subsequent years) plus $400K State Government (final instalment of $2.0 million). No allowance made for other Grants on the basis that if received, it will be offset by related expenditure.
6. Investment Income – based on a rate of 2.00% per annum
7. Other Income - primarily relates to Dividends and other distributions received from Tas Water; and works undertaken on a recharge basis, has been indexed at the rate of 2.00% per annum. Reduction in YE 2018 due to the reduction in TasWater distributions (i.e. Dividends and Tax Equivalents)
8. Salaries & Wages - 0.00% real increase over the life of the ten-year plan (i.e. wage increases consistent with CPI). $347K has been deducted from the 2018/19 estimate due to overall staffing reductions reflecting the tourism centre closure. YE 2020 – Wages & Salaries reduced by $114K to reflect withdrawal (i.e. privatisation) of Milling Operations. YE 2020 - 5.00% real increase (equates to $180K) takes into account the commencement of the Aquatic Centre operation (i.e. current Pool salaries of $58 plus $180K – total of $238K.) Any additional increases granted in accordance with the Enterprise Bargaining Agreement will be offset through efficiencies and other savings.
9. Contractual Services (Materials & Contracts) – indexed at the rate of 1.50% per annum over the life of the strategy. YE 2019 – reduction of $115K to reflect closure of Visitor Centre (i.e. Retail/Café purchases etc.) YE 2020 – reduction of $76K to reflect withdrawal (i.e. privatisation) of Milling Operations. YE 2020 – additional 2.50% increase (over and above 1.50% increase) to reflect additional costs associated with Pool Operation.
10. Materials – incorporated in Contractual Services
11. Depreciation - Depreciation increase in YE 2019 by $52K; $87K in YE 2020; and $93K per year thereafter to reflect capital investment in Aquatic Centre. Amount is automatically calculated by the Financial Model based on capital expenditure – renewal and new assets.
12. Finance Charges - Amount is automatically calculated by the Financial Model based on the level of loan debt. The Model assumes that if there is available cash, it will be used to pay off debt.
13. Other Expenses - have been indexed by 1.50% per annum.

5.2.2 Statement of Cash Flows

This statement includes the cash based transactions shown in the Income Statement with the addition of estimated capital movements.

5.2.3 Statement of Financial Position

1. Financial Assets - Cash and cash equivalents - Council needs to make sure that enough funds are on hand each year end to meet all current liabilities. This model will ensure Council's cash liquidity. A measure of liquidity is the current ration which is discussed within this strategy.

2. Financial Assets - Current Trade and other receivables - current balance for receivables has been maintained
3. Financial Assets - Current Other Financial Assets - Nil
4. Financial Assets - Non-Current Other Financial Estimates - Nil
5. Non Financial Assets - Inventories – current balance for inventories has been maintained
6. Non Financial Assets - Investment property – Council's investment in Tas Water – current balance has been maintained
7. Non Financial Assets - Infrastructure, Property, Plant and Equipment – values are based on movement in depreciation, valuations and acquisition and disposal.
8. Non Financial Assets- Other Non-current Assets - Nil
9. Current Liabilities - Trade & Other Payables - current balance has been maintained
10. Current Liabilities – Borrowings – financial model assumes that all loan borrowings are repaid if cash is available
11. Current – Provisions – current balances have been maintained
12. Other Current Liabilities - Nil
13. Non-current - Trade & Other Payables - Nil
14. Non-current – Borrowings - financial model assumes that all loan borrowings are repaid if cash is available
15. Non-current – Provisions - current balances have been maintained
16. Non-current - Other Non-current Liabilities - Nil
17. Accumulated Surplus
18. Asset Revaluation Reserve – includes all Reserves - current balances have been maintained
19. Other Reserves – Nil

6. Key Strategic Outcomes

The following table highlights the outcomes, strategies and key actions of this LTFP. The key strategies provide direction for the preparation of the Council's Budgets.

Section	Outcomes	Strategy	Key Actions
Financial Indicators	Achieve a break-even positon within the ten-year period of the Strategy. That Council has enough cash to fund daily cash requirements and have flexibility to respond to unforeseen events and/or consider opportunities as they arise.	Council ensures compliance with the Long Term Financial Plan when developing future budgets. Council to achieve a consistent and gradual improvement in the Comprehensive Income Statement. Maintain a cash balance of $1.50 million in excess of unspent grant funding. Maintain a current ratio above the proposed benchmark of 1.5:1.	Council reviews and updates the long Term Financial Plan on an annual (ongoing) basis. Council continue to budget in accordance with the assumptions underlying the Long Term Financial Plan. Ensure that the budgeted cash position is sufficient to fund daily cash requirements as well as provide funding for unforeseen events and short term contingencies. Adopted budget maintains the minimum desired cash balance. Council monitor compliance with its investment policy.
Rating and other Revenue	Level of rating and and income from other charges is sufficient to achieve the break-even position. To provide a reasonable degree of consistency and stability in the level of the rates burden.	Council to consider the most appropriate rating strategy to provide adequate funds to achieve a gradual improvement in the Comprehensive Income Statement. Achieve a sustainable cash flow. Raise sufficient income to fund capital renewal projects	Council continue to budget in accordance with the assumptions underlying the Long Term Financial Plan. Council investigate other revenue raising sources to reduce burden on rate payers.

Section	Outcomes	Strategy	Key Actions
Asset Management	Maintenance of Councils existing assets at desired condition levels. Capital Works Program (Renewal) Capital Works Program (New)	Ensure that all Asset Management Plans are updated for all classes of the Council's assets with a focus on ensuring the assets are fit for purpose and provide the level of service to the community. That the Council allocates from operations cash funds equivalent to depreciation expense. This will enable the Council to achieve a renewal index of at least 1:1. Any new capital works (capital expenditure) proposals must include lifecycle cost evaluation exercise that identifies and costs the asset construction, maintenance, operating and depreciation costs i.e. Whole of lifecycle costs.	Regular review of all Asset Management Plans – process to include an assessment of service levels. Raise sufficient income (consistent with the LTFMP) to allocate towards renewal / replacement of existing assets. Review and finalise long-term capital works program and review on regular basis. Allocate a maximum of $250K per annum which can be allocated to investment in new assets. Subject to the preparation of 'whole of life cycle' cost estimate for inclusion on review of LTFMP.
Investments	Achieve optimum investment income and to ensure that cash is available when needed for planned expenditure	Ensure careful management of cash reserves Funds will be invested in a manner that allows them to earn interest for as long as possible while retaining flexibility in accessing those funds for Council purposes.	Invest surplus funds in accordance with Council's Investment Policy. Council will ensure that enough funds are on hand at 30 June each year to ensure that all current liabilities can be met.
Borrowings	That the Council undertakes actions to consider options available so that it continues to minimize overall reliance on borrowings	Any new loan borrowings are to be used to fund intergenerational capital investments where the community benefits are long term.	That the Council borrows funds for capital expansion projects that provide intergenerational equity. That the Council retains its debt servicing and redemption costs at or below 10 cents in the rate revenue dollar over the life of this LTFP
Statutory and Discretionary Reserves	That the Council generates sufficient funds from operations to fund daily operations and replace assets	That wherever possible any material favourable budget variations realized in a given financial year be specifically quarantined and reserved.	That the Council maintains discretionary reserves for stand-alone operations or investments.