

5.3.6 LATE ITEM: 2015/16 Draft Budget

Ward:	Both	Date:	22 May 2015
Precinct:	All	File Ref:	SC245
Attachments:	1 – Draft Budget Commentary 2 – Statutory Statements 3 – Management Statement – Detailed Nature and Type 4 – Management Statement – Summary of Income/Expenditure by Service Area 5 – Draft Capital budget 6 – Fees and Charges Schedule		
Tabled Items:	-		
Reporting Officer:	J Paton, Director Corporate Services		
Responsible Officer:	J Paton, Director Corporate Services		

OFFICER RECOMMENDATION:

That Council:

1. **ADVERTISES** the 2015/16 Draft Budget in accordance with the Community Consultation Policy No 4.1.5;
2. **NOTES** that any public submissions received in response to advertising of the Draft Budget will be presented to Council for consideration; and
3. **APPROVES BY ABSOLUTE MAJORITY** the:
 - a) establishment of an Asset Sustainability Reserve, with the following purpose:

“To assist Council in funding its long term asset management objectives by providing a means to spread the cost of intergenerational assets over multiple years”; and
 - b) transfer of any surplus for 2014/15 to the new Asset Sustainability Reserve to commence contributing funds to meet the City’s outstanding asset renewal obligations.

PURPOSE OF REPORT:

To consider the 2015/16 Draft Budget for advertising and to establish an Asset Sustainability Reserve to meet the City’s asset renewal obligations.

BACKGROUND:

Between 1 June and 31 August each year, local governments are required to prepare and adopt a budget for the financial year. A key part of the budget development is identifying the ‘budget deficiency’ to be made up from the levying of Council Rates. Once an estimate of that budget deficiency is known, local governments are required to give local public notice of any intention to levy differential rates.

Council considered a proposal to levy Differential and Minimum Rates at its Ordinary Council Meeting held 5 May 2015 and adopted the following resolution:

“That Council:

1. *APPROVES advertising by local notice, in accordance with Section 6.36(1) of the Local Government Act 1995 its intention to levy the following Differential Rates and Minimum Rates in 2015/16 to include an invitation for submissions on the proposal from electors and ratepayers for a period of 21 days:*

Rating Category	2015/16	
	Rate-in-\$	Minimum
Residential	0.05951	\$907
Commercial Vacant	0.11578	\$1,414
Other	0.06281	\$907

2. *NOTES any public submissions received in response to the invitation will be presented to Council for consideration.”*

In developing the Draft Budget, the following timetable has been followed:

DATE	ITEM/ACTIVITY
March 2015	Budget inputs
9 April 2015	Preliminary Budget prepared
14 April 2015	Council member Budget Workshop 1
21 April 2015	Council Member Budget Workshop 2
5 May 2015	Ordinary Council Meeting – Proposed Differential Rating
12 May 2015	Differential rates - Advertised for public comment (21 days)
2 June 2015	Ordinary Council Meeting - Draft Budget
3 June 2015	Differential Rating - Public comment period closes
9 June 2015	Draft Budget - Advertised for public comment (14 days)
24 June 2015	Draft Budget - Public comment period closes
7 July 2015	Special Council Meeting – Adoption of Budget
27 July 2015	Rates distributed

It is noted that the public submission period for the Differential and Minimum Rates expires on 3 June 2015 and will be incorporated into the Budget Adoption report. In the interim, any submissions received prior to the compilation of the agenda for the Ordinary Council Meeting of 2 June 2015 will be incorporated into this report.

In developing the Draft Budget, it has been necessary to undertake a significant review of the current financial position and past budget decisions and practices that have contributed to this position. Key elements of that review have been incorporated into a Budget Commentary document (see **Attachment 1**).

Major observations from that document that have been used to inform the Draft Budget include:

- The City’s Underlying Operating result for the last five years has consistently been a deficit.
- The Own Source Revenue Coverage Ratio for 2012/13 was in the ‘Intermediate’ standard, 2013/14 in the ‘Advanced’ standard and also reached the ‘Advanced’ standard in the 2014/15 Revised Budget. This ratio measures a local government’s ability to cover its costs through its own revenue efforts. This is generally a good outcome, demonstrating that despite the operating deficits, the City has the capacity to fund its operations, including the depreciation component (which can loosely be aligned to renewal expenditure demand).

- The Asset Sustainability Ratio for 2013/14 was 0.5 and 0.4 for the 2014/15 Revised Budget, which indicates the City would not have been replacing or renewing existing assets at the rate the overall asset stock was wearing out.
- The City has the lowest Minimum Rate in the metropolitan area, when the waste collection charge is factored in and the fourth lowest rates of the 29 local governments benchmarked.
- The City appears to have a significant proportion of depreciable assets, including buildings and other structures that contribute to the level of depreciation which is contributing to some of the unfavourable Ratio results.

DETAILS:

The 2014/15 Draft Budget as presented, includes the following components:

- Statutory Budget Statements (**Attachment 2**)
 - Statement of Comprehensive Income by Nature and Type – this statement details the Operating income and expenditure categorised by the nature of the income or expenditure, together with non-operating (capital) grants and profit/loss on asset disposal. Details of the 2014/15 Adopted and Revised Budget, together with year to date Actual are included for comparative purposes.
 - Statement of Comprehensive Income by Programme – this statement categorises the income and expenditure by the Program (function) it applies to.
 - Rate Setting Statement – this statement identifies the amount of rates necessary to undertake all activities for the year, once all income is recognised, non-cash items are adjusted back, Reserve transfers are incorporated and opening balance is factored in.
- Management Statements
 - Income Statement: Detailed Nature and Type – this Statement expands the level of detail summarised in the Statutory Statement of Comprehensive Income and shows the total Operating Income or Expenditure within the individual activities at the overall organisation level. (**Attachment 3**)
 - Summary of Income and Expenditure by Service Areas – this statement provides a breakdown of the organisation by service area and a summary of the applicable Operating Income and expenditure. (**Attachment 4**)
- 2015/16 Draft Capital Budget (**Attachment 5**)
- Fees and Charges Schedule (**Attachment 6**)

Operating Budget

	2012/13	2013/14	2014/15			2015/16
	Audited Actual	Audited Actual	Adopted Budget	Revised Budget	Forecast	Draft Budget
REVENUE						
Rates	23,825,952	25,362,390	26,909,021	27,302,021	27,418,736	29,063,813
Operating Grants, Subsidies and Contributions	1,567,459	1,435,384	2,473,885	1,493,840	1,542,267	1,565,895
Fees and Charges	15,304,231	19,187,447	20,337,630	20,747,640	19,628,090	20,984,415
Interest earnings	1,243,366	897,486	854,120	854,120	970,858	785,980
Other Revenue	3,590,513	1,099,417	163,975	1,144,020	1,240,142	1,128,305
	45,531,521	47,982,124	50,738,631	51,541,641	50,800,093	53,528,408
EXPENDITURE						
Employee Costs	(20,737,967)	(22,996,728)	(19,008,330)	(23,097,796)	(23,243,109)	(24,790,490)
Materials and Contracts	(14,495,855)	(14,385,556)	(15,054,925)	(15,348,526)	(14,417,443)	(15,728,520)
Utility Charges	(1,983,195)	(2,176,874)	(1,914,770)	(1,914,770)	(1,950,000)	(1,946,150)
Depreciation on Non-Current Assets	(8,906,059)	(11,760,170)	(8,566,790)	(11,223,490)	(11,223,490)	(11,144,595)
Interest Expenses	(1,199,652)	(1,145,812)	(1,096,580)	(1,096,580)	(1,096,580)	(991,375)
Insurance Expenses	(794,498)	(878,414)	(915,330)	(1,136,305)	(1,165,332)	(1,009,145)
Other Expenditure	1,204,412	(449,720)	(4,972,685)	(906,219)	56,192	(156,870)
	(46,912,814)	(53,793,274)	(51,529,410)	(54,723,686)	(53,039,762)	(55,767,145)
OPERATING RESULT	(1,381,293)	(5,811,150)	(790,779)	(3,182,045)	(2,239,669)	(2,238,737)

The above table shows the movements in the Operating Budget since 2012/13. It is of note that the most significant increase occurred in 2013/14 and a substantial contributor to that was the increase in Depreciation resulting from the phased introduction of the Fair Value method of asset valuation. The forecast actual for 2014/15 is reflecting well in comparison to 2013/14, although valuation updates are still being received, which may yet have an impact on the depreciation charge in 2014/15. This is a non-cash expense, but does impact on reported results and ratios.

The total Operating Revenue is reflecting an increase of 3.8%, compared to the 2014/15 Revised Budget. Significant factors include:

- Rates is an overall 6.5% increase. (For details on the rating strategy, see Section 9)
- The 2014 Federal Budget froze indexation of the Commonwealth Financial Assistance Grants for a three year period commencing 2014/15. Therefore, the relevant budget provision (\$1.129 million) will remain the same until 2016/17.
- Fees and Charges are providing a very moderate 1% increase compared to the 2014/15 Revised Budget, however a 6.9% increase on the forecast actual for 2014/15. The Fees and Charges Schedule (**Attachment 6**) has been reviewed to update those charges prescribed by legislation and provide appropriate indexation to others.
- Interest on investment is a reduction of 8% reflecting lower interest rates and portfolio balance.

The total Operating Expenditure Budget is reflecting a 1.9% increase over the 2014/15 Revised Budget. Major factors impacting on the level of increase over 2014/15 include:

- Annual indexation of employee costs, together with a provision for an additional five positions. It is proposed to increase the establishment by seven, however two of those positions are currently on contract in Planning and not an actual increase to the budget.
- A 7% increase (\$24,000) has been allowed to cover an increase in the annual Perth Parking Licence (levy). The new rate has recently been published in the Government Gazette and it is reflecting a 22.4% increase in the fee (\$995.80 per bay up from \$813.30). As a result, a further adjustment will be required to increase the budget by \$34,500 to cover the increase in the licence fee.
- Leasing costs have been increased by the value of additional equipment leases.
- An \$80,000 provision for the cost of the 2015 local government elections to be undertaken by the Electoral Commission.
- Various consultancy fees, including a provision for finalisation of the City's Asset Management framework and other strategic projects associated with the Strategic Community Plan and Corporate Business Plan.
- A reduction in the Interest Expenses budget, partially linked to the reduction in the loan balance following the proposed repayment of Loan No 7 (81 Angove Street), which is scheduled to occur following Settlement on the sale of this property prior to 30 June 2015.

Non-Operating Budget

The 2015/16 Draft Budget has factored the following non-operating income and expenses:

- Capital Grants to the value of \$1,462,428, directly related to specific projects listed in the Capital Budget.
- Proceeds from the disposal of Assets to the value of \$2,089,333. This relates to:
 - Sale/trade in value of \$256,000 associated with the light fleet and heavy plant replacement programme, as listed in the Capital Budget.
 - Payments from the Tamala Park Regional Council of \$1,833,333 for the City's share in the proposed land sales.
- Non-cash entries for Profit/Loss on Asset Disposals, related to the items above.

In addition, the Rate Setting Statement also lists the Principal loan repayments scheduled for 2015/16, being \$760,288. This is reflecting a substantial reduction on 2014/15 total of \$1,743,478, which included scheduled principal repayments and a lump sum payout of Loan No. 7.

Capital Budget

The table below compares the 2015/16 Draft Capital Budget (as detailed in **Attachment 5**) against the Adopted and Revised Budget for 2014/15. In comparing the totals, it is important to recognise that the 2014/15 Adopted Budget included carry forward projects to the value of \$6,753,959, with the new projects totalling \$10,141,875. Carry forwards will 2015/16 will be reported in the Draft Budget to be presented to the Special Council Meeting on 7 July 2015.

Category	2014/15		2015/16
	Adopted Budget	Revised Budget	Draft Budget
Land & Buildings	1,774,275	1,038,275	2,151,876
Infrastructure Assets	13,762,767	10,988,071	5,455,658
Plant and Equipment	1,205,167	1,854,775	1,627,650
Furniture and Equipment	153,625	209,075	364,800
Total	16,895,834	14,090,196	9,599,984

Key Projects scheduled to be undertaken in 2015/16 include:

- Cheriton Street Redevelopment (Community Centre) \$653,000
- Britannia Reserve – installation of path lighting (stage 2) \$140,000
- Black Spot intersection projects \$180,000
- Mary Street Piazza Development \$165,000
- Other 'Place Making' Initiatives \$202,000
- Bicycle Network and Travelsmart projects \$1,403,000
- Greening Plan projects \$297,500
- Public Artwork projects \$227,500

Following Budget Workshop 2, the following adjustments have been made and are drawn to the attention of Council:

Land and Buildings

- A new budget item has been listed for consideration:
'Depot fitout and relocation expenses' \$70,000

Plant and Equipment

- The budget for Parking Machines has been increased by \$2,250 to provide for the purchase of a spare cash box with each machine.

For the avoidance of doubt, the following projects deferred by Council during the Budget review last year have not been included in the 2015/16 Draft Budget.

The principle reason for omitting these projects is that prioritisation should be undertaken in context of the broader asset management review to be undertaken during 2015/16.

Unless otherwise determined by Council, these projects will not be carried out in the new financial year and will in future need to compete with all other new capital projects and asset management items.

- Forrest Park Croquet Club - W/C & Change rooms \$40,000
- Woodville Res pavilion - Air con \$15,000

Cash Backed Reserves

The Rate Setting Statement reflects transfers to Reserve of \$3,834,397, with the transfer from Reserves totalling \$1,737,050, thereby providing in the 2014/15 Draft Budget for a net inflow to the City's Reserves.

The transfers from Reserve are funding specific projects listed in the Draft Capital Budget (**Attachment 5**). Transfers to Reserves is made up of the following:

- \$203,680 interest earnings from the Reserves and reflects the anticipated income listed in the Operating Budget (0304: Interest Received Reserve – Detailed Nature and Type Statement)
- \$250,000 to the Cash in Lieu of Parking Reserve and reflects the anticipated income listed in the Operating Budget (0072: Cash in Lieu Contributions – Detailed Nature and Type Statement).
- \$6,900 to the Loftus Community Centre Reserve and reflects income received from the Lessee as prescribed under the lease for asset management.
- \$63,900 to the Loftus Recreation Centre Reserve and reflects income received from the Lessee as prescribed under the lease for asset management.
- \$12,000 to the State Gymnastics Centre Reserve and reflects income received from the Lessee as prescribed under the lease for asset management.
- \$1,833,333 proceeds/dividend payment from Tamala Park Regional Council.
- \$1,464,584 transfer to a proposed new Asset Sustainability Reserve.

LEGAL/POLICY:

The following clauses from the *Local Government Act 1995* are relevant to the preparation of the Annual Budget.

6.2. Local government to prepare annual budget

- (1) *During the period from 1 June in a financial year to 31 August in the next financial year, or such extended time as the Minister allows, each local government is to prepare and adopt*, in the form and manner prescribed, a budget for its municipal fund for the financial year ending on the 30 June next following that 31 August.*

** Absolute majority required.*
- (2) *In the preparation of the annual budget the local government is to have regard to the contents of the plan for the future of the district made in accordance with section 5.56 and to prepare a detailed estimate for the current year of —*
 - (a) *the expenditure by the local government; and*
 - (b) *the revenue and income, independent of general rates, of the local government; and*
 - (c) *the amount required to make up the deficiency, if any, shown by comparing the estimated expenditure with the estimated revenue and income.*
- (3) *For the purposes of subsections (2)(a) and (b) all expenditure, revenue and income of the local government is to be taken into account unless otherwise prescribed.*
- (4) *The annual budget is to incorporate —*
 - (a) *particulars of the estimated expenditure proposed to be incurred by the local government; and*
 - (b) *detailed information relating to the rates and service charges which will apply to land within the district including —*
 - (i) *the amount it is estimated will be yielded by the general rate; and*
 - (ii) *the rate of interest (if any) to be charged by the local government on unpaid rates and service charges;*

and
 - (c) *the fees and charges proposed to be imposed by the local government; and*
 - (d) *the particulars of borrowings and other financial accommodation proposed to be entered into by the local government; and*
 - (e) *details of the amounts to be set aside in, or used from, reserve accounts and of the purpose for which they are to be set aside or used; and*
 - (f) *particulars of proposed land transactions and trading undertakings (as those terms are defined in and for the purpose of section 3.59) of the local government; and*
 - (g) *such other matters as are prescribed.*

- (5) *Regulations may provide for —*
- (a) *the form of the annual budget; and*
 - (b) *the contents of the annual budget; and*
 - (c) *the information to be contained in or to accompany the annual budget.*

The fees and charges schedule has been reviewed in conjunction with the Budget development. The following provisions are relevant to the implementation of fees and charges.

6.16. Imposition of fees and charges

- (1) *A local government may impose* and recover a fee or charge for any goods or service it provides or proposes to provide, other than a service for which a service charge is imposed.*
** Absolute majority required.*
- (3) *Fees and charges are to be imposed when adopting the annual budget but may be —*
- (a) *imposed* during a financial year; and*
 - (b) *amended* from time to time during a financial year.*
- * Absolute majority required.*

Community Consultation Policy No. 4.1.5.

Policy No 4.1.5 prescribes the Draft Budget to be advertised via a local public notice for a period of 14 days. Copies of the Draft Budget will also be placed on the City's website and in the Library. The Policy also requires a letter and copy of the Draft Budget to be sent to local business and community groups.

STRATEGIC IMPLICATIONS:

Council's budget process is in accordance with Council's Strategic Community Plan 2013-2023 and Corporate Business Plan 2013-2017, Objective "4. Leadership, Governance and Management":

"4.1.2 Manage the organisation in a responsible, efficient and accountable manner"

"4.1.4 Plan effectively for the future":

SUSTAINABILITY IMPLICATIONS:

A substantial part of the preparation of the Draft Budget has been establishing a better understanding of the City's current financial position and long term financial sustainability. This process has revealed a range of issues that impact on the confidence level of the City's forecasting capability beyond a 12 month period. This is primarily due to the following issues:

- The standard of the Strategic Community Plan and associated Corporate Business Plan and level of integration to the City's Resourcing Plans;
- The extent of asset data available to support the Asset Management Plans, to define and effectively plan for asset renewal/replacement requirements; and
- The absence of a 10 Year Capital Works Program to inform the Long Term Financial Plan.

Plans are being developed and factored into the 2015/16 Draft Budget to prioritise the implementation of a range of corporate projects over the next 12 months to develop the strategic management capacity of the City. This includes the review of the Strategic Community Plan, Corporate Business Plan and to progress the asset management data capture and renewal planning. This will enable an integrated approach to the 2016/17 Budget preparation, including development of an informed 10 Year Capital Works program, which will in turn facilitate the enhancement of the City's 10 Year Long Term Financial Plan.

In the interim, the development of the 2015/16 Draft Budget, has been undertaken with a view to improving some of the fundamentals for long term financial sustainability. This includes a number of Budget Principles proposed to establish guidelines, objectives and strategies to progressively enhance the financial performance of the City and ensure sustainable service delivery for our community. These include the establishment of an Asset Sustainability Reserve to enable the accumulation of funds for the capital renewal expenditure associated with the City's intergenerational assets.

FINANCIAL/BUDGET IMPLICATIONS:

Following the public consultation process for the Draft Budget and Differential/Minimum Rates, it is proposed to present the Draft Budget with any submissions received to a Special Council Meeting scheduled for 7 July 2015. Subject to Adoption, the Rates notices would then be able to be distributed from 27 July 2015.

COMMENTS:

The 2015/16 Draft Budget is considered overall, to be a consolidating budget. Operationally, it is stable, with the Capital Budget funded within the annual financial capacity. However, it is recognised that the state of data held on the current condition and renewal/replacement requirements for depreciable assets, means there is a risk that an asset renewal backlog liability exists.

This risk is supported by various prescribed ratios which would indicate the City has not been consistently renewing and replacing its assets at the same rate that they have been consumed (as reflected through depreciation). Given the experience of other local governments in dealing with significant asset renewal backlogs, a major focus of this budget has been to commence a process of quantifying the risk and developing funding strategies.

To assist in this process, a range of Budget Principles are proposed, to assist in guiding future decisions. The financial assessment and rationale is detailed in section 8 of the Budget Commentary document (**Attachment 1**), however the general premise is the City has a stewardship role of assets that provide services across generations. It is therefore important that servicing of those inter-generational assets, including decisions of maintaining, renewing and replacement are undertaken within a long term and sustainable financial framework, minimising impacts on rates and/or debt levels.

In order to achieve this, within the financial capacity of the community, this will involve a range of strategies, including:

- optimising the level of rates generated;
- identifying opportunities for widening or increasing the City's other source revenue;
- reviewing the range and standard of services provided by the City;
- seeking opportunities to achieve operational efficiencies; and
- prioritisation of asset renewal within the capital works program.

Budget Principles:

1. Budgets should aim to achieve a balanced Underlying Operating Result (to ensure an appropriate level of funding is available to service the asset renewal demand – aligned to the level of depreciation).
2. In accordance with Policy 2.2.12 Asset Management, capital renewal expenditure will be prioritised ahead of new capital expenditure, unless cost benefit analysis justifies otherwise.
3. The LTFP must be supported by a 10 Year Capital Works Program that matches the annual works program with the financial and resourcing capacity of the City.
4. An Asset Sustainability Reserve shall be established to benefit Council and ultimately the community, by enabling the allocation of funds for future capital expenditure for the purpose of replacing and renewing intergenerational assets. This will assist in minimising impacts on rates and/or debt levels.
5. The Asset Sustainability Reserve shall be funded from planned surpluses identified in the Long Term Financial Plan. Improved performances which result in an end of year surplus, will also be transferred to the Reserve, to ensure consistent funding source allocation, rather than the potential for the surplus to be used to subsidise subsequent budget and rating decisions.
6. Proceeds from Asset disposal shall be available to be applied to expanding and enhancing the level of services and facilities provided by the City.
7. Financing the services and facilities provided by the City is a shared responsibility and should be met equitably through the adoption of a Differential Rating system and establishment of Minimum Rates at a level that recognise a minimum cost of services available to all ratepayers regardless of the value of their property.
8. Reserves are to be used to smooth out significant expenditure requirements listed in the LTFP, to minimise disproportionate impacts on rates or demand to increase debt.

In addition to consulting on the Draft Budget, given it is likely the net result for 2014/15 will now be a surplus, substantially driven by improved level of proceeds from the sale of assets, it is proposed to seek Council's approval to establish the Asset Sustainability Reserve and endorse the transfer of the surplus to the new Reserve.