SURF COAST SHIRE COUNCIL

Our Financial Story

Surf Coast Shire Council is a regional local government authority, located an hour south-west of Melbourne. The municipality has an approximate population of 33,000 in 2020, a mix of coastal and hinterland communities and has experienced strong overall population growth over recent decades.

Council provides 100+ services to the local community, and maintains $800 million worth of community assets to support both the local population and the 2.5 million people who visit the area on an annual basis.

The purpose of this document is to share the financial challenges faced by Council and to outline the important principles that underpin the development of its annual budgets and financial plans. By sharing these challenges and principles with the community, Council hopes to inform and engage its most critical stakeholders in finding solutions to Council's financial challenges.

Council has a 10 year rolling financial plan, called the Long Term Financial Plan to inform Council's decision-making. The Long Term Financial Plan, and Financial Principles, have been developed through extensive review and refinement over a number of years.

The **Challenge**

Council has a responsibility to current and future communities that leads to significant demands on its finances, in particular:

- An asset renewal requirement that is increasingly falling due
- The expectations of a growing community for new initiatives and ongoing services

The Victorian State Government introduced the "Fair Go Rates" legislation in 2016, and since then, rate revenue increases have been capped to State Government inflation forecasts.

Whilst acknowledging that household affordability is important, the introduction of rate capping has significantly constrained revenue for local government authorities. Council must carefully consider the allocation of its financial resources in this environment and continue to pursue important efficiency reforms.

Asset **Renewal**

Council's delivery of services significantly depends on maintaining its assets in good condition for as long as the community needs them.

Council's asset management practices are mature and incorporate infrastructure and financial elements of the asset base. This includes thorough and extensive asset condition reviews that feed into detailed asset modelling. This modelling takes account of asset use and ageing, and ensures that Council can plan to renew its assets when this will be required.

The asset modelling then projects the asset renewal demand over the coming 20 years and calculates a smoothed annual allocation for asset renewal. This has been formally documented in Council's Asset Renewal Funding Strategy and is considered a foundation for the Long Term Financial Plan.

When assets have reached a condition where renewal is desired, but funding may not be allocated at that time, they are referred to as Council's "Asset Renewal Backlog". Until recently, this backlog was sitting at a very low level of $2 million, or 0.25% of the asset base, which is much lower than the industry norm. However, a large portion of Council's assets are becoming due for intervention, meaning that Council must start allocating more funds to asset renewal soon, or service levels may reduce.

Council's Asset Renewal Funding Strategy recognises the additional investment that is required to maintain its ageing assets, and shows a requirement for a significant increase in annual asset renewal funding going forward. Current modelling shows that an increase of 9.5% in funding is required every year for the next 20 years. In the Long Term Financial Plan, that equates to an increased allocation to asset renewal, moving from $7 million per year in 2020 to $16 million per year in 2030.

The growing need for asset renewal expenditure is a significant challenge for Council and without major reform to Council's services and operations it will mean less money is available to fund new initiatives and existing services.

New **Initiatives**

Council's Long Term Financial Plan in 2020/21 has almost $7 million of funding allocations to provide for new initiatives that are important to support a growing and changing community, including:

- Projects identified within Development and Infrastructure plans,
- Loan principal and interest costs, noting loans were used to fund new infrastructure, and
- Annual allocations towards new discretionary initiatives, which are important projects that respond to current issues and demands.

Council does have some funding sources that assist with new initiatives, including:

- Development and Infrastructure plans are strategically important because they ensure developer contributions are committed with certainty, however these also create long-term commitments from Council.
- Council has been successful at attracting grants from other levels of government to help fund new projects. This partnership funding remains essential however it is important to note that the operating and future renewal costs will still fall to Council and must be taken into account.
- New residential developments in the Shire do provide increased rate revenue for Council which can help fund new items, and these supplementary rates are important. However, the growing community also needs Council to deliver new services, and maintain and renew new assets when necessary, so the supplementary rates do not solve Council's financial challenges.

It is important to acknowledge these sources of funding do provide support for new initiatives. However, Council needs to consider the funding it would require to contribute under any funding agreements and the level of discretionary funding it wishes to have available. Council's capacity to provide this funding is reducing over time and this will lead to it being unable to meet the expectations of its growing community.

Transition **Strategy**

Despite Council's challenging financial situation, it has sufficient financial reserves to cover annual shortfalls in the medium term. Accordingly, the Long Term Financial Plan still sees about $7 million per annum available for new initiatives for most of the life of the plan. And for communities not growing, the increasing commitment to asset renewal aims to ensure that they can continue to benefit from the assets that they enjoy today.

Drawing on reserves to support these allocations does not however solve the underlying issue and is not sustainable. Ultimately, Council's operations need to generate sufficient surplus to adequately fund both new initiatives and the renewal of its existing asset base. Accordingly, Council needs to review what it delivers to the community and what this costs, to ensure it can afford to deliver services and initiatives into the future.

The Long Term Financial Plan indicates that by drawing on reserves, Council can maintain its current level of discretionary spending for most of the next ten years. But there is no capacity to respond beyond that to new challenges or opportunities, or even return to the higher levels of discretionary spending enjoyed in the past.

Council will have sufficient funds in its reserves to provide this cover for a number of years. If a longer term solution is not found, Council will need to adjust materially discretionary spending again. The changes needed to create greater financial capacity will require assistance and input from the community and other partners. This takes time and so it is important that Council continues to work on this challenge, identify solutions and make necessary changes soon.

Financial Principles

Long Term **Financial Plan**

1. The Long Term Financial Plan will be updated and endorsed as part of the annual budget process.
2. An unallocated cash deficit in any year must be funded by a reserve allocation; however this is only an interim solution with a strategy required to return to an ongoing surplus.
3. A minimum balance of $250,000 must be retained in the Accumulated Unallocated Cash Reserve to provide for unexpected demands.
4. New borrowings will only be taken where there is capacity to fund debt servicing costs for every year of the loan and will not be taken out to fund deficits or asset renewal requirements.
5. Proceeds from asset sales will be allocated to the Accumulated Unallocated Cash Reserve unless related to the sale of open space (ie. must be allocated to the Open Space Reserve).

Recurrent **EBITDA**

6. Focus on operational performance by budgeting and reporting against Recurrent EBITDA, as this provides the funding for funding allocations.
7. Recurrent EBITDA must include allowances for growth (both discretionary and non-discretionary) and compliance costs.
8. Growth in Recurrent EBITDA is required to fund increases in obligations and discretionary allocations.
9. Setting user fees and charges should be done with a view to minimising Council subsidy and to provide equity across user groups.
10. Projected Recurrent EBITDA savings must be realistic and driven by identified and funded initiatives.
11. Proposed discretionary projects that create new or improved assets must be assessed for the impact on Council's future Recurrent EBITDA and renewal requirements, and the ability for this to be afforded in the Long Term Financial Plan.

Allocations

12. Council must fund obligations before allocating funds for discretionary purposes.
13. Asset renewal is fundamental to Council's service and financial sustainability; the asset renewal allocation is derived from formal assessments and is one of Council's most important commitments.
14. Council's contribution to Developer and Infrastructure Plans and debt principal and interest form part of its allocation to new projects.
15. A consistent level of discretionary allocation should be provided across all years of the Long Term Financial Plan.