



ESSENTIAL SERVICES COMMISSION
Local Government

Higher cap – Application cover sheet (2016/17)

Horsham Rural City Council (HRCC)
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Base Average Rate per assessment 2015-16 (\$): \$1,747

Proposed increase for 2016-17:

Proposed increase in Average Rate %	3.5% (Cap plus 1%)
Proposed increase in prescribed rate revenue (\$)	\$736,941 (Cap \$526,941 + 1% \$210,000) (Total Rates \$21,814,600)

Summary of the key reason(s) for the application:

HRCC, like most council's, has previously identified a growing gap between the renewal spending required to maintain our existing assets and the available funding for that purpose. As a result, since 2008/09 we have been identifying a component of our rate rises and tagging that to specifically help contribute to this growing gap. During this time we have been actively pursuing service delivery efficiencies through a regular program of service reviews. We have also achieved efficiencies / reductions in expenditure to reduce over \$0.50 million from our operations budget over the last 3 years. This represents a real cut of 3% in operating costs whilst still maintaining service levels, with expanding population.

HRCC plays an important role as a regional city in the isolated western region of the state and continues to invest in new cultural, community and recreational facilities to provide services to the community beyond our municipality's boundaries. Current examples of this are: Leadership of the Grampians Peak Trail project, coordinating drought, aged care study, regional emergency management, GIS shared services, regional livestock exchange, regional Performing Arts Centre, secretariat to WHAC and to Wimmera transport group.

Council's rate increases since 2002/03 have been as follows:

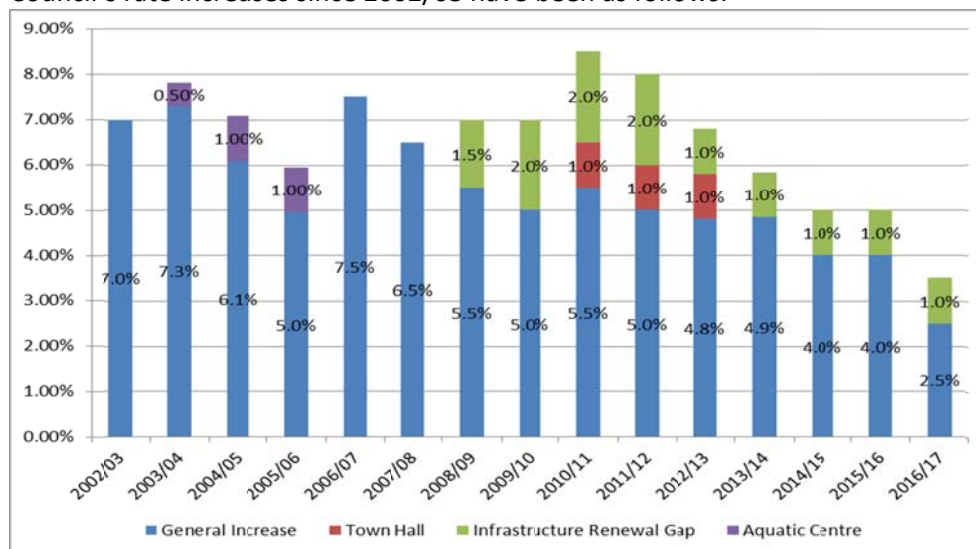


Figure 0.1

HRCC recognises the challenge of maintaining a large public asset base for the long term sustainability of the community. HRCC is addressing its social responsibility to manage these assets effectively for the best "long term" interests of the community. Reducing the rate base would not be an appropriate response with this growing asset renewal gap if we want to maintain the standards for our community. Short term thinking will not bring about the desired outcomes and impacts for our community. HRCC recognises that rates are a part of the overall tax burden on the community but is strongly of the belief that taxes are something that must be paid in order to have a strong and vibrant community for all.

The other side of this equation is that council does not "waste" funds on inefficient or ineffective services or service delivery. To this end HRCC has been implementing a regular service review program looking vertically down a number of its services each year in order to achieve efficiencies and improvements, at the same time attempting to look holistically across all services to ensure funds are targeted towards priorities identified by the community. HRCC does not wish to reduce

services, it believes it already uses resources efficiently and that continued efficiency improvements will occur over time with increased use of technology and gradual adoption of workplace change. Councils Enterprise Agreement has seen salary increases of 3.5% for the last 3 years and is being renegotiated now for the next 3 years. Salary increases of 2.0% have been budgeted for (plus allowance for band movement), and any increase beyond this, may be met by either reductions in service delivery, possible reductions in workforce, cuts to initiatives or capital investment.

Road infrastructure is a constant challenge for HRCC and all rural municipalities. HRCC has a network of 2,976 kilometres of road, 32% of which is sealed. This equates to around 7 people per kilometre of road. Soil substrates within the municipality have been identified as some of the most re-active across the state and this reduces the average life of a road. (Council has been lobbying the Victorian Grants Commission for some years to have this better recognised in the roads component of their grants calculations **SE 0.1 Submission to Victorian Grants Commission Feb 14**). Larger vehicles and more frequent road use as farming practises change and evolve is also significantly contributing to the deterioration.

Addressing the renewal gap through targeted rate rises has been a specific strategic objective for many years. It has been strongly articulated through the Council Plan, Asset Management Policy, Asset Management Improvement Strategy, Asset Management Plans, prior year's budgets and Strategic Resource Plans. This funding needs to continue for a number of years if we are to address the declining condition of our assets and complete the goal that has been started.

Councils Strategic Resource Plan from 2015-16 specified rate rises of 4.5% for the next 4 years comprising of a 2.5% rate rise for operations and a 2% allocation for Infrastructure Renewal. However, only a 1% rate rise for infrastructure renewal has been budgeted over the last four years since 2011/12 in recognition of the burden that rates place on the community, but at the same time additional expenditure on renewal has been achieved through an ongoing program of operational efficiency (**See Figure 2.3 Page 7**). The effect of drought on the community generally, in 2015-16 has also influenced HRCC's decision re the level of the Infrastructure Levy for 16-17.

The VAGO Report from Feb 2014 – Asset Management and Maintenance by Councils highlights the challenge for councils in maintaining and renewing assets. The Auditor General John Doyle in the Executive Summary states “A 1998 report to government warned that unless steps were taken to address council's asset renewal gaps, the budget councils require for renewal would more than double by 2012. These predictions have materialised despite this warning.” He goes on to say further in that summary “Without appropriate and concerted corrective action, the provision of council services to communities is likely to be put at risk. While this may require some hard financial decisions and trade-offs, failure to address this problem now will only lead to more difficult decisions in the future”.

HRCC has made and is continuing to make these hard decisions even with the introduction of rate capping as we recognise the importance and gravity of this situation for our community **SE 0.2 VAGO Report Feb 14 – Asset management and maintenance by Councils**.

Council is of the strong opinion that this strategy is both necessary and successful in dealing with this issue and wishes to continue with this into the future without the need to acquire further debt or to cut other services to meet this need.

Supporting Evidence

SE 0.1 – Submission to the Victorian Grants Commission Feb 14

SE 0.2 – VAGO Report Feb 2014 – Asset Management and Maintenance by Councils

1. CRITERION ONE – PROPOSED HIGHER CAP

An application must specify a proposed higher cap for each specified financial year.

Council is seeking a 1% increase over and above the 2.5% rate cap for 2016-17.

This is expected to generate additional rate revenue of \$210,000.

The calculation of the rate increase is as follows:

	2015-16 Budget	Rates for Cap Calc	2016-17 Draft Budget as at 22/3/16
Calculation of Rate Income:			
General Rates	-20,729,745	-20,729,745	
Rates - Supplementary	-100,000	-231,301	
Additional Supps est March - June		-12,650	
Annualise Supp Rates		-103,963	
Total Rates Incl Supps	-20,829,745	-21,077,659	-21,604,600
Rates Additional re 1% Cap Variation			-210,000
Rates Including 1% Variation			-21,814,600

Supporting evidence

*SE 1.1 Council Resolution – sign-off/approval of application> minutes from council 29 March
HRCC – ESC Rate variation 16-17 Ver2.xls (Budget Baseline Information)*

2. CRITERION TWO – REASONS

The reason(s) for which the council seeks the higher cap.

In formulating the 2016-17 Budget HRCC has contained cost increases within its operations to 2.04% increase on the 2015-16 budgeted figures. This needs to be considered in the context of 2.5% rate cap and also the freeze in the Financial Assistance Grants from the Federal Government. This freeze has seen effective reductions in HRCC's grant of \$0.15m per year or cumulative over the last 3 years a reduction of nearly \$1.0m and ongoing reductions from this year going forward of \$0.5m annually.

Cost savings achieved in the 2016-17 budget are across a range of service areas, but particularly in the back office areas where cost increases in the Corporate Services functions have been kept at 1.19% - cost savings have been achieved by recognising some staff savings in the customer service area as a result in part of decreased transactional workload as more transactions are undertaken electronically and also a change to casual backfill arrangements, otherwise non-salary cost increases have been kept to a minimum across the board. Savings have also been achieved in the Community Services Group through improvements in the delivery of HACC Services and operational impacts from a full year of operations of the new performing arts venue. This is a significant achievement given that salaries have been factored in at 2.5% (2.0% Increase plus 0.50% band movement).

Meanwhile, core functions of Planning, Building & Economic and Technical Services have had increases of just over 3% on the 15-16 Budget which is higher than overall increases due to the need to grow some service areas to meet the expanding needs of the growing community and to address the degradation of council's building assets.

Containing operational costs has enabled HRCC to continue to invest \$0.639m (\$0.592m in 15-16) for operational initiatives. These are specific one off budget items allocated to ensure that strategic objectives are met and further efficiencies are gained. At the same time spending from General Revenue on capital has increased by 10.8% or \$0.538m which is split 80% renewal & 20% new and upgrades. (The 1% rate cap variation, \$0.210m, is included in the \$0.538m and the 80% renewal.)

Road and related infrastructure assets comprise approximately 84% of Councils total asset base (excluding land) or \$341.4m based on current written down values. Based on our assessments of road decline alone, annual capital renewal expenditure needs to reach \$6.02m before it will keep up with the annual rate of deterioration of our roads.

In 2015-16 the revenue raised from the cumulative 11.5% of tagged rate rises since 2008/09 (see figure 0.1) was \$1.742m. A further increase of \$1.350m annually would be required to ensure that roads do not deteriorate from their current levels.

Similar challenges exist for our building assets which comprise approximately 12% of Councils asset base or \$50 million based on current written down values. However the exact value of renewal work required is not yet accurately determined for this class of assets and more detailed work is being undertaken and will need to be completed before this is known with the same degree of accuracy as we do for roads. It is however clearly evident within the community that further renewal works are long overdue for many of Council's building assets and this is an area where we need to start increasing renewal investment in the years ahead.

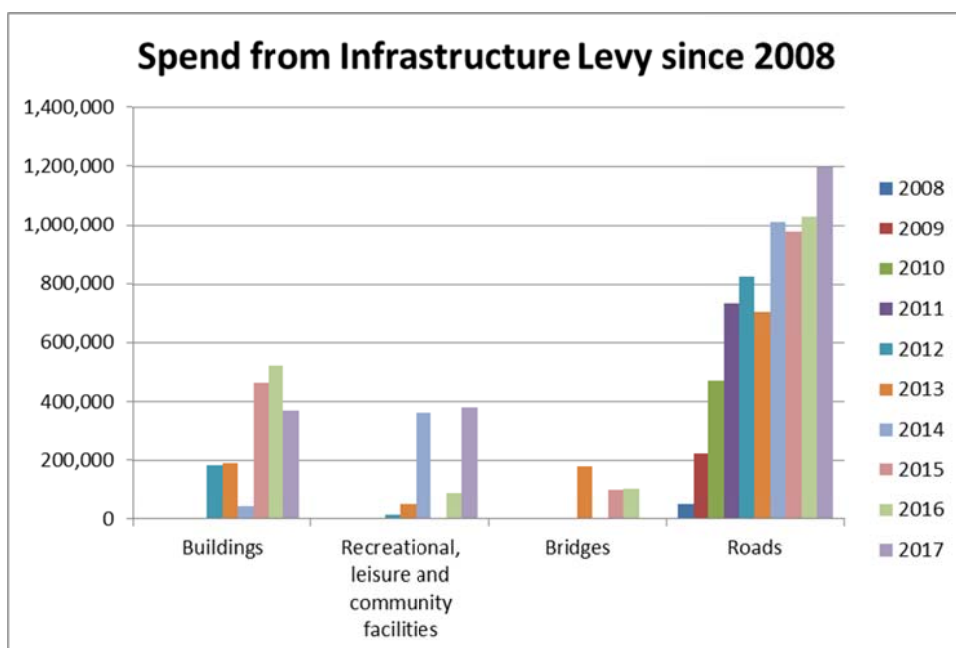


Figure 2.1

	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
Buildings	0	0	0	0	184,950	191,000	43,000	465,000	520,600	371,000
Recreational, leisure and community facilities	0	0	0	0	15,000	50,000	363,000	0	90,000	380,000
Bridges	0	0	0	0	0	180,000	0	100,000	105,000	0
Roads	50,000	226,000	470,600	734,000	826,050	706,000	1,012,000	980,000	1,027,400	1,201,000
	50,000	226,000	470,600	734,000	1,026,000	1,127,000	1,418,000	1,545,000	1,743,000	1,952,000

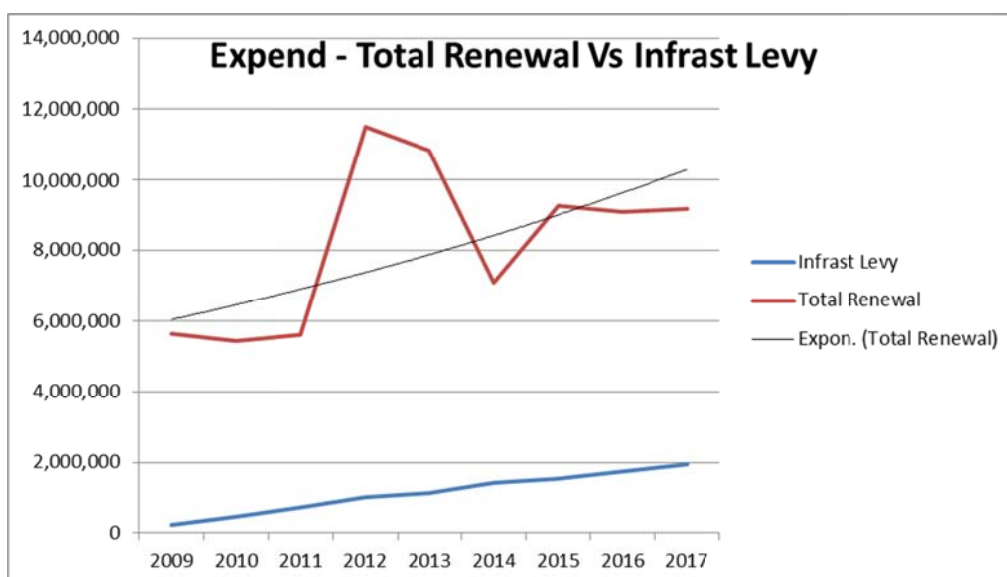


Figure 2.2

	2009	2010	2011	2012	2013	2014	2015	2016	2017
Infrast Levy	226,000	470,600	734,000	1,026,000	1,186,000	1,418,000	1,545,000	1,697,000	1,952,000
Total Renewal	5,636,524	5,438,076	5,607,460	11,513,422	10,839,000	7,100,000	9,253,000	9,087,445	9,168,768

Note: Source, Annual accounts until 2016 & 2017 where have used budget (excluding c/fwd). Peak in 2012 & 2013 as a result of flood recovery works.

HRCC's expenditure on renewals has been steadily increasing in total, not just from the Infrastructure levy, but also from General Revenues and Roads to Recovery. Funding from Reserves and Other Sources tends to fluctuate based on specific projects e.g. in 2015 the Horsham Town Hall and Performing Arts Centre included a significant renewal component from reserves.

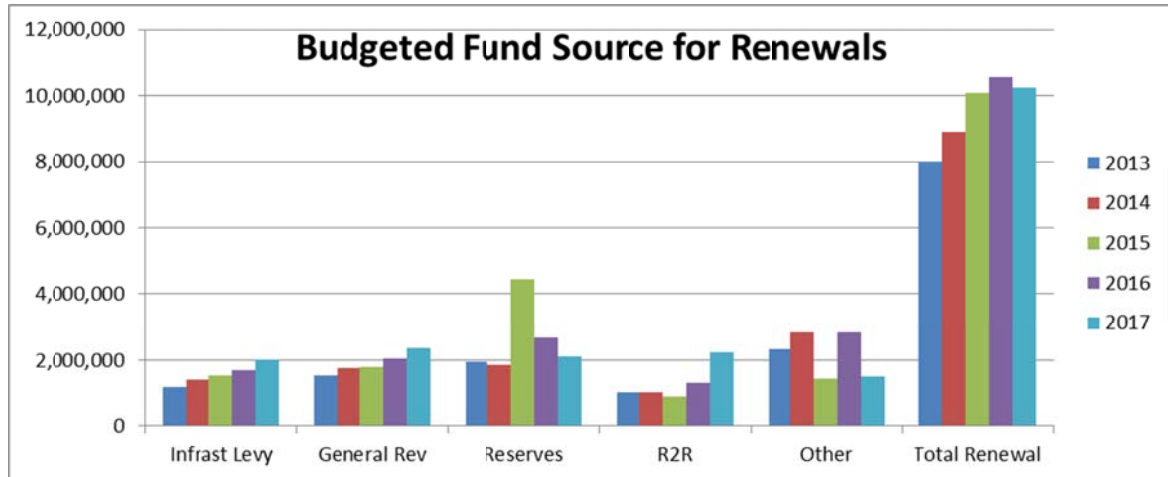


Figure 2.3 Note: These numbers are not adjusted for the impact of carried forward works between years.

Justification for 1% Rate Cap variation

HRCC employed Moloney Asset Management System to conduct the condition assessment of its entire road network in July 2014 as a part of its 3 yearly cycle of condition assessment. A comprehensive report was presented by Peter Moloney following the completion of condition assessment with all his findings and recommendations on how to manage HRCC's road assets in the long run. **SE 2.2 Moloney Road Report June 2014.**

Analysis of current and previous data (degradation curves and asset conditions) was undertaken to do the renewal forecasting for next 20 years. Any impact on the road infrastructure renewal demand impacts heavily on the entire asset renewal program.

Following are some of the findings and recommendations of the Moloney report.

- The total present renewal shortfall or backlog in over intervention assets for the whole roads group is estimated at \$6,524,768 representing 2.41% of the total road asset valuation. This is considered to be reasonable but it should not be allowed to grow.

Figure 1.2 below, shows that with current renewal expenditure, about 2.41% of road asset stock is over intervention (Approx. \$1.0m in 2014 and accumulating each year thereafter), or in simple terms needing some urgent renewal/rehabilitation works. This means that 1 in every 40 roads you come across are nearly in unserviceable condition. If the same amount of expenditure is continued for the next 20 years, the % of assets over intervention will jump to about 16% which means nearly 1 in every 6 roads are nearing end of their lives.

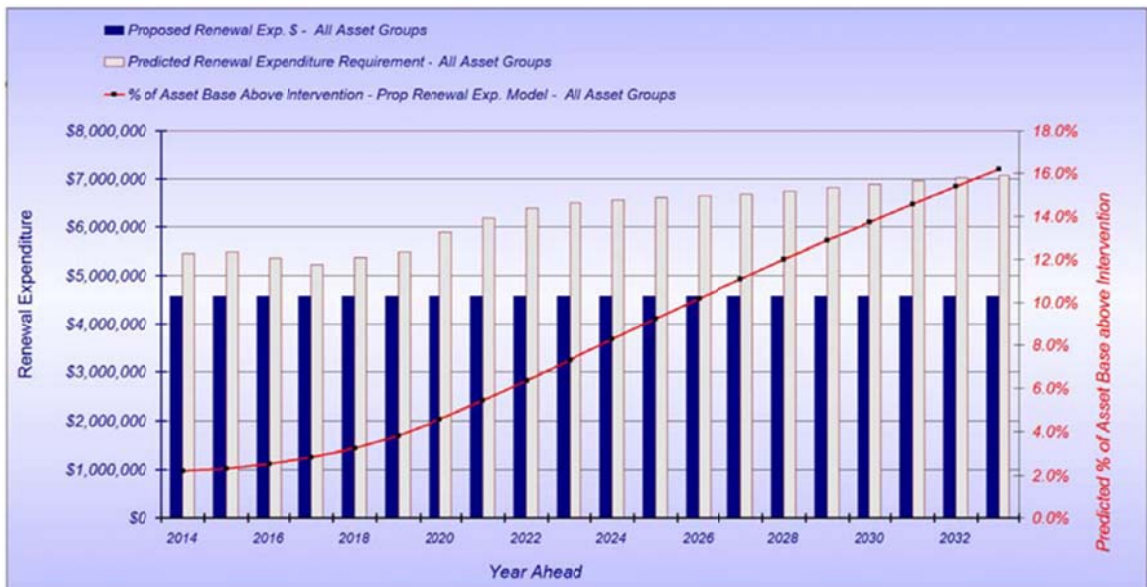


Fig 1.2 Future Predicted Condition Based on Continuation of Present Renewal Expenditure

Moloney say “Figure 1.2 indicates that if the current total level of renewal expenditure is maintained over the next 20-years, a steady rise in the total extent of over intervention assets will occur to dangerous and unacceptable levels. The upper limit of total assets over intervention on the road network is considered to be around 3.0% - 3.5%. The model predicts that council has 5-years at the current funding levels before this rises above 3.5%.”

- Renewal demand is predicted to rise steadily over the next 20-years as the assets age and it was found that at a whole of roads group level council needs to raise its total renewal expenditure by around 3.0% compounding for the next 10-years.

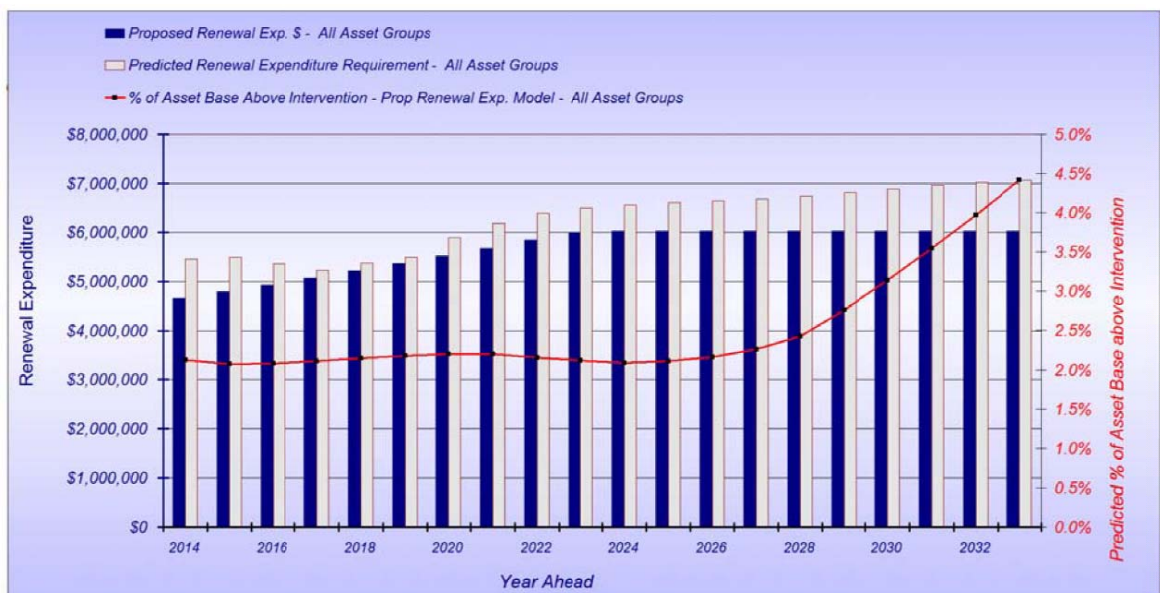


Fig 1.3 Recommended future funding profile with future predicted extent of over intervention assets

- Moloney recommends increasing the current renewal expenditure by around 3% compounding for next 10 years to maintain the current level of service in the road infrastructure (as represented in Fig 1.3 above). This increase will help maintain the % of

assets over intervention to about the level of 2.14% (same as current). It can be noticed that the red line (% of asset over intervention) starts rising rapidly after 2026. This implies that the current strategy needs to be revised in about 10 years.

- Moloney says “With ageing assets and some of the most difficult subgrades in the state the rising renewal demand should come as no real surprise”. **SE 2.2 Moloney Road Report June 2014** Figure 1.3 Page 8.

The figures quoted in the Moloney report from 2014 have not factored in additional funding of approximately \$2.2m for renewal works from the Roads to Recovery program. (In 2014/15 \$1.0m (all renewal), in 2015/16 \$2.154m for renewal and 2016/17 \$2.243m for renewal). These funds have helped address some of the backlog in roads but have not removed the underlying renewal gap problem and certainly has not addressed any renewal issues for HRCC’s buildings and other asset classes in a sustainable way.

HRCC’s Asset Management Plans have utilised the information from the Moloney Report to establish appropriate processes to address the growing renewal gap **SE 2.3 Asset Management Plan Part B Roads**, Section 6.7. Schedule 3 also shows financial projections based on the Moloney information.

Supporting evidence

SE 2.1 HRCC Full List of Infrastructure Levy projects.

SE 2.2 Moloney Road Report June 2014

SE 2.3 Asset Management Plan Part B – Roads

3. CRITERION THREE – ENGAGEMENT

How the views of the ratepayers and the community have been taken into account in proposing the higher cap.

HRCC has conducted budget engagement for many years in accordance with the requirements of Section 223 of the Local Government Act. Within these engagements HRCC's establishment of a tagged rate rise to address ageing infrastructure has always been a point of discussion. Projects that are then conducted using these funds are clearly sign posted to reflect they are being funded from this levy, thus insuring the community is well informed of this approach. The following sign is an example of a current project:



Figure 3.1 – Geodetic Road

However it has always been difficult to engage widely with a broad range of community members and the traditional approach of holding budget information sessions and promoting those as a means for people to come along and engage with Council has not been achieving the desired outcomes as attendance numbers in these have been declining. Over the last 10 years Council has received very minimal submissions to its annual budget (1 to 2 each year), therefore by default perhaps indicating broad acceptance of HRCC's budget direction.

- **ENGAGEMENT 2015-16**

As a result of declining attendance, a different approach was taken for the 2015-16 Budget, where a number of new ways to engage with the community were trialled. A drop-in session was introduced, 2 budget talks were held in Natimuk and Horsham, an electronic survey was promoted and 8 Budget talks were taken out to the community via attendance at service club meetings and other community groups. In these discussions HRCC addressed in total 227 members of the community (which was a significant improvement on the 5 to 10 people from previous years).

- **ENGAGEMENT 2016-17**

The engagement undertaken in 2015-16 has been further enhanced for the 2016-17 Budget. During 2015-16 HRCC reviewed its community engagement policy and framework and this has been used to

establish a detailed engagement plan, which is contained in the report to council **SE 3.2 Report to Council on Community Engagement 2016-17**. The core activities in this engagement plan are to conduct the usual community budget sessions, continue to speak with community groups and to broaden the number and type of groups that we want to offer this to, conduct an electronic survey that is more targeted and easier to complete, promote opportunities for engagement across a broader range of media than just the local newspaper, speak regarding councils budget on public radio as and when possible.

- **CONTENT AND FEEDBACK**

The presentations provided at both the 2015-16 and 2016-17 budget engagements sessions are provided as **SE 3.3 Example of 2015-16 Budget presentation & SE 3.4 Example of 2016-17 Budget presentation**. Essentially the focus of these engagements were to increase the understanding of how council's budget is made up and the services that council provides, then to discuss the challenges of balancing the budget and the constant need for compromise and trade-offs in establishing relative priorities. Discussion from these sessions always tended to be significantly broader than just the budget and comments ranged from matters that really should be customer service request/complaints to serious points of view on matters such as contracting out of services or procurement processes.

A comprehensive list of comments and discussion was recorded and from that over 60 actions identified, some very short term and others more general than just the budget process. These actions are being addressed as and when appropriate during the budgeting and planning cycles for 2015-16 and 2016-17, **SE 3.1 Budget 2015-16 community feedback**.

A summary report is provided of the online survey conducted in early 2016, **SE 3.5 Online Budget survey 2016-17 report to Council**, and the community engagement sessions undertaken to date in 2016-17, **SE 3.6 2016-17 Community Engagement Sessions feedback**. These documents were discussed with Council at the budget meeting held 22 March 2016.

There were over 200 respondents to the online survey and approximately 80 attendees at the community meetings held to date. More community meetings are scheduled during the period to end of May 2016.

The online survey contained a specific question re would a person be willing to accept an additional 1% rate rise above the cap knowing that it would be used to fund council's ageing infrastructure - 36.3% said "yes", 41.8% said "No" and 21.9% said "maybe".

Council has over many years clearly articulated its approach and priority with regard to addressing the infrastructure gap funding shortfall. This is evidenced not only in the presentations that have been made in recent years but also in the existence of this in a range of long term planning documents since 2008/09 (see Criteria Section 6). It has been a topic of conversation at many consultation meetings and many council meetings over the course of this time, the response to the on-line survey is evidence that the arguments made are reasonably well accepted across the community.

The issue of trade-offs and alternative funding options has been a part of the consultations in so far as Council has communicated its approach to service efficiencies, desire to continue to deliver existing services at existing levels, important regional role that the city plays in the western region of the state, and the policy to borrow funds only for new projects and not renewal or upgrades.

- **OTHER ENGAGEMENT ACTIVITIES**

Throughout the year Council always actively engages with the communities that surround the main town of Horsham by holding regular community consultation sessions as part of its annual meeting agenda. At these sessions the whole of council and the executive team attend often very small communities or districts with the view to discuss any issues either broadly or specific to these local areas. Actions arising from these are then either tracked through HRCC's Customer request system (Merit) or with other matters being managed through an action list that is reported regularly to the Executive Management Group.

In order to further improve community engagement HRCC has introduced a public question time in to its meeting agenda, which commenced in February 2016.

Council also participates yearly in the Local Government Victoria Community Satisfaction Survey **SE 3.7 Community Satisfaction Survey 2015**, and last year asked the question whether the community would prefer a cut in services rather than an increase in rates. The responses to this are shown on Page 32. The responses received for the HRCC survey closely aligned with the other 25 councils who asked this question across the state. 27% said probably or definitely would prefer a rate rise, 56% said probably or definitely prefer a service cut and 17% said they couldn't say. Overall satisfaction with HRCC from these surveys show when compared to other similar sized councils HRCC performs above the average and is on a par with the overall state average – this is even though we have had a specific infrastructure levy component included in our rate rises for the last 8 years.

Furthermore, a key recommendation was also made (Page 10) that Council focus its attention on sealed road maintenance following from the poor community feedback in this area. This provides further evidence of the need to address this declining condition of our road assets.

- **SUMMARY**

Community engagement is a continual process and policy matters such as cutting or discontinuing a service, changing councils risk appetite re borrowings, long term service provision and investments are not matters that should change on a whim.

There needs to be a good level of understanding of council's role within the community, and the engagement process needs to be about education and informing as well as seeking feedback and input. Councils that embark upon participatory processes in the formulation of components of their budgets tend to spend significant effort on education of the participants so that they can truly make informed decisions rather than the off-the-cuff uninformed input that occurs otherwise. The challenge of considering often competing priorities and complex issues of public versus private goods and benefits is something that many have never properly thought through.

The variety and extent of services that HRCC delivers is not well understood within the community, and HRCC is certainly endeavouring to lift its approach to engagement to improve this understanding. HRCC is attempting to tap in to the knowledge, passion and interest generally within the community, but this is a difficult and long road.

The views expressed by some within the community have certainly been acknowledged and will continue to shape the future direction of council in consideration of future budget development and council planning processes.

The following recent policy shifts are evidence that HRCC has responded to community feedback on important matters and therefore substantiates that it is listening to the community. Examples in

recent times include: extension of the farm differential from 10% to 20%, review of farm differential eligibility, undertaking a major change in our approach to the rating of Culture & Recreational assessments, continuation of a limited hours customer service desk at the Natimuk Council office and holding the municipal charge down in order to improve equity within the rating structure.

Supporting evidence

SE 3.1 – Budget 2015-16 community feedback

SE 3.2 – Report to Council on Community Engagement 2016-17 (contains the community engagement plan as an attachment)

SE 3.3 Example of 2015-16 Budget presentation

SE 3.4 Example of 2016-17 Budget presentation

SE 3.5 Online Budget survey 2016-17 report to Council

SE 3.6 2016-17 Community Engagement Sessions feedback

SE 3.7 Community Satisfaction Survey 2015

4. CRITERION FOUR – VALUE AND EFFICIENCY

How the higher cap is an efficient use of council resources and represents value for money.

As stated in the previous criteria, HRCC is seeking the Rate Cap variation for the sole purpose to continue to build its investment in Infrastructure Renewal.

HRCC believes that it already uses resources efficiently and that continued efficiency improvements will occur over time with increased use of technology and gradual adoption of workplace change. Operational costs are essentially being “pegged” to the rate cap which in turn is driving efficiencies and improvements in service delivery. **SE 4.1 HRCC Current Service Reviews list**

Some broad objectives that have been utilised in framing the 2016-17 Budget are that Operational costs should be contained at 2% across each of the 4 directorate groups of council, funding for Operational Initiatives should be retained at prior year’s levels plus at least CPI in order to continue with further efficiencies in service delivery or to address one-off tasks, and any growth funds should be allocated to capital investment to further reduce the Infrastructure gap and deliver on new capital works as appropriate.

The Budget Development Guidelines that are distributed to staff provide details of the key parameters, processes and assumptions that have been put in place for the development of the 2016-17 Budget. **SE 4.2 HRCC Budget Development Guidelines 16-17 Ver 3**

The budget principles contained in this document are as follows:

- Grants are to be based on confirmed funding levels if known or informed estimates.
- All revenue sources should be identified wherever possible and estimated based on known available information.
- Revenue from miscellaneous fees and charges will be reviewed individually with consideration to costs, rate % increase, CPI and other factors. (Except for those which are set by legislation).
- Service and activity levels are being assessed through a Service Review process which may lead to some changes in service delivery levels.
- Any increases to Service levels (including increases in staff FTE’s) should be made via the separate “Budget Submission” process to initiatives, (even if they are being funded from some specific identified savings).
- New initiatives for recurrent programs will be kept to a minimum and should ideally only be approved with an offset by efficiency gains in other areas
- There is always the over-arching aim to use fewer resources with an emphasis on innovation and efficiency.
- Increases in contract charges are based on actual contracted agreements wherever these are known.
- Salaries and Wages to be increased by 2.5% to allow for the 2.0% EBA increase plus an allowance for within band progressions.
- The cost of all salaries & wages including on-costs will be factored in to the budget either through recurrent or capital.
- Operating budgets for ongoing functions and services should not increase by more than 2% in total (3% Local Govt Cost Index less a 1% efficiency reduction).
- Borrowing costs are factored in at 4.1% interest rate with principal to be repaid over a 10 year period.
- All budget movements greater than 10% or greater than \$5,000 per line item will require an explanation for the variance.

The application of increased funding to community infrastructure (particularly roads) represents good value for money in terms of provision of services to ratepayers as roads are seen as the highest priority service that councils provide (**SE 3.5 Online Budget survey 2016-17 report to Council**). If money is not spent on roads, these assets will continue to decline in condition, leading to poorer road conditions and increased maintenance costs. Roads in bad condition are much more vulnerable to pot holes and edges falling apart with resultant impacts on private vehicle maintenance costs.

If we allow roads to deteriorate it will require a massive injection of funds at a later stage to catch up, this may be an even greater burden on ratepayers. It is more efficient to renew roads before we start incurring significant additional maintenance costs.

HRCC has in place robust processes for the documentation, evaluation & prioritisation of its Capital Works Programs and its Operational Initiatives as part of its annual budget processes. The pro-forma used for these evaluations are shown in **SE 4.3 Capital Works requests pro-forma** and **SE 4.4 Operational Initiatives request pro-forma**.

In terms of Councils financial sustainability, the financial indicators on Page 53 of the 2015-16 Budget document, **SE 6.2 Budget 2015-16**, provides evidence of how council is tracking and projected to track for the term of the strategic resource plan. A strong cash position (backing of asset replacement reserves), working capital is forecast to decline yet still remain in an overall strong position, debt compared to rates and debt repayment to rates are increasing but are mid-range of accepted limits.

Supporting evidence

SE 4.1 Current Service Reviews List

SE 4.2 HRCC Budget Development Guidelines 16-17 Ver 3

SE 4.3 Capital Works requests pro-forma

SE 4.4 Operational Initiatives request pro-forma

5. CRITERION FIVE – TRADE-OFFS AND ALTERNATIVE FUNDING OPTIONS

What consideration has been given to reprioritising proposed expenditures and pursuing alternative funding options and why those funding options are not adequate?

HRCC takes seriously the need to maintain the assets that it has responsibility for and believes this is a core expectation from the community. HRCC also acknowledges its role within the west of the state as a regional city and the extra challenge this sets in order to provide and maintain a greater range of services than would otherwise be necessary for a city of our size.

What's already been achieved

HRCC has continued to add to capital investment above the rate percentage increases by obtaining increased grant funding, funding operational efficiency initiatives, keeping operational costs down, and maintaining debt at manageable levels. (See Figure 2.3 Page 7)

The 1% rate rise above the cap in 2016-17 will contribute \$0.210m, and overall capital spend from general revenues has increased by \$0.538m or 10.8%. Expenditure on Renewal has increased by \$0.757m or 8% from 2015-16. This demonstrates that the dual approach of containing operational costs and a 1% targeted rate rise is helping close the gap but more will be needed in to the future to meet the 3% required for roads according to Maloney's report, and future requirements for other asset groups such as buildings and recreation.

Alternative options considered

HRCC has over time looked at alternative actions to meet the shortfall in capital funds for renewal of ageing assets.

Discussions have included:

1. Asset divestment (this is an ongoing discussion and part of our overall Asset Management Strategy and Council Plan 4 year priority 3.1.3 see **SE 6.1 Council Plan and Strategic Resource Plan**). Over 80% of our asset value however is in roads and many of these cannot be closed easily. Roads that may possibly be closed with less impact are consequently the low volume roads which are also low maintenance cost.
2. Additional grant funding and obtaining funds from other sources - other tiers of government seldom make funds available for renewal projects (except for the Federal Roads to Recovery funding which specifically targets renewal). HRCC avails itself of as many opportunities for grant funding as possible and employs a full time Grants Officer to assist in obtaining and managing grants.
3. Further cuts to operational costs, beyond what has already been achieved by:
 - o Scaling back on service delivery, considered through the service planning process, but the community's needs are very broad and so too are their expectations. There are a range of service overview documents and individual service review documents that are available if required.
 - o Discontinuing services handed to Local Government by the state. Cost shifting by state government continues to add pressure to the bottom line, libraries, SES, school crossings, Maternal and Child Health and Home care are all areas where the State

Government has handed over services and then progressively withdrawn funding. Community expectations are high with respect to these services.

- Seeking fair and reasonable cost increases for the services provided to Council by state government e.g. Victorian Electoral Commission costs of running elections, VAGO annual audit costs, EPA Landfill levies, Fire Services Levy. These costs have been increasing at a much higher rate than the 2.5% imposed cap on Local Government rates.
 - Achieving economies of scale by undertaking shared services – HRCC has been sharing service for many years with the Wimmera Regional Library Corporation and the Wimmera Development Association. There is a balance to be achieved here in managing the sensitivities of local impacts, the impact of geographic realities and the costs to setup such arrangements. Other more recent examples include the collaborative procurement project for bituminous products, regional LED streetlight replacement project, sharing of Environmental Health Officers and Regional GIS services. (Documentation is available for these projects if required)
4. Increasing levels of compliance are also being imposed which adds to Local Governments cost base, there needs to be an active review of "red tape" requirements by the State Government to assist councils in containing costs.
 5. Loan borrowings have been increasing for new assets serving both HRCC and the broader Wimmera region. These have been in line with council's borrowing policy (**SE 5.1 Loan Borrowings Policy**) and HRCC's strategic resource plan. HRCC applies the principle that borrowings are utilised for new assets on the basis that new assets are providing a service to future generations who are then paying for the borrowing costs. On the other hand renewals are funded from existing revenues or reserves put away in the past, as these are maintaining existing assets for which the benefit, has been, and is currently being, received. The following indicators from the 2015-16 Budget demonstrate the extent of Council's current and projected borrowings.

Indicator	Measure	Notes	Forecast	Budget	Strategic Resource Plan			Trend	Expected band Range of Result
			Actual		Projections				
			2014/15	2015/16	2016/17	2017/18	2018/19	+/-	
Obligations									
Interest Paid to Rates	Interest bearing loans and borrowings / rate revenue	3	16.9%	30.9%	37.2%	38.1%	43.4%	-	20 - 60%
Debt Repayments to Rates	Interest and principal repayments / rate revenue	4	3.6%	3.1%	3.4%	3.6%	3.7%	-	0 - 5%
Indebtedness (Longterm Obligations)	Non-current liabilities / own source revenue	3	24.0%	37.4%	42.5%	43.1%	44.8%	-	10 - 40%

Note: Expected Band Range of Results are as stated in the Local Government Performance Reporting Framework (LGPRF) documentation. VAGO assesses indebtedness of 40% to 60% as medium risk and greater than 60% as high risk.

Figure 5.1

Supporting evidence

SE 5.1 Loan Borrowings Policy

6. CRITERION SIX – LONG-TERM PLANNING

That the assumptions and proposals in the application are consistent with those in council's long-term strategy and financial management policies set out in the council's planning documents and annual budget.

It has been clearly shown in the other 5 criteria above that council has had an ongoing policy since 2008/09 and this has been embedded in our key planning documents. Whilst the level of the rate increase tied to infrastructure renewal is recommended to be as high as 3% by Maloney and 2% in HRCC's Asset Management Policy, 1% has been considered to be acceptable within the community in recent years, and will still allow HRCC to close the infrastructure gap over time, or at least not allow it to grow further. Additional contributions to renewal expenditure have been achieved through directing growth income to Capital Renewal and through achieving operational efficiencies.

Council Plan & Strategic Resource Plan (Supporting Evidence 6.1)

Council's key strategic planning document the Council Plan references the need to address the issue of ageing infrastructure in a number of places.

- Page 11 - Guiding Principles that underlie and inform council's operations "Evaluate refurbishment of appropriate assets before construction of new facilities"
- Page 14 - For the Municipality to be a good place to live and to preserve our natural environment we need to "Maintain Assets that meet the community's needs"
- Page 23 - Goal 3 – Asset Management – one of the 4 goals of the Council Plan – supports the overall focus on maintaining council's assets for the long term sustainability, amenity and safety of the community and includes targets for expenditure on renewal
- Page 32 – Strategic Resource Plan Table 1 – shows planned rate increases of 4.5% for next 3 years
- Page 33 Strategic Resource Plan – the plan states the following regarding the key objectives that underpin the financial plan. "Provide for rate increases that establish a sustainable funding level, including increasing capital funding for asset renewal. A modest increase in rates is planned at 4.5% from 2016/17 to 2018/19, comprising annually of 2.5% for operations and 2.0% for further infrastructure renewal. This reflects expected general cost increases but does not allow for continued growth in service demand across the municipality. Any growth will need to be met through improving efficiencies in existing operations and services."
- Page 38 – Strategic Resource Plan – the statement of capital works shows increasing baseline asset renewal from 2017 \$7.372m to 2019 \$10.78m. (Renewal expenditure is higher in the budgeted year 2015-16 \$10.562m due to one large project for the renewal of the Horsham Town Hall which is a project of around \$20m in total with around 50% funded from state and federal grants).

Budget 2015-16 (Supporting Evidence 6.2)

- Page 6 – Chief Executives Summary supports HRCC's intentions to continue with the Infrastructure levy approach and to apply for this rate variation:

"2. Rates and Municipal Charge –This year's rate increase is in line with the level foreshadowed in Council's Strategic Resource Plan adopted in the previous year. (The rate increase for the 2014/15 year was 5%). Future year's rate increases have been based on a CPI of 2.5% plus continuing a 2% allocation for infrastructure renewal. Given the State Government intends to bring in a policy for Rate Capping as of 2016/17 it is understood that

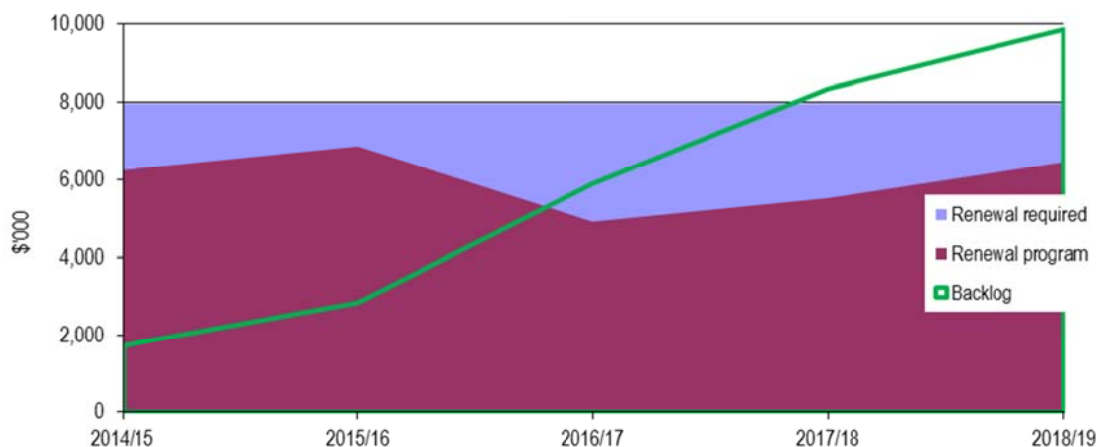
Council will likely need to apply to the Essential Services Commission to argue its case for a rate rise above CPI, and to continue with this important investment in asset renewal.”

- Page 41 – Infrastructure Gap Reserve – “Council's Asset Management Plan, through the MAV's STEP program has identified a significant infrastructure renewal funding gap. One of the strategies to address this gap has been to levy an additional percentage rate rise in its budget which is then specifically targeted to fund asset renewal on identified priority Council assets. This process began in 2007/2008 when a 0.5% rate rise was set. A further 1.5% was set the following year and then an additional 2% annual rate rise to 2011/2012, 1% in 2012/13, 2013/14, 2014/15 and 2015/16. These funds are placed in this reserve and the total funds raised are to be expended within the financial year on asset renewal to improve the overall condition of Council's asset stocks.
- Page 51 – Strategic Resource Plan – 8.1 Plan Development – two of the key financial objectives that underpin the SRP is stated to be “Provide a rate increase that establishes a sustainable funding level” and “Increasing capital funding for asset renewal and ensure critical renewal items are funded annually”.
- Page 53 & 54 – Financial performance indicators – the following indicator is shown for asset renewal based on a 2% Infrastructure Renewal Rate Increase. However Council is only applying for a 1% variation to the rate cap for 2016-17 and this will impact on these figures.

Indicator	Measure	Notes	Forecast		Strategic Resource Plan			Trend +/-
			Actual 2014/15	Budget 2015/16	Projections			
					2016/17	2017/18	2018/19	
Asset renewal	Asset renewal expenditure / depreciation	5	101.9%	101.6%	70.1%	79.1%	100.2%	+

- Page 55 – 9.2 Current year rate – “.....1% of the 5% rate increase has been earmarked to further contribute to the Infrastructure Renewal component. Council would prefer to tag 2% towards the Infrastructure Gap but this has not been again possible to achieve in 2015/16. A 2% rate increase was applied towards the Infrastructure Gap in the financial years 2009/10 to 2011/12 and a 1.5% increase in 2008/09. 2012/13 to 2014/15 it has only been 1%. The combined effect of these rate increases now generates approximately \$1.70m for the Asset Renewal Reserve. This amount is spent annually on assets above condition 8. The amount is still insufficient to cover the growing infrastructure funding gap. \$4.89 million from Rates Revenue contributes toward capital investment for the 2015/16 year.
- Page 59 – 10.2 Infrastructure – “The Council based on the knowledge provided by various Asset Management Plans, predicts infrastructure consumption, renewal needs and considers infrastructure needs to meet future community service expectations. The renewal strategy has been developed through consultation and evaluation. The key aspects of the process are as follows:
 - Long term capital planning process which integrates with the Council Plan, Strategic Resource Plan and Annual Budget processes
 - Identification of capital projects through the preparation of asset management plans
 - Prioritisation of capital projects within classes on the basis of evaluation criteria
 - Business Case template for officers to document capital project submissions.
A key objective is to maintain or renew Council’s existing assets at desired condition levels. If sufficient funds are not allocated to asset renewal then Council’s investment in those assets will reduce, along with the capacity to deliver services to the community.

The graph below sets out the Renewal required, the current and planned Renewal program and the accumulative Renewal backlog (or accumulated Asset Renewal Gap) arising from the programmed renewal being less than the required renewal.



At present, Council is similar to most municipalities in that it is presently unable to fully fund asset renewal requirements identified. While Council is endeavouring to provide a sufficient level of annual funding to meet ongoing asset renewal needs, the above graph indicates that in later years the required asset renewal is not being addressed creating an asset renewal gap and increasing the level of backlog. Backlog is the renewal works that Council has not been able to fund over the past years and is equivalent to the accumulated asset renewal gap. In the above graph the backlog at the beginning of the five year period was \$1.72 million and \$9.85 million at the end of the period.

Backlog accumulated prior to 15/16 has not been factored into the Strategic Resource Plan. It is expected that during the period from 15/16 to 18/19 the backlog will continue to increase much higher than was originally estimated in the 2014/15 Strategic Resource Plan. The reason for this is the impact of the State Government Policy on Rate Capping due to be introduced in 2016/17 which will restrict Council's ability to address this renewal gap through targeted rate increases.

Following table shows projected borrowings for future years.

Summary of funding sources					
Year	Total Capital Program \$'000	Grants \$'000	Contribution \$'000	Council Cash \$'000	Borrowings \$'000
2014/15	19,768	5,790	265	12,882	830
2015/16	19,284	4,576	1,170	9,543	3,995
2016/17	15,078	5,779	200	6,729	2,370
2017/18	14,805	5,671	680	7,293	1,161
2018/19	14,416	3,359	680	7,955	2,422

Asset Management Policy (Supporting Evidence 6.3)

- Page 4 – 5. Principles – “Council will endeavour to progressively reduce the Infrastructure Renewal Gap. This will be achieved by a combination of:
 - Seeking additional external funding.

- Seeking improved efficiencies in the delivery of asset maintenance and renewal practices to obtain improved value in this investment.
- Including an annual rate increase of up to 2% per year, cumulative, added over and above any other adopted rate increase, specifically targeted to reduce the gap.
- The level of the additional annual commitment will be assessed in the context of the affordability of rates on a year-to-year basis, recognising Council’s desire to minimise the rate burden for ratepayers.”

Asset Management Improvement Strategy (Supporting Evidence 6.4)

- Page 15 – Future Vision – “..... Annual rate increase of up to 2% per year.....”

Asset Management Plan – Part A General Information (Supporting Evidence 6.5)

Section 6.7 on Page 43 details HRCC’s Renewal Replacement plan and processes and section 6.7.5.2 on Page 45 specifically addresses the Asset Renewal funding gap and links with the ongoing policy and strategy for up to a 2% targeted rate rise.

Rates Strategy (Supporting Evidence 6.6)

- HRCC’s Rating Strategy does not specifically refer to the quantum of any rate increase or the purpose of any rate increase; this is a matter for consideration within the budget. However the Rating Strategy does clearly articulate the policy positions of council in relation to achieving an equitable and efficient distribution of the rates burden with the municipality and hence is relevant background to this rate variation application.

Council Annual Report (Supporting Evidence 6.7)

- Annual Report is also provided as general background as includes a good general overview of HRCC and provides relevant Local Government Performance Reporting (LGPRF) indicators and financial accounts.

Supporting evidence

SE 6.1 Council Plan and Strategic Resource Plan

SE 6.2 2015-16 Budget

SE 6.3 Asset Management Policy

SE 6.4 Asset Management Improvement Strategy

SE 6.5 Asset Management Plan Part A General Information

SE 6.6 Rates Strategy

SE 6.7 Council Annual report