Higher Rate Cap Application 2018/19 - Further Information Part 3

Monash City Council

14 May 2018

Question

1.1 Does Monash have a target(s) for its adjusted underlying result indicator in its long term financial plan?

Monash's Response

Council's Long-Term Financial Plan (LTFP), regularly referenced during Budget Planning sessions with staff and Councillors, forecasts underlying results for the life of the Plan with comparative data to a risk matrix (>0% = Low, -10-0% = Medium, > -10% = High). The LTFP is not a published document (refer Table1).

					STRATEGIC RESOURCE PLAN									
				2017/18 FORECAST	2018/19 BUDGET (Yr 1)	2019/20 (Yr 2)	2020/21 (Yr 3)	2021/22 (Yr 4)	2022/23 (Yr 5)	2023/24 (Yr 6)	2024/25 (Yr 7)	2025/26 (Yr 8)	2026/27 (Yr 9)	2027/28 (Yr 10)
	Red	Yellow	Green											
OVERALL FINANCIAL SUSTAINABILITY RISK RATING	HIGH	MEDIUM	LOW	✔	✔	✔	✔	✔	✔	✔	✔	✔	✔	✔
Underlying Result Ratio	<-10%	-10% - 0%	>0%	6.67%	8.32%	5.31%	5.00%	5.42%	5.43%	5.52%	5.41%	5.69%	5.63%	5.90%
Liquidity	<100%	100% - 150%	>150%	224.74%	190.85%	166.22%	175.79%	163.23%	161.69%	158.87%	157.06%	157.18%	159.95%	163.30%
Indebtedness	>60%	40-60%	<40%	2.46%	2.41%	2.36%	2.31%	2.26%	2.21%	2.17%	2.12%	2.08%	2.04%	2.01%
Self-financing	<10%	10%-20%	>20%	26.48%	31.29%	21.50%	20.38%	25.85%	24.38%	24.48%	23.93%	23.86%	23.37%	23.44%
VAGO Renewal/Upgrade Ratio	<100%	100%	>100%	145%	164%	119%	113%	135%	143%	144%	145%	144%	140%	142%
LG Renewal Gap (Renewal only)	<100%	100%	>100%	113%	128%	92%	96%	118%	126%	131%	130%	130%	128%	129%

The 2018/19 Budget projects a surplus of $16.9M for 2018/19 (Forecast 2017/18 $13.3M) and an adjusted underlying result surplus of $14.3M. As Monash is debt-free the $14.3M underlying surplus forms part of the net cash from operating activities that, including capital grants ($3.9M), will be solely applied to fund capital works payments in 2018/19.

The Strategic Resource Plan lists the underlying ratio ranging from 7.6% - 6.3% slightly reducing over time, however remaining above 0%. That range is low compared to the Adjusted Underlying result for Metro Council for 2016/17 at 12.62% and around ball-park for "All Council's".

Link: http://www.monash.vic.gov.au/About-Us/Council/Have-Your-Say/Draft-Council-Budget-2018-19

Question

1.2 If yes, What is the target and does it differ from the target ranges suggested by LGV and VAGO?

Monash's Response

The target is to remain in the "Low" risk category >0%. This is in-line with the VAGO recommendation that, to be financially sustainable, councils should aim to generate enough revenue from their own operations to meet their financial obligations, and to fund asset replacement and asset acquisitions.

Monash's approach is not inconsistent with LGV who also look for a sustainable positive operating result as a requirement to enable a Council to continue to provide core services and meet its objectives. Further, that improvement in financial performance is expected over time and councils should be wary of continued losses meaning reliance on cash reserves or increased debt to maintain services.

Question

1.3 What is the rationale for this target?

Monash's Response

As the Underlying Result is a measure of operating financial performance calculated after adjusting for non–recurrent capital grants and contributions we believe it is an important measure of financial sustainability as it excludes income which is to be used for capital from being allocated to cover operating expenses. Further Monash believes that financial plans that have a positive underlying surplus (over time) is as an indicator that we are generating enough funds from operations to fund asset management plans.

Question

1.4 Is this target and rationale published in any public financial documents?

Monash's Response

The projected results/targets are published each year in the Draft and Adopted Budget documents and the audited results are also published in the Annual Report.

Link: www.monash.vic.gov.au/About-Us/Council/Publications/Annual-Report

Question

2.1 We note that council has a target for its working capital ratio for 150%. What is rationale for this target?

Monash Council has, for several years, based its short-term and long-term financial planning with a strategic target of maintaining a liquidity ratio above 1.5:1. The Strategic Resource Plan (SRP), as part of the Long-Term Financial Plan, had, for many years (up until 2013/14 struggled to maintain or exceed a liquidity ratio above 1. It wasn't until Council made the strategic decision to sell its residential aged care facilities and business that we have consistently shown a liquidity ratio above 1.5.

For many years Council's financial direction was aimed at achieving or maintaining a sustainability assessment generally in-line with targets set by the Victorian Auditor General's Office (VAGO). This was the benchmark mechanism reported during Budget planning sessions and discussions with our Audit & Risk Committee when discussing annual financial reports.

One of the major focuses of the 2018/19 budget is Council's continued commitment to long-term financial sustainability, including being debt free in the short-term and maintaining Council's Working Capital Ratio (Current Assets/Current Liabilities) at above 150 per cent over the life of the SRP.

Question

2.2 Is this target and rationale published in any public financial documents?

Monash's Response

The projected results/targets are published each year in the Draft and Adopted Budget documents including a reference to maintaining a working capital ratio above 150%. The audited results are also published in the Annual Report with reference to maintaining a working capital ratio above 150% (refer links listed above).

Question

2.3 Please provide an explanation for the difference between this target, and the target range suggested by LGV and VAGO.

Monash's Response

The financial sustainability indicators (and the risk ratings) were generally accepted by Council as being the ones they should target (refer Table 2). Over recent years we understand VAGO have reduced the liquidity risk factors, however we have maintained the target of equalling or exceeding the 1.5:1 liquidity ratio (Refer Table 3).

Monash's liquidity ratio target 150% is below the all council average across the collected LGPRF data (State average for 2016/17 293.07%[1]) and VAGO's State-wide result of 2.4 (refer Table 4)

Table 2 – VAGO Indicators 2012

Figure E2
Risk assessment criteria for financial sustainability indicators

Risk	Underlying result	Liquidity	Indebtedness	Self-financing	Capital replacement	Renewal gap
High	**Negative 10% or less** Insufficient revenue is being generated to fund operations and asset renewal.	**Equal to or less than 1.0** Insufficient current assets to cover liabilities.	**More than 60%** Potentially long-term concern over ability to repay debt levels from own-source revenue.	**Less than 10%** Insufficient cash from operations to fund new assets and asset renewal.	**Equal to or less than 1.0** Spending on capital works has not kept pace with consumption of assets.	**Equal to or less than 0.5** Spending on existing assets has not kept pace with consumption of these assets.
Medium	**Negative 10% to zero** A risk of long-term run-down to cash reserves and inability to fund asset renewals.	**1.0–1.5** Need for caution with cash flow, as issues could arise with meeting obligations as they fall due.	**40–60%** Some concern over the ability to repay debt from own-source revenue.	**10–20%** May not be generating sufficient cash from operations to fund new assets.	**1.0–1.5** May indicate spending on asset renewal is insufficient.	**0.5–1.0** May indicate insufficient spending on renewal of existing assets.
Low	**More than zero** Generating surpluses consistently.	**More than 1.5** No immediate issues with repaying short-term liabilities as they fall due.	**40% or less** No concern over the ability to repay debt from own-source revenue.	**20% or more** Generating enough cash from operations to fund assets.	**More than 1.5** Low risk of insufficient spending on asset renewal.	**More than 1.0** Low risk of insufficient spending on asset base.

Source: Victorian Auditor-General's Office.

[1] https://knowyourcouncil.vic.gov.au/home

Table 3 – VAGO Indicators 2014/15

Financial sustainability risk indicators – risk assessment criteria

Risk	Net result	Liquidity	Indebtedness	Internal financing	Capital replacement	Renewal gap
High	**Negative 10% or less** Insufficient revenue is being generated to fund operations and asset renewal.	**Less than 0.75** Immediate sustainability issues with insufficient current assets to cover liabilities.	**More than 60%** Potentially long-term concern over ability to repay debt levels from own-source revenue.	**Less than 75%** Limited cash generated from operations to fund new assets and asset renewal.	**Less than 1.0** Spending on capital works has not kept pace with consumption of assets.	**Less than 0.5** Spending on existing assets has not kept pace with consumption of these assets.
Medium	**Negative 10%–0%** A risk of long-term run down to cash reserves and inability to fund asset renewals.	**0.75–1.0** Need for caution with cash flow, as issues could arise with meeting obligations as they fall due.	**40–60%** Some concern over the ability to repay debt from own-source revenue.	**75–100%** May not be generating sufficient cash from operations to fund new assets.	**1.0–1.5** May indicate spending on asset renewal is insufficient.	**0.5–1.0** May indicate insufficient spending on renewal of existing assets.
Low	**More than 0%** Generating surpluses consistently.	**More than 1.0** No immediate issues with repaying short-term liabilities as they fall due.	**40% or less** No concern over the ability to repay debt from own-source revenue.	**More than 100%** Generating enough cash from operations to fund new assets.	**More than 1.5** Low risk of insufficient spending on asset renewal.	**More than 1.0** Low risk of insufficient spending on asset base.

Source: Victorian Auditor-General's Office.

Table 4 - 2015/16 Sustainability Results – Local Government

Financial sustainability risk indicators for the local government sector at 30 June 2016

Indicator		Average across councils for year ended 30 June 2016					
		All councils	Metro	Interface	Regional	Large	Small
Net result	per cent	11.4	13.7	29.0	9.4	4.9	–0.1
Liquidity	ratio	2.4	2.2	2.9	2.1	2.2	2.7
Internal financing	per cent	138.0	211.7	171.6	111.7	101.8	93.2
Indebtedness	per cent	26.1	16.3	27.6	36.2	30.3	20.2
Capital replacement	ratio	1.5	1.6	1.6	1.5	1.3	1.2
Renewal gap	ratio	1.0	1.1	0.9	0.9	1.0	1.0

Note: Yellow result = medium risk assessment; green result = low risk assessment.
Source: VAGO.