

# Report on 2019-20 Council Budgets

Local Government Victoria



## Author

Local Government Victoria

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We acknowledge and respect Victorian Traditional Owners as the original custodians of Victoria's land and waters, their unique ability to care for Country and deep spiritual connection to it. We honour Elders past and present whose knowledge and wisdom has ensured the continuation of culture and traditional practices.

We are committed to genuinely partner, and meaningfully engage, with Victoria's Traditional Owners and Aboriginal communities to support the protection of Country, the maintenance of spiritual and cultural practices and their broader aspirations in the 21st century and beyond.



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ISBN 978-1-76077-893-4 (pdf/online/MS word)

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# Report on 2019-20 Council Budgets

Section 127 of the *Local Government Act 1989* (the Act) requires that councils prepare a budget for each financial year that contains financial statements, a description of the services and initiatives to be funded, and information about rates and charges.<sup>1</sup>

The budget is council's key resource planning document for the next financial year (short term), and commonly includes an extract of the four year Strategic Resource Plan (medium term).

## Executive summary

Each year Victorian councils must develop a proposed budget for consideration by their community.<sup>2</sup> After complying with the relevant legislative requirements, including giving public notice and considering any submissions on the proposed budget, a council may adopt its budget.<sup>3</sup>

This report by Local Government Victoria (LGV) identifies some of the key financial trends across the local government sector.

Victorian councils have reported that in the 2019-20 financial year:

- Collectively, the sector is budgeting to generate an operating surplus of \$1.7 billion;
- Revenue from rates and charges totals \$6.25 billion;
- The average increase in general rates and municipal charges (revenue) publicised by councils for the 2019-20 year is 2.64% (2.24% in 2018-19);
- 75 of the 79 councils have adopted budgets within the Fair Go Rates System cap set for 2019-20 of 2.50% with two councils (Warrnambool and Mansfield) successful in applying to the Essential Services Commission for a variation to the cap for the current year and two councils (Towong and West Wimmera) having variations approved in previous years which cover 2019-20;
- Government grants represent 15.6% (\$1.67 billion) of total budgeted revenue of \$10.71 billion;
- The sector is budgeting to hold cash and investments of \$4.36 billion by 30 June 2020;
- Borrowings of \$1.23 billion as at 30 June 2020 represents no net increase in debt from 2018-19;
- Borrowing costs of \$55.0 million represent less than 1% of total expenses;
- Sector-wide capital works expenditure of \$3.47 billion is budgeted for 2019-20;
- Eighty per cent of planned capital expenditure is to be funded by council's own source revenue;
- Councils employ 37,866 full time equivalent staff members at 30 June 2020 across a broad range of occupations;
- Employment costs remain relatively stable at \$3.78 billion (42% of total expenditure); and
- Councils are custodians of assets valued at \$108.7 billion and incur depreciation expenses of \$1.59 billion which is 17.7% of total expenditure.

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1. Sections 127(2)(a), (b) and (e) of the *Local Government Act 1989*. Section 130 of the *Local Government Act 1989* requires all councils to submit a copy of the budget, or revised budget, to the Minister for Local Government within 28 days of adopting the budget.

2. Section 127(1) and 129(1) of the *Local Government Act 1989*

3. Section 130(1) of the *Local Government Act 1989*

# Analysis

The analysis contained in this report is based on data extracted from the 2019-20 adopted council budgets unless otherwise stated. At times, the analysis has been supplemented with data from the 2019-20 Strategic Resource Plans (SRP), which contain medium term (four year) budget intentions of councils.

The analysis presented separates the 79 councils into groupings based on size and geographic location. These cohort groups are as follows: Metropolitan Councils, Interface Councils, Regional Cities, Large Shires and Small Shires. These groupings are consistent with the Know Your Council website groupings. A list of council cohorts and their membership is attached at **Appendix A**.

## Revenue

Councils in aggregate are budgeting for total revenue of \$10.71 billion in 2019-20. The composition of this total budgeted revenue is shown in **Figure 1.1**. The largest revenue items are rates and charges (\$6.25 billion or 58.4%) and grants of \$1.67 billion which represents 15.6% of annual budgeted revenue. User fees and contributions are also key sources of revenue for councils, accounting for 9.4% and 10.2% of forecast total revenue, respectively.

The composition of total revenue varies significantly between cohorts, as shown in **Figure 1.2**. Small rural councils have a greater dependency on government grants (38% of total revenue) whilst rates and charges represent 51% of total revenue. This reflects the fewer revenue raising options for small rural councils and their significant dependence upon external grant funding.

Interface councils are recipients of significant developer contributions of 25% of total revenue (both monetary and gifted assets) and also receive 12% of total revenue by way of government grants. General rates and charges contribute 50% of the total revenue in this cohort.

Within council cohorts there can also be significant variability in the amount of total revenue forecast by each individual council. The small rural council with the highest forecast revenue is Buloke Shire Council (\$37.67 million including some flood recovery grants), more than two times the size of the Borough of Queenscliffe (\$17.2 million), the small rural council with the lowest forecast revenue. The variability of forecast revenue between interface councils is also significant. Wyndham City Council's forecast revenue (\$554 million) is more than five times the lowest forecast revenue within the cohort, belonging to Nillumbik Shire Council (\$103.8 million). It is important to highlight this variability within cohort groupings to better appreciate the context for this analysis.

**Figure 1.2** below also shows that 66% of metropolitan council revenue is raised through rates and charges. The proportion of revenue raised by rates and charges for all other cohorts is lower however it is important to acknowledge that for all five cohorts at least half of total revenue is generated through their own-source revenue stream of rates and charges.

Aggregate Council Budgeted Revenue  
2019-20

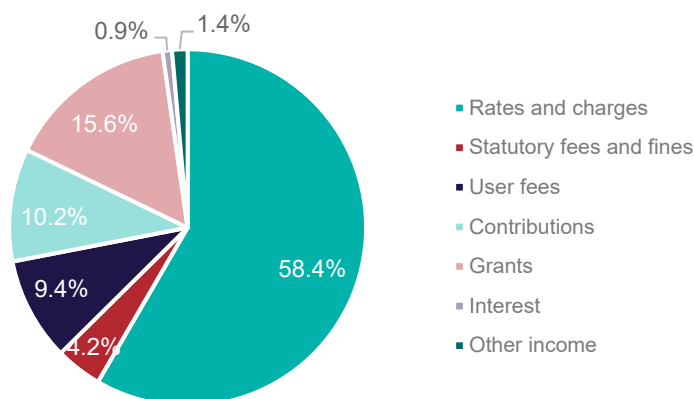


Figure 1.1 - Aggregated council budgeted revenue

## COMPOSITION OF REVENUE BY COHORT 2019-20

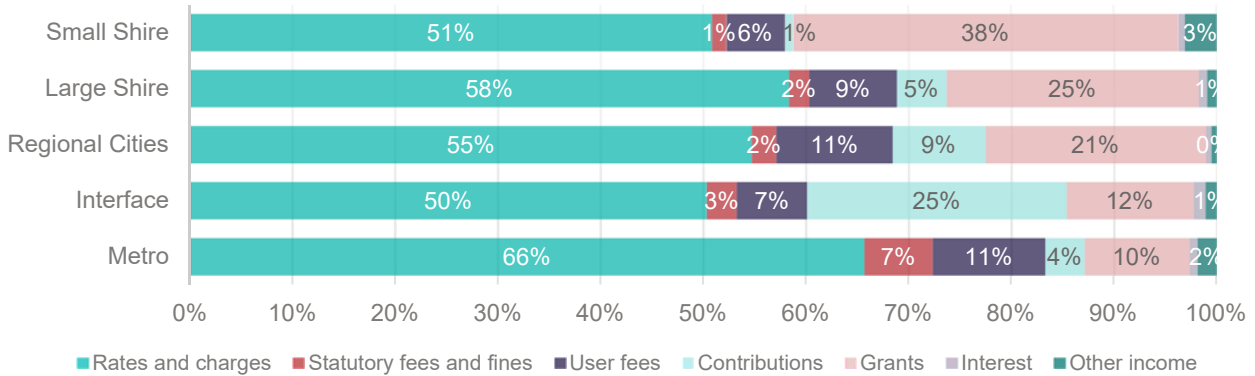


Figure 1.2 – Composition of Revenue by Cohort

### Rates and Charges

Rates and charges are the primary source of revenue for councils, representing approximately \$6.25 billion or 58.4% of total budgeted revenue in 2019-20. **Figure 1.3** shows that \$5.3 billion (86%) of total rates and charges revenue is raised through general rates, while the rest is raised through waste, municipal and other charges.

### Composition of rates and charges revenue across the whole sector 2019-20

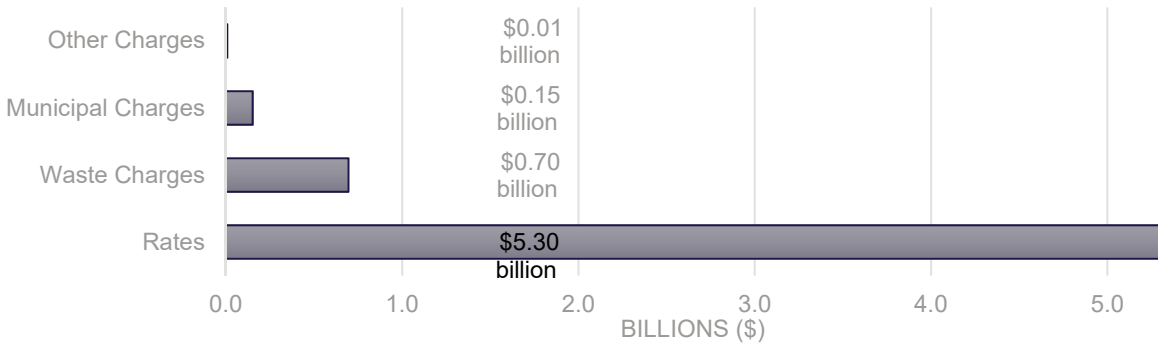


Figure 1.3 – Composition of rates and charges revenue

### Growth in rateable assessments

The local government sector continues to experience year on year growth in the number of assessments (i.e. rated properties). The collective growth has averaged around 1.8% per annum over the past ten years.

**Figure 1.4** shows the percentage change in the number of assessments between 2014-15 and 2019-20 by cohort. Small rural councils experienced a small decline in assessments in 2014-15 however all cohorts have otherwise experienced growth in the number of assessments over this period. While the rate of growth varies by cohort and over time the growth in the number of assessments in interface councils is notable, exceeding 3% every year since 2016-17.

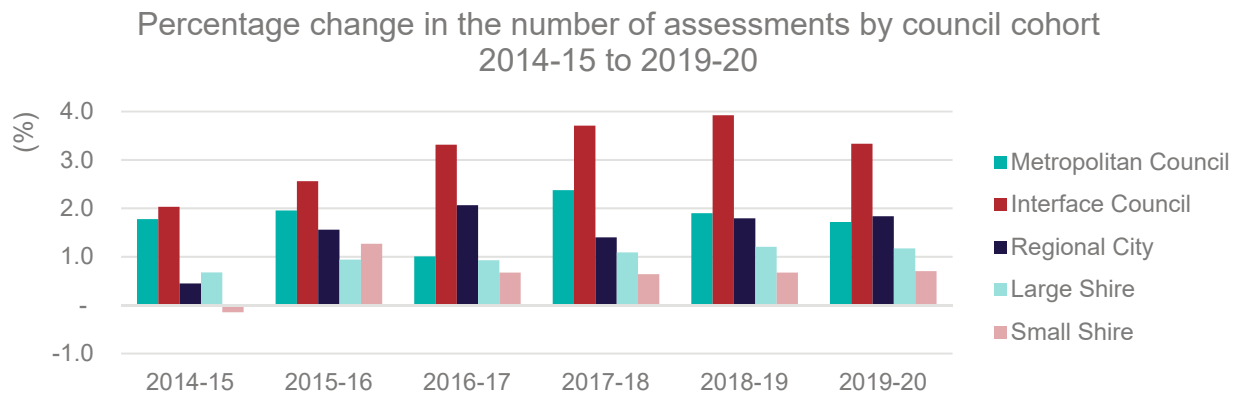


Figure 1.4 – Percentage change in no. of assessments

The growth in new rateable properties (assessments) is reflected in the percentage increase in total rates and charges revenue, as distinct from the increase in the average rate, or the rate in the dollar.

In 2019-20, councils have budgeted for an additional 59,519 rateable properties which represents an increase of 1.9% taking the total number of assessments to 3,054,074 (2,994,555 in 2018-19 adopted budgets). The number of assessments by council cohort is shown in **Figure 1.5**. Metropolitan councils account for almost half of the total number of assessments, budgeting for 1,454,428 assessments in 2019-20.

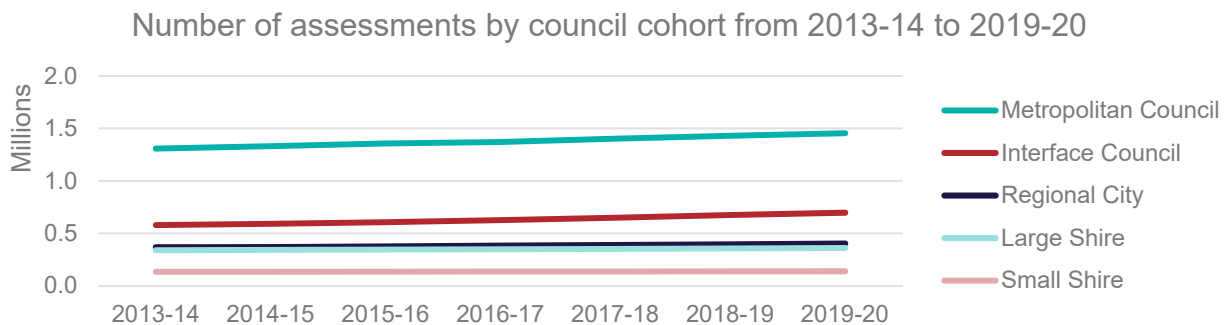


Figure 1.5 – No. of assessments by council cohort

The average growth in local government assessments is broadly consistent with Victoria’s population growth between 2009 and 2018, which averaged an increase of 2.1% per annum.

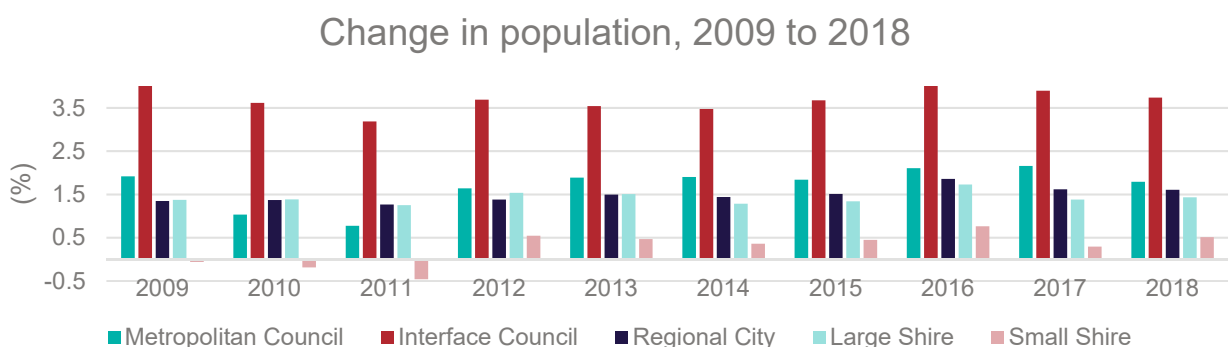


Figure 1.6 – Change in population (Source: ABS)

**Figure 1.6** shows the percentage change in population by council cohort over the 10 years to 2018. Interface councils have consistently seen the largest rate of growth in their population, around 3.5% per annum. Small shires are the only council cohort to experience population growth of less than 0.5% over these ten years and recorded a decline in population between 2009 and 2011. This demonstrates how the rate of population growth in the past decade has been most concentrated in the interface councils, and the challenge of declining and aging populations for small rural shires.

### ***Total rates and charges increase***

The increase in the total rates and charges revenue for the 79 councils is 4.65% (5.6% in 2018-19), for a budgeted total amount of \$6.25 billion. This combined pool of revenue includes general rates, municipal charges, waste charges, supplementary rates and revenue in lieu of rates.

For the past four years the difference between the capped increase and the increase in the total rate revenue pool has varied between 2.0% and 3.35% which is predominately driven by the increase in the number of rateable assessments. This year the gap between the capped increase and the increase in the total rate revenue pool is 2.15%. This variance is also the result of the increase in waste charges which have been higher than the rate cap increases and the equivalent Consumer Price Index (CPI) increases. The main driver of increased waste charges in recent years has been the change in China's policy in 2018 to stop the import of low quality mixed recyclable materials.

### ***Fair Go Rates System and publicised rate rises***

In 2019-20, 65 councils declared a rate rise of 2.5% in line with the rate cap. The average general rate increase by councils for the 2019-20 year is 2.64% (2.24% in 2018-19). The average increase is marginally above the rate cap of 2.5%. This is due to the four rate cap variations in place for the 2019-20 financial year, partially offset by other councils who chose to declare rate increases lower than the rate cap.

For the 2019-20 financial year, Mansfield Shire Council and Warrnambool City Council had requests for rate cap variations approved by the Essential Services Commission (ESC) while two other councils previously had rate cap variations approved for multiple years. The single year and multiple year applications approved by the ESC for 2019-20 are as follows:

- Mansfield Shire Council (**2019-20: 13.94%**);
- Warrnambool City Council (**2019-20: 4.5%; 2020-21: 4.5%**);
- Towong Shire Council (**2019-20: 5.55%, 2020-21: 5.55%**); and
- West Wimmera Shire Council (**2019-20: 3.5%, 2020-21: 3.5%**).

Nine rural councils and one metropolitan council declared rate increases at a level below the FGRS rate cap of 2.5% in 2019-20 as follows:

- Colac Otway Shire Council (0.50%);
- Glenelg Shire Council (2.10%);
- Hindmarsh Shire Council (1.90%);
- Hobsons Bay City Council (2.47%);
- Horsham Rural City Council (2.25%);
- Nillumbik Shire Council (2.25%);
- Southern Grampians Shire Council (2.48%);
- Strathbogie Shire Council (2.25%);
- Swan Hill Rural City Council (1.02%); and
- Yarriambiack Shire Council (2.23%).



### Average assessment

An indicator of the change in rates and charges over time is the calculation of an average assessment by cohort as shown in **Figure 1.7**. The average assessment represents the total (by cohort) of general rates and municipal charges divided by the total number of assessments. When considered over time this calculation of the average amount raised per assessment can be used to measure the change in rates and charges.

**Figure 1.7** shows the average assessment has risen steadily in all council cohorts between 2013-14 and 2019-20. It also shows that following the introduction of the Fair Go Rates System (FGRS) in 2016-17 the original trajectory of the year on year increase of the average assessment has flattened for all council cohorts, showing the effect of the rate cap.

Average assessment by council cohort 2015-16 to 2019-20

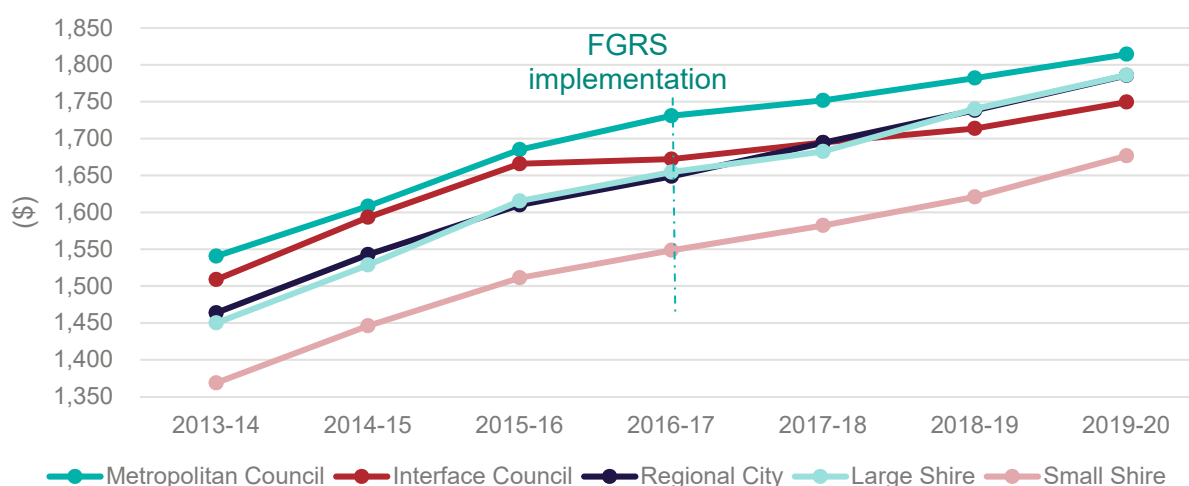


Figure 1.7 – Average assessment by council cohort

The 2019-20 year in **Figure 1.7** shows that the metropolitan council average assessment was the largest at \$1,814, \$138 higher than the small shire average assessment of \$1,677. The average assessment by cohort for 2019-20 is shown in **Figure 1.7a** below.

Council cohort	Budgeted 2019-20 average assessment
Metropolitan	\$1,814
Interface	\$1,750
Regional City	\$1,786
Large Shire	\$1,786
Small Shire	\$1,677

Figure 1.7a – 2019-20 budgeted average assessment by cohort

The average rateable assessment is impacted by the availability of alternative revenue streams to rates. For example, the average assessments in metropolitan and interface cohorts are positively impacted by revenue from user fees and charges while rural councils are impacted by higher government grants.

The average assessments of small shires and large shires can be impacted by a larger proportion of their rates revenue, (36% and 19% respectively) raised through farm rates. The amounts paid in rates for farms are typically higher than most residential rate assessments due to the much larger land holdings and values compared to residential assessments. This is despite the use of differential rates to affect a discount for farm assessments in some municipalities.

Under the *Local Government Act 1989* Victorian councils can determine whether their general rates will be raised by a uniform rate, differential rates or limited differential rates.<sup>4</sup> This simply means councils either apply a single rate in the dollar for all types or classes of land (uniform rate) or they choose to apply different rates in the dollar for different types or classes of land. Common types or classes of land to which differential rates are applied include residential, commercial, industrial or farm land. The Act includes some limitations on the use of differential rates, for example the Capital Improved Value (CIV) system of valuation must be used (except in the case of limited differential rates) and the highest differential rate can be no more than four times the lowest differential rate.<sup>5</sup> **Figure 1.7b** shows how general rates are applied across Victorian councils based on adopted 2019-20 budgets and highlights the widespread use of differential rates.

Application of general rates	Number of councils (from 2019-20 budgets)
Uniform rate	14
Differential rates	64
Limited differential rates	1
<b>TOTAL</b>	<b>79</b>

*Figure 1.7b – Application of general rates by Victorian councils*

### **Average residential assessment**

Residential assessments often represent the largest proportion (by number and amount of revenue) of the rate base of Victorian councils. The average residential assessment provides a useful perspective on the change in residential rates over time. The average residential assessments for each cohort for the last four financial years are presented in **Figure 1.8** below.

4. Section 158 (1)(b)(i),(ii),(iii) of the *Local Government Act 1989*

5. Section 161(1),161(5) and 161A of the *Local Government Act 1989*

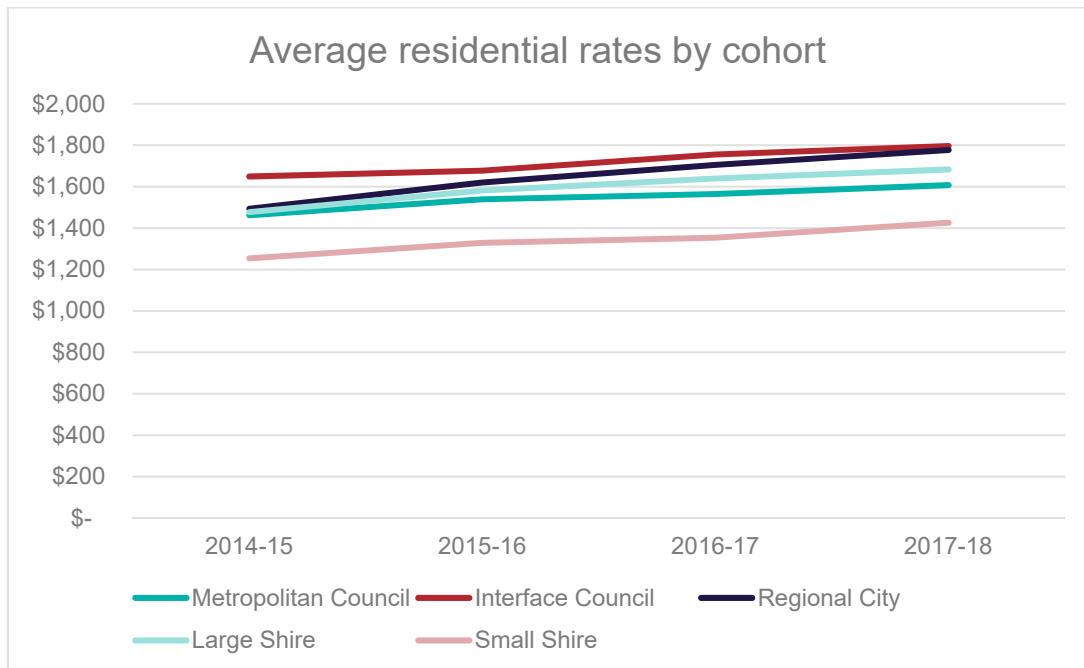


Figure 1.8 – Average residential rates by cohort (Source: Annual Victoria grants commission (VGC) returns)

Figure 1.8a shows the actual average residential assessment amounts by council cohort for 2017-18. The average residential rates for small rural councils are significantly less than their overall average assessment.

Council cohort	2017-18 average residential assessment
Metropolitan	\$1,607
Interface	\$1,796
Regional City	\$1,777
Large Shire	\$1,683
Small Shire	\$1,426

Figure 1.8a – 2017-18 average residential assessment by cohort (Source: Annual VGC returns)

This is also illustrated in the figure 1.9 below which compares residential and overall average assessments for this cohort. The graph indicates the impact of farm rates in small rural councils which increases their overall average.

### Small rural councils - Average Assessments

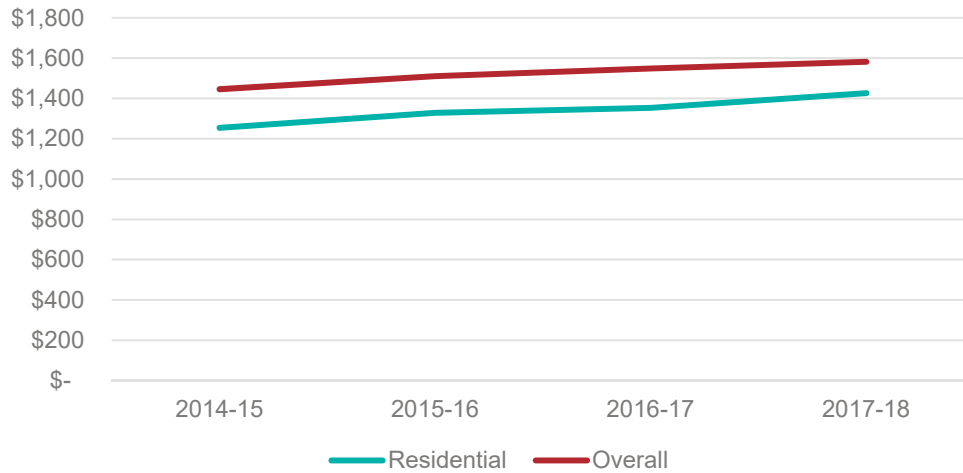


Figure 1.9 – Average assessment by council cohort

Figure 1.10 below demonstrates that in the forward projections of councils for the first 4 years since the implementation of FGRS, there is a trend of lower growth in forecast income from rates and charges as compared to 2015-16 (prior to cap) projections. The dotted line represents the projected increase in rates and charges based on 2015-16 budget projections.

### Strategic Resources Plan Rates and Charges Projections (includes waste charges)

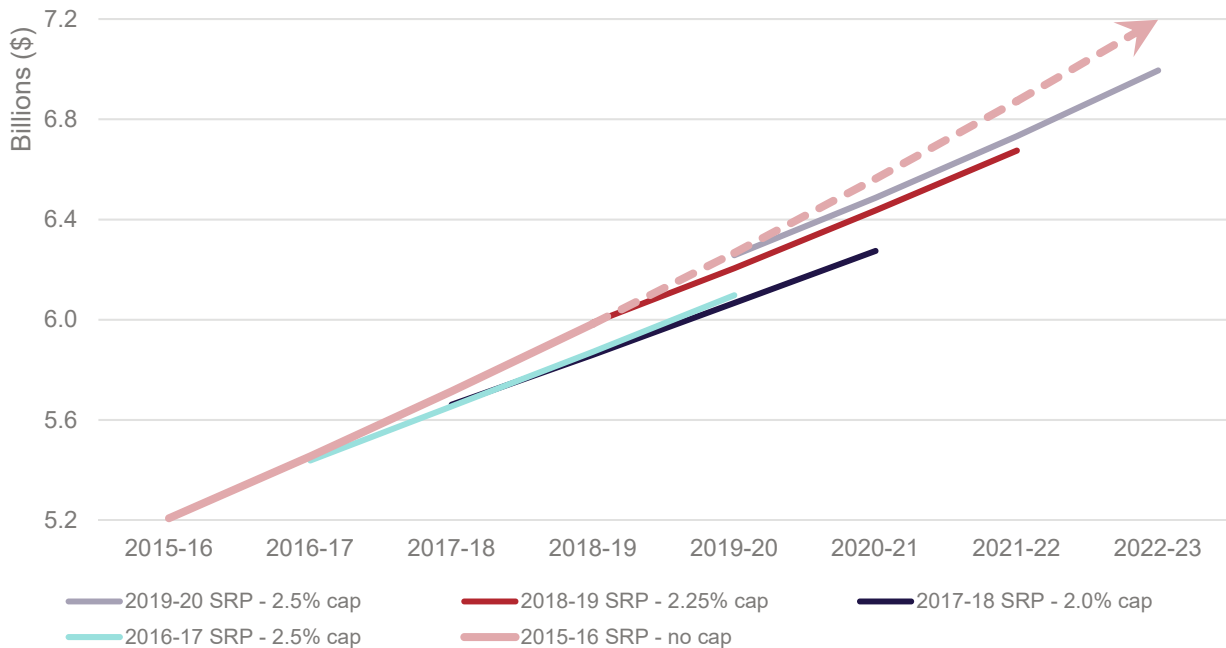


Figure 1.10 – SRP rates and charges projections

In the 2015-16 Strategic Resource Plans (SRPs), the forecast year-on-year growth of rates and charges averaged 4.7%. A relatively flatter rate of increase after the implementation of the rate cap from 2016-17 onwards, reflects the constraint on growth due to rate capping. The SRPs also give a broad indication of

future expectations of councils in respect of FGRS. The graph also demonstrates the impact of the increase in waste charges (discussed below) resulting in an overall increase in income from rates and charges in the years 2018-19 and 2019-20. This is a result of an increase in waste service charges due to China's policy to stop the import of low quality mixed recyclable materials.

Over the period, there is no discernible evidence of widespread reduction in council service levels although several councils have flagged this as possible in the future. The Victorian Auditor-General's Office have noted this potential risk and highlighted the importance of longer term service planning in consultation with local communities.<sup>6</sup>

### **Mix of rates and charges revenue**

Under the *Local Government Act 1989*, councils have discretion to determine what rates and charges will be levied and how this burden will be distributed.

In 2019-20 Mildura Rural City Council has resolved to abolish its municipal charge whilst Maribyrnong City Council has changed its valuation system from Net Annual Value (NAV) to Capital Improved Value (CIV). To accommodate this change Maribyrnong City Council has also introduced both a municipal charge and a waste management charge. Overall 74 of the 79 councils use CIV as their valuation system. The remaining 5 councils that use NAV as their valuation system are Glen Eira City Council, Melbourne City Council, Port Phillip City Council, Whittlesea City Council and Yarra City Council.

Two councils have also sought to rectify historical arrangements which created a distortion in the amounts recovered between the cost of waste services and general rates. Mansfield Shire Council, following their successful application to the ESC for a rate cap variation, transitioned revenue previously collected through its waste service charges into its general rates. Similarly, Wodonga City Council transitioned revenue previously collected through its waste service charges into its general rates.

### **Municipal charges**

Pursuant to section 159 of the Act, councils may declare a Municipal Charge to cover some of the administrative costs of the council. In 2019-20 the budgeted total to be collected is \$152.64 million, an increase of \$1.4 million or 0.93% on 2018-19 levels. In 2019-20 Municipal Charges are being levied by 40 councils, six of which are metropolitan councils.

### **Waste charges**

Section 162 of the Act allows councils to raise service rates and charges. Service charges are most commonly raised in relation to waste services. Service charges are not currently subject to the capping provisions of the Fair Go Rates system. Across the sector there is a great diversity in waste service charges. The revenue collected by way of waste charges can also be determined by the service level chosen by the ratepayer. Any comparisons should therefore be mindful of the increased service offerings of some councils in response to the needs of their community.

Separate waste charges are levied by 74 of the 79 Councils. This effectively means that the waste services provided by the remaining five councils are funded 'by way of general rates'. Banyule City Council, Melbourne City Council, Whitehorse City Council, Yarra City Council and Port Phillip City Council do not currently levy a separate waste charge. Port Phillip City Council includes a nominal amount as service charges revenue in its Adopted budget 2019-20, mainly in relation to discretionary waste services provided by council. In the past two years Maribyrnong City Council and Monash City Council have introduced partial waste charges to cover some of their additional costs.

The increase in budgeted waste charges revenue over the last three years has been substantially higher than both budgeted general rates revenue and consumer price index increases, with a 5.7% increase in 2017-18, 11.0% in 2018-19 and 5.8% in 2019-20.

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6. Results of 2016-17 Audits: Local Government, Victorian Auditor-General's Office, November 2017

## Government Grants

Councils forecast receiving \$1.67 billion in grant funding during 2019-20.

\$1.1 billion (or 66.8%) of grant funding is expected to be recurrent operating funding, and a third (or \$344 million) of this funding is expected to go to metropolitan councils. Another \$409 million or 24.5% of grant funding is expected to be non-recurrent capital. The **figure 1.11** below provides a breakdown of grants.

As identified in earlier analysis in **Figure 1.2**, small and large rural councils have a greater dependency on government grants. When combined with relatively lower population levels this means that 'grants per capita' in small and large rural councils are greater compared to metropolitan and interface councils. As shown in **figure 1.12** below the rates and charges per capita is also higher in these councils than their metropolitan counterparts.

## Grants, 2019-20 - \$'000s

■ Capital - Non-recurrent 
 ■ Capital - Recurrent 
 ■ Operating - Non Recurrent 
 ■ Operating - Recurrent



Figure 1.11 – Grants by type

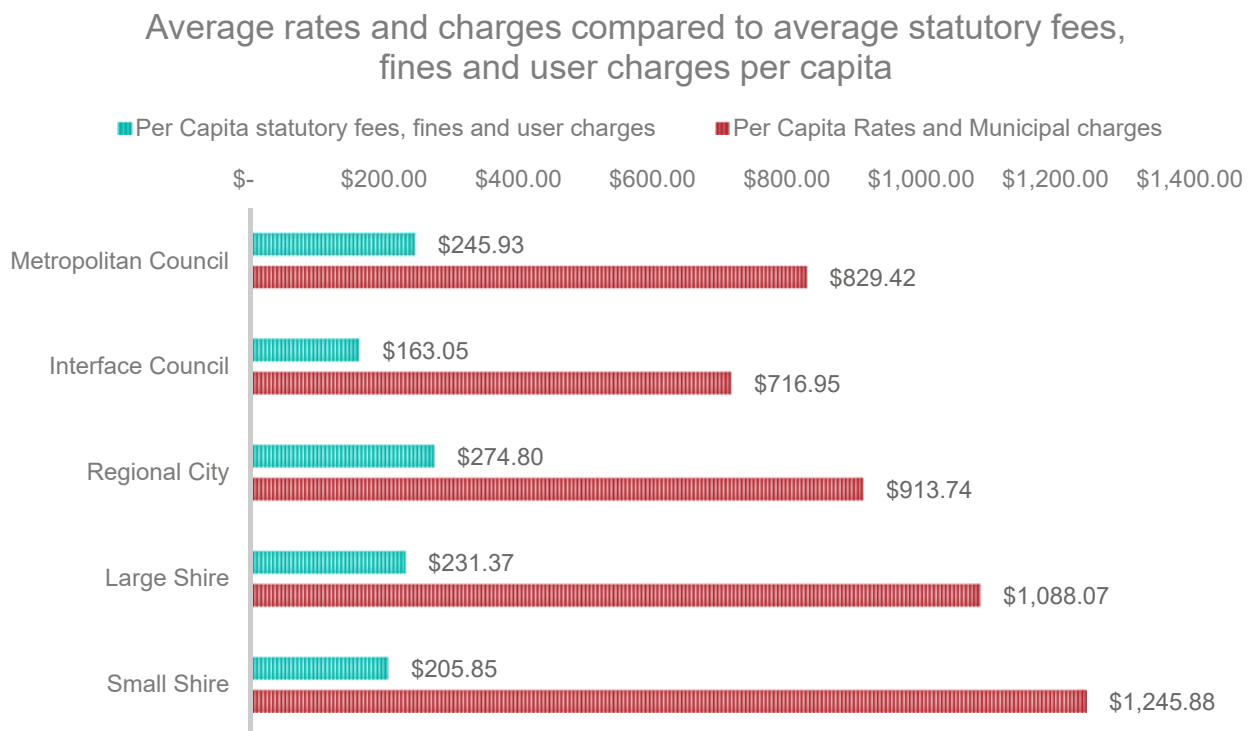
### Fees, fines and user charges

The local government sector has budgeted revenue from fees, fines and user charges of \$1.454 billion, representing 13.56% of total revenue. The contribution of fees, fines and user charges to the total revenue of councils varies significantly in total dollar terms by cohort.

Fees, fines and user charges as a percentage of total revenue are as follows:

Metropolitan	\$0.784 billion (17.6% of total revenue)
Interface	\$0.276 billion (9.8% of total revenue)
Regional	\$0.219 billion (13.7% of total revenue)
Large rural	\$0.136 billion (10.5% of total revenue)
Small rural	\$0.038 billion (7.0% of total revenue)

**Figure 1.12** shows the per capita distribution of rates and charges revenue against statutory fees, fines and user charges. It highlights the relatively higher dependence of small shires on revenue from rates and charges on a per capita basis.



*Figure 1.12 – Per capita rates & charges / statutory fees & fines and user charges*



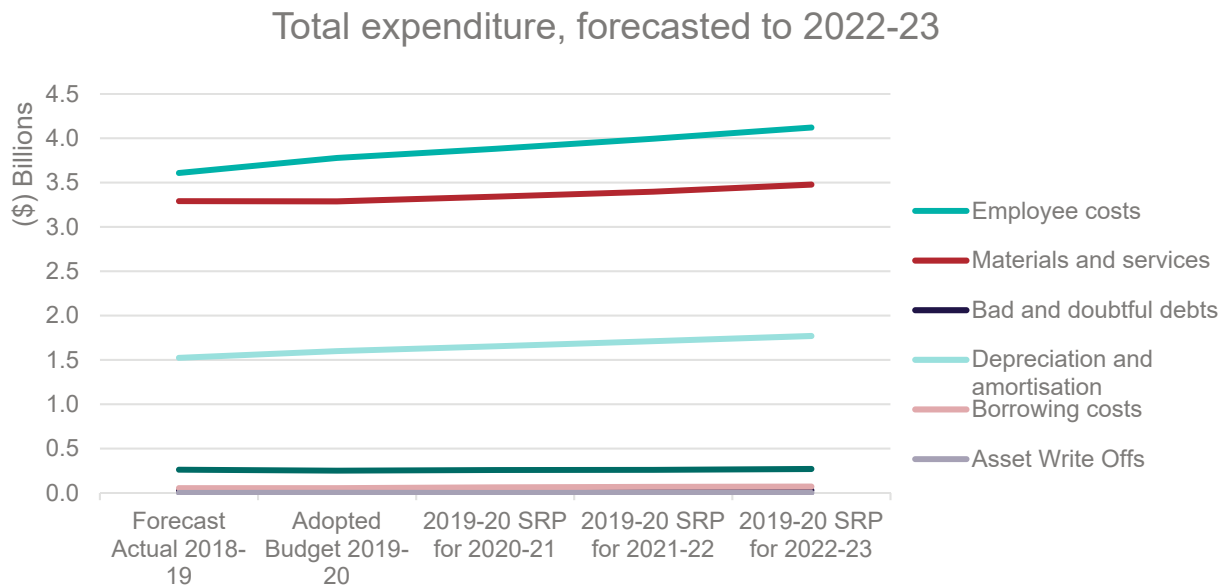
## Expenditure

Councils are budgeting for total expenditure of \$9 billion in 2019-20 resulting in an operating surplus across the sector of \$1.7 billion.

Employee costs (\$3.78 billion or 42%) are the largest cost to councils followed closely by materials and services (\$3.28 billion or 36.5%).

Another significant expenditure item is depreciation. Depreciation is the allocation of the cost of an asset over its useful life and reflects the pattern of consumption of the asset (i.e. wear and tear) over time. Depreciation is a significant expense of local government due to the asset intensive nature of the sector, particularly in relation to the management of fixed assets such as roads, bridges, drains and buildings.

**Figure 2.1** below shows the main expenditure budgeted by councils, noting that employee costs, materials and services and depreciation expense are projected to incur modest increases over the four-year life of the Strategic Resource Plan. Other elements have been forecast to decline or remain constant.



**Figure 2.1 – Total expenditure forecasted to 2022-23**

Expenditure is forecast to increase at a steady rate over the next four years, with depreciation and amortisation growing at an average of 3.82% per year, and employee costs growing at an average of 3.38% per year.

Council expenditure by type and cohort, 2019-20 (depreciation highlight) \$'000s

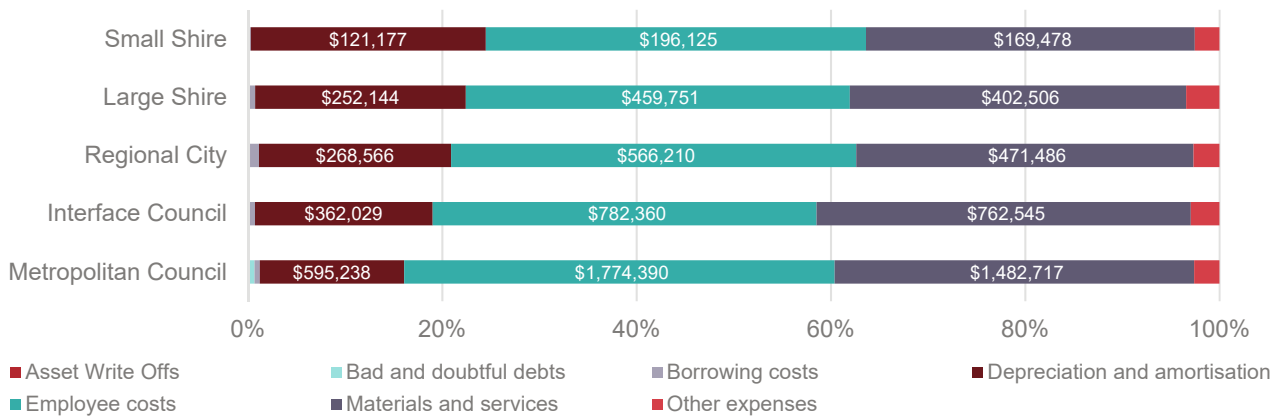


Figure 2.2 – Expenditure by type and cohort

The composition of council expenditure by cohort is illustrated in the **figure 2.2** above, specifically identifying depreciation as a challenge for rural and regional councils. While the rural council spend on depreciation and amortisation is a significantly lower figure than that in metropolitan councils, it accounts for a significantly larger *proportion* of their total expenditure. This can be primarily attributed to small shires having much larger road networks relative to their overall asset maintenance responsibilities. To illustrate this disparity, the Shire of Buloke has a road network totalling 5,313 kilometres. This contrasts with the City of Stonnington, which has a road network of just 309 kilometres but enjoys significantly greater revenue.

To cover the cost of depreciation expense, the impact in rural and regional councils is far greater than on metropolitan councils. The **figure 2.2a** below shows 2019-20 depreciation expense as a percentage of rates and charges and total expenditure:

	Depreciation expense as a percentage of rates and charges	Depreciation expense as a percentage of total expenditure
All local governments:	24.90%	17.3%
Metropolitan	20.33%	14.86%
Interface	25.40%	18.32%
Regional	30.70%	21.22%
Large rural	33.33%	21.64%
Small rural	44.00%	24.23%

Figure 2.2a – Depreciation expense as percentage of rates & charges revenue and total expenditure

## Capital Works

The local government sector has forecast combined capital expenditure of \$3.47 billion in 2019-20. This is an 8% increase over the previous year. Councils have projected that 80% of the four-year capital works program will be funded through rates and other own-sourced revenue.

Over the next three years, 44% of the overall capital works of \$9.8 billion are expected to be delivered by metropolitan councils, while only 18.5% are expected to be delivered by large and small rural councils. These figures include road construction and maintenance, which constitute a significant responsibility for rural and regional councils. Metropolitan, interface and regional cities together account for 81% of capital works while their combined population comprises of 87.9% of the Victorian total. In contrast, the 38 large and small rural councils are projected to deliver 19% of capital works expenditure for 12.1% of the population due to geographically larger areas with relatively larger road networks and higher costs.

**Figure 2.3** shows 2019-20 capital expenditure by cohort and highlights the magnitude of spending planned by metropolitan councils (\$1.4 billion).

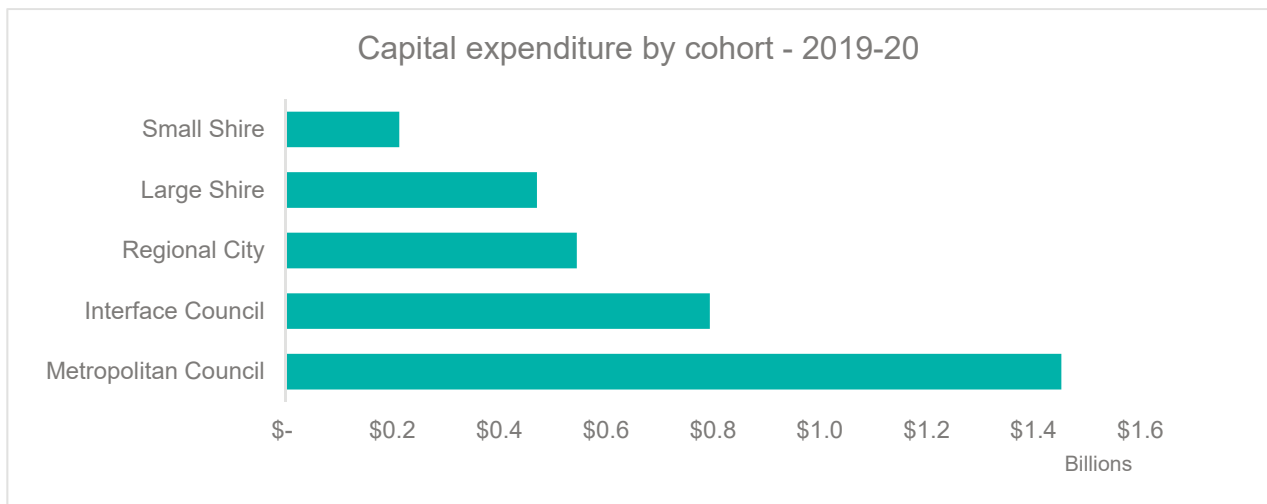


Figure 2.3 – Capital expenditure by year

**Figure 2.4a** shows the sector’s total planned capital spend over the next four years. **Figure 2.4b** shows a further breakdown of expenditure by type and highlights asset renewal expenditure as the major expenditure type in each of the four years.

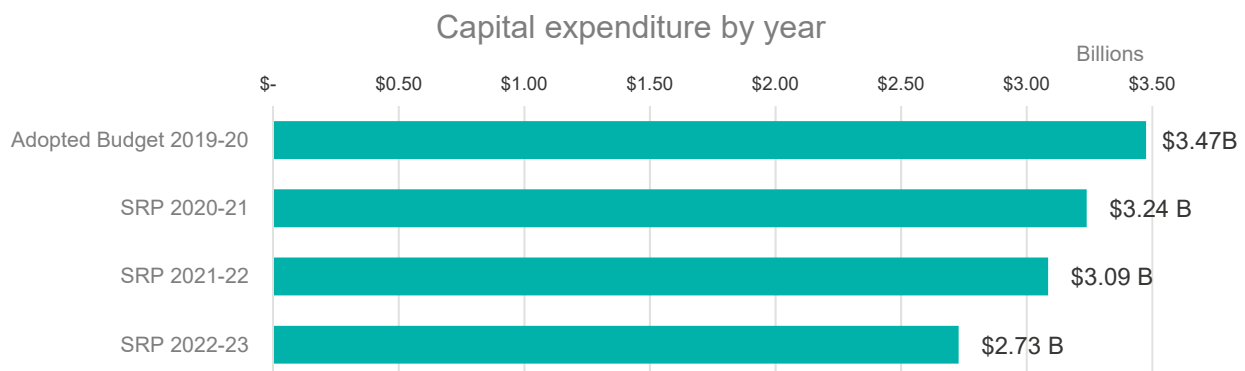


Figure 2.4 a – Capital expenditure by year

### Capital expenditure by type

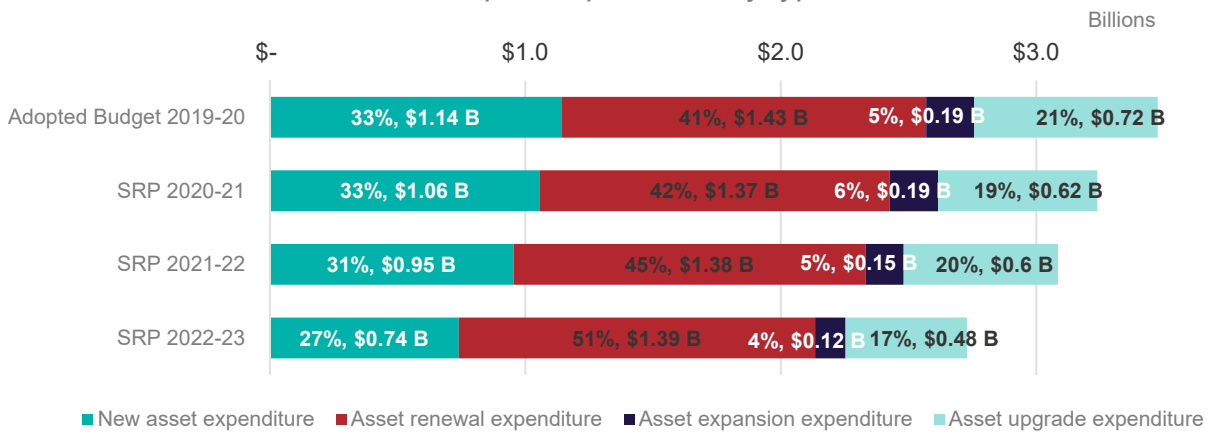


Figure 2.4 b – Capital expenditure by type

Figure 2.5 below shows the forecast changes to council capital expenditure over the next four years by council cohort. Both small and large shires are forecasting decreases in capital expenditure over the next four years, however this can be matched to decreased forecasts in capital grant funding, which is not in line with historical outcomes. Interface councils receive large developer contributions including gifted assets. These gifted assets are not reflected in the capital expenditure forecasts shown below. However the asset lifecycle in assets of interface councils is also reflected in the lower percentage of funds allocated to asset renewal works.

### Capital expenditure, 2018-19 to 22-23

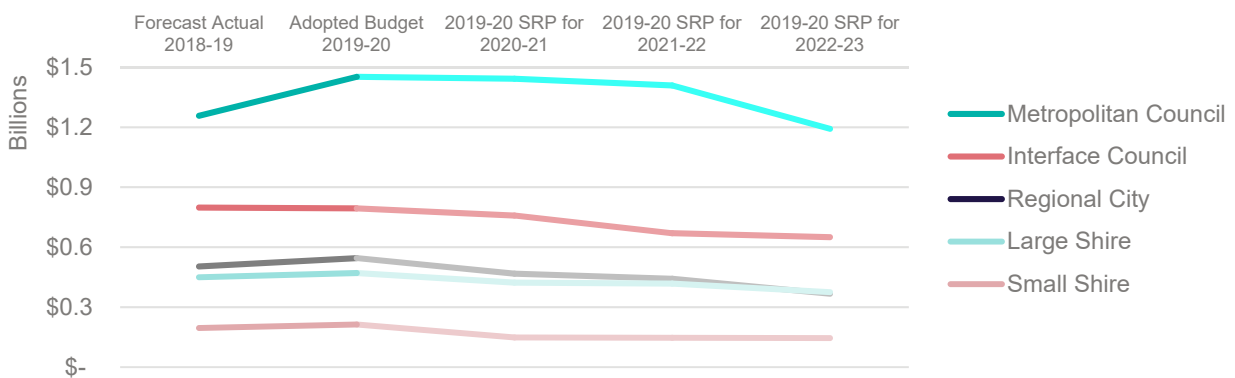


Figure 2.5 – Capital expenditure by cohort

Figure 2.6 shows the composition of capital works expenditure in 2019-20. It shows that interface councils and regional cities spend a much larger proportion of their budget on new assets compared to the other council cohorts, and significantly less on asset renewal. As the interface council populations stabilise and their asset base matures, it is likely they will decrease their expenditure on new assets and increase expenditure on renewal. Interestingly regional cities are budgeting to spend more on new assets, on a percentage basis, than interface councils.

## Composition of capital works expenditure, 2019-20

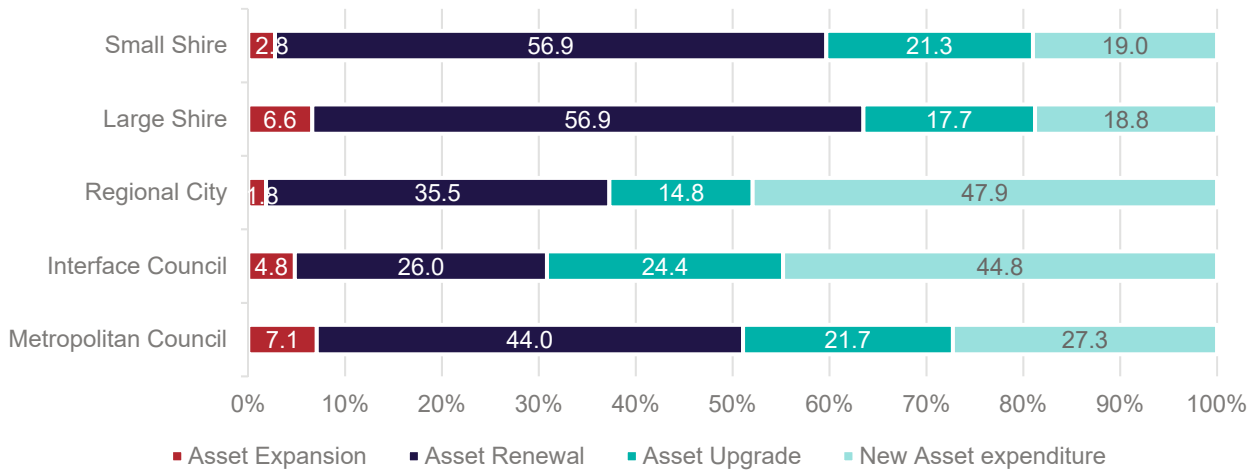


Figure 2.6 – Composition of capital works

## Asset renewal compared to depreciation

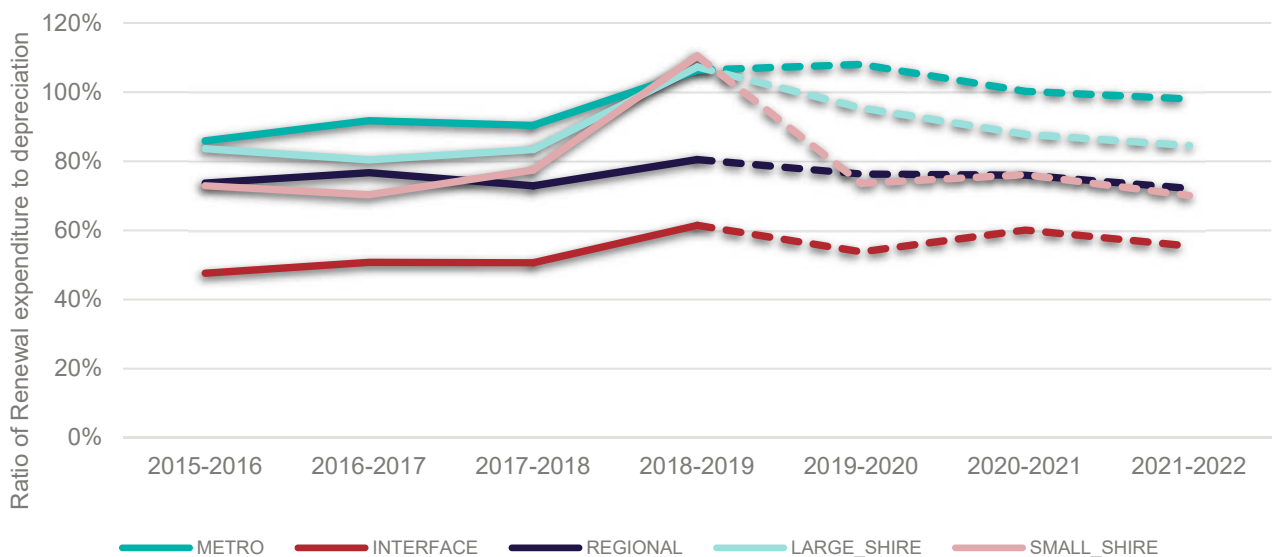


Figure 2.7 – Asset renewal compared to depreciation

Figure 2.7 above shows the actual and forecast asset renewal ratio (sometimes referred to as the ‘renewal gap’) which is the potential gap between planned expenditure on asset renewal compared to the forecast cost of depreciation. The ratio is an indicator of whether council spending on asset renewal is keeping pace with the rate of consumption of those assets and a ratio of 100% or greater is desirable. The chart shows that interface councils have lower levels of asset renewal spending due to their asset expenditure typically focusing on new rather than established assets due to recent growth. According to this indicator metropolitan, small and large rural council cohorts reach a level of 1:1 renewal spend against depreciation in 2018/19. Only metropolitan councils continue to project this rate of renewal in their forward estimates.

It is important to note that the renewal ‘gap’ is hypothetical but does highlight the possibility that some councils may not be planning to invest sufficiently to maintain assets at their current levels. This can be due to planned service level reductions, financial constraints or both.

**Figure 2.8** below shows that a significantly larger proportion of capital works in rural and regional council areas are reliant on grant funding, while most metropolitan and interface council capital works are funded by own source revenue.

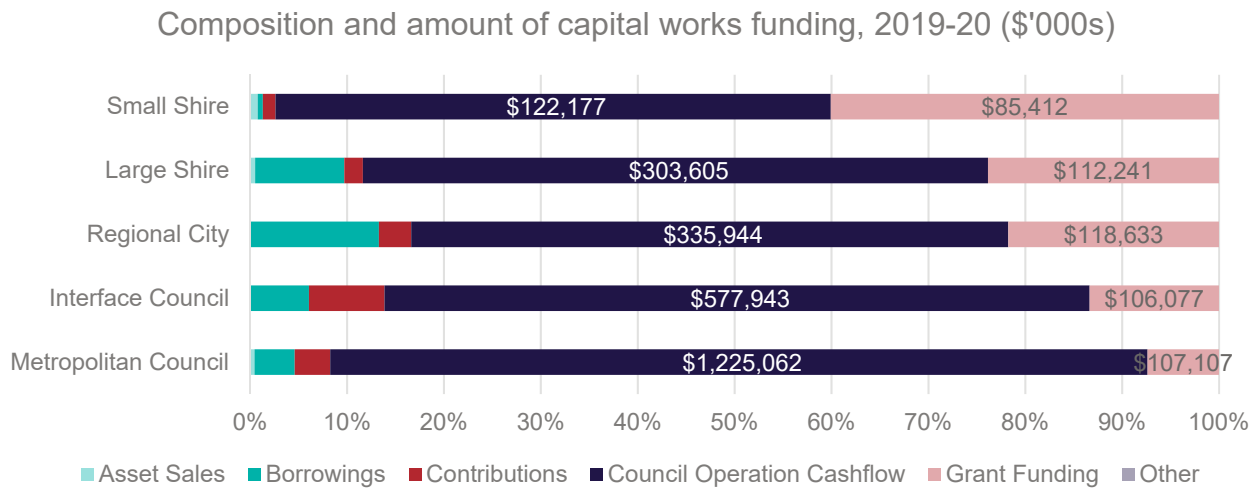


Figure 2.8 – Composition and amount of capital works funding

### Staff expenditure

Adopted budgets forecast that employment expenses will cost councils \$3.78 billion in 2019-20 which is an increase of 4.7% from 2018-19. By 2022-23 the staff expenditure will increase by 9% to \$4.12 billion from the budgeted amount of \$3.78 billion in 2019-20. The largest growth in staff expenditure over the next four years will be experienced by the interface council cohort, at 12.8%, due to increasing service requirements. **Figure 2.9** below shows staff expenditure by each cohort.

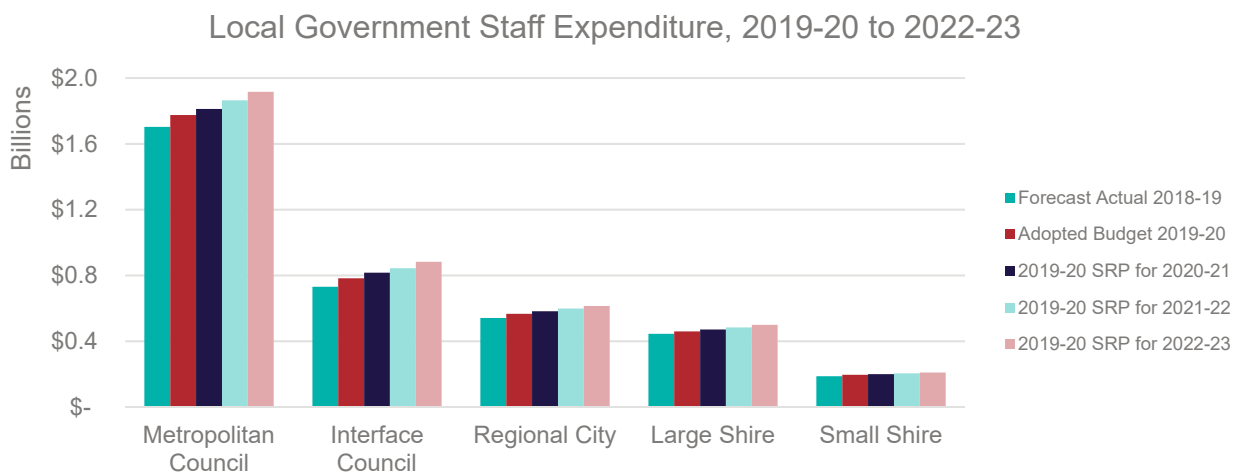


Figure 2.9 – Staff expenditure

The council adopted budgets forecast that 37,865 full time equivalent staff members will be employed in the Victorian local government sector at 30 June 2020. Budgets forecast that this will increase by 0.6% to 38,107 by 30 June 2023.

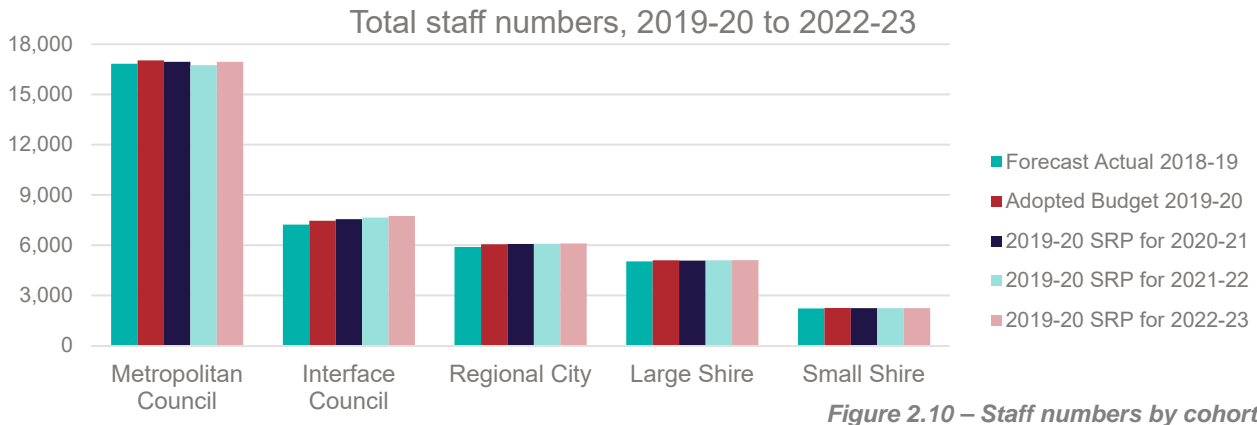


Figure 2.10 – Staff numbers by cohort

Figure 2.10 above shows a breakdown of budgeted council staff numbers by cohort and highlights the relative stability of employee numbers across the sector. Consistent with the growth in their staff expenditure figure 2.10 shows interface councils have forecast growth in staff numbers over time.

### Overall financial performance and position

Collectively, Victorian councils are budgeting to generate an operating surplus of \$1.7 billion in 2019-20. The most recent actual operating surplus for the sector was for 2017-18 and amounted to \$2.17 billion. Both the budgeted and actual surpluses have been impacted by the advance receipt of Commonwealth financial assistance grant funds. The Victoria Grants Commission (VGC) paid councils approximately 50% of their 2019-20 allocation in June 2019. Under Australian Accounting Standards these funds must be recognised as revenue upon receipt and therefore inflates the 2018-19 surplus. Consequentially, most councils have also adjusted their budgeted 2019-20 grant income, reducing the 2019-20 surplus.

The late timing of decisions by the Commonwealth make it difficult for councils to budget and accurately forecast. It is likely that councils will have adopted budgets prior to the Commonwealth's announcement and therefore impact forecast actual results and budgets. In the production of the year end financial statements councils must report on variations to budget and this will be the area of largest discrepancy.

Overall, the projected financial position of the sector is strong, with low overall debt levels and significant cash reserves. The two main indicators are the 'Net Operating Result' and the 'Adjusted Underlying Result'.

The net result indicator shows the operating result (e.g. surplus or deficit) as a percentage of total revenue, and is derived from the comprehensive income statement of each council. A positive result indicates a surplus, and the larger the percentage, the stronger the result.

A negative result indicates a deficit.<sup>7</sup> Figure 3.1 below shows that rural and regional councils generally have lower net results, and that small shires in particular, are forecasting their net results to decline over the next four years. The financial sustainability challenges of small shires were identified in VAGO's November 2016 report *Local Government: 2015-16 Audit Snapshot*.

Figure 3.1 also highlights that the interface cohort have consistently had the highest net results over the past five years, however this is mostly due to the significant value of developer contributed assets they receive and the requirement of the Australian Accounting Standards that these be recognised as revenue upon receipt.

The volatility in the graph largely reflects the timing of payment of financial assistance grants.

7. Results of 2017-18 Audits: Local Government, Victorian Auditor-General's Office, December 2018

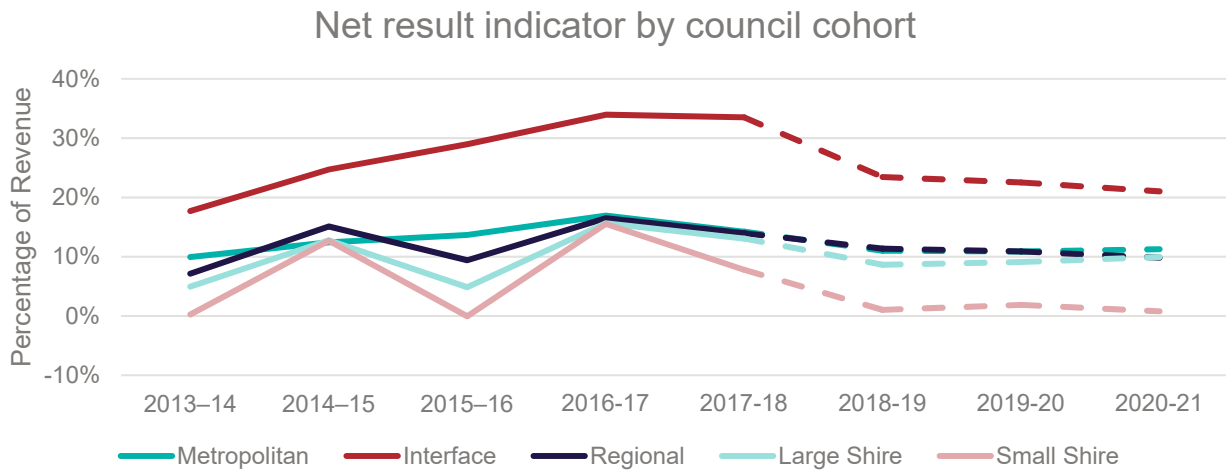


Figure 3.1 – Net result indicator

The *adjusted* underlying result indicator adjusts the council’s revenue and operating result to exclude items considered non-recurrent or capital in nature. This allows the indicator to measure the underlying operating performance of council in the ordinary course of business. To remain financially sustainable a council should ideally generate an underlying operating surplus, as operating deficits cannot be sustained in the longer term.

Figure 3.2 below again highlights the volatility caused by the different timing of payments of financial assistance grants over recent years (causing sizeable deficits in one year followed by strong surpluses in the following year).

Figure 3.2 also identifies annual underlying operating deficits, both actual and forecast, of small rural councils whereas regional and large rural councils are projecting a dip in 2018-19 results before slight improvements in 2019-20 and 2020-21 results. The operating surpluses of the metropolitan and interface council cohorts have generally remained 5% or above and are forecast to continue to do so.

These two indicators are used by the Victorian Auditor General to assess financial sustainability in their annual audits of local government finances and are replicated here by cohort group.

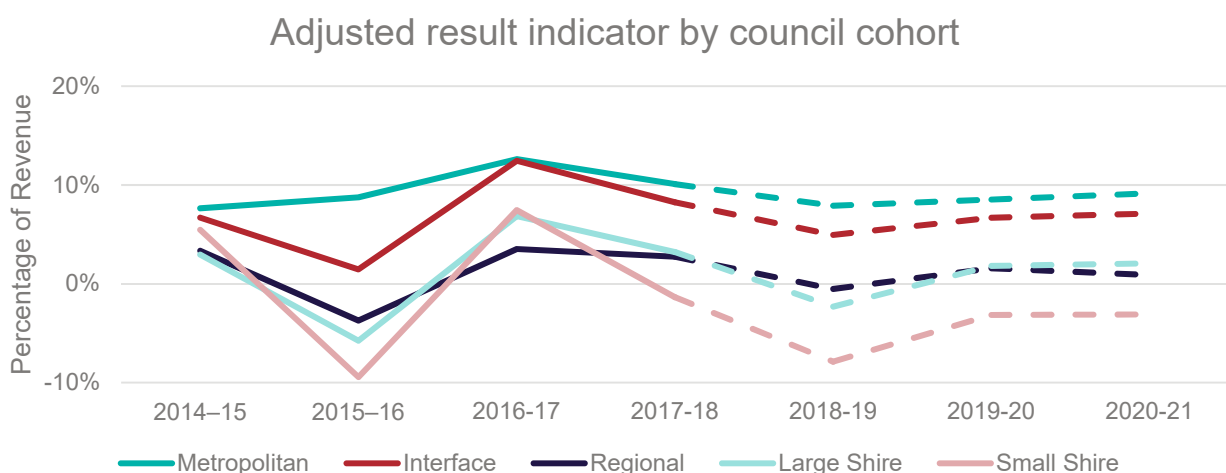


Figure 3.2 – Adjusted result indicator



## Balance Sheet - Cash and debt

The sector is budgeting to hold cash and investments of approximately \$4.3 billion at 30 June 2020. The sector's forecast actual cash and investments at 30 June 2019 was \$4.8 billion. These forecast actual levels of cash and investments may have been positively impacted in some instances by the advance receipt of Commonwealth grant funds. **Figure 4.1** below shows the comparison of budgeted cash and debt for each of the 5 council cohorts. The regional city cohort is the cohort with the smallest gap between their budgeted cash and debt.

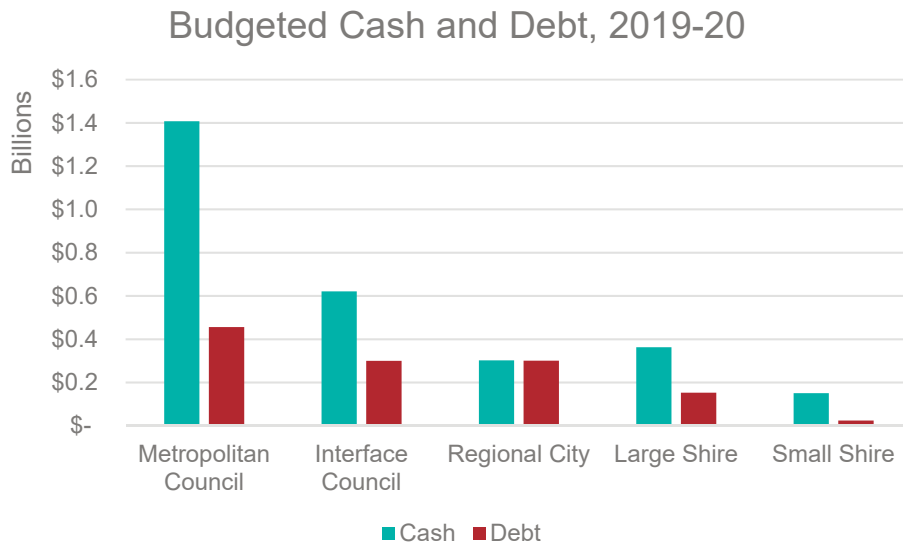


Figure 4.1 – Budgeted cash and debt

Councils are budgeting collective borrowings of \$1.23 billion by 30 June 2020.

The forecast actual level of debt at 30 June 2019 was \$1.17 billion. The forward forecast for the next three years sees total borrowings increase to \$1.48 billion by 30 June 2023. The increase in borrowings over the next three years is influenced by a forecast increase in the use of loan funds by the City of Melbourne. They forecast their borrowings to increase from \$28.5 million at 30 June 2018 to \$120.3 million by 30 June 2023. **Figure 4.2** below reflects this increase.

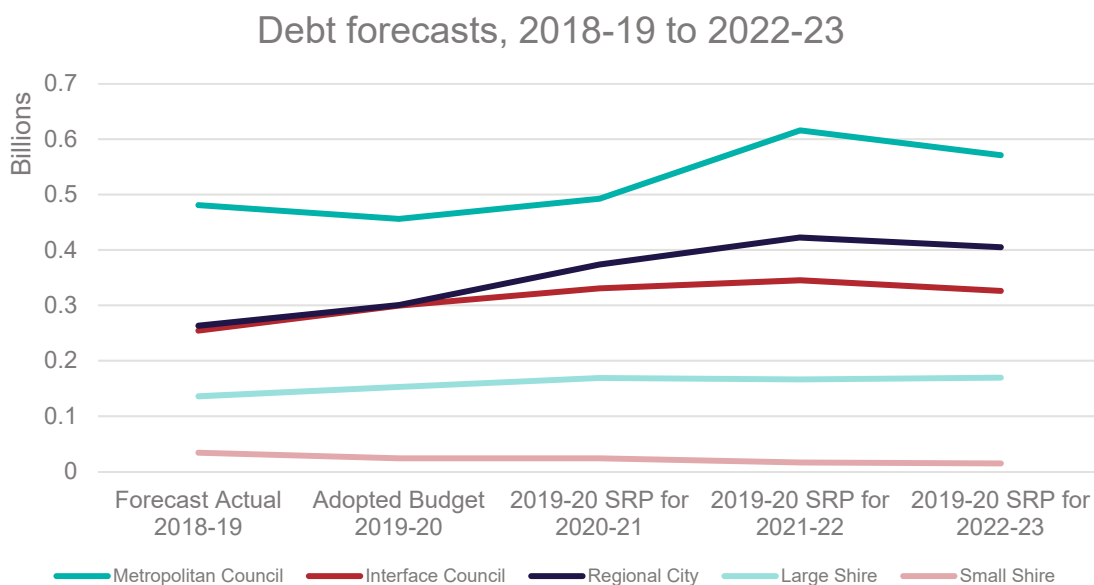


Figure 4.2 – Debt forecasts

## Conclusion

- The 79 Victorian councils adopted budgets for the 2019-20 financial year portray a picture of continued financial sustainability across the sector. There are variations both between and within cohorts;
- The sector as a whole has projected an operating surplus, and this is expected to continue over at least the next four years based on Strategic Resource Plans;
- It is now 4 years since the introduction of the Fair Go Rates System (FGRS) and over this time more than ninety-five per cent of councils have elected to set rate increases within the FGRS annual cap;
- There is no evidence of any deterioration in the finances of Victorian councils or evidence of cuts to services over this time based on budgeted expenditure levels. Capital works expenditure remains strong and a focus on asset renewal remains present;
- Rural councils remain more dependent upon government grants for their financial sustainability. This is evidenced in *Figure 1.2 - Composition of revenue by cohort* included in this report. However, even small rural councils continue to reduce debt levels and still deliver significant capital works programs. The cash to debt ratio has also been improving for all cohorts except for regional cities which is at a similar level as prior to implementation of FGRS;
- On average the planned annual capital spend by rural and regional councils according to their 2019-20 strategic resource plans is \$1.04 billion. This exceeds the previous forecast of average annual capital spend by rural and regional councils of \$850.7 million according to their 2016-17 strategic resource plans (the first year of the FGRS rate cap).



# Appendices

## Appendix A Council Cohorts

COUNCIL	VLGCG GROUPING
Banyule City Council	Metropolitan
Bayside City Council	Metropolitan
Boroondara City Council	Metropolitan
Brimbank City Council	Metropolitan
Darebin City Council	Metropolitan
Frankston City Council	Metropolitan
Glen Eira City Council	Metropolitan
Greater Dandenong City Council	Metropolitan
Hobsons Bay City Council	Metropolitan
Kingston City Council	Metropolitan
Knox City Council	Metropolitan
Manningham City Council	Metropolitan
Maribyrnong City Council	Metropolitan
Maroondah City Council	Metropolitan
Melbourne City Council	Metropolitan
Monash City Council	Metropolitan
Moonee Valley City Council	Metropolitan
Moreland City Council	Metropolitan
Port Phillip City Council	Metropolitan
Stonnington City Council	Metropolitan
Whitehorse City Council	Metropolitan
Yarra City Council	Metropolitan

COUNCIL	VLGCG GROUPING
Cardinia Shire Council	Interface
Casey City Council	Interface
Hume City Council	Interface
Melton Shire Council	Interface
Mornington Peninsula Shire Council	Interface
Nillumbik Shire Council	Interface
Whittlesea City Council	Interface
Wyndham City Council	Interface
Yarra Ranges Shire Council	Interface

<b>COUNCIL</b>	<b>VLGCG GROUPING</b>
Ballarat City Council	Regional City
Greater Bendigo City Council	Regional City
Greater Geelong City Council	Regional City
Greater Shepparton City Council	Regional City
Horsham Rural City Council	Regional City
Latrobe City Council	Regional City
Mildura Rural City Council	Regional City
Wangaratta Rural City Council	Regional City
Warrnambool City Council	Regional City
Wodonga City Council	Regional City

<b>COUNCIL</b>	<b>VLGCG GROUPING</b>
Bass Coast Shire Council	Large Shire
Baw Baw Shire Council	Large Shire
Campaspe Shire Council	Large Shire
Colac Otway Shire Council	Large Shire
Corangamite Shire Council	Large Shire
East Gippsland Shire Council	Large Shire
Glenelg Shire Council	Large Shire
Golden Plains Shire Council	Large Shire
Macedon Ranges Shire Council	Large Shire
Mitchell Shire Council	Large Shire
Moira Shire Council	Large Shire
Moorabool Shire Council	Large Shire
Mount Alexander Shire Council	Large Shire
Moyne Shire Council	Large Shire
South Gippsland Shire Council	Large Shire
Southern Grampians Shire Council	Large Shire
Surf Coast Shire Council	Large Shire
Swan Hill Rural City Council	Large Shire
Wellington Shire Council	Large Shire

<b>COUNCIL</b>	<b>VLGCG GROUPING</b>
Alpine Shire Council	Small Shire
Ararat Rural City Council	Small Shire
Benalla Rural City Council	Small Shire
Buloke Shire Council	Small Shire
Central Goldfields Shire Council	Small Shire
Gannawarra Shire Council	Small Shire
Hepburn Shire Council	Small Shire
Hindmarsh Shire Council	Small Shire
Indigo Shire Council	Small Shire
Loddon Shire Council	Small Shire
Mansfield Shire Council	Small Shire
Murrindindi Shire Council	Small Shire
Northern Grampians Shire Council	Small Shire
Pyrenees Shire Council	Small Shire
Borough of Queenscliffe	Small Shire
Strathbogie Shire Council	Small Shire
Towong Shire Council	Small Shire
West Wimmera Shire Council	Small Shire
Yarriambiack Shire Council	Small Shire