Our **Financial Strategy**

Having a Financial Strategy is one of the key tools to the Council achieving its vision for the future. It sets out the overall approach to the financial side of the Long Term Plan 2015-2025 (LTP) based on the current financial position and future direction of Council and our community.

The Financial Strategy is based on key assumptions on the projected demographics of our Community, the financial position and trends, economic trends and the current context and condition of our asset base. In particular:

- the demographics of Tairāwhiti indicate a static and ageing population
- high social deprivation and low household income means that rates affordability continues to be a concern
- Council needs to operate within a fiscal envelope that matches the communities' ability to pay as defined within the Financial Strategy
- Council has good asset information on which to base its planning
- overall, there is sufficient asset provision (i.e. no significant deficiencies) for current use and future demand
- the current use of land in the district is likely to remain.

What is Council's Financial Strategy?

The overarching aim of our Financial Strategy is to be **financially sustainable**. To Council this means that our commitments (that are prescribed by statutes and what our community expects from us) are funded in a way that the community can afford and which meet Council's obligation to be good stewards of the assets of the district.

To achieve the aim of being financially sustainable our Financial Strategy sets out six key directions.

Council will monitor the Financial Strategy regularly through quarterly financial reporting to Council through the Performance, Audit and Risk Committee. The Financial Strategy may be reviewed at any time if circumstances change. The Strategy will be formally reviewed at three yearly intervals as part of the long term planning process.

Financial Strategy Key Directions

1. Minimise and smooth rates increases

Total rates revenue will comprise up to 70% of Council's funding requirements.

Total rates increases will be no more than 2% of total rates for the first three years of the LTP. For the remainder of the Plan, total rates increases will be between inflation and 3%.

2. Minimise debt levels

External debt is the money we owe to banks and other institutions. Internal debt is the funds we borrow internally from other activities and reserves. Rather than have external debt and also money on deposit to cover reserve and activity balances, we use these fund balances to internally fund some projects. Taken together the external and internal debt make up our total debt.

External debt will be kept in the low to medium band ($18m - $55m).

Total debt will be kept below $80m.

3. Balance user pays emphasis with public good

The Revenue and Financing Policy, including Rates Remissions Policies, will be used to allocate the cost of services and "public good". Consideration of increasing the use of district-wide funding to spread the cost of infrastructure for small communities.

4. Increase other income (not from rates)

Fees and cost recoveries will be consistent with those charged by other councils or the private sector. Grants and subsidies to be "grown". The objective for holding and managing commercial investments is to provide income streams that are available to reduce rates.

Commercial operations target will be to grow income to 4-6% of asset value with a goal to increase commercial revenue to 10% of total Council income over the next ten years. This target has not been reflected in the budgets.

The Municipal Building activity is included as part of the Commercial Operations group of activity. The council has amended the Long Term Plan in November 2015 and transferred the Municipal Building activity and assets to its wholly owned subsidiary, Gisborne Holdings Ltd.

5. Activities and infrastructure at service levels that meet community needs

The focus will be on delivering and maintaining essential services and infrastructure (community and network infrastructure) at levels that are appropriate to meet community needs.

6. Assist in improving the district's ability to pay – growing our rates revenue base

Economic agencies will be supported to assist in growing the district's economy.

Key stakeholders and others will be helped to improve the productivity of Māori land.

Infrastructure to support and attract businesses into our district will be provided.

Rates remissions to attract businesses into our district or encourage existing businesses to expand.

Community infrastructure will be provided that attracts people to the district to "Live, Work, and Play".

Key Direction 1 – Minimise and smooth rates increases

Limits on rates

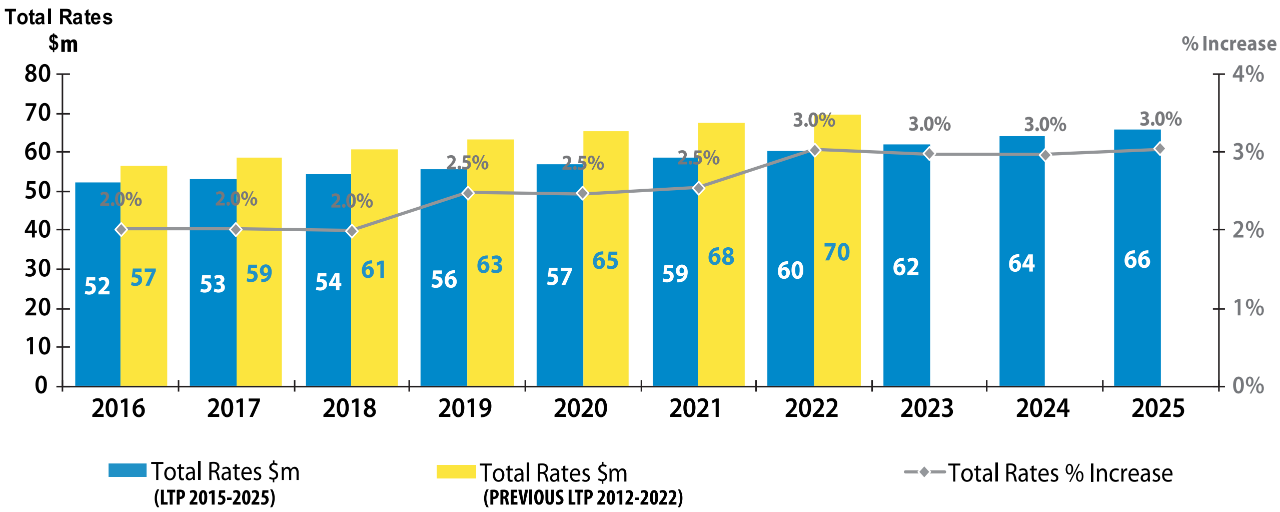
In order to balance the rates affordability challenges while continuing to provide services to our communities, Council has set the following limits on rates revenue and rates increases for the duration of this plan:

- Total rates revenue will comprise no more than 70% of Council's funding requirements. This assumes that Council Controlled Trading Organisations (CCTOs) and other enterprise operations generate the budgeted level of revenue and provide Council with the agreed level of return to offset rates requirements.
- Total rates increases will be 2% for the first three years of the LTP and between inflation and 3% over the remaining term of the LTP.

This limit will enable Council to provide and maintain the existing levels of service and to meet limited additional demands.

There can be large movements in some of Council's rates, especially targeted rates, when services are extended or cyclical expenditure occurs (e.g. Waiapu river erosion control, Wainui foredune protection). In setting limits on rates, Council has included a small level of flexibility in the majority of years to allow for unforeseen events such as increased Central Government requirements or communities requesting additional services.

Graph 1: Rate Movement (within limited increase range to 2025)



Balancing the budget

Council sets operating income at a level to meet each year's operating expenditure. This is to ensure that there is access to enough funding to enable the services to continue to be provided long term. However, there are activities where this approach may not be practical or prudent due to the long term nature of the activity i.e. wastewater, forestry, soil conservation nurseries. Over the next ten years Council intends to:

- smooth rates increases by running activity deficits/ surpluses or repaying activity deficits
- not fund a portion of depreciation on specific assets or components of assets funded through capital rates or subsidies (i.e. wastewater treatment plant and some roading assets)
- use operational reserves and/or activity balances to fund some specific operational expenditure where appropriate.

In making these decisions Council has considered the overall impact of its financial management policies, levels of service and ensured the cash flow is neutral or positive in each year (excluding major projects).

Key Direction 2 – Minimise debt levels

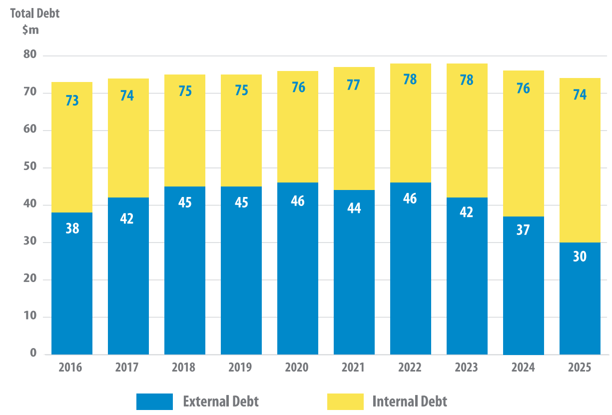
Council has a relatively low level of debt compared to similar councils which reflects Council's financial strategy of minimising debt levels. Council takes into account the following when considering the appropriate level of debt:

- possible impact on Levels of Service (LOS)
- Council's ability to service and repay borrowing
- rates affordability
- deferred maintenance
- intergenerational equity
- the long term sustainability of Council and its activities.

The total debt graph shows debt rising to $78m in 2022. External Net debt peaks at $45m to $46m in 2018 – 2020. The debt profile reflects our proposed capital works programme and its funding.

Council has amended its Long Term Plan to reflect the transfer of the Municipal buildings activity to Gisborne Holdings Ltd. This has the impact of reducing our debt to reflect the rebuild of the Fitzherbert Street building which will now be undertaken by Gisborne Holdings Ltd.

Graph 2: Total Debt (external and internal) to 2025



Limits on debt

Borrowing occurs to support working capital requirements and the Council's capital expenditure programme.

Council considers a low to medium level of Net External Debt ($18m to $55m) and Total Debt of $80m to be financially sustainable over the term of the LTP.

Securities for borrowings

Council does not currently provide security over any specific assets. Council has a debenture trust deed, representing the interests of all lenders to Council. The debenture is a floating debenture but provides the lenders with a specific charge over the rates revenue of Council.

Council is a guarantor of the New Zealand Local Government Funding Agency Ltd (LGFA). The LGFA was incorporated in 2011 with the purpose of providing debt funding to local authorities in New Zealand. Council is part of a cross-guarantee agreement in relations to the LGFA. Together with other shareholders and guarantors, Council is a guarantor of all of the LGFA's borrowings.

Intergenerational equity

Council has a desire to build a better district for current and future generations. Council also seeks to ensure that today's ratepayers only pay for the services and assets which are currently provided and not for benefits that will be received by the community in the future. This is known as intergenerational equity. Our strategy is to partially loan-fund new major projects. This allows us to pay for the new facilities over a longer period of time, often 20 – 30 years. By doing this, the people who use the asset in the future also help pay for the asset. If we didn't do this today's ratepayers would pay much higher rates.

Intergenerational equity is also achieved by funding the cost of renewing and replacing assets through rate funded depreciation reserves. Depreciation is the allocation of the wearing out of the asset over its life. By funding depreciation through rates current ratepayers are paying for the portion of the asset they are using.

Key Direction 3 – balance user pays emphasis with public good

Council services are funded by a variety of rating tools. These are outlined below:

- general rates pay for Council activities which the community requires and has available to them but no identifiable person or property benefits. How much you pay depends on the capital value of your property
- Uniform Annual General Charge (UAGC) also pays for Council activities that everyone benefits from. Every ratepayer pays the same amount wherever they live in the district
- targeted rates. The majority of our rates are based on the services you receive or have access to - like drainage, public transport, water, stormwater, wastewater, roads and rubbish collection.

How Council uses these rating tools can impact on the incidence of rates across our district.

Revenue and Financing Policy

The Revenue and Financing Policy determines from where and whom Council is seeking to fund its operations. The policy sets out why and how the funding sources are used. The Council has reviewed its Revenue and Financing Policy as part of the LTP preparation. In order to ensure the review was robust and consistent, Council applied the following general principles to the review:

1. reduce complexity and ratepayer impact
2. reduce administration and costs of implementation
3. increase predictability in reporting
4. enhance consistency of application
5. phased implementation of major changes
6. fairness and equity.

The Revenue and Financing Policy was presented and adopted as part of the draft LTP at the 25 June 2015 Council meeting.

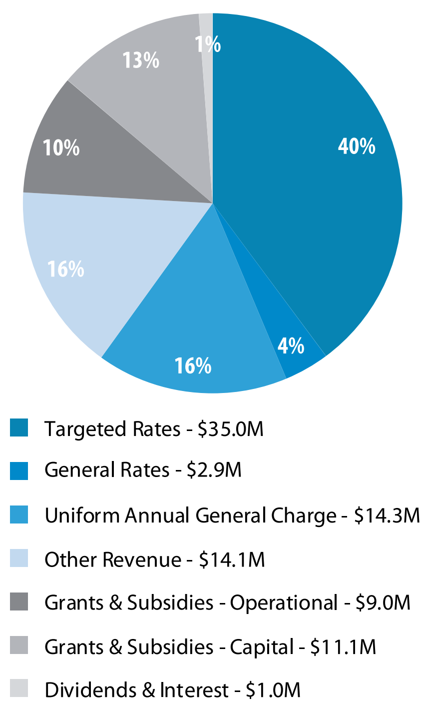
Key Direction 4 – Increase other income (not from rates)

Council mainly collects income through rates. The rates increases over the term of the LTP have been smoothed with increases ranging from 2% to 3% pa. The balance of the funding is from grants, subsidies, dividends/subvention payments and user fees.

Rates make up 60% of the expected income in the 2015-16 year.

There are no major changes anticipated for Council's funding policies or sources of income over the term of the LTP, therefore the Council income chart below is representative of the funding sources over the next ten years.

Graph 3: Where does the money come from?



Structuring of investments and commercial activities

Council maintains a number of investments in CCTOs. Its largest investment is in Gisborne Holdings Ltd. In addition to Gisborne Holdings Ltd's trading operation of Tauwhareparae Farms Ltd, it will also own and run the Municipal buildings. Council also runs a number of non-core commercial activities. These include:

- Commercial Forestry
- Commercial Property
- Gisborne Vehicle Testing
- Waikanae Beach Top 10 Holiday Park.

Council does not take a pure commercial approach to its investments. These investments are all located in the district and some are held for historic or legacy reasons. Revenues will vary and rates may need to be increased to offset reduced dividends sometimes.

Council has reviewed its Investment Strategy and as a result over the next year Council will review the governance and ownership structures of the investments and commercial activities.

An advisory group has been set up to investigate and provide professional advice and guidance to the Chief Executive on the Investment Strategy and operations of our commercial investments. They investigated three options for our commercial investments:

- Internal Management and operational (status quo)
- Divestment
- Establish a Single Commercial Entity (Council Controlled Trading Organisation)

At this point in time there has been no formal recommendation to Council on the proposals/options. Any changes to these operations will be subject to a special consultation procedure. It is likely that options will be decided upon within the next financial year.

This will be with a view to ensure that returns are maximised for Council by having in place an effective plan to leverage the commercial assets of Council. This may involve introducing additional equity partners and/or disposal of under-performing investments.

Council's primary objective for holding and managing these investments is to provide income streams that are available to reduce the rates. The quantified targets for returns from these investments are set out below.

Council's investment in Civic Assurance, Local Government Funding Agency and Bay of Plenty Local Authority Shared Services (BOPLASS) is for operational rather than investment purposes and therefore no return is budgeted.

Council has amended its Long Term Plan as a result of transferring the Municipal Buildings activity and asset to Gisborne Holdings Ltd.

The remaining Commercial investments will be reviewed in the next year. These are:

- Gisborne Vehicle Testing Station

- Waikanae Beach Top 10 Holiday Park

- Airport

- Forestry

- Social Housing may also be included.

Table 1: Council's Investment Structure to 2024/25

	2015/16 $000	2016/17 $000	2017/18 $000	2018/19 $000	2019/20 $000	2020/21 $000	2021/22 $000	2022/23 $000	2023/24 $000	2024/25 $000
Gisborne Holdings Limited										
	1,000	1,459	1,833	2,246	2,642	3.766	4.166	4.380	4.153	4.439
Interim dividend of $1m pa, final dividend making a total of 70% of the net distributable income. The increase in income in the latter years of the plan reflects the forestry harvesting at Tauwhareparae Farms Ltd.										
Waikanae Beach Top 10 Holiday Park										
	-27	64	106	144	237	253	265	268	290	310
100% of the operating surplus as a dividend. In addition to the above dividend the park contributes approximately $225k pa internal lease charges and $155k pa in overheads.										
Gisborne Vehicle Testing station										
	-15	6	46	86	92	102	109	105	123	137
100% of the operating surplus as a dividend. In addition to the above dividend the GVT contributes approximately $65k in internal lease charges and $210k pa in overheads. It retains approximately $5k pa surplus to fund capital projects.										

Key Direction 5 – Activities and infrastructure at service levels that meet community needs

Council is not planning anything significantly new to current activities and services. It will focus on delivering and maintaining essential services and infrastructure (community and network infrastructure) at their current levels or improve them where there has been deterioration in the past. Council has reviewed expenditure levels to ensure they realistically match the agreed LOS set out for each activity.

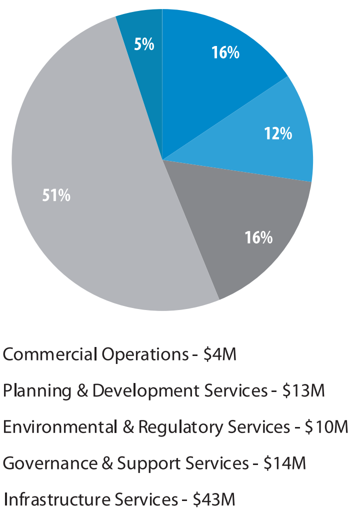
Council considers the following factors when reviewing LOS of activities:

- maintaining the Council's asset base
- consideration of ratepayer expectations
- how community infrastructure LOS impact on the attractiveness of Tairāwhiti as the first choice for people and lifestyle
- competition with other provincial centres for investment, economic growth and skilled staff
- possible alternatives to providing minimum LOS
- rates affordability.

Operational expenditure

The cost of Council doing its day to day business is driven by a number of factors. These include inflation, debt levels, salary and wage inflation, the amount of assets we own (and therefore have to maintain) and whether we increase or decrease our services to the community. The chart below shows that Council's spend on infrastructure makes up 51% of our total expenditure.

Graph 4: How the money is spent



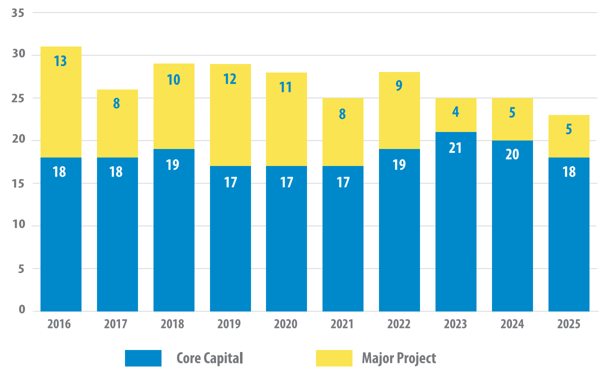
Council has $1.9b invested in fixed assets. These are mainly used to provide essential services to our communities – roads, water, stormwater, wastewater, flood protection, parks and open spaces and community facilities. Council must ensure these assets are maintained and replaced if necessary so that the services they provide can continue now and into the future. The maintenance and depreciation on Council's assets is costly. In 2016 depreciation is forecast to be $20m; this is 24% of Council's costs.

Capital Expenditure

Over the last five years Council's core capital expenditure has ranged between $17m and $21m (renewals for the last three years were between $17m and $19m). Therefore we anticipate the capital expenditure to maintain Council's asset base would continue at a similar level. Council proposes to spend $269m on capital projects over the next ten years. These are focused on core and major community infrastructure renewal projects.

To maintain our assets, so they provide the same level of service to the community, Council plans to spend around $17m and $21m a year on these routine / core projects. These are mainly renewals of existing assets that have come to the end of their useful life.

Graph 5: Capital projects - core and major



Managing capital project costs and debt

Council has staff dedicated to major project management. This has resulted in a marked improvement in Council's ability to deliver the right projects at the right place, right price and right time. Council has a programme of major community infrastructure projects planned for the next ten years. Potential funders of these projects have an expectation that Council will fund between 30% and 33% of most of the proposed major projects. This means that, for the agreed projects, Council will aim to achieve about 70% of funding from other sources outside Council. When considering major projects, Council is aware of the ongoing pressures on rates affordability.

Key Direction 6 – Assist in improving the district's ability to pay

A major theme running through our LTP is the district's ability to pay. There are two aspects to the ability to pay challenge. The first relates to the cost of Council's goods and services on the community and the way these costs are allocated. Council can control those aspects. The second relates to the value of a rate payer's property and other income.

For Council, this means (in addition to reducing costs) looking at ways in which we can maintain, and more importantly, increase our rating basis (i.e. our population). Council can assist in improving the economic performance of the district and therefore increase ratepayers' ability to pay. With limited growth projected and the current income challenge our strategy is to:

- support economic agencies to assist in growing the district's economy
- work with key stakeholders and others to improve the productivity of Māori land
- provide infrastructure to support and attract businesses in to our district
- provide the necessary community infrastructure to make Tairāwhiti the first choice for people and lifestyle.