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Committee Policy, Finance and Strategy
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Financial Report for the Nine Months ended 31 March 2004

1. Purpose

To receive the March 2004 Financial Statements (forwarded under separate cover) and to inform the Committee of the updated forecast year-end position.

2. Background

Councillors will be aware that the Chief Executive and Chief Financial Officer conduct a comprehensive review of the organisation's performance each quarter. As part of this review, management has re-examined the forecast financial position to the end of this financial year. The revised forecast position to 30 June 2004, in respect of both operating surplus and capital expenditure, is explained in sections 4.1 and 4.2 of this report.

The year to date figures to 31 March reflect favourable results, with the operating surplus ahead of budget (\$3.5 million favourable variance) and capital expenditure below budget (\$1.5 million favourable variance). The terms 'favourable' and 'unfavourable' are used in this report in a financial sense only. It is accepted that a case by case assessment is needed to assess whether or not a favourable financial variance is indeed favourable overall to the Council.

As part of the third quarter review, Managers have also been requested to identify those projects which need to be rebudgeted between years (generally projects are delayed from the current year to later years but in some cases projects can also be brought forward as a result of external influences).

These recommendations for rebudgeted expenditure and associated funding (generally through carrying forward matching funding from the current year surplus) will be considered by the Committee on 14 June 2004 as part of finalisation of the figures for inclusion in the Council's 2004/05 Annual Plan.

Last year approximately \$0.9 million of the operating surplus was carried forward to fund expenditure items that had been rebudgeted into 2003/04 and

based on the re-budget requests received to date from Divisional Managers I expect at least the same amount being carried forward from the 2003/04 surplus into 2004/05.

Such a practice avoids the Council rating the community twice for the same projects.

3. Financial Performance for the Nine Months to 31 March 2004

3.1 Operating Surplus

As noted above, the year to date operating result after nine months reflects an operating surplus ahead of budget of \$3.5 million. Detailed variances from budget are shown in the following table:

| | 2003/04 YTD Actual \$000s | 2003/04 YTD Budget \$000s | Actual vs Budget Variance \$000s | 2003/04 Year Outlook \$000s | 2003/04 Year Budget \$000s | Outlook vs Budget Variance \$000s |
|--|---------------------------------|------------------------------------|---|--------------------------------------|-------------------------------------|--|
| OPERATING SURPLUS (DEFICIT) | | | | | | |
| Water Group | 1,309 | 387 | 922 F | 1,048 | 335 | 713 F |
| Plantation Forestry | (172) | 173 | 345 U | (371) | 229 | 600 U |
| Utility Services | 1,137 | 560 | 577 F | 677 | 564 | 113 F |
| Transport | (977) | (502) | 475 U | 721 | (510) | 1,231 F |
| Landcare | 2,183 | 1,432 | 751 F | 1,985 | 1,973 | 12 F |
| Environment | 361 | 72 | 289 F | 40 | (284) | 324 F |
| Wairarapa | (215) | 102 | 317 U | (901) | 36 | 937 U |
| Corporate Advisory Services | 132 | 102 | 30 F | 8 | (15) | 23 F |
| Finance & Administration | 241 | (109) | 350 F | 128 | (270) | 398 F |
| Chief Executive | 156 | 22 | 134 F | 173 | 29 | 144 F |
| Investment in Democracy | 149 | 64 | 85 F | 178 | 85 | 93 F |
| Rates Collection | 128 | 0 | 128 F | 327 | 0 | 327 F |
| Net Divisional Surplus(Deficit) | 3,295 | 1,743 | 1,552 F | 3,336 | 1,608 | 1,728 F |
| Investment Mgmt | 7,094 | 5,123 | 1,971 F | 9,363 | 8,086 | 1,277 F |
| Business Unit Rates Contribution | (5,163) | (5,163) | - | (6,884) | (6,884) | - |
| Total Operating Surplus (Deficit) | 5,226 | 1,703 | 3,523 F | 5,815 | 2,810 | 3,005 F |

N.B: The 'outlook' figures represent updated forecasts provided by Managers as part of the third quarter review.

Significant components of the \$3.5 million favourable year to date variance are as follows:

- (1) Water Group \$0.92 million favourable variance, due to:
 - Both, direct cost savings of \$630,000, on for example contractors and consultants, chemicals, rates and insurance premiums, and indirect cost savings of \$290,000 arising from lower financial costs and depreciation charges.

- (2) Plantation Forestry \$0.35 million unfavourable variance, due to:
- The combined impact of the sustained >0.60 NZ / US dollar exchange rate and weak local demand having generated difficult operating conditions and depressed harvesting returns, whereby total expenditure savings of \$288,000 are completely outweighed by a total revenue deficit of \$633,000.
- (3) Transport \$0.48 million unfavourable variance, due to
- Bus contract price increases as a result of the recent tender round. This has been caused by external factors impacting the business of the bus operators – \$148,000 unfavourable variance.
 - Trolley bus inflation, underestimation for years 2001, 2002 & 2003 – \$806,000 unfavourable variance.
 - Non-implementation of new kick-start services & the cost of kick-start projects coming in below budget – \$695,000 favourable variance.
 - Rail contract inflation payments being below budget 2003/04 – \$394,000 favourable.
 - Delays in the English Electric Refurbishment project - \$210,000 favourable.
 - Delay in the Integrated Ticketing project - \$167,000 favourable.
 - Delay in the Porirua Interchange project to 2004/05, review of existing material to happen in 2003/04 – \$148,000 favourable variance.
 - Delays in the Rail Station upgrades, \$100,000 to be spent on upgrade of Taita station by end of 2003/04 - \$113,000 favourable.
 - Personnel costs savings as a result of an Access Planner vacancy and internal cover of maternity leave - \$91,000 favourable.
 - Depreciation savings due to delays in capital expenditure - \$92,000 favourable.
 - Bus Priority Measures, phasing difference between budget & cost of Dixon/Manners St bus lane. Development will be over budget by \$105,000 by end of financial year - \$141,000 unfavourable.
 - Refund to Transfund for overpayment of patronage growth funding in 2001/2 & 2002/03 - \$750,000 unfavourable.
 - Reduction in expected patronage growth funding for 2003/04 - \$539,000 unfavourable.
 - Road pricing project delayed to 2004/05 - \$100,000 favourable.

- Marketing & Communications funding has been provided by Transfund, which was not anticipated within the budget - \$158,000 favourable.
- Lower than anticipated level of Transfund funding for admin activities - \$200,000 unfavourable.

Councillors should note the significant turnaround in the Transport Division financial position in the third quarter moving from a favourable result at the half year to an unfavourable result after nine months. This is primarily due to the recognition within the third quarter of the reduced patronage funding from Transfund. However, the Division is forecasting to recover this lost revenue through use of Transfund ‘credits’ in the fourth quarter (refer section 4.1 of this report).

(4) Landcare \$0.75 million favourable variance, due to:

- The February floods, a shortage of suitable rock for protection works, and the difficulty in finding a mechanism for the land swap with Hutt City Council (HCC) which have delayed work programmes. There have also been savings in personnel costs, depreciation and financial costs as a result of delays in the capital expenditure programme.

(5) Environment \$0.29 million favourable variance, due to:

- Increased revenue from some large notified consents. The most significant of these were CentrePort’s resource consent applications to dredge the harbour’s entrance and near the vessel berths in the inner harbour (\$95,000) and the Lyall Bay Reef Charitable Trust (\$23,000).
- Personnel costs being under budget by \$35,000 as a result of staff vacancies. Over the last few months the appointment of a communications advisor (unbudgeted) has reduced the extent of savings.
- Materials, Supplies and Services were less than budget by some \$56,000. However, there are significant costs in the pipeline. The *Take Action* resource material is being revised and additional resources to help teachers undertake *Take Action* projects will be printed at the end of the year. Further, the Barrett Reef buoy, was changed over in April (\$20,000).
- Consultant costs were over budget by \$96,000 largely due to legal costs associated with consent applications (e.g. CentrePort) and the successful prosecution of KCDC for breaching its consent for the Waikanae River.
- Savings resulting from changing our contractors for laboratory services in connection with our freshwater programmes.

(6) Wairarapa \$0.32 million unfavourable variance, due to:

- Additional river scheme expenditure of \$350,000 for flood damage repairs, the repainting of the Barrage gates, which was brought forward from 2004/05, and the Lower Wairarapa Valley Development Scheme Review.

- A favourable variance in Biosecurity of \$150,000 due to savings in personnel costs and Pest Plant control contracts.
 - An unfavourable variance in BioWorks (Council's recently established Business Unit) of \$159,000, largely relating to the timing of Bovine Tb control operations.
- (7) Finance & Administration \$0.35 million favourable variance, due to:
- A favourable variance in Records Management of \$43,000, which is primarily due to reduced expenditure on materials and depreciation.
 - A favourable variance in IT Operations of \$187,000, which is primarily due to increased internal revenue from PCs of \$63,000, reduced depreciation charges of \$36,000, reduced expenditure on licensing fees \$40,000 and savings in personnel expenses of \$24,000.
 - A favourable variance in IT Systems Support of \$89,000, due to the delay in Council Website project.
 - An unfavourable variance in RCC Occupancy of \$47,000, which is primarily due to the renovation and re-organisation of the Regional Council Centre project completed during the year.
- (8) Chief Executive \$0.13 million favourable variance, due to:
- A decrease in personnel costs primarily made up of a refund of employer contributions to staff superannuation funds of \$120,000 (as a result of staff leaving prior to vesting date) and reduced training costs of \$35,000. These savings were partially offset by an increase in other personnel costs of \$40,000.
- (9) Investment in Democracy \$0.09 million favourable variance, due to:
- Savings in Direct Members costs, primarily Councillor Fees of \$35,000 due to the budget being set before the Remuneration Authority had set the indicative pool for Elected Members. Other savings in this area of \$45,000 are due to underspends in advertising and promotion, refreshments and consultants.
- (10) Rates Collection \$0.13 million favourable variance, due to:
- Additional rate penalty revenue compared with budget and reduced expenditure against budgeted expectations of one-off costs relating to setting up rates collection arrangements under the new legislation.
- (11) Investment Management \$1.97 million favourable variance, due to:
- A favourable variance of \$1.8 million in WRC Holdings activity mainly relates to a one-off sale at the end of March 2004 of Council tax losses to CentrePort (\$1.9 million).

This is in addition to the normal sale of tax losses which occurs each year between the WRC Holdings Group (mainly Port Investments Ltd) and CentrePort. As Councillors may be aware the Council has been steadily accumulating tax losses each year and has been recording a growing contingent asset in the notes to the financial statements within Council's Annual Report.

Officers have been working for some time, within the context of the Tax Loss Sharing Agreement entered into in 1998 between the Council, WRC Holdings Group and CentrePort, to see how best to utilise Council tax losses. After consultation with CentrePort and Horizons Regional Council I was able to reach agreement in March that CentrePort would buy some of the Council's stock of past tax losses.

The benefits of the sale of tax losses are that the Council has been able to realise value for approximately half of its stock of tax losses and CentrePort has been able to make use of approximately half of its stock of imputation credits, while the other shareholder in CentrePort, Horizons Regional Council, remains in a neutral position.

At the time of preparing Investment Management budgets for 2004/05, as part of the proposed 2004/05 Annual Plan, officers anticipated receipt of this money within Council's Treasury function. Its impact on reduced Council debt is therefore already factored into next year's budget. Given the potential for Council debt to be increased significantly in future in respect of transport it is prudent in my view to apply the \$1.9 million from CentrePort to debt reduction.

- The average year-to-date interest rate (5.79%) on the \$44 million liquid financial deposit has been higher than the budgeted interest rate of 5.60%. This has resulted in additional interest revenue of \$60,000.
- An underspend of \$100,000 in WRC Admin Properties mainly relates to the deferral of planned air conditioning maintenance of the Masterton office of \$75,000 (due to the review of Masterton office accommodation). There was also a delay to the work on Upper Hutt Depot roof (which is expected to be completed by the end of June 2004).

3.2 Net Capital Expenditure (capital expenditure net of disposals)

As noted above, the year-to-date net capital expenditure for the nine months to 31 March 2004 is \$1.5 million below budget. Detailed variances from budget are shown in the following table:

| | 2003/04 YTD Actual \$000s | 2003/04 YTD Budget \$000s | Actual vs Budget Variance \$000s | 2003/04 Year Outlook \$000s | 2003/04 Year Budget \$000s | Outlook vs Budget Variance \$000s |
|--------------------------------|------------------------------------|---------------------------------|---|--------------------------------------|-------------------------------------|--|
| NET CAPITAL EXPENDITURE | | | | | | |
| Utility Services | 2,770 | 4,419 | 1,649 F | 4,295 | 5,852 | 1,557 F |
| Landcare | 1,448 | 1,650 | 202 F | 2,688 | 2,947 | 259 F |
| Environment | 191 | 267 | 76 F | 237 | 267 | 30 F |
| Transport | 570 | 218 | 352 U | 734 | 238 | 496 U |
| Wairarapa | 317 | 274 | 43 U | 427 | 349 | 78 U |
| Corporate Advisory Services | 5 | 0 | 5 U | 5 | 0 | 5 U |
| Chief Executive | 30 | 34 | 4 F | 34 | 34 | - |
| Finance & Administration | 246 | 234 | 12 U | 247 | 513 | 266 F |
| Rates Collection | 21 | 0 | 21 U | 21 | 0 | 21 U |
| Investment in Democracy | 0 | 5 | 5 F | 5 | 5 | - |
| Net Capital Expenditure | 5,598 | 7,101 | 1,503 F | 8,693 | 10,205 | 1,512 F |

N.B: The 'outlook' figures represent updated forecasts provided by Managers as part of the third quarter review.

Significant components of the \$1.5 million favourable year to date variance are as follows:

- (1) Utility Services \$1.65 million favourable variance, due to:
 - Project deferrals and slower than anticipated progress on various Water Group and Plantation Forestry capital work projects have generated favourable differences against budget to date of \$1.20 million and \$25,000 respectively. In addition, significantly fewer than budgeted minor asset acquisitions have occurred during the year to date resulting in a further saving of \$200,000.
- (2) Landcare \$0.20 million favourable variance, due to:
 - Almost all the capital works projects were affected by the February storms. In addition, capital works in East Harbour have been delayed until the land swap with HCC is complete.
- (3) Transport \$0.35 million unfavourable variance, due to:
 - Transfer of ownership of the new Petone Station from HCC to the Council as a result of change in legislation and completion of the project. This project was not budgeted as a capital project.

4. Year End Outlook Position

4.1 Revised year end Operating Surplus

The projected year-end operating surplus has been revised as part of the March quarterly review process. The projected year-end operating surplus is now \$5.8 million, an increase of \$2.6 million over the December forecast of \$3.2 million.

Detailed movements from the December forecast to the current forecast (labelled outlook) are shown in the following table:

| | 2003/04 Year March Outlook \$000s | 2003/04 Year December Forecast \$000s | Variance \$000s |
|--|---|---|--------------------|
| OPERATING SURPLUS (DEFICIT) | | | |
| Water Group | 1,048 | 979 | 69 F |
| Plantation Forestry | (371) | (457) | 86 F |
| Utility Services | 677 | 522 | 155 F |
| Transport | 721 | 219 | 502 F |
| Landcare | 1,985 | 2,025 | 40 U |
| Environment | 40 | (225) | 265 F |
| Wairarapa | (901) | (500) | 401 U |
| Corporate Advisory Services | 8 | (54) | 62 F |
| Finance & Administration | 128 | (189) | 317 F |
| Chief Executive | 173 | 29 | 144 F |
| Investment in Democracy | 178 | 148 | 30 F |
| Rates Collection | 327 | 210 | 117 F |
| Net Divisional Surplus (Deficit) | 3,336 | 2,185 | 1,151 F |
| Investment Management | 9,363 | 7,937 | 1,426 F |
| Business Unit Rates Contribution | (6,884) | (6,884) | - |
| Total Operating Surplus (Deficit) | 5,815 | 3,238 | 2,577 F |

Significant components of the overall increase in forecast operating surplus are:

- (1) Transport increase in forecast surplus of \$0.50 million, due to:
 - Forecast use of Transfund Patronage Growth ‘credits’ to fund projects which were originally 100% rates funded e.g. Wellington Interchange Service Level Agreement.

- (2) Environment increase in forecast surplus of \$0.27 million, due to:
 - Increased revenue forecast from some large notified consents (\$90,000).
 - Further savings anticipated with Council’s freshwater programmes as a result of the changes in Council’s contractors for laboratory services.

- (3) Wairarapa decrease in forecast surplus of \$0.40 million, due to:
- River Scheme flood damage repair works which has been separately reported to the Council.
- (4) Finance & Administration increase in forecast surplus of \$0.32 million, due to:
- Savings of \$47,000 forecast in the Finance Department primarily in personnel expenses and consultants.
 - The majority of costs associated with the Council Website redevelopment project have been forecast to occur next year (\$157,000).
 - Further savings of \$80,000 have been forecast in IT and Support Services Department in license fees and depreciation, and additional internal income re PCs of \$40,000.
- (5) Chief Executive increase in forecast surplus of \$0.14 million, due to:
- Receipt of credit of excess employer contributions on staff superannuation funds of \$120,000 offset by increased other personnel costs of \$40,000.
 - Reduced training costs of \$35,000 and reduced management consultancy costs of \$30,000.
- (6) Rates Collection increase in forecast surplus of \$0.12 million, due to:
- Additional revenue associated with rate penalties and further savings in one-off costs relating to setting up rates collection arrangements under the new legislation.
- (7) Investment Management increase in forecast surplus of \$1.43 million, due to:
- An increase in forecast surplus of \$1.53 million in the WRC Holdings activity which mainly relates to a one-off sale of Council tax losses to CentrePort for \$1.87 million. This was offset by a further decrease of \$0.34 million in the expected dividend revenue from WRC Holdings Ltd as a result of lower than budgeted dividends from CentrePort.
 - A decrease in forecast surplus of \$100,000 in the Treasury function mainly relates to reduced interest revenue on funds borrowed by internal departments.

4.1.1 Analysis of Operating Surplus – Area of Benefit

It is important to identify which areas of the Council are forecasting surpluses and deficits as there are different communities of interest involved.

| | 2003/04 year end outlook (\$000) | 2003/04 year end budget (\$000) | Outlook vs Budget variance (\$000) |
|---------------------------------|---|--|---|
| Water supply | 1,048 | 335 | 713F |
| Transport | 721 | (510) | 1,231F |
| Other regional responsibilities | 4,046 | 2,985 | 1,061F |
| | 5,815 | 2,810 | 3,005F |

N.B: the 'outlook' represents the latest view of the forecast position to 30 June 2004.

As has been past Council practice, the funding surplus above budget in the Regional Water Supply area is forecast to be applied to debt reduction and the funding surplus in Regional Transport is forecast to be transferred into the Transport reserve. The forecast balance in the Transport reserve at 30 June 2004 will need to be considered by the Committee as part of finalising the 2004/05 Annual Plan.

The Other Regional Responsibilities surplus is primarily due to sale of Council tax losses to CentrePort. As noted above, this has been assumed to be applied to debt reduction.

4.2 Revised year end Net Capital Expenditure

Overall, capital expenditure is now projected to be \$8.7 million at year-end compared to the December forecast of \$8.6 million. Detailed movements from the December forecast to the current forecast (labelled 'outlook') are shown in the following table:

| CAPITAL EXPENDITURE | 2003/04 Year | 2003/04 Year | Variance \$000s |
|----------------------------------|----------------------------|--------------------------------|--------------------|
| | March Outlook \$000s | December Forecast \$000s | |
| Utility Services | 4,295 | 3,986 | 309 U |
| Landcare | 2,688 | 2,934 | 246 F |
| Environment | 237 | 267 | 30 F |
| Transport | 734 | 384 | 350 U |
| Wairarapa | 427 | 349 | 78 U |
| Chief Executive | 34 | 34 | - |
| Corporate Advisory Services | 5 | 60 | 55 F |
| Finance & Administration | 268 | 557 | 289 F |
| Investment in Democracy | 5 | 5 | - |
| Total Capital Expenditure | 8,693 | 8,576 | 117 U |

Significant components of the increase in forecast capital expenditure since December 2003 are:

- (1) Utility Services increase in forecast capital expenditure of \$0.31 million, due to:
 - The availability of more accurate finalised project costs within the 2003/04 Water Group capital works programme, as various activities approach completion.
- (2) Landcare decrease in forecast capital expenditure of \$0.25 million, due to:
 - Timing variances on the Ava to Ewen Project, and the decision not to undertake some planned capital works in East Harbour Regional park until the land swap with HCC is completed.
- (3) Transport increase in forecast capital expenditure of \$0.35 million, due to:
 - Transfer of ownership of the new Petone Station from Hutt City to the Council as a result of change in legislation and completion of the project. This project was not budgeted as a capital project.
- (4) Finance and Admin decrease in forecast capital expenditure of \$0.29 million, due to:
 - A portion of the IT capex programme (\$261,000) and the Records management system project (\$65,000) have now been forecast not to occur in 2003/04 due to a decision to extend the life of existing hardware and timing delays of various projects.

5. Compliance with Treasury Management Policy

As at 31 March 2004, all Treasury Management Policy limits have been complied with. (Refer **Attachment 1**).

As the Committee may recall the Treasury Management Policy which was adopted in 30 June 2003 included new consolidated borrowing compliance limits. However, we have recently discovered that we have been incorrectly reporting on these limits since the September 2003 quarter. The calculation has now been revised to reflect the intended definitions when the limits were introduced i.e. to align our newly introduced consolidated limits with the approach adopted by Standards and Poor's when they assess Council's financial health. The effect of this change has been to reduce the actual measures recorded compared with the limits.

6. Communications

The financial results continue to be favourable. However, it is expected that the year end position will provide the key communications opportunity.

7. Recommendations

That the Committee recommend to Council that it:

- (1) Receive the report and note its contents.*
- (2) Approve the revised forecast figures to 30 June 2004 (termed 'outlook' within this report) and note that they will replace the forecast figures prepared as part of the half year review.*

Report prepared by:

Approved for submission:

Marie Kitchener
Financial Accountant

Greg Schollum
Chief Financial Officer

Attachment 1: Treasury Management Compliance Report