



Report 03.535
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Committee Policy, Finance and Strategy
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Annual Report for the year ended 30 June 2003

1. Purpose

To report the results of the Council for the year ended 30 June 2003 and to seek Committee approval of the draft Annual Report (forwarded as a separate document).

2. Background

Under the Local Government Act 1974, the Council is formally required to adopt the Annual Report by 30 November each year to enable the Audit Certificate to be released by Audit New Zealand. (The Local Government Act 2002 will apply to next year's Annual Report.)

The Council normally adopts the Annual Report by the end of October each year, which is the case again this year.

Rudie Tomlinson, our audit Director from Audit New Zealand, will be in attendance at the meeting on 30 October 2003 to summarise the results of the annual audit and to answer any questions that the Committee may have.

Although, at the time of writing this report Audit New Zealand have yet to provide formal clearance on the Annual Report, we are confident that clearance will be provided before the meeting so that the signed Audit Certificate will be available at the meeting on 30 October 2003, once the accounts are adopted by the Committee.

3. 2003 Annual Report Document

The 2003 Annual Report has been modelled on those prepared in previous years, which is not too surprising given it is fundamentally a compliance report, with the majority of disclosures required by law.

The 2003 Annual Report reports against the third year of the Council's Long Term Financial Strategy, "Investing in the Future 2000-2010".

Next year will be the first time we report against the Council's recently adopted Long Term Council Community Plan "Towards a sustainable region

2003-2013". It will also be the first year we need to comply with the reporting provisions of the new Local Government Act 2002.

I expect that the format of next year's report to be different as it will be the first year we report on our progress towards achieving the outcomes, in the form of "Take 10" targets that the Council specified within the "Towards a sustainable region" document.

Also, the legal deadline for when the Annual Report must be adopted by the Council has been shortened by one month to the end of October. However, this should not cause the Council any significant problems as we have traditionally adopted the Annual Report by this date.

4. Financial Performance for the year ended 30 June 2003

4.1 Net Surplus

The Council's net surplus for the 2002/03 financial year was \$23.7 million compared with a budgeted net surplus of \$3.6 million, resulting in a net surplus ahead of budget of \$20.1 million.

Normally the net surplus for the Council is the same figure as the operating surplus of the Council, which we report to the Council each month, showing the operating result of the Council's activities. However, this year there is a second component to the net surplus with the Council recording an unbudgeted one-off gain in the Statement of Financial Performance of \$14.9 million.

This non cash gain has occurred as a result of the asset revaluation exercise undertaken within the Parks and Forests areas of the Council. The Parks and Forests assets were last valued in 1991 for the purposes of bringing these assets into the Council's balance sheet for the first time.

Normally an upwards revaluation in asset values is credited to reserves. However, in this case the revaluation exercise identified a range of assets which were not on the Council's fixed asset register (i.e. such assets were either never recorded initially, or have since been written off).

In such a situation the appropriate accounting treatment is to recognise the credit within the Council's net surplus. For obvious reasons we have chosen to separate it out and disclose it after operating surplus.

4.2 Operating Surplus

The Council's operating surplus for the 2002/03 financial year was \$8.7 million compared with a budgeted operating surplus of \$3.6 million, resulting in an operating surplus ahead of budget of \$5.1 million.

The majority of the surplus has been generated within the Water Supply, Transport, Investment Management and Rates Collection areas.

Variances from the budget, by activity, are shown below:

	2002/03 Actual \$000s	2002/03 Budget \$000s	Variance \$000s
NET SURPLUS (DEFICIT)			
Water Group	2,001	565	1,436 F
Plantation Forestry	(285)	(224)	61 U
Utility Services	1,716	341	1,375 F
Transport	1,718	(106)	1,824 F
Landcare	1,941	1,558	383 F
Environment	130	(135)	265 F
Wairarapa	25	(108)	133 F
Corporate Advisory Services	(249)	(15)	234 U
Finance & Admin	(109)	(170)	61 F
General Manager	(129)	(55)	74 U
Investment in Democracy	115	(3)	118 F
Rates Collection	670	0	670 F
Net Divisional Surplus (Deficit)	5,828	1,307	4,521 F
Investment Management	8,773	8,162	611 F
Business Unit Rates Contribution	(5,827)	(5,827)	-
Total Operating Surplus (Deficit)	8,774	3,642	5,132 F
Parks and Forests asset adjustment	14,916	0	14,916 F
Net Surplus (Deficit)	23,690	3,642	20,048 F

Significant components of the \$5.1 million favourable variance in operating surplus are as follows:

4.2.1 Water Supply favourable variance of \$1.44 million, primarily due to:

- Lower than budgeted expenditure of \$784,000 by all Water Supply departments, across all major types of materials, supplies and services procurement, but most significantly on chemicals, energy and rates.
- Financial cost savings of \$524,000 arising from lower than planned debt levels throughout 2002/03.

4.2.2 Plantation Forestry unfavourable variance of \$0.06 million, primarily due to:

- The combined impact of the NZ dollar appreciating against the US dollar throughout the financial year and weak local demand for wood, which generated difficult operating conditions.

4.2.3 Transport favourable variance of \$1.82 million, due to:

- The delay of the English Electric refurbishment & Waikanae Rail electrification project - \$1.1 million favourable variance.
- The delay and/or non-implementation of new kick-start services, & the cost of kick-start projects coming in below budget - \$1.3 million favourable variance.
- The delay in the start of the new rail station at Petone - \$278,000 favourable variance.
- Patronage revenue from Transfund NZ being below budget - \$500,000 unfavourable variance.
- The cost of the new Strategic Transport Model being above the original budget - \$223,000 unfavourable variance.
- The cost of the new bus lanes in Hunter Street & Lambton Quay not being included in the budget - \$135,000 unfavourable variance.

4.2.4 Landcare favourable variance of \$0.38 million, due to:

- Savings in personnel costs of \$330,000 as a result of the restructuring which took place in 2001/02 and natural attrition.
- \$230,000 savings in depreciation resulting from a lower capital spend in 2001/02 and 2002/03 in Flood Protection (largely a result of delays in the Strand Park realignment) and the revaluation of Flood Protection assets in June 2002.
- An unfavourable variance of \$127,000 from write-offs of Parks and Forests assets as a result of the revaluation in June 2003 (more than offset by the one-off gain of \$14.9 million relating to the same revaluation exercise).

4.2.5 Environment favourable variance of \$0.27 million, due to:

- Increased revenue of \$64,000.

In the latter months of the year more applications for resource consents were processed than had been budgeted. However, some of this revenue increase has been offset by higher than budgeted commissioners' fees (\$22,000) arising from notified consents. These fees are fully recoverable from applicants.

In addition, some unbudgeted internal transfers occurred (e.g. the Wairarapa Division transferred \$25,000 for the QE11 private land covenant programme).

- External Contractors and Consultants were \$261,000 under budget.

The underspend is mainly associated with the unwanted agricultural chemical collection project (\$60,000), the stormwater investigation work (\$22,000) and contaminated sites work (\$29,000). In addition, there are a range of other smaller savings.

4.2.6 Wairarapa favourable variance of \$0.13 million, due to:

- The Land and River Operations Department being \$134,000 below budget because of reduced QEII expenditure arising from delays in covenant signing, and reduced maintenance expenditure for River Schemes due to the capitalisation of new flood protection assets constructed during 2002/03.
- Several offsetting variances including; reduced logging income and expenditure of \$0.6m for Reserve Forests because of delays to Tauanui logging, reduced Bovine Tb vector control income and costs of \$0.6m because of contractor savings and lower pest densities. (i.e. some control work wasn't required)

4.2.7 Corporate Advisory Services unfavourable variance of \$0.23 million, due to:

- Increased personnel costs of \$123,000 due to having an unbudgeted staff member in the communications department, as well as increased management training costs, temporary staff and unbudgeted recruitment costs across the division.
- Increased expenditure on consultants and materials of \$149,000 mainly related to costs associated with the LTCCP process (additional costs of consultation, information gathering and document preparation) and rebranding.

4.2.8 Finance and Admin favourable variance of \$0.06 million, due to:

- Reduced personnel costs as a result of staff vacancies.

4.2.9 General Manager unfavourable variance of \$0.07 million, due to:

- Unbudgeted expenditure of \$72,000 on the renewable energy project. While preliminary work on this project commenced during 2002/03 a new project was added into the Council's work programme as part of finalising the Council's Long-term Council Community Plan.

4.2.10 Investment in Democracy favourable variance of \$0.12 million, due to:

- Savings in personnel costs of \$30,000 in the Council Secretariat.

- Savings in Elected Members of \$87,000 primarily in relation to lower than budgeted legal costs 18,000, travel costs \$120,000, depreciation \$130,000, Councillor fees of \$23,000, and advertising of \$23,000.

4.2.11 Rates Collection favourable variance of \$0.67 million, due to:

- Additional rates revenue of \$693,000 of which \$490,000 relates to 2001/02 revenue not previously recognised, due to an error in the calculation of the 2002 closing balance by one of our collecting agents (WCC). New rate collection procedures instituted with effect from 1 July 2003, including full monthly reconciliations, should reduce the likelihood of this recurring in future. The remaining additional revenue related to this financial year.

4.2.12 Investment Management favourable variance of \$0.61 million, due to:

- An unbudgeted non cash gain in the value of shares in WRC Holdings Ltd of \$545,000 as a result of a similar write-up of the value of the Regional Council Centre in the books of Pringle House Ltd.
- Dividend revenue for the year being \$177,000 higher than budget. This is primarily due to an increase in the final dividend that the Council receives from WRC Holdings Ltd.
- Subvention revenue from Pringle House Ltd being \$215,000 higher than budget. This is due to an increased taxable surplus within Pringle House Ltd (which is transferred to the Council by way of a subvention payment).
- Average year-to-date interest rates on the Council's liquid financial deposits being lower than the budgeted interest rate. This has resulted in an unfavourable variance of \$285,000.

4.3 Net Capital Expenditure

Net capital expenditure for the year was \$2.1 million below budget.

Variances from the budget, by activity, are shown below:

	2002/03 Actual \$000s	2002/03 Budget \$000s	Variance \$000s
NET CAPITAL EXPENDITURE			
Utility Services	3,008	3,094	86 F
Landcare	1,271	3,282	2,011 F
Environment	290	299	9 F
Transport	64	27	37 U
Wairarapa	578	290	288 U
Finance & Admin	166	484	318 F
Investment in Democracy	58	30	28 U
Total Net Capital Expenditure	5,435	7,506	2,071 F

Significant components of the \$2.1 million favourable variance are as follows:

4.3.1 Landcare favourable variance of \$2.01 million, due to:

- Delays in the procurement of land required for the Strand Park channel realignment resulting in a project underspend for the year (including land purchase) of \$1,761,000.
- A prolonged consultation process with KCDC and Kapiti residents which delayed the construction of the Otaihanga stopbank, resulting in an underspend of \$184,000. The job should be completed in 2003/04.
- The new toilet blocks at Queen Elizabeth Park also being delayed, with construction to be completed in the 2003/04 year. The savings in 2002/03 were \$88,000.

4.3.2 Wairarapa unfavourable variance of \$0.29 million, due to:

- New flood protection structures for River Schemes of \$187,000, offset by savings in operating expenditure noted earlier in this report.
- Taunau forestry road construction costs of \$163,000.
- The \$100,000 Te Whiti stopbank construction not proceeding as planned (this has been rebudgeted in 2003/04).

4.3.3 Finance and Admin favourable variance of \$0.32 million, due to:

- Deferral of part of IT hardware replacement programme and part of the Records Management System until 2003/04 which has reduced capital expenditure in 2002/03 by \$305,000.

4.4 Funding Position

The table below summarises the overall funding movements of the Council compared with budget:

	2002/03	2002/03	
	Actual	Budget	Variance
	\$000s	\$000s	\$000s
Regional Water Supply	2,001	565	1,436
Regional Transport	1,725	(96)	1,821
Regional Stadium	700	700	-
Other Regional Responsibilities	4,348	2,473	1,875
Operating Surplus (Deficit)	8,774	3,642	5,132
Movement in Reserves	(2,365)	(122)	(2,243)
Add Back Non Cash Items	7,735	8,123	(388)
Funding Surplus from Operations	14,144	11,643	2,501
Less:			
Net Capital Expenditure	5,435	7,506	(2,071)
Investment Additions	1,551	1,500	51
New Loans	(6,386)	(8,493)	2,107
Investment Redemption	-	-	-
Net Capital Expenditure and Investment	600	513	87
Working Capital Movement	(2,633)	(5,000)	2,367
Debt Repayment	16,177	16,130	47
Net Funding Surplus (Deficit)	-	-	-

As has been past Council practice, the funding surplus above budget in the Regional Water Supply area has been applied to debt reduction and the funding surplus in Regional Transport has been transferred into the Transport reserve.

Other funding surpluses or deficits relating to other separate areas of benefit (eg. River and Pest rates) have also been applied to their specific reserves, in proportion to their respective revenue and financing policy ratios (refer to section 4.5.3 below on reserves).

Reserves have also been adjusted to reflect the expenditure rebudgeted from 2002/03 into 2003/04. Through the expenditure rebudgeted and associated reserve transfers the Council has effectively carried forward approximately \$0.9 million of the 2002/03 surplus into the 2003/04 year.

The Council has a longstanding policy of using all surplus funds after reserve transfers and working capital requirements to repay debt. While there are no additional funds available this year for debt repayment, the actual movement in working capital compared to budget has enabled maturing debt to be repaid in early 2003/04 (Sept 2003).

The figures presented do not include a forestry dividend for the 2002/03 year and it is recommended that the 2002/03 dividends from both forestry areas, Plantation Forestry and Reserve Forests be waived.

4.5 Financial Position at 30 June 2003

The Council's financial position remains strong.

4.5.1 Debt Position

Net Council debt has decreased by \$12.1 million during the year from \$78.4 million at 30 June 2002 to \$66.3 million at 30 June 2003. The consolidated position, incorporating the WRC Holdings Group (including CentrePort) also makes good reading with net debt decreasing by \$14.2 million during the year from \$148.2 million at 30 June 2002 to \$134.0 million at 30 June 2003.

The main components of the Council debt include the Water Supply debt, Flood Protection debt and the debt associated with Council's contribution to the Stadium.

This further decline in debt levels and surpluses above budget should provide the Standard and Poor's rating agency (S&P) with continuing comfort around our ability to service our financial obligations.

4.5.2 Investments

The Council manages a significant portfolio of investments comprising equity investments, liquid financial deposits, sinking funds, special funds, forestry, stadium advance and, from time to time, short-term money market deposits. The Treasury Management Policy (last updated 30 June 2003) includes the Council's philosophy and approach to management of its investments.

These investments are explained in more detail within the Annual Report. (Refer to Note 6 on page 36 and the Investments section on page 124).

4.5.3 Reserve Position

A detailed analysis of reserve movements during the 2002/03 year is provided as **Attachment 1** of this report, along with explanations of variances between budgeted and actual reserve movements. All variances from budgeted reserve movements need to be approved by the Council as part of its adoption of the 2003 Annual Report. (The budgeted reserve movements were implicitly approved as part of the 2002/03 Annual Plan.)

A reminder that the Council has four types of reserves. They can be categorised as follows:

- *Reserves for each Different Area of Benefit.*

These reserves are used where there is a discrete set of rate or levy payers as distinct from the general rate, e.g. Regional Water Supply, Transport, Bovine Tb, Parks Land Purchase, River Rates, and Wairarapa Schemes.

Any funding surplus or deficit relating to these separate areas of benefit is applied to the specific reserves, in proportion to their respective revenue and financing policy ratios.

If the Council establishes other separate funding sources in the future the same will apply. Such reserves are often long-term in nature, in that the use of the available funding spans many years.

- *Contingency Reserves*

The Council has traditionally set aside reserves that can be made available when a specific unforeseen event occurs. This currently includes Water Supply Quality, Environment Legal, Flood and Rural Fire Contingency reserves.

The release of these funds generally can only be approved by Council, with some delegation to Divisional Managers. Again, these reserves are typically long-term in nature.

- *Reserves where there has been Rebudgeting of Expenditure*

As part of each planning process Department Managers indicate the funds needed to achieve specific outputs during the year. Any surpluses generated as a result are available for Council use (unless there is an area of benefit issue) and unless determined otherwise by the Council, those surpluses will be used to reduce Council debt. This benefits the Council as a whole.

One exception to this rule is where a specific project has been planned to be completed during the financial year, but has not been. If this project is still a priority of the Council, then it is appropriate to rebudget this expenditure in the following year. This process is undertaken as part of finalising the Annual Plan in June each year. Funds are made available in the following year to fund these projects and the main mechanism to achieve this is through the use of a reserve (except for loan funded projects where the raising of the loan is merely delayed). By doing this the Council does not rate the community twice for the same project. The actual transfer to reserve occurs now as part of finalising the Annual Report.

- *Special Reserves*

The only special reserve of the Council is the Election Reserve. The reserve is necessary to smooth the costs of the local body elections across the three years of each triennium.

4.5.4 Asset Management

Asset management plans remain an important building block in Council's financial management framework. The majority of the Council's asset base consists of Regional Water Supply, Flood Protection and Parks and Forests assets. These important community assets are required to be maintained and, where possible enhanced, to enable the Council to continue to provide the agreed service levels to the community in future years.

During the year the Council made further progress in its asset management planning with the Parks and Forests Infrastructural Assets being revalued, resulting in an increase in value of approximately \$28.5 million.

In 2003/04 officers plan to conduct another revaluation of the Water Supply assets. These assets which were last valued in 1999 need to be revalued at least every five years.

5. Non Financial Results

The Council is required by law to report in its Annual Report its achievements against the performance indicators published in the 2002/03 Annual Plan.

Reporting is therefore grouped into Council's significant activities as follows:

Environment Management

Regional Transport

Regional Water Supply

Land Management

Flood Protection

Parks & Forests

In addition we have separately reported on Investment in Democracy and the Council's involvement with the Stadium and other Investments.

Overall, it is pleasing to see that once again the majority of performance targets have been met. Where shortfalls have occurred, the reasons are clearly stated.

6. Compliance with Treasury Management Policy

The Treasury Management Policy in force for the majority of the year was adopted by the Council in November 1999 (refer **Attachment 2**). With one exception, all borrowing limits have been complied with during the year:

- On 17th June 2003 Standard and Poor's dropped the credit rating on the Council's main transaction bank, the National Bank (NBNZ), from AA- to A+. The Council's Treasury Management Policy at that time required that investment counterparties have a credit rating of at least AA-. As a consequence the Council was in breach of its policy from 17th June 2003 to 30 June 2003 (when the new Treasury Management Policy was adopted). On 30 June 2003, the Council reviewed the counterparty limits in the policy and after taking advice from its Treasury Advisor, reduced the policy limit from AA- to A.

On 30 June 2003 the Council adopted a new Treasury Management Policy as part of the Council's Long Term Council Community Plan. All measures and borrowing limits under the new policy have been complied with since 30 June.

7. Costs associated with solving the Rail situation

The updated schedule of external costs associated with the Council's attempts to resolve the rail situation (primarily the costs associated with the joint venture option which was "parked" in December 2002) is attached as **Attachment 3**.

8. Communications

The Council's Annual Report is essentially a compliance report, which is required by law. However, Council's continued good financial performance and prudent debt management should be communicated publicly. A suitable press release has been prepared.

9. Recommendations

That the Committee recommend to Council that it:

- (1) *Receive the report and note its contents.*
- (2) *Approve the following net amounts, in addition to those budgeted, be added to, or deducted from, the respective reserves:*

(a) <i>Transport Rate</i>	<i>\$1,496,000</i>
(b) <i>Bovine Tb Rate</i>	<i>\$6,000</i>
(c) <i>Wairarapa Schemes – Catchment Awhea</i>	<i>\$6,000</i>
(d) <i>Wairarapa Schemes – Catchment Homewood</i>	<i>(\$2,000)</i>
(e) <i>Wairarapa Schemes – Catchment Mataikona</i>	<i>3,000</i>
(f) <i>Wairarapa Schemes – Catchment Maungaraki</i>	<i>\$2,000</i>
(g) <i>Wairarapa Schemes – Drainage</i>	<i>(\$23,000)</i>
(h) <i>Wairarapa Shingle Royalty</i>	<i>\$36,000</i>
(i) <i>Wairarapa workshop</i>	<i>\$2,000</i>
(j) <i>Akura Nursery</i>	<i>\$3,000</i>
(k) <i>Wairarapa Schemes – River LWV</i>	<i>(\$190,000)</i>
(l) <i>Wairarapa Schemes – River Waiohine</i>	<i>(\$6,000)</i>
(m) <i>Wairarapa Schemes – River Upper Ruamahanga</i>	<i>\$10,000</i>
(n) <i>Wairarapa Schemes – River Waipoua</i>	<i>(\$4,000)</i>
(o) <i>Wairarapa Schemes – River Waingawa</i>	<i>(\$14,000)</i>
(p) <i>Wairarapa Schemes – River Lower Tauera</i>	<i>\$4,000</i>
(q) <i>Wairarapa Schemes – River Lower Whangaehu</i>	<i>\$1,000</i>
(r) <i>River Rate – Hutt City</i>	<i>\$91,000</i>
(s) <i>River Rate – Kapiti Coast District</i>	<i>(\$19,000)</i>
(t) <i>River Rate – Porirua City</i>	<i>(\$13,000)</i>

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|------|--|-------------------|
| (u) | <i>River Rate – Upper Hutt City</i> | <i>\$14,000</i> |
| (v) | <i>River Rate – Wellington City</i> | <i>(\$6,000)</i> |
| (w) | <i>Expense Rebudget – IT Capex</i> | <i>(\$9,000)</i> |
| (x) | <i>Expense Rebudget – Coastal Landscape</i> | <i>(\$12,000)</i> |
| (y) | <i>Expense Carry Forward – Lab TOC Analyser</i> | <i>(\$60,000)</i> |
| (z) | <i>Expense Carry Forward – Planning Vehicle</i> | <i>(\$22,000)</i> |
| (aa) | <i>Expense Carry Forward – Moving/Storage Costs</i> | <i>(\$60,000)</i> |
| (ab) | <i>Expense Rebudget – Land Swap HCC</i> | <i>\$55,000</i> |
| (ac) | <i>Expense Rebudget – Bovine Tb contract</i> | <i>\$6,000</i> |
| (ad) | <i>Expense Rebudget – East Harbour</i> | <i>\$12,000</i> |
| (ae) | <i>Expense Rebudget – Parks Mgmt Plans</i> | <i>\$20,000</i> |
| (af) | <i>Expense Rebudget – RPS/Care Groups (Policy)</i> | <i>\$8,000</i> |
| (ag) | <i>Expense Rebudget – Stormwater Investigation</i> | <i>\$35,000</i> |
| (ah) | <i>Expense Rebudget – Catchment Mgmt</i> | <i>\$85,000</i> |
| (ai) | <i>Expense Rebudget – Pedestrian Strategy</i> | <i>\$13,000</i> |
| (aj) | <i>Expense Rebudget – Petone Station Upgrade</i> | <i>\$160,000</i> |
| (ak) | <i>Expense Rebudget – QE2 National Trust</i> | <i>\$92,000</i> |
| (al) | <i>Expense Rebudget – IT Ops Hardware</i> | <i>\$215,000</i> |
| (am) | <i>Expense Rebudget – Finance Mgr Vehicle</i> | <i>\$14,000</i> |
| (an) | <i>Expense Rebudget – Ecobus</i> | <i>\$32,000</i> |
| (ao) | <i>Expense Rebudget – Office Reorganisation</i> | <i>\$150,000</i> |
| (ap) | <i>Expense Rebudget – RPS/Care Groups (Co-ordination)</i> | <i>\$13,000</i> |
| (3) | <i>Agree that the requirement for the forestry business units to pay a dividend be waived for the 2002/03 year.</i> | |
| (4) | <i>Agree that in line with Council policy, the remaining surplus after reserve transfers and working capital requirements, be applied to debt reduction.</i> | |
| (5) | <i>Adopt the Financial Statements and accompanying notes for the year ended 30 June 2003, subject to receipt of the Audit Report, and agree that any minor adjustments requested by Audit New Zealand be</i> | |

considered by officers and, if necessary, amended, pursuant to resolution (6) below.

- (6) *Agree that the 2003 Annual Report be published subject to any minor editorial amendments approved by the Chief Financial Officer, in conjunction with the Chairperson.*

Report prepared by:

Report approved by:

Paul Laplanche
Manager, Finance

Greg Schollum
Chief Financial Officer

Attachment 1: Department Reserve Analysis

Attachment 2: Compliance with Treasury Management Policy

Attachment 3: Rail external costs to 30 June 2003

2003 Draft Annual Report is enclosed as a separate attachment to this report