

Part Three – Significant forecasting assumptions and risks

Significant forecasting assumptions and risks

Schedule 10 (section 11) of the Local Government Act 2002 contains provisions relating to 'significant forecasting assumptions'. The Act requires that Council identify the significant forecasting assumptions and risks underlying the financial estimates. Where there is a high level of uncertainty, Council is required to state the reason for that level of uncertainty and provide an estimate of the potential effects on the financial assumptions.

The Council has made a number of assumptions in preparing this LTCCP. These assumptions are necessary as the planning term for the LTCCP is 10 years and the assumptions ensure that all estimates and forecasts are made on the same basis.

Forecasting assumptions	Risk	Likelihood of occurrence	Financial materiality	Reasons and financial effect of uncertainty
Population growth – The population of the District will decline during the period of the plan.	That population growth is higher than projected, putting increased pressure on Council to provide additional infrastructure and services.	Low	Low	Population projections are based on demographic assumptions that do not change quickly. Existing infrastructure and service levels are not likely to require increased investment if population is static or has a small increase.
Inflation - The financial information is based on costs and income adjusted for inflation. Council has used the BERL forecasts of price level changes to calculate costs and income for years 2 to 10 of the plan. The average projected increases are 9.0% for 2010, 2.9% for 2011 and 2.7% for 2012. Council has applied one-off cost savings for 2009-10, and a double BERL adjustment for cost inflators for the year 2010-11.	That actual inflation will be significantly different from the assumed inflation.	Low Years (1-3) Medium Years (4-10)	Low Years (1-3) Medium Years (4-10)	Inflation is affected by external economic factors. Council's costs and the income required to fund those costs will increase by the rate of inflation unless efficiency gains can be made.
Interest – Interest on term debt is calculated at 6.5% per annum. Interest on investments is calculated at 6.0%, and interest on call deposits at 5.0%.	That interest rates will change from those used in the calculations.	Medium	Medium	Interest rates on borrowed funds are largely influenced by factors external to the New Zealand economy.

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				Council is projecting a significant increase in debt to finance various projects including the Mahia Sewerage Scheme. Based on Council projected debt levels, interest cost will increase/decrease by up to \$100,000 per year for every 1% movement in interest rates.
Term Loans – Loans taken out by Council will have a maturity profile from 25 to 40 years, with principal repaid at the end of the term. Simple interest will be charged each year, and sinking funds will be set up for each loan to repay the principal at the expiration of the loan.	That Council will be unable to source loans for the length of term desired.	Medium	Medium	Council has projected debt levels based on the best estimate of the length of term required. If Loans cannot be sourced at the estimated terms projected, the costs will differ from those estimated in the Council financial statements..
New Zealand Transport Agency (NZTA) requirements and specifications for the performance of subsidised work will not alter to the extent that they impact adversely on operating costs. The NZTA subsidy Council has used in the LTCCP is 66% for all years of the plan.	Changes in subsidy rate and variation in criteria for inclusion in subsidised works programme.	Low	Medium	NZTA funding priorities may change as a result of the Land Transport Management Act 2003. Variations in subsidy are possible given the new Government priority given to Auckland roads. A 1% decrease in subsidy will increase Council's cost by approximately \$80,000.
Consent Renewals – Council bases its future projections on the expectation that consents will be renewed for its activities including Sewerage, Waste Management and Stormwater.	That approving bodies will fail to renew any of the consent renewals that council requires to carry out its activities.	Low	High	Council has no reason to believe that any of the consents that it operates under will not be renewed. Any failure to renew consents could significantly affect the ability of Council to provide an effective service, with a potentially high cost to Council.
Revaluation – These projections include a three-yearly estimate to reflect the change in asset valuations.	Infrastructure Assets are to be revalued for 2010-11, 2013-14 and 2016-17, which	High	Low	Variation in values expected to be 10% unless valuation methodology changes. Revaluations affect the carrying value of infrastructure assets and the depreciation charge in

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	may alter the depreciation expense.			the year. Financial effect of uncertainty unable to be quantified.
Funding sources – Sources of funds are as per the revenue and financing policy.	That some user charges may not be achievable.	Low	Low	Levels of charges have been set at previously achieved levels. Some user charges under budget will be likely to be offset by some user charges over budget.
Funding sources re Mahia Sewerage Treatment Scheme – The scheme will proceed with 50% subsidy from Ministry of Health with the remainder funded from loans.	That Ministry of Health will provide less than 50% subsidy towards the cost of the Mahia Sewerage Treatment Scheme.	Low	Low	Council has received verbal assurances that the level of subsidy will be 50%.
Rating Differentials – The current rating differentials will remain constant throughout the life of the plan, which includes district rating revaluations in 2009, 2012, 2015 and 2018 affecting rates in the following year.	That differentials will change as a result of the revaluations of property values in the district.	Moderate	Moderate	Property values could change significantly, and only in certain areas of the district. Differentials would need to change to equalise rates collection in different areas of the district.
Depreciation on planned asset acquisitions – Council has used depreciation rates for planned asset acquisition.	That more detailed analysis of planned capital works once complete may alter the depreciation expense.	Low	Low	Council has an asset management planning and upgrade programme in place. Asset capacity and condition is monitored, with replacement works being planned in accordance with standard asset management and professional practices. Depreciation is calculated in accordance with normal accounting and asset management practices.
Bank Funding – This plan is based on the continuity of funding from an approved banking institution.	That the bank does not continue to provide finance to fund Council activities.	Low	High	Council believes that the likelihood of the withdrawal of Bank funding is low, due to the good credit rating and relatively low risk Council has as a public entity. In addition, Council has the ability to set rates at a level sufficient to cover its costs.

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Asset Sales - This plan has included sale of assets as a source of finance in replacement of assets.	That Council will not achieve the level of funding from the sale of assets anticipated in the plan.	Moderate	Moderate	Council believes that it has made reasonable assumptions on the likely financial return from the sale of assets, but recognises that there is a reasonable degree of uncertainty in achieving these estimates.
Tawhara Reservoirs – Council has assumed that the Tawhara reservoirs will not need replacing in the next ten years.	That Council is required to replace the Tawhara Reservoirs within the 10 years of this plan.	Moderate	Moderate	Council believes that it has made reasonable assumptions on the likely continuity of the Tawhara Reservoirs, but recognises that there is uncertainty that could result in earlier replacement than anticipated.
Wastewater Treatment Plant Mahia – Council has consulted with the community to benefit from the scheme, and has assumed they will support the introduction of the Mahia wastewater scheme.	That the community will not support the Mahia Wastewater scheme.	High	High	If the proposed scheme at Mahia does not proceed, ratepayers would be responsible for management of their own wastewater. Council could not ensure that the natural environment would be protected, and all potential negative economic, environmental, social and cultural effects will be identified and properly managed. There would be a saving of capital expenditure of \$12 million, and the loss of subsidy from the Ministry of Health of \$4.5 million (excl. GST).
Regional Development Rooding – The programme of Rural Development roading will proceed as budgeted in the LTCCP	That the government will reduce the level of funding or delete the funding for the RDR programme	Low	Moderate	Council has received assurances that the program will proceed Council believes that the probability is high that the program will proceed

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External Funding - Council has assumed that it will continue to receive external funding at current levels from government agencies such as SPARC, Internal Affairs etc.	That the government agencies will reduce or eliminate funding for various programs	Low	Low	Council has received assurances that the programs will proceed Council believes that the probability is high that the program will proceed
Return on Investment – Council has based its projection of dividends from Quality Rooding and Services (Wairoa) Ltd on their Statement of Corporate Intent for 2009 & 2010.	That QRS will not achieve the level of tax-paid profit as estimated in the Statement of Corporate Intent, resulting in reduced dividend, and reduced overall income.	High	Moderate	QRS is in a relatively volatile and high risk business of contracting, and income will fluctuate from year to year. Council expects to receive a dividend of not less than \$125,000 in 2010 and 2011, and any reduction would have an effect on the rating requirement.
Useful Lives of Significant Assets – Council has estimated the useful lives of its significant assets as detailed in the Statement of Accounting Policies	Assets will not last as long as forecast and will need to be replaced before funds are available for replacement of these assets.	Low	Low	Council has an asset management planning and upgrade programme in place. Asset capacity and condition is monitored, with replacement works being planned in accordance with standard asset management and professional practices.
Currency movements and related asset values – It has been assumed that currency movements of exchange rates will not fluctuate significantly during the 10-year period.		High	Low	Council does not have exposure to currency movement risk in respect of significant assets or liabilities.
Approach to potential societal changes Council has prepared the 10-year plan on the basis of best estimates, with a relatively stable society, and little societal change.	That there is significant change in society that impacts Negatively on Council.	Moderate	Moderate	While change is likely, the implications cannot be quantified. In addition some outcomes may be positive for Council, such as the devolving of responsibility for activities passing from Council to Central Government.

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Climate Change Response (Emissions Trading) Amendment Act – In the absence of more detailed information, Council has applied a one-off increase in costs of 1.10% in 2010/11 in operational and renewal costs and a 1.10% increase in capital costs to the BERL inflation estimates.	The cost will be significantly different from those forecast in the BERL forecast.	Moderate	Moderate	Variations in the actual effect of emissions trading is likely, although not all the additional costs will be able to be recovered from user charges.

Other information

Consultation – There will be increasing levels of community consultation required as a result of the provisions of the Local Government Act 2002.	Increased resources required to meet legal requirements. Increased community expectations regarding consultation and engagement.	Medium	Low	Increased legislative requirements around the need for consultation are occurring and more such legislation is being considered.
Levels of service – Changes in customer expectations regarding levels of service will not significantly change so that they impact on asset requirements or operating costs unless otherwise stated in the text.	There are significant changes in customer expectations regarding levels of service.	Low	Medium	Most communities have already defined the levels of service they expect, and what they are prepared to pay for that level of service. While customer expectations may change, the practicality of meeting these changes through amendments to contracts and level of service agreements would be a long term process.

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<p>Council policy - There will be no significant changes to Council policy as summarised in this plan.</p>	<p>New legislation is enacted that requires a significant policy response from Council.</p> <p>Election of a new Council with different objectives to the current Council.</p>	Medium	Low	<p>Changes to Council policy to deal with new legislative and Council requirements are part of normal business.</p> <p>Any significant change to Council policy would be assessed in terms of impact upon Council's financial position. The Local Government Act 2002 would ensure that changes in policy have to follow due process.</p>
<p>Governance – The structure of the elected representation on Council will not change from that adopted for the 2007 elections.</p>	<p>There will be applications made to Council for representation reviews.</p>	High	Low	<p>Council is required to review the number of elected members by November 2009.</p>
<p>Natural disasters – There will be no natural disaster requiring emergency work that cannot be funded out of the budgetary provisions.</p>	<p>That there will be natural disaster event(s) requiring emergency work that cannot be funded out of normal budgetary provisions.</p>	Medium	High	<p>Although Council has faced natural disaster events in the past, and coped adequately, climate change predictions are that some events could become more frequent and more intense. The potential effect of a natural disaster on Council's financial position is dependent upon the scale, duration and location of the event. Central government assistance and insurance contracts would reduce some of the Council financial risk.</p>
<p>Replacement assets – The replacement of existing assets does not mean an increased level of service, unless otherwise stated in the text.</p>	<p>That the replacement of existing assets increases the level of service due to technological changes or through adoption of best practice.</p>	Low	Low	<p>In most cases increased levels of service are associated with construction of new assets. Council asset managers have already adopted known best practice techniques.</p>

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<p>New assets – The construction of new assets increases level of service and/or capacity, unless otherwise stated in the text.</p>	<p>That the construction of new assets does not meet the agreed level of service and/or does not provide adequate capacity.</p>	<p>Low</p>	<p>Low</p>	<p>For most new assets there are relatively long project planning and design phases. Wherever possible asset managers design and construct new assets with future levels of service and capacity in mind.</p>
<p>Contracts – There will be no significant variations in terms of price from the re-tendering of operation and maintenance contracts and renewal of service level agreements, other than those variations recognised in this plan.</p>	<p>There is a significant variation in price from re-tendering contracts and renewal of service level agreements.</p>	<p>Low (Years 1-3) Medium (Years 4-10)</p>	<p>Low Medium</p>	<p>Council has been able to manage contracts within a narrow range of cost variations. If contract prices were to increase significantly then Council would review the amount of work programmed and undertaken. Adjustment for known and projected increases in contracts have been included.</p>
<p>Renewal and capital work – Programmes are completed on time and on budget</p>	<p>Delays in completion of a major capital project may delay completion of other projects due to extra pressure on staff and on council funding.</p>	<p>Low</p>	<p>Medium</p>	<p>Council regularly manages capital projects that are carried forward from previous accounting periods. Projects with lower priority and that are less time sensitive would be delayed.</p>
<p>External factors – There will be no unexpected changes to legislation or other external factors that alter the nature of services provided by Council.</p>	<p>There are unexpected changes that alter the services provided by Council.</p>	<p>Medium</p>	<p>Low</p>	<p>Most changes to legislation are programmed and known about in advance. Only in extraordinary circumstances (such as public outcry over a particular incident) would unexpected changes to legislation be promoted. Central government is likely to share part of any cost associated with major legislative changes.</p>

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<p>Capital works costs – On average, costs of major capital works will not vary significantly from costs estimated at the concept stage and adjusted for inflation.</p>	<p>That some project costs turn out greater than estimates, resulting in increased debt levels.</p>	<p>Medium Years (1-3)</p> <p>High Years (4-10)</p>	<p>Medium</p> <p>Medium</p>	<p>Council has a higher level of confidence regarding the costs of capital projects in the short term but less certainty in the longer term due to possible fluctuations in the economy, growth patterns, consent conditions etc. Council is proposing to build a Sewerage System for Mahia estimated to cost \$12 million.</p> <p>The potential effects of the uncertainty on the financial statements would be difficult to estimate.</p>
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