

ENVIRONMENT COMMITTEE REPORT

Agenda Item 5.3

6 February 2007

SUSTAINABLE MELBOURNE FUND – PERFORMANCE RESULTS TO 30 JUNE 2006

Division Sustainability

Presenter Geoff Lawler, Director Sustainability & Innovation

Purpose

1. To present the performance results and progress for the twelve months ended 30 June 2006 of the Sustainable Melbourne Fund (“SMF”).

Recommendation from Management

2. That the Environment Committee accept the financial statements for 2005/06 of the Sustainable Melbourne Fund.

Key Issues

3. On 13 December 2005 Council passed the following resolution:

“That Council, subject to obtaining the necessary approval from the Minister for Local Government and the Treasurer in accordance with section 193 of the Local Government Act 1989, amend the project charter of the Sustainability Melbourne Fund to reflect:

- *the reduction in the required Return on Investment of the Sustainable Melbourne Fund from 4.5% over the first ten years of the Fund, to preserving the \$5 million capital base of the Fund;*
- *extending the Term of Investment from 3 years to 6 years; and*
- *introducing a formal Council review process with the Trustees, once every five years.”*

4. On 11 August 2006 the section 193 approval was granted subject to the following conditions:

- *that Melbourne City Council will set a hurdle rate of return for the Fund on at least a triennial basis but that it should be no less than the rate of inflation;*
- *that Melbourne City Council will set a maximum investment term that is not more than 6 years but which can be reviewed up to that limit at any time by Melbourne City Council; and*
- *that Melbourne will undertake a review of the Fund with the Fund Trustees at least once every 3 years.*

5. The net effect of the Council's resolution and the Minister's approval is that the Fund's current operating parameters are:
 - 5.1. the hurdle rate of return for the Fund must not be set below the rate of inflation and Council will have to set a hurdle rate before August 2009;
 - 5.2. the maximum term of investment is 6 years; and
 - 5.3. Council and the Trustees will have to undertake a formal review of the Fund before August 2009.
6. Because this report is covering financial performance prior to the Minister's approval, the following financial assessments are made against the previous targeted rate of return of 4.5%.

Relation to Council Policy

7. The SMF is an initiative of Melbourne City Council.

Finance

8. The SMF has earned income of \$0.323 million in the 2005/06 financial year. Based on an average balance of \$5.603 million during the financial year, this represents a gross annual return of 5.76%. The Fund's investment yield compares favourably to the average Reserve Bank of Australia (RBA) cash rate for the year of 5.5% and the Fund's previous target growth rate of 4.5%. However, the Fund's return of 3.74% net of fees is below the previous targeted growth rate. It is anticipated as projects are identified the targeted net return is expected to increase.
9. The Finances of the SMF have been audited by the Auditor General and have received an unqualified audit report.

Overall Performance

Performance Results for the twelve months to 30 June 2006

10. The following table reflects the key performance results for the twelve months to 30 June 2006:

PROFIT & LOSS	2006	2005
INCOME		
Interest on Investment	\$288,976	\$286,584
Project Income	33,936	19,744
Total Income	\$322,912	\$306,328
EXPENDITURE		
Management Fees	\$102,500	\$ 97,375
Administrative Costs	900	1,703
Accounting Fees	6,150	6,150
Bank Charges	76	166
Audit Fees	3,690	4,100
Advertising		500
Total Expenditure	\$113,316	\$109,993
Surplus	\$209,596	\$196,335

11. The higher surplus during 2005/06 was mainly attributable to an increase in project income with a smaller increase in interest income.

Balance Sheet

12. The following table reflects the balance sheet as at 30 June 2006:

BALANCE SHEET	2006	2005
ASSETS		
Cash at Bank	\$476,978	\$27,935
Cash Investments	5,079,726	4,935,767
Receivables – Current	137,364	473,609
Receivables – Non Current		74,846
TOTAL ASSETS	\$5,694,068	\$5,512,157
LIABILITIES		
Payables	\$6,886	\$6,160
Deferred Income	8,340	36,751
Distributions Held in Trust	678,742	469,146
TOTAL LIABILITIES	\$693,968	\$512,057
NET ASSETS	\$5,000,100	\$5,000,100

13. Total assets including cash at bank, cash investments and receivables totalled \$5.694 million, an increase of \$0.182 million from the previous year.
14. Cash investment funds represent 89% of the total assets and were invested in the short-term retail fixed money markets. The available funds were invested through Negotiable Certificates of Deposit (“NCD’s”) with approved deposit taking institutions.
15. The SMF has liabilities of \$0.693 million as at 30 June 2006, with \$0.678 million attributable to distributions held in trust. The Trust Deed requires that the net income of the fund for each financial year be classified as distributions held in trust.

Legal

16. The Sustainable Melbourne Fund was established under an approval pursuant to section 193 of the *Local Government Act 1989* which imposed various conditions on the Council, including a requirement that Council seek consent for any amendments to the Trust Deed from the Minister for Local Government and the Treasurer. In order to give effect to Council’s resolution of 13 December 2005 and in accordance with the conditional approval of 11 August 2006 of the Treasurer and Minister for Local Government, the Trust Deed was amended by way of a Supplemental Deed dated 2 January 2007 and executed on behalf of Council and the Trustees.

Sustainability

17. The charter of the SMF requires it to consider social benefits associated with the investments it makes in environmental projects. The SMF is required to be self-sustaining and meet Council’s financial performance targets. As such it is a model for investment in the environmental management sector and will facilitate new business development in that sector.

18. The charter of the SMF allows it to invest in projects that will deliver environmental benefits in biodiversity, water consumption and quality, renewable energy and energy efficiency, clean and efficient transport and waste minimisation. The focus of the Fund has been on water and energy efficiency projects. Through the water efficiency project investments made in 26 buildings, the estimated annual water savings that have been achieved equate to 134,000 kilolitres per year. This represents an average saving of between 12-15% of water use.

Investment Strategy, Projects and Achievements

19. The Sustainable Melbourne Fund's investment strategy is to continue to invest in water and energy efficiency projects where a "payment by savings" investment proposition can be made. The payment by savings is a unique proposition to building owners with the benefits being; no upfront payment, repayments made in lieu of energy and water savings and a permanent cost savings once the funds are repaid.
20. The Fund has built up considerable expertise in the "packaging" of turn-key solutions for water and energy efficiency which includes audit, implementation and financing. Importantly the water and energy efficiency solutions that the Fund has developed has also involved applying our expertise in the formation of partnerships, development of a marketing and sales plan, establishment of commercial contracts, negotiation and project delivery.
21. In 2006, the Fund established a new energy efficiency service with Investa Property Group. Investa are the largest listed owner of office property in Australia and we have teamed up with them to offer the Investa Greenhouse Guarantee, which is a turn-key energy efficiency financing package to help tenants address climate change by implementing state of the art energy efficiency improvements. The first successful project has was signed in September 2006 with JHD Urbis to undertake \$60,000 worth of energy efficiency work which will deliver a reduction in Greenhouse of 115 tonnes. The Fund expects to sign a number of new energy efficiency contracts in 2006/07.
22. The Fund continues to finance the Savewater Efficiency service in partnership with South East Water and Yarra Valley Water. In the CBD the Fund will finance water efficiency projects directly with building owners. Several new contracts are under negotiation.
23. The Fund is also working strategically with the City of Melbourne's Building Improvement Partnership initiative as a key partner and principal financier of the CBD building retrofit program.
24. As a result of the changes in the Project Charter the Fund is also looking at investing in sustainability projects that demonstrate application of new clean technologies, enhance alliances with other private sector parties and projects that need the Fund's finances to help overcome financial barriers to implementation. The Fund has budgeted to invest \$1.5 million in the 2006/07 financial year across all project areas.
25. The Fund has made considerable efforts to form alliances with other organisations that are also committed to investing in sustainability projects. This has culminated in the Fund being a signatory to the Victorian Sustainability Accord. Other organisations invited to be part of the Accord include; the City of Melbourne, Sustainability Victoria, VECCI and the EPA. The Fund Chairman Peter Buzzard, signed the Accord along with Lord Mayor, John So, and the Premier, Steve Bracks, on 21 September 2006 at Raheen.

26. The Fund has been actively promoting its successes with Fund Manager, Peter Castellás, being invited to present at a number of conferences including the Melbourne Forum Green Buildings event and the National Business and Sustainability Summit. The Fund has also developed new marketing collateral and has an updated website. The Fund is currently developing, in conjunction with the City of Melbourne, a comprehensive corporate communications plan that will be better aligned with the City of Melbourne's marketing and communications.

Background

27. Council established the Fund on 17 April 2002 to support Council's environmental objectives through strategic investment in external entities. Independent Trustees, initially appointed by Council, administer the Fund. Investments from the Fund must deliver environmental benefits related to biodiversity, water consumption and quality, renewable energy and energy efficiency, clean and efficient transport or waste minimisation.
 28. The Council provided \$5 million to establish the Fund, which is expected to be financially self-sustaining (including administration costs) and deliver a return of at least 4.5% over the first 10 years. The Council is the sole beneficiary and unit holder of the Fund. Council may wind-up the fund on 3 months notice.
 29. Seven Trustees were appointed to the Fund in April 2002. A further Trustee was appointed in 2004. Under the terms of its Charter, the Trustees are given fairly wide discretion in the types of investment but are limited by the financial and environmental objectives of the Fund and a number of internal prudential rules, designed to ensure that a portfolio approach is taken to managing financial risk.
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Attachment:

1. Auditor's Report

AUDITOR GENERAL
VICTORIA**INDEPENDENT AUDIT REPORT****Sustainable Melbourne Trust Fund****To the Members of the Parliament of Victoria and the Trustees of the Fund****Scope***The Financial Report*

The accompanying financial report for the year ended 30 June 2006 of Sustainable Melbourne Trust Fund consists of the income statement, balance sheet, statement of changes in equity, cash flow statement, notes to and forming part of the financial report, and the trustees declaration.

Members' Responsibility

The Trustees of Sustainable Melbourne Trust Fund are responsible for:

- the preparation and presentation of the financial report and the information it contains, including accounting policies and accounting estimates
- the maintenance of adequate accounting records and internal controls that are designed to record its transactions and affairs, and prevent and detect fraud and errors.

Audit Approach

As required by the *Audit Act 1994*, an independent audit has been carried out in order to express an opinion on the financial report. The audit has been conducted in accordance with Australian Auditing Standards to provide reasonable assurance as to whether the financial report is free of material misstatement.

The audit procedures included:

- examining information on a test basis to provide evidence supporting the amounts and disclosures in the financial report
- assessing the appropriateness of the accounting policies and disclosures used, and the reasonableness of significant accounting estimates made by the members
- obtaining written confirmation regarding the material representations made in conjunction with the audit
- reviewing the overall presentation of information in the financial report.

These procedures have been undertaken to form an opinion as to whether the financial report is presented in all material respects fairly in accordance with Accounting Standards and other mandatory professional reporting requirements in Australia, and the financial reporting requirements of the *Financial Management Act 1994*, so as to present a view which is consistent with my understanding of the Fund's financial position, and its financial performance and cash flows.

The audit opinion expressed in this report has been formed on the above basis.



AUDITOR GENERAL
VICTORIA

Independent Audit Report (continued)

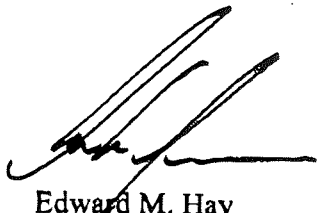
Independence

The Auditor-General's independence is established by the *Constitution Act 1975*. The Auditor-General is not subject to direction by any person about the way in which his powers and responsibilities are to be exercised. The Auditor-General and his staff and delegates comply with all applicable independence requirements of the Australian accounting profession.

Audit Opinion

In my opinion, the financial report presents fairly in accordance with applicable Accounting Standards and other mandatory professional reporting requirements in Australia, and the financial reporting requirements of the *Financial Management Act 1994*, the financial position of Sustainable Melbourne Trust Fund as at 30 June 2006 and its financial performance and cash flows for the year then ended.

MELBOURNE
29 September 2006



Edward M. Hay
Acting Auditor-General

FINANCE ATTACHMENT

**SUSTAINABLE MELBOURNE FUND – PERFORMANCE RESULTS TO 30 JUNE
2006**

The financial implications and impacts have been identified throughout the body of the report.

Joe Groher
Manager Financial Services

LEGAL ATTACHMENT

**SUSTAINABLE MELBOURNE FUND – PERFORMANCE RESULTS TO 30 JUNE
2006**

The Sustainable Melbourne Fund was established under an approval pursuant to section 193 of the *Local Government Act 1989* which imposed various conditions on the Council, including a requirement that Council seek consent for any amendments to the Trust Deed from the Minister for Local Government and the Treasurer. In order to give effect to Council's resolution of 13 December 2005 and in accordance with the conditional approval of 11 August 2006 of the Treasurer and Minister for Local Government, the Trust Deed was amended by way of a Supplemental Deed dated 2 January 2007 and executed on behalf of Council and the Trustees.

Ongoing legal advice will be provided as required by virtue of Council being the sole holder of units in the Fund.

Kim Wood
Manager Legal Services