

## **INQUIRY INTO LOCAL GOVERNMENT IN NEW SOUTH WALES**

**Organisation:** Muswellbrook Shire Council

**Date received:** 3/07/2015

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**The Hon Paul Green MLC  
Chair  
General Purpose Standing Committee No.6  
NSW Legislative Council  
Macquarie Street  
SYDNEY NSW 2000**

By email: [gpscno6@parliament.nsw.gov.au](mailto:gpscno6@parliament.nsw.gov.au)

Dear Mr Green,

**RE: Inquiry into Local government in New South Wales**

I refer to the reference provided by the NSW Legislative Council to the General Purpose Standing Committee No. 6 to inquire into Local Government in New South Wales. Muswellbrook Shire Council ("Council") has resolved to make a submission to the Committee's Inquiry.

Background

1. On 10 September 2014 the Minister for Local Government, the Hon Paul Toole MP, announced the NSW Government's response to the Independent Local Government Review Panel's recommendations into local government reform. The Government's response included the announcement of the *Fit for the Future* (FFTF) scheme.
2. Councils across NSW were directed by Circular 14-23 to prepare submissions in response to the Government's FFTF scheme.
3. Council was identified by the Independent Local Government Review Panel (ILGRP) as sustainable in its own right and it was not identified as a potential merger partner. The ILGRP's preference was for Council to be a standalone council within a Joint Organisation (Hunter Councils).
4. Council is a Group 11 council and was classified as a 'Rural Council' for the purposes of FFTF by IPART.
5. Council prepared a 'Council Improvement Plan' as part of its Template 2 submission, which was endorsed by Council at an Extra Ordinary meeting on 25 June 2015.
6. Council will meet each of the benchmarks in full by 2017/18.

### The Fit for the Future process

7. At the time of the announcement of the FFTF scheme, the criteria and process against which councils would be assessed had not been finalised in any detail and only broad based information was made available, including the broad generic performance benchmarks. This created uncertainty in the sector and resulted in councils commencing the process to prepare submissions without full knowledge of the scheme's requirements.
8. Notwithstanding that the Government had almost ten months between announcing the FFTF scheme and the deadline for submissions, IPART was not appointed as the assessment panel until late April and did not finalise the methodology against which proposals would be assessed until 5 June – 25 days before the close of submissions.
9. Council is uncritical of the role played by IPART and notes the unreasonable timeframes placed on it by the Government.
10. It is noted that in the absence of the detailed assessment process, it was very difficult to properly prepare a document that would effectively address the assessment criteria. This placed councils across the State in the unfair position of having to second guess the expectations of the Government.
11. In October 2014, Council commenced work on the preparation of its Template 2 submission and 'Council Improvement Plan' without a full understanding of how the proposal would be assessed. This represented an opportunity cost for Council which in time yielded little benefit. As the deadline for submissions drew closer, and without access to the assessment methodology, Council was compelled to engage a consultant to undertake much of the work, particularly with respect to financial modelling.
12. Given the complexity of proposals prepared defensively by those councils identified for possible merger, the late confirmation of the methodology would have placed those councils at an even greater disadvantage than that experienced by Council.
13. At no time was an indication provided by the Government or its agencies as to what the consequences may be for a council that is not deemed by IPART to be 'fit'. Indeed at a seminar organised by the OLG for councils in November, it was conceded by a senior official that the government had not contemplated a council not being deemed fit, and as a result the OLG could not speculate on the likely outcome for any such council.

### The Benchmarks

14. FFTF relied upon a series of benchmarks to assess the performance of councils in financial sustainability; infrastructure and services; and efficiency.
15. The requirement of the FFTF scheme for the measurement of all councils against the performance benchmarks strikes at the heart of the flaw of the scheme, as it was unreasonable and impossible to properly compare all councils against these measures. It is noted that IPART lessened the burden of performance for 'Rural Councils' towards the end of the process but the point is valid in any case: it is simply not possible using a simplistic benchmarking exercise to properly compare council performance with any level of confidence or fidelity.



### Asset Maintenance Ratio

16. The suggestion that road maintenance should represent a percentage of asset value for roads is in Council's view unrealistic. Whilst it may be true for some asset types, it is expected that the scatter of data for roads maintenance would be very wide and any comparisons effectively meaningless.

The degree of road maintenance required in a local area will vary with a number of factors, including:

- the asset condition;
- traffic loadings and volumes;
- terrain, geology;
- quality and availability of materials and technologies;
- environmental factors, including rainfall; storms, seasonal variations; heat, snow, ice, dust;
- network layout and access to plant, labour and material, etc;
- level of service decisions; and
- organisation capability, scale and efficiency

As such, an appropriate maintenance percentage could only be developed after taking factors such as these into account.

17. Council submits that figures developed locally, taking into account the impact that the above factors have on local conditions, should take precedence over industry figures in circumstances where the Council can demonstrate an appropriate methodology carried out by appropriately qualified staff. Any Council that demonstrates the existence of an appropriate methodology to its auditor and, if necessary TCorp and the OLG should have been able to provide the resultant figures as indications of their financial sustainability.

### Infrastructure Renewals Ratio

18. TCorp provided a weighting of 7.5% to this ratio. Council submits that this ratio is more important than TCorp's weighting implies, after all the ability to replace and renew infrastructure should be the foremost measure of a Council's sustainability.
19. However, the ratio was based on an annualised depreciation figure which is not the preferred methodology in the long-term. The asset replacement required should be considered in light of the replacement and renewal of long-lived assets that by nature have 'lumps' and also 'periodic peaks and troughs' in renewal expenditure requirements. The ratio is therefore only a good measure for short-lived assets, such as plant or networks of many assets that each have short lives (for example, road sealed surfaces) and this difference should have been recognised.
20. The high degree of variability between councils reported levels of service, asset lives, and valuations makes it impossible to make any conclusions regarding relative performance of councils using this ratio.
21. As Asset Management Maturity improves, the more preferred measure will be asset renewal expenditure levels relative to asset management plan identified renewal needs. Such figures need to be developed at a local level, taking into account the variable factors that are outlined above. A stronger tie between Asset Management Plans (AMPs) and budgets is required, together with a template for more consistent and comparable AMPs.

22. If this cannot be achieved presently across the State due to the lack of adequate AMPs, then the default could have been the current ratio. However, for those councils with a demonstrated level of reliability in their AMP, the denominator should have been based on data from the AMP.

#### Infrastructure Backlog Ratio

23. In 2014, Council based its estimation of the cost to Bring to Satisfactory (BTS) as being equal to the replacement cost for the assets given a condition rating of Five (5) – that is requiring urgent renewal and replacement. This was based upon in part, condition data, age based analysis, and other assumptions.
24. It has been suggested that the cost to bring to satisfactory is equal to the backlog or unfunded renewals. It is important that the backlog be calculated based upon the level of renewal and replacement desired by Council but unable to be funded and not include works that Council has made a deliberate decision not to undertake.

Council supports the following Jeff Roorda Associates<sup>1</sup> suggested definition:

Cost to bring to assets to satisfactory (BTS) should be determined by asset and risk management plans... [T]he cost to bring to satisfactory should be the total unfunded cost to renew all high residual risk assets in the current risk register.

25. Council further submits that the BTS analysis must be carried out for each material asset component. Network averages should not be used to determine BTS.
26. If service levels are declining in accordance with an adopted agreed and communicated asset management strategy, this is not backlog, nor a financial sustainability risk, provided these risks are managed and communicated.
27. Council is also required to report the percentage of assets in each condition rating group, which seems to have an expected relationship with 'cost to bring to satisfactory'. This is not explained in the Financial Statement Special Schedule 7 notes. They are problematic to calculate in some cases, particularly with complex assets. In addition, guidance is not provided by the OLG as to whether the percentage of assets in each condition should be determined based on their replacement costs or their measureable physical attributes.

#### Efficiency (Real Operating Expenditure) Ratio

28. The efficiency benchmark was highly flawed. To measure performance by way of operational expenditure over population took no account of a council's unique characteristics. Rural councils for instance allocate large sums on operational roads maintenance and yet often have small population bases. To compare the capacity of a small metropolitan council with a large population and relatively small operational expenditure is illogical.

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<sup>1</sup> Jeff Roorda and Associates submission to the NSW Independent Pricing and Regulatory Tribunal: *Methodology for Assessment of Council Fit for the Future Proposals*, 2015.



30. This measure appeared pitched to ensuring that Councils will no longer provide new services without removing services that they have previously offered. By only measuring the expense per capita, the ratio does not take into consideration sources of revenue that might be inherent in operating the new service. Under the current calculation, a new or expanded service that operated on a cost recovery or even profitable basis would perversely have a worsening impact on this ratio despite having a neutral or even positive impact on a Council's financial situation.

Council appreciates the opportunity to comment. If you require further information, please contact \_\_\_\_\_

Yours faithfully,

Steve McDonald  
**General Manager**