Submission No 78

INQUIRY INTO LOCAL GOVERNMENT IN NEW SOUTH WALES

Organisation: Shoalhaven City Council

Date received: 6/07/2015

Council Reference: 44629E (D15/186168)
Your Reference:

The Hon. Paul Green MLC
Chair Upper House Inquiry into Local Government
Parliament House
Macquarie Street
SYDNEY NSW 2000

Dear Hon. Paul Green MLC,

RE: Fit for the Future – Standing Committee Inquiry

Firstly, I congratulate you on your initiative to commence this inquiry and either I or another council representative would be willing to appear in person at any public hearing if this is required.

Please find comments below regarding Shoalhaven City Council's response to the Upper House inquiry into the Fit for the Future Reforms OF Local Government in NSW.

"(a) the NSW Government's 'Fit for the Future' reform agenda"

Comment:

The underlying 'agenda' is clearly the financial sustainability of the local government industry and the necessity to have sufficient funds to properly maintain Council assets and provide the facilities and services the community require.

Over many years the evidence of 'cost shifting' from Federal and State Government to local government has been documented and quantified. There has been minimal action to address this issue - is it reasonable for ratepayers to continue to bear these costs?

The untied Financial Assistance Grants (Federal Government) have been frozen for three years and this has the long term impact of permanently reducing funding to local government. This has an impact of about $700,000 less funding to Shoalhaven City in 2015/16 and of course the cumulative longer term impact is very significant and impacts on council's ability to invest funds into infrastructure.

The backlog works and costs to bring local government assets back to a satisfactory condition, is well documented and quantified.

All three of the above factors indicate that Councils will become more reliant on their own source revenues (rates, fees and charges) to meet future financial commitments. However does the community really understand this and do they have the capacity to pay more?

The reform agenda however appears to solely relate to financial matters and does not directly consider human values, as well as social and environmental factors.

"(b) the financial sustainability of the local government sector in New South Wales, including the measures used to benchmark local government as against the measures used to benchmark State and Federal Government in Australia."

Comment:

There are various sets of benchmarks for NSW Councils:

- Office of Local Government - Comparative Information Report (annual)
- Department of Planning - Local Development Performance Monitoring Report (annual)
- TCorp - "*Financial Sustainability of NSW Local Government Sector*" April 2013

The TCorp report rated Shoalhaven City Council's financial position as 'sound' with a 'negative' outlook. There were 32 councils rated 'sound' with 18 having 'negative' outlook.

It would certainly be helpful to have similar benchmarks for the NSW and Commonwealth Governments for comparative purposes, especially in relation to Asset Renewal & Infrastructure backlog, and the Inquiry must be in a position to publish that detail.

"(c) the performance criteria and associated benchmark values used to assess local authorities in New South Wales."

Comment:

The Operating Performance Ratio is requiring councils to raise sufficient operating revenue to not only meet the costs of operations but also the non-cash depreciation expense. Many councils in NSW do not achieve this benchmark at the current time, and anecdotal evidence suggests that this particular benchmark is putting upward pressure on many councils to factor in Special Rate Variation increases in the out years in their FFF application. There is also evidence showing that many councils have already applied SRVs in recent years to increase expenditure on infrastructure needs. The Inquiry should examine this particular outcome (i.e. SRVs) arising from the FFF benchmarks over the last two or three years AND into the future.

Council has also made representations to IPART concerning the 7 benchmarks used to assess NSW Councils. These comments are as follows:

A number of the performance measures appear to work against each other.

The KPIs around asset maintenance, renewal and backlog require Council to be spending substantially more than it currently does to see an improvement in these areas and to move towards the actual benchmark requirements.

The efficiency ratio however requires Council to be spending less per capita on its operations (i.e. the less you spend per capita in your operational budget then according to the State Government you are more FFTF).

The efficiency KPI (i.e. measuring a decrease in real operating expenditure per capita over time) in some respects is a clumsy and superficial measure and does not take into account the many variable factors including how progressive the council has already been in reducing operating costs through service reviews & market testing.

Shoalhaven City Council has shown it was already on the path to financial sustainability as part of its Transformation Program which it embarked upon late in 2012. This has involved an organisational restructure (savings of $2.5M) and a rolling program of service reviews and continuous improvement initiatives including a productivity 'dividend' driven by holding most operational expenditure (not including infrastructure maintenance) which has achieved $3M worth of savings to date.

The more you spend on Asset maintenance to achieve that benchmark your result for the Efficiency KPI gets worse unless it is intended that council discounts these increased operational expenditures from the calculations.. The only way to achieve both is to spend more on asset maintenance AND be more efficient and reduce other services/facilities.

There may be other Efficiency measures that could be considered that relate to the relationship between the services & facilities actually provided and average residential rates, or a ratio between Average household income & the services/facilities residents receive. The bottom line is it is considered that the Efficiency performance measure may be an unreliable benchmark.

"(d) the scale of local councils in New South Wales."

Comment:

The 2013 TCorp Report demonstrates that 'size' is not necessarily a good measure of financial sustainability. In its assessment it found small councils including Conargo, Lockhart and Temora were financially 'sound' while some larger councils were 'weak' (Coffs Harbour and Port Macquarie) and ‘very weak’ (Greater Taree). Similar differences were evident across Metropolitan councils.

The size and scale criteria need far greater analysis. Population density and the geographic area and spread need to be considered in determining the most effective boundaries. Geographic size seems a more valid issue rather than population alone in the metropolitan area.

“(e) the IPART role in reviewing the future of local government in New South Wales, assisted by a South Australian commercial consultant.”

Comment:

IPART have experience in assessing applications from councils for SRVs for several years and therefore have some understanding of the financial pressures and demands particularly to maintain infrastructure and address backlog works. It would seem reasonable that IPART could make assessments however as the benchmark criteria have already been determined, IPART’s role to critically examine whether the criteria is effective and appropriate in the first place is negated. Thus IPART’s role seems to be no more than an administrative exercise to assess FFF applications against the criteria determined by the State government.

IPART should be given more autonomy to refine or redefine appropriate benchmarks given the extensive industry feedback to IPART on the ‘Methodology’ Discussion Paper. This would also necessitate a deferral of the 30 June ‘Fit for the Future’ application date.

“(f) the appropriateness of the deadline for 'Fit for the Future' proposals.”

Comment:

Councils have been working on their ‘Fit for the Future’ financial strategies and applications for many months and then only recently were thrown into some uncertainty when IPART was appointed as the ‘independent assessor’. IPART then released its Discussion Paper on 27 April inviting submissions until 25 May on the proposed “*Methodology for Assessment of Council Fit for the Future Proposals - April 2015*”. This doesn’t present an issue provided there is not a significant change in the benchmarks that would adversely impact on councils’ endorsed financial strategies for the future. However as stated at (e) the benchmarks should be reviewed and the deadline deferred.

“(l) the role of co-operative models for local government including the 'Fit for the Futures' own Joint Organisations, Strategic Alliances, Regional Organisations of Councils, and other shared service models, such as the Common Service Model.”

Comment:

Council has been an active participant in the Southern Councils Group for many years and now in the IPJO. The model for regional cooperation is excellent and has potential to become an important entity in the overall ‘Fit for the Future’ reforms to contribute to individual council members’ longer term financial sustainability.

“(o) the impact of the 'Fit for the Future' benchmarks and the subsequent Independent Pricing and Regulatory Tribunal performance criteria on councils' current and future rate increases or levels.”

Comment:

For the past three years Shoalhaven City Council has been on a transformation journey to reduce operating costs, investigate new or increased revenues, improve efficiency and put in systems and resources to improve customer service and communication with the community. By the start of 2015/16 Council will have identified over $6million in savings that have been stripped out of the Operational budget.

Nevertheless, this achievement alone will not be sufficient to reach the benchmarks set in ‘Fit for the Future’, in particular the Operational Performance Ratio, Building and Infrastructure Asset Renewal Ratio, Infrastructure Backlog Ratio, and Asset Maintenance Ratio.

Council’s strategy to increase rates by 7.5% above ratepegging for two years (2017/18 to 2018/19) will achieve the Operational Performance Ratio on the proviso that Council does not introduce new services or facilities. However without further revenue increases it will still be difficult to demonstrate a significant improvement path for the Building and Infrastructure Asset Renewal Ratio, Iand Asset Maintenance Ratio, unless Council either reduces some services (with community support) or windfall grants are obtained.

The last community survey (see below & see Attachment ‘B’) demonstrates community needs for increased expenditure on roads and paths which is validated by the information compiled in Special Schedule 7 in the Annual Financial Statements.

Notwithstanding this, when comparing Council's Financial Statements for 2003/04 and 2013/14 the following trends are identified:

- Operating Expenditure (excluding depreciation) increased 59%.
- Rates & Annual Charges increased 60%.
- Depreciation increased 157%.

  This indicates the growth in new assets plus impact of better asset data and asset revaluations.
- Operations expenditure on Administration increased 37%.
- Operations expenditure on Public Order, Emergency Services & Safety increased 71%.
- Operations expenditure on Recreation & Cultural facilities increased 132%.

  This reflects the growth in new facilities provided including Aquatics Centre, Shoalhaven Entertainment Centre, sportsgrounds at North Nowra, St Georges Basin, Ulladulla and new park areas and facilities.
- Operational expenditure on Local Roads increased 129%.

  This reflects successive councils' decisions to put more focus on road maintenance and renewal works plus the annual increase in road assets transferred to Council through subdivision and growth.

All of this points to the need for significant increases in expenditure and the pressure to increase rates.

The final report of the ILGR Panel ‘telegraphed’ to councils and communities, throughout the report, the message that the reform agenda will impact on rates.

Here is a sample of quotes from the final report:

- *There is broad acceptance that council rates may need to increase faster to avoid cuts to local services and make necessary improvements.*
- *Polling results in relation to rate increases and amalgamations suggest that the respective concerns of State and local governments in these areas are probably over-stated. Surveys have shown consistently that Special Rate Variations costing in the range $1-2 per week are widely accepted: such increases represent up to 10% on average residential rates across NSW.*
- *Changes to the rating system and rate-pegging are essential to generate the revenues needed to fund infrastructure and services, and - equally as important - to make the system more equitable.*

- *3.2 The fiscal outlook*
    - *The available evidence points to a difficult fiscal outlook for NSW and Australia as a whole: weaker revenues during a time of relatively slow economic growth, coupled with the need to fund infrastructure gaps and increasing demands for services. The federal budget is much more constrained than it has been for decades due to the government’s aim to bring it back into surplus and reduce the debts incurred during the Global Financial Crisis.*

      This suggests that local government cannot expect increases in total state and federal funding and may well see a declining trend in specific purpose grants as some regional development and climate change programs are wound back. Making the best use of the existing pool of grants and of local government’s own tax base - rates - will assume even greater importance.

      The ‘Henry’ tax review of 2009 covered a number of issues of significance for local government:

        - *the need for councils to have sufficient autonomy in setting rates.*
- *…..many more councils should have been applying for Special Rate Variations to restore and strengthen their revenue base….*
- *As TCorp makes clear, a concerted, medium-long term strategy is required. This will need to combine fiscal discipline with improved financial and asset planning, accelerated increases in rates and charges where required, redistribution of grant funding, and improved efficiency and productivity.*

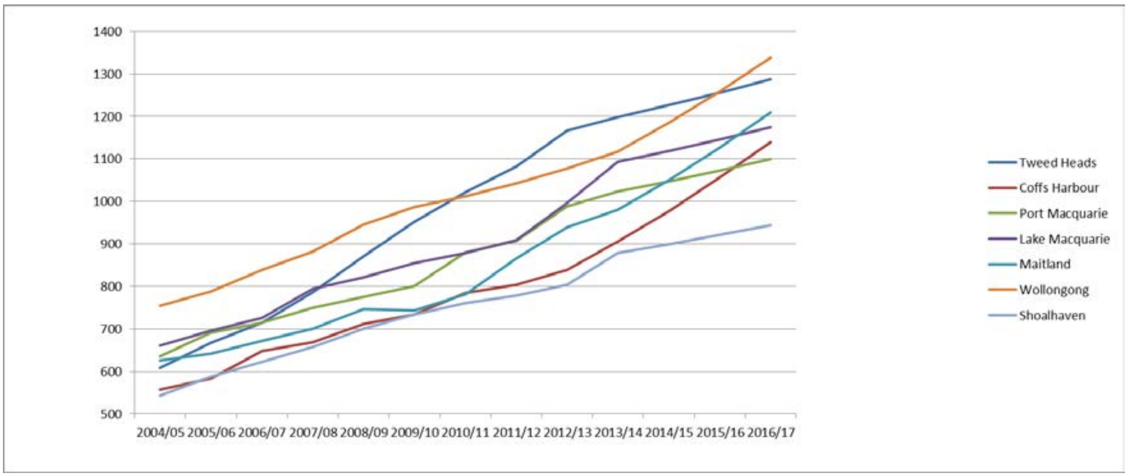
- *….a new focus on what it terms ‘fiscal responsibility’ - by which asset and financial management, the level of rates and charges, distribution of grants…*
- *At least breakeven annual operating positions are essential.*
- *Rate increases must meet <u>underlying</u> costs as well as annual growth in expenditure.*
- *Medium-term pricing paths are needed for ongoing adjustments to rates and charges.*
- *Rates are a tax, not a fee-for-service; they need to be set in accordance with principles of taxation - equity, efficiency, simplicity, sustainability and policy consistency.*
- *Existing options for minimum rates, base charges and differential rates should remain, but overly complex use of those mechanisms should be discouraged.*
- *There is considerable potential for greater use of special rates.*
- *Some concessions for disadvantaged ratepayers are justified, but social welfare should not be a local government responsibility; arrangements for pensioner concessions should be reviewed.*
- *The Panel’s investigations also indicate that rate-pegging has had significant unintended consequences, in particular:*
    - *Unrealistic expectations in the community (and on the part of some councillors) that somehow rates should be contained indefinitely, even though other household expenditures are rising.*
    - *Excessive cuts in expenditure on infrastructure maintenance and renewal, leading to a mounting infrastructure backlog.*
    - *Reluctance to apply for Special Rate Variations (SRVs) even when clearly necessary, because exceeding the rate peg is considered politically risky, or because the process is seen as too complex and requiring a disproportionate effort for an uncertain gain.*
- *….the rate-pegging system in its present form impacts adversely on sound financial management. It creates unwarranted political difficulties for councils that really can and should raise rates above the peg to meet genuine expenditure needs and ensure their long-term sustainability.*
- *IPART suggested increased flexibility for councils to set rates within a margin of 3% above the rate-pegging limit. That would add around 60 cents per week to the average residential rate (over and above the typical rate-pegging increase of around 3.5% or 70 cents per week). However, based on TCorp’s assessments, the Panel considers that a margin of up to 5% would be more realistic where councils need to make significant short-medium term inroads into*

infrastructure backlogs and correct operating deficits. This would result in a total increase for the average residential ratepayer of around $1.70 per week, which is well within the range of affordable and acceptable increases indicated by survey data.

- *IPART would continue to review and determine applications for SRVs of more than 5% pa above the peg. It would also advise the Minister on which councils might be exempted from rate-pegging.*

The full report is found at:
http://www.localgovernmentreview.nsw.gov.au/documents/LGR/Revitalising%20Local%20Government%20-%20ILGRP%20Final%20Report%20-%20October%202013.pdf

\# On examining the comparative data published by the Office of Local Government on average residential rates for the Group 5 councils, it is plain to see that Shoalhaven is the lowest in the Group & will fall further behind our comparable councils up to 2016/17 (see below & see Attachment 'C' for colour).



Note:
- Years 2003/04 to 2013/14 obtained from OLG website
- Years 2014/15 to 2016/17 calculated by adding ratepeg limit other than SRVs approved by IPART for:

Coffs Harbour	7.9% (2014/15)	8.14% (2015/16)	7.75% (2016/17)
Maitland	7.25% (2014/15)	7.25% (2015/16)	7.25% (2016/17) (+7.25% for another 4 years)
Wollongong	6.13% (2014/15)	6.23% (2015/16)	6.24% (2016/17)
Ratepeg	2.3% (2014/15)	2.4% (2015/16)	2.5% (est 2016/17)

By 2016/17 Shoalhaven City's average residential rate will be 17% below Port Macquarie and 42% lower than Wollongong, and below the other councils by 21% to 34%. However in referencing the latest Comparative Information on NSW Councils issued by the Office of Local Government it is evident that Shoalhaven has a far greater asset base than most other Group 5 councils, particularly relating to length of roads, number of pools/aquatic centres, number of public halls, area of open public space to maintain etc.

However, discussions on proposed rate increases are generally highly politically charged. The Standing Committee Inquiry needs to examine this issue in detail. There needs to be an independent review process that can assess a council's efficiency and justification for rate increases taking into consideration the variable factors of:

- geographic size and population spread;
- the Community facilities provided including libraries, pools, cultural centres, recreational facilities, area of parks and reserves, length of roads and footpaths, community halls, waterways, infrastructure, etc;
- services delivered and service levels;
- impact of tourist visitation and impact on infrastructure needs; and
- extent of climate change challenges.

This would be preferable rather than IPART simply examining a council SRV application, and would possibly be more acceptable to the community if some independent assessment was required rather than council itself

A coastal council such as Shoalhaven City has huge challenges with 49 towns and villages, 14 estuary systems, 150 kms of coastline, approx. 2.5 million tourists visits per annum, over 1,700 kms of roads and high numbers of development applications and growth - all these factors require high expenditure to meet community demands. The tension between needs and rating levels is compounded within Shoalhaven by the higher than NSW State average unemployment rates and lower than State average household income.

If you need further information about this matter, please

Yours faithfully

R.D Pigg
GENERAL MANAGER
01/07/2015