

State of the Organisation Summary Paper

“Strategic choices for a sustainable future”

8 January 2022

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1. Introduction

The purpose of this paper is to formally advise the new Council of the state of the organisation. Each stakeholder has been briefed on a range of operational and financial matters that are impacting on the cash flow and liquidity of Kiama Municipal Council (KMC). The Department of Planning, Industry and Environment, the Audit, Risk and Improvement Committee (ARIC), the Finance Advisory Committee (FAC), and the Blue Haven Board have been made aware of these matters, as has TCorp (our financier).

A summary of issues, documentation and action that have been undertaken are also outlined. The document concludes with an outline of short term and long term actions and options that could contribute to the sustainability of KMC. It is to be noted that this document is operationally focused,

with responsibility falling to the CEO. The role and lens for reading this document for the elected representatives is to:

- build an understanding and awareness of operational matters impacting on the state of the organisation;
- utilise this information to create a shared understanding of the emerging priorities for the elected body during the term; and
- commence forming a shared strategic direction on the priorities and policies that will guide the business to ensure sustainability now, and into the future, which can then be communicated to the ratepayers.

KMC is structured around two distinct businesses, one being the aged care residential facility known as Blue Haven and the other being the traditional local government services.

It is important for the new Council to understand that the matters facing KMC are not unusual to local governments, cash flow, asset management, lack of governance are all issues that councils experience, however the added complexity of the aged care business presents an unusual circumstance. It is worth noting that many of the matters that are impacting on the business have taken decades to arrive at their current state. Across the board there has been a lack of planning, governance, staffing and quality systems and procedures to help inform quality Council decisions.

In short summary there are three fundamental matters immediately affecting the business and future:

1. Financial sustainability – cash flow, liquidity, and financial management
2. Organisational capability, culture and performance – investment in people, systems, performance management and culture has been weak
3. Risk and governance – risk exposure created by lack of strategic direction, policy, poor decision making and lack of resources and revenue.

This document is written in the spirit of transparency and due diligence, no blame is attributed to any previous officers or elected representatives. Seeking to blame is not considered useful in correcting the situation or propelling the organisation towards a more sustainable business model.

As the CEO of two businesses, both facing significant viability risks I have responsibility to make the elected representatives and our three key stakeholder board members aware of the situation and appraised of what management action and options can be explored in addressing these matters. Beyond this level of disclosure, there is a responsibility on the elected representatives and the administration, to develop an effective communication and engagement strategy on these matters that gives the ratepayers a sense of sustainability and confidence in the future of KMC.

Coordinated and deliberate actions will need to be taken to ensure the future sustainability of both businesses. Collective decision making on priorities and unified commitment to striving towards sustainability must become a shared goal of the new Council. The businesses in their current operating states, without immediate and sustained correction are not sustainable, and it is this reality that presents both the adversity and the opportunity for the term of Council.

2. Summary of Blue Haven summary of matters

KMC has a 40 year history of running the aged care services known as Blue Haven (BH). Up until 2019 KMC had operated a 53 bed residential facility and a small number of independent living units.

The **Blue Haven** facility today has four distinct service offerings:

- a residential aged care facility (RACF) with 134 beds, currently operating at full capacity;
- approximately 262 independent living units with 99% occupancy;
- maintenance and asset renewal for all sites, and
- in-home aged care support services to several hundred clients throughout the Illawarra.

The residential aged care business is scheduled for an accreditation process to occur within the next eight 8 weeks and currently has compliance issues across each of the quality standard performance indicators and challenges with prudential requirements. Blue Haven has no separate operating accounts and its finances are completely merged with Council's general ledger.

Of significant immediate concern in relation to Blue Haven is:

- the negative EBITDA (earnings before interest, tax, depreciation and amortisation),
- lack of strategic plan guiding business, its workforce and operations,
- staffing costs and culture,
- clinical care and active commission complaints,
- independent living unit (ILU) resident dissatisfaction,
- whilst KMC has sufficient reserves to make the 2023 loan repayment to TCorp, the future loan repayments (required beyond 2023) are dependent on refinancing and Council being in positive cash flow.

The consequences of failing accreditation are sanctions, which require immediate cost requirements and corrective strategies, alongside product and reputational damage to the brand. This would in turn affect the value proposition of the business, and cause shareholder (ratepayer and RACF / ILU residents) concern.

It is also evident that significant underreporting to the Audit, Risk and Improvement Committee (ARIC) and the Blue Haven Board (BHB) has historically occurred. The following material provides a brief overview of the issues being experienced in areas of this business.

2.1 Blue Haven Bonaira RACF planning and loan

- Investment in Blue Haven RACF – with an initial indication of funding required being \$56M. Total project costs is \$106M.
- Documentation of how project costs increased are not fully reported or easy to obtain from the public record.
- Significant contract variations approved with insufficient delegations in delivery of capital project.

- Loan for Blue Haven and other operational projects totalling \$45M, adequate reserves to make repayments, with a focus on dependent on loan refinancing options required.
- No strategic plan, operational plan to guide operations.

2.2 Blue Haven Bonaira RACF

- EBITDA trending negative.
- Profit Improvement Assessment reports indicates financial unsustainability of the RACF in its current operational model.
- Urgent equipment needed to support quality clinical care, resulting in unplanned expenditure but enhanced care outcomes.
- Quality assurance and clinical care project established, resulting in \$300,000 of unplanned expenditure.
- Lack of operational staff planning, resulting in workforce pressures and need to review master roster.
- Building defects and closure of new build contract are a key focus.
- Improving governance, scheduling, planning and reactive maintenance services needs to occur.
- Recent commission complaints and open disclosure meetings have yielded some constructive feedback on areas to improve that require significant resources and investment.
- Staffing impacts due to COVID and current lockdown is affecting morale and culture of the workforce.
- Lack of financial policies and reporting to the Department and council, especially concerning audits into business operations.
- Prudential requirements under the *Aged Care Act 1997* in respect to the liquidity, governance, records and disclosure standards need to be consistently met.
- Services offerings suspended due to consumer act breaches in offerings, currently under urgent review and scheduled to be corrected.
- Recruitment drive to address significant staffing shortfalls have yielded 5 new registered nurses, but critical vacancies in care service employees (CSE). CSE roles total 34 with 26 existing vacancies. This is causing excessive staff costs through a mix of overtime, agency usage, temporary staffing and use of the casual workforce.

2.3 Independent Living Unit (ILU) build and operations

- The Bonaira facility was completed using design and construct. Changes to units above the RACF were not properly planned and are causing significant resident concern regarding noise, shared spaces and lack of policies to enable harmonious living. Addressing these complaints and correcting the facility design issues, would require planning, construction funds and resources.
- Single road access to the facility is creating campus issues.
- No asset management planning or replacement programs for existing ILU stock at the Terralong Street facility. Age, condition and vision for ILU's is unclear.

- Series of open disclosure meetings held with residents have revealed a need for transparency in maintenance programming, reporting on closed jobs and better collaboration / communication between Council, caretakers and the ILU Manager.
- Integration between the ILU's and the home care team needs to be strengthened, with a focus on relationship building that create a community type atmosphere for our residents.

2.4 Havilah Place abandoned RACF site

- No planning or budgeting work for the decommissioning of the old Havilah Place dementia site was undertaken prior to moving into new facility. Budget bid underway to undertake this urgent task.
- Future use or disposal of site needs to be urgently considered.

2.5 Blue Haven Board

- The newly created skills-based board for Blue Haven is a great asset and their role and ability to make decisions to guide the business needs to be strengthened.
- Greater clarity between the relationship of the Board, to Council's Audit Risk and Improvement Committee (ARIC) needs to be established.
- The BH Board have requested the separation of finances, assets, liabilities and staffing from Kiama's general ledger to enable a clear line of sight of the true costs of the service.
- ARIC has formally requested the development of operation plans, long term strategy and vision for the whole Blue Haven Service.
- Some staff in Blue Haven work under the Local Government Award.

3. Summary of Local Government general ledger matters

KMC is the region's largest employer with responsibility for delivering extensive Council services directly to the public. Much of the organisation's governance processes (policies / procedures) either do not exist, have extensive gaps or have not been updated for many years. A review of governance procedures and processes has been completed and reported to Council. Governance requires resourcing.

Likewise, the industrial instruments for the Local Government workforce are very aged, with five enterprise bargaining agreements (EBA) due for renegotiation this year, it will not be possible to complete all of these.

The lack of comprehensive human resource policies and procedures, alongside outdated industrial instruments cause significant workplace cultural issues either in their implementation, or varied lack of application. This affects culture and morale of the workforce and hampers delegated decision making.

In the 2021/22 financial year KMC is projecting an operational deficit of \$2.7M. Recent unplanned urgent expenditure will add to this deficit. Our financial statements are submitted in draft to the external auditors Deloitte's and require significant input and finalisation. Deloitte have advised our financials will not be audited until March 2022. This places Council in a difficult position in terms of onboarding a new Council and understanding the current actuals. Lack of sound financial policy, long term financial planning, software cutover issues and staff turnover, or understaffing in this area have critically affected our financial performance and reporting.

The organisation is not able to generate satisfactory monthly financial reports and is failing to meet its legislative obligations for financial reporting to the Elected Members. Managers and staff do not feel informed of immediate budgets and have had minimal reporting to enable them to keep good oversight of expenditure.

Staff shortages across the general ledger side of the organisation exist, and recruitment or redesignation of roles to priority areas is slow. Acute risk due to insufficient staffing exists in governance, assets, and finance. There is no set policy or process for requesting workforce needs or additional staff. Annual reporting / benchmarking on staffing has always included Blue Haven staff, skewing ratios and workforce planning for the general ledger side. Recruitment across the board is challenging due to the competitive marketplace and salary positioning of the organisation.

Culturally the organisation has challenges and lacks deliberative organisational development and planned workplace culture, supported by a robust training and development and performance management program. Staff have experienced a difficult few years and have not had structured training and development or clear performance expectations. The age of the workforce is older in demographic profile. Many staff across Council are of retirement age, some hold critical roles and require knowledge transfer to minimise risk. A cultural survey was completed over twelve months, but does not separate the two sides of the business and has had little follow through in terms of organisational development.

Service levels are not routinely set and some departments have business plans, but not all. The cycle for using business plans to inform planning and budget build each year is not clear, defined and changes from year to year. Managers and Directors have had variable degrees of access or involvement in budget development and monitoring. This year the budget build has been set, with managers provided training and Directors involved. KPI's for budget performance have been set, but insufficient financial reporting is failing to track and monitor actual expenditure against projections.

The business is currently undergoing a process of consultation with staff and unions to refine the existing organisational structure. An interim two director model is in use, with significant direct reports to the CEO role. The Blue Haven Chief Operating Officer (COO) role was created in September 2021 and recruited in November 2021. While clear KPIs are in place for this financial year, it is difficult and to an extent unfair, to determine effectiveness of performance of executive and management staff when the business is without sufficient systems, processes, resources and skill development opportunities.

The challenges facing the business have been known to some degree for several years, some staff have spoken up about this, or reported issues and that is appreciated. Reporting did not always eventuate in actions. Whilst known it is apparent that whole picture has gone without adequate understanding, robust discussion amongst staff, Councillors and the community and without due risk analysis.

Each year the Auditor General completes the audit of the financial statements and provides commentary to Council on issues to be addressed by management. The management letter sent to KMC by the Auditor General in 2021 identified 14 issues, 5 of which are repeat issues.

KMC has a strong ARIC who have recently been refreshed and better informed with reports. The advice of ARIC has largely not been heeded. The outgoing Chair who resigned in December 2021 (Chair since 2017) expressed a level of concern in staff turnover, poor quality of financials, lack of shared action and dialogue between management and Council specifically on actions arising from audit matters which have impacted on the effectiveness of ARIC.

Moving forward to address many of the issues noted above and summarised below, it is expected that the advice and support of ARIC, the BHB and the FAC will be instrumental in assisting Council in responding to these challenges. The following provides a high level summary of general ledger challenges.

3.1 TechnologyOne Project

- Investment in TechnologyOne enterprise software, contract and operational costs was not costed or fully reported until discovered. Project management, governance and control remains a core issue.

3.2 Employee matters and costs

- Casual conversion has not occurred in line with award requirements.
- Rising staffing costs due to overtime, agency, temporary and casual costs.
- Leave management and leave entitlements are a significant risk to the business and there is not adequate funding in reserves (there is \$1.5M) and the total amount payable is \$7.5M. Cash reserves for leave need to be increased and leave needs to be managed.
- Salary system and the competency performance payment protocol requires complete re-write (policy is over 20 years old). A recent Industrial Commission dispute cost \$260,000.
- Significant vacancies across the business and impacts of COVID has recently shut services and put at risk core services such as waste. Affecting approx. 20% of workforce.
- Retirement and long service leave obligations for several key staff will result in backfill, short term contracts and will disrupt the business.

- Council not adequately informed of executed deeds of agreement and penalties paid as a result of claims.
- Complaints handling, customer service standards require improvement and clear policies.

3.3 Restricted cash movements and cash flow

- Inappropriate movement from restricted reserves to general revenue. \$1M from development funds, corrected via retrospective resolution in 2021.
- Further concerns over removal of restricted reserves will be analysed by the forensic accountants and duly reported to Council.
- Failure to meet the liquidity ratio required by the Office of Local Government (OLG) for 3 years.
- Lack of financial policies and reporting to department managers, CEO and council.

3.4 Regulatory / Statutory responsibilities

- Proactive swimming pool compliance inspections not undertaken for 12 months and requires resourcing.
- No asset management planning or replacement programs for existing Administration Centre, depots, or Holiday Parks.
- Compliance matters at Holiday Parks require reporting to Council and comprehensive corrective programs.
- Infrastructure contributions policy recently audited and requires resourcing and urgent work. Significant revenue opportunities have been lost and under reporting in lines with legislative requirements.
- Capital project delivery over run of \$600,000 for lowering the roof at Gerringong Library and Museum. Project management, contract management and operational planning require improvement. Project evaluation will be completed and reported to Council.
- Project management resources and governance framework for future projects needs assigning priority and resourcing to avoid costly mistakes and to better support staff.
- Delegation Register needs a review and rewrite.
- Implementation of audit actions and Council decisions requires improved governance and reporting.
- Development assessments not assessed within legislative timeframes. A comprehensive development reform program and action plan is in place and improvements are ongoing. Matter has been reported to Council and extensive work undertaken.
- Asset management plans not reviewed since 2016, asset work needs resourcing and supporting process improvements.
- Significant improvements required to Council's Integrated Planning and Reporting Framework to ensure compliance with new IP&R Guidelines, including the development of a workforce plan, resourcing strategy and review of existing CSP and DPOP.

4. Strategic choices and options for discussion

The State of the Organisation report provided to Council, also noted a clear list of CEO actions to date, but given much of that information involves detailed operational issues, industrial / staffing or commercial in confidence business areas, that detail has been removed this public report. It is the only information removed.

Given the suite of challenges facing the organisation there is a need to ensure that strategic decisions are made to help guide the future sustainability of the business. Some of the decisions are the remit of the CEO, and others the remit of Council's Elected Body.

Agreement on priorities for Council's Elected Body is required to ensure that effort and resources are directed where needed. There is also a need to effectively communicate and engage the community in the program of sustainability and priorities of the new Council.

Of critical importance is the understanding that there is no quick fix for the three fundamental challenges facing the organisation, but there must be a coordinated, collective understanding and agreement on priorities.

Councillors and the community can be assured that regular reporting on many of these items will occur over the course of the term and it is recommended that the CEO provide a further state of the organisation reports on strategic improvement plans each quarter.

5.1 Blue Haven

Short term actions / options

- Develop a strategic plan for Blue Haven and an operational plan, including a long term financial plan for this aspect of the business.
- Separate the financial, assets, liabilities etc for Blue Haven from the General Ledger.
- Audit culture of Blue Haven staff and develop a comprehensive organisational development program to support staff.
- Establish a Finance Audit and Risk Committee for Blue Haven and clarify responsibilities for reporting to ARIC.
- Clarify roles and responsibilities for the board and their interaction with Council.
- Emergency expenditure approved and reported through ordinary meeting.
- Deliver the project focused on improving clinical management of Blue Haven / compliance management expertise during accreditation phase
- Review services, contracting and materials costs
- Consider proceeding to market for lease of Barroul House café to reduce operating costs
- Resolve commission complaints and establish clear complaints handling an open disclosure processes and policies
- Resolve building defects and consider options for ILU's above RACF
- Finalise master roster and develop structural options
- Emergency equipment purchases reported to council

- Recruitment drive to staff adequately and manage impacts of COVID and shortages
- Federal Government liaison regarding grant funding for business improvements
- Prudential requirements review
- Prepare cost estimate of either demolishing old Havilah site, or selling as is and seek Council decision
- Prepare asset management plans based on condition audits and whole of life considerations for all ILU's
- Comprehensive financial review of reserves / contracts of sale for enduring commitments to renovation, replacements etc
- Design and building issues between building 4 Bonaira residents and staff to be documented with costs for solutions reported to Council
- Defects at Bonaira ILU to be resolved and bond released
- Communication plan on the final costs / project costs for Blue Haven Boniara to fully inform community

Longer term actions / options

- Optimal staffing structure
- Outsourcing, leasing, joint venture or retained management opportunities / models of service
- Establish a Finance Audit and Risk Management subcommittee of the BHB with a clear relationship to Council's ARIC
- Prepare asset management plans for all holdings and understand true costs
- Prepare maintenance structure and operational costs for Council and Blue Haven to ensure adequate service levels
- Establish clear return on investment required by KMC
- Comprehensive financial plan for Blue Haven services

5.2 Local Government General Ledger

Short term actions / options

- Employee costs and salary model review and discussion with Council and staff, work either continues or ceases depending on affordability and resourcing
- Forensic accountant enquiry into previous investment decisions and deliver these findings to Council
- Immediate resources required (human and financial) in the finance department to establish monthly reports and meet legislative requirements for financial reporting
- Development of long-term financial plan for the whole organisation
- Develop an asset management program and resources for assets
- Improvement and investment in governance (human and financial)

- Essential service and service levels review
- Explore special rate variation or rates parameters
- Organisational structure, parameters for staffing ratios, critical vacancies and optimal business structure
- Appropriate policies and procedures for reserves and cash flow
- Separate budgets for Blue Haven and Council
- Risk strategy and register reset
- Increased grants revenue
- Correct reserves for leave
- Ensure adequate budget for organisational cultural development and training and development as business transformation will not occur without staff buy-in and support
- Review of fees and charges
- Project management office and improved resources for better project governance and oversight

Longer-term actions / options

- HR specialist to work with unions and workforce to review all five EBA's
- Documentation for special rate variation if pursued
- Commercial considerations report that explores business outsourcing or shared service models for some services
- Commercial services review of waste and holiday parks
- Salary system review
- Review of the full suite of HR policies to ensure workforce is properly managed
- Resolution of Holiday park compliance matters
- Strategic disposal and acquisition of assets
- Review of infrastructure charges and strategy