22 April 2021

Fiona Towers
Executive Director, Pricing and Policy
IPART NSW
PO Box K35
HAYMARKET POST SHOP NSW 1240

Contact: Sheridan Rapmund
Contact email: Sheridan_Rapmund@ipart.nsw.gov.au

Dear Ms Towers,

Formal opportunity to comment – Central Coast Council's Special Variation Application 2021-22

Thank you for providing Council with this opportunity to comment. Thank you also for your time on Monday, 19 April 2021.

Below are Council's responses to your specific questions.

Has the Council considered the option of a temporary special variation while it implements planned initiatives to achieve cost savings?

Yes. Council considered at least five options. Details of the individual options are attached in the Supporting Information section, but here is a summary.

A temporary special variation was considered unsuitable because:

- Council reverts to structural deficits as soon as the SRV is terminated, which is unsustainable because there is no unrestricted cash buffer.

- Council is unable to raise the $110M required to repay the restricted reserves debt over the committed 10-year period because Council either makes cumulative losses over the 10-year period or does raise the expected $110M which are unsustainable because:

  - Council does not have unrestricted cash
  - Council does not have capacity to borrow and
  - Council will breach the Office of Local Government requirement to repay the restricted reserves.

© Central Coast Council

- Council's $150M of new commercial loans, associated with the financial situation, are amortised over 15 years which means Council needs to make surpluses for at least that period. If not, the repayments are at risk and the banks may call on their debt.

Council has already implemented the planned structural initiatives to achieve ongoing cost savings.

Council has delivered 69% ($51M) of the required $74M in structural operational savings. This is the break-down of the composition of Council's $51M of savings:

- $31M has been made from staff cuts. Council has removed 570 positions from the structure (337 vacant roles, 212 occupied roles through voluntary redundancies and a further 21 roles through forced redundancies to be completed prior to 30 June 2021.)

- $20M has been made from significant structural cuts to materials and contracts.

The remaining 31% can only come from the permanent special rate variation. If Council does not obtain the permanent rate variation further staff cuts will be required and this will cause irreparable harm. Central Coast Council would cease to operate as a functioning urbanised local government entity.

If IPART considers the option of a temporary special variation, does the Council have a preferred timeframe for the special variation income to remain in the Council's rate base?

A temporary special variation will jeopardise Council's existing in its current capacity. A temporary special rate variation is simply not a financially sustainable option – as detailed above and in the attachment.

Council requires a permanent special rate variation of at least 15% to remain a going concern as a financially sustainable entity.

However, were a temporary special variation approved by IPART Council would prefer a 10-year or longer timeframe.

What are the reasons for the Council's preferred duration/timeframe?

Council's preference is for a permanent special rate variation due to the following reasons:

- OLG's requirement to repay $110m in restricted reserves debt over 10 years;
- It will provide certainty and confidence to a couple of major banks that Council will be able to repay their loans and therefore will prevent them from calling on their debt prematurely.

Other matters for consideration by the Tribunal

= Council accessed restricted funds because of financial unsustainability at a structural level. The Council unwittingly and unlawfully drew down over $200M in conducting its general operations, which are to be repaid as follows:

  - $110M over the next 10 years from Council's surpluses;
  - $40-$60M from property sales;
  - $20M written off from internal reserves;
  - $10-$30M of commercial loans at the end of the 10 years

- Council is required to repay over $110M of the restricted funds debt over the next 10 years and that has been the driving factor of preparing the Long Term Financial Plan for the next 10 years. Council will be foregoing any surpluses to repay debt and this means service levels will decline.

- The adopted Long-Term Financial Plan is an aggressive plan and with in-built efficiencies and no cash buffers.

- On top of the $51M in structural savings included from next year's budget onwards, Council will deliver an additional $35M in efficiencies ($15M from Other Expenses and $20M from employee costs) over the next ten years. Council has not applied CPI increases to "Other Expenses" in the Long-Term Financial Plan and it has not provided for growth in staff levels or staff progression in the Long-Term Financial Plan.

- Council has obtained $150M in new commercial loans, associated with the financial situation, to ensure its continued operation. The loans are amortised over 15 years. These loans were provided contingent on Council being able to implement measures including a permanent special variation.

- The Office of Local Government requires that Council repay the restricted funds within the next ten years.

- Even with a permanent special variation Council returns to deficit in year eleven.

- Even with a 15 % rate variation, Central Coast Council's comparable residential rates will be lower than those of our neighbouring Councils. And lower than Councils of the same category.

Without a permanent special rate variation, the $51M in savings already made and the future $35M in efficiencies Council will be in deficit for the foreseeable future.

Any suggestion that Council is relying solely, or even predominantly, upon a special rate variation to address the financial situation is incorrect.

Thank you again for the opportunity to clarify this information and provide further background.

Yours sincerely,

[redacted]

David Farmer
Chief Executive Officer
Reference No: F2020/03181 – D14593514

Supporting Information

- Consideration of options
- Cost saving actions taken by Council
- Efficiencies and service levels
- Comparative rates

Consideration of options

10% Temporary for 7 years as per Council Resolution as at 26 November 2021

This was financially modelled and determined unsustainable for the following reasons:

- Council reverts to structural deficits in year 1 and 7 (which are unsustainable because there is no unrestricted cash buffer);

- Council is unable to raise the $110M required to repay the restricted reserves debt over 10 years and instead the cumulative result for Council over those 10 years is a loss of $39M (this includes a projected expectation of obtaining at least a $20M increase from IPART's water and sewer determination), which is unsustainable because:

  - Council does not have unrestricted cash.
  - Council does not have capacity to borrow more.
  - Council will breach its commitment to OLG to repay the restricted reserves debt in 10 years.

- Council's $150M of loans are amortising over 15 years, making surpluses necessary until at least year fifteen. Otherwise, the loan repayments will be at risk and the banks may call on their debt.

As a result this option was not formally adopted by Council

10% Permanent

This was financially modelled and deemed unsustainable for the following reasons:

- Council reverts to structural deficits in year 1 and 7 (which are unsustainable because there is no unrestricted cash buffer);

- Council is unable to raise the $110M required to repay the restricted reserves debt over 10 years. Instead the cumulative result for Council over those 10 years would contribute only $12M of the $110M reserves repayment requirement (this includes a projected expectation of obtaining at least a $20M increase from IPART's water and sewer determination), which is unsustainable because:

- Council does not have unrestricted cash.
- Council does not have capacity to borrow more.
- Council will breach its commitment to OLG to repay the restricted reserves debt in 10 years.

- Council's $150M of loans are amortising over 15 years, making surpluses necessary until at least year fifteen. Otherwise, the loan repayments will be at risk and the banks may call on their debt.

15% Temporary for 4 years

This was financially modelled and deemed unsustainable for the following reasons:

- Council reverts to structural deficits in year 5 (which are unsustainable because there is no unrestricted cash buffer);

- Council is unable to raise the $110M required to repay the restricted reserves debt over 10 years and instead the cumulative result for Council over those 10 years is a loss of $50M (this includes a projected expectation of obtaining at least a $20M increase from IPART's water and sewer determination), which is unsustainable because:

  - Council does not have unrestricted cash.
  - Council does not have capacity to borrow more.
  - Council will breach its commitment to OLG to repay the restricted reserves debt in 10 years.

- Council's $150M of loans are amortising over 15 years, making surpluses necessary until at least year fifteen. Otherwise the loan repayments will be at risk and the banks may call on their debt.

15% Temporary for 7 years

This was financially modelled and deemed unsustainable for the following reasons:

- Council reverts to structural deficits in year 8 (which are unsustainable because there is no unrestricted cash buffer);

- Council is unable to raise the $110M required to repay the restricted reserves debt over 10 years and instead the cumulative result for Council over those 10 years would contribute only $27m of the $110m reserves repayment requirement (this includes a projected expectation of obtaining at least a $20M increase from IPART's water and sewer determination), which is unsustainable because:

  - Council does not have unrestricted cash.
  - Council does not have capacity to borrow more.
  - Council will breach its commitment to OLG to repay the restricted reserves debt in 10 years.

- Council's $150M of loans are amortising over 15 years, making surpluses necessary until at least year fifteen. Otherwise the loan repayments will be at risk and the banks may call on their debt.

15% Permanent (Application lodged with IPART)

This was financially modelled and deemed sustainable with the following caveats:

- Council reverts to structural deficits in year 11 (which are unable to be sustained because there is no unrestricted cash buffer).

- Council is able to raise the $110M required to repay the restricted reserves debt over 10 years.

- Council obtains at least a $20M increase from IPART's water and sewer determination for 2022/23.

- Council's $150M of loans are amortising over 15 years, making surpluses are necessary until at least year fifteen.

- A further special rate variation or blunt restricting of expenditure will be necessary before the end of next 10 years otherwise the loan repayments will be at risk and the banks may call on their debt.

Cost saving actions taken by Council

Council has taken the following radical and blunt actions to return to financial sustainability and be able to repay the $200M restricted reserves debt.

Staff and cost reductions

Council has delivered $51M (69%) of the $74M structural operational changes to bring Council back to financial sustainability. This is made up of:

- $31M structural reduction in employee costs through the removal of 570 positions from Council being:

  337 vacant roles wiped out of the Organisational Structure,

  212 occupied roles removed through the voluntary redundancy program (at a cost of $20m), of which 178 people have already exited the organisation,

  21 forced redundancies which are currently being processed.

- $20M structural reduction in materials and contracts

The above actions result in a 15% reduction in wage costs.

If Council were not to receive a special variation, it would not be possible to reduce staff levels further. As stated in our application, Council would likely need to reduce the workforce by a further third. This would bring staff levels to below those prior to amalgamation which have been identified as artificially low.

To do this would result in unacceptable drops in service levels to the point where Council may not be able to meet its statutory obligations.

In addition, Council would simply not be able to fund the redundancy payments required if further staff cuts were required.

As a result of the recent staff cuts there will be a service reduction. Any efficiencies gained or savings realised in future years will be used to return service to their former levels as expected by the Central Coast community.

Council requires that the special variation is permanent so that it can undertake strategic workforce planning to meet future needs with confidence that there will be a stable income base. If the special variation were temporary, Council would not be able to plan for service delivery and the appropriate resources required.

Sale of assets

Council currently has $40-$60M of property for sale on the market. Income from these sales will be used as one-off partial repayment of the restricted reserves debt.

In addition, Council has considered a second tranche of assets for sale and will soon consider the third tranche.

The following are the estimated expected sale prices:

Tranche 1 -	$56,434,000
Tranche 2 -	$ 4,026,000
Tranche 3 -	$30,163,956

When considering a permanent special variation it is important to note that the income from the sale of assets is a one-off cash injection. It is an option which will not be available to Council in the future.

Other actions

Council has written off $20M in internal reserves reducing the amount that is to be repaid.

Council has capped the capital program at the level of Council's depreciation cost. This is to prevent further restricted reserves load and growing operational load.

Council will also need to consider an additional loan towards the end of the 10 year period.

Council will likely need to consider a further SRV toward the end of the 10 year period.

Efficiencies and service levels

Council has forcefully in-built efficiencies by removing any CPI increases in the Other Expenses line of its Long-Term Financial Plan. Doing so delivers $15M in efficiencies over the next 10 years.

Council has consciously stripped the growth in staff progression in order to drive further efficiencies and control employee cost growth. This is $20M in efficiencies over the next 10 years.

The Plan provides for increases in employee costs at 2.5%. This represents the minimum Award increase that Council is obliged to pay and the Superannuation Guarantee. It does not include provision for any performance increases or salary progression. Further, the Plan anticipates employee costs increasing by only 2% after Year 5.

It is a fact that community expectations as to service levels and infrastructure quality is increasing particularly as the local area is continuing to urbanise. Council has consciously not allowed for an incremental increase in service levels over the next 10 years in response to Council's growing population. This is in an effort to force efficiencies to enable the delivery of services.

Council's strategy is driven on the premise of returning services without any additional costs. This is reflected in the adopted Long-Term Financial Plan.

The following shows that the Long-Term Financial Plan model results in Council returning to deficit after the tenth year. For this reason, Council requires that the special variation is permanent.

	1	2	3	4	5	6	7	8	9	10	11
	2021/22	2022/23	2023/24	2024/25	2025/26	2026/27	2027/28	2028/29	2029/30	2030/31	2031/32
	$'000	$'000	$'000	$'000	$'000	$'000	$'000	$'000	$'000	$'000	$'000
Operating Income											
Rates	179,357	183,841	188,437	193,148	197,977	202,926	207,999	213,199	218,529	223,992	229,592
SRV	22,859	23,431	24,016	24,617	25,232	25,863	26,510	27,172	27,852	28,548	29,262
Annual and User Charges and Other Income	415,084	437,160	439,345	441,542	443,750	445,969	448,198	450,439	452,692	454,955	457,230
Operating Grants	34,856	34,856	34,856	34,856	34,856	34,856	34,856	34,856	34,856	34,856	34,856
Operating Contributions	14,635	14,635	14,635	14,635	14,635	14,635	14,635	14,635	14,635	14,635	14,635
Total Income attributable to Operations	**666,792**	**693,922**	**701,290**	**708,798**	**716,450**	**724,249**	**732,198**	**740,302**	**748,564**	**756,987**	**765,575**
Operating Expenses											
Employee Costs	175,832	180,228	184,733	189,352	194,086	197,967	201,927	205,965	210,084	214,286	218,572
Borrowing Costs	17,471	17,351	17,231	17,111	16,991	16,871	16,751	16,631	16,511	16,391	16,271
Materials and Contracts	188,517	189,460	190,407	191,359	192,316	193,277	194,244	195,215	196,191	197,172	198,158
Depreciation	177,106	182,606	188,106	193,606	199,106	204,606	210,106	215,606	221,106	226,606	232,106
Other Expenses	100,822	100,822	100,822	100,822	100,822	100,822	100,822	100,822	100,822	100,822	100,822
Total Expenses attributable to Operations	**659,748**	**670,467**	**681,300**	**692,250**	**703,321**	**713,544**	**723,850**	**734,239**	**744,715**	**755,277**	**765,929**
Operating Result after Overheads and before Capital Amounts	**7,043**	**23,456**	**19,990**	**16,548**	**13,129**	**10,705**	**8,349**	**6,063**	**3,849**	**1,709**	**(354)**

Comparative rates

Central Coast Council has amongst the lowest Rates for Councils in Office of Local Government Group 7. The residential rate and our farmland rate is second lowest. The business rate is the third lowest.

When comparing Central Coast to other Metropolitan Fringe Councils, the residential rate and farmland rate is second lowest. The business rate is in the middle.

Compared to neighbouring Councils, Central Coast Council has the lowest residential rate and farmland rate.

A permanent special variation will simply bring rates for Central Coast Council to the minimum level appropriate for a Council of its location and size.