

Mr Edward Jenkins
Independent Pricing and Regulatory Tribunal

To be submitted via online portal

Dear Mr Jenkins,

Additional Special Variation Application

At the Ordinary Council Meeting 26 April 2022, City of Newcastle (CN) resolved to apply for the Additional Special Variation (ASV) under section 508(2) of the Local Government Act 1993 (the Act) as a permanent special variation for the full 2.5%, consistent with our long-term financial plan.

Achieving financial sustainability is our key objective and we have undertaken many initiatives to maintain this, resulting in six consecutive years of modest budget surpluses, only ended by the impact of COVID-19 in 2019/20.

CN showed local leadership throughout the pandemic by electing to utilise internally reserved funds to implement two phases of an award winning Community and Economic Resilience Package. The works program was boosted to \$102.4 million in 2020/21 and \$105.1 million in 2021/22 with REMPLAN analysis estimating CN's stimulus spend created almost 1,400 local jobs and increased total economic output in the LGA by approximately \$500 million.

Supporting the local economy throughout the pandemic has helped limit the full force of the economic impact of restrictions implemented to limit the spread of COVID-19 during the first 18 months of the pandemic. However, the resulting lost revenue and increased expenditure experienced during the three affected financial years makes it critical CN's rate revenue grows by the proposed 2.5% to help offset the pressure creating by surging inflation, both in 2021 and this year. Without the additional rate revenue possible under a rate cap of 2.5%, CN will have no choice but to consider reductions in service or postponement of proposed projects in our LTFP to ensure future delivery of balanced budgets.

The 2022/23 rate peg determined by IPART for CN of 1.2% inclusive of the 0.7% base peg and the population growth component of 0.5%, is an unexpected challenge that further constrains revenue projections still recovering from public health orders and related community restrictions. The rate peg is the lowest in two decades and limits CN's ability to maintain service levels affected by a CPI growth rate of 3.5% in calendar year 2021. The Cordell Construction Cost Index also showed that national construction costs increased by 7.3% during this time which is of relevance to CN given it invests more than \$100 million annually into the local economy via its budgeted capital works program. The draft 2022/23 capital works program forecasts a works program spend of \$132 million, the largest ever under by a local council in the Hunter region.

Our financial modelling confirms that the ASV is the best way to achieve a sustainable operating surplus while maintaining the services and facilities the Newcastle community expects. All other options to increase revenue or reduce costs have been considered and are reflected within the Operational Plan. However, to mitigate future risks and ensure CN can maintain current service levels and infrastructure spending, it remains committed to identifying opportunities for future income streams, further reducing the reliance on rating income from the current 60%.

The additional rate increase of 1.3% requested by CN will generate an additional \$2.2 million in 2022/23. The average residential rate payer in the local government area will contribute an additional \$20.95 or 40 cents per week if the rate peg is lifted to the requested 2.5%. This is considered reasonable by the elected Council and the resolution was carried by a significant majority of Councillors.

CN sort to proactively disclose to the community its intention to apply for a 2.5% ASV, communicating this to local media last week. The ASV was subsequently extensively reported in newspapers, and on radio and television news. To date neither myself nor CN have received any objections from the community to the proposed 2.5% rate cap.

CN has provided its 2021/22 IP&R documentation as required by the IPART information paper however that Long-Term Financial Plan (LTFP) appears flawed for the same reason the rate peg was fundamentally inadequate. The LTFP was prepared in the first half of 2021 after the Australian economy shrank by 1.1% in 2020, the first recession in nearly 30 years. The LTFP did not factor in revenue reductions from soon to come COVID-19 variations or sky rocketing CPI growth that has not yet reached its peak. Data released on 27 April 2022 shows the annual inflation rate has now further increased to 5.1%.

It is more appropriate to use the 2022/23 – 2031/32 Long-Term Financial Plan that CN has placed on public exhibition to assess the need for the ASV. This LTFP projects the operating performance ratio will only be above 2% once between 2021/22 and 2026/27 and will average 1.49% across the time. This ratio demonstrates the need for the permanent ASV as outlined in the IPART Circular 22-07.

Ratios

Ratio	Benchmark Per OLG	2021/22	2022/23	2023/24	2024/25	2025/26	2026/27
Operating performance ratio	> 0.00%	1.67%	1.56%	0.54%	1.20%	2.47%	1.54%
Own source operating revenue ratio	> 60.00%	91.28%	86.75%	86.86%	87.03%	87.11%	87.18%
Unrestricted current ratio	> 1.5x	2.07x	2.41x	2.37x	2.52x	2.48x	2.47x
Debt service cover ratio	> 2x	5.55x	4.65x	5.37x	5.72x	6.36x	6.27x
Rates, annual charges, interest and extra charges outstanding percentage	< 10% regional & rural	4.14%	4.07%	4.24%	4.07%	4.07%	4.07%
Cash expense cover ratio	> 3 mths	785 mths	716 mths	721 mths	703 mths	708 mths	6.85 mths

CN will use the additional revenue of the ASV to support recovery from COVID-19 induced budget deficits in 2019/20 (\$3.6 million), 2020/21 (\$32.5 million) and 2021/22 (forecast \$13.5 million).

These deficits were unavoidable due to CN losing more than \$40 million in forecast revenue due to public health orders that included the closure of its Civic Theatre, Stockton Holiday Park, parking meters and venue hire business. CN's Own Source Revenue ratio is 87% and comfortable the highest amongst its peers within the Office of Local Government Group 5 – Regional City. This ratio demonstrates the significant amount of commercial revenue that subsidises the cost of providing services to Newcastle ratepayers but also highlights its exposure to market forces that hinder its return to surplus while commercial revenues remain sluggish.

The ASV is required to be permanently held within the rate base and will be critical to CN increasing its works program to the \$115 million required annually to deliver the strategies of the recently, unanimously adopted "Newcastle 2040" Community Strategic Plan. CN has

planned a record \$132 million works program in 2022/23 that commences four significant 'City Shaping' projects that continues CN's strong focus on strategic investment and delivering on the initiatives and actions agreed with our community.

Should you require any further information on this matter please contact Scott Moore, Manager Finance on ([REDACTED])

Yours faithfully

[REDACTED]

Jeremy Bath
Chief Executive Officer

Date: 28/04/2022