

Council Ref: SC2566-02
Your Ref:

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Municipal
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30 July 2015

Dr Peter J Boxall AO
Chairman
Independent Pricing and Regulatory Tribunal
PO Box K35
Haymarket Post Shop
SYDNEY NSW 2000

Dear Dr Boxall

Thank you for the opportunity to provide this brief submission to the Independent Pricing and Regulatory Tribunal (IPART) in response to the Fit for the Future Voluntary Merger Proposal submitted to IPART by Randwick City Council and Waverley Council.

The purpose of this submission is to expand on comments made in Woollahra Council's previously submitted Existing Structure Improvement Proposal regarding assertions made in the Randwick/Waverley merger proposal that the inclusion of Woollahra Council in the merger would result in significantly greater cost savings.

More specifically, the Randwick/Waverley Template 1 Merger Proposal submitted to IPART states the following on page 41:

*“Based on financial modelling this merger would result in cost savings and hence an opportunity to increase services by **\$235m over ten years** while meeting the seven ‘Fit for the Future’ ratio **benchmarks in two years**, eliminating the **backlog** of works required on roads, footpaths, drains, buildings and in parks and beaches in five years and repaying **debt.**”*
(Randwick Options Analysis, May 2015, page 12 (Attachment 2.5)).

The Proposal further states on page 26 in respect of the Randwick/Waverley merger that:

*“This merger is projected to result in cost savings and hence increased services over ten years of **\$103m (\$485 per resident)**, providing scope to undertake new functions and major projects.”*

The conclusion drawn from these statements is that the inclusion of Woollahra Council in the expanded three council merger option will bring an additional \$132m in increased service opportunities over 10 years, or some \$13m per annum. These projections are after providing for the cost of amalgamation.

The service cost modelling submitted to IPART with the Randwick/Waverley merger proposal indicates that efficiencies of \$17m per year could be secured by applying Randwick's service unit costs to Woollahra. On a cost base of \$67.5m derived from the report, this suggests savings in the order of 25%.

As stated in our Existing Structure Improvement Proposal submission to IPART, Woollahra Council has rejected any proposal to join this voluntary merger as it considers that Waverley and Randwick Councils' estimates of cost savings under the merger are not achievable, and in any event, do not justify the unacceptable rate increases that would result from Woollahra Council's inclusion in the merger proposal.

Table 1 summarises the basis of the service cost modelling undertaken by Randwick Council in its Fit for the Future submission. The data is drawn from each Council's *Special Schedule 1 – Net Cost of Services* in the Financial Statements for the year ended 30 June 2014. Woollahra's total *Expenses from Continuing Operations*, less depreciation and borrowing costs, totalled \$67.5m for 2013/14 across 13 service areas.

Table 1 – Operating expenditure less depreciation and borrowing costs by Service Area per dwelling

Service costs \$	Service Areas												
	Governance	Administration	Public Order and Safety	Health	Environment and Street Cleaning	Solid Waste Management	Community Services and Education	Housing and Community Amenities	Recreation and Culture	Mining, Manufacturing and Construction	Transport and Communication	Parking Areas	Economic Affairs
Randwick	80	49	144	1	240	528	114	255	500	55	103	74	-1
Waverley	0	204	251	37	163	571	382	332	660	30	250	543	23
Woollahra - Gross Cost	115	758	234	15	180	381	126	277	502	55	459	62	74
Less Dep'n & Borrowing	0	0	-9	-0	-71	-33	-13	-32	-112	-3	-161	-5	-11
Admin Distribution	34	-598	66	4	32	102	33	72	115	15	88	17	19
Woollahra - Net Modelled	149	160	291	19	142	450	147	317	505	66	385	73	82
Botany	0	319	96	4	140	489	332	142	944	248	327	0	550
Sydney	66	2,140	317	145	45	306	175	394	621	0	-416	105	424
Rwk Service Level?	YES	YES	YES	NO	NO	NO	YES	YES	NO	YES	YES	NO	NO
in SGS ORIGINAL	YES	YES	YES	NO	NO	NO	YES	YES	NO	YES	YES	NO	YES
Woollahra's Grossed up Service Costs \$	3,612,083	3,885,373	7,054,816	461,850	3,448,562	10,910,616	3,559,603	7,675,554	12,228,690	1,604,402	9,338,335	1,772,998	1,984,118
Cost Base for Services Modelled at Randwick's unit cost	36,730,166												

The modelling of savings that would be derived from an amalgamation of councils is calculated in the model by simply applying Randwick's service cost per dwelling to other councils in the group for a selection of service areas as identified by the row titled '*Rwk Service Level?*' in Table 1 above. The cost of these services areas (highlighted above in green) in Woollahra's case is \$36.7m.

Table 2 summarises the modelled savings. It indicates that Woollahra's service costs would reduce from \$67.5m to \$50.2m, saving some \$17.3m (or 47% of the cost base) as a consequence of applying Randwick's service cost per dwelling.

Table 2 – Modelled savings in service costs derived from applying Randwick's cost per dwelling to Woollahra

Service costs \$	Service Areas												
	Governance	Administration	Public Order and Safety	Health	Environment and Street Cleaning	Solid Waste Management	Community Services and Education	Housing and Community Amenities	Recreation and Culture	Mining, Manufacturing and Construction	Transport and Communication	Parking Areas	Economic Affairs
Randwick	80	49	144	1	240	528	114	255	500	55	103	74	-1
Waverley	80	49	144	37	163	571	114	255	660	55	103	543	23
Woollahra	80	49	144	19	142	450	114	255	505	55	103	73	82
Woollahra's real cost	80	49	144	19	189	484	114	255	544	55	103	68	89
Botany	80	49	144	4	140	489	114	255	944	55	103	0	550
Sydney	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a
Modelled Service Costs	1,929,410	1,182,542	3,494,741	461,850	3,448,562	10,910,616	2,770,679	6,172,730	12,228,690	1,341,631	2,489,814	1,772,998	1,984,118
Reduction in Service Costs	1,682,673	2,702,831	3,560,075	0	0	0	-788,925	1,502,825	0	262,771	6,848,521	0	0
Saving as a percentage of Cost Base	47%												

This submission challenges the validity of the modelling on a number of grounds.

Firstly, the exclusion of depreciation was done on the basis of Randwick's percentage of depreciation in service areas. Deducting actual depreciation from Woollahra's services areas provides a quite different per dwelling service cost. Table 3 below shows that, notwithstanding Council's other concerns with the assumptions used in the modelling, the purported savings derived from the modelling would reduce by 17% (to \$14.4m) if depreciation were excluded based on actual costs.

Table 3 – Effect on savings of deduction of depreciation on the basis of actual cost

	Governance	Administration	Public Order and Safety	Health	Environment and Street Cleaning	Solid Waste Management	Community Services and Education	Housing and Community Amenities	Recreation and Culture	Mining, Manufacturing and Construction	Transport and Communication	Parking Areas	Economic Affairs	
Service costs \$														
Woollahra's Reported Special Schedule 1	2,789,490	18,371,452	5,671,027	359,243	4,373,001	9,235,496	3,057,571	6,710,370	12,155,602	1,324,136	11,122,449	1,497,538	1,800,197	78,467,572
LESS: Depreciation		-2,222,105	-60,983		-585,318		-342,174		-1,758,619		-4,938,777	-254,538	-91,258	-10,253,772
LESS: Borrowing Costs		-676,521												-676,521
	2,789,490	15,472,826	5,610,044	359,243	3,787,683	9,235,496	2,715,397	6,710,370	10,396,983	1,324,136	6,183,672	1,243,000	1,708,939	67,537,279
Admin Distribution \$														
	822,080	-14,486,620	1,605,620	105,110	784,870	2,483,170	810,140	1,746,900	2,783,160	365,150	2,125,330	403,520	451,570	0
	3,611,570	986,206	7,215,664	464,353	4,572,553	11,718,666	3,525,537	8,457,270	13,180,143	1,689,286	8,309,002	1,646,520	2,160,509	67,537,279
Real per Dwelling Cost	149	41	298	19	189	484	145	349	544	70	343	68	89	
Reduction in Service Costs using Woollahra's 'real' per dwelling cost	1,682,160	-196,336	3,720,923	0	0	0	754,858	2,284,540	0	347,655	5,819,188	0	0	14,412,989

Secondly, it is noted that there is a period of protection for staff in an amalgamation. The legislated 3 year period has been extended to 5 years by the signing of a memorandum of understanding by Randwick and Waverley Councils. Staffing costs make up a significant proportion of each Council's cost base. Table 4 shows Woollahra's staffing costs by service area after having distributed the same proportion of Administration staffing costs to other services areas on the same basis as the modelling.

Table 4 – Woollahra staffing costs by service area

	Governance	Administration	Public Order and Safety	Health	Environment and Street Cleaning	Solid Waste Management	Community Services and Education	Housing and Community Amenities	Recreation and Culture	Mining, Manufacturing and Construction	Transport and Communication	Parking Areas	Economic Affairs	
Woollahra's Staffing Cost by Service \$	1,549,136	9,187,713	1,600,719	345,359	2,471,071	3,062,056	1,908,999	4,259,395	5,802,342	1,173,472	3,287,125	5,703	214,074	34,867,163
Admin Distribution \$*	488,148	-8,602,107	953,412	62,414	466,053	1,474,498	481,058	1,037,303	1,652,631	216,825	1,262,014	239,609	268,141	0
	2,037,284	585,606	2,554,131	407,773	2,937,124	4,536,554	2,390,057	5,296,698	7,454,974	1,390,297	4,549,139	245,311	482,215	34,867,163

* Based on Randwick's Admin Cost Distribution

Table 1 indicated that the cost base of Woollahra's services that the modelling is applied to is \$36.7m. Table 4 shows that \$18.8m of this is staffing costs, which are protected for a period following amalgamation.

While it is acknowledged that some reduction in cost would be achieved at the senior staff level and through natural attrition or voluntary redundancy, the \$18.8m staffing costs represent 51% of the total \$36.7m cost base. The effect of this is that the \$17.3m reduction in costs in the model (refer Table 2) would need to be obtained from a \$17.9m cost base (\$36.7m less \$18.8m) for at least the first five years. In this regard, Council contends that a 97% (\$17.3m / \$17.9m) efficiency saving is a completely flawed assumption to include in the modelling.

Indeed, in some instances, Woollahra's staffing costs alone exceed the modelled service costs derived from the application of Randwick's service cost per dwelling. Comparing Table 4 to Table 2 shows, for example, staffing costs in Transport and Communication at \$4.5m and the modelled service costs at \$2.5m. This is simply unachievable with staff protected for five years. Thirdly, the use of the number of dwellings as the uniform denominator for the modelling is also challenged. It is simply inappropriate. For example, Woollahra's Emergency Management Contribution of \$2.5m (and forming part of Public Order and Safety) is based on land value and will not be reduced as a consequence of amalgamation.

Street lighting is another example of a \$1.4m cost for Woollahra Council that will not change in these circumstances.

Taking the assumption used in Randwick's modelling to its logical conclusion, does a kilometre of road in Woollahra that has 10 dwellings on it cost twice as much to maintain as a kilometre of road in Randwick with 20 dwellings on it?

Clearly, the answer to the question is 'no' and indeed the two councils may well use the same contractors through the Southern Sydney Regional Organisation of Councils supplier agreements to maintain their roads. However, the modelling presents resultant savings that would assert this to be the case.

Council contends that similar flawed logic is applied in the modelling for other services such as processing of development applications (which are also income deriving), building control and compliance, local law enforcement and a broad range of community services.

There is also a flaw in the modelling in that it pays no regard to specific service standards across the councils which have been developed over many years in consultation with and having regard to, community demands and expectations. Adopting lower standard service costs will no doubt lead to lower service standards.

Fourthly, it also appears that there has been no regard for revenue positive services. For example, the Public Order and Safety service area includes \$2m in costs associated with parking enforcement which generated some \$5.6m in infringement revenue in 2014/15. The Transport and Communications service area includes \$1m in expenditure associated with utilities and builders restorations which generated some \$1.2m in restoration charges revenue. Reducing costs in these areas would have a detrimental effect on Woollahra Council's bottom line and consequently the resultant cost savings derived from any modelling of merger options.

Council considers these matters to be significant flaws in the modelling that should raise serious questions with IPART as to the reliability of the financial analysis contained in the Randwick/Waverley Merger Proposal.

Council raises these serious concerns directly with IPART given the assertions made in the Randwick/Waverley Merger Proposal that the cost savings are greatly improved through the inclusion of Woollahra Council as a merger partner. Woollahra Council does not agree with the findings of the Randwick/Waverley service modelling.

Should you require any further information in relation to this submission, please contact Council's Director Corporate Services, Stephen Dunshea on [REDACTED] or [REDACTED]

Yours sincerely

[REDACTED]
Gary James
General Manager