



Special variation and minimum rate increase

Kiama Municipal Council 2018-19

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1 Executive Summary

The Independent Pricing and Regulatory Tribunal of NSW (IPART) has set the rate peg for 2018-19 at 2.3%. Councils may apply to increase their general income above the rate peg. For most councils, general income consists entirely of rates revenue.

Kiama Municipal Council (Kiama Council) applied for a multi-year special variation to:

- ▼ increase its general income by 6.00% each year in 2018-19, 2019-20 and 2020-21, a cumulative increase of 19.10%, and
- ▼ retain this increase in its rate base permanently.¹

The council also applied to increase the minimum amount of its business rates by 6.00% each year in 2018-19, 2019-20 and 2020-21, a cumulative increase of 19.10%.²

IPART has assessed the council's application against the criteria in the Office of Local Government (OLG) Guidelines. This report sets out our decision, and explains how and why we reached that decision. Box 1.1 outlines the context for this process.

1.1 We have approved in part Kiama Council's application for a special variation and not approved minimum rate increases

We decided to allow the special variation on a temporary basis for one year. Our decision requires the portion of this increase that is above the 2.3% rate peg to be removed from the council's rate base at the end of 2018-19.

Our decision means that Kiama Council may increase its general income in 2018-19 by the annual percentages shown in Table 1.1. This will allow the council to fund operating and capital expenditure in 2018-19 for its key assets - buildings, roads and bridges, parks and footpaths.³

The council could apply to IPART in future years if it wants a permanent increase in rate revenue to fund these projects and improve its financial sustainability.

Table 1.1 IPART's decision on Kiama Municipal Council's application for a special variation in 2018-19

	2018-19
Percentage increase above the rate peg (temporary)	3.70
Rate peg	2.30
Total increase	6.00

¹ Kiama Municipal Council, *Special Variation Application Form Part A, 2018-19* (Kiama Council, *Application Part A*), Worksheet 1.

² Kiama Council, *Application Part A*, Worksheet 5a

³ Kiama Council, *Application Part A*, Worksheet 6 and *Application Part B*, p 12.

We decided not to approve the requested increase in minimum rates.

Box 1.1 Context for IPART's decision

Each year, IPART sets the rate peg, which is the maximum amount by which councils can increase their general income in that year.

Councils may apply for a special variation that allows them to increase their general income by more than the rate peg. For a single year increase, they apply under section 508(2) of the *Local Government Act 1993* (the Act). For successive year increases (up to a maximum of seven years), they apply under section 508A of the Act.

IPART assesses these applications against the criteria set by the Office of Local Government in its *Guidelines for the preparation of an application for a special variation to general income* (OLG Guidelines).

Councils may also apply to increase their minimum rates above the statutory limit set in the *Local Government (General) Regulation 2005* (clause 126). IPART assesses these applications against criteria for minimum rates increases set by OLG.

The OLG Guidelines emphasise the importance of the council's Integrated Planning and Reporting (IP&R) processes and documents to the special variation process. The IP&R documents, in particular the Delivery Program and Long Term Financial Plan (LTFP), must contain evidence that supports a council's application for a special variation.

The criteria for assessing applications for special variations and increases in minimum rates are listed in Appendix A.

1.2 The council's application for special rates variation does not meet the criteria


We have decided not to approve the special variation in full after assessing Kiama Council's application against the OLG criteria. This is because it has not fulfilled the requirements of Criterion 4.

Criterion 4 requires the council to exhibit (where required), approve and adopt the relevant IP&R documents before the council applies to IPART for a special variation.⁴ The Delivery Program exhibited during public consultation period (November 2017 to January 2018) did not mention the special variation proposal. Subsequently, the council put an updated Delivery Program with the special variation amendments on its website on 24 January 2018. However, this did not provide an adequate time period for the community to consider the proposed special variation, and provide feedback to the council, prior to the council submitting its application to IPART on 12 February 2018.⁵

The exhibited Long Term Financial Plan (LTFP) discusses a 6% special variation compounding over 3 years. However, the exhibited IP&R documents did not discuss the cumulative percentage increase, or the total dollar increase for the average ratepayer, by rating category.

⁴ OLG Guidelines, p 9.

⁵ Kiama Council, *Application Part B*, p 8.








The exhibited LTFP contained only the special variation scenario and did not have comparisons with a base case scenario (ie, a business as usual model that excluded the special variation).⁶ This lack of comparison between a base case and special variation scenario would make it difficult for the community to consider the benefits and costs of the council's proposed special variation and provide meaningful feedback to the council.

Our decision is to approve the council's requested special variation in part. That is, on a temporary basis for one year.

Our assessment against the criteria is summarised in Table 1.2.

⁶ Criterion 1 requires that relevant IP&R documents should canvas alternatives to the rate rise and the LTFP must indicate the financial impact of the base case and special variation scenarios. See *Assessment criteria for special variation applications and minimum rate increases* in Appendix A.

Table 1.2 Assessment of Kiama Municipal Council's special variation application

1. Financial Need	
	<p>The council demonstrated the financial need for the special variation (SV):</p> <ul style="list-style-type: none"> ▼ Operating Performance Ratio (average from 2018-2019 to 2027-28) is <ul style="list-style-type: none"> – 2.2% with SV – -0.2% without SV revenue and assuming SV expenditure. ▼ Infrastructure backlog ratio is estimated at 1.8% in 2027-28 with SV but 4.3% in 2027-28 without SV. ▼ Asset renewals ratio above 100% benchmark to 2027-28 with SV (average 109%), but falls below the benchmark, averaging 78%, without the SV expenditure. <p>However, the IP&R documents, specifically the exhibited Delivery Program and LTFP did not adequately consider the base case and the special variation scenario (see criterion 4).</p>
2. Community awareness	
	<p>On balance, the council demonstrated the community is aware of the rate rise. It:</p> <ul style="list-style-type: none"> ▼ used a range of engagement methods to make the community aware of the need for, and extent of rate increase ▼ provided detailed explanation about the purpose and impact of the SV and sought feedback, and ▼ satisfactorily considered community feedback on the rate increase. <p>However, the council's IP&R documents, specifically the Delivery Program and LTFP did not fully meet the requirements in detailing the extent of the general fund rate rise under the special variation (see criterion 4).</p>
3. Impact on ratepayers	
	<p>Impact on ratepayers will be substantial, as current rate levels are higher than Group 4 and neighbouring councils. However the impact is reasonable as the:</p> <ul style="list-style-type: none"> ▼ rates to income ratio is similar to other councils ▼ outstanding rates ratio is lower than neighbouring councils and the Group 4 average, and ▼ SEIFA ranking (108) is higher than neighbouring councils. <p>We note the council's exhibited Delivery Program and LTFP did not fully meet the requirements in assessing the impact on ratepayers (see criterion 4).</p>
4. IP&R documents exhibited	
	<p>The council did not appropriately update its IP&R documentation. Specifically the:</p> <ul style="list-style-type: none"> ▼ LTFP did not compare a base case with the SV scenario, and did not discuss the full cumulative increase in rates or the impact on ratepayers. ▼ Delivery Program exhibited during the public consultation did not identify the requested SV. The updated Delivery Program with the proposed SV amendments did not provide sufficient time for the community to fully consider the proposed SV. <p>The Delivery Program and LTFP did not fully meet the requirements in considering financial need (criterion 1), community awareness (criterion 2) and impact on ratepayers (criterion 3).</p>
5. Productivity improvements and cost containment	
	<p>Commencing in 2012, the council has implemented cost containment strategies and efficiency measures which resulted in savings of:</p> <ul style="list-style-type: none"> ▼ \$1.26 million from reduced workers compensation insurance premiums ▼ \$187,538 from a procurement optimisation process in 2015-16, and ▼ \$153,000 per year from waste management reductions. <p>The council has also realised additional revenue of \$1.35 million from asset sales. It also included further savings in the LTFP from further optimisation in procurement processes, road surface treatment review, projects design and delivery innovations and environmental initiatives.</p>

1.3 The council's application for minimum rates increases does not meet the criteria




The council proposed an increase to the minimum amount of its business rates by the same 6% increase each year from 2018-19 to 2020-21 as proposed under the special variation.

After assessing the council's minimum rate application, and based on our decision above on the council's special variation application, we have decided not to approve the requested increases in minimum rates.

We have not approved the minimum rate increase, which would have allowed the council to permanently increase its minimum rate. The approved special variation only allows a temporary increase in rates above the peg for one year.

We also found the council's proposed increases did not meet the OLG criteria for minimum rates. In particular, it did not satisfy the requirement to communicate dollar and percentage increases in minimum rates in its community consultation materials. Our assessment against the minimum rates criteria is summarised in Table 1.3.

Table 1.3 Assessment of Kiama Municipal Council's minimum rate application

1. Rationale	
	<p>The council clearly demonstrated the rationale for increasing minimum rates. The purpose of the increase is to:</p> <ul style="list-style-type: none">▼ Maintain consistency with its rating structure, and▼ Avoid skewing rate increases towards ratepayers with higher land values.
2. Impact on ratepayers	
	<p>The impact on ratepayers is not reasonable given we have only allowed the special variation on a temporary basis:</p> <ul style="list-style-type: none">▼ If we had approved the minimum rate application, the minimum rate could have increased by 19.1% to 2020-21, whereas rates on average would only increase by an estimated 7.5% to 2020-21.^a This would shift future rate increases disproportionately onto those paying the minimum rate, which may not be reasonable.▼ Approving the increase for one year only in line with the special variation decision would allow an increase in the minimum rate that would remain permanently after 2018-19, while our special variation decision only allows a temporary increase that would be removed from the rate base after 2018-19.
3. Community awareness	
	<p>The council's consultation was not adequate:</p> <ul style="list-style-type: none">▼ The council did not clearly show the proposed increases in minimum rates in consultation material and it did not show the dollar and percentage increase in minimum amounts in the Delivery Program it exhibited.▼ The council did not seek community feedback on its proposal to increase minimum rates

^a Based on an assumed rate peg of 2.5% in 2019-20 and 2020-21 and absent a future special variation application.

1.4 We have attached conditions on how the council can spend its extra revenue

We have attached conditions to this decision, including that the council uses the income raised from the special variation for purposes consistent with those set out in its application. Box 1.2 summarises these conditions.

Box 1.2 Conditions attached to Kiama Municipal Council's approved special variation

IPART's approval of Kiama Municipal Council's application for a special variation in 2018-19 is subject to the following conditions:

- ▼ The council uses the additional income from the special variation for the purposes of improving financial sustainability, funding capital and operational expenditures and reducing its infrastructure backlog as outlined in the council's application and listed in Appendix B.
- ▼ The council reports in its annual report for year 2018-19 on:
 - expenditure consistent with the council's application and listed in Appendix B, and the reasons for any substantial differences from the proposed expenditure, and
 - the outcomes achieved as a result of the actual program of expenditure.
- ▼ On 1 July 2019, the council is to reduce its general income to what it would have been without the special variation.

1.5 Structure of this report

The rest of this report explains our decision and assessment of the council's application in more detail:

- ▼ Chapter 2 outlines the council's application for the special variation and minimum rates increase.
- ▼ Chapter 3 explains our assessment of the council's application against each criterion.
- ▼ Chapters 4 and 5 discuss how our decision will impact the council and its ratepayers.

2 Kiama Municipal Council's application

Kiama Council applied for a special variation to increase its general income by a cumulative 19.10% over the 3-year period from 2018-19 to 2020-21, and to permanently retain this increase in its general income base.⁷ The proposed increase was 11.62% more than the assumed rate peg increases over the same period.⁸

It also applied for minimum rate increases of a cumulative 19.10% over the 3-year period from 2018-19 to 2020-21.

The council estimates its permissible general income would increase from \$15.67 million in 2017-18 to \$18.66 million in 2020-21 if the requested special variation is approved. Over the 3-year period of the special variation to 2020-21, this would generate additional revenue of \$3.58 million compared to rate increases at the assumed rate peg. This figure would increase to \$17.67 million over a 10-year period, as the additional revenue raised would remain permanently in the council's rate base.

The council indicated it intends to use the additional revenue to fund operating and capital expenditure for its key assets – buildings, roads and bridges, parks and recreation and footpaths – and to improve its financial sustainability.⁹

The council's 2015 Fit for the Future (FFTF) submission proposed a special variation with a cumulative rate increase of 17.40% over the 3-year period from 2018-19 to 2020-21, including the rate peg, and indicated the additional funds raised would be applied to improve its financial sustainability.¹⁰

The council's FFTF Action Plan included the special variation to ensure the future financial sustainability of its asset management program. The council considered it was necessary to increase its rate revenue to meet the operating performance ratio (OPR) within five years, and assist in achieving the required renewal and maintenance of infrastructure to satisfy the FFTF benchmarks.¹¹ It also responds to the NSW Treasury Corporation (TCorp) assessment of the council's financial sustainability in 2013, which recommended the council address its forecast operating deficits and review its forecast level of capital expenditure.¹²

During the 3-year period of the special variation, the council expects to spend \$17.73 million on its capital works program.

The council indicates over the period from 2018-19 to 2027-28 it proposes to spend the additional special variation revenue as follows:

- ▼ \$8.63 million on capital expenditure associated with buildings renewals, including public amenities

⁷ Kiama Council, *Application Part A*, Worksheet 1.

⁸ Based on an assumed rate peg of 2.5% after 2018-19.

⁹ Kiama Council, *Application Part A*, Worksheet 6 and *Application Part B*, p 9.

¹⁰ IPART, *Assessment of Council Fit for the Future Proposals: Appendix C* – Kiama Council, p 251.

¹¹ Kiama Municipal Council, *Fit for the Future Council Improvement Proposal*, June 2015.

¹² TCorp, *Kiama Municipal Council – Financial Assessment and Benchmarking Report*, 3 October 2012, p 31.

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- ▼ \$6.24 million on capital expenditure associated with transport infrastructure
 - ▼ \$2.00 million on increased operating expenditure for park service maintenance, and
 - ▼ \$0.85 million on footpath and buildings operational maintenance.¹³

More detail on the council's proposed program of expenditure to 2027-28 is provided in Appendices B and C.

¹³ Kiama Council, *Application Part A*, Worksheet 6.

3 IPART's assessment

To make our decision, we assessed Kiama Council's application against the criteria in the OLG Guidelines. We also considered the council's most recent IP&R documents, its FFTF proposal, and a range of comparative data about the council set out in Appendix D.¹⁴

We found that the Kiama Council's application did not meet the requirements of the criteria. In particular, the council exhibited IP&R documents that did not contain sufficient information about the proposed special variation increases, and the updated IP&R documents were not exhibited for a sufficient amount of time before being adopted and a special variation application being made to IPART.

Our assessment of the council's application against the criteria is summarised in Table 1.2 and discussed in more detail in the sections below.

3.1 The council demonstrated financial need for the special variation

We found that Kiama Council has demonstrated the need for, and purpose of the requested special variation, which is to:

- ▼ fund asset maintenance, renewal and operational costs, and
- ▼ improve financial sustainability.

However, the council's IP&R documents, specifically the exhibited LTFP did not adequately consider the base case and the special variation scenario (see section 3.5 for a detailed discussion of this issue).

The council's application indicates that the community's priorities were to maintain infrastructure and assets to support the needs of the population.¹⁵

The council has also analysed the financial impact of the special variation on its operating performance, asset maintenance ratio and infrastructure backlog, and canvassed alternative funding strategies.¹⁶

3.1.1 Impact on council's operating performance

The operating performance ratio (OPR) measures whether a council's revenues fund its costs. The OPR is defined as:

¹⁴ See Appendix D. Kiama Council is in OLG Group 4, which is classified as Urban Small/Medium Regional Town/City (population up to 70,000). The group comprises 28 councils, including Port Stephens, Shellharbour City, Byron Shire and Wingecarribee Shire.

¹⁵ Kiama Council, *Application Part B*, p 9.

¹⁶ Kiama Council, *Application Part B*, pp 39-46.

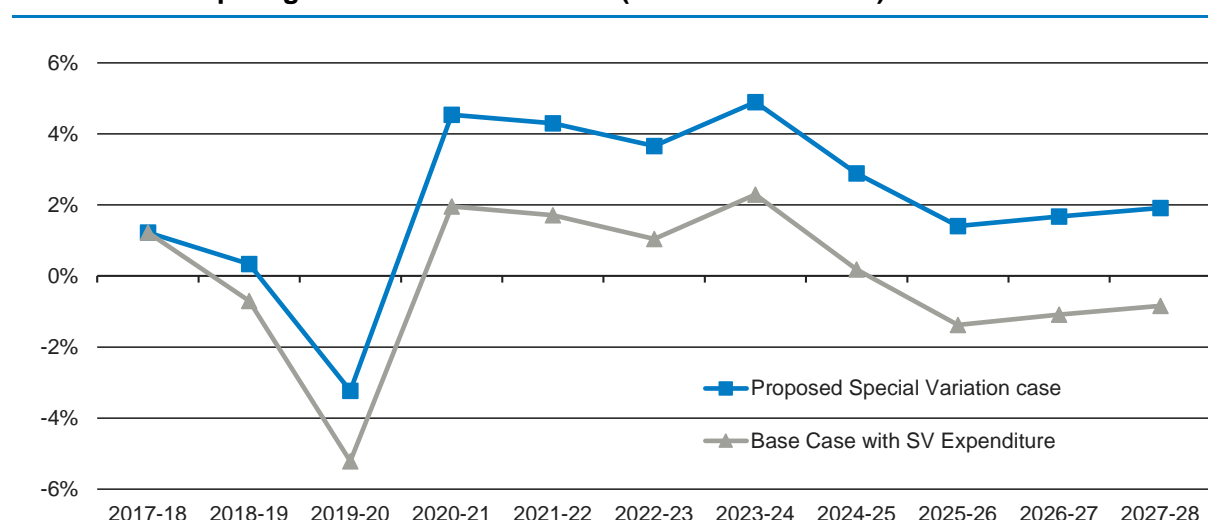
$$OPR^{17} = \frac{\text{Total operating revenue} - \text{operating expenses}}{\text{Total operating revenue}}$$

Under the special variation scenario, the council forecasts consistent operating surpluses, increasing to 1.9% of income by 2020-21.¹⁸ The cumulative value of these forecast surpluses is \$16.64 million to 2027-28.¹⁹ These surpluses would allow the council to reduce its infrastructure backlog and service a growing community.

Without the special variation and assuming its expenditure is the same as under the special variation scenario, it forecasts some surpluses and some deficits to 2027-28, as shown in Figure 3.1 and Table 3.1. The net deficit over the period is \$1.03 million to 2027-28.²⁰ This suggests the council may be less sustainable over the long term if it proceeds with its proposed expenditures without receiving the additional special variation revenue permanently.

The special variation improves the council's financial sustainability and allows it to generate more funds to reduce the infrastructure backlog and spend on asset renewals.

Figure 3.1 Kiama Municipal Council's Operating Performance Ratio (%) excluding capital grants and contributions (2017-18 to 2027-28)



Note 1: The base case with SV expenditure scenario shows the impact on the council's operating position if the special variation projects were to go ahead without the special variation revenue.

Note 2: The council forecasts around \$4 million extra revenue in 2020-21, including fees & charges (\$2 million), interest income (\$1 million) and other revenue (\$1 million), that causes a substantial increase in the forecast OPR

Source: Kiama Council, *Application Part A*, Worksheet 7 and IPART calculations.

¹⁷ Expenditure and revenue in the OPR measure are exclusive of capital grants and contributions, and net gain/loss on sale of assets.

¹⁸ The council has estimated over \$5 million per year in revenue from projected land sales in 2018-19 and 2019-20. The council estimates net gains from asset sales from 2020-21 onwards of over \$800,000 per year, *Kiama Council application attachment, LTFP 2017 – 2021* and IPART calculations.

¹⁹ Kiama Council, *Application Part A*, worksheet 7 and IPART calculations.

²⁰ Kiama Council, *Application Part A*, worksheet 7 and IPART calculations.

Table 3.1 Projected operating performance ratio (%) for Kiama Council's special variation application

	2018-19	2019-20	2020-21	2021-22	2022-23	2023-24	2024-25	2025-26	2026-27	2027-28
Application - including SV	0.3	-3.2	4.5	4.3	3.7	4.9	2.9	1.4	1.7	1.9
Base case with SV expenditure	-0.7	-5.2	2.0	1.7	1.0	2.3	0.2	-1.4	-1.1	-0.8

Source: IPART calculations based on Kiama Council, *Application Part A*, Worksheet 7.

3.1.2 Impact on council's infrastructure backlog

The council estimates that it would cost \$3.30 million to bring its assets to a satisfactory standard, eliminating its infrastructure backlog in 2018-19.²¹ This is consistent with its General Purpose Financial Statements.²²

Measured as a percentage of the written down value of infrastructure assets,²³ the council estimates an infrastructure backlog ratio of 1.36% in 2018-19, which meets the FFTF benchmark of less than 2%. With the special variation expenditure, the council forecasts the infrastructure backlog ratio will be 1.77% in 2027-28.

Without the special variation expenditure, it forecasts the infrastructure backlog will increase to \$11.1 million in 2027-28 as its assets deteriorate, with the infrastructure backlog ratio forecast to be 4.25%, which is substantially above the FFTF benchmark.

Table 3.2 shows the projected infrastructure backlog ratio including and excluding the special variation expenditure.

Table 3.2 Projected infrastructure backlog ratio (%) for Kiama Council's special variation application

	2018-19	2019-20	2020-21	2021-22	2022-23	2023-24	2024-25	2025-26	2026-27	2027-28
Application including SV	1.36	1.45	1.52	1.61	1.61	1.68	1.70	1.70	1.77	1.77
Excluding SV	1.36	1.56	1.87	2.15	2.47	2.81	3.14	3.50	3.88	4.25

Note: These ratios are based on 3 year averages as defined by FFTF.

Source: Kiama Council, Attachment *LTFP Graphs – Scenario Comparison*, worksheet 'Figures'.

3.1.3 Impact on council's infrastructure asset renewal ratio

The council plans to use the special variation funds to spend more on asset renewal and maintenance.

Table 3.3 shows the projected asset renewal ratio including and excluding the special variation expenditure.²⁴ With the special variation expenditure the council meets the (greater than

²¹ Kiama Council, Application, Attachment, *LTFP Graphs – Scenario Comparison*.

²² Kiama Council, *General Purpose Financial Statements*, 2016-17, Special Schedule 7, p 8.

²³ Historical cost less accumulated depreciation.

²⁴ The asset renewal ratio is the amount spent on renewals divided by depreciation, amortisation and impairments.

100%) benchmark over the period to 2027-28. Without the special variation expenditure, the council's asset renewal ratio falls below the benchmark averaging 78% to 2027-28.

Table 3.3 Projected asset renewal ratio (%) for Kiama Council's special variation application

	2018-19	2019-20	2020-21	2021-22	2022-23	2023-24	2024-25	2025-26	2026-27	2027-28	Avg.
Application including SV	98	99	108	112	108	111	114	109	113	117	109
Excluding SV	94	84	75	76	76	79	75	55	85	81	78

Note: These ratios are based on 3 year averages as defined by FFTF.

Source: Kiama Council, Attachment *LTFP Graphs – Scenario Comparison*.

The council's application is similar to its FFTF proposal. Box 3.1 summarises our assessment of Kiama Council's 2015 FFTF proposal.

Box 3.1 FFTF Assessment

IPART's Fit for the Future assessment in 2015 found that Kiama Council:

- ▼ Did not meet the criterion for financial sustainability. The council forecast it would not meet the operating performance benchmark by 2019-20 despite a proposed special variation with a cumulative increase of 17.4% over three years from 2018-19, and would not meet the own source revenue benchmark or the asset renewal benchmark by 2019-20.
- ▼ Met the criterion for infrastructure and service management, as it forecast an improvement in the infrastructure backlog ratio, and the asset maintenance ratio in all years. The council met the debt service benchmark in all forecast years, however it was close to exceeding the debt service benchmark by 2019-20.
- ▼ Did not meet the efficiency criterion based on a forecast increase in real operating expenditure per capita from \$2,200 in 2014-15 to \$2,450 in 2019-20.

TCorp observed in 2013 the council's financial position was 'moderate' and its outlook was 'neutral'.

The council submitted a revised FFTF Proposal to the Office of Local Government (OLG) in May 2017. OLG assessed the council as Fit for the Future based on adjusted revenue and expenditure targets and successfully applying for the proposed special variation.

Source: Kiama Council, *Council Improvement Proposal*, June 2015; IPART, *Assessment of Council Fit for the Future Proposals*, October 2015, pp 251-252; NSW Treasury Corporation (TCorp), *Financial Sustainability of the New South Wales Local Government Sector*, April 2013, p 17; Kiama Council, *SV Application Part B*, 2018, pp 8,27, and Kiama Council, *OLG – Fit For The Future Reassessment report – round 2*, May 2017, p 11.

3.1.4 Alternative funding strategies

In recent years, the council has implemented a number of alternative revenue raising and cost containment strategies to improve financial sustainability. Key strategies include:

- ▼ cost savings from continuous process improvements

- ▼ asset sales, and
- ▼ optimising working capital.²⁵

The council concluded that it still required a special variation to fund the proposed program of works and improve its financial sustainability.

3.2 The council demonstrated community engagement and awareness

We found that Kiama Council demonstrated that its community is aware of the need for and extent of the proposed rate increase through its direct consultation with its community. However, the council's IP&R documentation, specifically its Delivery Program and LTFP did not fully meet the requirement to discuss and assess the impact on ratepayers of the proposed special variation (see section 3.5).

In 2017, the council reviewed some of its IP&R documents in consultation with the community.²⁶ It clearly explained the need for, purpose, and extent of the proposed special variation. In particular, it communicated the full cumulative increase of the special variation in percentage terms in its public consultation.²⁷ Ratepayers could estimate the total increase in dollar terms for the average ratepayer by rate category via a specifically designed tool provided on the council's website.²⁸

The council also provided reasonable opportunities for community feedback, and used a variety of methods to engage with its community including:

- ▼ a council newsletter to every household in November 2017 which detailed the special variation proposal and invited submissions
- ▼ a specific special variation banner on the council's website, linking to a designated FAQ page, which attracted 611 direct hits during the community engagement campaign
- ▼ a council e-news and Facebook account providing regular updates about the special variation
- ▼ community meetings held at four different locations with over 200 people attending, and
- ▼ local radio and television coverage.²⁹

3.2.1 Outcome of consultation with community

Although this criterion does not require councils to demonstrate community support for the special variation, they are required to consider the results of their community consultation in preparing their application. Kiama Council indicated its community's preference was to have a financially sustainable council.³⁰

²⁵ Kiama Council, *Application Part B*, pp 87-91.

²⁶ Detailed discussion of exhibition of IP&R documents is provided in Section 3.5.

²⁷ Kiama Council, *Application Part B*, pp 57-58.

²⁸ Kiama Council, *Application Part B*, p 60.

²⁹ Kiama Council, *Application Part B*, pp 8, 60-63

³⁰ Kiama Council, *Application Part B*, p 12.

Based on this, the council decided to proceed with lodging the special variation application to IPART.

3.2.2 Submissions from the community

The council received 12 written submissions on the special variation application, including 11 opposing the application and one in favour. The main reasons for opposition were:

- ▼ current rates are already too high
- ▼ excessive amounts of money are spent on tourism rather than local priorities, and
- ▼ current services provided are at an unsatisfactory level.

The council has considered its community's feedback by referring to the appropriate council staff to investigate, research and respond.³¹

IPART received two submissions.³² All submissions opposed the special variation, mainly on the grounds that:

- ▼ the council's rates are already too high, and
- ▼ the special variation is not warranted on financial grounds as the council generates substantial additional revenue through land sales for development.

3.3 The impact on ratepayers is substantial but reasonable

As Chapter 2 discussed, Kiama Council requested a 3-year cumulative increase of 19.10% that would remain permanently in the rate base; 6.00% in 2018-19, 2019-20 and 2020-21.

We found that the impact of these increases on ratepayers will be substantial but reasonable, given:

- ▼ current average rate levels
- ▼ the council's rates to income ratio is similar to neighbouring and Group 4 councils
- ▼ its outstanding rates ratio is below neighbouring and Group 4 councils, and
- ▼ the economic conditions in Kiama, and its median household income are higher than neighbouring and Group 4 councils.

3.3.1 Council's consideration of impact on ratepayers

The council considers the existing community has the capacity and willingness to pay. The council conducted multiple surveys of the community and identified community dissatisfaction with key infrastructure assets, particularly the road network, parks and footpaths.³³

The council also examined socio-economic indicators for its local government area. It found:

³¹ Kiama Council, *Application Part B*, p 65.

³² We also received some submissions received outside our consultation period.

³³ Kiama Council, *Application Part B*, pp 16-19.

- ▼ employment is increasing, with a 9% increase in jobs from 2011 to 2016
- ▼ the unemployment rate was 2.7% compared to a NSW average of 4.6% in June 2017
- ▼ there was higher economic growth, averaging 4.3% per year over the past 6 years, compared to 2.6% per year for the Illawarra region, and
- ▼ Kiama has a higher income level, and a relatively high SEIFA ranking compared with neighbouring councils.³⁴

The council submitted that it also has a hardship policy available to all ratepayers, and offers a rate deferral scheme for ratepayers who cannot afford to pay the full amount of their rates.³⁵ The council decided to provide an additional pensioner rebate in order to offset a portion of the proposed special variation increase.³⁶

3.3.2 IPART's assessment of impact on ratepayers

To assess the reasonableness of the impact of the special variation on ratepayers, we examined the council's special variation history and the average annual growth of rates in various rating categories. We found that since 2007-08:

- ▼ the council has applied for and been granted three special variations that were used for infrastructure maintenance and renewal, improving the council's financial sustainability and for funding road network renewal works, and
- ▼ the average annual growth in residential rates was 3.48% and 5.12% for business rates, which is higher than the average annual growth in the rate peg of 2.7% over the same period.

We also compared current rates and socio economic indicators in the LGA with OLG Group 4 and neighbouring councils as shown in Table 3.4.

³⁴ Kiama Council, *Application Part B*, pp 73-75 and 77-78.

³⁵ Kiama Council, *Application Part B*, pp 79-80.

³⁶ Kiama Council, *Application Part B*, pp 80-81.

Table 3.4 Kiama Municipal Council- comparison of rates and socio-economic indicators with neighbouring councils and Group 4 averages (2015-16)

Council (OLG Group)	Average residential rate (\$) ^a	Average business rate (\$)	Median annual household income (2016) ^b	Average rate to median income ratio (%)	Outstanding rates ratio (%)	SEIFA Index NSW Rank ^c
Shellharbour City (4)	1,287	4,442	69,836	1.8	4.6	66
Shoalhaven City (5)	934	2,167	51,584	1.8	5.0	50
Wollongong City (5)	1,283	11,340	69,628	1.8	4.8	94
Wingecarribee Shire (4)	1,238	3,637	69,420	1.8	3.1	100
Kiama (4)	1,342	2,178	78,468	1.7	2.2	108
OLG Group 4 Average	1,013	3,619	62,656	1.6	4.5	-

a The average residential rate (ordinary and special) is calculated by dividing total Ordinary Rates revenue by the number of assessments in the category.

b Median annual household income is based on 2016 ABS Census data.

c The highest possible ranking is 130 which denotes a council that is least disadvantaged in NSW.

Source: OLG, *Time Series Data 2015-2016*; ABS, *Socio-Economic Indexes for Areas (SEIFA) 2016*, March 2018; ABS, 2016 Census DataPacks, General Community Profile, Local Government Areas, NSW, *Median Weekly Household Income* and IPART calculations.

Based on 2015-16 data, we found that Kiama Council's:

- ▼ median household income was higher than the average for Group 4 councils and neighbouring councils
- ▼ outstanding rates ratio of 2.2% was lower than the average of 4.5% for Group 4 councils and lower than neighbouring councils
- ▼ SEIFA ranking of 108 is second highest in the OLG group ⁴³⁷ indicating the area is less disadvantaged compared with other councils in this group
- ▼ average residential rate (\$1,342) was 32% higher than the average for Group 4 councils and 13% higher than neighbouring councils
- ▼ average business rate (\$2,178) was 40% lower than the average for Group 4 councils and 60% lower than neighbouring councils, and
- ▼ average rate to income ratio was 6% higher than the average for Group 4 councils and 6% lower than neighbouring councils.

Taking all these factors into account, we consider that the impact of the increases is substantial but reasonable.

3.4 The proposed increase in minimum rates is not reasonable

Kiama Council also requested a 3-year cumulative increase of 19.10% for its minimum business rates: 6.00% in 2018-19, 6.00% in 2019-20 and 6.00% in 2020-21.

We decided not to approve the minimum rate increases based on our finding that the council does not meet all the assessment criteria for minimum rates as discussed in the sections below.

³⁷ Queanbeyan-Palerang Regional Council has a SEIFA rank of 110, which is highest in OLG group 4.

3.4.1 The council explained its rationale for increasing minimum rates

We found that Kiama Council explained its rationale for increasing minimum rates.

There are currently 240 ratepayers in one business sub-category currently paying the minimum amount (\$702 in 2017-18). As seen in Table 3.5 this represents 50.5% of the sub-category subject to a minimum rate and 43.4% of all business ratepayers.

Table 3.5 Kiama Council - Ratepayer assessments on minimum rates

Rating category	Number of assessments on minimum rates	Number of assessments on ordinary rates	Total number of assessments	Proportion of assessments on minimum rates (%)
Commercial/Industrial	240	235	475	50.5
Other business rates categories	0	78	78	
Total Business	240	313	553	43.4

Note: The council does not have minimum rates for its residential or farmland categories.

Source: Kiama, *Application Part A*, Worksheet 3 and Worksheet 5a and IPART calculations.

The council submitted that it took into account the number of ratepayers on the minimum rate for this sub-category and decided to increase the minimum rate by the same percentage as the special variation to ensure:

- ▼ consistency with its rating structure, and
- ▼ that rate increases would not be skewed towards other ratepayers with higher land values in the same ratepayer categories.³⁸

3.4.2 The impact on ratepayers is not reasonable

While the council explained the rationale for increasing its minimum rate, we found that the impact on ratepayers from an increase in the minimum amount is not reasonable as:

- ▼ Approval of the 3-years requested would result in an increase of 19.1% in minimum rates to 2020-21 (11.6% more than the assumed rate peg). Under our special variation decision, rates on average would rise by an estimated 7.5% to 2020-21.³⁹ Hence, approving the minimum rate application would shift future rate increases disproportionately onto those paying the minimum rate, which may not be reasonable.
- ▼ Approval of an increase for one year only in line with our special variation decision would allow an increase in the minimum rate that remains permanently in the rate base from 2018-19, while our special variation decision allows a temporary increase that would be removed from the rate base after 2018-19.

Had we approved the special variation as requested, the minimum rate increase would have been reasonable as it would have maintained the same percentage rate increase and rating burden between ratepayers.

³⁸ Kiama, *Application Part B*, p 69-70.

³⁹ Based on an assumed rate peg of 2.5% in 2019-20 and 2020-21 and absent a future special variation application.

3.4.3 The council did not adequately consult the community on minimum rates

We found that the council did not adequately consult the community on minimum rates as:

- ▼ it did not specifically set out the proposed minimum rate increases either in its community consultation material or in its latest Delivery Program, and
- ▼ the council did not seek community feedback on its proposal to increase minimum rates.

3.5 The council's IP&R documents were not exhibited according to the guidelines

The council adopted its Community Strategic Plan in June 2017.⁴⁰ It exhibited its Delivery Program and Long Term Financial Plan between 16 May 2017 and 16 June 2017 and adopted these documents on 22 June 2017.⁴¹ The exhibited Delivery Program did not mention the special variation.

An amended Delivery Program with the full description of the SV scenario was exhibited for community review on 24 January 2018.⁴² The council applied to IPART for the special variation on 12 February 2018. The OLG Guidelines require the Delivery Program to be publicly exhibited for 28 days prior to the council applying to IPART for a special variation. The council did not provide the community with sufficient time, or a 28 day period, to consider and provide feedback on the Delivery Program prior to the council making its application on 12 February. The council also did not allow sufficient time to consider any community feedback before making its application.

The exhibited LTFP discusses a 6% special variation compounding over 3 years. However, the exhibited IP&R documents did not discuss the full cumulative percentage increase, or the total increase in dollar terms for the average ratepayer, by rating category.

The exhibited LTFP contained the special variation scenario only. It did not compare this scenario with a base case scenario reflecting the business as usual model excluding the special variation, as required under Criterion 1 of the OLG guidelines.⁴³

Without the base case, the community did not have access to all the information to fully consider the proposed special variation. This could have made it difficult for the community to provide meaningful feedback to the council because the LTFP lacked the required comparison of the base case and special variation scenarios.

3.6 The council explained its productivity improvements and cost containment strategies

The Kiama Council's application sets out the productivity improvement and cost containment initiatives it has undertaken in recent years and plans to implement in the future.

In particular, it submitted that it had achieved past savings and cost containment through:

⁴⁰ Kiama Council, *Application Part B*, p 84.

⁴¹ Kiama Council, *Application Part B*, p 84.

⁴² Kiama Council, *Application Part B*, p 85.

⁴³ See Criterion 1 in Appendix A.

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- ▼ expense reduction initiatives, such as a safety audit – resulting in \$1.26 million cumulative savings from reduced workers compensation insurance premiums between 2012-13 and 2016-17
 - ▼ procurement cost reductions resulting in savings of 1.75% for materials and contracts costs which is equivalent to \$187,538 for 2015-16
 - ▼ a waste management strategy for landfill waste reduction with estimated savings of \$153,000 per year
 - ▼ a property portfolio review which resulted in some asset remediation, redevelopment and realisation, with proceeds reinvested into key infrastructure projects, and
 - ▼ identification of future asset disposal opportunities.⁴⁴

The council also indicated it has included efficiency initiatives in its current 10-year Long Term Financial Plan including:

- ▼ procurement costs savings of \$350,000 to \$400,000 per year
- ▼ a review of road surface treatment and reseal operations to improve road quality and optimise expenditure
- ▼ reducing the costs of development assessments
- ▼ a preventative asset maintenance program to reduce costs, and
- ▼ environmental and energy savings initiatives of about \$360,000 per year.⁴⁵

⁴⁴ Kiama Council, *Application Part B*, pp 86-92.

⁴⁵ Kiama Council, *Application Part B*, pp 92-93.

4 Our decision's impact on the council

Our decision means Kiama Council may increase its general income in 2018-19 by 6.00% or \$933,598 as indicated in Table 4.1. Although Kiama Council sought a permanent increase, we have approved a temporary increase for one year. Our decision requires the increase above the 2.3% rate peg, approximately \$580,000, to be removed from the council's rate base at the end of 2018-19.⁴⁶

Table 4.1 shows the percentage increase we have approved, and estimates the annual increase in the dollar amount to the council's general income incorporating adjustments that will occur as a result of various catch-up and valuation adjustments. The effect on the council's general income is shown in Table 4.1.

Table 4.1 Permissible general income of Kiama Municipal Council for 2018-19 arising from the special variation approved by IPART

Year	2017-18	2018-19
Cumulative increase approved (%)		6.00
Annual increase in general income ^a		933,598
Permissible general income	15,674,515	16,608,113

^a An annual increase for 2018-19 includes an adjustment for the excess from the previous years of \$6,873.

Note: The above information is correct at the time of the council's application (February 2018).

Source: Kiama council *Application Part A*, Worksheets 1 and 4 and IPART calculations.

This extra income is the amount the council requested in year one of its special variation application to enable it to fund asset maintenance and capital renewal costs, and address the infrastructure backlog. It gives the council the necessary time to update its IP&R documentation and apply to IPART for a permanent increase in future years, if it chooses.

⁴⁶ General income in future years cannot be determined with precision, as it will be influenced by several factors in addition to the rate peg. These factors include changes in the number of rateable properties and adjustments for previous under- or over-collection of rates. The Office of Local Government is responsible for monitoring and ensuring compliance.

5 Our decision's impact on ratepayers

IPART sets the allowable increase in general income, but it is a matter for each council to determine how it allocates any increase across different categories of ratepayer, consistent with our determination.

In its application, Kiama Council indicated it intended to increase rates uniformly by 6.00% per year over the three years, or 19.10% in total, for each category.

The council has calculated that:

- ▼ the average residential rate would increase by 6.0% or \$86 in 2018-19
- ▼ the average business rate would increase by 6.0% or \$139 in 2018-19, and
- ▼ the average farmland rate would increase by 6.0% or \$147 in 2018-19.⁴⁷

Table 5.1 sets out Kiama Council's estimates of the expected increase in average rates in each ratepayer category.

Table 5.1 Indicative annual increases in average rates under Kiama Municipal Council's approved special variation in 2018-19

Rating category	Average rate 2017-18 (\$)	Increase (%)	Increase (\$)	Average rate 2018-19 (\$)
Residential	1,431	6.0	86	1,517
Business	2,298	6.0	139	2,437
Farmland	2,454	6.0	147	2,601

Note: 2017-18 is included for comparison. The average rate is calculated by Kiama Council, and includes the ordinary rate and any special rates applying to the rating category.

Source: Kiama Council, *Application Part A*, Worksheet 5a.

⁴⁷ Kiama Council, *Application Part A*, Worksheet 5a.



Appendices



A Assessment criteria for special variation applications and minimum rate increases

Table A.1 Assessment criteria for special variation applications

Assessment criteria

Criterion 1 – Financial need

The need for and purpose of a different revenue path for the council's General Fund (as requested through the special variation) is clearly articulated and identified in the council's IP&R documents, in particular its Delivery Program, Long Term Financial Plan and Asset Management Plan where appropriate.

In establishing need for the special variation, the relevant IP&R documents should canvas alternatives to the rate rise. In demonstrating this need councils must indicate the financial impact in their Long Term Financial Plan applying the following two scenarios:

- ▼ Baseline scenario – General Fund revenue and expenditure forecasts which reflect the business as usual model, and exclude the special variation, and
- ▼ Special variation scenario – the result of implementing the special variation in full is shown and reflected in the General Fund revenue forecast with the additional expenditure levels intended to be funded by the special variation.

Evidence to establish this criterion could include evidence of community need/desire for service levels/project and limited council resourcing alternatives. Evidence could also include analysis of council's financial sustainability conducted by Government agencies.

Criterion 2 – Community awareness

Evidence that the community is aware of the need for and extent of a rate rise. The Delivery Program and Long Term Financial Plan should clearly set out the extent of the General Fund rate rise under the special variation. The council's community engagement strategy for the special variation must demonstrate an appropriate variety of engagement methods to ensure community awareness and input occur. The IPART fact sheet includes guidance to councils on the community awareness and engagement criterion for special variations. In particular, councils need to communicate the full cumulative increase of the proposed SV in percentage terms, and the total increase in dollar terms for the average ratepayer, by rating category.

Criterion 3 – Impact on ratepayers is reasonable

The impact on affected ratepayers must be reasonable, having regard to both the current rate levels, existing ratepayer base and the proposed purpose of the variation. The Delivery Program and Long Term Financial Plan should:

- ▼ clearly show the impact of any rate rises upon the community
- ▼ include the council's consideration of the community's capacity and willingness to pay rates, and
- ▼ establish that the proposed rate increases are affordable having regard to the community's capacity to pay.

Criterion 4 – IP&R documents are exhibited

The relevant IP&R documents must be exhibited (where required), approved and adopted by the council before the council applies to IPART for a special variation to its general income.

Criterion 5 – Productivity improvements and cost containment strategies

The IP&R documents or the council's application must explain the productivity improvements and cost containment strategies the council has realised in past years, and plans to realise over the proposed special variation period.

Criterion 6 – Additional matters

IPART's assessment of the size and resources of the council, the size of the increase requested, current rate levels and previous rate rises, the purpose of the special variation and other relevant matters.

Source: OLG Guidelines, November 2017, pp 7-9.

Table A.2 Assessment criteria for minimum rate increase applications

Assessment criteria
Criterion 1 – Rationale The rationale for increasing minimum rates above the statutory limit.
Criterion 2 – Impact on ratepayers The impact on ratepayers, including the level of the proposed minimum rates and the number and proportion of ratepayers that will be on the minimum rates, by rating category or sub-category.
Criterion 3 – Community awareness The consultation the council has undertaken to obtain the community's views on the proposal.

Source: Office of Local Government, *Guidelines for the preparation of an application to increase minimum rates above the statutory limit*, November 2017, p 8.

B Expenditures to be funded from the special variation above the rate peg

Table B.1 and Table B.2 show Kiama Council's proposed expenditure of the special variation funds over the next 10 years.

The council will use the additional special variation revenue, above the rate peg, of \$0.58 million in 2018-19 to fund:

- ▼ \$221,564 on operating expenditure, and
- ▼ \$419,362 on capital expenditure.⁴⁸

As a condition of IPART's partial approval, the council will indicate in its 2018-19 Annual Report how its actual expenditure compares with this proposed program of expenditure.

⁴⁸ Kiama Council, *Application Part A*, Worksheet 6.

Table B.1 Kiama Municipal Council– Income and proposed expenditure over 10-years related to the special variation (\$000)

	2018-19	2019-20	2020-21	2021-22	2022-23	2023-24	2024-25	2025-26	2026-27	2027-28	Total
Special variation income above assumed rate peg	580	1,176	1,821	1,867	1,913	1,961	2,010	2,061	2,112	2,165	17,667
Funding for increased operating expenditures	222	234	248	262	276	291	306	322	338	354	2,853
Funding for capital expenditure	419	867	1,405	1,345	1,839	1,848	1,857	3,110	1,085	1,100	14,875
Total expenditure	641	1,101	1,653	1,607	2,116	2,139	2,163	3,432	1,423	1,454	17,728

Note: Numbers may not add due to rounding. Total special variation expenditure equals funding for increased operating expenditures plus funding for capital expenditure.

Source: Kiama Council, *Application Part A*, Worksheet 6.

Table B.2 Kiama Municipal Council– Proposed 10-year capital expenditure program related to the special variation (\$000)

	2018-19	2019-20	2020-21	2021-22	2022-23	2023-24	2024-25	2025-26	2026-27	2027-28	Total
Buildings Renewals	348	867	1,405	1,176	339	348	357	1,610	1,085	1,100	8,634
Transport Infrastructure renewals	72	-	-	169	1,500	1,500	1,500	1,500	-	-	6,241
Total Capital Expenditure	419	867	1,405	1,345	1,839	1,848	1,857	3,110	1,085	1,100	14,875

Note: Numbers may not add due to rounding.

Source: Kiama Council, *Application Part A*, Worksheet 6.

C Kiama Municipal Council's projected revenue, expenses and operating result

As a condition of IPART's approval, Kiama Council is to report in 2018-19 against its projected revenue, expenses and operating balance as set out in its Long Term Financial Plan (shown in Table C.1).

Revenues and operating results in the annual accounts are reported both inclusive and exclusive of capital grants and contributions. To isolate ongoing trends in operating revenues and expenses, our analysis of the council's operating account in the body of this report excludes capital grants and contributions.

Table C.1 Summary of projected operating statement for Kiama Municipal Council, 2018-19 to 2027-28 (\$000)

	2018-19	2019-20	2020-21	2021-22	2022-23	2023-24	2024-25	2025-26	2026-27	2027-28
Total revenue	62,747	69,730	71,175	73,020	74,354	75,775	76,250	77,045	79,185	81,183
Total expenses	56,204	64,338	66,052	67,976	69,743	70,146	72,089	73,972	75,871	77,646
Operating result from continuing operations	6,542	5,391	5,123	5,044	4,611	5,629	4,162	3,073	3,314	3,537
Net operating result before capital grants and contributions	5,368	3,217	3,948	3,870	3,436	4,454	2,987	1,899	2,139	2,363

Note: Numbers may not add due to rounding.

Source: Kiama Council, *Application Part A*, Worksheet 7.

D Comparative indicators

Performance indicators

Indicators of council performance may be considered across time, either for one council or for a group of similar councils, or by comparing similar councils at a point in time.

Table D.1 shows how selected performance indicators for Kiama Council have changed over the four years to 2015-16. Table D.2 compares selected published and unpublished data about Kiama Council with the averages for the councils in its OLG Group, and for NSW councils as a whole.

Overall, the tables show that:

- ▼ Full-Time Equivalent (FTE) staff has grown at 1.66% per year, but the ratio of population to FTE has remained stable.
- ▼ The council's number of FTE staff is lower than the OLG Group 4 average at 270 versus 343 respectively. However, its average cost per FTE, \$91,900 and employee costs as a percentage of total expenditures, 46.7% are higher than the Group average at \$79,862, and 38.4% respectively.

Table D.1 Trends in selected performance indicators for Kiama Municipal Council, 2012-13 to 2015-16

Performance indicator	2012-13	2013-14	2014-15	2015-16	Average annual change (%)
FTE staff (number)	257	265	338	270	1.66
Ratio of population to FTE	82	80	64	82	-0.02
Average cost per FTE (\$)	86,163	83,955	68,050	91,900	2.17
Employee costs as % operating expenditure (General Fund only)	44.9	40.0	44.3	46.7	N/A

Note: Except as noted, data is based upon total council operations that include General Fund, Water & Sewer and other funds, if applicable.

Source: OLG, unpublished data.

Table D.2

Select comparative indicators for Kiama Municipal Council, 2015-16

	Kiama Council	OLG Group 4 average	NSW average
General profile			
Area (km ²)	258	-	-
Population	22,044	-	-
General Fund operating expenditure (\$m)	53.2	63.1	70.2
General Fund operating revenue per capita (\$)	3,108	-	-
Rates revenue as % General Fund income	27.5	39.5	43.6
Own-source revenue ratio (%)	59.8	65.8	67.3
Average rate indicators^a			
Average rate – residential (\$)	1,342	1,013	1,017
Average rate – business (\$)	2,178	3,619	5,118
Average rate – farmland (\$)	2,369	2,029	2,366
Socio-economic/capacity to pay indicators			
Median annual household income, 2016 (\$) ^b	78,468	62,656	77,272
Average residential rate to median income ratio (%)	1.7	1.6	1.3
SEIFA, 2016 (NSW rank: 130 is least disadvantaged)	108		
Outstanding rates and annual charges ratio (%)	2.2	4.4	3.6
Productivity (labour input) indicators^c			
FTE staff (number)	270	343	354
Ratio of population to FTE	81.6		
Average cost per FTE (\$)	91,900	79,862	83,193
Employee costs as % operating expenditure (General Fund only)	46.7	38.4	39.7

^a Average rates equal total ordinary rates revenue divided by the number of assessments in each category.

^b Median annual household income is based on 2016 ABS Census data.

^c Data includes General Fund, Water & Sewer and other funds, if applicable (unless noted otherwise). There are difficulties in comparing councils using this data because councils' activities differ widely in scope and they may be defined and measured differently between councils.

Note: Except as noted, data is based upon total council operations for General Fund only.

Source: OLG, *Time Series Data 2015-2016*, OLG, unpublished data; ABS, *Socio-Economic Indexes for Areas (SEIFA) 2016*, March 2018, ABS, 2016 Census DataPacks, General Community Profile, Local Government Areas, NSW, *Median Weekly Household Income* and IPART calculations.