



Independent Pricing and Regulatory Tribunal  
New South Wales

# Special variation increase

## Muswellbrook Shire Council 2018-19

Determination  
Local Government

May 2018

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## Tribunal Members

The Tribunal members for this review are:

Dr Peter J Boxall AO, Chair

Mr Ed Willett

Ms Deborah Cope

Enquiries regarding this document should be directed to a staff member:

Lucy Garnier (02) 9290 8488

Elizabeth Harloe (02) 9113 7725



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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.

Muswellbrook Shire Council (Muswellbrook Council) applied for a single-year special variation to:

- ▼ increase its general income by 14.73% in 2018-19, and
- ▼ retain this increase in its rate base permanently.<sup>1</sup>

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 overleaf outlines the context for this process.

## 1.1 We have approved in part Muswellbrook Council's application for a special variation

We decided to allow the special variation on a temporary basis for one year. Our decision means that Muswellbrook Council may increase its general income by 14.73% in 2018-19, including the rate peg of 2.3%. 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.

This decision allows the council to begin funding its proposed suite of projects, including the development of a regional entertainment and conference centre, and the Olympic Park Precinct upgrade. Alternatively, it may choose to commence a selection of the proposed projects in 2018-19, rather than the complete suite.

The council could reapply to IPART in future years if it wants a permanent increase in rate revenue to fund these projects over the long term.

**Table 1.1 IPART's decision on Muswellbrook Shire Council's application for a special variation in 2018-19**

	%
Percentage increase above the rate peg (temporary)	12.43
Rate peg	2.30
Total increase	14.73

<sup>1</sup> Muswellbrook Council, *Special Variation Application Form Part A 2018-19* (Muswellbrook Council, *Application Part A*), Worksheet 1.

### 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 (OLG) in its *Guidelines for the preparation of an application for a special variation to general income* (OLG Guidelines).

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, must contain evidence that supports a council's application for a special variation.

The criteria for assessing applications for special variations are listed in Appendix A.

## 1.2 The council's application does not meet the criteria

We have decided not to approve the special variation in full after assessing Muswellbrook Council's application against the OLG's 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.<sup>2</sup> The council did not exhibit its IP&R documents containing the proposed 2018-19 special variation and showing the impact on the community before applying to IPART.<sup>3</sup> However, the council did communicate and consult with the community on the proposal using alternative engagement strategies.

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

Our assessment against each criterion is summarised in Table 1.2.






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<sup>2</sup> OLG Guidelines, p 9.

<sup>3</sup> Letter from Muswellbrook Shire Council to IPART Secretariat dated 26 February 2018.



**Table 1.2 Assessment of Muswellbrook Shire 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"> <li>▼ Operating Performance Ratio (average 2018-19 to 2027-28) is <ul style="list-style-type: none"> <li>– 1.9% with SV</li> <li>– 0.9% base case</li> <li>– -3.2% base case with SV expenditure, suggesting the council needs extra revenue if it proceeds with \$26 million of proposed projects</li> </ul> </li> <li>▼ Current net cash position is 13.0% of annual income <ul style="list-style-type: none"> <li>– It is forecast to fall to 2.6% by 2027-28 with SV</li> <li>– The council moves to a net <b>debt</b> position of 41.6% of income by 2027-28 without the SV revenue and with SV expenditure.</li> </ul> </li> </ul>
2. Community awareness	
	<p>The council demonstrated the community is aware of the rate rise. It:</p> <ul style="list-style-type: none"> <li>▼ Used a range of engagement methods to make the community aware of the need for and extent of rate increase</li> <li>▼ Provided detailed explanation about the purpose and impact of the SV and sought feedback</li> <li>▼ Satisfactorily considered community feedback on the rate increase</li> </ul> <p>Although the council demonstrated the community was widely aware of the rate rise, we note the council did not exhibit IP&amp;R documents containing the proposed SV.</p>
3. Impact on ratepayers	
	<p>Impact on ratepayers will be substantial but reasonable:</p> <ul style="list-style-type: none"> <li>▼ Current residential rate levels are similar to neighbouring and Group 11 councils</li> <li>▼ Current average business rates are similar to Group 11 councils</li> <li>▼ Rates to income ratio is lower than neighbouring and Group 11 councils</li> <li>▼ Outstanding rates ratio comparable with neighbouring and Group 11 councils</li> <li>▼ However, SEIFA ranking of 22 is in the lower quartile amongst NSW councils demonstrating that Muswellbrook Council has a relatively high level of disadvantage.</li> </ul>
4. IP&R documents exhibited	
	<p>The council did not adequately exhibit or update relevant IP&amp;R documents before applying to IPART:</p> <ul style="list-style-type: none"> <li>▼ The council's current Delivery Program contains details of a special variation sought in the previous year (2017-18).</li> <li>▼ The Long Term Financial Plan containing the 2018-19 special variation was not exhibited before applying to IPART. It was published on its website after applying to IPART for the SV</li> </ul>
5. Productivity improvements and cost containment	
	<p>Over the past three years, the council has realised annual savings of over \$300,000 per year in operating expenditure. Initiatives included:</p> <ul style="list-style-type: none"> <li>▼ An organisational review resulting in a staff reduction (\$250,000 pa)</li> <li>▼ Energy efficiency measures such as reticulated water use and solar PV generation (\$50,000 pa)</li> <li>▼ A review of its RMS maintenance contract (\$80,000 pa).</li> </ul>

### 1.3 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 Muswellbrook Shire Council's approved special variation**

IPART's approval of Muswellbrook Shire 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 funding operating and capital expenditure as outlined in the council's application and listed in Appendix B.
- ▼ The council reports in its annual report for 2018-19 on:
  - expenditure consistent with the council's application and listed in Appendix B, and the reasons for any significant 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 adjust its general income to what it would have been without the special variation.

### 1.4 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
- ▼ 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 Muswellbrook Shire Council's application

Muswellbrook Council applied for a special variation to increase its general income by 14.73% in 2018-19, and to permanently retain this increase in its general income base.<sup>4</sup>

In 2017, the council applied for a special variation requesting a 20.4% cumulative increase in rates over four years from 2017-18. IPART decided not to approve the 2017 special variation because the council did not make the community sufficiently aware of the rate rise and appropriately update its IP&R documents prior to applying to IPART.<sup>5</sup>

The council estimated that if its current application for a special variation in 2018-19 was approved, its permissible general income (PGI) would increase from \$12.8 million in 2017-18 to \$14.7 million in 2018-19.<sup>6</sup> Over the one-year period of the special variation in 2018-19, this would generate additional revenue of \$1.6 million compared to rate increases at the rate peg. If the special variation had been fully approved as requested, the PGI would have increased to \$18.4 million over a 10-year period, as the additional revenue raised would have remained permanently in the council's rate base.

The council proposes to spend \$26 million over 2018-19 to 2020-21 on two major capital projects:

- ▼ the development of a Regional Entertainment and Conference Centre (\$15 million cost)
- ▼ the development of the Olympic Park Precinct Upgrade (\$11 million cost).

The council proposes to fund these two capital projects through:

- ▼ a loan of \$11.8 million
- ▼ successfully applying for government grants of \$10.5 million, and
- ▼ revenue from voluntary planning agreements of \$3.7 million.<sup>7</sup>

The council proposes to use the special variation to fund:

- ▼ the interest and principal payments on the loan for the two capital projects
- ▼ the operating costs for the Entertainment Centre (the council estimates net costs of \$595,000 in 2020-21, rising to just over \$700,000 in 2027-28)
- ▼ the operating costs for the Olympic Park (around \$100,000 per year from 2020-21)
- ▼ improved stormwater management (\$300,000 annually)
- ▼ roads and parks asset maintenance (\$100,000 annually)

<sup>4</sup> Muswellbrook Council, *Application Part A*, Worksheet 1.

<sup>5</sup> IPART, *Muswellbrook Shire Council's application for a special variation for 2017-18*, May 2017, p 2.

<sup>6</sup> Muswellbrook Council, *Application Part A*, Worksheet 4.

<sup>7</sup> Letter from Muswellbrook Shire Council to IPART Secretariat dated 27 March 2018.

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- ▼ a job creation program (\$250,000 annually), and
  - ▼ a shortfall in mining rates resulting from a change in NSW Government policy (\$62,000 annually).<sup>8,9</sup>

Appendix B contains further detail on the council's proposed program of expenditure.

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<sup>8</sup> Note that Muswellbrook Council has forecast that these operating expenses will increase at 2.5% annually.

<sup>9</sup> Muswellbrook Council, *Application Part A*, Worksheet 6, and Muswellbrook Council, *Application Part B*, p 7.

## 3 IPART's assessment

To make our decision, we assessed Muswellbrook Council's application against the criteria in the OLG Guidelines. We also considered the council's most recent IP&R documents, and a range of comparative data about the council set out in Appendix C.<sup>10</sup>

We found that Muswellbrook Council's application did not meet the requirements of the criteria. In particular, we were not satisfied that the council demonstrated that its IP&R documents containing the relevant information on the 2018-19 special variation had been exhibited before applying to IPART.

Table 1.2 summarises our assessment of the council's application against the OLG's criteria. The sections below discuss our assessment in more detail.

### 3.1 The council demonstrated financial need for the special variation

We found that Muswellbrook Council's application for a special variation set out the need for, and purpose of the requested special variation. This is to fund a suite of projects, including the development of a regional entertainment and conference centre, and the Olympic Park Precinct upgrade.

Muswellbrook Council's revised Long Term Financial Plan<sup>11</sup> (LTFP) adequately sets out the need for, and purpose of the requested special variation. The council's application notes the community's priorities were to maintain infrastructure and assets to support the needs of the population as well as provide additional infrastructure to position Muswellbrook as a regional centre.<sup>12</sup>

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

#### 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:

$$OPR^{13} = \frac{\text{Total operating revenue} - \text{operating expenses}}{\text{Total operating revenue}}$$

<sup>10</sup> Muswellbrook Council is in OLG Group 11, which is classified as Rural Very Large. The group includes Upper Hunter Shire, Bellingen Shire, Cabonne and Inverell Shire councils.

<sup>11</sup> Muswellbrook Council, *Long Term Financial Plan 2019-2028*, February 2018.

<sup>12</sup> Muswellbrook Council, *Application Part B*, p 24.

<sup>13</sup> Expenditure and revenue in the OPR measure are exclusive of capital grants and contributions, and net gain/loss on sale of assets.



Figure 3.1 shows the OPR under three scenarios:

- ▼ The **proposed special variation case**: the OPR would be 1.9% on average from 2018-19 to 2027-28, assuming we had approved a 14.73% special variation on a permanent basis.
- ▼ The **base case scenario**: with no additional special variation revenue and associated expenditure, showing the council generating a modest ongoing operating surplus.
- ▼ The **base case with special variation expenditure**: the OPR would average -3.2% over the same period if Muswellbrook Council incurred the expenses proposed without receiving the special variation revenue.

Under the special variation scenario applied for by the council, it forecasts consistent operating surpluses, growing to 2% by 2027-28. The cumulative value of these forecast surpluses is \$7.90 million to 2027-28.<sup>14</sup> This suggests the council could fund its proposed projects and be financially sustainable over the long term if the special variation had been fully approved. Similarly, if the council does not receive the special variation and does not proceed with the special variation expenditure, the council is forecast to be financially sustainable.

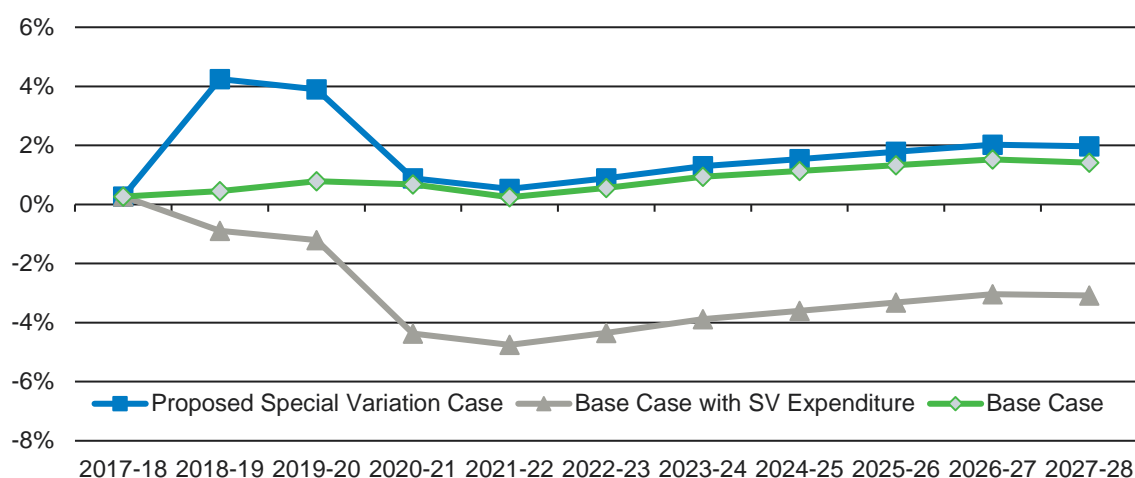
Under the base case with no additional special variation revenue, and assuming the council's expenditure is the same as under the special variation scenario, it forecasts consistent operating deficits, as shown in Figure 3.1 and Table 3.1. The cumulative value of these forecast deficits (before capital grants and contributions) is \$13.11 million to 2027-28. This suggests the council may be financially unsustainable over the long term if it proceeds with its proposed projects without receiving the additional special variation revenue permanently.

Our decision allows the council to achieve an operating surplus in 2018-19 if it proceeds with its proposed projects.

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<sup>14</sup> Excluding capital grants and contributions.

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



**Note:** The base case scenario is the business as usual model without the SV. 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.

**Source:** Muswellbrook Council, *Annual Financial Statements*, various; Muswellbrook Council, *Application Part A*, Worksheet 7 and IPART calculations.

**Table 3.1 Projected Operating Performance Ratio (%) for Muswellbrook 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	4.2	3.9	0.9	0.5	0.9	1.3	1.5	1.8	2.0	2.0
Base case with SV expenditure	-0.9	-1.2	-4.4	-4.8	-4.3	-3.9	-3.6	-3.3	-3.0	-3.1

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

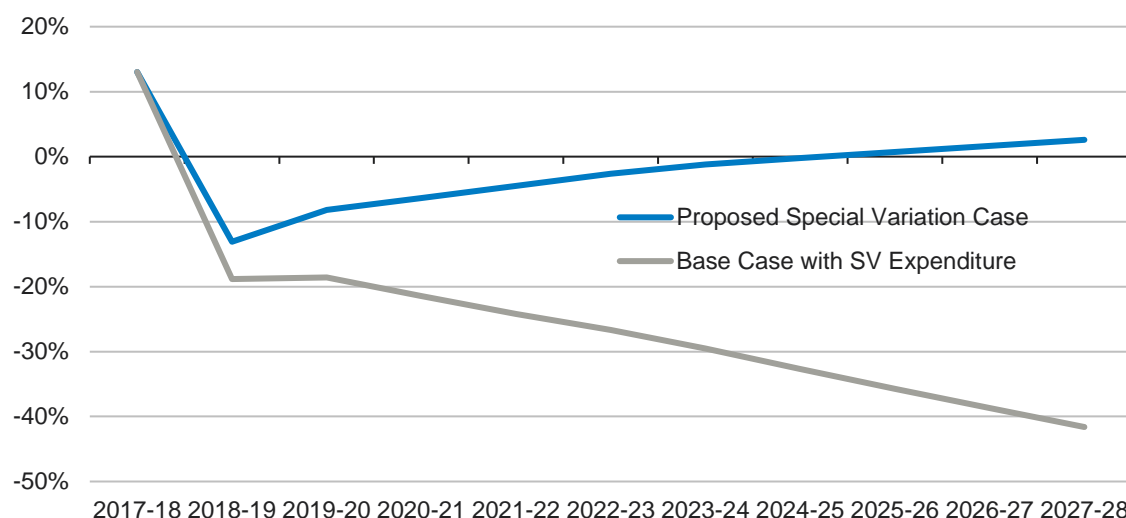
### 3.1.2 Impact on council's net debt

Net debt is the book value of the council's gross debt less any cash and cash-like assets on the balance sheet. Net debt shows how much debt the council has on its balance sheet if it pays all its debt obligations within its existing cash balances. Over time, a change in net debt is an indicator of council's financial performance and sustainability on a cash basis.

Figure 3.2 plots the council's net debt position, as a percentage of total income, over the next 10 years:

- ▼ assuming special variation expenditures and revenue (special variation case), and
- ▼ assuming special variation expenditure but without the additional revenue (base case with SV expenditure).

**Figure 3.2 Muswellbrook Shire Council's forecast net cash (debt) to total income (%) (2017-18 to 2027-28)**



**Note 1:** A number below 0% indicates the council has a net debt position, while a number above 0% indicates the council has a net cash position.

**Note 2:** We have also included current investments as cash in this net debt calculation to provide a more accurate picture of Muswellbrook Council's balance sheet.

**Source:** Muswellbrook Council, *Long Term Financial Plan*; IPART calculations.

With the special variation, Muswellbrook Council's forecasts its net cash to income position to fall in 2017-18 to a small net debt position, then to rise to 2.6% of income by 2027-28.

Without the special variation, Muswellbrook Council is forecast to move from a net cash to income position of 13.0% in 2017-18, to a net debt position of 41.6% of income by 2027-28. Figure 3.2 suggests that without the additional special variation revenue, Muswellbrook Council would be able to fund the special variation expenditure by accumulating modest but increasing levels of debt.<sup>15</sup> The council's financial position would likely decline over the long term if it commits to the proposed capital expenditure projects without the additional special variation revenue.

### 3.1.3 Alternative funding strategies

Muswellbrook Council has explored several sources of funding for the suite of proposed projects, outlined in Appendix B. It has conducted a review of fees and charges levied on specific users of the community's facilities, the appropriate use of debt and cash reserves, and external grant funding. Muswellbrook Council states its investigation of alternative funding strategies has informed its special variation application.<sup>16</sup>

## 3.2 The council demonstrated community engagement and awareness

Overall, we consider that Muswellbrook Council demonstrated that its community is aware of the need for and extent of the proposed rate increase; and provided detailed explanation

<sup>15</sup> We have also included current investments as cash in the net cash (debt) calculation.

<sup>16</sup> Muswellbrook Council, Special variation Application Form – Part B, p 16.



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about the purpose and impact of the special variation and sought feedback from the community.

The council has used a range of methods to engage with the community on the need for a rate increase and to seek community feedback, including:

- ▼ a mailout to all ratepayers detailing the proposed special variation and the projects it would fund
- ▼ meeting with stakeholder groups and community panels
- ▼ traditional and social media
- ▼ online information and feedback, and
- ▼ traditional and social media.<sup>17</sup>

Although the council demonstrated it had taken reasonable steps to ensure the community was widely aware of the rate rise, we note that the council did not update its IP&R documents with the proposed special variation for 2018-19 in time to exhibit these documents before submitting its application to IPART. This is addressed in Section 3.4.

### **3.2.1 Outcome of consultation with community**

Although this criterion does not require councils to demonstrate community support for the special variation, councils are required to consider the results of their community consultation in preparing their application. The results of Muswellbrook Council's consultation indicate the majority of its community do not support a special variation.<sup>18</sup>

### **3.2.2 Submissions from the community**

IPART received seven submissions on the proposed special variation during the consultation period. All seven submissions opposed the special variation proposed by Muswellbrook Council. Some of the concerns stakeholders voiced were that:

- ▼ The special variation and the projects were “unnecessary, fiscally irresponsible and unwanted”.<sup>19</sup>
- ▼ The community did not want and could not afford the entertainment centre.<sup>20,21</sup>
- ▼ Other funding options should be explored because ratepayers could not afford the increases.<sup>22</sup>

We also received submissions outside the consultation period objecting to the special variation.

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<sup>17</sup> Muswellbrook Council, Special variation Application Form – Part B, p 2.

<sup>18</sup> Jetty research, *A poll of Muswellbrook Shire residents to measure support for a proposed Special rate Variation*, December 2017, p 5.

<sup>19</sup> Individual submission, 10 March 2018, p 1.

<sup>20</sup> Individual submission, 9 March 2018, p 1.

<sup>21</sup> Individual submission, 12 March 2018, p 2.

<sup>22</sup> Individual submission, 7 March 2018, p 1.

### 3.3 The impact on ratepayers is reasonable

As Chapter 2 discussed, Muswellbrook Council requested a one-year increase of 14.73% to be retained permanently in the rate base. We found that the impact of this increase on ratepayers will be substantial but reasonable given:

- ▼ current average residential rate levels are typically lower than neighbouring councils
- ▼ the community's capacity to pay, given the rates to income ratio in Muswellbrook is below neighbouring and Group 11 councils, and
- ▼ the financial need for the special variation as the council may be unable to fund the proposed projects without the special variation revenue.

#### 3.3.1 Council's consideration of impact on ratepayers

The council examined socio-economic indicators such as unemployment, outstanding rates compared to other Group 11 councils and the median wage within the LGA to assess the impact of the proposed special variation on ratepayers.<sup>23</sup> It considers while the LGA's population demonstrates moderate levels of socio-economic disadvantage, residential rates are relatively affordable compared to other Group 11 councils.<sup>24</sup>

The largest proposed rate increases affect mining ratepayers. Muswellbrook Council notes that one mining ratepayer, BHP Billiton Limited, objected to the special variation during consultation. Muswellbrook Council submits the rate increase is not material when compared to BHP Billiton Limited's profit.<sup>25</sup>

#### 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 excluding this application, the council has applied for four special variations since 2007-08 and has been granted three special variations:

- ▼ 2007-08: a 9.44% one year permanent increase to fund infrastructure maintenance and renewals
- ▼ 2011-12: a 6.8% one year temporary increase related to a mining road.
- ▼ 2012-13: a 7.6% one year permanent increase to fund renewal and maintenance works related to a mining road.

Since 2007-08, the average annual growth in rates in Muswellbrook was 2.9% for residential ratepayers, 6.3% for business ratepayers and 3.7% for farmland ratepayers. This compares to the average annual growth in the rate peg of 2.7% over the same period.

Mining rates were introduced in 2011-12. Since introduction, the average annual growth has been 33.2%.

<sup>23</sup> Muswellbrook Council, *Application Part B*, p 36.

<sup>24</sup> Muswellbrook Council, *Application Part B*, pp 35 - 36

<sup>25</sup> Letter from Muswellbrook Shire Council to IPART Secretariat dated 26 February 2018, p 4.

We also compared current rates and socio economic indicators in Muswellbrook with neighbouring council areas and OLG Group 11 councils as shown in Table 3.2.

**Table 3.2 Muswellbrook Shire Council - comparison of rates and socio-economic indicators with neighbouring councils and Group 11 averages (2015-16)**

Council (OLG Group)	Average residential rate (\$) <sup>a</sup>	Average business rate (\$)	Median household income (2016) <sup>b</sup>	Average rate to median income (%)	Outstanding rates ratio (%)	SEIFA Index NSW Rank <sup>c</sup>
Upper Hunter Shire	714	863	64,584	1.1	6.5	67
Dungog Shire	794	866	63,752	1.2	3.6	83
<b>Muswellbrook Shire</b>	<b>722</b>	<b>1,859</b>	<b>69,992</b>	<b>1.0</b>	<b>5.3</b>	<b>22</b>
OLG Group 11 average	720	1,863	60,274	1.2	4.7	-

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

<sup>b</sup> Based on 2016 Census data on median household income.

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

**Source:** OLG, unpublished data; OLG, Time Series Data 2015-2016; ABS, *Socio-Economic Indexes for Areas (SEIFA) 2016*, March 2018; and IPART calculations.

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

- ▼ average residential rate, \$722, was similar to the average for Group 11 councils and neighbouring councils
- ▼ average business rate was higher than neighbouring councils but similar to the average for Group 11 councils
- ▼ average residential rate to income ratio was lower than the Group 11 councils and neighbouring councils, and
- ▼ outstanding rates ratio at 5.3% is comparable with Group 11 and neighbouring councils.

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

### 3.4 The council's IP&R documents were not exhibited

Muswellbrook Council did not exhibit IP&R documents containing the proposed 2018-19 special variation before submitting its application to IPART.

Under the IP&R framework, the Delivery Program and LTFP are key documents. Given the importance of the Delivery Program and LTFP under the IP&R documents, Criterion 4 of the special variation guidelines published by OLG requires:

The relevant IP&R documents<sup>26</sup> 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.<sup>27</sup>

The IP&R documents that Muswellbrook Council exhibited were prepared in February 2017 and they detailed costs and projects from the 2017-18 special variation application.

The council's Delivery Program was not updated to provide the community with information on the special variation for 2018-19 prior to the current application. The council's exhibited and adopted Delivery Program refers to a "Special Rate Variation accumulating over 4 years at 2.5 per cent each year".<sup>28</sup> This is quite different from the current proposed permanent increase of 14.7% over one year. The community may have inferred from this document the total rate rise under a special variation would be 2.5% per year.

The Delivery Program also refers to three major projects. The council's Delivery Program states:

...Council proposes a Special Rate Variation to fund three regionally significant projects: a Regional Convention and Performance Centre – a major component of the Muswellbrook Town Centre Plan, an expansion and upgrade to the Regional Aquatic Centre and the delivery of the Denman Town Centre revitalisation plan.<sup>29</sup>

We note that the projects in the Delivery Program do not correspond to the special variation application. The council has sought the special variation for two of these three major projects and several other projects.

Additionally, Criteria 1 to 3 in the OLG Guidelines make specific reference to requirements of the Delivery Program and LTFP. More detail on the criteria in the Guidelines is available in Appendix A.

The exhibited version of the LTFP also contained the special variation that was proposed for 2017-18, which refers to rate rises of 4% in 2017-18 and 5% in each of 2018-19 to 2020-21. This previous proposal differs from the current proposal in a number of ways:

- ▼ The previous proposal has a cumulative rate increase that is 8% more than the assumed rate peg from 2018-19 to 2020-21. The current proposed special variation is for an increase of 12.3% more than the rate peg in a single year in 2018-19.
- ▼ Expenditure under the previous proposal was for the Regional Convention and Performance Centre, Denman Town Centre Revitalisation plan and the Regional Aquatic Centre. The current suite of projects excludes the Denman Town Centre Revitalisation plan and includes several other initiatives, as detailed in Appendix B, Table B.1 and Table B.2.<sup>30</sup>

<sup>26</sup> The relevant documents are the Community Strategic Plan, Delivery Program, and Long Term Financial Plan and where applicable, Asset Management Plan. Of these, the Community Strategic Plan and Delivery Program require (if amended) public exhibition for 28 days. It would also be expected that the Long Term Financial Plan (General Fund) be posted on the council's website.

<sup>27</sup> OLG Guidelines, p 9.

<sup>28</sup> Muswellbrook Council, Delivery Program 2017-21, p 34.

<sup>29</sup> Muswellbrook Council, Delivery Program 2017-21, p 32.

<sup>30</sup> Muswellbrook Council, *Long Term Financial Plan 2017-2027*, February 2017, p 27.

The community may not have known from these documents whether the council was planning to re-apply for a special variation for 2018-19.

For these reasons we consider the council has not satisfied this criterion.

In addition, the Delivery Program and Long Term Financial Plan did not meet Criterion 3 of the OLG guidelines to:

- ▼ include the council's consideration of the community's capacity and willingness to pay rates, and
- ▼ establish the proposed rate increases are affordable.

The council's application to IPART included an updated Long Term Financial Plan that contained the required information on the proposed special variation.<sup>31</sup> However, the council adopted this version on 31 January 2018 and posted it on its website.<sup>32</sup> This would not have allowed the community reasonable time to provide meaningful feedback prior to the council making its special variation application.

For these reasons we consider the council has not satisfied Criterion 4.

### **3.5 The council explained its productivity improvements and cost containment strategies**

Muswellbrook 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 over the last three years, it has realised annual savings of around \$400,000 per year in operating expenditure due to initiatives including:

- ▼ an organisational review resulting in a staff reduction (\$250,000 pa)
- ▼ energy efficiency measures such as reticulated water use and solar generation (\$50,000 pa), and
- ▼ a review of its RMS maintenance contract (\$80,000 pa).<sup>33</sup>

It is also planning future savings through reducing salary costs.

<sup>31</sup> Muswellbrook Council, *Long Term Financial Plan 2019-2028*, February 2018.

<sup>32</sup> Letter from Muswellbrook Shire Council to IPART Secretariat dated 26 February 2018.

<sup>33</sup> Muswellbrook Council, *Application Part B*, p 46.

## 4 Our decision's impact on the council

Our decision means Muswellbrook Council may increase its general income in 2018-19 by 14.73% or \$1.89 million as shown in Table 4.1. Although Muswellbrook Council sought a permanent increase, we have approved a temporary increase for one year. Our decision requires that the portion of this increase that is above the 2.3% rate peg, approximately \$1.60 million, to be removed from the council's rate base at the end of 2018-19.<sup>34</sup>

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 Muswellbrook Shire Council in 2018-19 arising from the special variation approved by IPART**

Notional general income 2017-18 (\$)	Increase approved (%)	Annual increase in general income (\$)	Permissible general income 2018-19 (\$)
12,849,587	14.73	1,892,568	14,742,155

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

**Source:** Muswellbrook 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 a suite of projects, including the development of a regional entertainment and conference centre, and the Olympic Park Precinct upgrade. It gives the council the necessary time to update, exhibit and adopt its IP&R documentation and apply to IPART for a permanent increase in rates in future years if it so chooses.

If the council does not successfully apply for a special variation in future years, the council may need to review its financial and asset planning, and consider whether there is a need to adjust spending for its proposed projects.

<sup>34</sup> 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, Muswellbrook Council indicated it intended to increase rates uniformly across the residential, business and farmland categories by less than 14.73%. It proposes a larger increase for the mining category.<sup>35</sup>

The council has calculated:

- ▼ the average residential rate would increase by 12.3% or \$91 in 2018-19
- ▼ the average business rate would increase by 12.3% or \$292 in 2018-19
- ▼ the average farmland rate would increase by 12.3% or \$350 in 2018-19
- ▼ the average mining rate would increase by 18.3% or \$55,989 in 2018-19.

Table 5.1 sets out Muswellbrook Council's estimates of the expected increase in average rates in the main ratepayer categories.

**Table 5.1** Indicative annual increases in average rates in 2018-19 under Muswellbrook Shire Council's approved special variation

	Average rate 2017-18 (\$)	Increase (%)	Increase (\$)	Average rate 2018-19 (\$)
Average residential rate	736	12.3	91	827
Average business rate	2,373	12.3	292	2,664
Average farmland rate	2,850	12.3	350	3,200
Average mining rate	305,950	18.3	55,989	361,939

**Source:** Muswellbrook Council, *Application Part A*, Worksheet 5a and IPART calculations.

<sup>35</sup> Muswellbrook Council, *Application Part A*, Worksheet 5a.







## Appendices



## A Assessment criteria for special variation applications

**Table A.1 Assessment criteria for special variation applications**

Assessment criteria
<p><b>Criterion 1 – Financial need</b></p> <p>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&amp;R documents, in particular its Delivery Program, Long Term Financial Plan and Asset Management Plan where appropriate.</p> <p>In establishing need for the special variation, the relevant IP&amp;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:</p> <ul style="list-style-type: none"> <li>▼ Baseline scenario – General Fund revenue and expenditure forecasts which reflect the business as usual model, and exclude the special variation, and</li> <li>▼ 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.</li> </ul> <p>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.</p>
<p><b>Criterion 2 – Community awareness</b></p> <p>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 special variation in percentage terms, and the total increase in dollar terms for the average ratepayer, by rating category.</p>
<p><b>Criterion 3 – Impact on ratepayers is reasonable</b></p> <p>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:</p> <ul style="list-style-type: none"> <li>▼ clearly show the impact of any rate rises upon the community</li> <li>▼ include the council's consideration of the community's capacity and willingness to pay rates, and</li> <li>▼ establish that the proposed rate increases are affordable having regard to the community's capacity to pay.</li> </ul>
<p><b>Criterion 4 – IP&amp;R documents are exhibited</b></p> <p>The relevant IP&amp;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.</p>
<p><b>Criterion 5 – Productivity improvements and cost containment strategies</b></p> <p>The IP&amp;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.</p>
<p><b>Criterion 6 – Additional matters</b></p> <p>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.</p>

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

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

Table B.1 shows Muswellbrook Council's proposed expenditure of the special variation funds over the next 10 years.

The council anticipates funding from grants, voluntary planning contributions and loans to fund two large capital projects:

- ▼ the development of a Regional Entertainment and Conference Centre (\$15 million), and
- ▼ the development of Olympic Park Precinct Upgrade (\$11 million).

The council expects to spend \$26 million over three years for the development of these two projects. The council will use the additional special variation revenue above the rate peg (\$1.60 million in 2018-19) to fund:

- ▼ the loan repayments on the two capital projects
- ▼ the additional operating expenditure associated with the Regional Entertainment and Conference Centre (around \$600,000 in annual costs) and the Olympic Park Precinct Upgrade (around \$100,000 in annual costs)
- ▼ improved stormwater management (\$300,000 annually)
- ▼ roads and parks asset maintenance (\$100,000 annually)
- ▼ a job creation program (\$250,000 annually), and
- ▼ a shortfall in mining rates resulting from a change in NSW Government policy (\$62,000 annually).<sup>36,37</sup>

This expenditure is shown in Table B.2 and would be funded from grants (\$10.5 million), voluntary planning contributions (\$3.71 million), and loans (\$11.8 million).<sup>38</sup>

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

<sup>36</sup> Note that Muswellbrook Council has forecast that these operating expenses will increase at 2.5% annually.

<sup>37</sup> Muswellbrook Council, *Application Part A*, Worksheet 6, and Muswellbrook Council, *Application Part B*, p 7.

<sup>38</sup> Muswellbrook Council, *Long Term Financial Plan*, February 2018, p 21.

**Table B.1 Muswellbrook Shire Council – Income and proposed expenditure 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
<b>Special variation income above assumed rate peg</b>	<b>1,597</b>	<b>1,637</b>	<b>1,678</b>	<b>1,720</b>	<b>1,763</b>	<b>1,807</b>	<b>1,852</b>	<b>1,898</b>	<b>1,946</b>	<b>1,994</b>	<b>17,892</b>
Funding for increased operating expenditures											
Entertainment Centre	-	-	595	610	625	641	657	673	690	707	5,198
Olympic Park	-	-	100	103	105	108	110	113	116	119	874
Job creation	-	250	256	263	269	276	283	290	297	305	2,489
Mining shortfall	-	62	64	65	67	69	70	72	74	76	618
Drainage	-	-	300	308	315	323	331	339	348	357	2,621
Roads and parks	-	-	100	103	105	108	110	113	116	119	874
Loan repayments	682	634	594	594	594	594	594	594	594	594	6,071
Transfers to (from) reserves	1,210	994	-428	-414	-399	-384	-369	-353	-337	-320	-801
<b>Total expenditure</b>	<b>1,893</b>	<b>1,940</b>	<b>1,581</b>	<b>1,631</b>	<b>1,682</b>	<b>1,734</b>	<b>1,787</b>	<b>1,842</b>	<b>1,898</b>	<b>1,956</b>	<b>17,943</b>

**Note:** Numbers may not add due to rounding.

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

**Table B.2 Muswellbrook Shire Council – Proposed 3-year capital expenditure program related to the special variation (\$000)**

	2018-19	2019-20	2020-21	Total
<b>Total capex</b>	<b>11,800</b>	<b>11800</b>	<b>2,410</b>	<b>26,010</b>
Entertainment Centre (capital)	7,000	7,000	1,000	15,000
Olympic Park (capital)	4,800	4,800	1,410	11,010
<b>Total funding</b>	<b>-11,800</b>	<b>-11,800</b>	<b>-2,410</b>	<b>26,010</b>
Bank loans	-11,800	-	-	-11,800
Grants	-	-10,500	-	-10,500
Voluntary Planning Agreements	-	-1,300	-2,410	-3,710

**Note:** Numbers may not add due to rounding.

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

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

Overall, the tables below show that staff numbers and employee costs as a percentage of operating expenditure declined slightly over the period 2012-13 to 2015-16.

**Table C.1 Trends in selected performance indicators for Muswellbrook Shire Council, 2012-13 to 2015-16**

Performance indicator	2012-13	2013-14	2014-15	2015-16	Average annual change (%)
Full-Time Equivalent (FTE) staff (number)	170	164	158	165	-1.0
Ratio of population to FTE	97	100	104	100	1.1
Average cost per FTE (\$)	74,929	78,071	81,000	78,036	1.4
Employee costs as % operating expenditure (General Fund only)	40.8	37.4	35.8	31.4	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 C.2 Select comparative indicators for Muswellbrook Shire Council, 2015-16**

	Muswellbrook Shire Council	OLG Group 11 average	NSW average
<b>General profile</b>			
Area (km <sup>2</sup> )	3,405	-	-
Population	16,468	-	-
General Fund operating expenditure (\$m)	35.0	28.0	70.2
General Fund operating revenue per capita (\$)	2,843	-	-
Rates revenue as % General Fund income	29.2	33.7	43.6
Own-source revenue ratio (%)	50.0	57.2	67.3
<b>Average rate indicators<sup>a</sup></b>			
Average rate – residential (\$)	722	720	1,017
Average rate – business (\$)	1,859	1,863	5,118
Average rate – farmland (\$)	2,765	2,871	2,366
<b>Socio-economic/capacity to pay indicators</b>			
Median annual household income (\$) <sup>b</sup>	69,992	60,274	77,272
Average residential rate to median income ratio (%)	1.0	1.2	1.3
SEIFA, 2016 (NSW rank: 130 is least disadvantaged)	22	-	-
Outstanding rates and annual charges ratio (%)	5.3	4.8	3.6
<b>Productivity (labour input) indicators<sup>c</sup></b>			
Full-Time Equivalent (FTE) staff (number)	165	165	354
Ratio of population to FTE	99.8	-	-
Average cost per FTE (\$)	78,036	74,013	83,193
Employee costs as % operating expenditure (General Fund only)	31.4	38.0	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.



## D Fit for the Future assessment

Box D.1 summarises IPART's FFTF assessment of Muswellbrook Council.

### Box D.1 FFTF Assessment

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

- ▼ Met the criterion for sustainability. The council was forecast to meet the **operating performance benchmark** from 2019-20 based on its projected positive OPR, meet the own source revenue benchmark in all forecast years, and meet the asset renewal benchmark in 2019-20.
- ▼ Met the criterion for infrastructure and service management as it met the **infrastructure backlog benchmark** during the time of the assessment. The asset maintenance ratio was forecast to improve to 104% by 2019-20. The council met the debt service benchmark in all forecast years.
- ▼ Met the **efficiency criterion** based on a declining Real Operating Expenditure per Capita ratio.

The council did not indicate it planned to apply for a special variation during FFTF because at that time it did not envisage undertaking the two proposed community projects.

NSW Treasury Corporation (TCorp) observed in 2013 the council's financial position was moderate, and its outlook was neutral. This assessment was made largely because of its then negative operating performance ratio offset by its moderate level of borrowings.

**Source:** IPART, *Assessment of Council Fit for the Future Proposals*, October 2015, and New South Wales Treasury Corporation (TCorp), *Financial Sustainability of the New South Wales Local Government Sector*, April 2013.