Independent Pricing and Regulatory Tribunal
New South Wales

Special variation increase

Port Stephens Council 2019-20

Final Report
Local Government

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The Independent Pricing and Regulatory Tribunal (IPART)

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Tribunal Members

The Tribunal members for this review are:

Dr Paul Paterson, Chair

Mr Ed Willett

Ms Deborah Cope

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

Sheridan Rapmund	(02) 9290 8430
Thomas Partalis	(02) 9019 1936

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1 Executive summary

Port Stephens Council (the Council) applied to IPART for a special variation (SV)[1] to increase its general income above the rate peg[2] of 2.7% for 2019-20. It has **applied for a 7-year** SV to:

- Increase its general income by 7.5% per annum for each year from 2019-20 to 2025-26 (inclusive), **a cumulative increase of 65.9%**.
- Retain this increase in its rate base **permanently**.[3]

The Council intends to use the proposed SV funds to provide new infrastructure and services, upgrade existing infrastructure and reduce its infrastructure backlog.[4] This includes town centre revitalisation projects and the provision of additional footpaths and cycle ways.

The Council's proposed SV would generate an additional increase in its permissible general income (PGI) of $71.3 million (17.9% of total income) over seven years (see Table 1.1). As the proposed SV is permanent, it would mean a cumulative increase in its PGI of $133.4 million above the rate peg over 10 years (see Table 2.1).

IPART has assessed the Council's application against the criteria in the Office of Local Government's *Guidelines for the preparation of an application for a special variation to general income* (the OLG Guidelines).

This report sets out our decision (Section 1.1) and explains how and why we reached that decision.

1 In this context, the term 'special variation' refers to an instrument in writing given to the council by IPART (under delegation from the Minister) under s 508A of the Local Government Act 1993 (NSW).

2 The term 'rate peg' refers to the annual order published by IPART (under delegation from the Minister) in the gazette under s 506 of the Local Government Act 1993 (NSW).

3 Port Stephens Council, *Special Variation Application Form Part A 2019-20 (Application Part A)*, Worksheet 1.

4 Port Stephens Council, *Special Variation Application Form Part B 2019-20 (Application Part B)*, pp 4-5; and Port Stephens Council, *Delivery Program and Operational Plan 2018-2021 (Delivery Program)*, p 36.

Table 1.1 Permissible general income (PGI) of Port Stephens Council from 2019-20 to 2025-26 arising from the proposed SV

Year	Increase approved (%)	Cumulative increase approved (%)	Increase in PGI above rate peg ($)	Cumulative increase in PGI ($)	PGI ($)
Adjusted notional income 1 July 2019					42,063,042
2019-20	7.5	7.5	2,019,026	3,154,728	45,217,770
2020-21	7.5	15.6	4,330,390	6,546,061	48,609,103
2021-22	7.5	24.2	6,869,105	10,191,744	52,254,786
2022-23	7.5	33.5	9,653,572	14,110,853	56,173,895
2023-24	7.5	43.6	12,703,606	18,323,895	60,386,937
2024-25	7.5	54.3	16,040,543	22,852,915	64,915,957
2025-26	7.5	65.9	19,687,354	27,721,612	69,784,654
Total cumulative increase approved				102,901,807	
Total above rate peg			**71,303,597**		

Note: The above information is correct at the time of the Council's application (February 2019).

Source: Port Stephens Council, *Application Part A,* Worksheets 1 and 4; and IPART calculations.

1.1 We have not approved Port Stephens Council's application for a Special Variation

We decided not to approve the proposed SV.

Our decision means that the Council may only raise its general income by the rate peg of 2.7% in 2019-20 (see Box 1.1). This does not prevent the Council from making a new application for an SV next year or in subsequent years.

Box 1.1 IPART Decision – Port Stephens Council

Indicative percentage increase in general income from 2019-20 to 2025-26

	2019-20	2020-21	2021-22	2022-23	2023-24	2024-25	2025-26
Rate Peg	2.7	2.5	2.5	2.5	2.5	2.5	2.5

Rate peg increases only, unless a new SV proposal is approved in the future.

The rate peg of 2.5% for future years is assumed and may vary with the setting of the rate peg by IPART in September each year.

1.2 Reasons for our decision

Our decision reflects our finding that the Council's application does not meet the criteria in the OLG Guidelines.

The Council has only partly demonstrated a financial need for the proposed SV, as the SV expenditure is not needed to ensure financial sustainability or to meet infrastructure backlog and renewal benchmarks. The application also outlined a lack of community willingness to pay for the works the Council proposed be funded by the SV. The magnitude of the increase in total dollars for the average ratepayer under the proposed SV would be considerable.

Therefore, approval of the Council's application would not be reasonable in the circumstances.

Without the proposed SV revenue and expenditure, the Council forecasts a consistently positive Operating Performance Ratio (OPR), averaging 2.7% over the next seven years. On the other hand, if the Council incurred the expenditure proposed in its SV, the SV revenue would be required to ensure it achieves a positive OPR. This suggests that in the absence of the expenditure in the Council's SV proposal, there would be no financial need for the SV revenue; but that there would be this need with the expenditure. Therefore, we considered whether the proposed SV works are justifiable.

We found that the proposed SV expenditure is not required to reduce the Council's infrastructure backlog to reasonable levels. The Council's infrastructure backlog and infrastructure renewal ratio would be consistent with the benchmarks, even without the SV expenditure: the Council forecasts that its infrastructure backlog ratio without the proposed SV expenditure would remain at or below 2.0% for the next 10 years, consistent with the OLG benchmark of 2% or less, [5] while the infrastructure renewal ratio will exceed the benchmark of greater than 100%[6] with or without the proposed SV.[7]

We recognise, however, that there may be other justifications for the proposed SV particularly if, for example, ratepayers are willing to pay for it. However, in the case of Port Stephens, we found evidence that a significant majority of ratepayers are not willing to pay for the SV: a survey conducted for the Council showed only 14% of ratepayers surveyed were willing to pay for the proposed SV.[8]

The Council did consider alternatives to the proposed SV. The Council will be seeking to secure $60 million in loans over 20 years in addition to the SV revenue. The Council will continue to apply for grant funding, but has stated that it is unreliable.[9] The Council regularly revises its fees and charges, but has concluded that the required funds are too great to be raised entirely through alternative means such as fees and charges.[10]

5 Port Stephens Council, *Application Part A*, Worksheet 9.
6 Port Stephens Council, *Application Part A*, Worksheet 9.
7 Office of Local Government, *Improvement Proposal Reassessment Report Round 3 – June 2018*, p 10.
8 Port Stephens Council, *Attachment 6 – Community Consultation Feedback*, p 38.
9 Port Stephens Council, *Delivery Program*, p 8; and Port Stephens, *Application Part B*, p 32.
10 Port Stephens Council, *Application Part B*, p 32.

The Council has demonstrated that its community is aware of the need for, and extent of, the proposed rate increase. The Council has communicated the rates increase in cumulative percentage terms and as dollar increases to average rates using a variety of materials and engagement methods. It is apparent from the submissions that we have received that ratepayers are aware of the proposal and the resulting increase in rates.

We found that while the Council's current rate levels are relatively low compared to the rates of its OLG Group[11] and surrounding councils, the impact on affected ratepayers would have been high, with a cumulative increase over the seven years of the proposed SV of $690 for an average residential ratepayer.

The Council's Integrated Planning and Reporting (IP&R) documents contain sufficient information relating to the proposed SV and they have been appropriately exhibited, approved and adopted by the Council.

The Council has also outlined and quantified its productivity improvements and cost containment strategies.

In summary, we have not approved the proposed SV because our analysis of the information provided by the Council indicates that it is not needed to ensure the Council's financial sustainability or to meet infrastructure backlog and renewal benchmarks; a significant majority of ratepayers are not willing to pay for the SV; and the impact of the SV on rates would be considerable.

Table 1.2 below provides more detail about our assessment and key considerations in making our decision.

Table 1.2 Assessment of Port Stephens Council's proposed SV application

1. Financial Need	
Partly Demonstrated	The Council partly demonstrated there is a financial need for the proposed SV. Its: ▼ OPR over seven years averages: – 5.0% with the proposed SV – 2.7% without the proposed SV revenue and SV expenditure (the Baseline Scenario) – -2.3% without the proposed SV revenue but with the SV expenditure (the Baseline with SV Expenditure Scenario) ▼ Net cash is $19.4 million or 16.7% of general income in 2018-19, with effectively zero unrestricted cash and investments (as at 30 June 2018). ▼ Infrastructure backlog ratio (OLG Benchmark of <2%) in 2028-29 is estimated at: – 1.8% under the Proposed SV Scenario – 2.0% under the Baseline Scenario Currently, this ratio is 1.8%. ▼ Infrastructure renewals ratio (OLG Benchmark of >100%) in 2028-29 is estimated at: – 120.6% under the Proposed SV Scenario – 134.3% under the Baseline Scenario Currently, this ratio is 104.4%.

11 Port Stephens is in OLG Group 5, which is classified as Regional Town/City. The group comprises of 11 councils including Coffs Harbour, Maitland, Newcastle, Shellharbour and Wollongong.

2. Community awareness	
Demonstrated	The Council demonstrated the community is aware of the proposed rate rise. It: ▼ Developed a consultation strategy and used a range of engagement methods to make the community aware of the need for, and extent of, the proposed rate increase. ▼ Provided detailed explanation about the purpose and impact of the proposed SV in both cumulative percentage and dollar terms. ▼ Sought community feedback on the rate increase.
3. Reasonable Impact on ratepayers	
Partly Demonstrated	With the proposed SV, average residential rates would increase 7.5% per annum from 2019-20 to 2025-26. Over the seven years of the SV the increase in the average residential rate would be $690 (or 65.9% relative to 2018-19 levels). The Council examined the impact of the SV on ratepayers and stated that it would be reasonable. It considered: ▼ Current average residential rates in the Council's Local Government Area (LGA) are lower than other councils in the Lower Hunter Area. ▼ The Council's existing hardship and pensioner policies and proposed implementation of an additional Rates Assistance Program. ▼ Community feedback supporting infrastructure and service delivery improvements. IPART considered information on ratepayers from 2016-17 and found: ▼ Average residential rates without the SV were lower than the Group 5 average, and the lowest of the three comparison councils. ▼ Average business rates without the SV were lower than the Group 5 average, and lower than two of the three comparison councils. ▼ Average farmland rates without the SV were lower than the Group 5 average, and the lowest of the surrounding councils. ▼ Its SEIFA[12] ranking (70) is higher than surrounding councils. IPART also compared the Council's average rate levels with the proposed SV to the OLG Group 5 average rate levels over the proposed seven year SV period and we found that the Council's: ▼ Average residential rates in 2025-26 with the proposed SV would be $1,736, which would be higher than the estimated average residential rates of $1,491 for OLG Group 5 in 2025-26. ▼ Average business rates in 2025-26 with the proposed SV would be $7,388, which would be lower than the estimated average business rates of $8,639 for OLG Group 5 in 2025-26. ▼ Average farmland rates in 2025-26 with the proposed SV would be $2,689, which would be lower than the estimated average business rates of $3,339 for OLG Group 5 in 2025-26. IPART also considered the willingness of ratepayers to pay for the proposed SV. ▼ The phone survey conducted by Micromex for the Council indicates that only 14% of respondents were willing to pay for an SV of 7.5% or greater per annum. ▼ The online survey conducted by the Council found that only 7% of respondents preferred an annual increase of 7.5% or greater.

12 The Socio-Economic Indexes for Areas (SEIFA) is a measure that ranks areas based on their socio-economic conditions. The Australian Bureau of Statistics (ABS) ranks the NSW Local Government Areas in order of their score, from lowest to highest, with rank 1 representing the most disadvantaged area and 130 being the least disadvantaged area. IPART has referred to the Index of Relative Socio-economic Advantage and Disadvantage (IRSAD) for our assessment, one of the component indexes making up SEIFA.

4. IP&R documents exhibited	
Demonstrated	The Council: ▼ Exhibited its updated Community Strategic Plan, Delivery Program, Long Term Financial Plan (LTFP), and Strategic Asset Management Plan from 14 November 2018 to 21 December 2018. ▼ Adopted its amended versions on 29 January 2019. The Delivery Program and Long Term Financial Plan did not discuss the community's capacity and willingness to pay rates under the proposed SV.
5. Productivity improvements and cost containment	
Demonstrated	The Council has implemented a number of cost savings initiatives in the past. Some examples include: ▼ Service Review Program: a comprehensive 16-step, 4-yearly review of the Council's services based on the Australian Business Excellence Framework that seeks to find at least 2% efficiency savings. ▼ $2.1 million in savings since 2011, including its: – 2013 Children's Services review with $215,000 per annum saved. – 2018 Strategic and Environment review with $94,000 per annum saved. ▼ Energy efficiency initiatives including solar panelling and street light upgrades with an estimated 25% reduction in annual grid energy consumption. The Council has outlined future productivity and efficiency initiatives such as: ▼ Continuing the aforementioned Service Review Program. ▼ Leasing of Council land for an estimated additional revenue of $18 million over 12 to 15 years.

1.3 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 proposed SV
- Chapter 3 summarises the submissions received by IPART
- Chapter 4 explains our assessment of the Council's application against each criterion in the OLG Guidelines
- Chapter 5 discusses how our decision will impact the Council.

2 Port Stephens Council's application

The Council has applied for its proposed SV to increase its general income by 7.5% annually (including the rate peg) over seven years from 2019-20 to 2025-26 (a cumulative increase of 65.9%). The application is for an increase that remains permanently in the rate base. The Council indicated the proposed rate increase would be applied across all rating categories.

2.1 Purpose

The purpose of the proposed SV is to fund ongoing operations such as infrastructure maintenance and renewal, development of new infrastructure, and implementation of new services. This includes: revitalisation of the Nelson Bay, Raymond Terrace and Heatherbrae areas, expansion of the number of paths and cycle ways connecting major tourist or community areas, development of a community arts centre, and the upgrade or development of sports facilities.[13]

2.2 Need

The Council has identified the Nelson Bay, Raymond Terrace, and Medowie infrastructure renewals, as well as council works depot relocations, as the projects requiring the largest amount of expenditure.[14] Having considered alternative funding measures, it has found that it would require both the SV revenue and additional loan funding to continue with the proposed projects and remain financially sustainable.[15] The Council has not identified enhanced financial sustainability as a driver of the proposed SV application.[16]

2.3 Significance of proposal

The Council's application would mean a cumulative increase in its PGI of $133.4 million above what the assumed rate peg would deliver over 10 years. This represents 21.6% of the Council's total cumulative PGI over the 10-year period.

Assuming a rate peg of 2.5% per annum from 2020-21 to 2028-29, the proposed SV would result in a PGI that is 39.3% higher than if the Council increased its rates by the rate peg alone.

13 Port Stephens Council, *Application Part B*, pp 4, 5, 15, 16 and 19.
14 Port Stephens Council, *Application Part B*, pp 11, 12 and 77.
15 Port Stephens Council, *Application Part B*, p 36.
16 Port Stephens Council, *Application Part B*, p 4.

Table 2.1 Permissible general income (PGI) of Port Stephens Council from 2019-20 to 2028-29 under the proposed SV

Cumulative increase in PGI above rate peg ($m)	Total PGI over 10 years ($m)	SV revenue as a percentage of total PGI
133.4	617.3	21.6%

Note: The above information is correct at the time of the Council's application (February 2019).

Source: Port Stephens Council, *Application Part A,* Worksheets 1 and 4 and IPART calculations.

The Council indicated it would fund this by increasing rates for all rating categories. The Council has stated that the rates are affordable as the Council's current rates are low compared to other councils in the Lower Hunter region, and that it plans to implement a new Rates Assistance Program (see Section 4.3.1).

2.4 Resolution by the Council to apply for a Special Variation

The Council resolved to apply for the proposed SV on 29 January 2019. One councillor was recorded as opposing the application.[17]

17 Port Stephens Council, *Extra Ordinary Council Meeting Minutes*, 29 January 2019.

3 Submissions to IPART

IPART received 681 submissions during the consultation period from 11 February 2019 to 14 March 2019.

Key issues and views raised were:

- The magnitude of the proposed rate increases are too large
- High rates proposed impacting affordability for ratepayers
- Concerns around the Council's past financial management and use of funds
- Disagreement on the Council's past and proposed uses for the SV funds
- The inequitable proposed uses of the SV funds focussing on major centres and tourist areas
- The Council's application not meeting OLG's criteria including a lack of financial need and a lack of consideration of community feedback
- The costs incurred from the Council's past legal challenges being paid for by the ratepayers
- The Council's lack of transparency and rigour in its consultation process.

A small number of submissions have also raised reasons to support the proposal including:

- Long term gains can be realised from implementing large-scale projects now
- Potential to increase tourism for the area from new and improved infrastructure
- Recognising that some roads need repair and there is a lack of parks and sporting areas.

We considered all the submissions as part of our assessment of the Council's application against the criteria in the OLG Guidelines, which is discussed in the next chapter.

The volume of submissions we received on the Council's application indicates there is concern among ratepayers about the proposed SV. In particular:

- The majority of submissions commented on the magnitude of the proposed increase, the high rates after the increase, and the impact on affordability. We found that the Council's current rates are reasonable, but residential rates would increase considerably above the OLG Group 5 average by the end of the proposed seven year SV term (see Section 4.3).
- Some submissions suggested that the Council does not have, or has not demonstrated, a need for the additional SV revenue. We found that the Council has only partly demonstrated a need for the proposed SV revenue (see Section 4.1).

- A significant number of submissions were in relation to dissatisfaction with the Council's consultation during the SV application process. In particular, several submissions suggested that the Council's consultation process did not give sufficient opportunity for feedback and that the Council did not consider the community feedback when making its subsequent application to IPART. We found that the Council's level of consultation was sufficient and in line with the OLG Guidelines (see Section 4.3). However, we have some concerns that the Council did not give due consideration to the community's capacity and willingness to pay the proposed rates.

These issues raised through submissions were considered in our assessment and subsequent decision to not approve the Council's proposed SV.

4 IPART's assessment

To make our decision, we assessed the Council's application against the criteria in the OLG Guidelines.

The criteria in the OLG Guidelines are:

- **Criterion 1 – Financial need**: The need for, and purpose of, a different revenue path for the Council's General Fund is clearly articulated and identified in the Council's IP&R documents.
- **Criterion 2 – Community awareness**: Evidence that the community is aware of the need for, and extent of, a rate rise.
- **Criterion 3 – Reasonable impact**: The impact on affected ratepayers must be reasonable.
- **Criterion 4 – Integrated Planning and Reporting (IP&R)**: The relevant IP&R documents must be exhibited (where required), approved and adopted by the Council.
- **Criterion 5 – Productivity**: The Council must explain its productivity improvements and cost containment strategies.

While the criteria for all types of SV are the same, the OLG Guidelines state that the extent of evidence required for assessment of the criteria can alter with the scale and permanence of the SV proposed.

Our Assessment

We decided not to approve the proposed SV. Our decision reflects our finding that the Council's application does not meet the criteria in the OLG Guidelines. The Council has only partly demonstrated a financial need for the proposed SV, the SV expenditure is not needed to meet infrastructure backlog or renewal benchmarks, there is a lack of community willingness to pay for the works the Council proposed be funded by the SV, and the impact of the proposed SV on the average ratepayer would be considerable in terms of total dollar increase.

Therefore, approval of the Council's application would not be reasonable in the circumstances.

The Council has not sufficiently demonstrated that there is a case to fund the works in its SV proposal through its proposed increase in rates, particularly given the magnitude of this increase.

Without the proposed SV revenue and expenditure, the Council forecasts a consistently positive OPR, averaging 2.7% over the next seven years. On the other hand, if the Council incurred the expenditure proposed in its SV, the SV revenue would be required to ensure it achieves a positive OPR. This suggests that in the absence of the expenditure in the Council's SV proposal, there would be no financial need for the SV revenue; but that there would be this need with the expenditure. Therefore, we considered whether the proposed SV works are justifiable.

We found that the proposed SV expenditure is not required to reduce the Council's infrastructure backlog to reasonable levels. The Council's infrastructure backlog and infrastructure renewal ratio would be consistent with the benchmarks, even without the SV expenditure: the Council forecasts that its infrastructure backlog ratio without the proposed SV expenditure would remain at 2.0% or below for the next 10 years[18], consistent with the OLG benchmark of 2% or less, while the infrastructure renewal ratio will exceed the benchmark of 100% with or without the proposed SV.[19]

We recognise, however, that there may be other justifications for the proposed SV particularly if, for example, ratepayers are willing to pay for it. However, in the case of Port Stephens, we found evidence that a significant majority of ratepayers are not willing to pay for the SV: a survey conducted for the Council showed only 14% of ratepayers surveyed were willing to pay for the proposed SV.[20]

The Council considered alternatives to the SV. The Council will be seeking to secure $60 million in loans over 20 years in addition to the SV revenue. The Council will continue to apply for grant funding, but has stated that it is unreliable.[21] The Council regularly revises its fees and charges, but has concluded that the required funds are too great to be raised entirely through alternative means such as fees and charges.[22]

The Council has demonstrated that its community is aware of the need for, and extent of, the proposed rate increase. The Council has communicated the rates increase in cumulative percentage terms and as dollar increases to average rates, using a variety of materials and engagement methods. It is apparent from the submissions that we have received that ratepayers are aware of the proposal and the resulting increase in rates.

We found that while the Council's current rate levels are relatively low compared to the rates of its OLG Group and surrounding councils, the impact on affected ratepayers would have been high, with a cumulative increase over the seven years of the proposed SV of $690 for an average residential ratepayer.

The Council's IP&R documents contain sufficient information relating to the proposed SV and they have been appropriately exhibited, approved and adopted by the Council.

The Council has also outlined and quantified its productivity improvements and cost containment strategies.

Our assessment of the Council's application against each of the criteria in the OLG Guidelines is discussed in more detail in the sections below.

18 Port Stephens Council, *Application Part A*, Worksheet 9.
19 Office of Local Government, *Improvement Proposal Reassessment Report Round 3 – June 2018*, p 10.
20 Port Stephens Council, *Attachment 6 – Community Consultation Feedback*, p 38.
21 Port Stephens Council, *Delivery Program*, p 8.
22 Port Stephens Council, *Application Part B*, p 32.

4.1 Financial need for the proposed Special Variation

This criterion examines the Council's financial need for the proposed SV. The OLG Guidelines require the Council to clearly articulate and identify the need for, and purpose of, a different revenue path for its General Fund. This includes that:

- The Council sets out the need for, and purpose of, the proposed SV in its IP&R documents, including its Delivery Program, LTFP and Asset Management Plan where appropriate.
- Relevant IP&R documents should canvas alternatives to the rate rise.
- The Council may include evidence of community need/desire for service levels or projects.

IPART uses information provided by councils in applications to assess the impact of the proposed SV on the Council's financial performance and financial position, namely the Council's forecast:

- Operating performance
- Net cash (debt).

Where relevant, IPART also uses information provided by the Council to assess its need for the proposed SV to reduce its infrastructure backlog and/or increase its infrastructure renewals, by assessing the Council's:

- Infrastructure backlog ratio
- Infrastructure renewals ratio.

Generally, we would consider a council with a consistent operating surplus to be financially sustainable. The Council's forecast operating result shows whether the income it receives covers its operating expenses each year. We consider that the most appropriate indicator of operating performance is the operating performance ratio (OPR).

The OPR measures whether a council's income funds its costs and is defined as:

$$OPR^{23} = \frac{Total\ operating\ revenue - operating\ expenses}{Total\ operating\ revenue}$$

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

Based on the Council's application and LTFP (where appropriate), we calculate forecasts under three scenarios:

1. **The Proposed SV Scenario** – which includes the Council's proposed SV revenue and expenditure.
2. **The Baseline Scenario** - which shows the impact on the Council's operating and infrastructure assets' performance **without the proposed SV revenue and expenditure**.
3. **The Baseline with SV Expenditure Scenario** - which includes the Council's full expenses from its proposed SV, without the additional revenue from the proposed SV. This scenario is a guide to the Council's financial sustainability if it still went ahead with its full expenditure program included in its application, but could only increase general income by the rate peg percentage.

We consider that a council's average OPR over the next 10 years should be 0% or greater, as this is typically the minimum level needed to demonstrate financial sustainability. An OPR consistently well above 0% would bring into question the financial need for an SV. We note that other factors, such as the level of borrowings and/or investment in infrastructure, may affect the need for a council to have a higher or lower operating result than the OLG breakeven benchmark.

While the OPR is a good guide to a council's ongoing *financial performance* (or sustainability), we may also have reference to a council's *financial position*, and in particular its net cash (or net debt).[24] This may inform us whether the Council has significant cash reserves that could be used to fund the purpose of the proposed SV. We examined the Council's net cash position in 2018-19 and as a percentage of income to gauge its financial position.

We note the OPR is a measure of the Council's financial performance, measuring how well a council contains its operating expenditure within its operating income. As the ratio measures net operating results against operating revenue, it does not include capital expenditure. That is, a positive ratio indicates operating surplus available for capital expenditure. Therefore, we also further consider the impact of the proposed SV on the Council's infrastructure ratios, where relevant to the Council's application, given the management of infrastructure assets is an important component of the Council's function.

Where relevant, we consider the Council's infrastructure backlog ratio, which measures the Council's backlog of assets against its total written down value of its infrastructure. The benchmark set by OLG for the ratio is less than 2%. It is defined as:

$$Infrastructure\ backlog\ ratio = \frac{Estimated\ cost\ to\ bring\ assets\ to\ a\ satisfactory\ standard}{Carrying\ value\ of\ infrastructure\ assets^{25}}$$

Where relevant, we may also consider the Council's infrastructure renewals ratio, which assesses the rate at which infrastructure assets are being renewed against the rate at which

24 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 the Council's financial performance and sustainability on a cash basis.

25 Historical cost less accumulated depreciation.

they are depreciating. The benchmark set by OLG for the ratio is greater than 100%. It is defined as:

$$Infrastructure\ renewals\ ratio = \frac{Infrastructure\ asset\ renewals^{26}}{Depreciation, amortisation\ and\ impairment}$$

4.1.1 Assessment of the Council's IP&R documents and alternatives to the rate rise

The Council's Delivery Program clearly sets out the need for, and purpose of, the proposed SV, which is to:[27]

- Fund major one-off infrastructure projects
- Fund enhanced services with ongoing infrastructure maintenance
- Fund repayments for the loans borrowed to undertake the proposed infrastructure projects.

The Council's Delivery Program and LTFP also canvassed alternatives to the rate rise, including:

- Grants and developer contributions[28] - the Council will consider and apply for grants as they become available. However, it has indicated that grants are not a suitable replacement for SV funding as they:
  - Are not necessarily aligned with community priorities
  - Are unreliable
  - Often require matching funding, which the Council will need the SV revenue to provide
- Fees and charges - The Council has reviewed the option of increasing fees and charges or introducing new fees, but found that this would not be suitable due to the cost and long-term nature of the proposed projects.[29] Without the SV, the Council will continue to seek additional State and Federal Government grants.[30]
- Loans - The Council intends to borrow $60 million over 20 years to supplement the SV revenue to fund the development of new and renewed infrastructure.[31]

26 Asset renewals represent the replacement and/or refurbishment of existing assets to an equivalent capacity/performance as opposed to the acquisition of new assets (or refurbishment of old assets) that increases capacity/performance.
27 Port Stephens Council, *Delivery Program*, pp 11-12.
28 Port Stephens Council, *Delivery Program*, p 8.
29 Port Stephens Council, *Application Part B*, p 32.
30 Port Stephens Council, *Delivery Program*, p 36.
31 Port Stephens Council, *Long Term Financial Plan*, pp 13-14.

4.1.2 Assessment of the impact of the proposed SV on the Council's financial performance and position

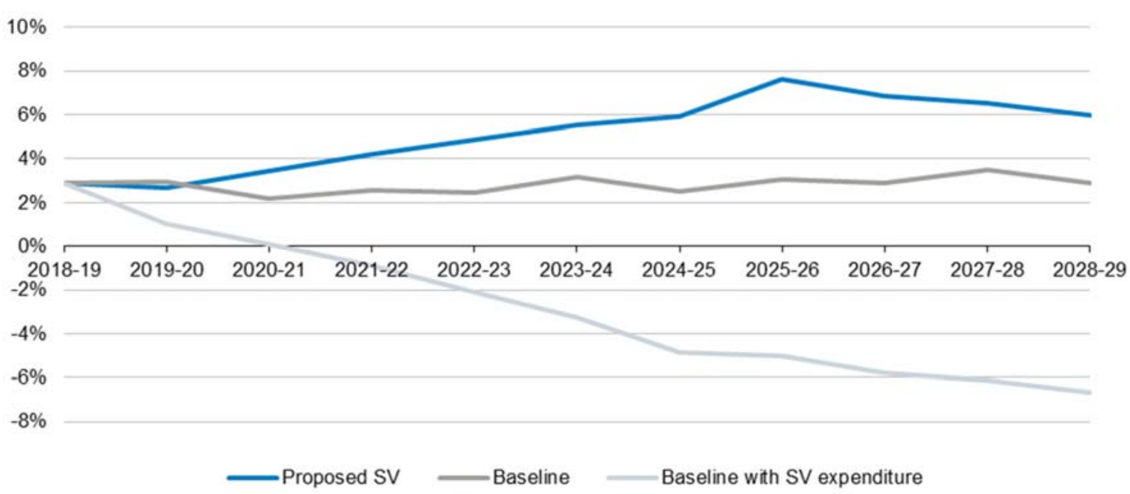
The Council's forecast operating result

Under the Proposed SV Scenario, the Council forecasts operating surpluses increasing to 6.0% by 2028-29. The cumulative value of the forecast operating surpluses (before capital grants and contributions) is $85.7 million to 2028-29. This would allow the Council to fund its proposed projects without becoming financially unsustainable.

Without the proposed SV revenue but assuming the Council's expenditure is the same as under the Proposed SV Scenario, the Council forecasts lower operating surpluses, moving to deficits (Baseline with SV Expenditure Scenario in Figure 4.1 and Table 4.1). Under this scenario, the Council forecasts operating results falling to -6.7% by 2028-29. The cumulative value of these forecast operating results under this scenario is -$46.5 million to 2028-29.

Under the Baseline Scenario (without the proposed SV expenditure and revenue), the Council forecasts a consistently positive OPR over the next 10 years, ranging from 2.2% to 3.5% (see Figure 4.1 and Table 4.1).

Figure 4.1 Port Stephens Council's Operating Performance Ratio (%) excluding capital grants and contributions (2018-19 to 2028-29)



Data source: Port Stephens Council, *Application Part A*, Worksheet 8 and IPART calculations.

Table 4.1 Projected operating performance ratio (%) for Port Stephens Council's proposed SV application (2019-20 to 2028-29)

	2019-20	2020-21	2021-22	2022-23	2023-24	2024-25	2025-26	2026-27	2027-28	2028-29
Proposed SV	2.7	3.4	4.2	4.8	5.6	5.9	7.6	6.9	6.5	6.0
Baseline	2.9	2.2	2.6	2.5	3.2	2.5	3.1	2.9	3.5	2.9
Baseline with SV Expenditure	1.0	0.1	-0.9	-2.1	-3.2	-4.8	-5.0	-5.8	-6.1	-6.7

Source: IPART calculations based on Port Stephens Council, *Application Part A*, Worksheet 8.

Our analysis indicates that over the next five years, the Council's financial performance shows an average OPR of:

- 4.2% under the Proposed SV Scenario
- 2.7% under the Baseline Scenario
- -1.1% under the Baseline with SV Expenditure Scenario.

Our analysis indicates that over the next seven years, the period of the proposed SV, the Council's financial performance shows an average OPR of:

- 5.0% under the Proposed SV Scenario
- 2.7% under the Baseline Scenario
- -2.3% under the Baseline with SV Expenditure Scenario.

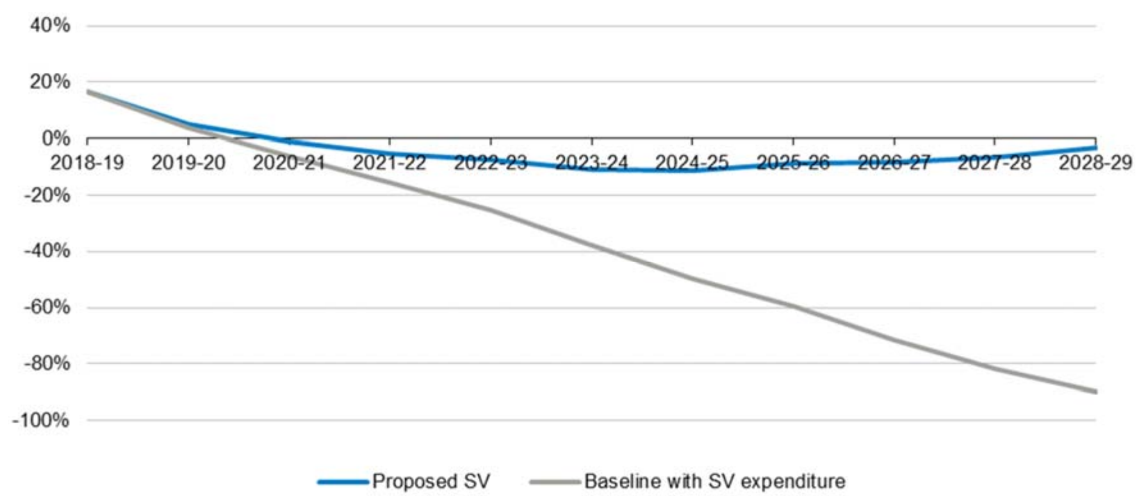
Impact on the Council's net cash (debt)

We calculate the Council's net cash is $19.4 million or 16.7% of general income in 2018-19. We calculate the Council's net cash is $6.3 million or 5.1% of general income in 2019-20 under the Proposed SV Scenario, and $4.3 million or 3.5% of general income in 2019-20 under the Baseline with SV Expenditure Scenario. Over the longer term, with the proposed SV revenue, net debt would increase then decrease as the Council repays its loans.

Under the Baseline with SV Expenditure Scenario, we estimate that net debt would uniformly increase each year.

The Council's forecast net cash (debt) position over the next 10 years is shown in Figure 4.2.

Figure 4.2 Port Stephens Council's net cash (debt) to income ratio (%) (2019-20 to 2028-29)



Data source: Port Stephens Council, *Application Part A*, Worksheet 8 and IPART calculations.

Our analysis indicates that over the next five years, the Council's financial performance shows an average net cash to income ratio of:

- -4.2% under the Proposed SV Scenario
- -16.9% under the Baseline with SV Expenditure Scenario.

Our analysis indicates that over the next seven years, the period of the proposed SV, the Council's financial performance shows an average net cash to income ratio of:

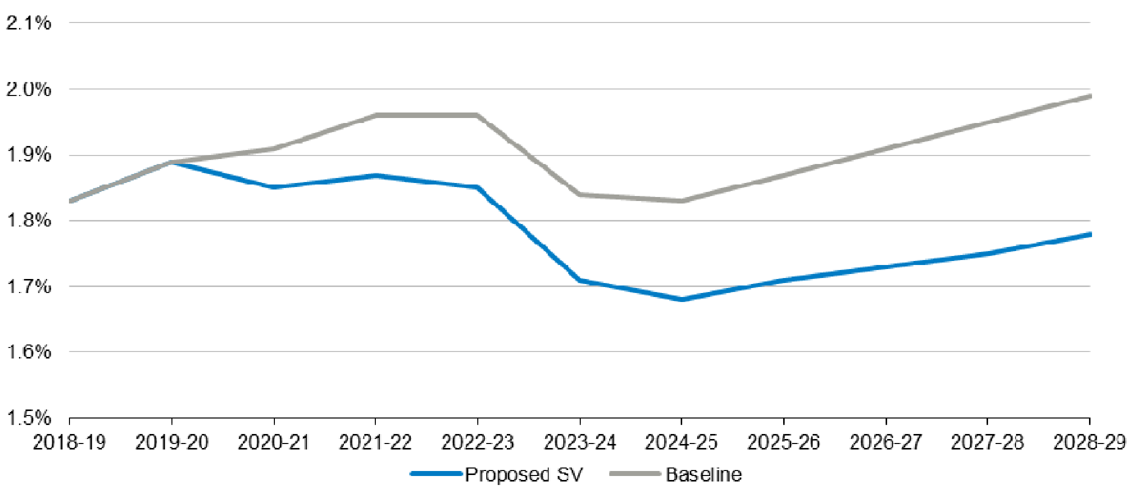
- -6.0% under the Proposed SV Scenario
- -28.4% under the Baseline with SV Expenditure Scenario.

Impact on the Council's infrastructure backlog ratio

The Council estimated its infrastructure backlog to be $12.0 million in 2017-18.[32] The Council indicated its infrastructure backlog has increased to $14 million in 2018-19.[33] Measured as a percentage of the written down value of infrastructure assets, the Council estimates an infrastructure backlog ratio of 1.8% in 2018-19, which meets the OLG benchmark of less than 2%.

The Council's forecast infrastructure backlog ratio over the next 10 years is shown in Figure 4.3. The Council forecasts its infrastructure backlog ratio will decrease marginally under the Proposed SV Scenario, from 1.9% in 2019-20 to 1.8% by 2028-29. Without the proposed SV expenditure, it forecasts the infrastructure backlog to increase to 2.0% by 2028-29.

Figure 4.3 Port Stephens Council's infrastructure backlog ratio (%) (2018-19 to 2028-29)



Data source: Port Stephens Council, *Application Part A*, Worksheet 9.

32 Port Stephens Council, *Special Schedule 7 – Report on Infrastructure Assets*, 30 June 2018.
33 Port Stephens Council, *Application Part B*, p 43.

Table 4.2 Projected infrastructure backlog ratio (%) for Port Stephens Council's proposed SV application (2019-20 to 2028-29)

	2019-20	2020-21	2021-22	2022-23	2023-24	2024-25	2025-26	2026-27	2027-28	2028-29
Proposed SV	1.9	1.9	1.9	1.9	1.7	1.7	1.7	1.7	1.8	1.8
Baseline	1.9	1.9	2.0	2.0	1.8	1.8	1.9	1.9	2.0	2.0

Source: Port Stephens Council, *Application Part A*, Worksheet 9.

Our analysis indicates that over the next five years, the Council's infrastructure backlog ratio averages:

- 1.8% under the Proposed SV Scenario
- 1.9% under the Baseline Scenario.

Our analysis indicates that over the next seven years, the period of the proposed SV, the Council's infrastructure backlog ratio averages:

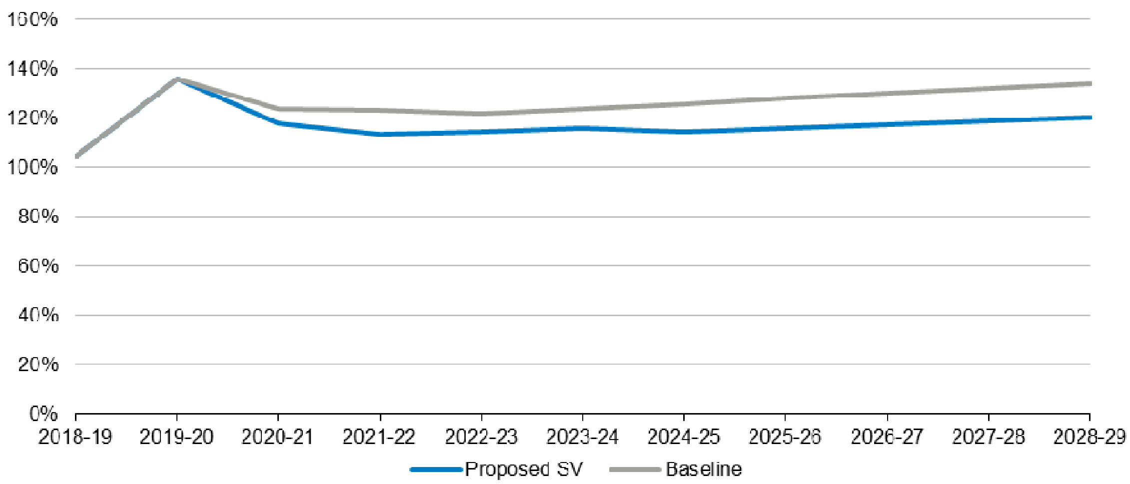
- 1.8% under the Proposed SV Scenario
- 1.9% under the Baseline Scenario.

Impact on the Council's infrastructure renewals ratio

With the proposed SV, the Council's infrastructure renewals ratio remains above the OLG benchmark of greater than 100%, averaging 118.4% over 10 years. Under the Baseline Scenario (ie, without the proposed SV revenue and without the SV expenditure), the Council forecasts it will still meet the OLG benchmark of greater than 100% over the 10 years to 2028-29, averaging 127.8%.

The Council's forecast infrastructure renewals ratio is shown in Figure 4.4 and Table 4.3 below.

Figure 4.4 Port Stephens Council's infrastructure renewals ratio (%) (2018-19 to 2028-29)



Data source: Port Stephens Council, *Application Part A*, Worksheet 9.

Table 4.3 Projected infrastructure renewal ratio (%) for Port Stephens Council's proposed SV application (2019-20 to 2028-29)

	2019-20	2020-21	2021-22	2022-23	2023-24	2024-25	2025-26	2026-27	2027-28	2028-29
Proposed SV	136.0	117.7	113.3	114.5	115.9	114.5	115.8	117.4	118.8	120.6
Baseline	136.0	123.6	123.2	121.6	123.7	125.8	127.9	130.0	132.1	134.3

Source: Port Stephens Council, *Application Part A,* Worksheet 9.

Our analysis indicates that over the next five years, the Council's infrastructure renewals ratio averages:

- 119.5% under the Proposed SV Scenario
- 125.6% under the Baseline Scenario.

Our analysis indicates that over the next seven years, the period of the proposed SV, the Council's infrastructure renewals ratio averages:

- 118.2% under the Proposed SV Scenario
- 126.0% under the Baseline Scenario.

Submissions from the community to IPART

IPART received 681 submissions during the consultation period from 11 February 2019 to 14 March 2019. A number of submissions suggested that the Council has not demonstrated a need for the revenue from the proposed SV and characterised the program of works proposed as 'nice to have' rather than needed. Other submissions noted that the Council had been found financially fit through the Fit for the Future program and queried how a 65.9% rate rise could now be required.

4.1.3 Overall assessment of the Council's financial need

Under the Baseline Scenario (without SV revenue and SV expenditure) the Council's OPR would average 2.7% over the next seven years which exceeds the OLG benchmark of greater than or equal to 0%. The Council's forecast under the Baseline with SV Expenditure Scenario shows that if it proceeds with the extensive program of expenditure included in its application without the proposed SV revenue, its OPR would average -2.3% over the next seven years, and -3.6% over the 10 years to 2028-29. This suggests that in the absence of the expenditure in the Council's SV proposal, there would be no financial need for the SV revenue, but that there would be this need with the expenditure. This therefore raises the question of whether the SV is justified to fund the proposed program of expenditure.

Our analysis also indicates that with the proposed SV revenue, the Council's forecast OPR in 2025-26 increases to 7.6% even after funding the proposed SV expenditure, which is above the OLG benchmark of greater than or equal to 0%. Over the seven years to 2025-26, the Council's OPR is forecast to average 5.0% with the SV, and 5.5% over the 10 years to 2028-29.

In some cases a higher level of operating surplus is needed to fund capital expenditure for example to reduce a council's infrastructure backlog. We found that the proposed SV expenditure is not required to reduce the Council's infrastructure backlog to reasonable levels. The Council forecasts that its infrastructure backlog ratio without the proposed SV expenditure would remain at 2.0% or below for the next 10 years, which meets the OLG benchmark of less than 2%. Similarly, the Council's infrastructure renewal ratio will exceed the OLG benchmark of 100% with or without the proposed SV.

We recognise that there may be other justifications for the proposed SV, particularly if, for example, ratepayers are willing to pay for it. However, we found evidence that a significant majority of the Council's ratepayers are not willing to pay for the proposed SV. The Council commissioned Micromex Research to conduct a phone survey measuring awareness and support for the proposed SV. The survey of 403 ratepayers presented four options, including rate peg only, a more modest 6.5% SV, the proposed SV and a more ambitious 8.5% SV. Only 8% of respondents preferred the proposed SV and a further 6% preferred the more ambitious 8.5% SV. 86% of respondents preferred either rate peg only or the more modest 6.5% SV.[34]

Taking into account the above factors, that the SV expenditure is not needed to meet infrastructure backlog or renewal benchmarks and the lack of community willingness to pay for the works the Council proposed be funded by the SV we have assessed that the Council has only partly demonstrated a financial need for additional revenue above the rate peg.

34 Port Stephens Council, *Attachment 6 – Community Consultation Feedback*, p 38.

4.2 Community engagement and awareness

The OLG Guidelines outline consultation requirements for councils when proposing an SV application. Specifically:

- The Council's Delivery Program and LTFP should clearly set out the extent of the General Fund rate rise under the proposed SV. 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 (see Section 4.4 for this assessment).
- The Council's community engagement strategy for the proposed SV must demonstrate an appropriate variety of engagement methods to ensure community awareness and input occurred.

Ultimately, we consider evidence that the community is aware of the need for, and extent of, a rate rise. That is, whether the consultation conducted by the Council with ratepayers has been effective.

In this section we assess the consultation process, including the clarity of the consultation, the timeliness of the consultation and whether an effective variety of engagement methods were used to reach as many ratepayers as possible across all relevant rating categories.

We also examine the effectiveness of any direct community engagement and any council response to community feedback.

4.2.1 Assessment of consultation with the community

The Council has published a Community Consultation Strategy.[35] It used this to guide and inform the consultation it carried out in relation to the proposed SV.

Process and Content

The material the Council prepared for ratepayers on its proposed SV contained the elements needed to ensure ratepayers were well informed and able to engage with the Council during the consultation process. Specifically, the Council:

- Clearly communicated the full impact of the proposed rate increase to ratepayers, including the cumulative increase and the rate increase across various categories of ratepayers.
- Communicated what the proposed SV would fund.
- Used a variety of engagement methods and materials.
- Provided opportunity for feedback.

35 Port Stephens Council, *Application Part B*, p 48.

Clarity

The Council's consultation material was clear in its presentation of the proposed SV and not likely to confuse ratepayers about the need for or impact of the proposed rate increase. The Council expressed the total rate increase including the rate peg.

Timeliness

The Council carried out community consultation on its SV proposal from July 2018 to November 2018.[36] This consultation period provided sufficient opportunity for ratepayers to be informed and engaged on the proposed SV.

Engagement methods used

The Council provided reasonable opportunities for community feedback, and used a variety of methods to engage with its community, including:[37]

- A mail-out to ratepayers detailing potential options for the rate rise as well as what the SV revenue would fund[38]
- A dedicated SV website with a fact sheet, SV booklet, and frequently asked questions with details on the proposed SV (and other options) and how to provide feedback[39]
- 28 public meetings with 540 total attendees[40]
- An online survey, a phone survey, and event exit-polls (see Section 4.2.2)[41]
- Advertisements online, print media, and social media and the Council's website[42]
- Hardcopy material handed out at events and displayed in public areas.[43]

The range of engagement methods used by the Council provided sufficient opportunity for ratepayers to be informed and engaged on the proposed SV. Using the various community engagement methods, the Council communicated the full cumulative increase of the proposed SV in both percentage terms and average dollar impact per ratepayer category.

We consider these methods were reasonable to communicate the impact of the proposed SV to the community.

36 Port Stephens Council, *Application Part B*, pp 53-55.
37 Port Stephens Council, *Application Part B*, pp 51-55.
38 Port Stephens Council, *Attachment 5 – Community Engagement Materials – Community Consultation*, p 19.
39 Port Stephens Council, *Attachment 5 – Community Engagement Materials – Community Consultation*, p 9; and Port Stephens Council, *Have Your Say Port Stephens*, https://haveyoursay.portstephens.nsw.gov.au/, accessed 30 April 2019.
40 Port Stephens Council, *Attachment 5 – Community Engagement Materials – Community Consultation*, p 7.
41 Port Stephens Council, *Application Part B*, p 66.
42 Port Stephens Council, *Attachment 5 – Community Engagement Materials – Community Consultation*, pp 51-53.
43 Port Stephens Council, *Attachment 5 – Community Engagement Materials – Community Consultation*, p 7.

4.2.2 Assessment of outcomes of consultation with the community

The Council received 198 submissions, 74% of which expressed a preference for a rate peg only increase, 16% preferred no specific option, and 10% expressed preference for an increase above the rate peg. The main reasons for opposition were:[44]

- The SV's impact on affordability, especially for those on fixed or low incomes
- The Council should live within its means and manage its budget better
- Inequitable spending across the LGA favouring larger tourist areas
- Lack of trust in the Council.

The Council indicated in its application that it considered its community's feedback and noted that it considered alternative options to the proposed SV. It concluded that without the rate increase it would not be able to fund the proposed projects, and it decided to proceed with an increase of 7.5% per annum instead of its initially preferred option of an increase of 8.5% per annum.[45]

4.2.3 Submissions from the community to IPART

IPART received 681 submissions during the consultation period from 11 February 2019 to 14 March 2019. A significant number were in relation to dissatisfaction with the Council's consultation during the SV application process. In particular, several submissions suggested that the Council's consultation process did not give sufficient opportunity for feedback, that the feedback received by the Council was overwhelmingly negative, and that the Council did not consider the community feedback when making its subsequent application to IPART.

We found that the Council's level of consultation was sufficient; that its consultation material was clear and included the relevant information; and that it provided adequate opportunities for feedback. We note that community feedback both during the Council's consultation period and IPART's consultation period was mostly negative. The Council is required to engage with its community and consider feedback.

4.2.4 Overall assessment of community engagement and awareness

The Council clearly communicated the rate increases in percentage terms and average dollars per ratepayer category, using a variety of materials and engagement methods. The Council sent a letter to all ratepayers and paid for online and print media, which directed ratepayers to the Council's website. The website and information booklet provided details on the proposed SV options. It is clear from submissions that we have received that ratepayers are aware of the proposal and the cumulative increase in rates at the end of seven years.

44 Port Stephens Council, *Application Part B*, pp 58-61.
45 Port Stephens Council, *Application Part B*, p 94.

A council should also seek feedback from its community on the proposed SV and demonstrate how it has considered and responded to issues of concern. Often these will revolve around the community's capacity and willingness to pay the proposed rate increase. The Council did seek feedback from ratepayers about its proposal, inviting submissions and conducting both phone and online surveys seeking ratepayer views on the proposal.

The Council demonstrated that its community is sufficiently aware of the stated need for, and extent of, the proposed rate increase.

4.3 Impact on affected ratepayers

The OLG Guidelines require that the impact of the proposed SV on affected ratepayers must be reasonable, having regard to both the current rate levels, existing ratepayer base and the proposed purpose of the variation. Specifically, the Delivery Program and LTFP 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
- Establish that the proposed rate increases are affordable, having regard to the community's capacity to pay.

Section 4.4 of this report considers the Council's Delivery Program and LTFP.

The focus of this criterion is to examine the impact the proposed SV would have on ratepayers, and in particular consider the reasonableness of the rate increase in the context of the purpose of the proposed SV.

In this section, we consider how the Council has informed ratepayers of the impact of the proposed SV on their rates and addressed affordability concerns.

We also undertake our own analysis of the reasonableness of the proposed rate increase by considering the average growth in the Council's rates in recent years, how the Council's average rates compare to similar councils, and other socio-economic indicators such as median household income and SEIFA ranking.

In its application, the Council indicated it intended to increase rates evenly for each rating category. The Council has calculated that:

- The average residential rate would increase by $78 in 2019-20 or cumulatively by $690 over seven years.
- The average business rate would increase by $333 in 2019-20 or cumulatively by $2,934 over seven years.
- The average farmland rate would increase by $121 in 2019-20 or cumulatively by $1,068 over seven years.

Table 4.4 sets out the Council's estimates of the expected increase in average rates in each main ratepayer category.

Table 4.4 Indicative annual increases in average rates under Port Stephens Council's proposed SV (2018-19 to 2025-26)

Ratepayer Category	2018-19	2019-20	2020-21	2021-22	2022-23	2023-24	2024-25	2025-26	Cumulative Increase
Residential $	**1,047**	**1,125**	**1,209**	**1,300**	**1,398**	**1,502**	**1,615**	**1,736**	
$ increase		78	84	91	98	105	113	121	690
% increase		7.5	7.5	7.5	7.5	7.5	7.5	7.5	65.9
Business $	**4,454**	**4,787**	**5,146**	**5,532**	**5,947**	**6,393**	**6,872**	**7,388**	
$ increase		333	359	386	415	446	479	515	2,934
% increase		7.5	7.5	7.5	7.5	7.5	7.5	7.5	65.9
Farmland $	**1,621**	**1,742**	**1,873**	**2,103**	**2,164**	**2,326**	**2,501**	**2,689**	
$ increase		121	131	140	151	162	174	188	1,068
% increase		7.5	7.5	7.5	7.5	7.5	7.5	7.5	65.9

Note: 2018-19 is included for comparison. The average rate is calculated by dividing total Ordinary Rates revenue by the number of assessments in the category and includes the ordinary rate and any special rates applying to the rating category.

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

4.3.1 Assessment of the Council's consideration of impact on ratepayers

In its application the Council examined socio-economic indicators such as its SEIFA index, average rates in comparison to other councils in the Lower Hunter region, median household income and mortgage and rent levels. The Council indicated it offers pensioner concessions for eligible pensioners. It also submitted it has hardship support measures in place and plans to introduce further measures if the proposed SV is fully approved. The Council also considered the willingness of its community to pay the proposed rate increases. The Council found that its:[46]

- Average residential rate is currently the lowest of comparable councils in the Hunter Region.[47] With the proposed SV, the Council's rates would be on par with Lake Macquarie, but less than that of Newcastle and Maitland.
- Average business rate is currently lower than that of Lake Macquarie, Newcastle, and Maitland, but higher than Cessnock. With the proposed SV, the Council's rates would be less than Newcastle and Maitland, but higher than Cessnock and Lake Macquarie.
- Average farmland rate is the lowest of comparable councils. With the proposed SV, the Council's rates would be less than Cessnock, Newcastle and Maitland, but higher than Lake Macquarie.
- Median weekly household income in 2016 ($1,180) is considerably lower than Lake Macquarie ($1,313), Newcastle ($1,368), and Maitland ($1,415), but higher than Cessnock ($1,117).
- Proportion of ratepayers who are pensioners (18.9%) is lower than Cessnock (20.1%) and Lake Macquarie (21.3%), but higher than Newcastle (18.7%) and Maitland (17.1%).

46 Port Stephens Council, *Application Part B*, pp 84-117.

47 The Council compared its average rates to Cessnock, Lake Macquarie, Newcastle, and Maitland.

On the basis of these indicators, the Council found that the impact on ratepayers would be reasonable.

The Council has stated that its community consultation showed little support for the rate rise, but strong support for infrastructure and service delivery improvements.

The Council intends to introduce a new Rates Assistance Program for non-pensioners if the proposed SV is approved. The Council's current and proposed hardship policy and Rates Assistance Program provide assistance measures including the following:[48]

- Flexible periodic payment options
- Interest reduction, with interest charges written off where payment of the interest would cause hardship
- Limited writing-off of rates and charges

The Council has measures in place to assist pensioners such as:[49]

- Deferral of rates against the estate for aged pensioners
- Reduction of specific charges such as the waste service charge
- Pensioner rate concession of $250 per annum

4.3.2 IPART's consideration of impact on ratepayers

To assess the reasonableness of the impact of the proposed SV on ratepayers, we examined the Council's SV history and the average annual growth of rates in various rating categories. We found that since 2008-09:

- The Council has applied for and been granted one SV, in 2008-09, for a single-year 5.3% permanent increase for its economic development program and to maintain existing services.
- Since 2009-10, the average annual growth in residential, business, and farmland rates was 3.1%, 3.0%, and 2.0%, respectively, which compares with the average annual growth in the rate peg of 2.5% over the same period.

We also compared current rates and socio-economic indicators in the LGA with OLG Group 5 and surrounding councils as shown in Table 4.5.

48 Port Stephens Council, *Application Part B*, pp 110-113.
49 Port Stephens Council, *Application Part B*, pp 88 and 110-113.

Table 4.5 Port Stephens Council – comparison of rates and socio-economic indicators with surrounding councils and Group 5 averages (2016-17)

Council (OLG Group)	Average residential rate ($)[a]	Average business rate ($)	Average farmland rate ($)	Median annual household income ($)[b]	Ratio of average rates to median income (%)	Outstanding rates ratio (%)	SEIFA Index NSW Rank[c]
Maitland (5)	1,224	6,552	3,056	73,580	1.7	2.1	75
Lake Macquarie (5)	1,257	4,543	2,000	68,276	1.8	0.0	89
Cessnock (4)	1,090	3,056	2,709	61,204	1.8	2.0	12
Port Stephens (5)	**969**	**4,047**	**1,703**	**61,360**	**1.6**	**2.8**	**70**
Group 5 Average	1,206	6,986	2,700	61,691	2.0	4.1	-

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 2016-2017; 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 2016-17 data, we found that the Council's:

- Average residential rates of $969 were 20% lower than the average for Group 5 councils and the lowest of the surrounding councils.
- Average business rates of $4,047 were 42% lower than the average for Group 5 councils and relatively low compared to surrounding councils.
- Average farmland rates of $1,703 were 37% lower than the average for Group 5 councils and the lowest of the surrounding councils.
- Average rates to income ratio was 0.4 percentage points lower than the average for Group 5 councils and relatively low compared to surrounding councils
- Outstanding rates ratio was 1.3 percentage points lower than the average for Group 5 councils and relatively high compared to surrounding councils
- SEIFA ranking indicates that the Council's area is roughly similar to Maitland and Lake Macquarie, but less disadvantaged than Cessnock.

We also compared the Council's average rate levels with the proposed SV to its OLG Group average[50] rate levels over the proposed seven year period and found that the Council's:

- Average residential rate of $1,736 in 2025-26 would be $245 (16.4%) higher than the estimated 2025-26 average residential rate for Group 5 councils of $1,491
- Average business rate of $7,388 in 2025-26 would be $1,252 (14.5%) lower than the estimated 2025-26 average business rate for Group 5 councils of $8,639.
- Average farmland rate of $2,689 in 2025-26 would be $650 (19.5%) lower than the estimated 2025-26 average farmland rate for Group 5 councils of $3,339.

50 Based on the 2016-17 data obtained from OLG, IPART has performed calculations to increase the OLG Group 5 average rate levels by the rate peg each year from 2017-18 to 2025-26 to allow for comparison of the Council's proposed average rate levels with the SV over the proposed SV period.

We have found that there is little ratepayer willingness to pay for the proposed SV. The Council commissioned Micromex Research to conduct a phone survey measuring awareness and support for the proposed SV. The survey of 403 ratepayers presented four options, including rate peg only, a more modest 6.5% SV, the proposed SV and a more ambitious 8.5% SV. Only 8% of respondents preferred the proposed SV and 6% of respondents preferred the higher 8.5% option. 86% of respondents preferred either rate peg only or the more modest 6.5% SV.[51]

Similarly the Council's online survey of 1,016 respondents found that 74% preferred a rate-peg only option, 10% preferred a 6.5% increase, 3% supported the proposed 7.5% increase, and 4% supported an 8.5% increase.[52]

Submissions from the community to IPART

IPART received 681 submissions during the consultation period from 11 February 2019 to 14 March 2019. A large portion of the submissions raised concerns regarding affordability of rates after the proposed SV is applied. In particular, the submissions raised concerns regarding the Council rates after seven years when the full 65.9% increase is in effect, especially for pensioners and young families. We have found that while current rates are reasonable, if the proposed SV were to be approved in full the average residential rates would be considerably higher than the estimated average residential rates of OLG Group 5.

4.3.3 Overall assessment of impact on affected ratepayers

We found that the impact of the proposed SV on affected ratepayers of the Council would be considerable and only partly reasonable, given:

- The cumulative dollar increase over seven years is substantial for the average residential ratepayer ($690)
- The comparison with the OLG Group 5 average shows that the Council's average rates in 2016-17 are relatively low across all rating categories, however, the projected residential rates by the end of the seven year proposed SV period would be considerably higher than the estimated rates for OLG Group 5
- The Council has only partly demonstrated a need for additional funding to implement the proposed projects
- There is a lack of ratepayer willingness to pay, as only 14% of respondents to the Council's phone survey and 7% of respondents to the online survey preferred an annual increase of 7.5% or more.

51 Port Stephens Council, *Attachment 6 – Community Consultation Feedback*, pp 23 and 34-38.
52 Port Stephens Council, *Application Part B*, pp 64-66.

4.4 Integrated Planning and Reporting documents

The IP&R framework provides a mechanism for councils and the community to engage in important discussions about service levels and funding priorities and to plan in partnership for a sustainable future. The IP&R framework therefore underpins decisions on the revenue required by each council to meet the community needs and demands.

The OLG Guidelines require the Council to exhibit, approve and adopt the relevant IP&R documents before submitting an application for a proposed SV to demonstrate adequate planning.

The relevant documents are the Community Strategic Plan, Delivery Program, LTFP and, where applicable, Asset Management Plan. Of these, the Community Strategic Plan and Delivery Program require (if amended) public exhibition for 28 days. The OLG Guidelines require that the LTFP be posted on the Council's website.

In this section, we assess whether the Council has included the proposed SV in its IP&R framework as outlined in Criterion 1 to 3 of the OLG Guidelines and exhibited, approved and adopted its IP&R documents.

According to the OLG Guidelines, the elements that should be included in the IP&R documentation are:

- The need for, and purpose of, the proposed SV
- The extent of the general fund rate rise under the proposed SV
- The impact of any rate rises upon the community.

4.4.1 Assessment of the content of IP&R documents

The need for, and purpose of, the proposed SV

The Council presented the need for, and purpose of, the proposed SV in both the Delivery Program and the LTFP. The Council's Delivery Program and LTFP also canvassed alternatives to the rate rise, such as grants, adjusting fees and charges, and applying for loans (see Section 4.1.1).

The LTFP shows the financial impact of the SV by presenting both a baseline scenario reflecting the business as usual model excluding the proposed SV and a proposed SV scenario reflecting the additional revenues and expenditures expected with the proposed SV in place.[53]

The extent of the general fund rate rise under the proposed SV

The Delivery Program includes the full cumulative increase of the proposed SV in percentage terms and dollar terms for the average ratepayer in each category.[54]

53 Port Stephens Council, *Long Term Financial Plan*, pp 69-71 and 89-92.
54 Port Stephens Council, *Delivery Program*, pp 7 and 23-27.

The impact of any rate rises upon the community

It is not evident from the Delivery Program nor the LTFP that the Council considered the community's capacity and willingness to pay rates under the proposed SV (although it did outline its consideration of this in its application, see Section 4.3.1).

4.4.2 Assessment of the exhibition, approval and adoption of IP&R documents

The Council publicly exhibited the updated versions of its Community Strategic Plan, Delivery Program, LTFP, and Strategic Asset Management Plan from 14 November 2018 to 21 December 2018. The Community Strategic Plan, Delivery Program, LTFP, and Strategic Asset Management Plan were adopted on 29 January 2019.[55]

Submissions from the community to IPART

IPART received 681 submissions during the consultation period from 11 February 2019 to 14 March 2019. Some submissions suggested that the Council's application to IPART, including its IP&R documents, did not reflect what was exhibited to the community during the Council's consultation period. We found that the Council's IP&R documents were amended after an initial round of consultation, but that these amendments were allowed under the OLG Guidelines as part of the consultation and feedback process as they are not substantial.

4.4.3 Overall Assessment of the IP&R documents

We consider that the Council's IP&R documents contain sufficient information relating to the proposed SV and they have been appropriately exhibited, approved, and adopted.

4.5 Productivity improvements and cost containment strategies

The OLG Guidelines require councils to explain the productivity improvements and cost containment strategies that have been realised in past years and are expected to be realised over the proposed SV period.

Achieving cost savings through improved productivity can reduce the need for, or extent of, the increase to general income needed through a proposed SV.

4.5.1 Assessment of efficiency gains achieved

The Council's application sets out the productivity improvements and cost containment initiatives it has undertaken in recent years. In particular, it submitted that it had:[56]

- Implemented a Service Review Program in 2011, a comprehensive 16-step, 4-yearly review of the Council's services based on the Australian Business Excellence Framework that seeks to find at least 2% efficiency savings. This has led to an estimated $2.1 million in savings, including its:

55 Port Stephens Council, *Application Part B*, p 55.
56 Port Stephens Council, *Application Part B*, pp 125-142.

- Children's Services review in 2013, which has generated an estimated $215,000 in annual savings
- Strategic and Environment review in 2018, which has generated an estimated $94,000 in annual savings

- Introduced numerous energy efficiency initiatives to reduce energy costs, such as installing solar panels on surf clubs and fire stations to reduce energy costs
- Entered its Karuah land into the NSW Government BioBanking scheme earning $533,000 in revenue since 2012-13
- Engaged in shared services with the Hunter Joint Organisation of councils[57] such as library services, weed management, records storage, legal services, regional procurement, and environmental services
- Introduced electronic lodgement and processing of development applications
- Received $5.5 million in revenue in 2017-18 from property sales.

4.5.2 Assessment of strategies in place for future productivity improvements

The Council indicated that it is planning future efficiency measures over the proposed SV period. Specifically, it proposes to:[58]

- Continue to seek and develop investment opportunities such as:
  - Investment in the Newcastle Airport Partnership and Greater Newcastle Aerotropolis Partnership Limited
  - Developing a lease for the extraction of sand from Council land at Cabbage Tree Road, Williamstown, with an estimated $18m in potential revenue over the next 12-15 years
  - Opening of a new koala sanctuary in Treescape Park.
- Achieve ongoing efficiency savings from recently installed solar panels on administration buildings, which would reduce annual grid energy consumption by an estimated 25% and generate 1,795 small-scale tradeable technology certificates, valued at $62,825.
- Continue to implement its Service Review Program by reviewing each council service at a minimum of once every four years.

4.5.3 Overall assessment of productivity improvements and cost containment strategies

We found that the Council has explained its productivity improvements and cost containment strategies. It has also quantified the cost savings that have resulted from the implementation of some of these strategies, and outlined future productivity improvements.

57 The Hunter Joint Organisation of Councils consists of Cessnock (list all 10 and then reference). Hunter Joint Organisation, Our Member Councils, http://strategicservicesaustralia.com.au/our-member-councils/, accessed: 30 April 2019.

58 Port Stephens Council, *Application Part B*, pp 144-145.

5 Our Decision

Our decision means that the Council may not increase its general income by more than the rate peg (2.7%) in 2019-20. The Council is to determine how the rate peg increase will be distributed among ratepayer categories.

If the Council wishes to use additional rates revenue provided by an SV to fund future projects, it could apply to IPART for an SV in future years.

Appendices

A Assessment criteria for Special Variation applications

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. The IP&R documents and the council's application should provide evidence to establish this criterion. This 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. 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. 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.
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 Plan 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.

Assessment criteria
Additional matters In assessing an application against the assessment criteria, IPART considers 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: Office of Local Government, *Guidelines for the preparation of an application for a special variation to general income*, October 2018, pp 8-9.

B Expenditures to be funded from the Special Variation above the rate peg

Tables B.1 and B.2 show the Council's proposed expenditure of the SV funds over the next 10 years under its application.

The Council intended to use the additional SV revenue, above the rate peg, of $133.4 million over 10 years to fund:[59]

- Major one-off infrastructure projects such as town centre upgrades
- Upgrades to existing infrastructure
- Footpaths and cycle ways
- Sports facility improvements
- Drainage improvements
- Carpark improvements
- Repayments on borrowings.

The Council intended to borrow $60 million in addition to the SV revenue to fund the proposed projects.[60]

59 Port Stephens Council, *Application Part A*, Worksheet 6.

60 Port Stephens Council, *Delivery Program*, pp 11-12; and Port Stephens Council, *Application Part B*, pp 11-12.

Table B.1 Port Stephens Council – Revenue and proposed expenditure over 10 years related to the proposed SV ($000) (2019-20 to 2028-29)

	2019-20	2020-21	2021-22	2022-23	2023-24	2024-25	2025-26	2026-27	2027-28	2028-29	Total
Special variation revenue above assumed rate peg	2,019	4,330	6,869	9,654	12,704	16,041	19,687	20,180	20,684	21,201	133,368
Funding for increased operating expenditures	1,300	1,823	2,516	3,882	5,374	6,085	6,423	7,160	7,237	7,063	48,862
Funding for capital expenditure	11,150	12,350	12,500	11,600	14,500	13,550	10,000	12,500	9,250	7,750	115,150
Other uses (principal repayments)	550	1,129	1,685	2,155	2,780	3,247	3,247	3,478	3,478	3,478	25,225
Total expenditure	**13,000**	**15,301**	**16,701**	**17,637**	**22,654**	**22,882**	**19,669**	**23,138**	**19,964**	**18,290**	**189,237**

Note: Numbers may not add due to rounding. Total SV expenditure equals funding for increased operating expenditures plus funding for capital expenditure. The Council indicated that it proposes to raise an additional $133.4 million from the SV revenue, which would be leveraged with loans of $60 million.

Source: Port Stephens Council, *Application Part A,* Worksheet 6, Port Stephens Council, *Delivery Program*, pp 11-12; and Port Stephens Council, *Application Part B*, pp 11-12.

Table B.2 Port Stephens – Proposed 10-year capital expenditure program related to the proposed SV ($000) (2019-20 to 2028-29)

	2019-20	2020-21	2021-22	2022-23	2023-24	2024-25	2025-26	2026-27	2027-28	2028-29	Total
Renewals											
Roads rehabilitation and reseals	500	1,000	2,500	3,150	4,000	4,000	4,000	5,000	5,500	5,500	35,150
Community Facilities & Amenities											
Public toilet renewals	1,000	1,000	-	-	-	-	-	-	-	-	2,000
BBQ amenities	500	-	-	-	-	-	-	-	-	-	500
New assets											
Town Centre Revitalisation											
Raymond Terrace and King St	375	375	2,500	2,500	2,250	2,250	2,250	2,250	250	-	15,000
Nelson Bay and Car Parking	375	375	2,500	2,500	2,250	2,250	2,250	2,250	250	-	15,000
Medowie and drainage	-	-	-	700	2,250	2,050	-	-	-	-	5,000
Karuah	500	1,500	-	-	-	-	-	-	-	-	2,000
Anna Bay	-	-	-	250	750	1,000	-	-	-	-	2,000
Lemon Tree Passage/Tanilba Bay	500	1,500	-	-	-	-	-	-	-	-	2,000
Fingal	-	-	500	-	-	-	-	-	-	-	500
Fern Bay	-	-	1000	-	-	-	-	-	-	-	1,000
Seaham projects	500	-	-	-	-	-	-	-	-	-	500
Community Facilities & Amenities											
Arts Centre	-	-	-	-	-	-	-	-	250	1,750	2,000

Birubi interchange	-	-	-	-	-	-	500	2,500	-	-	3,000
Mallabula Hall	-	-	500	-	-	-	-	-	-	-	500
Footpaths and Cycleways											
LGA wide	3,600	2,600	-	-	-	-	-	500	500	500	7,700
Bandy Hill	-	-	-	-	-	-	-	-	2,000	-	2,000
Sports Facilities											
Tomaree Sports Complex redevelopment	-	-	-	-	3,000	-	-	-	-	-	3,000
Hinton Sports Fields	800	-	-	-	-	-	-	-	-	-	800
King Park Sports field redevelopment	-	-	-	-	-	2,000	1,000	-	-	-	3,000
Shoal Bay Drainage	2,000	-	-	-	-	-	-	-	-	-	2,000
Soldiers Point Carparking	-	-	-	-	-	-	-	-	500	-	500
Street Lighting upgrade	-	1,000	500	500	-	-	-	-	-	-	2,000
Foreshore improvements	500	1,500	500	500	-	-	-	-	-	-	3,000
Depot relocation Raymond Terrace and Nelson Bay	-	1,500	2,000	1,500	-	-	-	-	-	-	5,000
Total Asset Renewal	**2,000**	**2,000**	**2,500**	**3,150**	**4,000**	**4,000**	**4,000**	**5,000**	**5,500**	**5,500**	**37,650**
Total New Assets	**9,150**	**10,350**	**10,000**	**8,450**	**10,500**	**9,550**	**6,000**	**7,500**	**3,750**	**2,250**	**77,500**
Total Capital Expenditure	**11,150**	**12,350**	**12,500**	**11,600**	**14,500**	**13,550**	**10,000**	**12,500**	**9,250**	**7,750**	**115,150**

Note: Numbers may not add due to rounding.

Source: Port Stephens Council, *Application Part A*, Worksheet.

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 the Council have changed over the four years to 2016-17. Table C.2 compares selected published and unpublished data about the Council with the averages for the councils in its OLG Group, and for NSW councils as a whole.

Table C.1 Trends in selected performance indicators for Port Stephens Council (2013-14 to 2016-17)

Performance indicator	2013-14	2014-15	2015-16	2016-17	Average annual change (%)
FTE staff (number)	405	419	419	408	0.2
Ratio of population to FTE	170	166	170	174	0.9
Average cost per FTE ($)	88,980	93,100	97,072	102,439	4.8
Employee costs as % operating expenditure (General Fund only) (%)	36.3	36.4	35.5	38.2	-

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 Port Stephens Council (2016-17)

	Port Stephens Council	OLG Group 5 average	NSW average
General profile			
Area (km^2)	858	-	-
Population (2016)	71,118	-	-
General Fund operating expenditure ($m)	109.5	154.6	76.3
General Fund operating revenue per capita ($)	1,859	-	-
Rates revenue as % General Fund income (%)	40.4	47.0	42.5
Own-source revenue ratio (%)	76.7	70.0	66.0
Average rate indicators[a]			
Average rate – residential ($)	969	1,206	1,053
Average rate – business ($)	4,047	6,986	5,738
Average rate – farmland ($)	1,703	2,700	2,500
Socio-economic/capacity to pay indicators			
Median annual household income, 2016 ($)[b]	61,360	61,691	77,272
Average residential rates to median income, 2016 (%)	1.6	2.0	1.4
SEIFA, 2016 (NSW rank: 130 is least disadvantaged)	70	-	-
Outstanding rates and annual charges ratio (General Fund only) (%)	2.8	4.1	3.5
Productivity (labour input) indicators[c]			
FTE staff (number)	408	671.1	356
Ratio of population to FTE	174.3	-	-
Average cost per FTE ($)	102,439	90,382	91,762
Employee costs as % operating expenditure (General Fund only) (%)	38.2	36.5	38.8

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

Source: OLG, *Time Series Data 2016-2017*, 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 Glossary

ABS	Australian Bureau of Statistics
Ad valorem rate	A rate based on the value of real estate.
Baseline Scenario	Shows the impact on the Council's operating and infrastructure assets' performance without the proposed SV revenue and expenditure.
Baseline with SV expenditure Scenario	Includes the Council's full expenses from its proposed SV, without the additional revenue from the proposed SV. This scenario is a guide to the Council's financial sustainability if it still went ahead with its full expenditure program included in its application, but could only increase general income by the rate peg percentage.
General income	Income from ordinary rates, special rates and annual charges, other than income from other sources such as special rates and charges for water supply services, sewerage services, waste management services, annual charges for stormwater management services, and annual charges for coastal protection services.
IPART	The Independent Pricing and Regulatory Tribunal of NSW
Local Government Act	*Local Government Act 1993* (NSW)
OLG	Office of Local Government
PGI	Permissible General Income is the notional general income of a council for the previous year as varied by the percentage (if any) applicable to the Council. A council must make rates and charges for a year so as to produce general income of an amount that is lower that the PGI.
Proposed SV Scenario	Includes the Council's proposed SV revenue and expenditure.
SEIFA	Socio-Economic Indexes for Areas (SEIFA) is a product developed by the ABS that ranks areas in

	Australia according to relative socio-economic advantage and disadvantage. The indexes are based on information from the five-yearly Census. It consists of four indexes, the Index of Relative Socio-economic Disadvantage (IRSD), the Index of Relative Socio-economic Advantage and Disadvantage (IRSAD), the Index of Economic Resources (IER), and the Index of Education and Occupation (IEO).
SV	Special variation is the percentage by which a council's general income for a specified year may be varied as determined by IPART under delegation from the Minister.