

Independent Pricing and Regulatory Tribunal
New South Wales

Special variation increase

Shoalhaven City Council 2018-19

Determination
Local Government

May 2018

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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.

Shoalhaven City Council (Shoalhaven Council) applied for a multi-year special variation to:

- ▼ increase its general income by 17.1% in 2018-19 and 5.0% in each year for 2019-20 and 2020-21, a cumulative increase of 29.1%, and
- ▼ retain this increase in its rate base permanently.¹

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

1.1 We have approved Shoalhaven City Council's application for a special variation

We decided to allow the special variation as requested.

Our decision means that Shoalhaven Council may increase its general income between 2018-19 and 2020-21 by the annual percentages shown in Table 1.1. This will allow the council to improve its financial sustainability, fund capital expenditure, reduce its infrastructure backlog, reduce its operating deficit, fund asset renewal and maintenance and make repayments on the Verons Estate Loan.²

The annual increases include the rate peg of 2.3% in 2018-19, and an assumed rate peg of 2.5% in 2019-20 and 2020-21.³

The cumulative increase that we have approved of 29.1% is 21.6% more than the assumed cumulative rate peg for these years. This increase may be retained in the council's general income base permanently.

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

	2018-19	2019-20	2020-21
Percentage increase approved	17.1	5.0	5.0

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

² Shoalhaven City Council, *Special Variation Application Form – Part B for 2018-19* (Shoalhaven Council, *Application Part B*), pp 5-6.

³ The special variation percentage approved will not change to reflect the actual rate peg in future years.

Shoalhaven Council has a temporary existing special variation that expires at the end of 2017-18, reducing the council's general income by 10.3%.⁴ The net increase in general income over 2017-18 levels over the three years to 2020-21 is 15.8% after accounting for the expiring variation.

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 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 meets the criteria

Our decision reflects our finding that the council's application meets the requirements in the OLG criteria.

Our assessment against each criterion is summarised in Table 1.2.

⁴ Shoalhaven Council, *Application Part B*, p 5 and Shoalhaven Council, *Application Part A*, Worksheet 1. The expiring component is 10.34% of the council's 2017-18 notional general income.

Table 1.2 Assessment of Shoalhaven City Council's special variation application

1. Financial Need	
	<p>The council demonstrated the financial need for the special variation (SV):</p> <ul style="list-style-type: none"> ▼ Operating Performance Ratio (average 2018-2019 to 2027-28) is: <ul style="list-style-type: none"> – 4.0% with SV, or – -2.6% without SV revenue and assuming SV expenditure. ▼ Infrastructure backlog ratio in 2026-27 is: <ul style="list-style-type: none"> – 2.0% with SV (meets benchmark of <2%), or – 3.2% without SV. ▼ Infrastructure renewal ratio in 2026-27: <ul style="list-style-type: none"> – 76.3% with SV (does not meet benchmark of >100%), or – 50.8% without SV.
2. Community awareness	
	<p>The council demonstrated the community is aware of the need for and extent of the rate rise. It:</p> <ul style="list-style-type: none"> ▼ provided a detailed explanation about the purpose and impact of the SV in its IP&R documentation and sought feedback ▼ used a range of engagement methods (eg, mail out, media, public meetings, interacting with Community Consultative Bodies and its website), and ▼ reported that its feedback from submissions shows some residents oppose the SV. IPART received three submissions all opposing the SV.
3. Impact on ratepayers	
	<p>The impact on ratepayers will be substantial, but reasonable given:</p> <ul style="list-style-type: none"> ▼ the average residential and business rates were lower than the OLG Group 5 average ▼ the average rate to median income ratio was lower than the OLG Group 5 average ▼ the SEIFA ranking (50) indicates some level of disadvantage ▼ the Verons Estate special rate is consistent with collecting revenue from those who should benefit from the proposed expenditure, and ▼ the council has a 13.2% temporary special variation expiring at the end of 2017-18. As a result, the net increase in rates from current levels will be smaller than the 29.1% the council has applied for (about 16% for residential, business and farmland ratepayers).
4. IP&R documents exhibited	
	<p>The council updated its Integrated Strategic Plan and adopted its Community Strategic Plan in June 2017. It:</p> <ul style="list-style-type: none"> ▼ exhibited its Deliver Program, Long Term Financial Plan, and additional Special Rate Variation Chapter during October and November 2017, and ▼ adopted its updated IP&R documents setting out the proposed special variation on 28 November 2017.
5. Productivity improvements and cost containment	
	<p>Over the past five years, the council has realised savings from initiatives including:</p> <ul style="list-style-type: none"> ▼ reviewing and reducing its operational costs and reducing costs, such as those relating to salaries, fleet size and electricity (\$6.4 million annually from 2012-13 to 2015-16), and ▼ reducing costs relating to materials and contracts (\$1.8 million in 2016-17). <p>It also estimates savings from future initiatives over the next two years from 2017-18 including:</p> <ul style="list-style-type: none"> ▼ improving management of employee fringe benefits and leave liabilities (\$280,000) ▼ performing reviews of its services and outsourcing (\$250,000), and ▼ pursuing purchases through the Illawarra Shoalhaven Joint Organisation (\$100,000).

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 Shoalhaven City Council's approved special variation

IPART's approval of Shoalhaven Council's application for a special variation over the period 2018-19 to 2020-21 is subject to the following conditions:

- ▼ The council uses the additional income from the special variation for the purposes of improving financial sustainability, funding capital expenditure, reducing its infrastructure backlog, reducing its operating deficit, increasing expenditure on maintaining and renewing infrastructure assets and making repayments on the Verons Estate Loan as outlined in the council's application and listed in Appendix B.
- ▼ The council reports in its annual report for each year from 2018-19 to 2027-28 on:
 - the actual revenues, expenses and operating balance against the projected revenues, expenses and operating balance, as outlined in the Long Term Financial Plan provided in the council's application, and summarised in Appendix C
 - any significant variations from its proposed expenditure as forecast in the current Long Term Financial Plan and the reasons for such variation
 - 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.

The council is to reduce its general income for 2018-19 by \$7,178,226 (the value of the expiring special variation) before its general income is increased in 2018-19 in accordance with IPART's determination.

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 Shoalhaven City Council's application

Shoalhaven Council applied for a special variation to increase its general income by a cumulative 29.10% over the 3-year period from 2018-19 to 2020-21,⁵ and to permanently retain this increase in its general income base.⁶ As required under the OLG Guidelines,⁷ the council applied for the special variation on the basis of its most recent, adopted Integrated Planning and Reporting (IP&R) documents, in particular its Integrated Strategic Plan 2017 which comprises the council's:

- ▼ Community Strategic Plan
- ▼ Delivery Program & Operational Plan (Delivery Program)
- ▼ Resourcing Strategy containing its Long Term Financial Plan, and
- ▼ an additional Special Rate Variation Chapter relating to its 2018-19 proposed special variation.

The increase in 2018-19 includes the renewal of an existing special variation that is due to expire on 30 June 2018.

In 2017-18, the council applied for a permanent special variation with a cumulative increase of 29.05% over two years.⁸ However, we only approved a temporary increase of 13.20% for 1-year because the council did not update its IP&R documents to include the special variation increase prior to applying to IPART.⁹ The council's application in 2018-19 is consistent with its 2017-18 proposal for a permanent increase in general income to improve financial sustainability and fund asset renewal and maintenance, operational works, and make Verons Estate loan repayments.¹⁰

The expiring special variation reduces the council's general income at the end of 2017-18 by 10.34%. Applying the proposed special variation of 17.10% in 2018-19 to this reduced base provides a total increase in general income of 5.04% between 2017-18 and 2018-19. In 2019-20 and again in 2020-21, general income will increase by 5.00%. The total increase over the three years is 15.81%.¹¹

The council estimates its permissible general income would increase from \$69.5 million in 2017-18 to \$80.4 million in 2020-21 if the requested special variation is approved. Over the

⁵ Shoalhaven Council, *Application Part A*, Worksheet 1. The council has a temporary special variation for 11.7% above the rate peg, which will expire 30 June 2018, reducing the council's general income by \$7,178,226. As a result, the net increase in the council's general income is estimated to be 15.81% over the three years.

⁶ Shoalhaven Council, *Application Part B*, p 5. The council is seeking to retain the 13.2% special variation (including the rate peg and Verons Estate component) approved as a temporary 1-year increase in 2017-18 as a permanent increase and for an additional 5.0% for each of the three years from 2018-19 (including the rate peg).

⁷ OLG Guidelines, November 2017, p 6.

⁸ IPART, *Shoalhaven City Council's application for a special variation for 2017-18*, May 2017, p 4.

⁹ IPART, *Shoalhaven City Council's application for a special variation for 2017-18*, May 2017, p 6 and 8.

¹⁰ IPART, *Shoalhaven City Council's application for a special variation for 2017-18*, May 2017, p 4.

¹¹ Shoalhaven Council, *Application Part A*, Worksheet 1.

3-year period of the special variation to 2020-21, this would generate additional revenue of \$34.0 million compared to rate increases at the assumed rate peg. This figure would increase to \$138.1 million over a 10-year period, as the additional revenue raised would remain permanently in the council's rate base.¹²

The council indicated it intends to use the additional revenue to fund operating expenses including repayments on its Verons Estate loan for infrastructure and capital expenditure for its assets – buildings, roads and parks and recreation facilities – and to improve its financial sustainability.¹³ The council indicates over the period from 2018-19 to 2027-28 it proposes to spend the additional special variation revenue as follows:

- ▼ \$89.4 million on capital expenditure as follows:
 - \$58.4 million on roads and transport renewals
 - \$25.4 million on buildings renewals, and
 - \$5.6 million on sports ground upgrades.
- ▼ \$36.0 million on increased operational expenditure
- ▼ \$11.2 million on infrastructure maintenance, and
- ▼ \$1.5 million on Verons Estate loan principal and interest repayments.¹⁴

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

When we assessed the council's Fit for the Future (FFTF) proposal in 2015 it indicated it was considering a special variation with cumulative rate increases of 21.00% over two years from 2017-18, including the rate peg. The council indicated that the additional funds raised would be applied to increasing infrastructure maintenance and renewal and improving financial sustainability.¹⁵ The purpose of the council's special variation application is consistent with its FFTF proposal. More detail on the council's FFTF assessment is available in Box 3.1.

The council's FFTF proposal also responded to the NSW Treasury Corporation (TCorp) assessment of the council's financial sustainability in 2012, which observed that the trend of declining operating results is not financially sustainable in the long term.¹⁶ TCorp also observed that asset maintenance and renewals performed is deteriorating, which would increase the council's infrastructure backlog.¹⁷ The council considered that it was necessary to increase its rate revenue to meet the benchmark for the Operating Performance Ratio by 2019-20, and assist in achieving the required spending on renewal and maintenance of infrastructure to satisfy the FFTF benchmarks.¹⁸

¹² Shoalhaven Council, *Application Part A*, Worksheet 1 and Worksheet 7.

¹³ Shoalhaven Council, *Application Part A*, Worksheet 6 and Shoalhaven Council, *Application Part B*, pp 5-6.

¹⁴ Shoalhaven Council, *Application Part A*, Worksheet 6.

¹⁵ Shoalhaven Council, *Council Improvement Proposal*, June 2015, pp 26, 47, 52 and 102.

¹⁶ Shoalhaven Council, *Council Improvement Proposal*, June 2015, p 93 and NSW Treasury Corporation, *Financial Assessment and Benchmarking Report*, October 2012, p 13.

¹⁷ NSW Treasury Corporation, *Financial Assessment and Benchmarking Report*, October 2012, p 17.

¹⁸ Shoalhaven Council, *Council Improvement Proposal*, June 2015, pp 47-50.

2.1 Verons Estate

The Verons Estate is a subdivision comprising 32 lots, each around eight hectares, near Sussex Inlet. The original owner sold off individual lots after 1964. The land was historically zoned rural. Rural zoning does not permit dwellings to be approved on these lots as they are smaller than the 40 hectare minimum required. Nevertheless, there are a number of structures that have been built on the estate.

The council has been investigating rezoning the estate to allow dwellings to be approved on each lot since 1993.¹⁹ The council has now rezoned land to allow for some development to occur on most of the plots. However, the rezoning is contingent on the estate meeting current development standards, particularly standards relating to mitigating bushfire risk. This means a number of roads within the estate need to be upgraded, as well as fire trails established, in order to ensure the safety of the residents and that the Fire Service has ready access to all dwellings.

The council proposes to cover 17.0% of the cost in recognition of the potential benefit of the road upgrades to the broader community.²⁰ The remainder of the cost will be met by a 20-year loan of \$2.3 million to provide essential fire safety and road infrastructure to the estate, which is being paid for by a special rate levied on the Verons Estate landowners.²¹

The Verons Estate special rate commenced on 1 July 2017 at an average rate of \$5,350 per year.²² It will continue for 20 years to fund loan principal and interest payments.²³ The council estimates the revenue from the Verons Estate special rate is 0.2% of its total notional general income in 2018-19.²⁴

The council notes the special rate is an application of the ‘beneficiary pays’ principle. The approach is similar to a previous special variation in 2015-16 for the Jerberra Estate subdivision.²⁵

Refer to section 3.3 for more detail on the impact of Shoalhaven Council’s proposed special variation on rates for Verons Estate landowners.

¹⁹ The state government placed a moratorium on rezoning land in this area from 1994 to 2007.

²⁰ Shoalhaven Council, *Application Part B*, p 11.

²¹ Shoalhaven Council, *Application Part B*, p 6.

²² There was a previous special rate averaging \$845 in Verons Estate in 2016-17 to fund road construction. See Shoalhaven City Council, *Special Variation Application Form Part A for 2017-18*, Worksheet 5a.

²³ The special rate for Verons Estate will be in place for the life of the 20-year loan and will cease once the loan is fully paid. See Shoalhaven Council, *Application attachment – Verons Information*, p 5; Shoalhaven Council, *Verons Estate*, at <https://www.shoalhaven.nsw.gov.au/Planning-amp-Building/Strategic-planning/Paper-subdivisions/Verons-Estate>, accessed on 9 April 2018 and Shoalhaven Council, *Verons Estate, Sussex Inlet Proposed Special Rate Variation to Upgrade Roads*, <http://doc.shoalhaven.nsw.gov.au/DisplayDoc.aspx?record=d16/379793>, accessed on 9 April 2018.

²⁴ Shoalhaven Council, *Application Part A*, Worksheet 3.

²⁵ Shoalhaven Council, *Application attachment – Verons Information*, pp 1 and 7.

3 IPART's assessment

To make our decision, we assessed Shoalhaven Council's application against the criteria in the OLG Guidelines. We also considered the council's most recent IP&R documents, its FFTF proposal, and a range of comparative data about the council set out in Appendix D.²⁶

We found that Shoalhaven Council's application met the requirements of the criteria.

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

3.1 The council demonstrated financial need for the special variation

We found that Shoalhaven Council's IP&R documents clearly set out the need for, and purpose of the requested special variation, which is to:

- ▼ fund infrastructure renewal and maintenance to reduce deterioration of the council's assets
- ▼ reduce the operating deficit, and
- ▼ improve financial sustainability.²⁷

The council's IP&R documents also clearly indicate that the community's priorities were for the council to:

- ▼ provide a safe and inclusive community with a focus on recreation facilities
- ▼ provide sustainable and liveable environments with a focus on infrastructure renewal
- ▼ support prosperous community development with importance placed on building sporting facilities, and
- ▼ ensure responsible governance.²⁸

In particular, renewing road infrastructure and delivering reliable services were high priorities for the community.²⁹

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

²⁶ See Appendix D. Shoalhaven Council is in OLG Group 5, which is classified as Regional Town/City. The group comprises councils such as Coffs Harbour, Lake Macquarie, Maitland, Newcastle, Port Macquarie-Hastings, Tweed Shire and Wollongong.

²⁷ Shoalhaven Council, *Integrated Strategic Plan 2017 - Chapter 7: Special Rate Variation (SRV)*, p 6 and 8.

²⁸ Shoalhaven Council, *Integrated Strategic Plan 2017 - Chapter 1: Our Priorities (Community Strategic Plan)*, pp 13-23.

²⁹ Shoalhaven Council, *Integrated Strategic Plan 2017 - Chapter 1: Our Priorities (Community Strategic Plan)*, pp 18 and 22.

3.1.1 Impact on council's operating performance

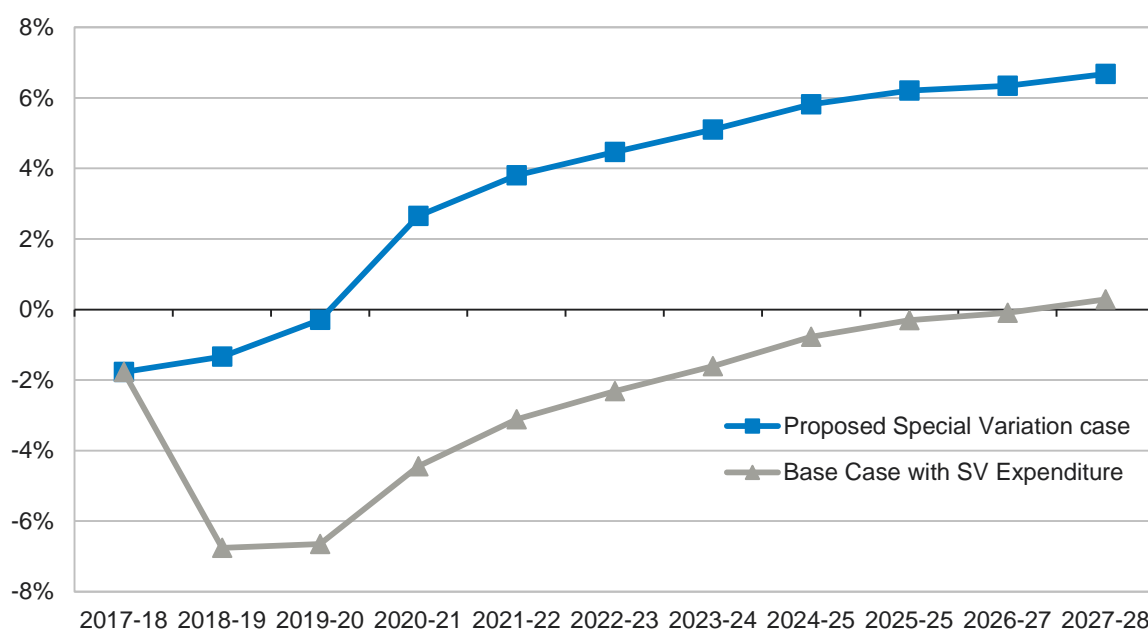
The operating performance ratio (OPR) measures whether a council's revenues fund its costs. The OPR is defined as:

$$OPR^{30} = \frac{\text{Total operating revenue} - \text{operating expenses}}{\text{Total operating revenue}}$$

Under the special variation scenario, the council forecasts persistent operating surpluses, growing to 6.7% by 2027-28. The cumulative value of these forecast surpluses is \$91.9 million to 2027-28. These surpluses would allow the council to fund its proposed expenditure, perform infrastructure renewals and maintenance, reduce infrastructure backlog and service a growing community.

Without the special variation and assuming the council's expenditure is the same as under the special variation scenario, it forecasts persistent operating deficits, as shown by the 'Base Case with SV expenditure' scenario in Figure 3.1 and Table 3.1. The cumulative value of these forecast deficits (before capital grants and contributions) is \$48.4 million to 2027-28 under this scenario. Hence, without the special variation, the council's sustainability would deteriorate before improving, and it may not generate sufficient funds to address its \$38.0 million infrastructure backlog and service a growing community.

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



Note: 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: Shoalhaven Council, *Application Part A, Worksheet 7* and IPART calculations.

³⁰ Expenditure and revenue in the OPR measure are exclusive of capital grants and contributions and net gain/loss on sale of assets.

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

	2018-19	2019-20	2020-21	2021-22	2022-23	2023-24	2024-25	2025-26	2026-27	2027-28
Application - including SV	-1.3	-0.3	2.7	3.8	4.5	5.1	5.8	6.2	6.3	6.7
Base case with SV expenditure	-6.8	-6.7	-4.5	-3.1	-2.3	-1.6	-0.8	-0.3	-0.1	0.3

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

3.1.2 Impact on the council's infrastructure backlog

The council's Resourcing Strategy estimates that it would cost over \$38.0 million to bring its assets to a satisfactory standard, eliminating its infrastructure backlog. In particular, the council estimates that roads is the asset category with the highest infrastructure backlog at approximately \$23.0 million.³¹

The council's infrastructure backlog ratio (measured as a percentage of the written down value of infrastructure assets)³² was 3.2%³³ in 2017-18. This is higher than the FFTF benchmark of less than 2.0%. With the special variation, it forecasts its infrastructure backlog ratio will improve to 2.0% and meet the FFTF benchmark by 2026-27. Without the special variation, the council forecasts its infrastructure backlog will consistently not meet the FFTF benchmark, with its infrastructure backlog ratio forecast to be 3.2% in 2026-27.

The council obtained feedback in 2012-13 from the community regarding its infrastructure. Based on the feedback obtained, the council concluded the community was dissatisfied with the condition of the council's assets, particularly roads and paths.³⁴ The council also concluded the community's priority was to maintain its assets. This is consistent with the council's Community Strategic Plan.³⁵ Hence, spending on infrastructure assets to reduce the infrastructure backlog is consistent with the community's priorities. Without the special variation revenue, the council may not be able to meet those priorities over the long term.

Table 3.2 shows the council's projected infrastructure backlog ratio including and excluding the special variation.

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

	2018-19	2019-20	2020-21	2021-22	2022-23	2023-24	2024-25	2025-26	2026-27
Application including SV	3.2	3.2	3.1	2.9	2.8	2.6	2.4	2.2	2.0
Excluding SV	3.2	3.2	3.2	3.3	3.3	3.3	3.2	3.2	3.2

Source: Shoalhaven Council, *Application attachment – Addendum to Long Term Financial Plan*.

³¹ Shoalhaven Council, *Integrated Strategic Plan 2017 – Chapter 6: Resourcing Strategy*, pp 30-31.

³² Historical cost less accumulated depreciation.

³³ Shoalhaven Council, *Integrated Strategic Plan 2017 - Chapter 7: Special Rate Variation (SRV)*, p 43.

³⁴ Shoalhaven Council, *Application Part B*, pp 56-57.

³⁵ Shoalhaven Council, *Integrated Strategic Plan 2017 - Chapter 1: Our Priorities (Community Strategic Plan)*, p 17.

3.1.3 Impact on the council's infrastructure renewal ratio

The council estimates that it would need to spend \$15.5 million per year on renewals³⁶ to 2026-27 to meet the FFTF benchmark of greater than 100%.³⁷ With the special variation, the council proposes to spend an additional \$77.3 million to 2026-27 towards renewals for road and transport infrastructure, buildings and sports grounds as detailed in Appendix B. It forecasts the renewal ratio³⁸ will be 76.3% by 2026-27. Although not meeting the benchmark, it forecasts that the renewal ratio will gradually improve.

However, without the special variation, it forecasts that the renewal ratio will persistently deteriorate to 50.8% by 2026-27 – significantly below the FFTF benchmark. Without the special variation, the council may not be able to meet the community's priorities for infrastructure renewals.³⁹ The council may face increasing pressure to provide the level of services expected by the community.⁴⁰

Table 3.3 shows the council's projected infrastructure renewal ratio including and excluding the special variation.

Table 3.3 Projected infrastructure renewal ratio (%) for Shoalhaven City Council's special variation application

	2018-19	2019-20	2020-21	2021-22	2022-23	2023-24	2024-25	2025-26	2026-27
Application including SV	61.2	60.1	69.0	69.2	74.7	70.9	69.9	72.7	76.3
Excluding SV	55.9	51.5	51.7	46.0	46.6	46.5	45.6	48.2	50.8

Source: Shoalhaven Council, *Application attachment – Addendum to Long Term Financial Plan*.

Similarly, with the special variation, the council proposes to spend an additional \$10.0 million to 2026-27 towards maintaining its roads, buildings and parks and reserves as detailed in Appendix B. It forecasts the asset maintenance ratio will meet the FFTF benchmark of greater than 100% at 100.7% by 2026-27.⁴¹

Without the special variation, it forecasts the asset maintenance ratio will be 97.3%⁴² by 2026-27, which is below the FFTF benchmark.

Our analysis on financial need is consistent with our FFTF assessment of Shoalhaven Council. Box 3.1 below summarises our assessment of the council's 2015 FFTF proposal.

³⁶ 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.

³⁷ Shoalhaven Council, *Application Part B*, p 37.

³⁸ The infrastructure renewal ratio is defined as spending on infrastructure renewals divided by depreciation, amortisation and impairment.

³⁹ Shoalhaven Council, *Integrated Strategic Plan 2017 - Chapter 1: Our Priorities (Community Strategic Plan)*, pp 15-17.

⁴⁰ Shoalhaven Council, *Application Part B*, p 5. This is consistent with TCorp's observations in their assessment of Shoalhaven Council performed in 2012. TCorp observed that the challenge for the council is to maintain service levels across new and existing facilities and highlighted that the council's growing population would place pressure on existing infrastructure. See NSW Treasury Corporation, *Financial Assessment and Benchmarking Report*, October 2012, p 18.

⁴¹ Shoalhaven Council, *Application attachment – Addendum to Long Term Financial Plan*.

⁴² Shoalhaven Council, *Application attachment – Addendum to Long Term Financial Plan*.

Box 3.1 FFTF Assessment

IPART's FFTF assessment in 2015 found that Shoalhaven Council:

- ▼ met the criterion for financial sustainability. The assessment was based on the council successfully applying for a proposed special variation of 21.0% cumulative over two years from 2017-18,
- ▼ met the operating performance benchmark from 2019-20, based on the proposed special variation. It met the own source revenue benchmark, but did not meet the asset renewal benchmark in all forecast years,
- ▼ met the criterion for infrastructure and service management, as it forecast a steady infrastructure backlog ratio, and proposed to increase maintenance expenditure to improve the asset maintenance ratio. It met the debt service benchmark in all forecast years, and
- ▼ met the efficiency criterion based on a forecast decline in real operating expenditure per capita from \$1,469 in 2014-15 to \$1,400 in 2019-20.

TCorp observed in 2013 the council's financial position was 'sound, but considered its outlook was 'negative'. This assessment was made largely because of:

- ▼ forecast operating deficits in all forecast years when excluding capital grants and contributions, and
- ▼ a weak liquidity position, indicating difficulty for the council in meeting day to day expenses.

Source: IPART, *Assessment of Council Fit for the Future Proposals*, October 2015, pp 339-340 and NSW Treasury Corporation, *Financial Assessment and Benchmarking Report*, October 2012, p 4.

3.1.4 Alternative funding strategies

Shoalhaven Council indicated that it has undertaken an extensive review of its services and programs between 2012-13 and 2015-16 resulting in annual reductions in expenditure of \$6.4 million.⁴³ The council implemented a number of cost containment strategies to improve financial sustainability. Key strategies included:

- ▼ restructuring and reducing salary costs
- ▼ reducing use of casual staff
- ▼ reducing its fleet size,⁴⁴ and
- ▼ retraining staff in pricing, marketing and costing methodologies.⁴⁵

The council indicated that it also investigated other strategies which it decided not to pursue:

- ▼ borrowing of funds – the council concluded that this option is limited as any borrowings, and its associated costs, used to finance operational costs would further impact the operating deficit,⁴⁶ and

⁴³ Shoalhaven Council, *Application Part B*, p 99.

⁴⁴ Shoalhaven Council, *Application Part B*, p 99.

⁴⁵ Shoalhaven Council, *Application Part B*, p 35.

⁴⁶ Shoalhaven Council, *Application Part B*, p 35.

- ▼ service level reductions – the council concluded that reducing services would lead to delays and increased complaints.⁴⁷

Shoalhaven Council's long term financial modelling identified that without the special variation, the council would not be able to maintain and renew its assets and the general fund would operate at a cumulative deficit of \$23.4 million to 2026-27. It concluded that increasing rates above the rate peg would be required to significantly improve its operating performance and allow it to maintain and renew ageing infrastructure.⁴⁸

3.2 The council demonstrated community engagement and awareness

We found that Shoalhaven Council demonstrated its community is aware of the need for and extent of the proposed rate increase.

The council identified a need for the special rate variation rate increases in its initial 2015-16 IP&R documents and has reaffirmed the need for additional revenue in successive years. In 2017, the council revised its IP&R documents in consultation with the community. Between October and November 2017, it exhibited its Integrated Strategic Plan including its updated Delivery Program, Long Term Financial Plan and Special Rate Variation Chapter, which clearly explained the need for, purpose, and extent of the proposed special variation. In particular, it communicated the increase of the special variation in percentage terms, and the total increase in dollar terms for the average ratepayer by rate category.

Refer to Section 3.4 for more detail relating to the council's IP&R documents.

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

- ▼ its rates newsletter mailed to all ratepayers
- ▼ its website and 'Get Involved Shoalhaven' webpage
- ▼ public meetings
- ▼ presentations to Community Consultative Bodies, and
- ▼ display materials such as fact sheets, television advertisements, social media posts, media releases and displays at council sites.⁴⁹

3.2.1 Outcome of consultation with community

Although this criterion does not require councils to demonstrate community support for the special variation, they are required to consider the results of their community consultation in preparing their application.

Shoalhaven Council consulted widely as part of its special variation application. The council received 13 written submissions in response to the public exhibition of its updated IP&R documents which outlined the proposed special variation. This was lower than the responses the council received as part of its 2017-18 special variation application. Of the

⁴⁷ Shoalhaven Council, *Application Part B*, pp 60 and 100.

⁴⁸ Shoalhaven Council, *Application Part B*, p 36.

⁴⁹ Shoalhaven Council, *Application Part B*, pp 53-54.

13 submissions, six submissions opposed the proposed special variation, three were in favour and four provided comments. The council identified the main reasons for opposition were:

- ▼ a view that the council should improve efficiencies before considering a special variation
- ▼ the rate increase is too large, and
- ▼ low and fixed income ratepayers would find the increase unaffordable.⁵⁰

The council has considered its community's feedback and noted that it considered alternative options to the special variation. It concluded that without the rate increase it would continue to operate in deficit and would not be able to fund the maintenance and renewal of ageing infrastructure.⁵¹ Based on this outcome, the council decided to apply for the proposed special variation.

3.2.2 Submissions from the community

IPART received three submissions⁵² opposing the application, mainly on the grounds of unaffordability, and the view that the council should manage its resources more effectively. We note the council has considered its ratepayers' capacity to pay and this is discussed in Section 3.3.1.

3.3 The impact on ratepayers is reasonable

As Chapter 2 discussed, Shoalhaven Council requested a 3-year cumulative increase of 29.1% that will remain permanently in the rate base; 17.1% in 2018-19, and 5.0% per annum in both 2019-20 and 2020-21.

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

- ▼ average residential and business rates were lower than the OLG Group 5 average
- ▼ the average rate to median income ratio was lower than the OLG Group 5 average
- ▼ Verons Estate special rate is consistent with collecting revenue from those who should benefit from the proposed expenditure, and
- ▼ expiry of a temporary 13.2% special variation at the end of 2017-18, which means the net increase in rates from current levels will be smaller than the 29.1% applied for (about 16% for residential, business and farmland ratepayers).

In reaching our decision, we considered the council's consideration of affordability, and assessed socio-economic indicators for Shoalhaven Council compared to its OLG group and its neighbouring councils.

⁵⁰ Shoalhaven Council, *Application Part B*, pp 89-92 and Shoalhaven Council, *Application attachment – Community Engagement Report*, pp 17-26.

⁵¹ Shoalhaven Council, *Application Part B*, p 36.

⁵² We also received some submissions outside our consultation period.

3.3.1 Council's consideration of impact on ratepayers

Shoalhaven Council provided a comparison of its average residential rates with most of its OLG Group 5 peers: Coffs Harbour City Council, Newcastle City Council, Tweed Shire Council, Lake Macquarie City Council, Port Macquarie-Hastings Council and Wollongong City Council. The council:

- ▼ compared the average residential rates of its OLG Group 5 peers, increasing by an assumed annual rate peg, against its own average residential rate increasing by the proposed special variation from 2014-15 up to 2018-19, and
- ▼ noted that even with the special variation, its average residential rate would be in the middle of its OLG group.⁵³

The council also examined various socio-economic indicators for its local government area to assess the impact on ratepayers, including SEIFA, income, population characteristics and unemployment rates. It acknowledged that it has the highest unemployment rate within its OLG group. However, it concluded that its ratepayers have the capacity to pay the increased rates based on the following factors:

- ▼ even with the lowest SEIFA ranking within the OLG Group 5, councils with only slightly higher rankings pay higher rates
- ▼ some councils within its OLG group pay a higher proportion of their income in residential rates, and
- ▼ the councils within its OLG group with a higher proportion of pensioner ratepayers pay higher average rates.⁵⁴

The council submitted it also has a hardship policy that may assist ratepayers with:

- ▼ writing off interest applied to overdue rates and charges, and
- ▼ waiving, reducing or deferring the payment of the whole or part of a rate increase due to valuation changes.⁵⁵

The council also noted the number of ratepayers accessing the hardship policy is low, only four ratepayers in 2016-17, and has been falling since 2015-16. It concluded that this is an indication that few people are experiencing hardship to the point where council assistance is required.⁵⁶

Based on the socio-economic indicators and additional considerations, the council concluded the community has the willingness and capacity to pay.

3.3.2 IPART's assessment of impact on ratepayers

To assess the reasonableness of the impact of the special variation on ratepayers, we:

⁵³ Shoalhaven Council, *Application Part B*, p 66.

⁵⁴ Shoalhaven Council, *Application Part B*, pp 65-71.

⁵⁵ Shoalhaven Council, *Application Part B*, p 72 and Shoalhaven Council, *Application attachment - Hardship Policy*, August 2017, pp 1-2.

⁵⁶ 10 ratepayers accessed the hardship policy in 2015-16. This fell to four ratepayers in 2016-17. See Shoalhaven Council, *Application Part B*, pp 69-70.

- ▼ examined the council's special variation history and the average annual growth of rates in various rating categories
- ▼ compared current rates and socio-economic indicators in Shoalhaven with its OLG Group 5 councils and neighbouring councils
- ▼ assessed the impact of the rate increase on the Verons Estate landowners, and
- ▼ considered the extent to which the expiring special variation would mitigate the impact of the proposed special variation.

Shoalhaven City Council's rates history

We found that since 2007-08, the council successfully applied for three special variations in:

- ▼ 2013-14, an increase of 8.0% retained permanently in its rate base for infrastructure renewal
- ▼ 2015-16, an increase of 3.9% to remain in the rate base for 10 years to service a loan to fund infrastructure works in the Jerberra Estate, and
- ▼ 2017-18, a 1-year temporary increase of 13.2% for financial sustainability, funding capital expenditure, reducing the council's infrastructure backlog and providing necessary infrastructure for Verons Estate, expiring on 30 June 2018.

Over this period, the average annual growth in residential rates was 5.8%, 4.5% for farmland rates and 1.9% for business rates, which compares with the average annual growth in the rate peg of 2.7% over the same period.

Comparison of Shoalhaven City Council to other council areas

We also compared current rates and socio-economic indicators in Shoalhaven with its OLG Group 5 councils and neighbouring councils as shown in Table 3.4.

Table 3.4 Shoalhaven City Council - comparison of rates and socio-economic indicators with neighbouring councils and Group 5 averages (2015-16)

Council (OLG Group)	Average residential rate (\$) ^a	Average business rate (\$)	Median annual household income (2016) ^b	Average rate to median income (%)	Outstanding rates ratio (%)	SEIFA Index NSW Rank ^c
Eurobodalla Shire ^d (4)	866	3,097	48,828	1.8	5.2	40
Goulburn-Mulwaree (4)	887	4,956	62,192	1.4	2.6	52
Kiama Municipal (4)	1,342	2,178	78,468	1.7	2.2	108
Queanbeyan-Palerange ^e	1,071	4,104	97,864	1.1	-	110
Shoalhaven City^d (5)	934	2,167	51,584	1.8	5.0	50
OLG Group 5 average	1,147	5,995	60,823	1.9	4.5	-

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

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

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

d Eurobodalla was granted a 3-year special variation of 6.37% per year from 2015-16 to 2017-18. Shoalhaven was granted a temporary 1-year special variation of 13.2% in 2017-18. The data in this table does not capture the increases from these special variations.

e Queanbeyan (OLG Group 4) and Palerang (OLG Group 11) merged in 2016.

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

Based on the comparative data, we found that Shoalhaven Council's:

- ▼ average residential rate was lower than the average for Group 5 councils and midway between neighbouring councils
- ▼ average business rate was substantially lower than the average for Group 5 councils and lower than neighbouring councils
- ▼ median annual household income was lower than the average for Group 5 councils and lower than most neighbouring councils
- ▼ average rate to median income ratio was lower than the average for Group 5 councils, but higher than most neighbouring councils
- ▼ outstanding rates ratio was higher than the average for Group 5 councils and higher than most neighbouring councils, and
- ▼ SEIFA ranking is midway between neighbouring councils and indicates some level of disadvantage.

Impact of the Verons Estate special rate

It is a matter for each council to determine how it allocates the recovery of general income across different categories of ratepayers. However, in making our decision to approve the special variation, we have considered the council's proposal to retain its special rate for the Verons Estate Landowners, introduced in 2017-18, in the context of assessing the reasonableness of the overall rate increase. This proposed special rate would raise the equivalent of 0.2% of the council's general income.⁵⁷

⁵⁷ Shoalhaven Council, *Application Part A*, Worksheet 3.

The impact on the Verons Estate ratepayers for necessary road and bushfire safety infrastructure is substantial. The council notes the special rate may cause hardship for some members of the estate and could lead to individuals having to sell their property.⁵⁸ However, the council notes the special rate is a clear application of the 'beneficiary pays' principle and that the infrastructure works funded by the special rate are necessary before the existing dwellings can receive council planning approval.⁵⁹

The council estimates the special rate for Verons Estate landowners with a building entitlement is \$5,350 each year, which commenced from 1 July 2017, over the period of 20 years in line with the duration of the loan.⁶⁰

Levying a special rate on the Verons Estate landowners is reasonable given:

- ▼ the estate's history of development. The special rate is being paid by those who have caused the need for the expenditure and who will most directly benefit from the infrastructure, which reduces cross subsidisation by other ratepayers
- ▼ the council proposes to cover 17.0% of the upgrade costs in recognition of the potential benefit of the road upgrades to the broader community⁶¹
- ▼ the council's long standing position since the start of the rezoning process that any cost of infrastructure works to develop the estate should be recovered from the landowners,⁶² and
- ▼ the value of the infrastructure works and subsequent planning approval should increase the value of the land in the estate. Hence, a special rate is consistent with collecting revenue from those who should benefit from the proposed expenditure.

Shoalhaven City Council has an expiring special variation

We have considered the impact of an expiring special variation, which means the increase in rates for most ratepayers will be less than the 29.1% cumulative increase the council has applied for.

After accounting for the impact of the expiring special variation from 2017-18 rates, the average net rate increases under the council's application, are estimated to be 15.7% for residential ratepayers, 15.9% for business ratepayers and 16.0% for farmland ratepayers over the three years of the proposed special variation.⁶³ These compare with the cumulative rate increase at the assumed rate peg over the period of 7.5%. Hence, the net increase in rates above the rate peg over the three years is substantial, but lower than the cumulative increase the council has applied for.

⁵⁸ Financial hardship is not applied to small lot rural subdivisions on which building is not permitted. This means the current policy does not apply to the Verons Estate landowners. See Shoalhaven Council, *Application attachment - Hardship Policy*, August 2017, p 1.

⁵⁹ Shoalhaven Council, *Application attachment – Verons Information*, pp 4 and 10.

⁶⁰ Shoalhaven Council, *Application Part A*, Worksheet 5a and Shoalhaven Council, *Verons Estate*, at <https://shoalhaven.nsw.gov.au/Planning-and-Building/Strategic-planning/Paper-subdivisions/Verons-Estate>, accessed on 3 April 2018.

⁶¹ Shoalhaven Council, *Application Part B*, p 11.

⁶² Shoalhaven Council, *Application attachment – Verons Information*, p 4.

⁶³ Shoalhaven Council, *Application Part A*, Worksheet 5a.

Summary

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

3.4 The council's IP&R documents were exhibited

The council adopted its Community Strategic Plan in June 2017.⁶⁴

It developed an Integrated Strategic Plan to consolidate its IP&R documents, which comprises the Community Strategic Plan, Delivery Program and Long Term Financial Plan. The council added a new chapter, Chapter 7 Special Rate Variation, to its Integrated Strategic Plan clearly setting out the special variation, the cumulative increase in rates in percentage and dollar terms, and the average impact on ratepayers. It also includes the impact of the expiring special variation. It updated its Delivery Program, Long Term Financial Plan and the new Chapter 7 Special Rate Variation in October 2017 to clearly set out and consult on its proposed special variation.⁶⁵

It exhibited its updated IP&R documents between 26 October and 28 November 2017 and adopted the documents on 28 November 2017.⁶⁶

3.5 The council explained its productivity improvements and cost containment strategies

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

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

- ▼ using a combination of reducing salary costs, reducing costs in its long run contracts, reducing its fleet size and reducing electricity costs producing annual savings in operating expenditure of \$6.4 million from 2012-13 to 2015-16⁶⁷
- ▼ targeting operational improvements relating to non-salary items, such as its materials and contracts expenses, producing savings of \$1.8 million in 2016-17,⁶⁸ and
- ▼ budgeting in its procurement activities with estimated savings of \$60,000 in 2017-18.⁶⁹

In addition, it has identified some additional future cost savings strategies in its application such as:

- ▼ approximately \$233,900 per year in salary savings targets included in its 10-year Long Term Financial Plan⁷⁰

⁶⁴ Email to IPART, Shoalhaven Council, 16 February 2018.

⁶⁵ Shoalhaven Council, *Attachment Part B*, p 87.

⁶⁶ Email to IPART, Shoalhaven Council, 16 February 2018 and Shoalhaven Council, *Attachment Part B*, pp 94-95.

⁶⁷ Shoalhaven Council, *Application Part B*, p 99.

⁶⁸ Shoalhaven Council, *Application Part B*, p 101.

⁶⁹ Shoalhaven Council, *Application Part B*, p 101.

⁷⁰ Shoalhaven Council, *Application Part B*, p 101.

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- ▼ improving management of employee expenses relating to fringe benefits and leave liabilities, with forecast savings of \$280,000 over the next two years⁷¹
 - ▼ performing reviews of its services and outsourcing, with forecast savings of \$250,000 over the next two years,⁷² and
 - ▼ pursuing more cost effective purchases through the Illawarra Shoalhaven Joint Organisation with forecast savings of \$100,000 over the next two years.⁷³

⁷¹ Shoalhaven Council, *Application Part B*, p 84.

⁷² Shoalhaven Council, *Application Part B*, p 33.

⁷³ Shoalhaven Council, *Application Part B*, p 33.

4 Our decision's impact on the council

Our decision means Shoalhaven Council may increase its general income over the 3-year special variation period from \$69.5 million in 2017-18 to \$80.4 million in 2020-21. Table 4.1 shows the percentage increases we have approved, and estimates the annual increases in the council's general income incorporating adjustments that will occur as a result of various catch-up, valuation adjustments and the renewal of an expiring special variation.

These increases will be permanently incorporated into the council's revenue base. After 2020-21, the council's permissible general income can increase up to the annual rate peg unless we approve a further special variation.⁷⁴

Table 4.1 Permissible general income of Shoalhaven City Council from 2018-19 to 2020-21 arising from the special variation approved by IPART

Year	Increase approved (%)	Cumulative increase approved (%)	Annual increase in general income (\$)	Permissible general income (\$)
2017-18 permissible general income				69,450,866
Adjusted notional income 1 July 2018 ^a				62,272,641
2018-19 ^b	17.10	17.10	10,679,503	72,952,143
2019-20	5.00	22.96	3,647,607	76,599,751
2020-21	5.00	29.10	3,829,988	80,429,738
Total increase approved			18,157,097	

^a Includes adjustment of -\$7,178,226 for a special variation that expires on 30 June 2018.

^b A prior catch-up of \$30,881 that had not been recouped by the time of the application was submitted to IPART is to be recouped in 2018-19.

Note: The above information is correct at the time of the council's application (February 2018). Numbers may not add due to rounding.

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

The council estimates that over the three years to 2020-21 it will collect, in total, an additional \$34.0 million of rate revenue compared to rate increases that are limited to the assumed rate peg.

This extra income is the amount the council requested to improve its financial sustainability, fund capital expenditure, reduce its infrastructure backlog, reduce its operating deficit, fund asset renewal and maintenance and make repayments on the Verons Estate loan.⁷⁵

⁷⁴ 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 OLG is responsible for monitoring and ensuring compliance.

⁷⁵ Shoalhaven Council, *Application Part B*, pp 5-6.

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, Shoalhaven Council indicated it intended to increase rates fairly evenly for each rating category.

The council has calculated, after accounting for the expiring special variation, that the:

- ▼ average residential rate would increase by 15.7% or \$182 over 3-years, or by \$59 in the first year (where the Verons Estate special rate for those with a building entitlement is forecast to remain at \$5,350 per year)
- ▼ average business rate would increase by 15.9% or \$317 over 3-years, or by \$102 in the first year, and
- ▼ average farmland rate would increase by 16.0% or \$363 over 3-years, or by \$118 in the first year.⁷⁶

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

⁷⁶ Shoalhaven Council, *Application Part A*, Worksheet 5a. The average rate is the average of the council's rating sub-categories, which includes ordinary and any special rates applying to the rating category.**Error! Reference source not found.**

Table 5.1 Indicative annual increases in average rates under Shoalhaven City Council's approved special variation 2018-19 to 2020-21

Year	2017-18	2018-19	2019-20	2020-21	Cumulative Increase
Residential rate \$	1,158	1,217	1,277	1,340	
\$ increase		59	60	63	182
% increase		5.1	4.9	4.9	15.7
Business rate \$	2,000	2,102	2,207	2,317	
\$ increase		102	105	110	317
% increase		5.1	5.0	5.0	15.9
Farmland rate \$	2,266	2,384	2,503	2,628	
\$ increase		118	119	125	363
% increase		5.2	5.0	5.0	16.0

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

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

The increases in average rates in 2018-19 is less than the rise in general income of 17.1%. This is because rates are first reduced by the value of the expiring special variation (\$7,178,226) and then increased by 17.1%. The net increase in permissible income for 2018-19 is approximately 5.0% for Shoalhaven Council.



Appendices



A Assessment criteria for special variation applications

Table A.1 Assessment criteria for special variation applications

Assessment criteria
<p>Criterion 1 – Financial need</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&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&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">▼ 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. <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>Criterion 2 – Community awareness</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 SV in percentage terms, and the total increase in dollar terms for the average ratepayer, by rating category.</p>
<p>Criterion 3 – Impact on ratepayers is reasonable</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">▼ 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.
<p>Criterion 4 – IP&R documents are exhibited</p> <p>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.</p>
<p>Criterion 5 – Productivity improvements and cost containment strategies</p> <p>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.</p>
<p>Criterion 6 – Additional matters</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 and Table B.2 show Shoalhaven Council's proposed expenditure of the special variation funds over the next 10 years.

The council will use the additional special variation revenue, above the rate peg, of \$138.1 million, over 10 years to fund:

- ▼ current service levels
- ▼ road, buildings, parks and reserves maintenance
- ▼ additional operations
- ▼ Verons Estate loan repayments, and
- ▼ capital expenditure.⁷⁷

The improvement in operating performance will fund \$89.4 million in extra capital expenditure for renewing roads and buildings and upgrading sports grounds over the period from 2018-19 to 2027-28 (see Table B.2).

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

⁷⁷ Shoalhaven Council, *Application Part A*, Worksheet 6 and Shoalhaven Council, *Application Part B*, pp 5-6.

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

	2018-19	2019-20	2020-21	2021-22	2022-23	2023-24	2024-25	2025-26	2026-27	2027-28	Total
Special variation income above assumed rate peg	9,216	11,271	13,467	13,804	14,149	14,503	14,865	15,237	15,618	16,008	138,139
Funding to maintain current service levels	4,653	4,332	3,027	838	-	450	567	587	172	-	14,626
Funding to maintain roads, buildings, and parks and reserves	1,000	1,025	1,051	1,077	1,104	1,131	1,160	1,189	1,218	1,249	11,203
Funding for additional operations	1,000	2,050	2,101	2,154	2,208	2,263	2,319	2,377	2,437	2,498	21,407
Funding for capital expenditure	2,414	3,714	7,140	9,586	10,689	10,510	10,670	10,935	11,642	12,113	89,413
Verons Estate loan borrowings costs	74	71	69	66	63	60	57	53	50	46	608
Verons Estate loan principal repayments	75	78	80	83	86	89	92	96	99	103	882
Total expenditure	9,216	11,271	13,467	13,804	14,149	14,503	14,865	15,237	15,618	16,008	138,139

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

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

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

	2018-19	2019-20	2020-21	2021-22	2022-23	2023-24	2024-25	2025-26	2026-27	2027-28	Total
Buildings renewals	800	1,000	2,081	2,607	3,000	3,060	3,121	3,184	3,247	3,328	25,429
Roads and transport renewals	1,114	2,202	4,533	6,440	7,137	6,884	6,969	7,157	7,786	8,160	58,382
Sports grounds upgrades	500	513	525	538	552	566	580	594	609	624	5,602
Total Capital Expenditure	2,414	3,714	7,140	9,586	10,689	10,510	10,670	10,935	11,642	12,113	89,413

Note: Numbers may not add due to rounding.

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

C Shoalhaven City Council's projected revenue, expenses and operating result

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

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

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

	2018-19	2019-20	2020-21	2021-22	2022-23	2023-2024	2024-25	2025-26	2026-27	2027-28
Total revenue	191,920	200,011	208,860	213,852	220,508	227,604	235,274	242,748	250,758	257,512
Total expenses	188,537	194,296	197,054	201,236	206,100	211,359	216,875	222,869	229,953	235,313
Operating result from continuing operations	3,383	5,715	11,806	12,616	14,408	16,245	18,399	19,879	20,805	22,199
Net operating result before capital grants and contributions	-2,482	-579	5,379	7,960	9,642	11,365	13,401	14,761	15,565	16,854

Note: Numbers may not add due to rounding.

Source: Shoalhaven Council, *Application Part A*, Worksheet 7

D Comparative indicators

Performance indicators

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

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

Overall, the tables below show that:

- ▼ although the Full-Time Equivalent (FTE) staff number has increased since 2013-14, the ratio of the population to FTE staff numbers has increased, and
- ▼ while the council's average staff cost per FTE has increased since 2012-13, the employee costs as a percentage of operating expenditure was lower than both the OLG Group 5 average and the NSW average.

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

Performance indicator	2012-13	2013-14	2014-15	2015-16	Average annual change (%)
FTE staff (number)	769	759	756	775	0.3
Ratio of population to FTE	126	129	131	131	1.3
Average cost per FTE (\$)	82,999	89,926	88,299	96,943	5.3
Employee costs as % of operating expenditure (General Fund only)	34.7	35.1	33.3	34.4	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 and IPART calculations.

Table D.2 Select comparative indicators for Shoalhaven City Council, 2015-16

	Shoalhaven Council	OLG Group 5 average	NSW average
General profile			
Area (km ²)	4,567	-	-
Population	101,777	-	-
General Fund operating expenditure (\$m)	167.7	155.6	70.2
General Fund operating revenue per capita (\$)	1,809	-	-
Rates revenue as % of General Fund income	40.8	47.2	43.6
Own-source revenue ratio (%)	76.1	68.5	67.3
Average rate indicators^a			
Average rate – residential (\$)	934	1,147	1,017
Average rate – business (\$)	2,167	5,995	5,118
Average rate – farmland (\$)	1,970	1,583	2,366
Socio-economic/capacity to pay indicators			
Median annual household income, 2016 (\$) ^b	51,584	60,823	77,272
Average residential rate to median income ratio (%)	1.8	1.9	1.3
SEIFA, 2016 (NSW rank: 130 is least disadvantaged)	50	-	-
Outstanding rates and annual charges ratio (%)	5.0	4.5	3.6
Productivity (labour input) indicators^c			
FTE staff (number)	775	721	354
Ratio of population to FTE	131	-	-
Average cost per FTE (\$)	96,943	87,137	83,193
Employee costs as % of operating expenditure (General Fund only)	34.4	37.2	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.