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Independent Pricing and Regulatory Tribunal
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Dear Sir/Madam

Measuring and Assessing Productivity Performance in Local Government

The City of Newcastle welcomes the opportunity to comment and respond to the IPART discussion paper titled Measuring and Assessing Productivity Performance in Local Government. The following responses are provided to the issues put forward;

- 1) *Is the current method of using an economy-wide measure of productivity and then discounting it for application to the NSW local government sector the most appropriate for future years? If so which ABS series would be most appropriate?***

The City of Newcastle supports the use of the Local Government Cost Index (LGCI) in lieu of CPI for calculation of the rate peg. However Council feels that the application of a productivity factor requires further development and suggests the consideration of criteria specific to individual councils as follows:

- Ability to demonstrate improved efficiency and a reduction in operational expenditure base
- Geographical area - rural, regional and metropolitan
- Range of services provided to the community
- Ability to raise alternative revenue sources other than rates
- Stage of the LGA's lifecycle (whether the LGA is a growing or mature LGA)

For example a coefficient for each criteria could be used which when multiplied by a Council specific score could result in an overall factor to apply to the rate cap.

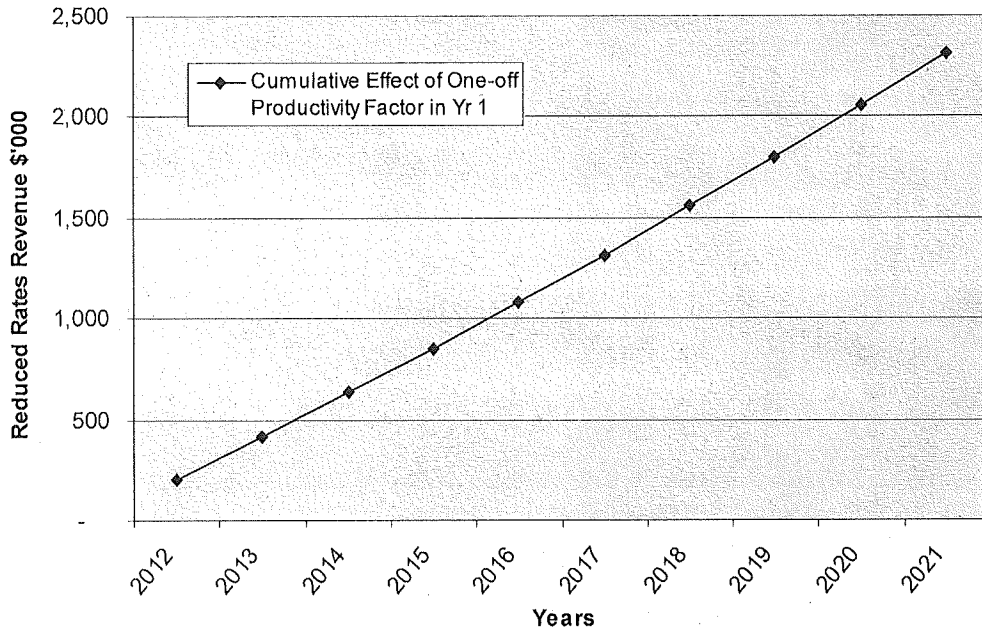
In addition to the considerations above we feel that it would be appropriate to undertake a weighted average analysis of the ABS series below rather than simply using one economy wide measure.

ABS series that may be considered relevant:

- Public Administration and Safety
- Administrative and Support Services
- Electricity, Gas, Water and Waste Services
- Construction
- Other Services (assuming applicability)

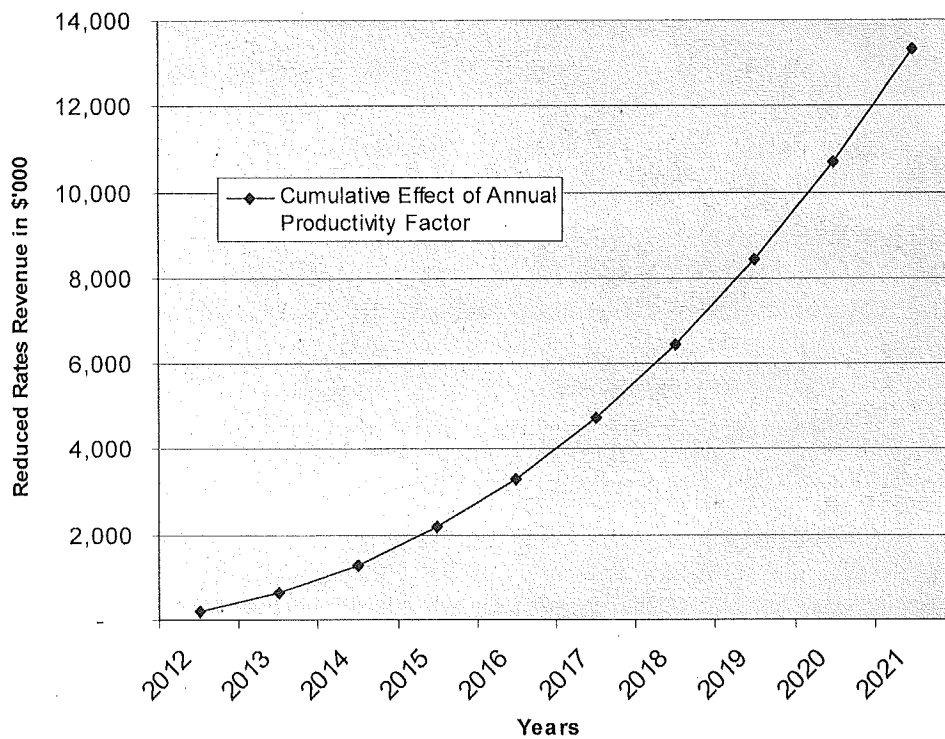
Council has performed an analysis to demonstrate the compounding effect of a one-off productivity factor of 0.2% over a 10 year period. By year 2021 the cumulative total of lost Rates Revenue is \$2,313,000. This continues to compound regardless of Council's improved efficiency.

Cumulative Effect of One-off Productivity Factor in Yr 1



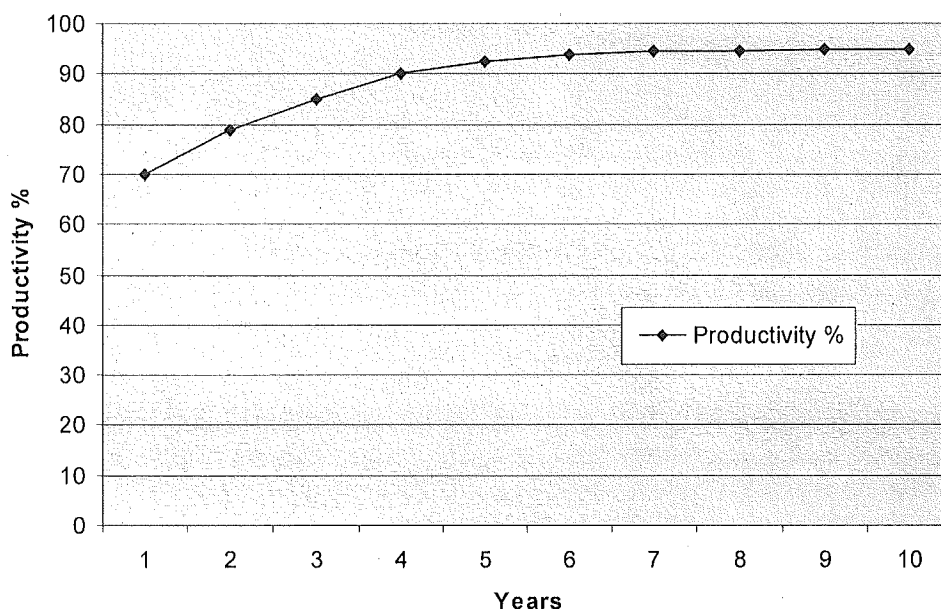
Following on from above the compounding effect of an annual productivity factor of 0.2% each year for the 10 years is \$13,309,000. This highlights the ongoing detrimental effect on Councils ability to keep up with cost increases.

Cumulative Effect of Annual Productivity Factor



The application of a productivity factor in the short term may refocus Councils and drive efficiencies. However, this approach is flawed in the long term as there is a diminishing return on how efficient an organisation can become. The graph below demonstrates that it is harder to achieve efficiency gains the closer an organisation comes to 100% efficient. The productivity factor therefore penalises Council revenues in a disproportionate manner to the cost savings that can be achieved.

Productivity Improvements Achievable Over Time*



*This graph is for illustrative purposes only and is not reflective of actual Productivity Improvements of The City of Newcastle.

2) If not, what alternative measure would be more appropriate for determining a productivity factor?

Refer above.

3) Can councils measure some (or all) of their productivity gains in terms of changes in physical units (that is, in volumes or quantities) of inputs and changes in prices paid for inputs? If so, in what ways would these changes be expressed?

The City of Newcastle can measure productivity gains in terms of net dollar savings, however we do not have systems in place which enables us to split this between price efficiency gains and volume efficiency gains.

Productivity savings for The City of Newcastle are reflected in the Quarterly Budget Statement as sustainability savings. Targets achieved for the City of Newcastle over the financial year 2009-10 was \$1,124,237, and over 2010-11 was \$871,890. These were reported in the June Quarterly Review documentation.

4) Are productivity improvements able to be captured within councils' Long Term Financial Plans? If so, please illustrate.

Past productivity improvement cost savings have been removed from Council's operating budget base to ensure that productivity savings are ongoing for our 2011/12 to 2020/21 Long Term Financial Plan (LTFP). However the LTFP doesn't individually show productivity improvements.

5) What indicators should IPART use in assessing the productivity of councils?

The City of Newcastle's financial sustainability is a key issue arising from constraints on rate capping, an ageing infrastructure network, cost shifting from other levels of government and the expectation of service delivery to the wider community.

In recent years, to address continued financial sustainability, The City of Newcastle undertook an extensive sustainability review to identify possible service rationalisation, cost reduction and sources of additional revenue raising opportunities.

Subsequently adopted annual Operational Plans have integrated any approved strategies which form the basis of the Long Term Financial Plan under Integrated Planning and Reporting. Continuing financial sustainability must be viewed in line with The City of Newcastle's other Integrated Planning & Reporting resourcing strategies.

Further, annually, Council completes the Financial Health Check which assesses Council's overall financial position as compared to industry guidelines. Council's overall financial position has been assessed to be sound within industry guidelines together with strong liquidity levels, including operational cash flows as well as a robust Balance Sheet.

Key ratios the City of Newcastle considers important when addressing a Council's operating surplus/deficit and assessment of ongoing financial sustainability are:

- Rates and Charges as a percentage of Operating Revenue
- Debt as a percentage of Rates Revenue
- Capital Works as a % of Total Expenditure (excluding depreciation)
- Total Expenses per Capita of LGS Population
- Employee Costs as a % of Total Expenditure
- Current Assets/Current Liabilities
- Operating Result from Continuing Operations
- Cost of Support Staff vs Total Operating Expenditure
- Cost of IT Services vs Total Operating Expenditure
- Cost of Operating Delivery Staff vs Total Operating Expenditure

Investment in maintenance and renewal of Council's asset base in parallel with ongoing asset rationalisation of under-performing assets will form the basis of The City of Newcastle's strategy for sustainable infrastructure.

When assessing the productivity of councils we recommend IPART leverage off the indices developed by the NSW Grants Commission for allocation of the Financial Assistance Grant. IPART could develop linkages with the Commission and share data. The Commission determines funding allocation based on indices such as:

- range of council services
- size of LGA
- length of roads to construct and maintain
- garbage collection services etc.

6) *How can productivity indicators be improved over time?*

The City of Newcastle recommends the development of an industry wide matrix for productivity indicators. The matrix would assist in the like-for-like assessment of individual council performance. Additional information for note on specific LGA variables could also be identified through commentary.

We suggest that support for this type of matrix would need to be endorsed by the following bodies:

- Division of Local Government
- Local Government Auditors Association
- Local Government Managers Association
- IPART and
- Any other relevant working parties with Council nominated representatives.

7) *Are net costs of individual services useful in measuring and comparing council performance?*

Each Council provides a unique combination of services to it's community, and also has developed it's own method of overhead cost allocation. For these reasons we feel it would be impossible to compare results between different councils without the application of set criteria to streamline the data.

It is likely that the application of set criteria to council results would be a challenging and lengthy process and it may still be questionable how comparable this data is, given other environmental influences and constraints such as the criteria noted in our response to question one.

We acknowledge it may be useful to compare an individual council's results year on year, however it is also noted that using the net costs of a service to measure performance does not take into account community expectations of service levels nor customer satisfaction of the service delivered.

8) *Can councils determine how the cost escalation assumptions in their Long Term Financial Plans are derived and why they are reasonable in the light of current inflationary trends?*

Attached in Appendix 1 is an extract of The City of Newcastle's Long Term Financial Plan which shows the percentage increases used in the projections. This table of assumptions was prepared based on publically available economic forecast information from sources including Westpac Bank and the Australian Bureau of Statistics.

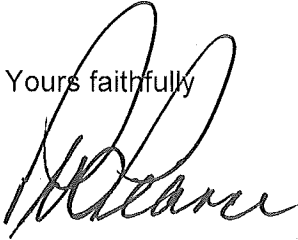
We believe it is the role of IPART or the DLG to set the forecast parameters for all Local Government LTFPs. This is will improve comparability of forecasts across

different LGAs. Parameters may have to have sensitivity applied for metropolitan, rural and regional areas.

The City of Newcastle would like to thank IPART for the opportunity to take part in this consultation process and will be available for further clarification or comment on the responses provided above.

If you require any further information please contact Mr Steve Edmonds, Director City Assets and Chief Financial Officer, on 02 4974 2134.

Yours faithfully

A handwritten signature in black ink, appearing to read 'Phil Pearce', written over the typed name.

Phil Pearce
GENERAL MANAGER

APPENDIX 1

Long Term Financial Plan - Percentage Increases

	<i>Notes</i>	<i>2012</i>	<i>2013</i>	<i>2014</i>	<i>2015</i>	<i>2016</i>	<i>2017</i>	<i>2018</i>	<i>2019</i>	<i>2020</i>	<i>2021</i>
Rates & Charges	1	2.80%	2.70%	2.20%	2.20%	2.40%	3.20%	3.25%	2.30%	2.00%	2.25%
User Fees & Charges	2	4.53%	7.72%	5.58%	5.08%	6.13%	6.13%	6.13%	6.13%	6.13%	6.13%
Interest Income	3	6.00%	6.00%	6.00%	6.00%	6.00%	6.00%	6.00%	6.00%	6.00%	6.00%
Grants & Contributions - Operating	4	4.17%	0.88%	1.91%	2.19%	1.66%	1.66%	1.66%	1.66%	1.66%	1.66%
Other Operating Revenues	5	0.52%	5.95%	0.62%	1.06%	2.54%	3.45%	2.50%	2.20%	2.45%	2.60%
Grants & contributions - Capital	6	-17.38%	-15.97%	2.36%	-2.69%	3.40%	3.45%	2.50%	2.20%	2.45%	2.60%
Employee Costs	7	2.15%	3.25%	3.25%	3.25%	3.25%	3.25%	3.25%	3.25%	3.25%	3.25%
Materials & Contracts	8	3.50%	2.40%	2.40%	2.60%	5.00%	5.00%	5.00%	5.00%	5.00%	5.00%
Borrowings	9	8.00%	8.00%	8.00%	8.00%	8.00%	8.00%	8.00%	8.00%	8.00%	8.00%
Depreciation & Amortisation	10	0.60%	7.85%	2.40%	2.60%	3.40%	3.45%	2.50%	2.20%	2.45%	2.60%
Other Operating Expenses - Waste	11	0.62%	16.69%	15.10%	13.87%	15.00%	15.00%	15.00%	15.00%	15.00%	15.00%
Other Operating Expenses - Residual	12	3.47%	1.54%	5.51%	0.57%	2.54%	2.54%	2.54%	2.54%	2.54%	2.54%

<i>Notes</i>	
1	Based on CPI delayed for one year discounted for productivity factor of 0.2%
2	Based on current projections followed by average of years 2013 - 2015
3	Based on expected average return on the portfolio
4	Based on current projections followed by average of years 2013 - 2015
5	Based on current projections followed by CPI forecasts
6	Based on current projections (major decrease due to less grant funding for Major Projects) followed by CPI forecasts
7	Employee Costs - based on signed award for years 2012-2014, then held at 3.25% for remaining years
8	Based on CPI followed by projected increase
9	Based on current borrowings rates
10	Depreciation - higher than previous increase in 2013 anticipated due to revaluation of infrastructure assets performed in 2011 and 2012
11	Based on current projections followed by average of years 2013 - 2015
12	Based on current projections followed by average of years 2013 - 2015