

LATE ADDENDUM

REPORTS THROUGH THE GENERAL MANAGER

REPORTS FROM THE GENERAL MANAGER

b10 [GM-CM] Local Government Reforms - Fit for the Future

SUBMITTED BY: General Manager

Valid



Civic Leadership

LINKAGE TO INTEGRATED PLANNING AND REPORTING FRAMEWORK:

1	Civic Leadership
1.3	Delivering the objectives of this plan
1.3.2	Council will seek the best value in delivering services

SUMMARY OF REPORT:

The NSW Government requested the Independent Pricing and Regulatory Tribunal (IPART) to undertake the role of the Expert Advisory Panel in assessing local government Fit for the Future (FFTF) proposals. The FFTF reforms aim to improve the strength and effectiveness of local government in providing services and infrastructure that communities need.

Consistent with the NSW Government's Terms of Reference and IPART'S Methodology Paper, IPART assessed the council proposals against the following criteria:

1. Scale and capacity to engage effectively across community, industry and governments;
2. Sustainability;
3. Effectively managing infrastructure and delivering services for communities; and
4. Efficiency.

Consistent with Council's FFTF submission in June 2015, IPART assessed Tweed Shire's submission at the time with then available data on assets as meeting the scale and capacity criteria but not meeting some of the financial criteria, in particular the Operating Performance Ratio which can be affected significantly dependent upon depreciation expenses.

LATE ADDENDUM

As part of Tweed's 30 June submission to IPART, Council advised that the assets were being revalued and their conditions assessed and that an update would be provided once that information had been received. That information has been received by the assessors in the past 2 weeks and an update will now be provided to IPART. Further in the Tweed the Future Is Ours program, covered in more detail within the report, Council's strategy is to engage with the community on service level preferences and the financial challenges and constraint of the FFTF criteria, to arrive at an acceptable solution.

Since the June 2015 submission, Council's general fund Operating Performance Ratio for 2014/15 has exceeded the required benchmark. In addition, results from the asset revaluation for transport and stormwater drainage indicate that Council should have a reduced depreciation expense in 2015/16 of around \$2m, further improving the Operating Performance Ratio.

It is recommended that Council make submission to both IPART and the NSW Government in relation to the new improved results.

In addition to the above, as Kyogle Council is a neighbouring council that was not fit due to scale and capacity, Council needs to indicate the merger preferences for Kyogle Council. It should be noted that Council cannot indicate its preference for who Kyogle Council should merge with, but rather whether Tweed Shire is willing to merge with Kyogle Council.

Given the Independent Local Government Review Panel's preference for Kyogle Shire to merge with either Lismore City Council or Richmond Valley Council, coupled with the geographical constraints servicing Kyogle Shire from the Tweed Shire area, and the communities of interest including distance between major centres of Kyogle, Lismore and Casino, it is recommended that Council decline to indicate its preference to merge.

RECOMMENDATION:

That Council:

1. **Receives and notes the Independent Pricing and Regulatory Tribunal (IPART) "*Assessment of Council Fit for the Future Proposals - Local Government - Final Report October 2015*".**
2. **Makes further submissions to both IPART and the NSW Government in relation to the new improved 2014/15 Operating Performance Ratio results detailed in Council's 2014/15 Annual Financial Statements and the outcome of the revaluation process on depreciation expense calculations.**
3. **Declines the invitation to merge with Kyogle Council.**
4. **Issues a Special Edition of the Tweed Link which informs the community of Council's response to the IPART report.**

LATE ADDENDUM

REPORT:

1. IPART REPORT - BACKGROUND AND FINDINGS

The NSW Government requested the Independent Pricing and Regulatory Tribunal (IPART) to undertake the role of the Expert Advisory Panel in assessing local government Fit for the Future (FFTF) proposals. The FFTF reforms aim to improve the strength and effectiveness of local government in providing services and infrastructure that communities need.

Consistent with the NSW Government's Terms of Reference and IPART'S Methodology Paper, IPART assessed the council proposals against the following criteria:

1. Scale and capacity to engage effectively across community, industry and governments;
2. Sustainability;
3. Effectively managing infrastructure and delivering services for communities; and
4. Efficiency.

The NSW Government has established the 'scale and capacity' criterion as the threshold criterion for councils, which requires councils to meet this criterion to be assessed as fit. Further, councils must also meet the remaining three financial criteria on an overall basis to be assessed as fit.

The IPART report sets out the assessment of whether local councils are fit or not fit for the future based on the proposals submitted. In undertaking the assessments IPART have used the Independent Local Government Review Panel's (ILGRP's) options for reform as a starting point for their analysis.

The NSW Government has announced that councils which are assessed as fit will have access to a range of benefits including a streamlined rate variation process, a State Government borrowing facility, priority for other government funding and grants, and eligibility for additional devolved planning powers. Funding will also be provided by the NSW Government to assist with the transitional costs of merging, establishing regional Joint Organisations (JO), and assisting regional and rural councils.

The assessments will now be considered by the NSW Government in determining the next stage of the reform process.

Key findings

IPART received 139 local council proposals from 144 councils including:

- Four Merger Proposals (involving nine councils)
- 115 Council Improvement Proposals, and
- 20 Rural Council Proposals.

LATE ADDENDUM

IPART assessed 52 proposals as being fit for the future, which represents 37% of the proposals received. To be assessed as fit, councils must have demonstrated they have sufficient scale and capacity and are financially sustainable.

IPART assessed 87 proposals as not being fit for the future, which represents 63% of the proposals received.

Of the 87 proposals assessed as not fit:

- 60 were assessed as not having sufficient scale and capacity, but did meet the financial criteria;
- 18 were assessed as having sufficient scale and capacity, but did not meet the financial criteria, and
- 9 were assessed as not having sufficient scale and capacity and not meeting the financial criteria.

In non-metropolitan areas, a number of councils were assessed as not having sufficient scale and capacity because the council's population is declining or static and is forecast to be below 10,000 by 2031. A population of this size would be likely to affect a council's efficiency and strategic capacity to meet the future needs of its community.

For both Metropolitan Sydney and non-metropolitan councils, the main reason councils did not meet the financial criteria was generally because they forecast an operating deficit throughout the period, including in the benchmark year of 2019-20, and other factors suggest the council has a weak financial position.

Non-metropolitan councils

Outside of Metropolitan Sydney, IPART received:

- 2 Merger Proposals
- 79 Council Improvement Proposals, and
- 20 Rural Council Proposals.

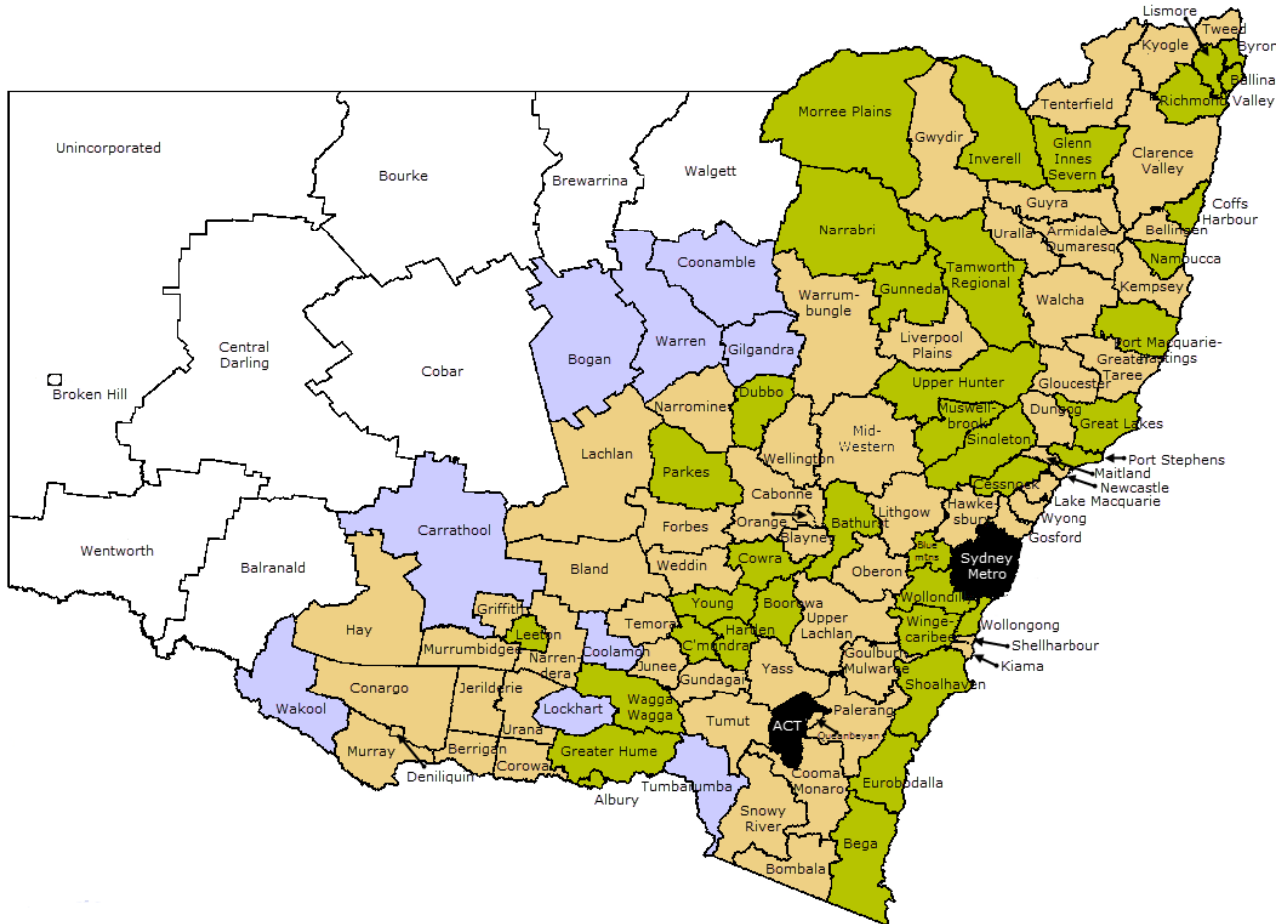
Of these 101 proposals:

- 43 proposals were assessed as fit (including nine Rural Council Proposals which were assessed as fit as Rural Councils), and
- 58 proposals were assessed as not fit for the future.

LATE ADDENDUM

Key:

- Indicates 'fit'
- Indicates 'fit as a Rural Council'
- Indicates 'not fit'



In relation to the 79 Council Improvement Proposals IPART received in non-metropolitan areas, IPART assessed 32 as fit and 47 as not fit.

Councils assessed as fit

IPART assessed 32 Council Improvement Proposals as fit in non-metropolitan areas. The councils that were assessed as fit are spread across all regions in NSW.

These councils were generally assessed as fit because:

- remaining a stand-alone council was consistent with the ILGRP's options for reform or
- IPART analysis has not identified evidence for a better alternative to the council's proposal to stand alone, and
- they met the financial criteria overall.

Councils in non-metropolitan areas were generally more likely to meet the scale and capacity criterion than councils in Metropolitan Sydney. This is because the ILGRP identified fewer preferred merger options in non-metropolitan areas

LATE ADDENDUM

Councils assessed as not fit due to insufficient scale and capacity

IPART assessed 28 Council Improvement Proposals in non-metropolitan areas as not fit because they did not have sufficient scale and capacity. This was generally because:

- the alternative merger option showed substantial gains that were greater than the council remaining a stand-alone council, or
- the council's population was forecast to decline to below 10,000 by 2031, which would be likely to undermine its scale to efficiently deliver services to the local community, and its long term strategic capacity to partner with other levels of government.

It is likely structural changes would be needed to enable these councils to be assessed as meeting the scale and capacity criterion.

Councils assessed as not fit due to not meeting the financial criteria

IPART assessed 13 Council Improvement Proposals as not fit in non-metropolitan areas as they did not meet the financial criteria overall. For these councils, improvements to their financial performance could enable them to become fit. For example, this could include measures to reduce costs through structural changes or by sharing services with neighbouring councils. However, as noted above, the appropriate strategies for each council will depend on their circumstances and the Government's policies.

Councils assessed as not fit due to not meeting the financial criteria and insufficient scale and capacity

IPART assessed six Council Improvement Proposals in non-metropolitan areas as not fit because they did not meet both the scale and capacity criterion and the financial criteria overall. For these councils, both structural changes and improvements to financial performance may be required to enable these councils to become fit.

2. IPART REPORT - TWEED SHIRE COUNCIL RESULTS (refer Attachment 2)

Fit for the Future – NOT FIT

1. *The council satisfies the scale and capacity criterion.*
2. *The council does not satisfy the financial criteria overall. Although it meets the efficiency criterion, the council does not meet the sustainability or the infrastructure and service management criteria.*
3. *The council does not meet the sustainability criterion based on its operating performance ratio being below the benchmark.*
4. *We consider a council's operating performance ratio is a key measure of financial sustainability that all Fit for the Future (FTFF) councils should meet, therefore the council is not fit.*

LATE ADDENDUM

Scale and capacity – satisfies

1. *We consider the council currently meets or partially meets most of the elements of scale and capacity.*
2. *The council's proposal is consistent with the ILGRP's option to stand alone.*
3. *Our analysis has not identified evidence for a better alternative to the council's proposal to stand alone.*

Sustainability – does not satisfy

1. *The council does not meet the criterion for sustainability based on its continuing operating deficits and relatively low building and infrastructure asset renewal ratio. The operating performance ratio was -8.1% in 2014-15 and is forecast to remain in deficit at -4.9% by 2019-20. We estimate that adjusting the operating performance ratio by removing interest income on section 94 Reserves would reduce the ratio by approximately one percentage point to -5.9% in 2019-20.*
2. *The building and asset renewal ratio was 54.1% in 2014-15 and is forecast to reach 52.2% by 2019-20. The own source revenue ratio is greater than the benchmark.*
3. *The council expects to achieve operating surpluses in the longer term, following some consultation with the community. This expected improvement is based on revising service levels and increasing revenue. Consultation regarding service reviews is expected to commence in future years.*

Infrastructure and service management – does not satisfy

1. *The council does not satisfy the criterion for infrastructure and service management based on its infrastructure backlog and asset maintenance ratios forecast neither to improve nor meet the benchmarks.*
2. *The council's infrastructure backlog was 7.3% in 2014-15 and is forecast to increase to 8.9% by 2019-20.*
3. *The asset maintenance ratio was 78.5% in 2014-15 and is forecast to be 71.3% in 2019-20.*
4. *The debt service ratio remains within the benchmark range.*

LATE ADDENDUM

5. *The council states it faces infrastructure and service provision challenges created by a large pensioner population (22%), dispersed populations, frequent flooding, coast erosion and tourism demands. While it has dealt with these to some extent through its large and growing rate base, it is not fully funding its current requirements. It proposes to review services, which may result in reducing the level of service to the community and/or revising the required condition of assets, which would improve the ratios.*

Efficiency – satisfies

1. *The council satisfies the criterion for efficiency based on a decline in real operating expenditure per capita over the period to 2019-20.*

3. IPART REPORT - COMMENTS

The results outlined for Tweed Shire in the IPART assessment against the FFTF criteria are consistent with Council's submission.

The strategy developed to address the non-conforming FFTF benchmark criteria is embedded in the 'Tweed The Future Is Ours' (TTFIO) program.

The program in summary has 3 main stages:-

Stage 1a - Assets

Before embarking on possible solutions to address the FFTF benchmark criteria shortfalls it was considered prudent to first verify our underlying data and projections relating to infrastructure assets.

Over recent months Council has engaged external independent consultants to rate the condition of and re-value our transport and stormwater drainage assets, which also involves reviewing previous assumptions relating to asset consumption and useful lives.

As Council has over \$2b dollars in general fund infrastructure, even minor changes of 1% can have an effect of \$20m and have a material impact on the depreciation expense calculations – which is a major element of the Councils income statement and therefore the Operating Performance Ratio.

Stage 1b – Service Levels

The concurrent stage of the TTFIO program is to document and quantify what current service levels are being provided to the community.

As with any investment decision, it is important to assess what outputs are being provided at what cost so informed decisions can be made.

Stage 2 – Community Engagement

The next all important stage, is to educate and consult with the community in relation to the information provided by stages 1a and 1b, particularly service levels.

LATE ADDENDUM

The service levels determined by the community can have a significant effect on the FFTF criteria results of Building & Infrastructure Renewal, Infrastructure backlog and Asset Maintenance Ratios.

This community engagement approach is consistent with the values embedded in the Integrated Planning & Reporting framework.

Stage 3 – Consolidating the results

The Tweed The Future Is Ours program is scheduled to provide information on assets, services, service levels and the communities preferences near to the election of a new council in September 2016 and the following IPR timetable that's requires a review the Community Strategic Plan, Delivery Program/Operational Plan for the 2017/18 financial year.

Criteria

As indicated in the submission, Tweed Shire Council meets the benchmarks for Scale and Capacity, Own Source Revenue, Debt Service Ratio and the efficiency ratio of decreasing real operating expenditure per capita.

The areas in need of attention within the FFTF criteria are the Operating Performance Ratio, Building & Infrastructure Renewal Ratio, Infrastructure backlog Ratio and Asset Maintenance Ratio.

The following extract from IPART addresses Tweed Shire Council's current approach to addressing the criteria not yet met:-

- 1. The Operating Performance Ratio is a key measure councils should be aiming to meet over time. However, this measure is influenced by depreciation, which is an accounting measure of the estimated consumption of the service potential of an entity's asset base during a period. It can often represent about 25% of a council's annual operating expenses. Thus, changes to a council's approach in estimating depreciation may have a material effect on the Operating Performance Ratio.*

This comment is the basis of TTFIO Stage 1a – Assets.

The 2014/15 Financial Reports show that Council has achieved the Operating Performance Ratio for the general fund. In addition results from the revaluation process outlined in Stage 1a of TTFIO indicate Council should have a reduced depreciation expense in 2015/16 of around \$2m, further improving the Operating Performance Ratio.

- 1. We note a number of councils are consulting with their community to determine if a lower standard of assets (such as roads) is acceptable. If so, under the Office of Local Governments Integrated Planning & Reporting Guidelines, councils may then maintain or renew assets to a 'satisfactory' condition (condition 3), rather than a 'good' condition (condition 2).*

LATE ADDENDUM

This altered approach to asset management effectively reduces both the costs and volume of asset maintenance and renewals over the medium term. This has the effect of improving a council's performance against the financial criteria by:

- *Extending asset lives and reducing depreciation on a yearly basis. This improves performance against the Operating Performance Ratio and the Building & Infrastructure Asset Renewal Ratio.*
- *Reducing the expenditure required to bring assets to an acceptable standard, which decreases the council's Infrastructure Backlog Ratio.*
- *Possibly reducing required asset maintenance, which improves performance against the Asset Maintenance Ratio without increasing current expenditure.*

As a result, many councils are showing improvements across a number of the ratios. In considering these changes, we have examined whether the assumptions used by the council are reasonable. Some councils have also had their altered approach to asset management externally reviewed by consultants. In undertaking the assessments, we have generally accepted these improvements, notwithstanding the fact they are largely a result of a changed approach to asset maintenance and renewal. This is because the new practices are likely to be acceptable to the community, more efficient, and consistent with the Office of Local Governments Integrated Planning & Reporting Guidelines.

This comment is the basis of TTFIO Stage 2 – Community Engagement

Methodology

Whilst the Local Government sector in NSW has had various opportunities to make submissions to various agencies through the local government reform process, it seems inappropriate that IPART's assessments on Councils Fit for The Future submissions, and the subsequent NSW Government decisions, have been conducted on unaudited and unverified information.

This appears at odds with:-

- previous research undertaken by the Independent Local Government Review Panel who commissioned NSW Treasury Corporation to undertake financial assessments of councils on actual audited figures, and
- the NSW Government's support in strengthening audit requirements for the local government sector to assist in identifying trends and opportunities for improvement.
- The NSW Government has also noted it recognises the potential value in giving the Auditor-General responsibility for the audit of councils' financial statements to:

LATE ADDENDUM

- improve quality, consistency, timeliness and financial management more generally, and
- ensure the provision of reliable data that can be used for sustainability assessments and benchmarking.

4. NEXT STEPS

20 October 2015

Councils receive briefing from the Premier and Minister on the findings of the IPART assessment of council Fit for the Future proposals.

21 October 2015

Councils receive an invitation from the Secretary of the Department of Premier and Cabinet to provide feedback on the IPART report and indicate their merger preferences.

By 18 November

Councils are encouraged to review IPART's assessment of their Fit for the Future submission and respond.

For councils that are assessed as being not fit due to scale and capacity, or who neighbour a council that was not fit due to scale and capacity, the Government would also like to know, through the online portal, the merger preferences of these councils.

By end 2015

The Government will consider responses from councils, decide on next steps and inform councils and the community.

Council will make submission to both IPART and the Government in relation to the new improved 2014/15 Operating Performance Ratio results and the outcome of the revaluation process on depreciation expense calculations.

In addition as Kyogle Council is a neighbouring council that was not fit due to scale and capacity, Council needs to indicate the merger preferences for Kyogle Council. It should be noted that Council cannot indicate its preference for who Kyogle Council should merge with, but rather whether Tweed Shire is willing to merge with Kyogle Council.

Given the Independent Local Government Review Panel's preference for Kyogle Council to merge with either Lismore City Council or Richmond Valley Council, coupled with the geographical constraints servicing Kyogle Council from the Tweed Shire area, and the communities of interest including distance between major centres of Kyogle, Lismore and Casino, it is recommended that Council decline to indicate its preference to merge.

OPTIONS:

Not applicable

LATE ADDENDUM

CONCLUSION:

The results outlined for Tweed Shire in the IPART assessment against the FFTF criteria are consistent with Council's submission.

Although Council is committed to the TTFIO program and discussing preferences and challenges with the Tweed community, it is recommended that Council update IPART and the NSW Government with the latest figures for the 2014/15 general fund Operating Performance Ratio and the changes to future depreciation expense calculations.

COUNCIL IMPLICATIONS:

a. Policy:

Not Applicable

b. Budget/Long Term Financial Plan:

Not Applicable

c. Legal:

Not Applicable.

d. Communication/Engagement:

Consult-We will listen to you, consider your ideas and concerns and keep you informed.

UNDER SEPARATE COVER/FURTHER INFORMATION:

Attachment 1. Excerpt from Special Edition of Tweed Link – Fit for the Future, 21 July 2015 (ECM 3836055).

Attachment 2. IPART Report Excerpt- Tweed Shire Council Results (ECM3836107).
