



Independent Pricing and Regulatory Tribunal

Lake Macquarie City Council's application for a special variation 2012/13

Local Government — Determination
June 2012



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1 Determination

The Independent Pricing and Regulatory Tribunal of NSW (IPART) is responsible for setting the amount by which councils can increase their general income, which mainly includes rates income. Each year, we determine a standard increase that applies to all NSW councils, based on our assessment of the annual change in their costs and other factors. This increase is known as the rate peg.

However, councils can apply to us for a special variation that allows them to increase their general income by more than the rate peg. We are required to assess these applications against criteria in the Guidelines provided by the Division of Local Government (DLG),¹ and may allow special variations under either section 508A or 508(2) of the *Local Government Act 1993* (the Act).

In 2012/13 Lake Macquarie City Council applied for a multi-year special variation under section 508A. The council requested annual increases ranging from 10.44% to 4.75% over the next 7 years, equal to a cumulative increase of 73.24% by 2018/19. After assessing its application, we made a decision to approve a smaller, though still substantial, cumulative increase. We have approved a cumulative rise of 57.48% over 7 years.

The percentage increases we have approved are consistent with the council's Option 2, which was the lower of 2 possible increases that the council put to the community during consultation on the proposed special variation.² We consider that this special variation will have a more reasonable impact on ratepayers, yet still allow the council to improve its financial sustainability during the period of the special variation, and make progress on addressing its maintenance and infrastructure backlog while maintaining current levels of services and assets.

We made this decision under section 508A of the Act. By the operation of the Act and the Guidelines, any increases in income determined under section 508A are permanently incorporated into the council's general income.³

¹ *Guidelines for the preparation of an application for a special variation to general income in 2012/2013.*

² See Chapter 2, section 2.6, and Lake Macquarie City Council, *Securing Our Future*, November 2011 (*Securing Our Future*).

³ Implied by the operation of sections 509(1) and (2) of the Act, and also included in the Guidelines, p 9.

1.1 Our decision

IPART decided that Lake Macquarie City Council can increase its general income by the annual percentages shown in Table 1.1, for a cumulative increase of 57.48% over the next 7 years, or 33.78% above the rate peg increase. For each year, the annual increase shown in the table is the total percentage increase allowed.

These increases incorporate the rate peg increases the council would otherwise be entitled to in these years (3.6% in 2012/13 and an assumed 3.0% in each of the subsequent years). Over the 7 years the annual increase is on average 4.83% above the rate peg. The annual increases in dollar amounts that we have calculated allow for the expiry of an existing special variation in June 2014.⁴

Table 1.1 IPART's determination on Lake Macquarie City Council's special variation for 2012/13 to 2018/19

Year	Increase in general income approved (%)	Cumulative increase in general income approved (%)	Annual increase in general income (\$)	Total permissible general income ^a (\$)
2011/12				83,411,250 ^b
2012/13	10.36	10.36	8,641,406	92,055,048 ^c
2013/14	10.17	21.58	9,361,998 -2,629,382 ^d	101,417,046
2014/15 ^e	6.23	29.16	6,154,471	104,942,136
2015/16	5.58	36.37	5,855,771	110,797,907
2016/17	5.25	43.52	5,816,890	116,614,797
2017/18	4.75	50.34	5,539,203	122,154,000
2018/19	4.75	57.48	5,802,315	127,956,315

a Permissible general income refers to the maximum general income that the Council can generate in the year. It equals the previous year's notional general income level adjusted for any expiring special variation, other adjustments (prior year catch ups, excesses, valuation objections and income adjustments for Crown land) plus the annual dollar increase permitted by the proposed special variation percentage.

b This income level is the 2011/12 adjusted notional general income level, not the permissible general income level. The income level in 2011/12 is not part of the council's application and is only included here to indicate the size of the base to which the special variation applies.

c The council's proposed permissible general income in 2012/13 includes the requested special variation of 10.44% and an increase of \$2,392 for a prior year catch up. It will also be subject to a reduction of \$48,783 due to a valuation objection proposed to be recouped in this year but which had not been recouped by the time of the council's application to IPART and therefore is not included in the calculations in the table.

d This is the effect of the expiry of the Sustainability Levy on 30 June 2014.

e The percentage for 2014/15 includes an amount equal to the value of the special variation that expires in June 2014.

Source: Lake Macquarie City Council, Emails to IPART dated 14 and 23 May 2012, and *Securing Our Future*, November 2011 (*Securing Our Future*) p 13, and IPART calculations.

⁴ The impact of the expiry in June 2014 of the existing special variation for the Sustainability Levy is to make the actual percentage increase in general income over the 7 years 53.40%, not 57.48%. It is not possible to determine the council's future general income with precision: see note 25.

We have attached conditions to this decision, including that the council use the income raised through the special variation for purposes consistent with those set out in its application. Box 1.1 lists these conditions.

In making this decision, we recognise that the council will not be able to undertake the full allocation of expenditure on the purposes set out in its application (see Appendix A), and will need to re-prioritise planned expenditures in future years.

Box 1.1 Conditions attached to IPART's decision on Lake Macquarie City Council's application for a special variation

IPART's approval of Lake Macquarie City Council's application for a special variation over the period from 2012/13 to 2018/19 is subject to the following conditions:

- ▼ The council uses the additional income from the special variation to fund service levels and community infrastructure consistent with the council's application.
 - ▼ The council reports in its annual report for each rating year over this period on:
 - expenditure on service levels and community infrastructure consistent with the council's application
 - the outcomes achieved as a result of the special variation
 - its asset renewal and maintenance expenditure
 - productivity savings achieved, and
 - any significant variations from its financial results as forecast in its Long Term Financial Plan and any corrective action taken or to be taken.
-

1.2 What did the council request and why?

Lake Macquarie City Council applied to increase its general income by a cumulative 73.24% over the 7-year period from 2012/13 to 2018/19, and to permanently incorporate this increase into its general income base.⁵ The increase included the rate peg available to all councils, and the value of an existing special variation due to expire in June 2014.

The council intended to use the income from the requested special variation to improve the council's financial sustainability, while maintaining or enhancing current service levels and improving community infrastructure.

Table 1.2 shows the components of the requested special variation.

⁵ Lake Macquarie City Council, *Section 508A Special Variation Application 2012/13 – Part A* (Lake Macquarie Application Part A), Worksheet 1.

The council estimated that if its requested special variation were approved, its permissible general income would increase from \$83.41m in 2011/12 to \$140.76m in 2018/19. This represents a cumulative increase of \$236.91m over 7 years, or \$171.25m above the rate peg increase.⁶

Table 1.2 Components of Lake Macquarie City Council's requested special variation for 2012/13 to 2018/19 (%)

Year	Rate peg ^a	Additional increase requested	Total annual increase
2012/13	3.6	6.84	10.44
2013/14	3.0	7.34	10.34
2014/15	3.0	6.77	9.77
2015/16	3.0	4.95	7.95
2016/17	3.0	4.29	7.29
2017/18	3.0	3.75	6.75
2018/19	3.0	1.75	4.75

^a In 2012/13, the rate peg of 3.6% reflects IPART's determination; in the following years it is assumed to be 3.0%.

Source: Lake Macquarie City Council, *Section 508A Special Variation Application 2012/13 - Part A* (Lake Macquarie Application Part A), Worksheet 1.

The council indicated that the additional income would be used in this way:

- ▼ More than \$170m would allow the council to maintain current levels of services to the community, including projects funded by the expiring Sustainability Levy: \$166.80m would remove the operating deficit expected until 2016/17, and a further \$3.83m would achieve operating surpluses in 2017/18 and 2018/19.⁷
- ▼ An allocation of \$53.32m would be used for additional infrastructure maintenance and ranger services, and to enhance some services and assets eg, roads, libraries and pools.
- ▼ \$14.19m would meet additional borrowing costs related to loans to implement a program of new capital investment, including improvements to parks and recreation facilities, major upgrades to 3 pools, 2 new libraries and upgrades to 3 others, upgrades to 9 major town centres, new footpaths and cycleways, upgrades to community facilities and 2 new centres for dementia day care and pensioners and community care.⁸

⁶ Lake Macquarie Application Part A, Worksheet 1 and IPART calculations. Appendix A, based on Lake Macquarie Application Part A, Worksheet 7 shows a cumulative rise of \$250.08m because it does not adjust for the reduced income related to the expiring levy.

⁷ Lake Macquarie City Council, *Section 508A Special Variation Application 2012/13 - Part B* (Lake Macquarie Application Part B), Supporting Document 3.1 *Lake Macquarie City Council Long Term Financial Plan* (updated February 2012) (Lake Macquarie LTFP), p 28, and Lake Macquarie Application Part B, Table 3.24 pp 101-103.

⁸ Lake Macquarie Application Part A Worksheet 7, and Part B, Supporting Document 3.15 *Financial Data for Special Variation Scenario 1, 2 and 3*, pp 15ff and IPART calculations. See generally Lake Macquarie Application Part B, Section 3 Need for the variation, pp 20-24, Table 3.1 pp 28-31, Table 3.15 pp 68-69, pp 70-73, and Tables 2.4 and 2.5, pp 12-17; and LTFP pp 9 and 28-29.

More detail on Lake Macquarie City Council's proposed program of expenditure to 2018/19 is provided in Appendix A and section 2.4.

1.3 How did we reach our decision?

We assessed Lake Macquarie City Council's application against the 6 criteria in the Guidelines for s508A applications. We found that the application addressed the criteria systematically and thoroughly, and included comprehensive supporting information. However, we found that it met some of these criteria only partially.

In particular, we were satisfied that the council has shown that significant rate increases are needed to improve its financial sustainability and to maintain its services and assets in line with community expectations. We were also satisfied that it provided evidence of community support for significant rate increases, and that Option 2 would have a more reasonable impact on ratepayers. We found that:

- ▼ A more moderate cumulative increase – such as the increase under the second of the 3 options the council consulted its community on (Option 2) – would still enable it to achieve financial sustainability (by eliminating its operating deficits) over the 7-year period, while also allowing for continuing growth in operating expenditure, additional asset maintenance, and funding loans for capital works.
- ▼ The council's consultations showed clear community support for rate increases at least as large as those in Option 2 but the extent of support for Option 3 was harder to assess.
- ▼ While socio-economic indicators suggest that the Lake Macquarie community has the capacity to pay higher rates than at present, we judged that a more moderate cumulative increase would have a more reasonable impact.

For these reasons, we decided to approve a cumulative rise in general income of 57.48% over 7 years (rather than 73.24% as the council requested). The approved increase is consistent with the council's Option 2.

Table 1.3 summarises our findings against each of the criteria.

Table 1.3 Summary of IPART's assessment against the criteria in the Guidelines

Criterion	IPART findings
1. Demonstrated need for the rate increases derived from the councils Integrated Planning and Reporting Framework	<p>The requested special variation:</p> <ul style="list-style-type: none"> ▼ is based on the council's long-term financial and strategic planning ▼ broadly reflects the community's priorities as identified through consultation in the IPRF and the special variation ▼ incorporates alternative revenue sources ▼ will fund an efficient and feasible program of expenditure. <p>The special variation will improve the council's financial sustainability. The council is to be commended for addressing its financial sustainability, including managing the backlog in maintenance and renewing its substantial and ageing asset base.</p> <p>However, this objective should be considered in light of evidence of the community's willingness to pay higher rates, and its capacity to pay over a relatively short period of time. The council has demonstrated the need for a significant increase in its general income to address its financial sustainability, but not shown that the increase needs to be as large as requested. Option 2 will still enable the council to eliminate its operating deficit within the 7-year period, and therefore take a major step towards financial sustainability.</p>
2. Demonstrates community support for the special variation	<p>The council engaged extensively with the community to determine its priorities and the level of support for a special variation.</p> <p>The consultation strategy was conducted in accordance with the advice to councils set out in the Guidelines.</p> <p>Consultation showed clear community support for significant rate increases of at least the size we have decided to approve. Most submissions to IPART indicated opposition to the special variation, many on the grounds of affordability of the proposed increase. Submissions also opposed the special variation because of the council's perceived poor performance.</p> <p>While we considered the views in submissions, we could not assess how statistically reliable or representative of the whole community they were.</p> <p>Many submissions expressed concerns about the consultation strategy, however, we consider that the council attempted to widely publicise its request for feedback on the proposed special variation.</p>
3. Reasonable impact on ratepayers	<p>The lower increases implied by Option 2 are considered to be more reasonable.</p> <p>We note:</p> <ul style="list-style-type: none"> ▼ socio-economic indicators suggest that the community has the capacity to pay higher rates, but not necessarily cumulative increases as high as those the council requested ▼ consultation undertaken by the council suggested that the community is prepared to pay higher rates, however public submissions expressed concerns about the affordability of the rate increases, particularly in the current economic

Criterion	IPART findings
	climate. The council has a payment assistance policy. Given the increases to rates we have approved, we expect the council to respond appropriately to ratepayers who have difficulty in meeting their rate obligations.
4. Sustainable financing strategy consistent with the principles of intergenerational equity	The council has a financing strategy that is consistent with intergenerational equity. It has a policy of borrowing, within prudent limits, to support its capital works program. The council has also incorporated alternative revenue sources to support operational costs.
5. An explanation of the productivity improvements and cost containment strategies the council has implemented in past years, and is planning over the requested special variation period	The comparative productivity indicators show that the council is relatively efficient compared with its peer group and NSW councils generally. The council has systematically identified productivity improvements and expenditure savings, and implemented other cost containment and revenue-sourcing strategies. The comprehensive Service Review (2009-2011) identified \$4.2m in ongoing savings. The council is committed to pursuing these approaches in the future. While submissions claimed that the council was inefficient and wasted expenditure, and should be able to reduce its expenditure and avoid rate increases, we found no evidence in submissions or comparative data to indicate the council's productivity was a major concern. It appears that significant reductions in expenditure are possible only if the scope and level of services to ratepayers are substantially reduced.
6. Implementation of Integrated Planning and Reporting Framework (IPRF)	All plans and documentation have been reviewed by the DLG which has advised IPART that the council's implementation of the IPRF has been satisfactory.

Note: In accordance with the Guidelines, IPART may also consider any other matters it considers relevant in assessing a council's application for a special variation. In the case of Lake Macquarie City Council's application, no other matters were identified.

1.4 What does our decision mean for the council?

Our decision means that Lake Macquarie City Council is able to increase its general income over the 7-year period from \$83.41m to \$127.96m in 2018/19 (see Table 1.1). After 2018/19, all other things being equal, the council's permissible general income will increase by the annual rate peg unless we approve a further special variation.⁹

⁹ The actual general income in future years will be influenced by a range of factors apart from the rate peg: see note 25.

We estimate that over these 7 years, the council will generate additional rate revenue of \$192.06m, or \$126.39m above the rate peg.¹⁰ This extra income is lower than the council requested, but council projections indicate that it would still allow the council to eliminate its operating deficit after 5 years while maintaining the level of services and assets its community expects, make progress in addressing its asset backlog, and fund a more limited program of new and replacement capital works.

The council will not be able to undertake the full program of expenditure it proposed for the additional revenue that would have come from its requested special variation, and will need to re-prioritise planned expenditures in future years.

1.5 What does our decision mean for ratepayers?

While IPART sets the allowable increase in general income, each individual council determines how it will allocate this increase to different categories of ratepayer. Councils usually set their rates in June or July for the following year.

In its application, Lake Macquarie City Council indicated that it intended to apply the requested rate increases differentially among its ratepayers. Similarly, when it put Option 2 to the community during consultation, it indicated that increases for business and mining ratepayers would be higher in the first 4 years than for residential and farmland ratepayers.¹¹

Assuming that the council will allocate the approved special variation in accordance with Option 2 as proposed during consultation, we expect that over the 7 years:

- ▼ average residential rates will rise by \$93 in the first year, and by \$524 over 7 years, a cumulative increase of 55.2%, and
- ▼ average business rates will rise by \$460 in the first year, and by \$2,332 over 7 years, a cumulative increase of 71.0%.

Table 1.4 sets out the annual percentage and dollar increases that the council indicated it would apply to average residential and business rates under Option 2.

¹⁰ Lake Macquarie City Council, Emails to IPART dated 14 and 23 May 2012, and IPART calculations.

¹¹ Lake Macquarie City Council, *Securing Our Future*, p 13.

Table 1.4 Indicative annual increases in average residential and business rates 2012/13 to 2018/19 as a result of IPART's determination of the Lake Macquarie City Council's special variation application

Year	Annual % increase		Average rate (\$)	
	Residential	Business	Residential	Business
2011/12			949	3,284
2012/13	9.75	14.00	1,042	3,743
2013/14	9.50	14.00	1,141	4,267
2014/15 ^a	6.00	7.50	1,209	4,588
2015/16	5.50	6.00	1,276	4,863
2016/17	5.25	5.25	1,343	5,118
2017/18	4.75	4.75	1,407	5,361
2018/19	4.75	4.75	1,473	5,616

^a The increase in 2014/15 has been adjusted for the impact of the expiring special variation for the Sustainability Levy which will expire in June 2014.

Source: Lake Macquarie City Council, *Securing Our Future*, p 13 and IPART calculations.

However, these rate increases are indicative only and the actual impact on rates is a matter for the council to determine, consistent with this decision.

1.6 What does the rest of this report cover?

The rest of this report discusses the council's application and our assessment and findings in making our decision in more detail:

- ▼ Chapter 2 focuses on the council's application
- ▼ Chapter 3 discusses our assessment against the criteria.

The appendices set out the council's proposed program of expenditure on services, assets and borrowing costs, provide a summary of the comparative data we considered in our assessment, such as average local government area (LGA) income levels and council labour costs, and outline the council's consultation strategy.

2 Lake Macquarie City Council's application

Lake Macquarie City Council applied to increase its general income over 7 years by a cumulative 73.24% – or 49.54% above the rate peg increase – and to incorporate this increase permanently in its general income base.¹²

The sections below provide some brief background information on the council, and its history of special variations. The subsequent sections outline its application for a special variation in 2012/13, how the council proposes to use the additional income it would raise, and how the necessary rate increases would affect different ratepayers. The final section outlines Option 2 that the council consulted the community on when it gauged the community's support for a special variation. IPART approved a special variation for the council consistent with the increases in general income under Option 2.

2.1 About the council

The Lake Macquarie LGA is in the Lower Hunter Valley, and circles Australia's largest coastal saltwater lake. With an estimated 201,000 residents in 2011, it is the fourth most populous LGA in NSW.

Urban settlement is dispersed around the lake, in 9 major townships and about 80 suburbs and villages. The economy is diverse. The main activities are primary industries (coal, timber, agriculture and fishing), manufacturing and tertiary industries (retail trade, health and community services, construction, technology and tourism).

The Lower Hunter Regional Strategy identifies Lake Macquarie as a growth area with population projected to grow by 60,000 between 2006-2031, creating demand for 36,000 new dwellings and 12,200 new jobs. Based on these projections, the council estimates that there will be 40,000 more residents between 2010 and 2031.¹³

¹² Lake Macquarie Application Part A, Worksheet 1.

¹³ Lake Macquarie Application Part B, pp 23 and 149-150.

As a result of this anticipated urban growth, the council will need to provide infrastructure and services to the new residents and industrial and commercial development. Another challenge for the council in the future will be working with the community on environmental management of the lake and the south and western semi-rural areas, dealing with the historical legacy of industrial activity and preparing for identified risks associated with flooding and sea level rise.¹⁴

The council is in DLG Group 5, which indicates it is classified as an "urban large/very large regional town/city".¹⁵ The 6 councils in this group have quite different characteristics, so we also compared the council with both its Group 5 peers and other large councils on urban fringes or with high population growth.

The Lake Macquarie LGA has a SEIFA ranking of 102, placing it among the top third least disadvantaged area in NSW.¹⁶ It has lower unemployment (September quarter 2011) and higher home ownership rates than the average for all LGAs across NSW. Its average income is slightly higher than the averages for DLG Group 5 and NSW.

In 2010/11, the council's average residential rate was \$880, which was close to the average for DLG Group 5 of \$889, but considerably higher than the average for NSW of \$659.¹⁷ Its average business rates were \$3,146, which was less than the average for DLG Group 5 (\$4,421), and significantly less than those of the more comparable councils in this group, Newcastle City Council (\$6,891) and Wollongong City Council (\$8,704).

In 2010/11, the council derived 50% of its General Fund¹⁸ revenue from rates and annual charges, which was marginally higher than the averages for DLG Group 5 (48.0%) and NSW (46.7%).¹⁹

¹⁴ Lake Macquarie Application Part B, Supporting Document 2.1 *Providing Enduring Value (Providing Enduring Value)*, p 5.

¹⁵ DLG, *Snapshot of NSW Councils: Comparative Information on NSW Local Government Councils 2008/09*, pp 11-17. The Australian Classification of Local Governments (ACLG) system classifies councils into 22 categories according to their socio-economic characteristics and their capacity to deliver a range of services to the community. The DLG has reduced this to 11 groups because some of the ACLG categories contained few or no councils in NSW. There are 5 other councils in DLG Group 5: Coffs Harbour City Council, Newcastle City Council, Shoalhaven City Council, Tweed Shire Council and Wollongong City Council.

¹⁶ SEIFA is the Socio-Economic Index for Areas published by the Australian Bureau of Statistics and incorporates a number of individual indexes that can be used to determine the level of social and economic well-being in regions relative to one another. One of the indexes is the Index of Relative Socio-economic Advantage and Disadvantage for NSW in 2006. The SEIFA used in this report ranks Local Government Areas from 1 to 153 (includes 1 ranking for "unincorporated NSW"). A ranking of 1 means the council is least advantaged relative to all the other councils in NSW. A ranking of 153 means it is least disadvantaged relative to all the other councils in NSW. See Appendix B.

¹⁷ DLG, unpublished comparative data, 2010/11.

¹⁸ General Fund refers to all council activities except Water and Sewer. In some cases, a council's General Fund may also exclude its other separate business activities eg, airports, but these General Fund data do not exclude this type of service revenue.

¹⁹ DLG, unpublished comparative data, 2010/11.

Comparisons on a per capita basis for Lake Macquarie City Council reflect its large population. Overall, General Fund revenues in 2010/11 were \$1,025 per person, which was lower than the averages for DLG Group 5 (\$1,282) and NSW (\$2,006). Spending on services per capita was low (\$554), compared with \$745 for DLG Group 5 and \$1,129 for NSW. Lake Macquarie City Council had 1 FTE staff member for every 227 residents, which was much higher than the ratios for DLG Group 5 (165) and NSW (126).

Appendix B provides a range of comparative data for the council.

2.2 History of special variations

In the past 12 years, the council has had 10 special variations approved by the Minister for Local Government, all under section 508(2) of the *Local Government Act 1993*:

- ▼ In 1999/2000, a special variation of 5.37% for 3 years was approved for Lake Macquarie remedial work.
- ▼ In 2000/01 a special variation for the Belmont Mainstreet program was approved, which was extended on 2 occasions, each time for 3 years (revenue \$70,000 to \$91,000 pa).
- ▼ The special variation for the Lake Macquarie remedial work was renewed in 2002/03 and 2005/06, each time for 3 years (revenue raised was between \$1.62m and \$1.74m pa).
- ▼ In 2007/08, a special variation of 8.54% (\$3.62m) to be permanently retained in the rate base was approved, for infrastructure maintenance and renewal.
- ▼ In both 2008/09 and 2009/10 single-year increases of 6.04% and 6.29% respectively, (revenue approximately \$2.02m and \$2.05m) were approved for lake improvement and sustainability activities and works.
- ▼ In 2010/11, an increase of 5.3% (2.7% above the rate peg, \$2.10m) for 4 years was approved as a 'Sustainability Levy'. The levy was to continue sustainability activities and works on the lake and local environment, including dealing with the increasing risk of climate change. It is due to expire in June 2014.²⁰

The council reports on spending under the 2 current special variations in its annual report.

²⁰ DLG, *Special Variation Master Record*, copy provided to IPART in October 2010 and Lake Macquarie Application, Part B Table 9.1 pp 182-183.

2.3 Requested special variation for 2012/13

Lake Macquarie City Council applied to increase its general income by a cumulative total of 73.24% over the 7-year period from 2012/13 to 2018/19.

The requested percentage includes an amount to improve its financial sustainability, and enhance services and assets, and also:

- ▼ The rate peg of 3.6% IPART has set for 2012/13 and an assumed rate peg of 3.0% in each of the following years.²¹ (Note that in setting the rate peg for 2012/13, IPART included a carbon price advance of 0.4% to assist councils to meet higher prices arising from the introduction of the carbon price from 1 July 2012²².)
- ▼ The value (2.59% or \$2.63m of rate revenue in 2013/14) of the existing special variation for the Sustainability Levy, which will expire on 30 June 2014. (The council is seeking to incorporate the value of this special variation into its rates base from 2014/15.)²³

Table 2.1 sets out the percentage increases in general income requested by Lake Macquarie City Council and its estimate of the total allowable increase in permissible general income from 2012/13 to 2018/19. This estimate has been verified by the DLG.²⁴

²¹ If the rate peg is higher or lower than the 3% assumed, this is unlikely to have an impact on the council's future general income, as the special variation percentage has been determined and will apply in the period specified. Under the Act, a council may apply to IPART to vary or revoke a special variation made under Section 508A. Any application will be assessed against any applicable Guidelines. However, IPART considers that a request to vary or revoke a special variation would be an exception or due to special circumstances eg, as a result of the carbon price adjustment in the 2012/13 rate peg decision.

²² Given that the effects of the carbon price will eventually be captured in the Local Government Cost Index (LGCI), we will reverse the upfront adjustment we have made in the 2012/13 rate peg over 2 years. We will deduct 0.1% in 2013/14 and 0.3% in 2014/15 from the rate pegs in these years. See *IPART, Effects of the carbon price on local councils*, Local Government – Information paper, December 2011 for more information.

²³ Lake Macquarie Application Part B, pp 14-15.

²⁴ DLG, *Assessment of Lake Macquarie City Council's s 508(A) Special Variation Application – Part A*, March 2012.

Table 2.1 Special variation requested by Lake Macquarie City Council 2012/13 to 2018/19

Year	Annual increase in general income (%)	Cumulative increase in general income (%)	Annual increase in general income (\$)	Cumulative increase in general income (\$)	Decrease due to expiry of special variation (\$)	Total permissible general income ^a (\$)
2011/12						83,411,250 ^b
2012/13	10.44	10.44	\$8,708,135	\$8,708,135		92,121,777 ^c
2013/14	10.34	21.86	\$9,525,392	\$18,233,526	-2,635,348 ^d	101,647,169
2014/15	9.77 ^e	33.77	\$9,673,455	\$27,906,981		108,685,276
2015/16	7.95	44.40	\$8,640,479	\$36,547,461		117,325,755
2016/17	7.29	54.93	\$8,553,048	\$45,100,508		125,878,802
2017/18	6.75	65.38	\$8,496,819	\$53,597,327		134,375,622
2018/19	4.75	73.24	\$6,382,842	\$59,980,169		140,758,464

a Permissible general income refers to the maximum general income that the Council can generate in the year. It equals the previous year's notional general income level adjusted for any expiring special variation, other adjustments (prior year catch ups, excesses, valuation objections and income adjustments for Crown land) plus the annual dollar increase permitted by the proposed special variation percentage.

b This income level is the 2011/12 adjusted notional general income level, not the permissible general income level. The income level in 2011/12 is not part of the council's application and is only included here to indicate the size of the base to which the special variation applies.

c The council's proposed permissible general income in 2012/13 includes the requested special variation of 10.44% and an increase of \$2,392 for a prior year catch up. It will also be subject to a reduction of \$48,783 due to a valuation objection proposed to be recouped in this year but which had not been recouped by the time of the council's application to IPART and therefore is not included in the calculations in the table.

d This is the effect of the expiry of the Sustainability Levy on 30 June 2014.

e The percentage for 2014/15 includes an amount equal to the value of the continuation of the special variation that expires in June 2014.

Source: Lake Macquarie Application Part A, Worksheets 1 and 4.

As a result of the special variation, the council estimates its permissible general income would rise by \$57.35m, from \$83.41m in 2011/12 to \$140.76 in 2018/19.²⁵ This increase would be permanently retained in the rates base from 2019/20. Although the cumulative percentage increase of the requested special variation is 73.24%, because of the impact of the expiring special variation, if IPART approved the request, the actual cumulative increase in permissible income would be 68.75%. The additional revenue from the special variation will amount to \$236.91m over 7 years, or \$171.25m above the rate peg increase.²⁶

²⁵ Lake Macquarie Application Part A, Worksheets 1 and 4. It is not possible to determine the council's future general income with precision. Actual general income is affected by many factors, including the number of rateable properties and adjustments for previous under- or over-collection of rates. The DLG is responsible for monitoring and ensuring compliance.

²⁶ Lake Macquarie Application Part A, Worksheet 1 and IPART calculations. Appendix A, based on Lake Macquarie Application Part A, Worksheet 7 shows a cumulative rise of \$250.08m because it does not adjust for the reduced income related to the expiring levy.

2.4 How the council proposes to use the income raised

The council is seeking the special variation to improve its financial sustainability, and to enhance services and assets. Over the 7 years to the end of the special variation period, the council projects that it would receive, relative to its baseline scenario without the requested special variation, increased rates revenue of \$173.67m and increased other revenue by \$20.30m (mainly from moderately greater interest received and user fees and charges).²⁷

It would use the extra income of \$193.97m over the 7-year period to:

- ▼ increase its recurrent operating expenses by \$41.05m
- ▼ fund higher borrowing costs of \$12.01m
- ▼ increase its depreciation allowances by \$7.96m
- ▼ use the balance of \$132.95m to turn around its operating deficits into small operating surpluses totaling around \$3.83m in 2017/18 and 2018/19.

In its application, the council explained how it would use its funds, not as the difference between its LTFP baseline and special variation scenarios (as explained above), but in terms of income and spending flows above their 2011/12 levels. In those terms, the cumulative increase in rates income amounts to a total of \$250.08m of which:

- ▼ approximately \$166.80m would be used to turn around the operating deficit expected until 2016/17, and about \$3.83m to achieve operating surpluses in 2017/18 and 2018/19²⁸
- ▼ \$53.32m would be allocated to infrastructure maintenance and to enhance some services and assets, primarily for road resurfacing and reconstruction, and also for libraries and pools, and for additional maintenance and ranger services
- ▼ \$14.19m would be used to meet additional borrowing costs for loans related to a program of new capital investment.²⁹

The additional income would allow the council to maintain current levels of services to the community, and continue projects funded by the expiring Sustainability Levy.³⁰

²⁷ Lake Macquarie Application Part B, Supporting Document 3.1 *Lake Macquarie City Council Long Term Financial Plan* (updated February 2012) (LTFP), p 28.

²⁸ Lake Macquarie LTFP, p 28.

²⁹ Lake Macquarie Application Part A Worksheet 7, LTFP pp 9 and 28, and Part B, Supporting Document 3.15 *Financial Data for Special Variation Scenario 1, 2 and 3*, pp 13-24. See generally Lake Macquarie Application Part B, Section 3 Need, pp 20-24, Table 3.1 pp 28-31, Table 3.15 pp 68-69, and Table 2.5, pp 16-17, and LTFP pp 28-29. The balance of the \$250.08m is largely the cumulative effect of the reduction in income that occurs when the existing special variation expires at the end of 2013/14.

³⁰ Lake Macquarie Application Part B, Table 3.24 pp 101-103.

The council's application indicated that additional income would also allow the council to address its maintenance and infrastructure backlog (currently estimated at \$67m) and make new capital expenditure of \$326m, and replacement capital expenditure of \$344m.

The major elements of additional expenditure on infrastructure construction and renewal to be made possible if the special variation were approved include an extra \$42.0m for road resurfacing and reconstruction, an extra \$16.8 for capital improvements to parks and sportsgrounds, \$20.4m for major upgrades to 3 pools, \$7.4m for 2 new libraries, \$7m for upgrades to major town centres, \$4.9m for upgrades to community facilities (including centres for dementia day care and pensioners and community care), \$3.5m for new footpaths and cycleways, and \$2.4m for a sculpture park and seminar rooms at the art gallery.³¹

The proposed expenditure from the revenue raised by the special variation in each of the 7 years is set out in Appendix A.

2.5 How does the council propose to allocate the special variation among ratepayers?

The council has 4 rating categories, and levies only an ordinary rate in each category. There are no special or minimum rates. In 2012/13, the council expects to issue 75,109 residential, 3,742 business, 53 farmland and 19 mining assessments.

The council indicated that it would apply the rate increases resulting from the requested special variation differentially among its ratepayers, with higher increases for business and mining ratepayers in the first 5 years. The cumulative increases would be 65.33% for residential rates, 64.17% for farmland rates, 86.61% for mining rates and 87.34% for business rates.³² Table 2.2 sets out the percentage increases in each category.

Table 2.2 Lake Macquarie City Council proposed percentage change in rates by rating category for requested special variation 2012/13 to 2018/19 (%)

Rating Category	2012/13	2013/14	2014/15 ^a	2015/16	2016/17	2017/18	2018/19
Residential	9.84	9.70	6.18	7.75	7.25	6.75	4.75
Farmland	9.07	9.70	6.18	7.75	7.25	6.75	4.75
Business	14.45	14.00	9.59	9.00	7.50	6.75	4.75
Mining	14.00	14.00	9.59	9.00	7.50	6.75	4.75

^a The percentage increase in 2014/15 is lower than the percentage increase in general income because the special variation for the Sustainability Levy expires in June 2014.

Source: Lake Macquarie Application Part A, Worksheet 5.

³¹ Lake Macquarie Application Part B, pp 70-73. See also Table 2.5, pp 16-17 and Table 3.1, pp 28-31.

³² Lake Macquarie Application Part A, Worksheet 5.

Table 2.3 shows the dollar impact of the proposed rate increases on the ratepayer categories. The increase in 2014/15 is reduced by the expiring Sustainability Levy.

Table 2.3 Lake Macquarie City Council estimated rate increases under the requested special variation 2012/13 to 2018/19

	11/12 ^a	12/13	13/14	14/15 ^a	15/16	16/17	17/18	18/19
Average residential rate (\$)	949	1,043	1,144	1,215	1,309	1,404	1,498	1,570
\$ Increase		93	101	71	94	95	95	71
% Increase		9.84	9.70	6.18	7.75	7.25	6.75	4.75
Average farm-land rate (\$)	1,622	1,769	1,941	2,061	2,221	2,381	2,542	2,663
\$ Increase		147	172	120	160	161	161	121
% Increase		9.07	9.70	6.18	7.75	7.25	6.75	4.75
Average business rate (\$)	3,284	3,758	4,284	4,695	5,118	5,501	5,872	6,152
\$ Increase		474	526	411	423	384	371	279
% Increase		14.45	14.00	9.59	9.00	7.50	6.75	4.75
Average mining rate (\$)	31,122	35,479	40,447	44,325	48,315	51,938	55,444	58,078
\$ Increase		4,357	4,967	3,879	3,989	3,624	3,506	2,634
% Increase		14.00	14.00	9.59	9.00	7.50	6.75	4.75

^a The increase in 2014/15 is lower because a special variation for the Sustainability Levy expires in June 2014.

Source: Lake Macquarie Application Part A, Worksheet 5, Part B, pp 143-144 and IPART calculations.

A cumulative increase of 65.33% for residential rates would mean that average residential rates would be \$621 higher in 2018/19 than in 2011/12. A cumulative increase for business rates of 87.34% would mean average business rates would be \$2,868 higher in 2018/19 than in 2011/12.

The council also intends to increase the annual Domestic Waste Management (DWM) charge for residential properties over the 7 years by a cumulative 40%, from \$350 in 2011/12 to \$490 in 2018/19.³³

³³ Lake Macquarie Application, Part A Worksheet 5. The DWM charge is a flat rate for waste services calculated annually on a cost recovery basis. It includes the waste levy charged by the state government.

2.6 What was Option 2 that the council consulted the community on?

In its consultation program for the proposed special variation, 'Securing Our Future', Lake Macquarie City Council sought the community's feedback on 3 options.³⁴ The council considered that Option 2 would allow it improve its financial sustainability while maintaining services and assets at current levels. It did not allow for the program of additional capital investment which would be funded by the additional revenue under Option 3.

Option 2 was for a lower percentage increase in rate revenue over the 7 years,

- ▼ average increase in residential rates of 7.7% pa, including the rate peg
- ▼ average increase in business rates of 9.9% pa, including the rate peg.

The indicative annual percentage and dollar increases for residential and business rates are set out in Table 1.4 in Chapter 1. The council stated that the rate increases applied to farmland rates would be similar to increases to residential rates, and increases to mining rates similar to business rate increases.

The major areas of expenditure proposed under Option 2 are:

- ▼ an extra \$6m over 7 years for maintenance of assets and infrastructure, so that current standards and response times will be maintained
- ▼ an extra \$16m over 7 years for road reconstruction and resurfacing
- ▼ minor upgrades of pool equipment but no upgrades of pools
- ▼ continue projects funded by the Sustainability Levy continue beyond 2013/14
- ▼ maintain current staff levels and increase ranger staffing
- ▼ maintain current levels of funding for boat ramps, jetties and drainage works
- ▼ maintain current level of funding for libraries and cultural activities, and tourism
- ▼ maintain current levels of funding of footpaths, cycleways and traffic facilities.

Financial projections showed that the council expected the operating deficit to reduce gradually until 2016/17, and become a surplus in following years, and the infrastructure backlog to be only partially addressed. Total new capital expenditure of \$269m and replacement capital expenditure of \$308m over 7 years was planned.³⁵

³⁴ See section 3.2 and Appendix C.

³⁵ Lake Macquarie City Council, *Securing Our Future*, pp 7-8 and 11.

3 | IPART's assessment

To make our decision on Lake Macquarie City Council's application for a multi-year special variation in 2012/13, we assessed this application against the 6 criteria for section 508A applications set out in the Guidelines. We found that the application addressed the criteria systematically and thoroughly, and included comprehensive supporting information. However, we considered that it met some of these criteria only partially.

In particular, we were satisfied that the council has shown that significant rate increases are needed to improve its financial sustainability and maintain and enhance its services and assets in line with community expectations. We were also satisfied that it provided evidence of community support for significant rate increases, and an increase in rate levels to at least Option 2 was reasonable. But we were not convinced that it has demonstrated the need, community support and capacity to pay for such a large cumulative increase as it requested. For example, we found that:

- ▼ A more moderate cumulative increase – such as the increase under the second of the 3 options the council consulted its community on (Option 2) – would still enable it to achieve financial sustainability (by eliminating its operating deficits) over the 7 year period, while also allowing for continuing growth in operating expenditure, additional asset maintenance, and funding loans for capital works.
- ▼ The council's consultation showed clear community support for rate increases at least as large as those in Option 2, but the extent of support for Option 3 was harder to assess.
- ▼ While socio-economic indicators suggest the Lake Macquarie community has the capacity to pay higher rates than at present, we judged that a more moderate cumulative increase would have a more reasonable impact.

For these reasons, we have not approved the special variation as the council requested. Instead, we have decided to approve a lower cumulative rise in general income that is consistent with Option 2. We note that while the proposed program of expenditure under Option 2 assumes some growth in current levels of services and infrastructure maintenance and construction, the special variation we have approved will not provide revenue to fund the program of enhanced services and capital expenditures the council proposed in its application (Option 3).

Table 1.3 (in Chapter 1) summarised our findings in relation to each of the criteria. The sections below discuss our findings in more detail.

3.1 Criterion 1 - Demonstrated need for the rate increase

Councils seeking special variations must demonstrate that their requested increase in general income is necessary. This includes:

- ▼ supporting their application with relevant strategic, asset management and long-term financial planning information
- ▼ providing evidence that the income raised by the special variation will be used to fund an efficient and feasible program of expenditure, and
- ▼ if possible, providing evidence that the special variation will improve their financial sustainability.

Lake Macquarie City Council requested a cumulative increase of 73.24% over 7 years for the purposes of securing the council's long-term financial sustainability, while maintaining and enhancing existing assets and levels of service in line with community preferences and expectations.³⁶ (See section 2.4 and Appendix A for more detail.)

We found that the council's application and supporting information shows that the requested special variation is based on the council's long-term financial and strategic planning. It also shows that the requested special variation broadly reflects the community's priorities, as identified through consultations about implementing the council's Integrated Planning and Reporting Framework (IPRF) and its proposals for a special variation.³⁷ However, we note that there is also evidence that not all in the community are willing to pay for the proposed level and scope of services. (This is discussed further in section 3.2.)

We are satisfied that rate increases are an appropriate and necessary source of revenue for funding the expenditure proposed in the council's application. The council has considered and utilised alternative revenue sources - including increasing fees and charges, expanding its sources of income, and increasing borrowing to fund capital expansion.³⁸

³⁶ Lake Macquarie Application, Part B, pp 2-24 and Table 2.5, pp 16-17.

³⁷ See generally Lake Macquarie Application, Part B, pp 25-34 and 43-45, and Supporting Documents 3.2 - 3.9, including *Draft Lifestyle 2030*, *Environmental Sustainability Action Plan 2011-18*, *Library Service Delivery Model 2011*, *Pool Service Delivery Model 2009*, *Sports Facility Strategy 2009*. In the Levels of Service Review in the initial phase of the 'Securing Our Future' consultation in 2011, the community was asked to identify the services it values and would be prepared to pay for with higher rates, and the services it would be willing to see reduced or eliminated if rates were not increased.

³⁸ Lake Macquarie Application Part B, pp 55-66 and 70-73.

We are also satisfied that the income raised by the special variation will be used to fund an efficient and feasible program of expenditure. While we did not undertake a detailed evaluation of the council's expenditure items, we accept that the proposed program of expenditure has been prioritised, and that program and project dates and cost estimates are based on previous experience, quantity survey information, and the application of standard rates.

In addition, we found that the requested special variation will improve the council's financial sustainability. Indeed, one of its main purposes is to eliminate the council's ongoing operating deficits, while also managing the backlog in maintenance and renewing its substantial and ageing asset base. We note that in 2011/12, the operating deficit (excluding capital grants and contributions) was \$14.48m, and would have been significantly more if the council had not been subsidising operating expenditure from the asset replacement reserve over recent years by some \$20m per year. The council also intends to use the extra rate revenue to address its asset backlog, which it estimates at \$67m.³⁹

We commend Lake Macquarie City Council for its commitment to addressing its financial sustainability. However, we consider that this objective must be assessed in light of ratepayers' willingness to pay, and their capacity to pay over a relatively short period of time, particularly given our findings in relation to criterion 3 (discussed in section 3.3).

In particular, we note that in its consultations, the council presented the community with 2 options for addressing its financial sustainability and enhancing its assets and services:

- ▼ Option 3 involved a cumulative increase of 73.24% over 7 years, consistent with the requested special variation.
- ▼ Option 2 involved a cumulative increase of 57.48% over 7 years, consistent with the special variation we have approved.⁴⁰

Both these options would enable the council to eliminate the operating deficit within the 7-year period, while also allowing for continuing growth in operating expenditure, additional asset maintenance, and funding loans for capital works. The main difference is that Option 2 allows for a lower growth in operating expenditure (3.9% per annum compared with an average of 5.0% under Option 3), and does not fund as many additional capital works, and has a more moderate impact on ratepayers.

³⁹ Lake Macquarie Application Part B, p 7, and LTFP, p 28.

⁴⁰ Lake Macquarie City Council, *Securing Our Future*. Under Option 1 rate peg only increases would apply, and services and assets to be significantly reduced. See section 1.2 and Table 1.1 above.

In addition, we consider that some of the additional capital projects to be funded under Option 3 can be seen as discretionary. We also note that Lake Macquarie's current asset backlog is comparatively low, and has built up over time. While we strongly support councils addressing their asset backlogs in principle, it is possible to stage this to balance expenditure with income, improving financial sustainability over time but with a lower impact on ratepayers.

Overall, our assessment is that the council has demonstrated the need for a significant increase in its general income to address its financial sustainability and enhance assets and services, but has not shown that the increase needs to be as large as requested. We note that the cumulative increase of 57.48% that we have decided to allow will still enable the council to eliminate its operating deficit in a relatively short period, and therefore take a major step towards financial sustainability

3.2 Criterion 2 - Demonstrated community support

Councils seeking special variations must demonstrate that they have undertaken extensive community consultation, and obtained community support for the special variation and the associated program of expenditure. Their consultation material must be clear and accurate, and it must explain what the rate increase will be used for and the impact on ratepayers.

In assessing Lake Macquarie City Council's application, we considered the information it provided about its consultations, and its findings and conclusions from these consultations. We also considered the large number of written submissions and other representations we received from ratepayers about the council's application.

3.2.1 The council's consultation program

The council conducted an extensive consultation program 'Securing Our Future' in 3 stages between April and December 2011. The first 2 stages explored the values of the community and the services it most desired, and reviewed the council's costs and service levels as a basis for developing the 3 options to put to the community. The third stage explained these options and sought feedback to gauge community preferences through 4 main survey methods:

- ▼ a random telephone survey conducted by the Hunter Valley Research Foundation (HVRF)
- ▼ a postal ballot by way of a tear-off slip from a 16-page brochure delivered to all households across the LGA
- ▼ an on-line survey conducted by Bang The Table, and
- ▼ electronic polling at community workshops.

Appendix C contains more detail on the council's consultation program.

The options put to the community were to increase rates by the rate peg and reduce services (Option 1); to increase rates above the rate peg over 7 years and maintain services (Option 2); and to increase rates by a larger amount over 7 years and improve services (Option 3). Apart from some minor additions to expenditure on infrastructure maintenance, the council's requested increase is consistent with Option 3.

All 4 surveys found that a higher proportion of respondents supported increases to rates above the rate peg (either Option 2 or 3) than rate peg increases only (Option 1). The random telephone survey – which is the most statistically reliable method of capturing feedback – found there was a higher level of support for the more moderate increase under Option 2 (48%) than Option 3 (36%). However, the postal ballot, online survey and polling at workshops – which are less statistically reliable because they are subject to a degree of self-selection bias – all found more support for Option 3 than Option 2. The council noted that an analysis of these 3 consultation methods demonstrated that they were reasonably representative of the wider Lake Macquarie community.⁴¹

Overall, taking the results of all 4 survey methods and the few written response into account, the council calculated that Option 3 had the highest level of support (50%) within the community. Further, the council noted that the council advisory groups it consulted also showed high levels of support for Option 3.⁴²

The council's summary of the outcomes of community feedback on the 3 options is provided in Table 3.1.

⁴¹ Lake Macquarie Application Part B, pp 128-129, and *Providing Enduring Value*, Section 3 and Appendix H.

⁴² Lake Macquarie Application Part B, Table 4.5, p 125.

Table 3.1 Lake Macquarie City Council 'Securing Our Future' consultation – Preferred option by feedback mode

Feedback mode	Number of respondents expressing a preference	Results		
		Option 1	Option 2	Option 3
Postal ballot (Funding Option Selection Form)	1784	581 33%	331 19%	872 49%
Online survey	661	210 32%	83 13%	368 55%
Telephone survey	528	89 17%	251 48%	188 36%
Written responses	5	1 20%	1 20%	3 60%
Polling at workshops	279	37 13%	50 18%	192 69%
TOTAL	3257	918	717	1623
Percentage of total responses		28%	22%	50%

Source: Lake Macquarie Application Part B, p 125.

3.2.2 Submissions to IPART

We received 303 individual submissions in relation to the council's application, as well as 7 petitions with 764 signatures, and 480 letters in 7 different standard forms. In our experience of assessing special variation applications so far, this indicates a high level of public interest.

The submissions and other representations overwhelmingly opposed the special variation. Many argued that the proposed cumulative rate increase was large and unaffordable for households and businesses, particularly in the current economic climate. We have considered this concern in relation to criterion 3, reasonable impact on ratepayers, discussed in section 3.3.

Many also expressed concern about the council's consultation strategy, including that it was not sufficiently publicised, did not survey ratepayers directly, or that the results were manipulated by the methodologies used. However, others stated that the phone survey undertaken by HVRF on the council's behalf was 'credible' and that HVRF itself was 'respected'.

Some representations put the view that the council's management practices were poor, and spending on managerial salaries and consultants excessive, that it operated inefficiently, failed to respond to specific requests for service, and that its recent financial and investment performance was poor. Some objected to specific programs and policies, including the council's policies responding to the predicted impact of

flooding and sea level rises caused by climate change, and notations on s149 certificates about contaminated land. They considered that several programs or policies were unnecessary, too costly or beyond the core functions of a local council. We have considered some of these views in relation to criterion 4, financial sustainability, and criterion 5, productivity and cost containment.

The few submissions that supported the special variation recognised the need for the council's requested increase in income in light of rising costs, and supported the level and quality of existing services delivered by the council. Some of these ratepayers had also participated in the council's consultation process, and expressed concern about criticism of the council's methodology made in submissions, local media and other forums.

We have no doubt that the views opposing the special variation expressed in the representations we received are strongly and genuinely held. However, we note that they are from a self-selected group within the Lake Macquarie community. As such, they cannot be considered to be statistically reliable, and are not necessarily representative of ratepayers as a whole. To some extent, they reflect campaigns by community organisations and individuals to generate submissions to IPART, which were publicised or advertised in the local media. Many submissions repeated claims made in the media and at public meetings. In addition, we found that most (but not all) did not appear to have considered the material in the council's application and many raised unrelated issues. Only a few specifically addressed the criteria in the Guidelines.

3.2.3 Our assessment

Overall, we found that Lake Macquarie City Council engaged extensively with the community to determine expenditure priorities and whether there was support for the requested rate increases. The council's consultation strategy was conducted in accordance with the advice to councils set out in the Guidelines. The materials clearly informed the broad community about the proposed special variation and its impact on rates. It captured community feedback by a range of methods that involved either a statistically reliable, or a representative, sample of the community. It also responded appropriately to concerns raised in the consultations, particularly in relation to amending its Payment Assistance Policy.⁴³

However, while the council's consultation showed clear community support for significant rate increases over a rate-peg-only increase, the extent of support for Option 3 is harder to assess.

⁴³ Lake Macquarie Application Part B, pp 131 and 153.

In addition, while it is clear that some ratepayers strongly oppose the requested special variation and question the consultation methodology used, on balance, we accept the evidence that the council attempted to widely publicise its request for feedback on the 3 options. We also accept the evidence that resulted from the council's consultation methods, especially the results of the independent and random phone survey, which showed very strong support (84%) for a large rate increase of at least of the size we have decided to approve.

3.3 Criterion 3 - Reasonable impact on ratepayers

This criterion is important, given that the primary purpose of regulating council revenues is to protect ratepayers from unreasonable increases in rates. To assess whether a council's application meets the criterion, we consider the magnitude of the impact of rate rises resulting from the requested special variation, the ratepayers' capacity to pay the increased rates, and evidence of community support for the requested special variation (discussed above).

In relation to Lake Macquarie City Council's application, we found that the socio-economic indicators we examined (see Appendix B), and those in the council's application,⁴⁴ suggest that Lake Macquarie's residents and business community do have the capacity to pay higher rates than the current moderate levels.

Lake Macquarie City Council's SEIFA ranking is 102, which indicates that it is among the top third of least-disadvantaged councils in NSW. While its average residential rate is similar to the average for DLG Group 5, the average level of household disposable income in Lake Macquarie is higher than in other comparable LGAs, the level of unemployment is comparatively low, and a higher proportion of households own their own home than the average across NSW.⁴⁵

Indicators for business ratepayers are not readily available. We note that in 2010/11, the council's average business rate of \$3,146 was well below the average for DLG Group 5 (\$4,421).⁴⁶ We also note that business chambers of commerce in 7 centres indicated to the council that they supported Options 2 or 3.⁴⁷ On the other hand, we received submissions from business operators who opposed rate increases.

In addition, the council has consistently reported an outstanding rates ratio that is the lowest in its group since at least 2000. In 2012/11 it was 3.0%. This is very low, compared to the average for DLG Group 5 (5.7%) and for all councils in NSW (7.3%). It suggests that its ratepayers have had little difficulty to date in paying rates.

⁴⁴ Lake Macquarie Application Part B, pp 145-152.

⁴⁵ See Appendix B and Lake Macquarie Application Part B, pp 145-149.

⁴⁶ The group business rate average is strongly affected by much higher average rates in Newcastle (\$6,891) and Wollongong (\$8,704), which are more comparable with Lake Macquarie than the other DLG Group 5 councils.

⁴⁷ Lake Macquarie Application Part B, Supporting Document 5.1 Letters of Support.

But while we are satisfied that in general ratepayers have the capacity to pay higher rates than at present, this does not necessarily mean they have the capacity to pay cumulative increases as high as those the council requested. We note that under Option 3:

- ▼ Average residential rates would increase by 65.33% over 7 years, taking them from \$949 in 2011/12 to \$1,570 in 2018/19. This represents an increase of \$620, or an extra \$427 above the rate peg increase.
- ▼ Average business rates would increase by 87.34% over 7 years, taking them for \$3,284 to \$6,152. This is an increase of \$2,868 or an extra \$2,188 above the rate peg increase.⁴⁸

Rate increases of this magnitude would mean that after 7 years, Lake Macquarie's City Council's average residential rate is likely to be considerably higher than the average residential rates of other councils in DLG Group 5. Its average business rates would still be lower than current average business rates in Newcastle and Wollongong.⁴⁹ We also note that many of the submissions we received indicated that capacity to pay was of concern, at least to some sections of the community and particularly in the current economic climate.

Taking account of these projections, and the evidence about community support for significant rate rises discussed in section 3.2, our assessment is that the impact of a more moderate special variation in line with Option 2 would be more reasonable than the requested special variation. Under this option:

- ▼ Average residential rates would increase by 55.20% or \$524 over 7 years, which is around \$330 above the rate peg increase.
- ▼ Average business rates would increase by 71.00% or \$2,332 over 7 years, which is around \$1,652 above the rate peg increase.⁵⁰

Although the cumulative increases under Option 2 are relatively large, we note that the council's telephone survey (the most statistically reliable survey method used) found that 77.1% of residential ratepayers and 68.1% of business ratepayers considered that the rate rises under Option 2 were affordable.⁵¹

⁴⁸ Lake Macquarie Application Part A, Worksheet 5 and IPART calculations.

⁴⁹ We have assumed that rates for DLG Group 5 councils would increase in line with assumed rate pegs and any existing special variations.

⁵⁰ Lake Macquarie City Council, *Securing Our Future*, p 13, Lake Macquarie Application Part A, Worksheet 5 and IPART calculations. See also Table 1.4.

⁵¹ Lake Macquarie Application Part B, Table 4.7, p 126.

We also note that the council offers the statutory pensioner rebates, and has adopted hardship provisions which provide for alternative payment arrangements, writing off interest charges and allowing rates to accrue as a debt against a pensioner's estate. As a result of feedback from the community consultation process, the policy is now called the Payment Assistance Policy and a monthly instalment payments option is available.⁵² Given the increase in rates that will occur as a result of this special variation, we expect the council to respond appropriately to ratepayers who approach them about difficulties in meeting their rate obligations.

3.4 Criterion 4 - Sustainable financing strategy

Councils seeking special variations must demonstrate that they have considered the use of all available financing options to address their capital expenditure requirements. Their financing strategy must be both sustainable and consistent with the principles of intergenerational equity.

The concept of intergenerational equity means that the costs of long-lived assets are shared between current and future users, based on their share of the use of these assets over their life. For example, this may be achieved by council borrowings, which spread the financing costs of infrastructure over a long period, rather than meeting these costs through large rate increases in the short to medium term.

We are satisfied that the council has a financing strategy that is consistent with intergenerational equity, and projected borrowings are within the prudent limits set in its borrowing policy. We do not agree with submissions that argued that the council's proposed large increase in debt was irresponsible

The council funds capital works with a mix of rate revenue, developer contributions, fees and charges, reserves and loans. Its policy is to use debt to fund only those assets whose useful life is at least equal to the borrowing term, and to borrow responsibly, with a maximum limit to its debt service ratio of 8.5%. This is within DLG's 'satisfactory' benchmark for a council's a debt service ratio of less than 10%. The council's application set out detailed information about the projects for which funds would be borrowed in each year.⁵³

Option 3 projected an increase in debt over 7 years of almost \$152m, which would result in the debt service ratio rising from 5.36% in 2012/13 to 7.31% in 2018/19. The council's modelling for expenditure under Option 2 projected a smaller increase in debt of \$92m over 7 years. As a result, the debt service ratio would rise to only 6.53% in 2018/19.⁵⁴

⁵² Lake Macquarie Application Part B, p 153.

⁵³ Lake Macquarie Application Part B, pp 154-156.

⁵⁴ Lake Macquarie Application Part B Supporting Document 3.15, p 19 (Special Variation Scenario); Option 2 projections draw on the Baseline Scenario at p 7.

3.5 Criterion 5 - Productivity impacts and cost containment strategies

Councils seeking special variations must demonstrate that they have implemented a program of productivity or efficiency improvements and cost containment strategies to ease expenditure pressures before considering an increase in rates. In particular, they need to provide details of the productivity improvements, efficiencies and cost containment strategies that they have implemented over the past 2 or more years, and details of those that they propose to realise over the period of the special variation.

We consider that the comparative productivity indicators demonstrate that Lake Macquarie City Council is relatively efficient. Furthermore, the council appears to have a culture of efficiency and continuous improvement. It undertook a comprehensive Service Review systematically across all its operations between 2009 and 2011 that identified \$4.2m in ongoing savings from productivity improvements and cost containment, as well as opportunities for revenue enhancement.⁵⁵ The application outlined plans to continue to pursue initiatives to realise efficiency gains, ongoing and one-off savings, and additional revenue across all operational areas. We encourage Lake Macquarie City Council to continue these efforts.

Some submissions argued that council should first improve its efficiency and reduce its expenditure before increasing rates. We found no evidence in these submissions, or in the council's application or DLG comparative data that indicated that the council's productivity or efficiency was a major concern. Although it is always possible for any organisation to reduce costs, it appears that significant reductions in expenditure are possible only if the scope and level of services to ratepayers are substantially reduced. Nor do we agree that the council's functions have extended beyond the 'core' local government roles into activities properly the responsibility of state and federal governments, as some submissions claimed.

Comparative data on council productivity from the DLG for 2010/11 is presented in Appendix B. These data show that Lake Macquarie City Council compares favourably with other DLG Group 5 councils. For example:

- ▼ The ratio of population to FTE staff is considerably higher (227) than the Group 5 average (165).⁵⁶ On this indicator, the council is not overstaffed.
- ▼ The proportion of employee costs to ordinary expenditure (41.3%) is higher than the Group 5 average (36.9%), but its consultancy/contractor expenses (\$12.9m) were half the Group 5 average (\$24.1m). The council's application also explained the reason for 2 recent large one-off consultancies.

⁵⁵ See Dollery, Brian, Walker, Glen and Bell, Brian, (2011) "'Bottom-up' Internal Reform in Australian Local Government: The Lake Macquarie City Council Review Process", *Journal of Economic and Social Policy*, Volume 14, Issue 2, Article 5.

⁵⁶ A higher ratio indicates that there are fewer council staff for each person in the community whereas a lower ratio indicates that there are more council staff.

- ▼ The council spends a higher proportion of its ordinary expenditure on services than the Group 5 or NSW averages, although spending on services per rate assessment (\$1,413) and per capita (\$554) is much lower than the average for Group 5 and NSW. This does not support the view that the council's spending is excessive.⁵⁷

We are satisfied that Lake Macquarie City Council has systematically identified productivity improvements and implemented cost containment strategies. The council is committed to pursuing these approaches in the future.⁵⁸ Some key actions include:

- ▼ implementing recommendations from the Service Review, which identified \$4.2m in ongoing cost savings from productivity improvements, cost containment and revenue enhancement⁵⁹
- ▼ adopting strategies to limit the cost of waste disposal, particularly in light of the NSW waste levy and introduction of the carbon price⁶⁰
- ▼ capturing other improvements in productivity/efficiency and identifying savings from catering, cleaning and fleet operations, better managing energy and water consumption and waste⁶¹
- ▼ reducing the costs of injury management, and assessing whether its workers compensation self-insured status remains cost-effective⁶²
- ▼ increasing income from other sources such as entrepreneurial activities including metal fabrication, selling valuation, printing, planning and building services to other councils and a Property Investment Strategy, and the proposed Sustainable Resource Centre at Teralba would yield surpluses from 2016/17.

The council intends to drive future productivity improvements and innovative management approaches by implementing the Australian Business Excellence Framework, which is recommended to councils by DLG. This involves evaluating management systems and performance, and benchmarking against other public and private sector organisations and focusing on continual operational improvement. In line with a resolution passed by the council in conjunction with deciding to apply for a special variation, the results will be reported annually.

⁵⁷ DLG, unpublished Special Schedule 1 council data, 2010/11. Group averages are \$1,716 and \$745 respectively. NSW averages are \$2,219 and \$1,129 respectively.

⁵⁸ See generally Lake Macquarie Application, Part B, pp 157-178, particularly Tables 7.4 and 7.5.

⁵⁹ Lake Macquarie Application, Part B, Table 7.1 p 160.

⁶⁰ Lake Macquarie Application, Part B, pp 164, 171, 177-178.

⁶¹ Lake Macquarie Application, Part B, pp 158-171.

⁶² Lake Macquarie Application, Part B, pp 161, 178.

Community views on productivity improvements and cost containment

Many individual submissions, as well as the petitions and form letters IPART received, claimed that the council needed to increase its efficiency and improve productivity before seeking a rate rise, and referred to excessive managerial numbers and salaries and use of consultants. In support of this view, a few offered anecdotal evidence, and some cited newspaper reports. However, we consider that the information provided in the council's application and the comparative DLG data do not provide evidence of obvious inefficiency.

Some submissions also put the view that the council was expanding its functions beyond the 'core' local government roles into activities properly the responsibility of state and federal government. We note that local government's involvement in a range of areas, such as managing the risks of the impact of climate change, may appear to be outside its traditional role, but can be the result of statutory or administrative obligations placed on local councils by other levels of government. We do not consider that Lake Macquarie's activities are outside the norm of functions exercised by councils of similar size and location. Ultimately, it is up to the councillors and the community to decide the scope of the council's discretionary activities.

Other submissions expressed concerns about the appropriateness and potential financial outcomes of the council being involved in entrepreneurial activities. The application indicated that potential income-generating opportunities are undertaken only after a full review of risks and rewards, and are subject to the requirements of the *Local Government Act 1993*.⁶³

3.6 Criterion 6 – Implementation of the Integrated Planning and Reporting Framework

To apply for a special variation under section 508A of the Act, councils must have implemented the IPRF, including developing a 10-year community strategic plan, a 4-year delivery program, an annual operational plan and a detailed resourcing strategy.

The council satisfactorily implemented the IPRF by 30 June 2010. The DLG has reviewed the council's IPRF documents and verified that the council has met this criterion. DLG had only a few minor concerns, and the council appears to have adopted the changes recommended.⁶⁴

⁶³ Lake Macquarie Application, Part B, p 60.

⁶⁴ Lake Macquarie Application Part B, p 180.



Appendices

A Lake Macquarie City Council's proposed expenditure of revenue from the special variation

Lake Macquarie City Council proposes that the revenue generated by the special variation will assist it to fund an expenditure program over the next 7 years that will be based in part on income generated from the special variation in rates, and on other income sources and borrowings. This appendix sets out the expenditure program as it relates to the income that would be generated by the proposed special variation.

The council intends to use the income from the proposed special variation to:

- ▼ turn its operating deficits into surplus by 2017/18 while maintaining expenditure on services and assets at their current scope and level
- ▼ enhance services in some areas, and
- ▼ fund capital enhancements by meeting borrowing costs.

The proposed special variation will result in additional revenue over the 7 years of \$250.08m (Table A.1). Adjusted for the expiry of the Sustainability Levy in mid-2014, the net cumulative increase (not showed in the table) is \$236.91m.

Of the \$236.91m, \$166.80m will fund the maintenance of current levels of service and asset maintenance, ie, it will fund the operating deficit of the baseline scenario (shown by expenditure line item #1). A further \$3.83m, not shown in the table, will fund the surpluses in 2017/18 and 2018/19.⁶⁵

Of the remaining \$66.27m, \$53.32m is to be spent on enhancing services (expenditure line item #2) and \$14.19m on borrowing costs (expenditure line item #3).⁶⁶

⁶⁵ Lake Macquarie LTFF, p 28 (net operating result).

⁶⁶ We have not been able to reconcile the balance of income of \$66.27m with the spending on enhanced services and borrowing costs which sum to \$67.51m.

Table A.1 Lake Macquarie City Council projected revenue and spending under proposed special variation (\$m)

	2012/13	2013/14	2014/15	2015/16	2016/17	2017/18	2018/19	Total ⁶⁷
Additional revenue								
From rate pegs only	3.00	5.77	8.74	12.00	15.52	19.29	23.32	87.64
From balance of SV	5.71	12.47	19.17	24.55	29.58	34.30	36.66	162.44
Total additional revenue	8.71	18.23	27.91	36.55	45.10	53.60	59.98	250.08
Proposed expenditure								
<i>1. Maintaining current services</i>	<i>17.77</i>	<i>17.90</i>	<i>21.52</i>	<i>25.24</i>	<i>26.89</i>	<i>27.44</i>	<i>30.04</i>	<i>166.80</i>
<i>2. Enhancing services</i>								
Pools operating costs	0.07	0.32	0.34	0.68	0.76	1.71	1.86	5.73
Libraries - operating costs	0.02	0.16	0.35	0.46	0.70	0.80	0.96	3.45
Maintenance	1.00	1.00	1.00	3.00	3.00	3.00	3.00	15.00
Rangers - operating costs	0.03	0.09	0.13	0.21	0.22	0.23	0.23	1.14
Roads	0.00	0.00	0.00	7.00	7.00	7.00	7.00	28.00
<i>Total enhanced services</i>	<i>1.11</i>	<i>1.57</i>	<i>1.81</i>	<i>11.35</i>	<i>11.68</i>	<i>12.74</i>	<i>13.05</i>	<i>53.32</i>
<i>3. Borrowing costs</i>								
Interest	0.00	0.40	0.61	1.54	2.12	3.17	4.17	12.01
Principal repayments	0.00	0.07	0.11	0.26	0.38	0.58	0.79	2.18
<i>Total borrowing costs</i>	<i>0.00</i>	<i>0.47</i>	<i>0.71</i>	<i>1.81</i>	<i>2.50</i>	<i>3.74</i>	<i>4.96</i>	<i>14.19</i>
Total expenditure	18.88	19.94	24.05	38.40	41.07	43.92	48.05	234.31

Note: Worksheet 7 does not appear to remove the expiring levy from the calculations.

Source: Lake Macquarie Application Part A, Worksheet 7 and IPART calculations.

The council's application sets out the major elements of additional expenditure on infrastructure construction and renewal, some of which will be funded by the increased borrowings supported by the special variation. These are noted in section 2.4.

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B Comparative indicators

Table B.1 Lake Macquarie, selected indicators, 2010/11

	Council	DLG Group 5 average	NSW average
General profile indicators			
Area (km ²) (land)	648	–	–
Population (2010)	199,277	–	–
General Fund operating expenditure (\$m)	169.97	–	–
General Fund revenue per capita (\$)	1,025	1,282	2,006
Rates revenue % total General Fund revenue	50.0	48.0	46.7
Average rate indicators^a			
Average rate level – residential (\$)	880	889	659
Average rate level – business (\$)	3,146	4,421	2,450
Average rate level - farmland (\$)	1,736	1,694	2,121
LGA socio-economic indicators			
Average annual income, 2009 (\$)	41,825	39,048	41,376
Growth in average annual income, 2006-2009 (%)	4.8	4.6	4.4
Ratio of average residential rates (2010/11) to average annual income, 2009 (%)	2.0	2.1	1.5
SEIFA, 2006 (NSW rank) ^b	102	–	–
Outstanding rates ratio (%)	3.0	5.7	7.3
Productivity indicators			
FTE staff (no) ^{c,d}	877	795	294
Ratio of population to FTEs	227	165	126
Average cost per FTE (\$) ^d	79,991	78,982	71,155
Employee costs as % ordinary expenditure – General Fund only	41.3	36.9	37.3
Contractor expenses (\$) ^d	12,881,000	24,125,833	6,238,288
Contractor expenses as % ordinary expenditure ^d	7.6	12.8	8.0

^a Average rate is total revenue from a given category divided by the number of assessments in that category in 2010/11.

^b See footnote 11 for SEIFA index.

^c FTE is full-time equivalent.

^d Based on total council costs ie, General Fund, Water and Sewer and other funds.

Note: NSW averages exclude Snowy River Shire Council (data not available).

Source: DLG database, 2010/11 and ABS, *National Regional Profiles, NSW*, November 2011, and Lake Macquarie Application Part B

C Lake Macquarie City Council's Consultation Strategy

Consultation Methodology used by Lake Macquarie City Council

The council's consultation strategy 'Securing Our Future' was conducted in 3 stages between April and December 2011.

Box C.1 Stage 1: April – August 2011, Understanding what we value

Purpose: to determine what the community values, by way of:

- ▼ online survey of attitudes to council services and facilities (2,121 respondents)
- ▼ community forums for residents and business owners (400+ attendees)
- ▼ online forums 'Have your say' and Budget Allocator (213 respondents).

At the same time, the council undertook an internal Levels of Service Review to assess current levels of service and current and future demand.

Stage 1 was publicised to stakeholders and the general community by:

- ▼ a flyer in rate notices to all ratepayers in June 2011
 - ▼ paid advertising in 4 local newspapers, media releases and opinion pieces
 - ▼ Mayor's Column and links on the council website
 - ▼ emails to existing users of council websites and council's database of 4,000+ community groups, businesses and other subscribers
 - ▼ communications with established council consultative committees and community groups
 - ▼ Have Your Say – Securing Our Future website – live from July 2011 (see below)
 - ▼ Fact sheets on the council's financial situation, its assets and services, and finding operational efficiencies, available on the websites, at community facilities and community workshops
-

Box C.2 Stage 2: September– October 2011: Developing funding options

Based on Stage 1 report and Levels of Service Review, 3 proposed funding options were developed with input from a Community Working Group (24 residents, randomly selected by HVRF). This built on feedback from the existing consultative committees:

- ▼ Community Advisory Group (existing group providing feedback on issues relating to council operations)
- ▼ Youth Advisory Council (7 members).

Stage 2 involved a community education and promotion strategy

Purpose: to further engage and inform the community about Council services.

Techniques included:

- ▼ online promotional video and press material using 5 'super users' selected from the community to be (unpaid) advocates talking about their use of council services
 - ▼ paid advertising in newspapers and a media release.
-

Box C.3 Stage 3: October – December 2011: Finding the right solution

Purpose: to gather feedback on community's preference out of the 3 funding options

Common questions asked across major feedback modes:

- ▼ What services are you willing and able to pay for?
- ▼ What levels of service are best?

Feedback modes used in this stage:

- ▼ **telephone survey – 528 respondents**
 - by HVRF of randomly selected and representative sample of resident and business ratepayers and renters, provided with an information pack
- ▼ **postal ballot – 1784 replies**
 - based on reply-paid tear-off Funding Option Selection Form' in a 16 page *Securing Our Future* information booklet delivered by Australia Post to approximately 82,000 dwellings in Lake Macquarie LGA
- ▼ **on-line survey – 661 respondents**
 - conducted via the Securing our Future consultation website
- ▼ **electronic polling at community workshops – 279 participants**
 - 11 workshops held in all 3 wards and included 1 for businesses owners/operators
- ▼ **5 written responses were received.**

Stage 3 was promoted to the community through:

- ▼ existing council website and to registered users (1,154) of www.haveyoursaylakemac.com.au
 - ▼ social media – twitter feeds (1,315 followers) and Facebook (150 followers)
 - ▼ media releases and advertisements in 4 local newspapers and business newsletters
 - ▼ invitations sent to the Lake Macquarie combined business chambers.
-